May 2015

Mitsui O.S.K. Lines, Ltd.

1. Supplemental Explanation for FY2014 Financial Results

■ Overall View

We would like to explain the reasons behind our performance in the fourth quarter (three months; Q4) in comparison with the third quarter (three months; Q3), and the upturn from the previous forecasts (January 2015).

In Q4, the yen depreciated (¥110.76 → ¥118.44), and bunker prices declined ($528/MT→ $393/MT) compared to Q3. Q4 saw the partial impact of those factors, with ordinary income of ¥21.5 billion, a ¥6.3 billion increase from ¥15.2 billion in Q3.

■ By segment: Bulkships

Ordinary income for Q4 was ¥22.4 billion, a ¥7.3 billion increase from Q3, and ¥6.6 billion above the previous forecast. While the impact of the slowdown in the dry bulker market was limited, ordinary income improved more than the previous forecast due to positive factors such as the sharp rise in the tanker market and the yen's depreciation. We secured the highest profit level of fiscal year 2014 during Q4.

<Dry Bulkers>

The slowdown in this market became pronounced at beginning of 2015, but the impact for FY2014 was limited because most spot vessels are operated by subsidiaries in Singapore, and their fiscal year ends in December. On the other hand, the segment enjoyed stable profits from mid- and long-term contracts and the tailwind of a weaker yen, allowing us to achieve the profit level in the forecast.

<Tankers/LNG Carriers>

We anticipated a large improvement in Q4 from Q3 even in the previous forecast due to a stronger market during second half of the fiscal year, but the segment's results improved even further as the market moved higher than forecast. The LNG carrier segment recovered swiftly as transient factors behind the earlier decrease in ordinary income, such as drydocking, were removed.

<Car Carriers>

The segment improved from Q3 and settled down in a slight upward trend compared to the forecast, thanks to the benefits of the depreciating yen, in addition to measures to improve operational efficiency.

■ **By segment: Containerships**

We anticipated considerable improvement in Q4 due partly to the impact of declining bunker prices even in the previous forecast. But ordinary income improved more than anticipated thanks to a smaller than forecast impact of port congestion on the North America West Coast, which was conservatively factored in. The deficit decreased from -¥10 billion for Q3 to -¥3.1 billion for Q4.

■ **Dividend**

In conjunction with ¥42.3 billion in net income for FY2014, we decided to pay a full-year dividend of ¥7 per share for FY2014, an increase of ¥1 per share for the year-end dividend over the previous forecast, by using 20% as the company's guideline for the dividend payout ratio.

■ **Progress of Midterm Management Plan STEER FOR 2020, and Cash Flow**

Turning to strategic investment tilts in growth fields, we have successfully acquired new LNG carrier projects and others almost according to our initial plan. Regarding "Cash Flows" on page 16 of the reference material, cash flows from investment activities for FY2014 were higher than those from operating activities. The yen's depreciation also became a factor in the increase of interest-bearing debts, but we took measures to alleviate this increase, such as allocating liquidity on hand to redeem debts.

2. FY2015 Full-year Forecast

We forecast ¥60 billion in consolidated ordinary income and ¥43 billion in net income for FY2015. The foreign exchange rate is assumed as ¥118-US$1 and bunker price $380/MT. That means ordinary income will increase by 17% from the previous year, with net income by a slight 2%. We recognize that these targets are on the conservative side, although there are various uncertain factors.

Ordinary income in the bulkships segment will deteriorate by ¥16.1 billion from the previous year. On the other hand, the containerships segment will improve by ¥29.1 billion. The containerships segment remains the biggest uncertainty we face in FY2015, but many of the previous year's negative factors in comparison with our competitors will be resolved, so we think the segment will recover to an ordinary level. However, we are not overly optimistic about this segment.

■ By segment: Containerships

Compared to FY2014, we forecast an improvement in the Containership segment of ¥29 billion, broken down as follows:

	(¥ billion)	
Foreign exchange (yen depreciation)	1.5	
Improvement of loss in bunker price hedging	8.5	(*1)
Decline in bunker prices	37	
Decline in net proceeds (gross profit)	-28	
System cost reduction	9	(*2)
Terminal profits improvement (TraPac automated termial)	4	
Logistics, subsidiaries/agencies, nonoperating	-4	
Other	1	
Total	29	

(*1) Improvement margin of about ¥10 billion hedge loss in FY2014

(*2) Rationalization of North-South routes, reduction of charter rates, the impact of returning mid-size vessels, etc.

Upward factors, which are not included above, include improvements due to the renewal of North America service contracts. We also conservatively forecast our capacity utilization rate and logistics earnings, but if we can maintain those factors at the same level as in FY2014, the segment will show further improvement.

■ By segment: Bulkships

<Dry Bulkers>

Subsidiaries in Singapore operate most of their vessels on spot contracts, and the results of these subsidiaries are posted in our consolidated results three months later (because their fiscal year ends in December). On the market assumption on page 10 of the reference material, Q1 is already determined as the market slumped from January to March, and the April-December period will be included in the forecast. The average of the Capesize market is assumed at a significantly lower level than in the previous year, and the market for Panamax and smaller size vessels down by more than $1,000~2,000/day. Looking at the gap of US$1,000/day from the assumption, the market sensitivity will be ¥4.16 billion including the impact of our interest in Daiichi Chuo Kisen Kaisha. But in so far as the Capesize free fleet, where the market fluctuation margin is large, the sensitivity is ¥940 million.

Pessimism dominates the dry bulker market, and this is not something to be welcomed. Values of futures are poor. So our assumption is based on those factors. On the other hand, vessel demolition has been pushed ahead, and there is a chance that market prices will move up in the second half of the year when shipments usually shift into high gear, and we have a good chance of exceeding our assumption.

<Tankers>
We project that the World Scale (WS) for very large crude carriers (VLCCs) will be 47 in the first half and WS52 in the second half, for a full-year average of WS50. The year average in Charter Base (CB) is $36,300/day. The average of the previous year was $34,300/day, which means the CB will be higher despite the same WS, because of lower bunker prices. Increased ton-miles from West Africa to China indicate stronger trade, and this contributes to a tightening of the fleet demand and supply balance. So far, WS is remaining at 50~60 and maintaining a strong market, even after March when it usually loses ground due to seasonal factors. We also anticipate that other types of tankers will be at the same level as the current market or slightly lower, and do not expect a collapse. We anticipate that ordinary income for this segment will decrease slightly from the previous year, but we also see opportunities for upward movement.

<LNG Carriers/Offshore Business>
The LNG carriers/offshore businesses segment showed deficits for the first half of the previous year due to unexpected repairs, although it was profitable for the full year. But this year, we anticipate that this segment will increase swiftly and smoothly, and contribute to stable profits throughout the year.

<Car Carriers>
We project that the total exports of all automakers from Japan will remain almost at the same level as the previous term, at around 4 million units. We will focus on new business in the Intra-Asia, Intra-Atlantic Ocean, and Europe-China trades, and anticipate that cross trades and backhaul trades will increase by about 7% from the previous year. We had a very difficult time with the launch of our service from Mexico, but it is getting smoothly under way now, and we will work to expand this trade.

Thus, in our ordinary income forecasts for the bulkships segment, an increase in the LNG carrier and offshore businesses will offset a slight decrease for tankers and car carriers, and a decline in dry bulkers from the previous year will result in an overall decline for bulkships.

The dry bulker market (subsidiaries in Singapore) from January to March was very weak, and so is the current freight rate level in the Asia-Europe containerships. We forecast that Q1 results will be very severe. But we are considering those factors in our full-year forecast. The key question is how much those factors will improve in and after summer.

■ **Dividends, Cash Flows**

Speaking of dividends, based on the forecasts we explained above, we are planning an interim payment of ¥3.5 and ¥3.5 at year end, for a total of ¥7 for the full year. The dividend payout ratio is 20% for the full year on our projected profits.

Turning to cash flows for this term, a large part of the amount we paid during the construction period will be returned by structuring project finance, leasing, and so on. Consequently, net cash flows from investment activities will be reduced to a lower level than cash flows from operating activities. We will continue our investment program with more than ¥100 billion for LNG carriers and offshore businesses in and after FY2016, in order to increasingly accumulate stable long-term profits. But we will decrease our balance of interest-bearing debts for this fiscal year, in part by reducing debts with cash on hand, putting us on course for a lower debt burden. We will continue investments aimed at ensuring the future stable management of our business.

2. Questions and Answers

[Containerships]

Q1) About containership freight rates: could you tell us what the forecast for rates on the North America, Europe, and South America East Coast routes will be during FY2015? And what about current rates?

A1) We look for freight rates to edge slightly higher on the North America route, compared to those in FY2014. On the European route, we anticipate lower rates that reflect the current falling spot rates. On the South America route, we expect rates to fall because of the lack of strength in the Brazilian economy.

Based on these forecasts, we anticipate the rate index for all routes averaged to be 76.5, which is slightly below current rates. It will negatively affect profits from cargo trade by some ¥20 billion in comparison with FY2014, and is duly reflected in the current forecast (full year ordinary profit of ¥5 billion).

Q2) Your forecast of ordinary income in the containership segment for FY2015 shows an increase of ¥29 billion, but can you tell us how much is from temporary causes and how much is from structural factors?

A2) Before (as of the January 2015 forecast), we listed factors for improvement as unique efforts within the company, i.e., a ¥9.5 billion loss reduction in bunker price hedging,

¥9 billion in reduced system costs, and ¥4 billion in terminal business profits for a total of ¥22.5 billion. All that has changed from those improvements is the margin loss reduction in bunker price hedging. We assumed bunker prices in fiscal 2015 to be somewhat higher than the previous assumption, meaning that our loss reduction in bunker price hedging would be ¥8.5 billion (a total of ¥21.5 billion). Other than that, there is no change from the previous outlook in January.

The remaining ¥7.5 billion is caused from external environmental changes excepting what can be improved from within our company. As explained earlier, those are mostly the net result of improvements realized because of decline in bunker prices and deterioration in net proceeds.

Deterioration in net proceeds was the result of worsened market trends in the current Europe route and dropping freight rates on the South America East Coast route. We can expect some additional improvement in renewals of yearly contracts on the North American route, but in our forecast we took a conservative approach, and expect only a marginal impact.

As far as the terminal business is concerned, the automated terminal operated by TraPac is already in full operation, and in terms of productivity, it already surpasses competitive terminals, and will undoubtedly contribute significantly to the profits.

[Bulkships]

Q1) About the market exposure noted on page 14 of the reference material you handed out, the dry bulker fleet (exposed to the market) is expected to be 144 vessels by the end of March 2016, down significantly from 177 vessels at the end of March 2015. Please tell us how you plan to reduce the number of vessels and how that will impact profits.

A1) Reductions in market exposure will mostly be reductions of Handymax and Small Handy vessels. Most are chartered vessels, and the vessels will be returned to their owners when the current charters expire. If there is flexibility built into the charters, we plan to return the vessels as quickly as possible under the charter terms. Doing this will result in no additional costs.

Q2) Tell us how many VLCCs and product tankers are operated on the spot market. Further, can you tell us what the market assumption will be like for product tankers in FY2015?

A2) Of our 33 VLCCs, seven are spot ships. In addition, two are on market-linked long-term contracts, which means that we can take advantage of favorable market conditions, too. At present, VLCC market rates exceed $60,000 per day, and although we face the summer slack season, we estimate rates at $36,300 per day for the full year average, a considerable upward movement over rates in FY2014.

About half of the 32 MR-type product tankers are time-chartered. This includes ships on charter contracts of less than a year that were signed when market conditions were on the upswing, which means profits are set. The remainder are spot vessels. But, where the market says they should be getting $14,000 a day, in reality, their rates are $17,000 per day. Our eleven LR1 product tankers are spot vessels (operated in the pool), and where the market is assumed at $18,500 per day for these vessels, they currently remain at $24,000-25,000 per day.

Q3) About the market of LPG tankers (VLGC), please tell us your forecasts for FY2015. Many new VLGCs are being launched, but what kind of impact do you think these new vessels will have?

A3) The market indices on page 11 are from Clarkson, and putting them into rate-based figures would show FY2014 at $93/MT. In the past, most LPG trade came from the Middle East, but from FY2014, a larger share comes from North American shale gas. As a result, in terms of supply-demand balance, 2014 was the best year yet.

We will see 35 new vessels launched within the second half of FY2015. When we consider that the worldwide LPG fleet scale about 170 vessels, there is some chance the market will drop in the second half of the year, so we forecast some $73/MT for the year.

[Overall, investment plans, others]

Q1) Compared to the previous forecast of ordinary income for FY2014 (¥41 billion on January 30, 2015), you made an upward revision of some ¥10 billion. Can you tell us why?

A1) The main factor is an upward trend of the tanker market in the Tanker Division. Another significant factor was reduction of deficit margin in the containerships segment, and, added to these, are upwards of the LNG Carriers and Car Carriers divisions.

The containership segment made an upward surge of some ¥3 billion from the previous forecast, mostly related to the conclusion of labor negotiations at ports on the North America West Coast. In January, we could not see an end to the negotiations, and thus took a very conservative view that assumed considerable adverse impact. Still, in the end, the adverse impact was not as much as we assumed. Higher than forecast profits in the logistics business also contributed to the improvement.
Thus, looking only at Q4, we see that except for the ¥7 billion loss incurred in bunker price hedges, the rest of the containership business is in the black, which we can say is the result of vigorous cost cutting measures that showed results in the fourth quarter.

Q2) You explained that business forecasts for FY2015 were somewhat conservative, but does that mean you consider conservative conditions within the market? Or does it mean you are buffering for conditions outside those of the market?

A2) Concerning market forecasts, first of all, we must estimate the probable market level, then we set a slightly lower level for forecasts. For operations, also, sometimes we do not include indications of an upturn, or when we can actually expect an upturn, we don't figure that in either. For example, in the containerships segment, we make very conservative estimates concerning subsidiaries' and logistics segment's profits. So you see we are conservative from both angles.

Q3) On cash flows from investment activities for FY2015, while the investment plan itself shows no change, why are you able to estimate less funds to be invested? You explained that it was because of increased off-balance-sheet investments, but what is the real reason?

A3) Our investments into LNG carriers and offshore businesses are steady and continuing. Where cash flows from investment activities are concerned, there is the portion paid during construction of a vessel and the portion paid when it is launched and turned over to the owner, and during FY2015, by coincidence, under-construction payments will slow down, which will result in less cash outflow. Further, for newly launched vessels, we will have cash incoming from project finance and other facility loans, so much of the cash outlay we put up while the vessels were being built will be paid back.

In addition, (along with LNG carriers and offshore businesses,) a number of the vessels scheduled for launch in FY2015 (mostly tankers) will be sold and then chartered back, in which case, the cash outflow that occurred during the vessels' construction will all be returned at the time of sale.

For these reasons, the cash flows from investment activities for FY2015 are forecast to be less than the cash flows from operation activities.

Nevertheless, investments in LNG carriers and offshore businesses will continue into FY2016 and beyond.

Concerning interest-bearing debts in FY2016, we will do everything possible not to increase such debts. We expect cash flows from investment activities to increase more in FY2016 than in FY2015, but we will also continue to move towards off-balance sheet structures for existing and newbuilding vessels, such as time-chartering, and will consider retrieving cash outlays for vessel construction, among other things.

[END]