October 30, 2020
Mitsui O.S.K. Lines, Ltd.

Financial Results Briefing for Q2 of FY2020 (Online Presentation)

Summary

In Q2 of FY2020, we achieved profitability, with an ordinary profit of JPY 32.7 billion and net income of JPY 30.2 billion. We posted year-on-year profit growth despite the unfavorable conditions caused by COVID-19. The financial results were higher than the forecast shown in the timely disclosure in late September due to reasons such as each division generally posting better-than-expected earnings and the dry docking of vessels, which had been scheduled for the first half being delayed due to COVID-19, causing dry docking expenses to be carried over to the second half.

We revised the FY2020 full-year forecast to to be determined in timely disclosure in late September but we now forecast ordinary profit of JPY 40.0 billion and net income of JPY 20.0 billion.

Outline of Q2 FY2020 Financial Results

[Overall]

<Please look at the explanations on pages 3 and 5 of the financial results briefing material slides. >

Revenue decreased by just under JPY 90.0 billion year on year. This was chiefly due to a sharp drop in the first half in the number of units transported by car carriers, and a downturn in the dry bulk market.

Ordinary profit increased by JPY 4.5 billion year on year. This was thanks to significant profit growth in the containerships business in addition to increased profit in the Energy Transport Business resulting from buoyant market conditions for very large crude oil carriers, favorable market conditions for other tankers and accumulated gains from long-term LNG carrier contracts, all of which offset large losses in the car carrier business due to COVID-19.

[By Segment]

<Please look at the explanation on page four and from the middle of page five of the slides. >

Dry Bulk Business

In early spring, the Capesize bulker market was weak because of sluggish shipments of Brazilian iron ore, attributable to the prolonged impact of the rainy season, and reduced shipments of iron ore bound for Japan and Europe. Whilst there were times between late June and mid-July when the market level exceeded the USD 25,000 ~USD 30,000 range due to strong crude steel demand in China, from late July onwards, the market remained in an adjustment phase, hovering around USD 20,000. If we look at the market environment in the three months from May to July, which affect our Q2 financial results, the average daily charter rate was USD 15,200, which is down just over USD 3,000 year on year. As a result, the Dry Bulk Business posted lower ordinary profit from a year earlier due to short-term contracts being affected by the decline in market and cargo movements, despite maintaining a stable profit base through medium-and long-term contracts.

In the small- and medium-sized bulkers market, rates were weaker than a year earlier, with shipments of raw and other materials for general industries languishing in the first quarter due to COVID-19, although trending upward from the summer onwards, supported by demand for grain shipments mainly bound for China. In terms of the financial results, profit decreased by only a small margin year on year because we significantly reduced our market exposure and the impact of market fluctuation on profit and loss is very limited.

Looking at specialized bulkers, the profitability of wood chip carriers under short-term contracts deteriorated due to decreased shipments attributable to sluggish demand for paper bound for Japan and the difficulty of using such carriers for other cargo. Open hatch bulkers operated by Gearbulk Holding AG, an equity-method affiliate, saw deterioration in profit, reflecting depressed dry bulk market conditions in their return voyages despite comparatively firm shipments of paper pulp bound for China.

As a result, the Dry Bulk Business overall posted year-on-year profit decline of JPY 5.2 billion.

Energy Transport Business

■Tankers

The very large crude oil carrier (VLCC) market surged in early spring as low crude oil prices spurred an upswing in demand for offshore storage, pushing daily charter rates above USD 100,000 from mid-March through to the end of April. Charter rates subsequently remained comparatively firm but then weakened through the summer, especially from August, when they dropped below USD 20,000. Although we have only a limited number of VLCCs operating under short term contracts, our success in securing several favorable contracts during this surging market contributed to profitability.

The product tanker market also saw improvement in profit, positively impacted by the strong VLCC market.

Profit for LPG tankers and chemical tankers similarly improved due to the strong market. Methanol tankers continued to earn stable profits through medium-and long-term contracts.

As a result of the foregoing, the tanker division posted significant year-on-year improvement in ordinary profit.

■LNG Carriers/Offshore Businesses

LNG carriers steadily accumulated stable profits mainly through eight LNG carriers delivered the previous fiscal year, with two LNG carriers delivered during the period under review also contributing. Profit in the offshore businesses decreased due to the allocation of one FSRU to a short-term contract between expiration of its initial medium-term prior contract in Turkey and entry into a long-term contract in Hong Kong next fiscal year.

As a result, the Energy Transport Business overall posted year-on-year profit growth of JPY 8.6 billion, bolstered by strong tanker market conditions in general, in addition to stable profits accumulated by LNG carriers and other factors.

Product Transport Business

■Containerships

Containership business integrated company, Ocean Network Express Pte. Ltd. (ONE), the Company's equity-method affiliate, reported substantial profit growth, achieving after-tax profit of USD 682 million for the first six months. Liftings decreased year on year but improved through Q2 following the sharp decline seen in Q1. As a result, the supply-demand situation improved rapidly, especially on Asia-North America routes, and freight levels also rose sharply. Furthermore, lower operating costs and falling fuel prices contributed to profitability.

If we look at page 3 of the materials prepared by ONE, the factors contributing to the increase in profit I have just explained are shown in the form of a waterfall chart. You can tell from this chart that ONE made up for more than half of the decrease in liftings caused by COVID-19 by reducing operating costs, including void sailings, and that, besides rising freight levels and falling fuel costs, reductions in variable expenses through ONE's own efforts, also contributed to profitability.

Returning to page 6 of our materials, profit from the terminal and logistics businesses, which belongs to the containerships subsegment, decreased by a small margin year on year due to a decline in cargo volumes in both businesses in Japan and overseas.

As a result, the containerships business overall posted year-on-year profit growth of JPY 17.9 billion.

■Car Carriers

In the car carrier business, transportation volume was far below the year-ago level from the start of the period under review due to COVID-19. However, as each automaker resumed operations, transportation volume on a shipment basis bottomed out in April and May and began to recover, regaining the previous year's level in September. During this time, we made efforts to cut costs, for example, by reducing the fleet by 12 vessels through redelivery and sale as well as temporarily idling ships. As a result, the car carrier business posted a large loss, but the size of the loss reported in Q2 was much smaller than that reported in Q1.

■Ferries and Coastal RoRo Ships

The ferries and coastal RoRo ships business performed more firmly than initially anticipated despite the impact of COVID-19 on shipments of automotive related products and other cargoes. However, the impact on ferry passengers was considerable, with an inevitable large decline in passenger traffic and, consequently, the ferries and coastal RoRo ships business profitability deteriorated year on year and posted a loss.
As a result, the Product Transport Business overall posted year-on-year profit growth of JPY 2.6 billion, with higher profit in the Containerships business outweighing the losses of the car carriers and ferries and coastal RoRo ships businesses.

Associated Businesses and Others

Profit decreased by JPY 1.4 billion, reflecting postponement of the resumption of cruises until at least October in the cruise ship business and large declines in business travel in the travel agency business, despite continued steady profits in the real estate business.

This concludes the summary of the financial results for Q2.

Outline of the FY2020 full-year earnings forecasts

<Please turn to our forecasts starting from page 7 in the slides.>

[Overall]

As mentioned at the start, our full-year earnings forecasts are ordinary profit of JPY 40.0 billion and net income of JPY 20.0 billion. In the second half, we forecast ordinary profit of JPY 7.3 billion, with profits expected to fall sharply from the first half.

This is mainly because we expect that forecast improvement in profitability in the car carrier business will be offset by decreased cargo movements and weaker market conditions in the containerships business and the absence of the usual second half rebound in the tanker market given the market surge experienced in the first half. In addition, expenses expected to be recorded in the first half will be recorded in the second half or later after COVID-19 caused the dry docking of vessels to be postponed to the second half or later.

[By Segment]

Dry Bulk Business

The Capesize bulker market remains in an adjustment phase but shipments are expected to increase going forward, mainly in Brazil ahead of the rainy season. On this basis, we expect the market will remain firm and therefore raised the market assumption for Q3 to USD 20,000. However, from early in the new year, the market is anticipated to weaken, with a decrease in exports due to seasonal factors in loading ports.

In the small- and medium-sized bulker market, shipments of raw and other materials such as cement and salt for general industries are likely to be affected; however, thanks to our longstanding efforts to reduce market exposure, the impact of the market fluctuations on our business results will be limited.

Regarding specialized bulkers, as explained earlier, the profitability of open hatch bulkers and wood chip carriers is expected to worsen on a full-year basis with cargo movements declining and market conditions remaining sluggish, since it is difficult to flexibly adjust the fleet size depending on changing cargo movements given their lack of versatility.

As a result, we have raised our ordinary profit forecast for the Dry Bulk Business overall by JPY 2.0 billion, from an ordinary loss of JPY 3.0 billion announced at the end of July to an ordinary loss of JPY 1.0 billion, mainly to reflect improvement in market assumptions for the Capesize bulkers in Q2 and Q3.

Energy Transport Business

■Tankers

The very large crude oil carrier (VLCC) market began to weaken through the summer, leading us to lower our market assumptions for Q3 and, given that there may not be a major rebound even despite the winter demand period, we left our market assumption for Q4 unchanged at USD 20,000. However, this fiscal year, the boost to profits from short-term contracts secured in early spring during the market surge will partially remain in the second half and contribute to profitability, along with stable profits from medium-to-long-term contracts, which most of our VLCC fleet operate under.

The product tanker market benefited from favorable market conditions in early spring but, like the VLCC market, is likely to experience decline in actual demand and falling market rates on a full-year basis. However, we do expect there to be some rise in the winter given the seasonal nature of demand for heating oil, etc. compared to crude oil.

Chemical tankers are expected to achieve improved profits compared to the previous year. This is one of the areas we have focused investment on, and we are starting to see the results of this.

Methanol tankers are expected to continue generating stable profits through long-term contracts.

■LNG Carriers/Offshore Businesses

The LNG carrier division is projected to continue generating stable profit, with all carriers operating under long-term charter contracts, including five carriers that are to be delivered this fiscal year contributing to profit accumulation. The offshore businesses are likely to report a year-on-year decline in profit as a result of one FSRU engaging in a short-term contract and with FPSO having no prospect of any bonus for high utilization rates as in the last fiscal year. Whilst both the LNG carrier and offshore businesses generate stable profits through medium-and-long-term contracts, the second half will be less profitable than the first half due to advancement of the recognition of some revenue and postponement of recording of some expenses.

As a result, we have raised our full-year forecast for the Energy Transport Business overall by JPY 1.0 billion from the figure announced at the end of July, and forecast ordinary profit of JPY 25.0 billion.

Product Transport Business

■Containerships

In the containerships business, we forecast ordinary profit of JPY 30.0 billion on a full-year basis. This is attributable to the strong performance of ONE and we expect profit in the second half. While cargo movements and freight levels currently remain strong, we anticipate second half profit to be below the first-half level, despite increasing year on year, because of economic uncertainty in Europe and the United States, including the resurgence of COVID-19, in addition to factors such as slack demand during the lunar new year in China. Please refer to the information from page 5 in ONE's materials for further details.

On top of our equity in the earnings of ONE, the terminal and logistics businesses are also expected to achieve improvement in profitability, with handling volumes exceeding initial expectations.

■Car Carriers

In the car carrier business, shipments are now back on a par with year-ago levels and, as of the end of September, there were no idling vessels, which were noticeable in the first half especially Q1. Shipments are expected to maintain an upward trend going forward, with some routes faring better than others, and, factoring in the effect of cost reductions achieved through fleet reduction in the first half, we expect substantial improvement in performance in the second half.

■Ferries and Coastal RoRo Ships

In the business of ferries and coastal RoRo ships, cargo transport is on the recovery path and there are signs of an improvement in ferry passenger demand thanks to the government's Go To Travel campaign. However, we anticipate a slight loss in the second half mainly due to seasonal factors.

As a result, in the Product Transport Business overall, we forecast ordinary profit of JPY 13.0 billion, an improvement of JPY 39.0 billion from the forecast announced at the end of July.

Associated Businesses, Others and Adjustment

We expect to continue recording steady profits in the real estate business. On the other hand, in the cruise ship business, we have started trial cruises from October and will resume commercial cruises from the start of November next week. Nonetheless, profitability is expected to deteriorate year on year due to the implementation of measures against COVID-19 including halving the number of passengers.

This brings me to the end of my presentation of forecasts for each business segment and I would now like to give a supplementary explanation concerning our overall net income forecast. The reason we set our net income forecast at JPY 20.0 billion when our ordinary profit forecast is JPY 40.0 billion is because our net income forecast factors in measures to be implemented in the second half, intended to contribute to performance in the coming fiscal years for a return to a growth trajectory as stated in our Rolling Plan 2020, including the disposal of unprofitable vessels, but which are still to be determined.

Dividend

We will pay ¥15 per share as an interim dividend and plan to pay ¥20 per share at year-end, making the annual total dividend ¥35 per share. In the timely disclosure on September 24, we announced that we planned to pay ¥10 per share as an interim dividend, with the year-end dividend to be determined.

Comparison of Mega Trend Forecasts in Rolling Plan 2020 with Recent Forecasts by a Survey Agent

<Next, please look at page 11 of the slides.>

This shows cargo movement trends of main cargoes indicated at the time of announcement of this fiscal year's management plan "Rolling Plan 2020" at the end of June (forecasts for 2020 in MOL's mega trend forecasts) and recent annual cargo movement forecasts by a survey agent as available to us at the moment. You can see from this that cargo movements of resources and energy such as iron ore, crude oil, and LNG and product transport shipments such as container shipments have been exceeding MOL's mega trend forecasts as the reasons why our first-half results beat our initial expectations.

WAKASHIO Accident

<Please look at page 12 of the slides.>

This page is the overview on the oil spill accident which occurred on August 6 after the Capesize bulker WAKASHIO, which we were using as charterer, ran aground off the coast of Mauritius on July 25.

We would once again like to offer our sincere apologies to our shareholders and investors for the inconvenience and concern this accident has caused.

Our basic stance on this matter is that, as a charterer who was using the vessel, we are deeply aware of the great impact that the accident had on the lives of local people and the precious natural environment, and will fulfill our social responsibilities by restoring the natural environment and contributing to the local community.

Regarding the impact on our results in the current fiscal year, we will incur expenses as a result of sending personnel to Mauritius and providing equipment and materials, and we expect that these costs will amount to around 100 to 200 million yen in total.

Our initiatives to date include sending employees to Mauritius and providing equipment and materials such as oil adsorbents and protective clothing and donating a reefer container.

Moving forward, we will focus on restoring the natural environment in Mauritius and contributing to local communities through support for the Mauritius natural environment recovery projects and the establishment of a project fund, in line with our contribution measures announced on September 11.

Questions and Answers

Q1)
What is your view on the businesses whose performance deteriorated, namely the open hatch bulker, wood chip carrier and cruise ship businesses?

A1)
Gearbulk, which operates the open hatch bulkers, has implemented structural reforms through measures such as hire reduction and waiver. Given that the open hatch bulker market has not deteriorated as much as anticipated and is comparatively firm, assuming the structural reforms progress smoothly, we are hopeful that business results will recover.

As for wood chip carriers, Japanese paper manufacturers are facing an uphill struggle due to decreased demand for paper.
Whilst COVID-19 is likely causing a major impact, remote work and paperless business style may become common in the future and we expect that the demand environment will remain challenging. We have one of the world's largest woodchip carrier fleets and whilst many vessels operate under long-term contracts, we may have reached the stage where we have to take some kind of action including disposal with respect to those that do not operate under long term contracts and we are currently examining this internally.

Regarding cruise ships, we have somehow successfully managed to resume cruises despite COVID-19 pandemic. With the support of our customers, we hope to get this business back up to speed. Fortunately, I hear that bookings (for cruises due to resume in November) are fairly strong.
Unfortunately, the number of passengers we accept is about half of the cruise ship capacity, which rules out a dramatic improvement in profitability, but we plan to properly assess the reaction of passengers and take things from there.

Q2)
When was the forecast for the containerships business prepared? To what extent does the forecast reflect market conditions between China's National Day holiday and today?

A2)
ONE's forecast for the second half was approved by the Board of Directors last week and was estimated based on the latest information available at that time. I guess you are implying that in average years, during China's National Day holiday, plants stop

operating and at the same time cargoes for Thanksgiving in the United States are past their peak, such that cargo movements decline. This year, whilst cargo movements declined for around a week after China's National Day, between then and now, vessels on Asia-North America and Asia-Europe routes have been almost fully loaded. Freight rates have also reached their highest level of recent years for Asia-North America route in mid-September and have yet to fall despite concern they would.

Q3)

It's my understanding that the improvement in the forecast for the Product Transport Business excluding the containerships business is JPY 9.0 billion compared to the previous forecast. Does the car carrier business account for most of this?

A3)

Yes, you are correct. This improvement is largely attributable to the car carrier business. However, the improvement is not solely down to the car carrier business. The ferries and coast RoRo ship business has also improved. Back in July, our forecast was cautious because the outlook for passengers was extremely uncertain and there was concern whether cargo demand would continue. Please consider that around 60-70% of the improvement is by the car carrier business.

Q4)

According to your forecast, the Energy Transport Business will be less profitable in the second half than the first. How much of this is down to the postponement of the drydocking of vessels?

A4)

The vessels which will be dry docked are tankers and LNG carriers and drydocking expenses for them will amount to billions of yen.

Q5)

ONE's revenues amounted to USD 5.91 billion in the first half and second half revenues are expected to be higher at USD 5.99 billion but after-tax profit was USD 680 million in the first half and is expected to be lower at USD 240 million in the second half. Why is this?

A5)

Earlier today I mentioned that October results were strong. Whilst strong results are expected to be maintained for a while after entering November, the outlook after that is full of uncertainty. Our outlook for the consumption of goods, which has held firm, is comparatively conservative from the end of the year through to March, given the possibility that additional financial support will be limited as a result of the increasing levels of public debt in the U.S. and Europe, the U.S. presidential election possibly affecting U.S.-China trade conflict, and other factors, and we expect that freight rates will fall from the latter part of the second half. We also anticipate higher SG&A expenses, etc.

Q6)
In your explanation concerning net income, you said that extraordinary losses related to the disposal of unprofitable vessels may arise in the second half. Which types of vessels are you referring to?

A6)
We have only just started examining this matter internally and I am unable to say which types of vessels at the present time. We have to fully consider which vessel will lead most reliably to an improvement in business results moving forward and at this time it is undetermined.

Q7)
Please explain why you decided to set the dividend for this fiscal year at 35 yen. Was this decision based on an awareness of a dividend payout ratio of 20%? Will there be any increase in the dividend, if forecasts are revised?

A7)
We announced our dividend forecast, acutely aware of the dividend payout ratio. I cannot speak hypothetically about what would happen if our results fluctuate. However, we remain firmly committed to our existing dividend policy. We would prefer to make a decision once we have seen the level of profit we are ultimately able to generate in the second half.

Q8)
Why do you think that cargo movements bound for North America were still strong in October in the containerships business? I imagine this was partly a rebound from the slump in the April-June quarter but what is your view?

A8)
We forecasted cargo movements in the containerships business in the Rolling Plan

announced in June, but we honestly did not anticipate this kind of trend. In April and May, cargo movements on Asia-North America routes momentarily fell by around 20% but they gradually picked up from June and fully came back to life in the summer (August-September), registering positive year-on-year growth.
Data analyzed to date shows that in the U.S., while consumption in the entertainment, food service and travel-related industries, especially airlines, plummeted, consumption patterns have changed considerably, shifting from services to goods. In September and October, sales of daily necessities, food products and retail sales were still up more than 10% year on year and our analysis is that this is reflected in the high levels of shipments on Asia-North America routes.

[END]