JFE Holdings, Inc.

JFE Group Investor Meeting
(FY2020 2Q Financial Results and FY2020 Earnings Forecasts)
Summary of Q&A Session on November 9, 2020

Q. Your 2H financial performance outlook is roughly flat versus the previous forecast in August, but what do you expect in terms of hot-rolled steel export prices and raw materials prices? Also, the recent recovery in India is striking. Please tell us about the 2H earnings contribution from equity-method affiliate JSW Steel.

A. Export steel prices have been on a recovery trend since bottoming in April–June, and we expect hot-rolled steel export prices in 2H to factor in the recent recovery to an extent. As for raw materials, meanwhile, we expect iron ore prices to remain high amid strong demand in China. Coking coal prices are in a downtrend of late, but we expect them to rise somewhat during latter 2H owing to the global economic recovery as well as coal producing regions coming into their rainy seasons.

In India, the recovery trend strengthened in July–September, with auto sales volume above year-earlier levels, for instance. We expect JSW Steel's financial performance to improve as well, but we have not necessarily factored all of this into our 2H financial performance, so our outlook may be slightly conservative.

Q. On Page 21 of the slides, you show segment profit excluding one-off factors in FY2020. Other than inventory valuation differences, what sort of one-off factors were there?

A. One-off factors comprise R&D costs shifted from 1H into 2H due to the spread of COVID-19, the increase in losses on the sale and disposal of assets above and beyond normal levels due to efforts to improve our financial condition by reducing the asset base and so forth, and the total amount of inventory valuation differences. These are not new costs, but we have identified these amounts as one-offs because they diverge from the usual pattern and magnitude of such costs.

Q. Sales and raw materials (metal spread) declined by 10.0 billion yen from FY2019 2H through FY2020 1H, and you expect a 5.0 billion yen decline from FY2020 1H through 2H. What are the trends for the domestic and export metal spread, particularly for domestic contract customers?

A. Sales and raw materials (metal spread) for exports, which does fluctuate from period to period, is expected to be largely unchanged from FY2019 2H through FY2020 2H, but in the domestic market, the metal spread is expected to worsen. As for efforts to pass increases in raw materials prices to steel prices, a portion is not likely to pass along this fiscal year. For products subject to contract customers, however, we intend to pass along increases swiftly.

Q. In your efforts to improve steel prices, you indicate you will conduct a comprehensive review of price extras. Please explain how these efforts differ from your other efforts so far, such as passing commodity price increases to product prices.

A. Regarding commodity price increases, we have long been working to improve prices and customers have agreed in the majority of cases. As for price extras, time has elapsed since many of these were set. Going forward, we will be reevaluating whether manufacturing and development costs, as well as the functionality and value offered by our technical proposals to help customers reduce costs, are commensurate with the value that customers perceive. We will redesign our pricing structures based on appropriate assessments of product value and value-added.

Q. You anticipate 100 billion yen in cost reductions in FY2020. How sustainable will your cost reductions be next fiscal year and beyond?

A. In FY2020, we anticipate cost reductions of 100 billion yen, including around 10 billion yen in fixed costs, such as lower repair costs due to structural reforms. The roughly 16-billion-yen reduction in depreciation associated with impairment booked in FY2019 is not included in that 100 billion yen. We are unable to give a specific cost reduction figure for next fiscal year at present, but we anticipate considerable cost reductions to come from (a) the effects of investments in new equipment started up this fiscal year being realized over a greater number of months, and (b) the effects of large-scale investments in equipment slated to go into operation in the coming future, such as the Kurashiki district’s new continuous casting machine and the Fukuyama district’s No. 3 coke oven (Battery B). We believe that by steadily executing these investments, we will be quite capable of achieving profitability in FY2021.

Q. Please tell us about your goals and efforts to maintain financial soundness.

A. To maintain financial soundness, we aim for a D/E ratio of 100%. In pursuit of this goal, we are looking to reduce asset holdings by 170 billion yen, primarily through the sale of cross-shareholdings, and to reduce the steel business’s domestic capital investment by 130 billion yen.

Q. The Fukuyama No. 4 blast furnace moved into normal operations from mid-September. Please tell us about its operating status and demand trends since then.

A. We were able to start the Fukuyama No. 4 blast furnace up within a month of resuming hot blasting, and it has been operating smoothly since. As for demand trends, automotive demand is stronger than expected, and we believe it may recover to above year-earlier levels in October–December. The Fukuyama district has high exposure to automotive demand, so the early return of the No. 4 blast furnace to normal operation ensures our ability to capture demand as it recovers.

Q. You project weak demand in shipbuilding and energy in 2H. To what extent will this impact FY2020 earnings?

A. We cannot give specific figures, but the decrease in demand for steel plate, steel pipe, etc. for shipbuilding and energy applications is hurting the product mix, the earnings impact of which is quite large.

Q. You project year-over-year growth in automotive demand in October–December. Is this

factored into your 12.3-million-ton forecast for crude steel production in 2H? Please also tell us what you expect the trends in crude steel production and shipment volumes to be in October–December and in January–March.

A. Automotive demand has been recovering robustly of late, but we have not necessarily factored in all of this. As for trends during October–December and January–March, we expect crude steel production volumes to remain largely flat over these periods, and we expect shipment volumes to rise slightly in January–March.

Q. Would you be able to achieve profitability in FY2021 assuming FY2020 2H crude steel production levels?

A. Assuming crude steel production of 12.3 million tons, we forecast a FY2020 2H segment loss, excluding one-offs, of 12.0 billion yen. Annualized, this works out to crude steel production of 24.6 million tons and a segment loss of 24.0 billion yen. But we believe we can achieve profitability in FY2021 as this loss should be adequately offset by the effects of investments in equipment started up this fiscal year being realized over a greater number of months and the effects of investments in equipment slated to go into operation in the coming future. In addition, we expect selling prices to fully reflect increased costs of key raw materials from FY2020, and we will make additional efforts to improve selling prices and so forth, all of which will add to profit.

Q. How certain is the 100-billion-yen cost reduction for FY2020, and how much potential upside is there?

A. Variable costs increased in 1H due to the substantial reduction in production, but we believe we can definitely achieve 100 billion yen in cost reductions by streamlining operations, cutting fixed costs, and so on. We are also aiming for additional cost reductions on top of that.

Q. In China, automotive and sheet steel have been firm, whereas the rate of growth for construction applications has slowed somewhat. What is your view of the steel supply and demand outlook in China?

A. China's crude steel production levels have been very high, fueled by domestic demand mainly in the construction sector due to the Chinese government's domestic stimulus measures. Daily crude steel production hit record highs in two consecutive months—August and September. China's steel product import volume also remains high. We will be keeping a close eye on steel supply and demand trends, of course understanding that some risk always exists.