JFE Holdings, Inc.

JFE Group Investor Meeting
(FY2019 Financial Results and FY2020 Earnings Forecasts)
Summary of Q&A Session on May 12, 2020

Q. What was your underlying profit excluding one-off effects for FY2019 2H?
A. Of the Steel Business's segment loss of 26.4 billion yen in FY2019 2H, around 26.0 billion yen was due to inventory valuation and a concentrated disposal of fixed assets at the yearend. Excluding those factors, our underlying profit was essentially zero.

Q. Some say that nationwide crude steel production will fall below 18 million tons per quarter. How much of a decline in volumes do you envision?
A. Given the current situation with orders, we expect production to decline by about 25% in April–June of FY2020 vs. FY2019 2H to a level somewhere below 70% of capacity. We will bank the Fukuyama district's blast furnace No. 4 at the end of June. We are unable to forecast volumes for July–September onward at this stage, but we believe that by adjusting tapping ratios we can adjust production volume by ±15% or so in response to the 25% reduction in blast furnace capacity.

Q. If the current export metal spread is $110 per ton, does that mean the hot coil price is below $400 per ton?
A. As you suspect, the current hot coil price is below $400 per ton.

Q. If steel demand falls short of expectations even after the effects of COVID-19 ease, will you need any downsizing, such as shutting down any of the West Japan Works' blast furnaces, in addition to shutting down upstream processes in the East Japan Works' Keihin district?
A. At present, we do not anticipate any structural reforms beyond the shutdown of the Keihin blast furnace. As the East Japan Works operates only one blast furnace in each district, if demand were expected to fall further, including from the effects of COVID-19, it would be difficult to shut down the Keihin blast furnace ahead of schedule or to shut down the Chiba blast furnace, so blast furnaces at the West Japan Works would probably be a temporary option.

Q. Please tell us what level of cost reductions you hope to make in FY2020.
A. We are aiming at cost reductions on the order of 100 billion yen in FY2020. We envision this being fairly evenly divided between fixed and variable costs. Fixed cost reductions will be centered mainly on repair-cost reductions and measures to address labor costs. As for variable costs, we expect the effects of major capital expenditures on the Fukuyama district's No. 3 coke oven (A) and No. 3 sintering plant to contribute across the full fiscal year. And with some additional measures on top of that, we hope to reduce costs by 100 billion yen.

Q. You have implemented cost reductions during past downturns, including by over 100 billion yen after the Lehman collapse. What are the key aspects of your current cost reductions, including how they differ from past efforts? Also, could reducing repair costs have an adverse effect on facilities and equipment later? What are your views?
A. As mentioned, about half of the 100 billion yen in cost reductions we aim to achieve in FY2020 is to come from reductions in fixed costs, including repair and labor costs. At present, we believe we need to reduce repair costs in a manner commensurate with the significant reductions in production levels. Past experience gives us extensive insight into reducing costs appropriately, in a manner commensurate with operating rates, and we believe we can suppress any adverse effects on facilities and equipment. In addition to fixed cost reductions, which we have undertaken in the past, we also seek to maximize the effects of capital expenditures in terms of variable costs, regardless of any COVID-19 impact.

Q. What is your stance on how to raise domestic contract prices?
A. Our sales personnel have been working to garner customer understanding regarding price increases, and more than half of our customers have agreed, but we have not yet reached price levels sufficient for generating enough profit to sustain growth. We will continue to work closely with each customer to achieve better pricing.

Q. My understanding is that, although you have used your technological capabilities to reduce mainly variable costs in recent years, you have had to accept that fixed costs would rise owing to increasing investment outlays to renew aging equipment and the like. Can we expect the structural reforms announced in March and these cost reduction measures for FY2020 to reduce both fixed and variable costs and thereby reduce the breakeven point, such that lasting changes are realized in your cost structure beyond the effects of emergency measures?
A. We expect the structural reforms announced on March 27 to deliver an annual earnings impact of around 85.0 billion yen from FY2024. This will comprise around 60.0 billion yen, mainly from the reduction of fixed costs such as labor/repair costs, and around 25.0 billion yen from reduced depreciation. We also anticipate that reduced investment in the renewal of aging equipment will benefit cash flow by around 200.0 billion yen over 10 years. These current cost reductions certainly do feed into our efforts to reduce the breakeven point through structural reforms as an overarching trend.

Q. Please tell us about your strategy for overseas growth once you have streamlined domestic operations through structural reforms, in particular your strategy for JSW in India and FHS in Vietnam as upstream facilities overseas.
A. Our overseas growth strategy encompasses the expansion of investment, licensing of technology, and utilization of sales networks. A potential strategic move would be to step up the licensing of our technology to companies like JSW and FHS in emerging markets where demand is growing for high-grade steel products, such as high-tensile automotive steel, and thereby expand sales to Japanese, European, and U.S. automakers. We recognize this as an issue we need to study going forward.

Q. Do efforts to reduce inventory mean that steel production will decline by more than shipments this fiscal year?
A. We are looking to reduce inventories of not only steel products but also raw materials and supplies. This does not necessarily mean that steel production will decline by more than shipments. However, as these inventory reductions are taking place in the context of the current business environment, there is a possibility that we will move to reduce production by more than shipments in some areas.

Q. Please tell us about your medium/long-term strategy for commodity steel exports. Will you bolster cost competitiveness to maintain volumes, or will you be looking to downsize volumes?
A. As indicated with our structural reforms announced on March 27, taking the Keihin district’s upstream processes offline and reducing crude steel production capacity by 4 million tons are aimed at reducing our exposure to commodity steel exports—an area where metal spreads are low and competition from Chinese mills, etc., is fierce—and expanding our business in areas that involve higher levels of added value.

Q. Which product areas will you target in the global steel market? Tell us where you expect your strengths to be.
A. In the domestic market, where demand is on the order of 50–60 million tons, we will draw on strengths, such as our fine-grained quality and delivery-management capabilities, to flexibly serve the needs of diverse customers in the manufacturing and construction sectors, without limiting ourselves solely to high-added-value products. In overseas markets, we aim to be a steel company that offers advanced technological capabilities in high-added-value areas, such as high-tensile automotive products and electrical steel sheets. Concurrently, we aim to reduce our exposure in

commodity exports, as explained earlier.

Q. Could investment in the new continuous casting machine in Kurashiki be frozen depending on demand trends?
A. The new continuous casting machine in Kurashiki is an important investment with respect to our plans for shutting down upstream processes in the Keihin district and expanding capacity at the West Japan Works. There might be a possibility of the machine's startup being pushed back somewhat because of factors like demand trends, but we do not envision putting a freeze on it.

Q. Thinking about how likely you are to achieve 100 billion yen in cost reductions, is it correct to characterize reductions in variable costs, which account for around half of the total reduction, as residual cost reductions due to reduced production volumes?
A. We believe that cost reductions of 100 billion yen are fully achievable. However, variable costs certainly are affected by production volumes, as you point out, and for now we assume they will be on par with FY2019 2H. We expect April–June crude steel production to be down 25% vs. FY2019 2H, but the outlook for production volumes in July–September and the ultimate reduction in variable costs over the entire fiscal year is unclear at present.

Q. Cash flow from investment activities in FY2019 was around 360 billion yen. How much will this decline in FY2020?
A. We cannot give a specific value for FY2020 at present. However, we are currently conducting a thorough review of capital expenditures, primarily in the Steel Business, including investments that are already approved, so we do expect outlays to fall relative to FY2019.

Q. What is behind the increase in exports in January–March of FY2019? You've said the export metal spread is currently around $110 per ton. Is this level profitable?
A. The FY2019 2H metal spread was at levels high enough to be profitable until around March, so we increased exports. But we have to admit that $110 per ton is quite tight, so we will be making order determinations based on individual contract prices and so forth.