

Explanatory Material

Re: Sanyo Special Steel (Sanyo) becoming a Subsidiary
of Nippon Steel & Sumitomo Metal (NSSMC)

“ Special Steel ” - specialized, and exists in everyday life

 **SANYO SPECIAL STEEL Co., Ltd.**

September 10, 2018



<http://www.sanyo-steel.co.jp>

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Integration for Maximizing Synergies

As Is

Technology and product superiority in special steel

NIPPON STEEL & SUMITOMO METAL

Other shareholders

100% subsidiary
 Mar. 2018 : Entered into share purchase agreement
 Jun. 2018 : Made OVAKO 100% subsidiary

15% Equity method affiliate

OVAKO

Mainly located in Europe

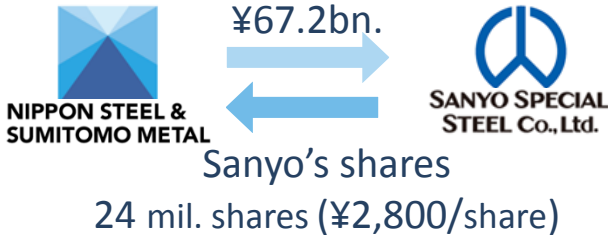
SANYO SPECIAL STEEL Co., Ltd.

Mainly located in Japan & Asia

OVAKO and Sanyo are both special steel makers with global top level technology regarding high-cleanliness steel for bearing steel etc.

Enhancing Global Business

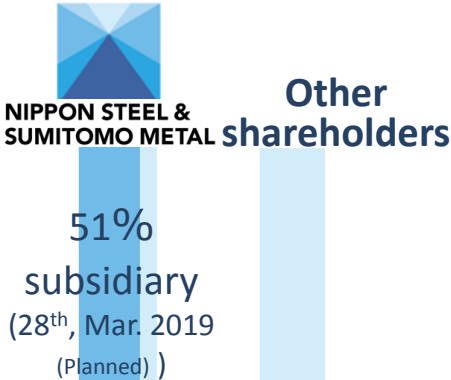
(1) Sanyo will become a consolidated subsidiary of NSSMC through third party allotment



(2) Sanyo will acquire all the shares in OVAKO from NSSMC



To Be



SANYO SPECIAL STEEL Co., Ltd.

100% subsidiary (28th, Mar. 2019 (Planned))

OVAKO

Maximize synergies among 3 companies

Transaction Structure

Points of the Structure

- ❑ Background of making Sanyo a subsidiary of NSSMC and OVAKO a subsidiary of Sanyo
 - Capital structure for maximizing synergies
 - In order to maintain and make use of the established brand of “Sanyo’s bearing steel” in the special steel market, Sanyo will continue to be listed on the First Section of TSE even after becoming a subsidiary of NSSMC by making NSSMC’s shareholding in Sanyo 51% .
- ❑ Financing needs by Sanyo for the acquisition of OVAKO’s shares
 - Secure capital for the upcoming large-scale capital and other investments scheduled under the 10th Medium-Term Business Plan (¥50 billion of capital investment planned by March 2020)
 - To maintain the sound financial position that Sanyo presently enjoys (the amount of debt carried by OVAKO is ¥30 billion. If Sanyo was to borrow ¥67.2 billion (*1) which is the amount necessary for acquiring OVAKO’s shares through debt, the D/E ratio will become approximately 1.2x in comparison to the current 0.3x)
- ❑ EPS
 - The dilution due to third-party allotment is to be covered by the accumulation of OVAKO’s profit and the synergy generated.

Methods of making Sanyo a subsidiary of NSSMC + making OVAKO a subsidiary of Sanyo(*2)

Third-Party Allotment

**Financing and becoming a Subsidiary simultaneously
(D/E change 0.3x → 0.5x)**

**(Dilution of the EPS will be covered by the accumulation of
OVAKO’s profit and the synergy generated)**

Tender Offer + Borrowing Loan

**Requires additional financing
(D/E deterioration 0.3x → 1.2x)**

**(concerns of corporate value declining due to increasing financial
costs and deteriorating D/E)**

(* 1) The difference between the ¥51.7 billion spent for acquisition of OVAKO by NSSMC (June 2018) and ¥67.2 billion spent by Sanyo (scheduled March 2019) is due to the OVAKO’s periodic cash flow intake since NSSMC’s acquisition of OVAKO’s shares worth approximately ¥10 billion, in addition to NSSMC’s additional capital contribution of approximately ¥5.5 billion in response to the future capital requirements of OVAKO.

(* 2) Methods which accompanies public offering was not adopted in order to avoid uncertainties in relation to the structure and schedule.

Technology of Sanyo Special Steel

- **Unique Manufacturing Technology for High-Cleanliness Steel (“Steel You Can Count On”)**

- Development of Manufacturing Process for Ultra-Cleanliness Steel (SURP : Sanyo Ultra Refining Process)

- **Leading Bearing Steel Manufacturer in Japan**

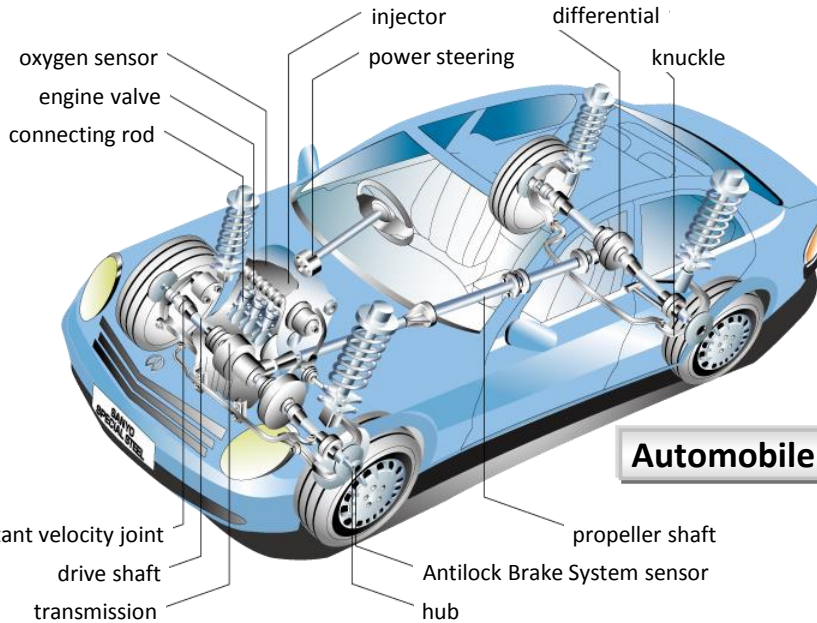


Sequential casting world record of 100 heats with a single tundish (FY2015)

[Example of Use]



Ball Bearing



Automobile



Bearing for Wind Power Generation

Contributing to the development of society by providing “Steel You Can Count On” which has earned a high degree of confidence from the market in respects of development, quality and stable supply

Product Lineup of Sanyo Special Steel and OVAKO

 **SANYO SPECIAL STEEL Co., Ltd.**

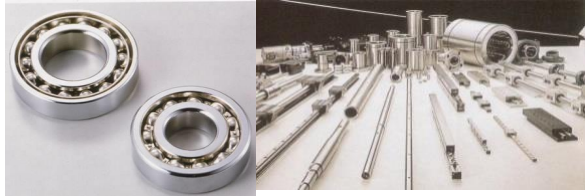
OVAKO

Bearing Steel

High-carbon chromium steel

Bearing steel

Linear motion bearing



BQ-Steel

Bearing Quality

High cleanliness steel used for bearings, with higher loads, downsizing effect, and longer service life



IQ-Steel

Isotropic Quality

Isotropic and ultra clean steel with multidirectional fatigue strength. Contributes to smart solution of components.



Alloy Steel

Shafts for auto

Transmission gears

Gears for differential



Special Steel Market

Material in critical parts for various industries (autos, industrial machinery, wind power generation & robot etc.)

Demand for high-quality special steel will continue to grow steadily

WR-Steel

Wear Resistant

Wear-resistant steel with excellent formability and weldability which contributes to design flexibility and longer service life



M-Steel

Machinability

Low alloyed free cutting steel with exceptional toughness and fatigue strength. Contributes to operational efficiency and cost reduction of component manufacturers.



High Alloy Steel

Precision pipes and parts

Invar alloy for electric power cable

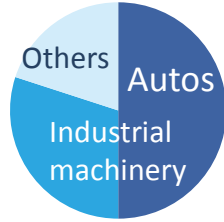
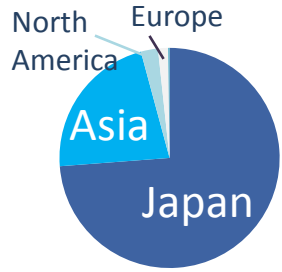
Hot extrusion dies



Markets & Locations of Sanyo Special Steel and OVAKO

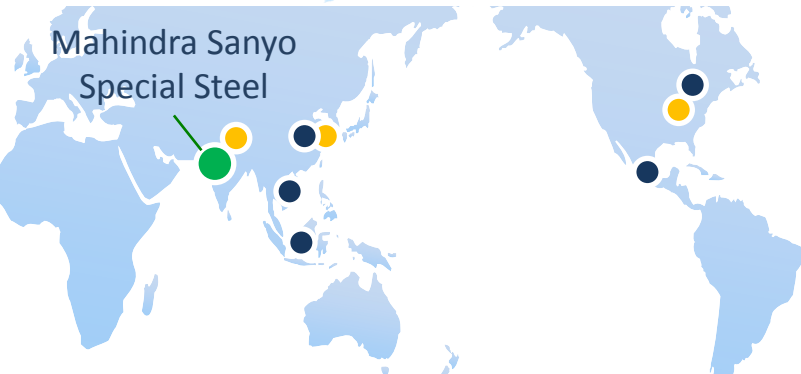
SANYO SPECIAL STEEL Co., Ltd.

< Market > < Customers > < Equipment >



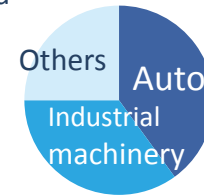
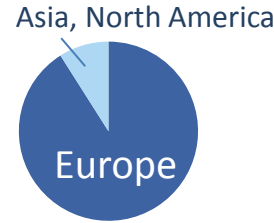
Crude Steel (MMT / year)		1.3
Equipment	EF	2
	LF	2
	RH Degasser	2
	CC	2
	IC	1

< Locations >



OVAKO

< Market > < Customers > < Equipment >



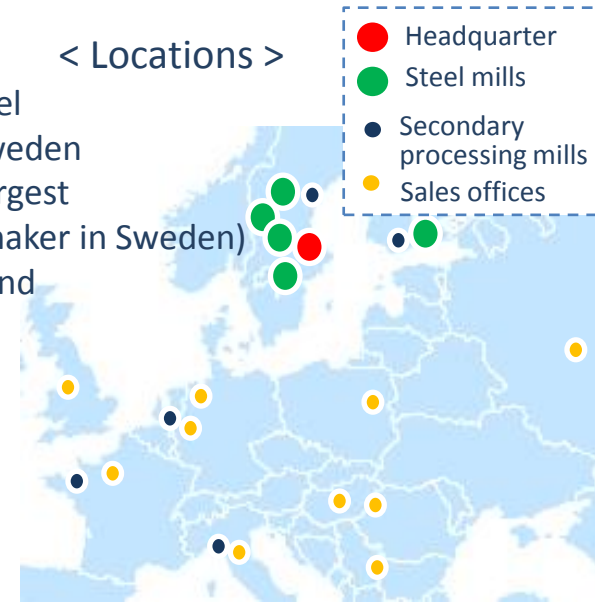
Crude Steel (MMT / year)		1.0
Equipment	EF	3
	LF	3
	RH Degasser	2+1 (plan)
	CC	2
	IC	1

< History >

- 17th Century : Entered in steel business in Sweden
- 1916 : Bought by SKF (the largest global bearing steel maker in Sweden)
- 2010 : Acquired by Triton Fund
- 2018 : Acquired by NSSMC



< Locations >



cf. World's major bearing steel manufacturers

Sanyo Special Steel & OVAKO are the main suppliers for the companies below.

- (1) SKF <Sweden>, (2) Schaeffler <Germany>, (3) NSK <Japan>, (4) NTN <Japan>, (5) JTEKT <Japan>

NSSMC's Special Steel Bar & Wire Rod Business

<Location>

- Special Steel Bar & Wire Rod
- Other Products

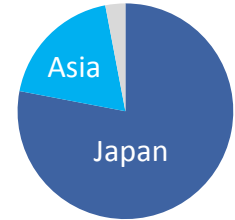


NSSMC has superiority in Structural Steel, Sanyo and OVAKO have superiority in bearing steel respectively

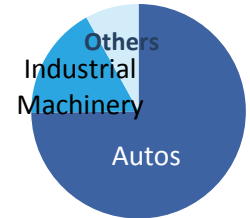
Crude Steel Production (FY2017)

	(10K t/y)
Muroran	143
Yahata(Kokura Area)	120
Subtotal	263
Sanyo Special Steel	130
OVAKO	100
Total (Special Steel)	493
Consolidated (NSSMC Group)	4,912

Market



Customers



<Overseas>

- Special Steel Bar & Wire Rod
- Other Bar & Wire Rod Business
- ★ Overseas Offices



NSSMC Group

**Overseas downstream bases capacity: 22 million tons
inc. Bar & Wire Rod: 1.2 million tons**

★ Global Business Support System of NSSMC

Taking advantage of abundant experience of overseas business regarding various products, support globalization of Special Steel Bar & Wire Rod business

- Global Business Support Center (in Headquarters)
: Support from a professional standpoint on overseas business
- Overseas offices (18 bases in 12 countries)
: Investigation on site, collection of information, communication with various agencies





● Company of Special Steel Bar & Wire Rod

OVAKO AB (Sweden, Subsidiary in 2018 ~ Special Steel)

Suzuki Garphyttan AB (Sweden, Subsidiary in 2009 ~ Valve Spring Wire)

Expected Synergies

Responding to globalization of customers and needs for high quality products,
Sanyo and OVAKO will aim to realize ¥5 billion /year or more synergies
 out of the Approximately ¥10 billion /year total synergies expected for the NSSMC Group

Expected Synergies	Cost Reduction (year)	Efficient Production (year)	Total	Timing of Synergy Realization
 <p>Between Sanyo / OVAKO</p> 	Approximately ¥2.5 billion (included in amount below)	Approximately ¥2.5 billion (included in amount below)	¥5 billion or more (included in amount below)	Synergies are expected to be realized sequentially after 2019; * 50% effect in third year * 100% effect in sixth year is expected, but Sanyo will make efforts to accelerate the timing of realization
 <p>Among Sanyo / OVAKO / NSSMC</p> 	Approximately ¥5 billion	Approximately ¥5 billion	Approximately ¥10 billion	

Breakdown of Synergy	Cost Reduction	<ul style="list-style-type: none"> Improvement of yield rate / consumption rate through the sharing of technical / operational know-how Reduction of labor and repair costs by improving productivity Reduction of shipping costs by replacing the area of production Reduction of procurement costs for materials and equipment
	Efficient Production	<ul style="list-style-type: none"> Aggregate the production of specialty products Improvement of productivity through sharing the manufacturing know-how (utilizing available capacity) etc

Note: Since NSSMC and OVAKO are currently competitors of Sanyo, they cannot exchange necessary information for further analysis of synergies such as customer information, cost information, etc. Accordingly, the above synergy estimates were made based on information that can be duly obtained by each company.

Financial Highlights of Sanyo Special Steel and OVAKO



CY2017
(130¥/€)

Crude steel	1.30 MMT/year (2EAFs)	1.01 MMT/year (3EAFs)
Sales volume	1.07 MMT/year	0.78 MMT/year
Net sales	¥157.4 bn.	€921 mil. (approx. ¥120.0 bn.)
Net profit	¥7.0 bn. [FY2018(E) ¥8.0 bn.]	€15.2 mil. (approx. ¥2.0 bn.) [Jan.-Jun, FY2018 €26mil. (approx. ¥3.4bn.)]
Total assets	¥210.2 bn.	€743mil. (approx. ¥97.0 bn.)
Interest bearing debt	¥28.4bn.	€251mil. (approx. ¥34.6 bn.)
Employees	2,666	Approx. 3,000

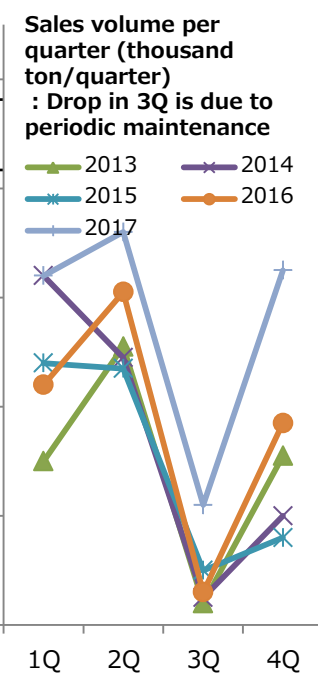
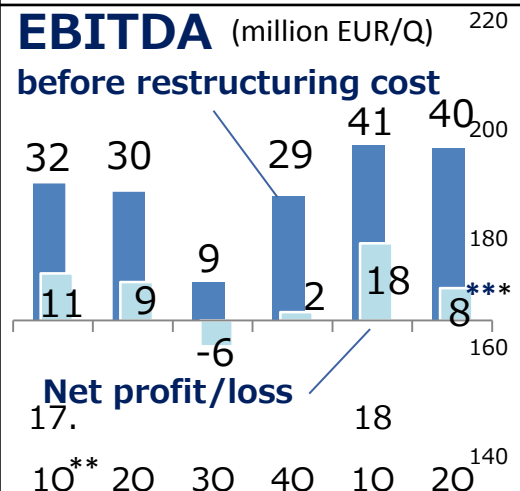
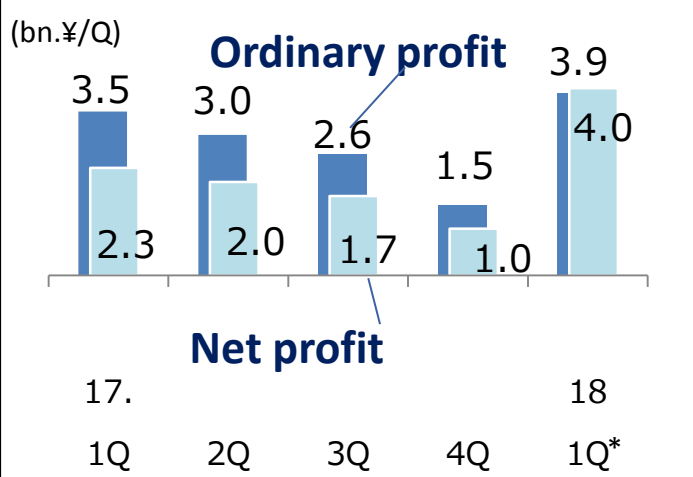
Profit

(bn.¥/Q)

*Sanyo's FY18.1Q net profit incl. gain on step acquisitions of Mahindra Sanyo Special Steel (¥1.46bn.)

**OVAKO 1Q=Jan.-Mar.

***OVAKO 18.2Q Net Profit incl. one-off costs (costs for advanced redemption of bonds etc.) (€12.2mil.)



OVAKO's Expected Net Profit and Financial Position

Net Income

¥6.8 bn. when Net Income for the period of Jan. – Jun. 2018 is annualized

(1st Half Net Income ¥3.4 bn. × 2)

Cf. Depreciation expense is approximately ¥5 bn. / each year

Changing factors assumed from the 1st half to the 2nd half of the year

- ① Seasonal factor (Downside factor for the 2nd half of the year)
 - Decrease in sales volume and increase in cost by periodic maintenance in 3Q
- ② Interest cost reduction (Upside factor for the 2nd half of the year)
 - Switched from bonds to bank loans in the 1st half of the year



Practically zero interest rate
(Will stand the same from this year onward)

- ③ Excluding the effects of one-off costs (Upside factor for the 2nd half of the year)
 - One-off costs incurred due to redemption of bonds (€12.2mil.)

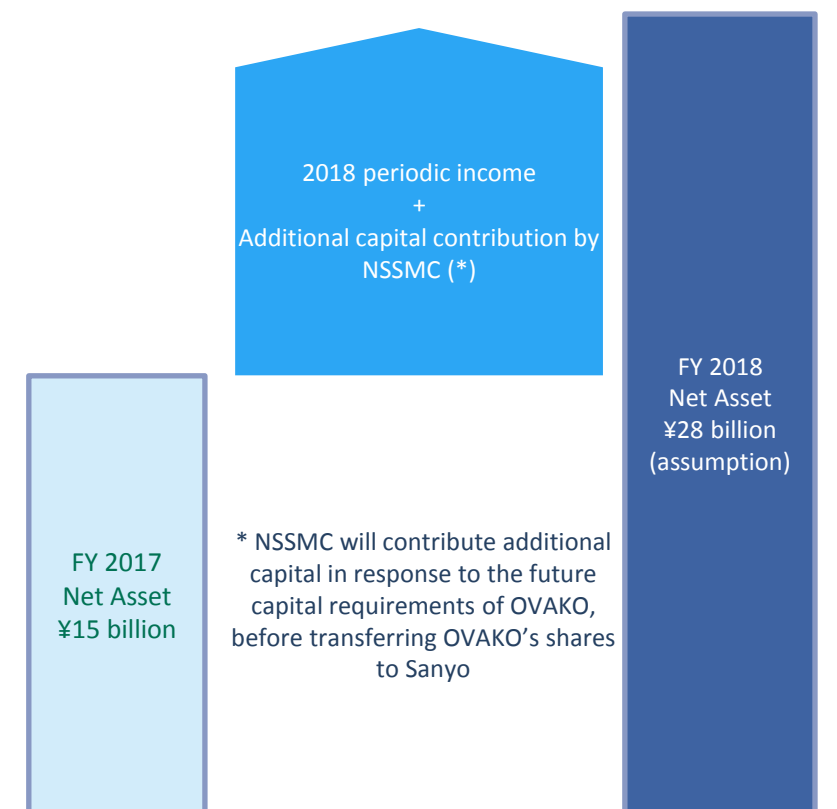
Acquisition of OVAKO by Sanyo: March 2019 (plan)

Net Asset

Net Asset will increase due to additional capital contribution by NSSMC to OVAKO, in addition to FY2018 net income

Amount of **goodwill: ¥30-40 bn.** (assumption)

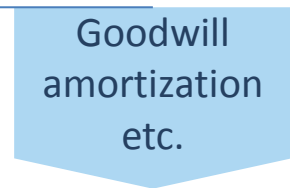
(the amount changes depending on market value of OVAKO's assets and debts/**amortization period is TBD**)



Impacts on Sanyo Special Steel's Consolidated Net Profit

Although synergies are expected to be realized in full on 6th year, below are calculated based on a hypothetical assumption that synergies are fully realized in FY 2018 to provide a image.

cf. Targeted synergy effect
 Before tax : more than **¥5.0 bn.**
 After tax : more than **¥3.5 bn.**



cf.
 Jan. – Jun.,
 FY2018
 Net profit
¥6.8 bn.
 (annualized basis)

Funds are used for
 acquiring OVAKO shares



72% increase
 (75% after
 deducting
 treasury
 shares)



cf.
 FY2018(E)
 Net profit
¥8.0 bn.
 incl. gain on
 step acquisitions of
 Mahindra Sanyo Special
 Steel (¥1.46 bn.)



- OVAKO's earnings are approx. **85%** of Sanyo's earnings (②÷①)
- Total amount of OVAKO's earnings and synergies (after tax, excluding amortization of goodwill) is approx. **130%** of Sanyo's earnings ((② + ③)÷①)

EPS is expected to improve

Schedule

Jun 1st, 2018 – Acquisition of OVAKO by NSSMC

Aug 2nd, 2018 – Execution of agreements;

(a) making Sanyo a subsidiary of NSSMC,

(b) transferring all shares of OVAKO to Sanyo from NSSMC

After Aug, 2018 – Approval from competition authorities in Japan and overseas

Around Feb. 2019 (plan) – Sanyo’s Extraordinary general shareholders’ meeting

Mar. 28th, 2019 (plan) – Payment date of Third-Party Allotment & obtaining OVAKO’s shares

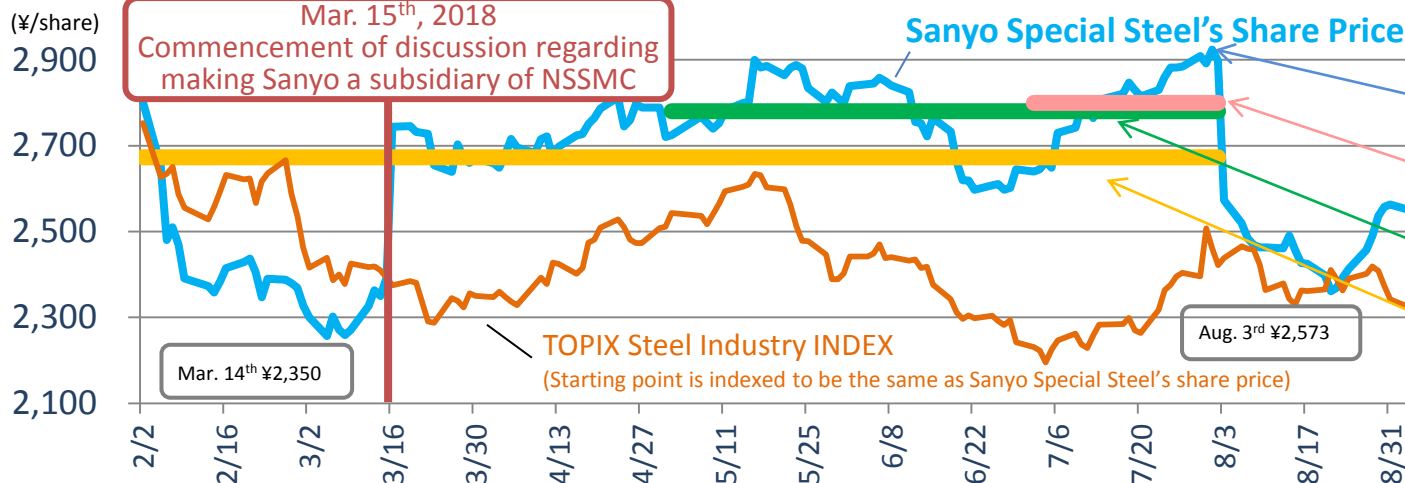
The policy is to maintain the listing of on the First Section of the TSE after the transaction

~Overview of the procedure and

measures to secure fairness of the transaction~

- Sanyo appointed Chuo Sogo Law Office, an independent third party, as its legal affairs advisor and received extensive advice on legal issues concerning the conversion into a subsidiary in the course of procedures
- Sanyo established an **Independent Committee**, consisting solely of independent parties, and obtained an opinion that the purpose and procedures of the transaction are fair and appropriate
- Furthermore, in order to properly reflect the shareholders’ intention, the capital increase through a third-party allotment of shares is subject to the condition that Sanyo obtains approval from the shareholders at the **extraordinary general shareholders’ meeting** scheduled to be held in Feb. 2019
- Please refer to the press release disclosed in Aug 2nd, 2018 “Notice on Issuance of New Shares Through a Third-Party Allotment to Nippon Steel & Sumitomo Metal Corporation and Change in Parent Company” for above details

Trend of Sanyo Special Steel’s Share Price



Issue Price

= ¥2,800

(+19% Mar. 14th price)

The reference date

(Aug. 1st) = ¥2,924

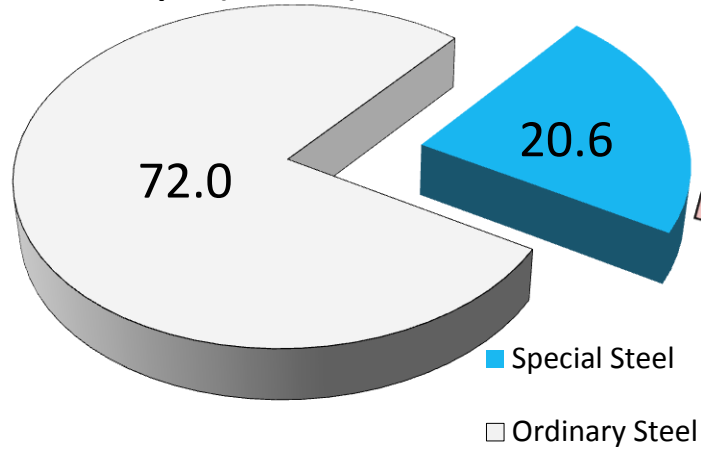
1 month ave.=¥2,800

3 months ave.= ¥2,780

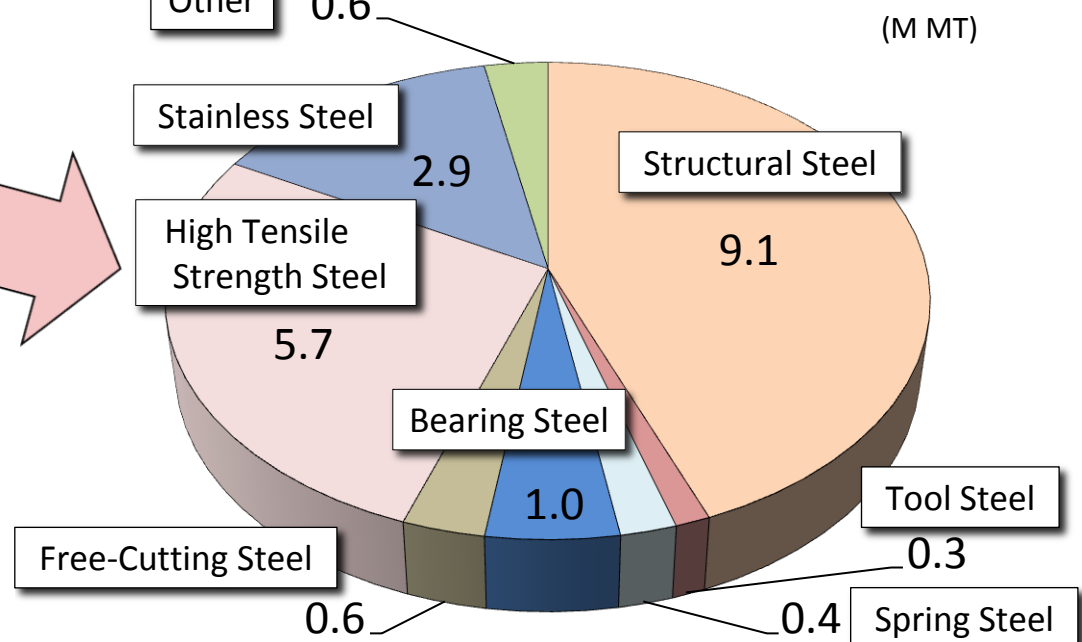
6 months ave.= ¥2,673

(Ref.) About Special Steel

Hot-rolled steel production in Japan(FY 2017)



Breakdown by special steel grade



Classification of Steel

- Ordinary Steel—Mild Steel—Rolled Steel for General Structure(SS), Rolled Steel for Welded Structure(SM), Steel Bars for Concrete Reinforcement(SR,SD), Low Manganese Non-Tempered High Tensile Strength Steel
- Special Steel
 - Structural Steel—Mechanical Structural Carbon Steel(S10C, S45C etc.)
 - Mechanical Structural Alloy Steel—Chromium steel(SCr), Chromium Molybdenum Steel(SCM), Nickel Chromium Molybdenum Steel(SNCM)
 - Pressure Vessel Steel—Carbon Steel for Boilers and Pressure Vessels(SB), Chromium Molybdenum Steel for Boilers and Pressure Vessels(SCMV)
 - Tool Steel—Carbon Tool Steel(SK), Alloy Tool Steel(SKD SKT), High-Speed Steel(SKH)
 - Steel for Special Use—(Low-Alloy Steel) Spring Steel(SUP), Bearing Steel(SUJ), Free-Cutting Steel(SUM), Non-Tempered High Tensile Steel
 - (High-Alloy Steel) Stainless Steel(SUS), Heat-Resistant Steel(SUH), High-Manganese Non-Magnetic Steel
 - (Carbon Steel) Spring Steel(SUP), Piano Wire Rod Steel(SWRS)

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