Daido Steel Co., Ltd.

FY2023 Financial Results Briefing

Q&A Session (Summary)

Date : May 10, 2024 (Friday)

Respondents: Tetsuya Shimizu, President & CEO, Representative Executive Director
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Q. While the third quarter operating income included temporary positive factors, the fourth quarter operating income has transitory negative factors. Could you tell us about the total situation, including the impact of the decline in nickel prices. Also, the nickel price is currently in the upper part of the $8.0 / Lb. range, compared to $7.5 / Lb., the figure that the company had estimated. What will be the impact if the nickel price continues at the current level?

A. The consistent decline in nickel prices has had a negative impact of about 2 billion yen on the fourth quarter's operating income, due to the surcharge gap where the selling prices of products using nickel fall ahead of costs, and also due to inventory write-downs. In addition, the company's strategy was that production was accelerated in the third quarter and the inventory thus built up was used in the fourth quarter, taking advantage of seasonal power cost differences. This resulted in a profit of about 500 million yen on the one hand and a loss of the same amount on the other, reflecting the operating rates during these quarters. Furthermore, the payment of several hundred million yen of business taxes resulted from the posting of large gains on the sale of assets held by the company. In terms of sales volume, in addition to that the fourth quarter saw a decrease from the strong shipment of automotive parts in the third quarter, the downturn was further exacerbated by several unexpected events that occurred after year end. We recognize that the combined effect of these factors will have a one-time negative impact of about 3 billion yen on the fourth quarter's operating income. A nickel price of $7.5/Lb. is used in the FY2024 plan, and we understand the possibility of a negative impact on our profit plan if that price is assumed, but if the current $8.5/Lb. price is maintained or the price rises, this will be a positive factor, so we will be keeping a close eye on the trend.

Q. You said that there are many orders for open-die forgings, and production is not keeping pace with orders. Will the company be able to solve its problems by increasing capacity and improving on-site productivity, and will this lead to profits in FY2024 and beyond?

A. Orders for open-die forgings are extremely strong, so we are planning to increase capacity for these products in the next medium-term management plan. Currently, we are pushing to operate beyond the appropriate production level. By expanding our future capacity to produce open-die forgings, we are trying to respond to the strong order environment and accept more orders, commensurate with that expanded capacity. However, the production of open-die forgings presents some challenges right now, in terms of production costs, because of insufficient in-house productivity and increased outsourcing. Therefore, if either the number of orders or production gets a little off track, profits will be lower than expected. However, we are implementing improvements in the factories to deal with this, and we believe that we can continue to earn 2.5 to 3 billion yen per quarter in the Parts for Automotive and Industrial Equipment segment in FY2024.

Q. You said that proceeds from asset sales will be used for capital investment. I think it would be better to use part of the profits for dividend increases and stock buybacks for the purpose of improvement in PBR. What do you think of that approach?

A. We need to make strategic investments in order to reform our product portfolio, with an eye on the progress of EVs. That's why we will prioritize the use of the proceeds for capital investment. We intend to keep the dividend target payout ratio at about 30%. However, we fully understand the need to manage the company with P/B ratios in mind, and we will consider shareholder returns in the next mid-term management plan.

Q. In February of this year, you announced price increases for specialty steel, stainless steel, and tool steel. I would like to know the status of the incorporation of such increased selling prices into the profit plan.

A. We expect that price negotiations will take place in the first half of the year, so we are factoring the effects from the second half of the year in our profit plan.

Q. I have heard that competition is intensifying in China among steel manufacturers of automobile-related products and that demand for Japanese steel is decreasing as Chinese customers are shifting to local procurement of steel products. What do you think of such a trend?

A. It is true that on a long-term basis there may be a shift in China to local procurement of automobile-use steel, but at this point the specialty steel we sell does not show the trend toward local procurement due to intensifying competition. Rather, we are concerned that the demand for steel will generally decrease as Chinese automakers rise to prominence, due to the expansion of NEVs and the overall sales volume of Japanese cars, produced by Japanese automakers in China, declines.

Q. Please tell us how your production capacity for open-die forgings will increase from next year onward.

A. We have been making efforts to eliminate bottlenecks, one by one, in the production of open-die forgings. Working on this, we started with the upstream processes. In FY2023, the efficiency of cutting process of open-die forgings came into focus at the final inspection process. For instance, some types of superalloys are difficult to cut, and dealing with them will be a time-consuming and costly process, especially for subcontractors we outsource the cutting process to. We have been eliminating various restrictions, one after another, to increase production capacity. Improved productivity is a constant quest, and now, we have finally been able to remove bottlenecks in all processes, including the issue found in the final inspection process, leading to increased open-die forging production capacity. At this point, we have indeed secured the production capacity necessary to achieve our profit plan for FY2024.

Q. I think an increase in stainless steel sales volume is the main reason for the increase in earnings expected in the High-Performance Materials and Magnetic Materials segment in FY2024. Is there an actual sense of strong demand reflected in terms of orders?

A. Orders received during the period from April to June 2024 have exceeded the number of orders estimated on the assumptions of the FY2024 profit plan. This is because orders for industrial equipment-related products appear to have bottomed out, and the nickel price has reversed, from a decline up to the $8/Lb. range. This is helping to overcome customers' buying restraint that had been due to their anticipation of lower prices. It is expected that orders for stainless steel for semiconductor manufacturing equipment in the April-June period will increase by a few percent above the assumption in the profit plan, although a steep increase in orders for such a product cannot be confirmed at present. It has been a long time since the number orders has exceeded the plan, and we believe that we are off to a good start at the beginning of the period.

Q. You said that open-die forgings production costs are increasing due to the use of outsourcing to meet the large number of orders received. Is there an option to raise the selling prices of these products and cater to select customers?

A. In order to maximize short-term profits, it is effective to accept orders selectively and to cater to orders made at a good price, based on the quantity and steel grade composition that we can produce most efficiently. However, we aim to reform our product portfolio and we are receiving inquiries from all over the world for superalloys. Under these circumstances, we would like to demonstrate our QCD capability to customers in terms of our presence, quality, delivery, etc. so that they will become repeat customers. Even if it means sacrificing a little short-term profit, we would like to respond enthusiastically to orders from the broad range of customers and work to maximize earnings that will come after future capacity expansions.

Q. The sales volume of specialty steel products for the first half of FY2024 is estimated at 526 thousand tons, but when converted to a quarterly sales volume, that figure will be less than 270 thousand tons, which gives the impression of a rather poor level. Could you provide additional information on the current sales situation of specialty steel?

A. As you pointed out, the sales volume of 526 thousand tons for the first half of FY2024 is slightly lower than the 529 thousand tons recorded for the first half of FY2023, and we grant that it is a very low level. We are assuming that demand for specialty steel for automotive parts will remain flat, without taking any chances, and that demand for specialty steel for industrial equipment parts will basically recover from the second half of the year. We do not assume a high sales volume in the first half of the year, because the first half is always a period of lower sales volume due in part to fewer operating days. However, we have the capacity to increase production, and if orders increase, we will be able to seize the opportunity and increase sales.