3Q 2019 POSCO Earnings Release
Q&A Transcript

October 24, 2019

Chinese winter production cut

Production control in China in this winter will last for 6 months started from October 1st. Previously in 2017 and 2018, companies were obliged to cut production volume at a universal rate by 50% or 30%. Recently the guideline for production cut has been specified to three grades, A, B, and C, according to environment grade by applying the pollutant emission regulation; A & B - no need to cut, C - 50% cut. In general, the intensity of production control seems to be weakened compared to the previous year.

Global Steel Market Trend

China is accounted for 55% of global steel production and it is hard to mention without China. China's crude steel production is over 1 billion tons this year and its oversupply situation is affecting other markets. Also, trading in general is not active in other areas due to various trade conflicts including U.S.-China trade war. Demand industries, broadly, are bearish, especially in the countries, such as China, India, and Mexico, where we are focused for auto sheets, and therefore distribution prices are generally in a weak trend in 4Q.

Price Negotiations and ASP Outlook

The price of shipbuilding plate in 1H stayed the same and we were not able to pass through higher raw materials cost to our shipbuilding clients. For 2H, we continued to try increasing by KRW 70k-80k/ton considering raw materials cost hike. However, shipbuilders appealed difficulties in taking new orders and we are talking to finalize the deal with a moderate increase as a result. Our long-term contract based customers are automakers, shipbuilders and home appliance makers. We are trying to stay or increase prices in 2H as we maintained the same price in 1H. However, we are at a downward pressure on prices negotiated monthly for re-rollers, pipe makers, distributors due to inflows of Chinese low priced goods, and we are handling comprehensively in consideration of each customer's situation, raw materials cost global economy and price trend.

In July and August, profitability was weaker as raw material price hike was not passed through, but since September, profitability recovered to a range higher than the average. In 1H, customers based on long term price contract, such as auto, shipbuilding and home appliances, have maintained the same prices even though we had heavy burden on input cost. In 2H, we expect to remain with the same price or slightly increase. For a monthly-negotiated customers, we are responding based on the conditions of clients and the global market.

Carbon steel average sales price(ASP) in 3Q is similar to 2Q. We increased price with a moderate amount industry by industry and decreased it for some customers negotiating monthly basis. Domestic market had shown some price dip and export market was recovered price drop from forex effect. For STS, we reflected Nickel cost increase in the price with some markups in 3Q.

4Q ASP would be steady for long-term contracts. For distribution prices, it tends to reflect China market prices one to two months later in general. 4Q distributor's ASP is likely to decrease compared to 3Q as we consider China's market price fall since Thanksgiving holiday and the tendency to minimize inventory level from end-users who concern on recession next year. We believe this tendency will be continued until October to November.

Stainless Steel Business

Nickel price has been fluctuating between USD 12,000 and USD 17,000 from June to November. Overall, there was an increase of USD 4,000. Based on the 300 series of 8% nickel, the price increased by USD320. The nickel price hike was not passed through to the product price at the most suitable time, but with a lag, we increased the product price to the degree where profitability is ensured.

Qingshan Stainless Steel

Qingshan is planning to have a joint venture with Gilsan in Korea, but there is no progress as the domestic industry participants and the steel association share the same thoughts with us on oversupply. Although we do not have much concern, POSCO continues to make efforts for diversifying procurement sources to offset material price increase. In terms of our STS product mix, 400 series take up more than 45%, with which we will fortify our competitive advantage globally.

Raw material prices

Iron ore price shot up to USD120 in July due to a series of events such as Vale dam collapse in January, cyclone in March and rainstorm for four months in Amazon. Today it is stabilized and marking the lowest level in 3Q. Due to expected cyclone in Australia during winter, re-stocking demand will grow, which will lift the price to USD95 in 4Q. 1H next year will show a tight supply as Vale production will still be on a recovery. Toward 2H, iron ore price will be lowered down and annual price is forecast to be USD85.

As for coking coal, a seasonal issue will affect supply volume in 4Q. Re-stocking demand in China, ahead of Australia's cyclone, will sustain the price to move around USD160. As we expect demand weakness next year from global economic slowdown, and supply expansion is forecast, coal price will be around USD175, slightly lower than this year. Both iron ore and coking coal prices will decline, but a decrease in a major scale is less likely.

Earnings Outlook

Internally, we are discussing on next year outlook and earnings forecast and our consensus is to meet this year level consolidated OP. However, as it is expected that the steel market will peak out, we are required to achieve stronger performances in Global & Infra segments than this year's.

In 2018, overseas upstream mills have turned profits. In 2H 2019, with the weakened steel market condition, overseas downstream mills, which are mainly targeted at automakers as primary customers, are difficulties compared to 1H 2019. To overcome the market situation, we are trying to do more marketing activities, such as increasing sales volume, developing new customers, etc. While the steel market would seem tough until 1H 2020, we are trying to set the business plan of 2020 at a similar OP level of 2019.

In the 4Q 2019, with the global economy gets weakened, steel sales prices keep going down in many countries. Even the Indian products that were not circulated in the Southeast Asian countries and Korea are now offered with very low price. This also gives downside pressure on the regional steel price. As the high price of iron ores in 3Q 2019 will be mainly reflected in the manufacturing costs in 4Q 2019, the mill margin is likely to be squeezed. To overcome this external environment, manufacturing cost saving efforts are continuously being made. Also, increasing WTP sales volume will contribute to narrowing the mill margin squeeze as the product group is less sensitive to market volatilities.

Non-steel Business (Global & Infra Segment)

Until 3Q 2019, operating profit of POSCO's non-steel segment, which is named as Global & Infra business, has been increasing sequentially. This is mainly contributed by the gas business of POSCO International from the positive gas price trend. It is expected that the earnings level will be mostly maintained in 4Q 2019.

Lithium Business

Last year in August, POSCO made a contract with Galaxy Resources to acquire mining rights of brine in Argentina and this deal was finally sealed in February this year. Confirmed reserve by Galaxy was 2.25 million tons based on M&I resources. After closing the deal, POSCO has been executing additional exploration in second and third stages on its own. As a result of second stage exploration, it is evaluated that 5.67 million tons are reserved volume, which is significantly larger than the initial evaluation, and extraction period can be extended from initially forecast 20 years to 50 years. The value of this asset's mining rights acquired at USD280 million could be higher as it is calculated in accordance with resources volume. To realize it to profits, the demo plant is currently being built and tested, and investment for commercialization should be decided in early 2021. Construction of commercial plant will start 1H 2020, and it will take 1.5 to 2 years until completed. Along with the brine mining, we are planning to invest in 40,000 tons of lithium production annually from hard rock mine. Within 1.5 to 2 years, commercialized plant construction will be finished as well.

In regards to the lithium price outlook, we view that the fall of lithium price this year was due to the rapid increase from previous years mainly in the Chinese market. The Chinese government's reduction on EV subsidies led to a demand weakening and the price as well. Passing the year 2020, the price will rebound according to our outlook. By 2022, next generation EV's produced mainly by European makers will be released in the market and the demand will also follow in a major scale.

New bonds issued

We are acknowledged investors' feedback on our newly issued bonds. While some of you would think that it is quite a large size, we prepared it preemptively as there are prevalent concerns of global recession. It will also be used for repayment.

Dividend

In relation to the dividend policy, the key factor we consider the most is that many of our investors are long-term holders. We think that the stable dividend amount has more value than dividend fluctuation. I would highlight again our long term stable cash dividend policy rather than being closely linked to earnings. This year dividend will be resolved in the BOD meeting and we will try to live up to investor's expectations by outperforming in our earnings .

CAPEX

In 2019, we view consolidated capex as 6.1 trillion KRW including 1.4 trillion KRW of set aside reserve. Until 3Q, execution was 1.83 trillion KRW on a consolidated basis. It is 2.43 trillion KRW on a parent basis including 1.2 trillion KRW for purchase of off-gas power generation from POSCO Energy.

In terms of POSCO steel capex, 600 billion KRW was spent on maintenance, 180 billion KRW in profitability enhancement and 160 billion KRW in environmental investment.

For domestic subsidiaries, 930 billion KRW was used in. Major investments include 240 billion KRW used in building cathode/anode plant of POSCO Chemical. POSCO international has invested 160 billion KRW in exploration of Myanmar gas field and

Ukraine's grain terminal. POSCO Energy spent 440 billion KRW to acquire LNG terminal. For overseas subsidiaries, 90 billion KRW was used in.

Overall, execution rate is 36% on a consolidated basis which is slower than original capex plan. We expect this year capex will be around 3.7 trillion KRW as roughly 72% of planned capex excluding reserve.

POSCO SS VINA

SS-VINA has been in a difficult situation due to intensified market competition in Vietnam. Rebar is traditionally red-ocean and competition in H-beam market is also fierce as supplies from Southeast Asia are flowing in.

Managements are well aware that it is difficult to be sustainable under this condition, and are considering various options to stabilize the business. It's too early to give details at this stage, we're in talks with a third partner about changing its business structure.

One-off Items

In the coming Q4, POSCO does not expect to recognize big expenses or impairments like the case of Synthetic Natural Gas in the 4Q of 2018. However, it is possible to see restructuring for some of the businesses that have difficult time to make profits due to bad market situations. A decline in some subsidiaries’ stock values might lead to recognition of impairment losses. POSCO's assets will be evaluated by some professional agencies that their values will be accounted in the book during the Q4.

Income Tax

Effective tax rate on a consolidated basis has increased temporarily due to the swap of the LNG terminal and the off-gas power generation facility between POSCO and POSCO Energy in 3Q. In this transaction, POSCO Energy recognized profits from off-gas power generator sold and paid related taxes. However, its profit has been eliminated in a consolidation process as it is an internal transaction and made the effective tax rate higher as a result.