JFE Group Investor Meeting

(FY2023 1H Financial Results and FY2023 Earnings Forecasts)

Summary of Q&A Session on November 6, 2023

Moderator: Now I would like to move on to the question and answer session.

First participant, please.

Participant: Please explain the factors behind the increase in steel prices and the improvement in spreads in the 1H results compared to the previous forecast, by sector, such as domestic contract, domestic market sector, and overseas. Can you tell me if the spread includes the impact of yen depreciation?

Also, regarding the forecast for 2H, since your company determines the selling price with its contract customers on a post-decision basis, is it correct to assume that with most of your customers you will follow the formula and pass on the higher coking coal prices to some extent in the selling price? On the other hand, we have not heard of any price increases from blast furnace makers in the market sector, so please tell us if we can consider this as a sector where the cost of main raw materials is not reflected.

Regarding exports, we have heard that the previous forecast assumed that exports would return to the level of the 1Q spread in 4Q, but I think the current forecast assumes that they will probably remain flat at the current level. Please explain your plans for 2H, including the incorporation of raw material prices.

JFE: 1H results show that sales price was positive for both domestic and exports. The positive in the domestic market is larger and is mainly in the contract field. This is because exports were slightly higher than the market assumptions in the forecast. As foreign exchange effects are excluded from this price difference in the analysis, the impact of yen depreciation is not included.

The assumption for 2H, as you have pointed out, is that we have factored in some of the raw material price increases that will be reflected in selling prices during 2H due to our pricing formula. However, due to relationships with individual customers and various other conditions, we do not believe that we will be able to pass on the entire raw material price increase during this 2H. It is assumed that the price pass-through will shift to some extent after 1H of 2024. For the market sector, we are factoring in figures based on a certain degree of visibility into current market conditions and other circumstances.

For exports, we are assuming that the current spread level will continue for 2H, and we do not see a recovery in this forecast.

As we mentioned in our explanation, we have factored in raw material prices for both iron ore and coking coal based on the assumption that the current price levels will continue for 2H.

Participant: With regard to stabilizing coking coal prices, there was an article in an industry magazine that stated that you will be actively involved in the spot market. I think the problem with coking coal prices is that they are indexed and determined by the prices of hearings by a very limited number of people, such as Platts and Argus. The index price is based on a contract price that is close to the price quoted by some Indian manufacturers in very low-distribution spot markets. I assume you are raising these issues, but could you please explain this area? Thank you.

JFE: Regarding the issue of coking coal, you are basically correct. We are aware that the number of contracts is uncertain because the number of contracts is very small and the details of the contracts are determined to some extent on a hearing basis. In particular, the number of contracts has been decreasing more recently due to the decline in purchases by Chinese mills. Therefore, we are in a situation where prices are determined by Indian mill contracts. In order to normalize this situation to some extent, one possible measure would be to increase transactions, which is why JFE Steel President Kitano mentioned this at the recent press conference of the Iron and Steel Federation.

Participant: Will the increased liquidity create more price depth, and will the price amplitude be smaller than it is now? Also, can I get the impression that the impact on your company's P&L is not very relevant?

JFE: Since spot transactions are not that large, we do not expect much impact on our P&L. Currently, we hear that there are very few transactions taking place, in some cases only one or two transactions per week. In such a situation, one would have to try it once.

Participant: I understand. By the way, the coking coal market is currently at USD340 to USD350 per ton. Is it correct to say that you saw it at that level?

JFE: We are looking at a level above USD300 per ton.

Moderator: Next question, please.

Participant: Please explain the P&L analysis for FY2022 versus FY2023 on page 20 of the document. The question is regarding point number five, others. The situation is the same as in the forecast at the beginning of the period, but even excluding the foreign exchange flow difference and depreciation, there are still about JPY30 billion of deteriorating factors. Please tell us the specifics and whether the same situation is likely to continue in the next year and beyond.

JFE: Regarding the other points of the P&L analysis compared to the previous year, as you noted, this has been the case since our initial forecast at the beginning of the period. There are many details, for example, headquarters expenses. Compared to the previous year, the current year has seen an increasingly higher level of activity and related expenses, such as more frequent business travel. Expenses for overseas offices are also affected and will increase further when converted to yen basis due to the weaker yen. IT also needs to be constantly updated, and we believe that the combination of these factors will have an impact of approximately JPY10 billion. In addition to this, price effects are also included. The Keihin area is expected to incur curing and other costs over several years as a result of structural reforms. These are not one-time expenses, but rather expenses that will continue over several years and are therefore included in others. That is all.

Participant: Next question is regarding the capital increase. The majority of the JPY114.5 billion raised through equity, which is also mentioned on page 32 of the document, will be used to invest in electrical steel sheets, but to what extent will this investment in electrical steel sheets increase capacity, and in the absence of clarity on the profitability of electromagnetic steel sheets? I generally find it difficult to calculate investment returns. What are your thoughts on this area?

JFE: I cannot give you a specific production volume of electrical steel sheets, but as I explained when we announced our capital investment, we plan to double the current volume in the Kurashiki district in 1H of FY2024, and to triple the current volume for FY2026. We cannot give you specifics on the level of profitability, but it far exceeds the JPY10,000 per ton target of our mid-term management plan.

Moderator: Next question, please.

Participant: In reviewing the current outlook, please allow me to confirm what changes have been made in the contributions of the group companies, especially overseas. I understand that there may be some positive or negative factors depending on the region, such as weak performance in China and strong performance in India, but please let me confirm your view of the current and next fiscal year for your overseas bases in these regions.

JFE: Regarding the point about group companies, looking at the movement from the previous to the current forecast, there are some positive and negative changes by individual company, but in general, there is not much change both in Japan and overseas. Overseas, there have been no major developments in China, India, or other regions that I would like to explain.

Participant: We are concerned that as we reap the benefits of future structural reforms, they will be offset by those structural reform costs and not remain effective. Please let me reconfirm whether the Company has a system in place that can demonstrate the results of structural reforms and capture the + α from each measure and + β from the recovery of market conditions.

JFE: The FY2023 forecast P&L of JPY200 billion, which is the base point for the path to the FY2024 medium-term management plan on page 23, is calculated excluding the Keihin area structural reform expenses of JPY20 billion. Since this is a one-time cost, we do not expect it to affect the next fiscal year and beyond.

The curing costs included in the FY2023 forecast P&L that I just explained are different from that one-time cost of JPY20 billion. We expect to incur curing costs in FY2024 as well, but they are neutral from this year to next and will not be a new negative factor. The curing cost is an expense that will eventually cease to be incurred. We believe that this could be a positive factor considering the future.

Against these structural reform expenses, the fixed cost reduction effect of JPY45 billion will be realized in the form of JPY20 billion this fiscal year and JPY25 billion next fiscal year, so I hope you will understand that we are definitely on a positive track from now on.

Moderator: Next question, please.

Participant: The non-consolidated crude steel production volume was revised downward this time, and you mentioned that the export HR Coil was the main factor. Could you tell us about the forecast of the demand for domestic and export, not only for 2H, but also for the next year and beyond?

JFE: Regarding the downward revision of non-consolidated crude steel production, it is basically centered overseas. Looking at Japan as a whole, demand for automotive applications is increasing, but on the other hand, general construction and civil engineering applications are slackening. So, the overall domestic situation has not changed significantly. On the other hand, we have made downward revisions to the demand for HR Coil, especially overseas, with the intention of not chasing volume at the current level of spreads.

Participant: Regarding the graph on the left side of page 22 of the document, which shows the metal spread of the HR Coil, you said that it was slightly revised downward from the last time to this time, but at what level is the actual level assumed?

JFE: Regarding the graph on metal spreads, this is the level of China's HR Coil minus the spot of the raw material, which is currently at a level below USD50. We are not at this price, but at a higher level, but we are in a very difficult situation right now, and for 2H, we expect the spread to fall below USD100.

Participant: In terms of export spreads, do you expect a slight recovery from the current situation? Or do you expect the current situation to continue?

JFE: I assume that the current situation will continue throughout this fiscal year.

Participant: Okay, thank you.

Moderator: Next question, please.

Participant: Regarding the page 22, I have a question about the incorporation of the spread on the right side and a question about domestic margins. There is talk that competitors are aiming for a certain level of reasonable margins. The Company plans to improve marginal profit by upgrading the order mix. On the other hand, can you tell us whether you expect your company's appropriate margin to still have room to increase in the next fiscal year and beyond, or whether it is getting to a certain level?

JFE: We have been actively working to improve our selling prices and are proceeding with a certain level of understanding from our customers. However, as was explained earlier, there are some aspects, such as the current rise in coking coal prices, which cannot be completely absorbed within this fiscal year. Therefore, it is necessary to continue working on this issue in the coming year.

In addition, with regard to the improvement of various prices, various cost-increasing factors are possible, such as the expected increase in the cost of electricity next year and the impact of higher labor costs. Therefore, we plan to continue to negotiate firmly with our customers and continue to make improvements.

Participant: Regarding the margins, I believe that coking coal and other main raw material costs can be passed on, although there is a timing gap. Also, as for commodity costs, I guess it depends on where you consider the starting point, but we believe that the improvement in margins was evident in the 1H results as a result of our efforts to pass on costs that had not been fully taken up. Please explain how this can be further improved in the future.

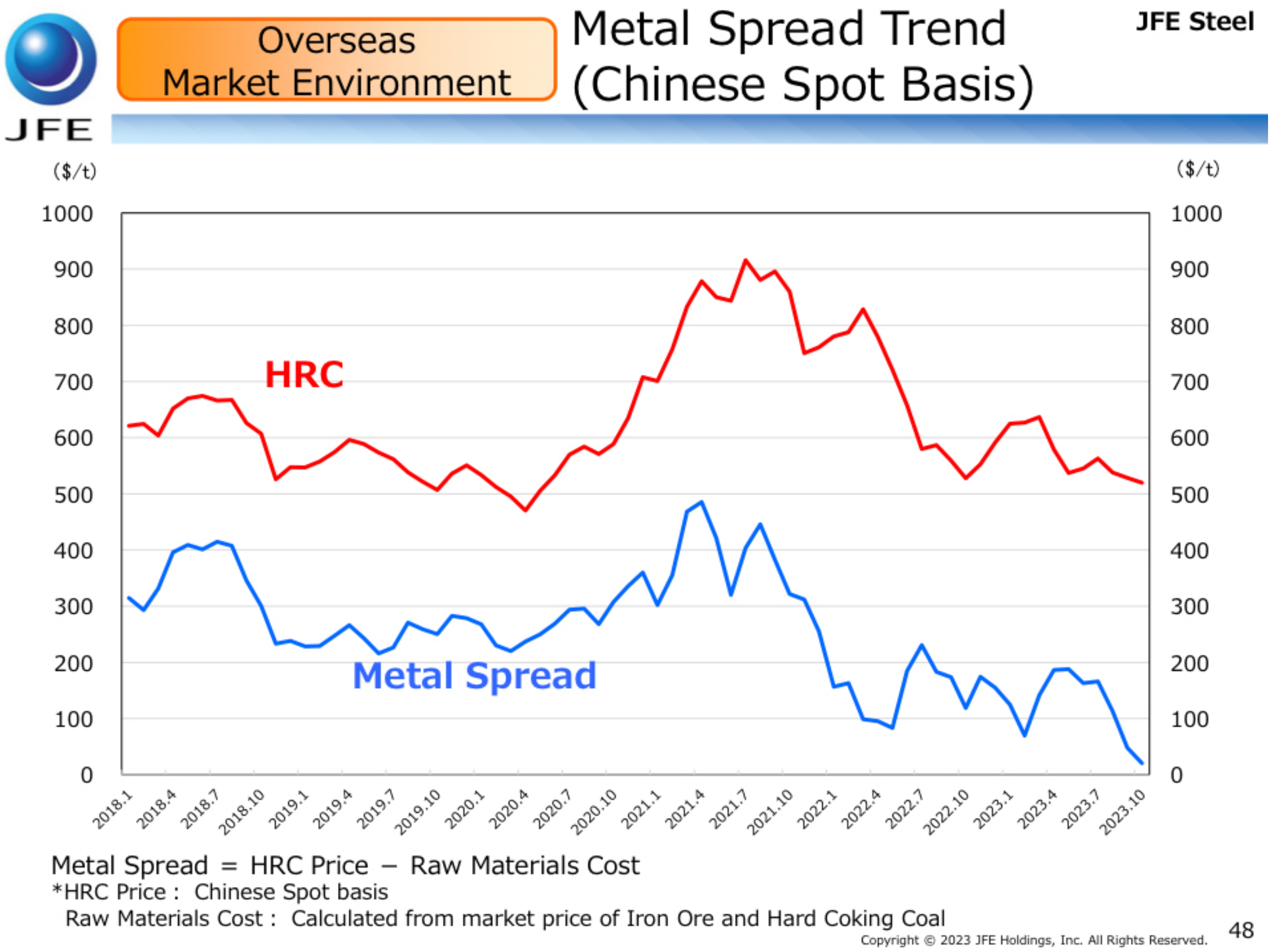
JFE: We are constantly working to improve our sales price levels to be sustainable. In addition to these efforts, we intend to further improve profitability by shifting quality to more profitable products and high value-added products as we suspend the upper process in Keihin at the end of September.

Participant: I would like to discuss the material on page 29. Regarding the suspension of the upper process in the Keihin area, you are saying that you will focus on high value-added products by bringing slabs and coils from Fukuyama and Kurashiki to Keihin, but I would like to confirm whether this direction is toward increasing profitability due to the logistics costs involved.

JFE: We expect some cost increases in the Keihin area, but we are working to reduce costs overall. In particular, since the Keihin area serves as a base for thick plates for customers in eastern Japan, we intend to secure earnings by taking advantage of its characteristics and other factors.

Participant: I understand. Thank you very much.

Moderator: Thank you very much. As the scheduled end time is approaching, the next person will be the last to ask a question. Please do.



Participant: Let me ask you about China and India.

First, regarding China, looking at the spread on page 48 of the document, it appears that the spread per ton is currently down to about USD50. This reminds me of the China Shock period in 2015. At the time, I remember stories of trillions of yen in losses in the steel industry.

However, we are not hearing much about that at the moment, and I wonder if this is simply because we are not hearing about it, or if the Chinese steel industry is making progress in many aspects and is stabilizing even in a bad situation. What is your perception of the current situation of the steel industry in China?

Next, let's look at India. I would appreciate your comments on the current supply and demand for steel products in India.

JFE: First, regarding China, there are some aspects of the current situation that are still unclear. Recently, we have received news that spreads have been deteriorating rapidly and that the P&L situation for Chinese mills is also worsening. However, as for the environmental aspects and the positioning of the mills themselves, I think they have changed since the past.

I believe that the mills themselves are no longer running to increase production compared to the past, as government-led production cuts have been underway in the last year and the year before. With the worsening economic situation in China, they are sure to act accordingly, so we are keeping a close eye on their movements.

Next, regarding India, the economy is relatively strong, with growth in the 6% range and inflation in the 5% range. We have heard that India’s domestic market is strong and that the Southeast Asian market is still holding up, as Chinese mills are expanding into Southeast Asia, but no exports are coming out of Indian mills.

Participant: I understand. Thank you very much.

Moderator: Thank you very much. With that, we would like to conclude the question-and-answer session. We will now conclude this briefing. Thank you very much for joining us today.

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