July 31, 2018

Mitsui O.S.K. Lines, Ltd.

Explanation by the CFO and Major Q&A

[Overall]

The total of ordinary profits for FY2018 Q1 was almost the same as our internal initial outlook, since downturns in the Car Carrier and Tanker businesses and losses by non-consolidated foreign exchange were offset by upturns in the Dry Bulk and Containership businesses. As we estimated in the initial outlook, the Company barely secured profitability for Q1, when more than half of the transitional expenses related to integration of the containership business were recorded.

The factors that affected the Q1 result also applied to the revision of the full-year forecast: ¥40.0 billion in ordinary profit was unchanged from the previous outlook, as a result of a slight upturn of the Dry Bulk and Containership businesses offset by the impact of a downturn of the Tanker Business and foreign exchange losses.

1. Outline of Q1 FY2018 Financial Results

[Overall]

Ordinary profit totaled ¥0.2 billion, a decrease in a year-on-year comparison, due in part to the impact of higher bunker prices and foreign exchange losses, but we secured profitability. It has improved from Q4 of the previous year. And this was assumed in our initial internal outlook. Revenue decreased by about ¥100 billion as a result of transferring our containership business to the equity-method company ONE.

[By Segment]

<Dry Bulk Business>

The Capesize spot market is currently around $25,000, but for a time in April declined to the $7,000 level. Ordinary profit for this division is recorded based upon the completion of voyages, so the current market is not reflected in this fiscal year. But it could be higher than the initial outlook.

Shipments in the Panamax and mid- and smaller-size market slowed down in April due to factors such as restrictions on coal imports to China, but afterward recovered on the same path as the upturn in the Capesize market. But fluctuations in the spot market for mid- and small-size bulkers have limited impact on our profits because we have significantly reduced our market exposure, as you know.

As a result, the Dry Bulk Business ended with a slight upturn from the initial outlook.

<Energy Transport Business>

- **Tankers**

The markets for all tanker types were slow.

Our market exposure for crude oil tankers was not significant, but the spot market temporarily fell below $10,000 in Q1. The negative factors, such as seasonal repairs at oil refineries during Q1 and consequent slow demand, were already factored into our previous forecast, but the market was even lower than that assumption.

The product tanker market was also stagnant as arbitrage trading stalled due to uncertainties over crude oil prices. Q1 was also a non-peak demand season when oil refineries in the Far East undergo periodic repairs. Profits from mid- and long-term contracts for crude oil tankers as well as methanol and shuttle tankers offset losses to a certain level, but overall, the Tanker Division showed a downturn compared to the initial internal outlook and in a year-on-year comparison.

- **LNG Carriers/Offshore Businesses**

This segment recorded stable profits from long-term contracts, ending at almost the same level as the outlook.

<Product Transport Business>

- **Containerships**

ONE finally commenced services from FY2018 Q1. As many of you already know from news reports, we faced a temporary difficulty when ONE's service was launched in processing customers' bookings. This was not a system-related problem, as some media reports suggested, but a problem caused by inexperience among staff responsible for information input and a shortage of personnel. These issues have already been addressed, and ONE has now recovered to nearly normal operation.

However, this disruption led some customers to avoid booking with ONE. We had anticipated a slowdown in utilization for Q1 at a certain level in the initial outlook, but the actual utilization was even lower, resulting in reduced gross margins. And while bunker prices rose during Q1, the impact was not significant thanks to reserve fuel purchased before higher prices took effect.

On the other hand, some positive factors in ONE offset these deteriorating factors to a great degree. In terms of the synergistic effects of the integration, we saw a greater-than-anticipated reduction in variable expenses such as inland transport costs and terminal costs. In addition, though this is purely an accounting factor, we saw an improvement from cost reductions as the time charter contract, which we initially assumed as "required as finance lease accounting," was approved as an operating lease accounting for this fiscal year. ONE's ordinary profit for Q1 ended with a deficit of $120 million, slightly lower than the initial outlook, so we included an ordinary loss of about ¥0.4 billion, reflecting our 31% share of equity in ONE.

Now let's look at Containership results besides ONE. As we disclosed at the end of April, for this fiscal year, we projected ¥11.5 billion in transitional costs related to the withdrawal of our own containership services. The costs remained lower than the outlook for Q1 results. In addition, profits improved from the initial outlook because of prior period adjustments for MOL's own containership services through March of the previous fiscal year.

So as I explained, overall ordinary profit in the Containership Business ended with an upturn from the initial internal outlook, because our operations other than ONE showed an improvement that offset the slight deterioration of equity in losses from our investment in ONE.

■ **Car Carriers**

Trade from Asia to Europe and the U.S. remains firm, while trade to the Middle East hit bottom. On the other hand, in March, several vessels could not enter ports on the route serving New Zealand due to a large infestation of insects in cargoes. That required us to charter additional vessels, resulting in an inefficient allocation of ships. Since those vessels' sailings were complete in Q1, this contributed to a downturn in profit.

2. Outline of the Full-year FY2018 Forecasts

[Overall]

We did not change our ordinary profit forecast for the full year from the ¥40.0 billion previously announced. We expect that ONE will secure profits at the same level as its initial outlook, rebounding from the negative impact of rising bunker prices, thanks to its independent efforts to improve profitability by stepping up the synergistic effects of the integration. Although our other business segments will show positive or negative results, the total profit including ONE will be at the same level as the initial outlook.

Meanwhile, our assumption of foreign exchange is unchanged from the previous ¥105/US$. And we have revised our assumption of bunker prices from Q2 to $450 in consideration of the current situation.

[By Segment]

<Dry Bulk Business>

Currently, the Capesize market is around $25,000, but we see an overheating of the market to some extent considering the season. Therefore, we anticipate that it will enter a temporary adjustment period in the future, albeit remaining firm overall. Because we anticipate the same movement in markets for mid- and small-size vessels, the market assumption was unchanged from the previous outlook.

For the full-year forecast, we also made a slight upward revision in the previously announced forecast by including the upturn for Q1.

<Energy Transport Business>

- **Tankers**

Speaking of crude oil tankers, we made a downward revision in our previous market outlook in consideration of the current low level. On the other hand, the number of VLCCs scrapped exceeded the number delivered, showing a trend toward a decrease in the net number of vessels. Under these circumstances, we may see a phase of sharply rising rates if the fleet demand and supply balance is highlighted when the crude oil market rises due to winter seasonal factors.

The product tanker market is also stagnant, but looking to the future, there is a viewpoint that product tankers represent a promising field in the tanker industry. We see some of the major players expanding pool operations.

Overall in this business division, since our VLCC market exposure is small and market changes have little impact, I think we can secure some profits, underpinned by stable profits from long-term contracts for methanol carriers and shuttle tankers.

- **LNG Carriers/Offshore Businesses**

This segment continues to record stable profits from long-term contracts, and will secure profits almost in line with the previous outlook.

<Product Transport Business>

- **Containerships**

I will explain based on the graph shown on page 11 of the handout titled "Business Performance". There are mainly two groups of factors, that is, fluctuations within ONE, and others within MOL, not ONE.

First, let me explain about fluctuations within ONE. Gross margins decreased significantly in Q1, due mainly to low utilization. But currently, utilization already shows a trend toward improvement, and we assume that utilization during the second half will be able to recover to the level of the initial plan. About a half of the decrease in gross margins in this graph appeared in Q1, so the reduction will be scaled down from Q2.

The delay in the transfer of overseas terminals, initially expected to start in Q2 but now slated for Q4, led to a decrease in profits for ONE. Another factor is the cost increase due to rising bunker prices. But there are three positive factors at ONE to counter these negative factors.

The first is the synergistic impact of the integration, which is progressing faster than the initial outlook. Next is reduction of product costs, and we expect to see improvements by optimizing some routes, including temporary stoppages, and enhancing the bunker oil cost reduction plan. Finally, we anticipate improvement due to a "change of lease accounting" as I touched upon in my explanation for Q1.

As a result of the above-mentioned factors, we plan to maintain ONE's full-year business performance at the same level as our initial outlook.

On the other hand, for the Containership Business segment other than ONE, we made a downward (positive) revision in our projection for transitional costs from ¥11.5 billion in our initial projections to around ¥9.5 billion for the full year, in consideration of the reduced portion in Q1. Also, considering improvements in Q1 from the prior period adjustments, we made an upward revision of the overall segment from ¥0.5 billion for the previous outlook to ¥4.0 billion.

■ **Car Carriers**

We see positive factors in the future such as solutions to temporary problems in Q1 and the Bunker Adjustment Factor (BAF) take effect from Q2 onward.

We have almost completed the scale-down of the division's fleet, and a major issue will be how we will improve operational efficiency with a reduced fleet.

<Dividend>

The dividend for this fiscal year is unchanged from the previous announcement. We plan to pay ¥50 per share for the full year, including the interim ¥20 per share, based on the policy of setting a dividend payout ratio of 20%.

3. Questions and Answers

[Containership Business]

Q1) You made a revision of transitional costs in the Containership Business from ¥11.5 billion in the initial outlook to ¥9.5 billion. Was this difference of ¥2.0 billion generated in Q1?

A1) Yes, that's right.

Q2) MOL's transitional costs in the containership business decreased compared to the outlook. What factors are behind that?

A2) The transitional costs refer mainly to operational costs and labor costs of overseas subsidiaries. Since the number of personnel has been reduced more swiftly than the outlook, the reduction in such costs was greater than in the initial outlook.

[Other]

Q1) What impact do you expect from external factors such as U.S.-China trade friction?

A1) We don't see the impact of the trade friction on current trade, but it is hard to determine whether it is leading customers to order goods ahead of time to avoid tariffs and so on, as some media have reported. If trade friction becomes really serious, this will have a significant impact on the entire shipping industry, but at the present point, we think it is difficult to include this in our forecasts.

Q2) You said the industry has some expectations for product tankers, but the market is currently stagnant. Did you make your forecasts with an outlook for improvement in the second half and later?

A2) We don't anticipate a rapid recovery in the product tanker market, and made a downward revision of the outlook for the second half. We have moved ahead to reduce the number of tankers under our policy to scale down the product tanker fleet to make us less susceptible to slumps in the market.

[END]