JFE Holdings, Inc.

JFE Group Investor Meeting
(Earnings Forecast Revisions and Steel Business Structural Reforms)
Summary of Q&A Session on March 27, 2020

Q. Please provide a breakdown of the roughly 60-billion-yen effect on annual earnings from your structural reforms and when this impact will appear.

A. We cannot give a detailed breakdown, except to say that reductions in fixed costs, such as repair and labor costs, are the main component. Shutting down certain facilities will also reduce variable costs, but this will be largely offset by increased transportation costs due to materials having to be supplied from other districts. Hence, fixed-cost reductions will account for the majority of the earnings effect. The figure of 60 billion yen does not include reductions in depreciation costs due to the recognition of impairment losses.

As to the timing of the impact, we expect it to fully materialize from FY2024 once the Keihin blast furnace is shut down, but we aim to reduce repair costs and the like ahead of schedule as much as possible.

Q. The Chiba District, rather than the Keihin District where upstream facilities will be shut down, is expected to account for a greater proportion of the impairment on the book value of fixed assets (excluding land). What is the basis for this? Also, will you recognize impairment only on depreciable assets? Also, is impairment possible in other areas, such as the West Japan Works?

A. We assess impairment for each district based on the present value of future cash flows and the value of business assets. It is not directly related to the relative proportions of impairment on current fixed-asset book values. Future cash flows also include the value of land, and one reason for the difference in impairment figures is that land in the Keihin District carries a higher valuation than that in Chiba. These impairments will be booked on depreciable assets.

At this time, no other steelworks or district shows any indication of impairment.

Q. What are your thoughts on executive compensation, etc., in relation to the downward earnings revision?

A. In response to our worsening financial performance, JFE Holdings implemented a partial return of executive compensation from February 2020. JFE Steel implemented a return of executive compensation from November 2019, and from April 2020 will increase the proportion of compensation returned for the foreseeable future, bringing it in line with JFE Holdings at 7% to 20%.

Q. How do you expect depreciation costs to change ahead?

A. The impairment losses recognized on the East Japan Works will reduce depreciation by around 25 billion yen per year. But the shortening of useful asset lives in the Keihin District due to equipment shutdowns will increase deprecation. The net effect will be an annual reduction of 10 billion yen in our depreciation cost. Meanwhile, capital expenditure remains high for the company as a whole. If our capital expenditure in FY2020 is on par with FY2019, we would expect the depreciation cost to increase by around 10 billion yen, which would bring the FY2020 company-wide depreciation cost largely in line with FY2019.

Q. What will unconsolidated crude steel production capacity look like after the structural reforms?

A. We are unable to provide specific figures on crude steel production capacity after the structural reforms.

Separate from the Keihin District blast furnace shutdown, we plan to put a new continuous casting facility into operation in the Kurashiki District at the end of FY2020, which we expect to increase crude steel production capacity in Kurashiki to some extent.

Q. Why did you choose to shut down the Keihin District blast furnace?

A. The Chiba District facilities are our East Japan Works' base for manufacturing a wide range of products, primarily automotive steel sheet, our priority field, as well as stainless steel and iron powder. They also produce base materials for high-grade seamless pipes, an area in which JFE Holdings' possesses technological strengths. Our decision to shut down the Keihin District blast furnace also reflects a comprehensive assessment of other factors, particularly the need to manufacture automotive steel sheet in an integrated blast-furnace facility because of stringent quality and delivery requirements as well as plans to cut spending on our renewal of aging facilities over the next 10 years or so. The Keihin district will remain as a profitable base for manufacturing steel plate, steel pipes, etc., mainly for construction in the domestic market.

Q. Do you have any plans to increase furnace volume and production capacity when refitting the Chiba District blast furnace?

A. We will decide our detailed plan for refitting the Chiba blast furnace going forward.

Q. What is your FY2020 earnings outlook?

A. Many uncertainties cloud our earnings outlook for FY2020, including the impact of the novel coronavirus (Covid-19) and the postponement of the Olympic and Paralympic Games. We cannot provide specifics at this stage.

Q. Will the reduction in facility renewal outlays due to the shutdown result in a decline in steel business capital expenditure?

A. We will carefully assess our capital expenditures going forward, so we cannot offer specifics at this stage.

Q. Why is FY2023 the target for shutting down the Keihin District blast furnace?

A. We plan to refit the Kurashiki District blast furnace in FY2021 and the Chiba District blast furnace in FY2023, so we decided to schedule the Keihin District blast furnace shutdown after we refit the Chiba District blast furnace.

Q. What kind of business environment do you envision (e.g., internal demand outlook) as a basis for shutting down upstream facilities in the Keihin District and recognizing impairment losses on Chiba/Keihin District assets? Also, are additional structural reforms likely?

A. In Japan, we expect domestic demand for steel materials to decline by around 1% per year due to the nation's declining population, etc., which mirrors The Japan Iron and Steel Federation's outlook. Overseas, our outlook takes into account factors such as the risk of growth in Chinese exports due to the country's declining domestic demand. In view of this business-environment outlook, we believe that shifting from eight to seven blast furnaces as announced is the best strategy at this time. We aim to generate sustainable growth under this new operating configuration.

Q. Are there indications of impairment in your steel business overseas? Also, what is view of overseas business over the medium to long term, including the use of overseas upstream facilities?

A. There is no indication of impairment in our overseas business at this time. Our overseas business strategy for the medium to long term incorporates a model for the vertical division of our manufacturing operations, including supplying semi-finished products for the production of automotive steel sheet and other products. The strategy also reflects our aim to expand business via footholds in growth regions, notably through alliances with JSW in India and FHS in Vietnam.

Q. How will this restructuring of production affect your product mix?

A. As far as our product mix is concerned, we will be shifting toward more profitable product types, but we cannot provide a detailed breakdown at this time.

Q. What impact will the four-million-ton reduction in production capacity have on production volumes, shipment volumes and market share going forward?

A. Primarily, we expect shipment volumes to decline to a degree in commodity exports, where competition is intense. In the area of high-grade steel, meanwhile, we fully expect to maintain our market share.

Q. Your February forecast of business profit remains unchanged. Is there any impact from Covid-19?

A. Our results through February were largely in line with our previous forecasts. Uncertainties have persisted into March, such as fluctuations in volumes and foreign exchange movements, but the impact of Covid-19 on our FY2019 earnings is not large. However, Covid-19 is now impacting automobile production, etc., so we will face considerable uncertainty in FY2020.