



**Nippon Steel & Sumitomo Metal Corporation FY2017, Third Quarter IR Briefing
February 1, 2018
Summary of Q&A**

Note: Based on information available as of the date of the IR Briefing

Representative from NSSMC

Katsuhiro Miyamoto, Managing Executive Officer

Q You appear to have two management issues: the issue of sluggish production and the structural issue of low absolute prices in contract-based sales. I would assume that given lower-than-projected production volume, you might have been forced to prioritize lower-priced sales to domestic customers while generating some opportunity loss by reducing exports at relatively higher prices. First, how are you tackling the issue of production volume?

A We have done our utmost efforts to increase capital spending such as for maintenance and renewals and to spend money for repairs. However, the Oita Steel Works had a plate mill fire accident in 2017 and some troubles in upstream processes in the first half. Long-used equipment was merely a part of the reasons. In fact, the Oita plate mill's fire started from a new facility. By investigating the causes of these troubles, we found that troubles tended to occur at the start-up phase of facilities. We suspect that, in addition to NSSMC, our vendors may have weaker equipment construction engineering capability than we thought in some aspects. Moreover, some steel mills and some processes exhibit stronger resistance to troubles while others do less. Against such a background, we have undertaken cross-functional initiatives aimed at raising engineering capability. Some people from the Plant Engineering and Facility Management Center (PFC) and the Technical Division in the head office were also assigned to help these initiatives. Comprehensive measures to enhance intangible "soft" aspects have also been carried out, such as tackling the issue of allocation of manpower who have to handle a very high construction work load, and the issue of further coordination between the frontline operating sections and the facility

maintenance section. As we regard secured stable production as our big challenge, we will implement those measures properly for dealing with the matter of production volume.

Q Why have you revised downward the forecast for second-half crude steel production?

A First, there was an impact of the two typhoons of last October. When raw materials are soaking wet, operation of blast furnaces tends to become unstable for a certain period. We therefore operated the furnace by increasing coal volume, which resulted in a decline in pig-iron production. In addition, the construction period for some projects was extended in order to take extra time to ensure good results, which also contributed to a decline in production volume.

Q You are planning to increase crude steel production in the fourth quarter compared to the third quarter. What is the probability of achieving this target? Do you think that the planned level of production in the fourth quarter will also be achievable throughout fiscal 2018?

A We are now in February and one month has already passed in the fourth quarter. As production has so far been sustained as planned, we think that the plan is achievable. Compared to past production levels, the level in the fourth quarter is not so high, in our view. A production plan for fiscal 2018 will be decided during the coming two months. As capital investment and repairs require construction work, which may result in some decline in production, we have to give due consideration to a balance between construction and production volume.

Q According to your ordinary-profit variance analysis of fiscal 2016 vs. fiscal 2017, a decreased production volume is estimated to have a negative impact of ¥57.0 billion in shipment. Isn't there any other impact from lower output, such as on the cost side?

A In addition to the impact from a decline in shipment volume, the lower production volume affected the cost side. A recovery in production volume is regarded as a pressing management issue for us. We will do our best to respond to that.

Q While you could not boost production, you might have prioritized lower-priced sales to domestic customers while generating some opportunity loss by reducing exports at relatively higher prices. During this period, some overseas steelmakers made substantially higher profit than you did, by expanding sales of steel sheet for automobiles, unlike your situation. My guess is that their sales prices to automakers might have been significantly higher than yours. While NSSMC was able to pass a surge in raw material prices on to your sales prices, prices of auxiliary materials and other prices have risen as well. As such, don't you need to further raise your price? Will you explain how you handle the issue of low contract-based prices in absolute terms?

A Given the present decline in production volume, we gave priority to domestic long-term customers, which resulted in reducing currently favorable exports. To our contract-based customers, we provide not only materials but solution proposals. We also maintain capability for just-in-time supply of stable- and high-quality products, and deliver the products needed all over the world, leveraging our global supply network. Despite this performance, Japanese steel product prices are depressed in the world market. While prices are supposed to be determined by the market mechanism, steel product prices to contract-based customers in Japan are persistently low relative to global prices despite the tight demand/supply balance in Japan. We need our customers to recognize the value of our products and services. Unless we accomplish this, we may not achieve sustainable reproduction nor make capital spending in the future. We will continue to patiently negotiate with customers and ask for their understanding.

Q According to your ordinary-profit variance analysis of fiscal 2016 vs. fiscal 2017, "steel prices & product mix and raw material prices" are estimated to generate a positive impact of ¥23 billion in total. How much margin improvement per ton are you aiming at for your sales in the domestic, export, contract-based, and spot markets?

A Please understand that I must refrain from disclosing details of margin improvement for each customer segment. Qualitatively and in general, I can say that margin improvement is higher for exports than for domestic sales and that among domestic sales, sales in the domestic spot market show higher margin improvement than

contract-based sales . We have enabled sales prices to reflect fluctuation of major raw material prices for all customers. However, in terms of covering an increase in cost of commodity materials and securing appropriate margins for sustainable reproduction, we have made significant improvements for exports and in the spot market but we will seek for more improvement for domestic contract-based sales.

Q How far are you improving margins in this fiscal year, relative to your annual target level?

A In the spot market, a price increase of ¥5,000 per ton is mostly being accepted. In the case of contract-based sales, we have been asking for more margin improvement, in addition to adjustments reflecting price fluctuation of major materials. It is a tough negotiation task but we, as a leader of the industry, inevitably have to do this. There is a significant price differential between Japan and overseas, which we regard as a big problem. The price gap must be dissolved for us to continue manufacturing in Japan over the next 10, 20 years. In the backdrop of such thinking, our plan for this fiscal year is to incorporate some margin improvement in contract-based sales.

Q Will you explain about the outlook for seamless pipes? I would assume that its sales environment should be affected by higher oil prices with about a six-month lag.

A As oil prices are on an uptrend, the sales volume of seamless pipes has picked up, particularly in North America. The shipment from our JV to North America is also increasing. However, it is likely to take a little more time for prices to rise. Recovery of large-diameter pipes for linepipes tends to lag even longer, partly as projects are big.

Q How about the sales environment of seamless pipes in the Middle East?

A We also see some pickup in order volume of seamless pipes. Pricing remains almost unchanged but we are looking forward to the future.

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