January 31, 2017

Mitsui O.S.K. Lines, Ltd.

Explanation by the CEO and Major Q&A

1. Supplementary Explanation of Q3 FY2016 Financial Results

[Overall]

Ordinary income for the first nine months was ¥13.8 billion, a significant decrease of ¥24.9 billion in a year-on-year comparison, but the income for three months from October to December was ¥8.3 billion, a sharp increase from the previous quarter. Three months ago, I explained here that "The results for the first half accounted for some of profits for the second half in advance," and we took a very hard look at our internal assumption for the third quarter. But Q3 ended substantially higher than our internal assumption.

Meanwhile, net income for the first nine months showed a surplus of ¥19.0 billion, due mainly to the sale of non-core assets during the first half as a part of the Business Structural Reforms.

[By segment]

<Bulkships>

■ **Dry bulkers**

The dry bulker market, which reached a record low from January to February of 2016, hit bottom after that but has yet to regain much strength.

The Capesize market showed a temporary recovery along with firm shipments of iron ore from Western Australia and Brazil in late November, but its move was limited in December, and the spot charter rate declined gradually. The average spot charter rate for nine months is approximately $9,000, which is the same level as the same period in the previous year and remains far below the industry's average cost.

Markets for Panamax and mid- and smaller-size vessels rode on the strength of the harvest season for North American grain and firm coal trade in November. However, towards the end of the year, the markets weakened due to the impact of the Christmas holidays.

On the other hand, the dry bulker division can earn steady profits even under today's difficult market environment due to the positive effects of the Business Structural Reforms we conducted last year, in addition to the stable profits earned from long-term cargo contracts, mainly for Capesize vessels. For the first nine months of the fiscal year, the division ended with a slight upturn from our previous internal assumption and with a substantial increase in a year-on-year comparison.

- **Tankers**

  The crude oil tanker market improved significantly since the beginning of fall, due to the restart of crude oil shipments from Nigeria after the domestic conflict settled down, which was one of the factors for the market slowdown in summer, and the start of the winter demand season. The product tanker market remained weak, while trade of vegetable oils and other cargoes remained stagnant and newbuilding vessels were delivered one after another.

  Overall, the market weakened from the previous fiscal year, but despite a significant decrease in a year-on-year comparison, the tanker division recorded profits in line with the previous internal assumption, as a result of efforts to boost operational efficiency through pool operation, in addition to stable performance under long-term contracts.

- **LNG carriers / Offshore businesses**

  The division recorded stable profits from long-term contracts, in line with our internal assumption.

- **Car carriers**

  While trade to the U.S. and Europe remained firm, trade to the Middle East, West Africa, and other resource-producing countries remained weak due to the impact of lower resource prices. There are two aspects to this situation. One is the impact of a decrease in trade volume from Asia to the Middle East and Africa, where profit margins are higher, despite smaller shipment volume compared to trade to Europe and the U.S. The other is that we could reduce costs for ballast sailings, i.e., repositioning vessels with no cargo to Japan, for example, by securing car shipments from Europe and the U.S. to the Middle East and Africa, or by chartering out vessels to European shipping companies that have cargoes on those trades. But in fact, shipments from Europe and the U.S. to the Middle East and Africa declined just as they did from Asia , making it difficult to achieve such efficient ship allocation. We have worked to improve operational efficiency, such by responding to changes in trade patterns and swiftly taking the initiative to reduce the number of vessels in our core fleet, and at the same time avoiding an increase in ballast sailing by using one-way spot charter vessels to cover increased trade volume from Asia for North America. But ordinary income deteriorated significantly in a year-on-year comparison, so we regret to report a slight loss for the first nine months.

Accordingly, combined ordinary income of the four divisions in the Bulkship segment for the first nine months was ¥25.8 billion, a significant decrease from the same period of the previous year, but ended with a slight upturn from the internal assumption at the previous announcement.

<Containerships>

On the Asia-North America route, cargo volume from Asia for October to December increased by nearly 10% in a year-on-year comparison. Cargo volume marked a record high, due partly to a rebound from the disruption of logistics by the bankruptcy of Hanjin Shipping in September. In particular, cargo volume remained firm for October – November, normally a slow season due to Golden Week holidays in China. Soon afterward in December, we saw an upswing in cargo volume apparently reflecting last-minute demand before the Chinese New Year. Freight rates rose due to these moves, and now stand at a record high for this fiscal year.

The Asia-Europe route remained firm without a decline in cargo volume during the normally slow season, and we have maintained full utilization on our vessels almost every week since November. And even though we saw some increase in freight rates on this route in December, the start of the busy season, but looking at the past three months, the average rates could not reach the expected level.

Overall for the third quarter, both cargo volume and freight rates increased more than the previous outlook, except for rates on the Asia-Europe route. The ordinary loss for three months was minus ¥4.7 billion, an improvement from the previous internal assumption despite deficits, due in part to a reduction in operating costs such as expenses for positioning empty containers through improved yield management. We can say we saw a significant improvement for the third quarter, which is ordinarily a slow season, from the ¥9.7 billion loss recorded in the previous quarter.

2. Explanation of FY2016 Full-year Forecast

[Overall]

While we made an upward revision of ordinary income/loss from a deficit of ¥3.0 billion in the previous outlook to a surplus of ¥11.0 billion, we made a downward revision of net income from the ¥7.0 billion previously announced, to zero. This downward revision is due to concerns about impairment of owned containerships resulting from a significant decline in secondhand containership prices.

In the previous fiscal year, we recorded an extraordinary loss of about ¥60.0 billion related to containerships as a part of the Business Structural Reforms, and much of the loss results from the impairment of owned containerships. Since then, in less than one year, the market prices for secondhand containerships faces an even more significant decline, and concerns are emerging about additional impairment in the fourth quarter, which depends on future trends in ship prices and a breakdown of targets for the next fiscal year. So, we conservatively included this possibility in the outlook and decided to announce it to our shareholders and investors in a timely manner.

Now let me explain a little further. Although I have talked about a decline in prices of secondhand containerships, these are merely indicative prices as there have been almost no actual sales and purchases recently. What is happening is that many containerships are being scrapped. During 2016, containerships equivalent to about 650,000 TEUs, a record high, were scrapped. This equals about 3% of total worldwide containership capacity. As a result, we see that the increase in supply for 2016 was far lower than the 3% assumed, and ended at around 1.5%. This is proof of progress in self-adjustment on the supply side, while the demand and supply balance has not improved for a long time. But that adjustment is still insufficient, reflecting a significant decline in secondhand containership (indicative) prices.

Turning to dividends, we made a ¥2 per share interim payment for the first half, which showed a surplus of ¥16.0 billion of net income, but as we project deficits for the second half, we decided not to pay a year-end dividend, which we previously stated as “to be announced.”

[By segment]

<Bulkships>

- **Dry bulkers**

Normally, the dry bulker market is on a downward trend from January to March. And it reached a historic low from January to March last year. But we forecast only a limited downward movement in the overall market this year, mainly because China’s demand for steel is firm and grain shipments from the East Coast of South America are showing an upward trend. As a result, ordinary income for the full year will be nearly the same as the previous outlook, and we project a surplus for this fiscal year, in contrast to the deficits of the previous year.

- **Tankers**

Turning to the tanker business, we made a slight downward revision of the earlier Q4 outlook for both VLCCs and product tanker markets, but we anticipate that ordinary income/loss for the full year will end nearly in line with the previous outlook. On the other hand, it will decrease significantly from the previous year, when the market boomed. Turning to the tanker business, we made a slight downward revision of the earlier Q4 outlook for both VLCCs and product tanker markets, but we anticipate that ordinary income/loss for the full year will end nearly in line with the

previous outlook. On the other hand, it will decrease significantly from the previous year, when the market boomed.

- **LNG carriers / Offshore businesses**

Fourteen new projects started during this fiscal year, ensuring a stable accumulation of profits.

- **Car carriers**

We still have not seen any sign of recovery in trade to resource-producing countries. We have worked continually to improve operational efficiency. As a part of these efforts, we reduced the number of vessels in our core fleet by four since the beginning of this fiscal year, but we are considering a further decrease depending on future trends. We regret to say that we anticipate slight deficits in ordinary income/loss for the full year.

As a result, we made a slight upward revision of ordinary income for the full year for the entire Bulkship segment, to ¥30.0 billion, from the previous outlook of ¥28.0 billion.

<Containerships>

The outlook for ordinary loss for the full year has improved from minus ¥44.0 billion at previous announcement, to minus ¥40.0 billion, though it is still a large deficit. It reflects factors including annual contracts at higher rates than the previous year for the Asia-Europe route, most of which have already been settled, in addition to increased liftings on the Asia-North America and Asia-Europe routes and a firm transition of spot rates, despite the impact of higher bunker prices.

Cargo volume is forecasted to decrease after the Chinese New Year holidays, but alliances have already announced measures to cut frequencies in response. Capacities on both the Asia-North America and Asia-Europe routes are projected to decrease significantly. However, we are anticipating some decline in freight rates in March and include this assumption in our outlook.

Looking toward renewals of annual contracts, the impact on ordinary income for this fiscal year is limited, but 90% of contract renewals on the Asia-Europe route have ended, and an encouraging number of rate hikes have been agreed upon. Many of the contract negotiations on the Asia-North America route will start somewhat later, but looking at the current situation, we strongly believe we will be able to make some progress in recovering contracted freight rates, which declined significantly in last year’s renewals.

In contrast with the decline in secondhand containership prices that I explained earlier, along with concerns about impairment, freight rates remain on a recovery trend that began in early autumn of last year. In the background, this is a recent rise in cargo trade, of course, but in addition, we see a megatrend with two aspects – one related to physical capacities and another related to market sentiment.

Concerning capacities, as I explained, the number of vessels scrapped has exceeded expectations, and about 60 of Hanjin Shipping’s former vessels (equivalent to 2% of the total capacity in the industry) are still not in operation. So the supply did not increase substantially from FY2015. It will still take time to significantly improve the demand and supply gap since large-size vessels are still slated for delivery. But we think that factor will help control expansion of the demand-supply gap.

From the viewpoint of sentiment, a sudden bankruptcy of a major shipping company like Hanjin Shipping is naturally a huge shock to customers as well. Customers started paying more attention to stably securing space with reliable, credible shipping companies that offer precise follow-up and can prevent problems in their supply chains. We see this as another factor.

In the containership business, we are seeing signs of gradual improvement although the profit picture remains difficult. Despite such situation, we regret that we made a downward revision of the net income outlook for this fiscal year. It is hard to deny that the number of containerships, which are not in high demand in the current market, is increasing, and while some will be scrapped, second hand containership prices remain on a downward trend. And we have no choice but to include these factors as concerns for impairment of owned containerships in the outlook we announced today. But over the coming year, we will continually endeavor to enhance cost reduction, sail before the favorable wind of recovery in the freight rate market, improve profitability to the greatest extent possible, and then finally, soundly hand over the business to the new joint-venture company. We would deeply appreciate your understanding and support.

3. Questions and Answers

[Concerns about Impairment Loss on Containership Business]

Q1) How did you set the ship price, which is the assumption of your forecast for the amount of impairment loss in the containership business?

A1) Actually, the current indicative price of secondhand containerships remains at half the level of our owned containerships’ book value. This is only the indicative price, and we need to keep a careful watch on trends in containership prices. We will monitor these trends as of the end of this fiscal year, and then post the amount of impairment as an extraordinary loss if necessary.

Q2) I understand that your decision whether or not to post the impairment loss and the amount of the impairment are determined by containership price trends. What do you mean when you say the impairment amount is also affected by the budget for the next year?

A2) As an evaluation criterion for the necessity of an impairment loss in containerships, and the amount thereof, we need to take into account the cash flow under the future profit plan, in addition to market prices of the assets we hold. In this regard, we have not set financial targets for coming fiscal years, but if the total amount of the future cash flow surpasses the book value of owned containerships, we don't need to claim an impairment loss. So our explanation reflects these considerations.

[FY2016 Full-year Forecast]

Q1) I understand that you projected an improvement of ¥4.0 billion from the previous forecast in the forecast of the containership business for the full-year 2016 and most of the improvement is due to the market conditions. What percentage is the result of your efforts to boost profitability, such as improving yield management?

A1) About half of the ¥4.0 billion improvement is due to self-supporting efforts such as improvement of operational efficiencies.

Q2) It seems that profit and loss in the containership business from Q3 to Q4 do not correspond with trends in the average freight index of all routes. Can you explain this mismatch to me?

A2) The containership business will deteriorate from Q3 to Q4 in terms of ordinary profit. As a breakdown of the difference, an increase in freight rates almost offsets an increase in bunker prices. On the other hand, a decrease in liftings due to a seasonal slowdown and increased feeder costs due to reduced frequencies account for one third of the drop. In addition, about one third is generated by adjusting agency outsourcing costs between MOL and its consolidated subsidiaries. This means the profit and loss improved in Q3, but the deterioration in Q4 offset Q3 improvement in accounting, so this does not have an impact on the full-year profit and loss.

Q3) Are costs related to the integration of containership business included in the results until Q3 or the forecast for Q4?

A3) We posted costs for consulting and surveys as costs related to the integration in this fiscal year. The new company has not been established yet, so no other costs occur.

Q4) In the FY2016 full-year forecast, the item of "Adjustment" is increased by ¥4.0 billion. I would like to make sure whether this is due to a temporary exchange gain.

A4) Yes, as you understand, the outlook for "Adjustment" is increased due to an exchange gain along with the depreciation of the yen.

[END]