Sanyo Special Steel Co., Ltd.

IR Briefing Regarding the Business Results for the FY2020 3Q

Q&A Summary

Date: Friday, January 29, 2021

Speaker: Director, Member of the Board and Managing Executive Officer;
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** Please be noted that the actual Q&A session was in Japanese and this English translation is prepared for reference purpose only.*

Q. Could you please give us any ideas of non-consolidated business forecast for FY2021? In the IR material (page 16), the ordinary income of the FY20/4Q is expected to be 1.1 billion yen and it includes negative factors of the time lag of the iron scrap surcharge -1.9 billion yen, therefore the ordinary income of the FY20/4Q at substantial basis is expected to be 3 billion yen. It seems to be 12 billion yen with annual basis. On the other hand, FY2020 forecast includes positive factors of temporary fixed cost reductions by emergency profit Improvement measures and actions and lower raw material prices in cost-based.

A. The non-consolidated business forecast for FY20/4Q is evaluated higher than reality as it includes temporary positive impact of emergency profit Improvement measures and actions such as the receipt of unemployment insurance for temporary leave program and relatively low overtime and expenses. Considering business forecast for FY2021, it basically would be affected by the degree of sales volume. When sales volume would recover, simultaneously the production cost would increase. In addition, the prices of iron scrap, ferroalloys and crude oil are in an inflationary trend. To wrap up, we have to consider factors such as, a)sales volume, b)production cost, and c) negative impact from expiry of emergency profit Improvement measures and actions which we have practiced since FY2019, to predict the outcome for FY2021.

Q. Is there any impact to Sanyo business by the decrease in automobile production due to the shortage of semiconductors?

A. We consider that there is no substantial impact in FY2020. There may be some negative impact in the first half of FY2021. We consider that stocking phase in automobiles is almost over, and hereafter we consider that sales volumes will shift along with actual demand.

Q. Could you tell us about how much sales volume is needed to record operating profit for Ovako and MSSS, respectively?

A. Ovako’s sales volume in FY2020 is expected to decrease by 95,000 tons compared to FY2019, and the impact is expected to be negative 6 billion yen. Accordingly, if the sales volume in FY2021 would be the same as that of FY2019, the profit may increase by 6 billion yen from FY2020. Since Ovako has in-house secondary process and trading company function, Ovako’s marginal profit unit price is higher than Sanyo’s, therefore Ovako is more vulnerable to volume fluctuations. On the other hand, there will be some negative factors such as a)the increase in fixed costs due to an increase in sales volume and b)expiry of unemployment insurance for temporary leave program in Sweden. As for MSSS, it is necessary for MSSS to have at least 30,000 tons/Q of sales volume to be positive in profit. (In fact, MSSS’s operating income for FY2020/4Q is deficit with sales volume 29,000 tons/Q). Our target for FY2021 is securing operating income that exceeds the goodwill amortization for Ovako, and recording positive income for MSSS.

Q. Iron scrap prices are falling. Could you please tell us about the impact on profit and loss?

A. Iron scrap prices in the Kansai area(western part of Japan) are falling a little, but it is not as sharp as in the Kanto area(eastern part of Japan). The decline of iron scrap prices in the Kansai area is expected to be within a certain range, and we consider that it will not decline significantly. Regarding FY2020(April 2020 to March 2021),we consider that there will be little impact on profit and loss because there are only two months left. However, there may be a significant impact on profit and loss in FY2021 depending on iron scrap price trends.

Q. Could you please tell us about demand trends in Ovako? How do you consider future demand including the impacts of the COVID-19 infection and a decrease in automobile production due to a shortage of semiconductors?

A. We have been discussing with Ovako about demand trends in Europe, and consider that the current recovery trend would be steady, mainly due to the following two factors such as a)Ovako has long supply chain, therefore sales orders are strong due to stocking on the customer side, and b)Ovako has strong sales inquiries because import from outside the EU has decreased due to high container freight.

Q. The amount of “deposits paid to affiliated company” is increasing. If those are surplus funds, would you consider paying dividends?

A. These deposits are operating funds for settlement, and the balance is temporarily increasing because lesser operating funds are required due to the decrease in sales. However the balance is expected to decrease because we need more working capital as sales will increase and payment for equipment will be necessary. We pay dividends based on structural basis net income and dividend payout ratio.

Q. Could you please tell us about demand trends in Sanyo? How do you consider future demand for special steel by each industrial sector?

A. We consider that stocking in the supply chain of automobiles industry has almost been completed, and future demand trends shift along with the actual demand. The demand of construction machinery sector has been recovering rapidly by movement of stocking due to the long supply chain. The demand of Industrial machinery sector such as semiconductor, agricultural machinery, wind power generation, railways, and robots has been recovering slightly. Although the demand increase in the automobiles sector is somewhat easing, the sector of construction machinery and industrial machinery are expected to grow, and we expect that strong demand trend would continue.

Q. Iron scrap prices could remain high, partly due to China's movement such as resuming scrap imports and etc. Is it possible to reflect the increasing iron scrap prices to the unit price of sales? Could you please tell us the application ratio of surcharges？

A. Iron scrap prices may be higher than before, due to a) China's movement to resume imports of iron scrap and b) expectation that demand for iron scrap will increase due to increasing production by electric furnaces, whose environmental impact are relatively low. The application ratio of our iron scrap surcharge is about 80%, consisting of 70% automatically linked, and 10% of semi-surcharge system that is linked to the iron scrap price, but some negotiation is needed. Out of the remaining 20%, 10% are high alloys and stainless steel linked to ferroalloy prices such as Nickel, and the remaining 10% are distributors and small sized customers, spot sales, and oversea sales requiring individual negotiations, but basically reflecting the trend of scrap price fluctuations.

Q. Could you please tell us about the significance of investing in No.2 Bar & Wire Rod Mill? How does this investment contribute to your company?

A. The trend of EV will accelerate in accordance with the worldwide movement towards carbon neutrality. Therefore, customer demand to improve electricity consumption and to reduce weight per unit would surely grow. Our customer will require smaller parts and smaller diameters with same strength. This is why we installed new Reducing and Sizing Block (RSB) rolling mill, which enables us, for instance, to produce high quality steel bars by manufacturing through higher reduction.