

Telephone conference on Financial Results for 1H FY2021 (November 11, 2021)

Questions and Answers

(Respondent: Hitoshi Sato, Senior Managing Executive Officer of SuMi TRUST Holdings)

Q.1	The full year forecast for Net income remained unchanged. It looks overly conservative. Could you share the reason and background behind the decision?
A.1	<p>Uncertainty in business environment has been decreased compared to 6 months ago. Having said that, we considered the following three points when we decided the forecast.</p> <p>First, it would take all of the 2H of the fiscal year to sell or improve the break-even points for several low break-even hedging transactions. Of course, we have a plan that a major part of losses generated from realizing unrealized losses of those transactions could be covered by profit from sales of strategic shareholdings.</p> <p>Second, regarding credit costs, we are keeping a conservative view on bipolarization of business and financial performance of client corporations, considering supply chain issues as well as soaring raw material prices which we have observed.</p> <p>Third, on the other hand, we have a conservative forecast on Net business profit before credit costs, which means we have potential upside as well.</p> <p>When we take these factors into consideration, we believe there is certain possibility of upward revision of Net income. We would like to meet the expectation of investors. However, we decided to keep the forecast figures unchanged to allow additional time for the assessment at this moment.</p>
Q.2	I would like to ask about the evaluation on current capital position and the outlook for the future. Regarding the outlook, I would like to know the direction of CET1 capital ratio and capital policy based on this ratio, rather than specific numbers.
A.2	<p>As you can find on page 15 of the “Summary of Financial Results for 1HFY2021 (hereinafter “Material”)", CET1 capital ratio based on finalized Basel III is close to 10%. Although our target is “stably above 10%", we do not assess our capital adequacy based on snapshot figure in a digital manner. We need to evaluate the adequacy of capital levels considering future outlooks as well. As such, we count on the expected reduction of risk weighted assets through divestment of strategic shareholdings.</p> <p>On the other hand, although we have been pursuing balance between adequacy and efficiency of capital, forecasted ROE for this fiscal year is around 6%. We are aware we need to improve the effective use of capital, including the potential share buyback as a tool to do so, in order to reach the medium to long term target of around 9%.</p>
Q.2	Are there any potential factors which may decrease CET1 capital ratio?
A.2	While there may potentially be some macro driven factors, but we do not believe that there are any such factors specific to our company at this time.

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Q.3	SuMi TRUST Bank issued a press release today regarding the voting rights guidelines for strategic shareholdings. Do you expect this to have any influence on dialogue with clients regarding the reduction of strategic shareholdings or any negative impact on business areas such as pensions, stock transfer agency, or lending?
A.3	We established these guidelines to explain our measure of dialogue with clients on the way to reduce conventional strategic shareholdings to zero. We recognize potential negative impact on our business due to reduction of strategic shareholdings. However, we believe that the guidelines themselves will not influence on divestment of strategic shareholdings nor on our business.

Q.4	CET1 capital ratio based on finalized Basel III improved by 0.2 percentage points due to reflection of clarified rules for capital floor. Could you explain the rule change? Please inform us if there will be further clarification in the future.
A.4	I won't go into details of calculation methodology, but simply speaking our previous calculation was conservative. We had not deducted loan loss reserves from required capital in the calculation of risk weighted assets. However, it has become clear that we could deduct it under the Draft Rules for the New Capital Adequacy Framework regarding finalized Basel III announced by Financial Services Agency in September of this year. Risk weighted asset decreased when the new rule was applied. We expect possibility of any further clarification to be quite limited since the Draft Rules has already been announced.

Q.5	I would like to ask about break down of 20bn yen of non-recurring profit in the explanation of YoY change of Net business profit before credit costs for SuMi TRUST Holdings. There is an explanation about it in the Material: 12bn yen of profits related to investment partnership and 3bn yen of dividends earned from a company with which our group has business partnerships with capital investment. Where is the remainder? I also would like to know non-recurring profit for SuMi TRUST Bank, if any.
A.5	Gains arising from counterparty risk of derivatives under CVA accounting, which has been applied from this fiscal year, made a positive contribution in the first half. A large part of the residual of non-recurring profit was due to it. As for the second question, all non-recurring profits other than 3 bn yen of dividends earned from a company with which our group company (namely Nikko Asset Management) has a business partnership with capital investment, belong to SuMi TRUST Bank.

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Q.6	<p>In the dialogue with the IR Department after the first quarter results, it was explained that the disposal of unrealized losses on hedging transactions would be done within the scope of gains on sales of strategic shareholding, and that this would not negate the upside of profits from other factors. Today's explanation seems to be different from the previous ones, as the company has posted a loss on Net gains on stocks with the disposal of losses on hedging transactions, and the forecast for the full-year Net income was also unchanged. We would like to know if this means that the plan has been revised, or if we should assume that the company will eventually dispose of the hedging transactions within the scope of gains from the sale of strategic shareholdings, but that this is just not visible at the time of the interim results.</p>
A.6	<p>Our basic stance on hedging transactions since the beginning of the fiscal year has been to carry as little risk as possible into FY 2022, and there has been no change in this stance. If investors are misled into thinking that we will use the unrealized losses on hedging transactions, which amount to approximately 350bn yen on a gross basis, as a means of adjusting bottom-line profits, we have explained that we have no such intention. We recognize that there is a certain range in the level of Net gains/losses on stocks depending on market movements as we take measures in line with our plan of carrying as little risk as possible into the next fiscal year.</p> <p>Posted loss on Net gains on stocks was not intentional, but rather a result of the process of conducting operations in anticipation of the next fiscal year. We will continue this process in the 2H of the fiscal year. Although we believe that the majority of the expected losses from disposal of hedging transactions we wish to address during the current fiscal year can be covered by gains on the sale of strategic shareholdings, since operations will take the entire 2H, we have decided to hold off on revising our bottom-line earnings forecast.</p>
Q.6	<p>Is it correct to say that you expect Net gains on stocks for the full year to be negative 30bn yen?</p>
A.6	<p>At this point in time, you can understand it as such.</p>

Q.7	<p>You have explained that you have made a conservative assumption for Net business profit before credit costs. I would like to know some additional information on the content and background of this. I would also like to know if it is correct to assume that variable costs will increase when you raise your annual forecast for G&A expenses by about 5bn yen.</p>
A.7	<p>The figures by segment are shown on page 8 of the Material. One point that we consider to be somewhat conservative is that we have set the full-year forecast for the Retail total solutions services net business profit before credit costs at 26bn yen, compared to 17bn yen in the 1H. I would like to add that we are not pessimistic that earnings will decline significantly in the 2H of the fiscal year, as we are seeing positive results in the business, especially in investment management consulting.</p> <p>Other businesses have some seasonality in nature and we also had some non-recurring profit in the 1H in Wholesale financial services. Taking that in account, we believe that the figures are generally in line with the actual situation. In addition, there is a difference between the total of each breakdown and the overall total in the data on page 8, and this is the profit and loss that belongs to head-office, which is not allocated to each business. We have a slight buffer in this area, and it can be said that there is room for upturn in response to guidance.</p> <p>As you expected, we are assuming that expenses will increase in line with the increase in gross business profit.</p> <p style="text-align: right;">(Continued to the next page)</p>

Q.8	I would like to ask you how you feel about the future reduction of strategic shareholdings, based on the status of dialogue with corporate clients.
A.8	(In addition to about 21% of clients with whom we are already discussing the timeline for the sale of strategic shareholdings), we are in a situation where we are continuing dialogue with 72% of our clients from whom we have understating on our policy. We are getting a sense that the sales will become more concrete as time goes by. It is a fact that dialogue is progressing where there is understanding and where it is easy to proceed, and from the 2H of the fiscal year onward, we believe that there may be different challenges in dialogues than in the 1H of this fiscal year, but as time passes, changes are occurring with clients, and we feel that the opinions of shareholders of clients are influencing management decisions.

Q.9	The fact that the dividends were left unchanged seems overly conservative. I think the company could have balanced the market's expectations a little more. I would like to know why it did so.
A.9	As for dividends, they are linked to the full-year earnings forecast, so your question may converge on why we left the guidance unchanged this time, but we recognize that an important topic is how to determine the ideal level of profit for the current fiscal year with an eye to the next fiscal year. We do not believe that the bottom line of 155bn yen is necessarily a satisfactory level, but we believe that it is important to determine the pace of profit growth going forward, and we want to assess various factors from that perspective. We would like you to understand that we have left dividends unchanged and we did not conduct share buyback because we believe that we need more time to assess the situation at this time.
Q.9	I would like to ask you whether management understand there is a gap between market expectations and the forecast shown this time, and whether you plan to address this issue in the future.
A.9	We are aware that there will be some comments that there is a gap from the expectations of investors, and we will once again take the comments we received today seriously.

Q.10	Profit attributable to deployment of surplus foreign currency funds was steady in the 1H, but what is your outlook for the 2H?
A.10	Profit attributable to deployment of surplus foreign currency funds for the 1H was approximately 5bn yen, which is almost unchanged from the approximately 5.5bn yen in the 1H of the previous fiscal year. As for the outlook for the 2H of the year, we are not too pessimistic because arbitrage opportunities tend to expand when the transactions could crossover year-end based on past track records, and we do not see any factor that would cause a deterioration compared to the 1H at this point.

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Q.11	I would like to ask you about your assessment of the real estate brokerage business for the corporate sector. The company has not revised the guidance for the real estate business. We would like to ask you about the outlook, including the status of the client appetites and transaction pipelines.
A.11	Results for the 1H of the fiscal year were generally in line with the plans, and we are satisfied with this. Compared to FY2019, the year prior to Covid-19 pandemic, profit from SuMi TRUST Bank and SuMi TRUST Realty were down approximately 3.9bn yen and 1.0 bn yen, respectively. However, if we take a look at our potential business pipelines as of the beginning of the 2H of this fiscal year, we have almost the same level with that of FY2019 and FY2020 when we had the highest level in the 2H of a fiscal year. In addition, while the selling needs of client companies are increasing in terms of financial requirements and improvement of capital efficiency, the buying needs of investors, both in Japan and overseas, are also very strong. So, we have a positive outlook.

Forward-Looking Statements

This document includes notes on future earnings.

Such descriptions are not in any way guaranteeing future earnings and are inclusive of risks and uncertainties.

Please be mindful that future earnings may differ against targets due to changes in the business environment and others.

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