30 October 2015

Mitsui O.S.K. Lines, Ltd.

1. Supplementary Explanation of FY2015 Q2 Financial Results

[Overall]

Ordinary income for the first half (H1) (six months) totaled ¥27.7 billion, exceeding the outlook announced on July 31. On the other hand, net income/loss showed a slight deficit due to the recording of a ¥26.2 billion extraordinary loss from stock revaluation of the equity method affiliate Daiichi Chuo Kisen Kaisha as a result of that company's decision to commence civil rehabilitation proceedings on September 29.

Ordinary income exceeded the previous outlook, although results varied by division—a downturn in the containership business was offset mainly by tankers. This situation continued even in the second quarter (Q2). In the tanker division, the product tanker market was higher than originally forecast, a key factor behind the company exceeding its previous outlook. Results for dry bulkers were close to the previous outlook.

In a year-on-year comparison, consolidated ordinary income increased by ¥13.2 billion. This was the result of favorable conditions including the depreciation of the yen and lower bunker prices in addition to a significantly improved tanker market.

[By segment]

<Bulkships>

■Dry bulkers

Ordinary income for the division decreased significantly year-on-year, but showed a slight upturn from the initial outlook, securing profitability. Most of the company's spot, mid- and small-sized vessels are operated by a subsidiary in Singapore, which closes its financial term in December, and the market from April to June is reflected in Q2, so the results for H1 are almost fixed as of July 31, when the previous announcement was issued. Therefore, changes from the previous outlook are limited to some spot-market vessels operated in Tokyo, including Capesize vessels, steaming coal carriers, and woodchip carriers. The markets for those vessels from July to September also remained at the same level as in the previous outlook.

Meanwhile, Daiichi Chuo Kisen was removed as an equity method affiliate due to its civil rehabilitation proceedings. As a result, starting in Q2, we did not record "equity in losses of affiliated companies" related to that company.

Looking at the dry bulker market, the Capesize market turned upward to the $20,000-level in August, due to increased shipments of iron ore from Brazil, which is a long-distance source, since June, in addition to steady shipments from Western Australia. At the same time, the number of Capesize vessels in operation showed a net decrease since the beginning of this year, with 77 new vessels built and 84 scrapped.

However, after August, the market followed a downward trend due to factors including the deceleration of the Chinese economy. Unfortunately, the markets for mid- and small-sized vessels also remained low level due to China's economic slowdown and concerns over stagnation in other emerging nations' economies.

■ Tankers

The market remains strong due to an increase in transport demand backed by low crude oil prices. Ordinary income for the previous year's Q2 recorded a slight surplus, but Q2 of this fiscal year brought a significant increase. It exceeded even the previous outlook as the product tanker market moved higher than anticipated.

■ LNG carriers/Offshore business

This division recorded stable profits due to long-term contracts. On a year-on-year basis, ordinary income increased significantly due to the start of new projects and the absence of temporary costs incurred during the previous fiscal year, such as dry-docking fees.

■ Car carriers

Trade to North America showed strength. On the other hand, trade to resource-exporting nations slowed as declining crude oil prices eroded their purchasing power. Trade volumes for West Africa and Russia, where MOL is relatively strong, showed a declining trend. There were both positive moves and negative moves, but on the whole, the division achieved the same level of results, in a year-on-year comparison, as the previous outlook.

Overall in the bulkship segment, consisting of these four business divisions, ordinary income increased significantly in a year-on-year comparison, marking an upturn from the previous outlook.

<Containerships>

Except for the Asia-North America route, markets declined more severely than anticipated, and the H2 results for the segment were lower than the previous outlook, despite a slight improvement in a year-on-year comparison.

By route, cargo movement on the Asia-Europe trade decreased, and consequently, the

supply and demand balance deteriorated significantly and the market declined. This was the biggest factor. Spot rates on the Asia-South America East Coast trade dropped down to under $200 per TEU as cargo traffic decreased due to Brazil's sluggish economy. As a result, these two routes suffered serious losses. On the other hand, the Asia-North America trade achieved profitability in Q2. Meanwhile, the Europe-South Africa and Asia-South Africa trades achieved stable profits. Profit/loss for the first half on the Intra-Asia trades, in which MOL holds a relatively strong share, improved sharply as a result of restructuring and rationalization. In the last year, all routes faced unfavorable situations, but this fiscal year, conditions on some routes became much worse, while some others showed improvement one way or the other.

<Others>

■ **"Ferry and domestic transport business," " Associated businesses," "Other businesses," and "Adjustment"**

After a tragic fire incident aboard the MOL Ferry-operated Sunflower Daisetsu, for which we offer our sincere apologies, our ferry service cut some of its initially planned voyages. But recent issues such as a shortage of truck drivers and the growing trend toward what is known as the "Modal Shift" are keeping demand strong and our profit has been in line with the outlook, except for the impact of the fire incident.

[Extraordinary profit/loss]

We recorded an extraordinary loss of ¥26.2 billion from the stock revaluation of our affiliate Daiichi Chuo Kisen. We do not have any other extraordinary losses related to this matter.
On the other hand, we recorded an extraordinary gain of ¥4.3 billion from cancellation fees for charter contracts in the bulkship segment. As a result, the net extraordinary profit/loss for the first half showed a loss of -¥19.2 billion.

2. Supplementary explanation of FY2015 full-year forecasts

[Overall]

Looking at our full-year forecast, we regret to say we made a downward revision of ¥18 billion in our previous forecast announced on July 31, from ¥60 billion yen to ¥42 billion, which was a decrease of 18% in a year-on-year comparison. The main reason for the revision is that we have reviewed the assumptions for freight rates and liftings of the containership segment in the outlook considering the current market situation. We did not change our forecast for the bulkship segment (¥55 billion for the full-year ordinary income) from the previous outlook, although from a division-wise viewpoint, the tanker

market is slightly stronger than the previous outlook, whereas the dry bulker market is expected to be slightly lower.

We made a downward revision of ¥26 billion for full-year net income from the previous outlook of ¥43 billion to ¥17 billion. We plan to record an extraordinary gain due to the sale of shares in the second half, and project a reduction in our net extraordinary loss from ¥19.2 billion in H1 to ¥8.5 billion for the full year.

[By segment]

<Bulkships>

■ Dry bulkers

We slightly reduced the market assumption. We expect the market to rise annually due to an increase in shipments during the winter season, but in reality, we could not see signs of recovery even as October began. China's ore import volume remains flat, and is in some cases declining. We think this is a major cause. However, the actual export volume of iron ore from Australia and Brazil shows a great increase. Speaking of vessel supply, we are seeing a net decrease, so it is hard to imagine a slackening of the market, but one factor we see in the background is that China's small and mid-sized steel companies are cutting back or even halting production. These small and mid-sized steel companies do not import mass volumes of cargo, which leads to inefficient unloading operations at ports. So, if production centers on major steel companies, the actual fleet supply will increase more than the apparent fleet supply because large-sized vessels like Valemax will be used and loading/unloading operations will become more efficient, which in turn improves the efficiency of overall vessel operation. This is the presumption of the division responsible for this business. Filling in the details will require more analysis, but in any event we do not anticipate a large upswing in the market this time. The supply and demand imbalance of small and mid-sized vessels is not showing improvement, so we expect the sluggish market to continue.

We secure profits from mid- and long-term contracts, and think we can secure profitability for the full-year even though we have spot vessels that are susceptible to market volatility.

■ Tankers

The tanker market is softening at this moment. We believe this is due to a temporary phenomenon—reaction to a large upswing of the market in October, or more vessels returning to service after dry-docking. We think the market is not fundamentally changing due to factors such as winter seasonal demand and low crude oil prices, increased refinery operating capacity, and higher inventories, so we expect the market to remain strong overall.

The product tanker market is also softening right now, in line with regular repairs of refineries and the end of the summer driving season, but we expect the market to recover due to seasonal demand for heating oil in the winter.

As a result, we project that ordinary income for the tanker division will show a significant increase for the full year in comparison to the previous fiscal year, exceeding the previous outlook.

■ **LNG carriers/Offshore business**

The division remains in a favorable position thanks to stable profits from long-term contracts. This year, four new LNG carriers and one FPSO (MOL's third) started operation, and these will contribute to the division's profits, so the outlook for the full year will be the same as previously announced.

■ **Car carriers**

We expect the car carrier market to continue the trend as we explained above, anticipating the same level as the previous outlook.

<Containerships>

We made a downward revision to a deficit of ¥28 billion for the full year due to a large deterioration of the market. We thought we could expect a temporary increase in freight rates in line with a rush in liftings before China's National Day holidays in October. But unfortunately this ended in failure. We see hardly any improvement in conditions from the beginning of autumn to winter. We anticipate a solid rise in rates before the Chinese New Year, but we have no choice but to make a large downward revision considering that we were unable to raise rates at the beginning of autumn. Although we did not address this issue in our outlook, we are planning a rate increase on the Asia-Europe and South America East Coast routes in November. If we succeed with the rate increase in November, this will become a positive factor. In any case, it is hard to imagine that the unimaginable low rates of $200/TEU or even near $100/TEU will continue.

As a matter of course, shipping companies have entered the adjustment stage of supply/demand gaps. On the Asia-Europe route, the G6 alliance has already decided to reduce space by 25%. On the Asia-South America East Coast route, the consortium we belong to has already reduced space by 30%. Thus, we have been making efforts to raise freight rates by reducing supply and demand gaps.

In addition, we are working on our own to restructure and rationalize routes. Aside from

the Asia-South America East Coast route, we integrated and restructured Intra-Asian routes serving Thailand and the Philippines. Services such as the Europe-West Africa, North America East Coast-South America West Coast, and China-Vietnam routes were already suspended. We have also worked earnestly to downsize the fleet. During the first half, we returned 19 charter vessels, mainly mid-sized ships, in some cases paying cancellation fees during the first half. On the other hand, we took delivery of four advanced 10,000 TEU vessels, which are highly competitive. We strive to increase competitiveness through such measures, and the number of vessels in operation decreased by 15 from 118 at the end of March to 103. Thus, we will continue to push ahead with rationalization to improve profitability, doing our best to ensure that our performance exceeds the outlook.

<Others>

■ **"Ferry and domestic transport business," " Associated businesses," "Other businesses," and "Adjustment"**

This time, we made a downward revision of ¥2.0 billion from the previous outlook in "Adjustment." This is due to our anticipation of a loss on the bunker swap in the headquarters' accounts in the second half related to declining bunker prices, and a decrease in foreign exchange gains from the previous outlook..

[Extraordinary profit/loss]

We plan to record an extraordinary profit from the sale of shares during the second half.

[Investment plans/Cash flows]

We expect that cash flows from investment activities will further decrease to ¥40 billion from ¥70 billion in the previous outlook for fiscal year 2015. This is not due to a scale-down of our investment plan itself, but rather to the sale of shares included in the second half, and returns of shareholder's loans from a joint venture, because project financing started earlier, in line with an earlier start for our FPSO project. We will continue investment in pursuit of stable profits in the future.

[Dividends]

We plan to make a downward revision of the initially planned full-year dividend, from ¥7 per share to ¥5 due to a downward revision of the full-year outlook. As for the interim payment, considering that we could achieve better results for H1 than the previous outlook, we maintained the ¥3.5 per share payment. So the year-end payment will be ¥1.5 per share. The dividend payout ratio for the full year will be 35%. Naturally, we remain hopeful that an improvement in profitability would allow the payment of a higher dividend.

3. Questions and Answers

[Containerships]

Q1) Please provide a breakdown by route and factor, regarding the downward revision of ¥14.5 billion for full-year ordinary income for containerships, compared to the previous outlook.

A1) By route, nearly half of the ¥14.5 billion is related to the Asia-Europe routes, followed by the North-South routes, particularly the Asia-South America East Coast route. Looking at the factors, the decline of bunker prices is a positive of ¥7-8 billion, so please understand that net out at ¥21 billion is a downturn from the outlook due to declining freight rates and liftings.

Q2) Please explain which directional trends led you to revise your assumption for freight rates. And is the spot ratio changed?

A2) Speaking of direction, there is a trend toward increasing rates even in the short term by reducing space, but the assumption of freight rates for Q3 is the same level as the actual rates as of the end of September or lower, and in Q4, rates will recover slightly due to the cargo rush before the Chinese New Year. Thus, we weave those directional trends into our assumption. Nonetheless, by route, we anticipate that freight rates on the Asia-North America routes will decline a little more slowly and that those on the Asia-Europe routes will decline to a greater degree in Q3. Our spot ratio has not changed up to this point.

Q3) Please explain if there is any room to further rationalize the containership business, and if you are examining the idea of completely stopping specific routes.

A3) We continue to work on reducing service frequencies and space on key routes through alliances, and as our independent measures, we are going take a surgical approach to cutting routes on which demand and supply are imbalanced, and those on which we can hardly expect profitability to improve in the mid- and long-term view. We will also take thorough measures to scale down the number of vessels in operation and to reduce the number of high-cost vessels in service. Meanwhile, we already stopped the Europe-West Africa route and North America East Coast-South America West Coast route. We continue rationalization including withdrawal and suspension of services as necessary.

Q4) The midterm management plan states the policy to expand the containership fleet and your company has already ordered large-scale vessels. You say you will further promote rationalization such as suspension of routes, but please explain whether the assumption of

the midterm management plan will be changed or not.

A4) We are facing a situation in which we need to make a slight revision from the trading environment we assumed when we established the midterm management plan, although this does not mean we will abandon the various targets stated in the plan. When we developed the plan, we thought the global container trade would grow smoothly and steadily, though at a slow pace, as long as population grows, and that we would not see a great degree of disorder in the fleet supply. We are planning to review our capacity again while rationalizing services and returning vessels as necessary to improve profitability.

[Bulkships]

Q1) This time you didn’t change the outlook for the full-year ordinary income of the bulkship segment, but please explain how you changed the breakdowns of dry bulkers, tankers, and others.

A1) Combining all factors — tankers are on an upturn, car carriers are leveling off, and dry bulkers are showing a slight downturn from the outlook – the end result is neutral from the previous outlook.

Q2) You anticipate that the tanker market for the second half will be improved from today’s level. Please explain your outlook of whether these favorable market conditions will be sustainable even for the next fiscal year and after.

A2) We expect the second half of this fiscal year to be firm. On the other hand, we feel it’s a little optimistic to assume that the current market situation will remain at the same level in FY2016. We think this requires further examination.

Q3) The tanker market, including VLCCs, has been quite strong. Are you working to build up stable profits in response?

A3) We do not have many spot VLCCs, but we have actually succeeded in building up mid- and long-term stable profits by cutting deals for a few vessels under the current favorable market conditions.

Q4) Please explain the effects of improvement in ordinary income by dropping Daiichi Chuo Kisen as an equity-method affiliate.

A4) Ordinary income improved by a little more than ¥1 billion in Q2 (three months).

Q5) Will you continue to invest in LNG carriers/offshore businesses, which contribute to stable profits? Based on today's situation, will future investments in such businesses be able to achieve profitability? What is the possibility of reducing investment?

A5) The environment surrounding LNG carriers and offshore businesses has changed drastically from the time when we established the midterm management plan. New drilling plans, particularly for overseas projects, are slowing down due to declining crude oil prices. Therefore, we have no choice but to say it will be hard to reach the targets set forth in the midterm management plan exactly as initially planned. However, this is a slowdown; it does not mean these projects will be completely put on the shelf. So we believe the movement of those projects depends on the movement of crude oil prices. The time frame may be changed, but these businesses will continue to be our key investment fields.

[END]