

IR Day (March 18, 2022) Questions and Answers

Page numbers in the Q&A correspond to the page numbers in each theme.

1. SuMi TRUST Group's climate change initiatives

(Respondent: Riro Sato, Executive Officer of SuMi TRUST Holdings)

Q.1	<p>I now have a better understanding of the strengths related to impact evaluation and the Technology Based Finance ("TBF") team. What are the current challenges SuMi TRUST faces in pursuing these sustainability initiatives?</p> <p>In addition, it seems possible to set KPIs such as ESG-related AUM, environment friendly real estate consulting services and inheritance-related business, which are unique to a trust bank and different from those of megabanks. I would like to ask the future direction of KPI setting.</p>
A.1	<p>Let me describe the status of each initiative. With regard to impact evaluation, we began pioneering efforts in 2019 and are steadily expanding our appeal to clients as we accumulate our track record of results. On the other hand, as for the TBF team, it was launched last year and is currently in the mould making stage.</p> <p>The challenge for future evolution is the same for both endeavors: how to expand and develop initiatives in each area vertically, horizontally and diagonally in the future. Particularly regarding the TBF team, the current situation is that they are carefully moulding their foundation in order to obtain an adequate return on their labor.</p> <p>As you pointed out, we are aware of the issues in designating KPIs in line with the themes of climate change and sustainability, which are typical of a trust bank group, and we are currently deepening internal discussions on this issue.</p> <p>We are not at the stage of being able to present this information today, but we would like to communicate it externally in the future at the appropriate time.</p>
Q.2	<p>The Bank of Japan has issued research on flood risks, and late last year, the Hong Kong Monetary Authority issued research on the sharp rise in mortgage default risk due to rising sea levels. To what extent is climate change risk factored into SuMi TRUST Group's pricing of mortgage loans? I would like to know whether you intend to refine pricing in the future.</p>
A.2	<p>Firstly, at this timing we do not reflect climate change risk to our mortgage loan pricing. An analysis of the physical risk of the mortgage loan portfolio has been conducted and published in the first TCFD report, and the risk driver is flood damage. We have a mortgage loan portfolio of about 10 trillion yen and our latest estimate of the financial impact from physical risk is about 7 billion yen. While we recognize that updates will need to be made on a case-by-case basis in the future, we are not in a situation where material risks will be overlooked unless we take immediate action to modify our pricing.</p> <p>However, this does not mean that significant risks will not arise in the future, as the negative impacts of climate change will continue to increase. In the future, we will consider incorporating this into our pricing as we sophisticate our analysis and other aspects of risk management.</p>

Q.3	<p>How do you think the current situation in Ukraine and Russia, which has led to rising resource and energy prices, will affect SuMi TRUST's sustainable management?</p> <p>Do you view this situation as a short-term issue or as a need to increasingly promote climate change initiatives?</p>
A.3	<p>Related to what was explained earlier regarding governance, we discussed the implications regarding our risk profile in light of the situation in Ukraine and Russia at the Risk Committee in early March. An external committee member suggested that we should not view this issue as a short-term or transitory one, but rather that we should consider a risk management framework based on the possibility that we may not revert to the international society and framework that we had considered normal in the immediate future.</p> <p>We have to reply that we are still in the consideration stage regarding specific measures to be taken in light of these opinions, but we will conduct simulations that include not only future strategies and measures, but also the impact on our investment and loan portfolio, based on the assumption that energy prices will remain elevated for an extended period of time.</p> <p>From this point onward, including my personal view, there are two major extremes that can be expected in the future in response to the recent energy price spike.</p> <p>The first scenario is that if new oil and gas fields are developed due to the difficulty of obtaining gas and oil from Russia, progress towards climate change will be curtailed by the inability to close wells to secure return on investment even after prices settle in the future. The second scenario is that the shift to renewable energy will be further accelerated and they will drive investment, especially in Europe.</p> <p>However, the point of aiming for net-zero emissions by 2050 should be considered as an immovable goal of the global community. Even though there will be further developments in response to various changes in the situation, we believe that it will be necessary to conduct simulations from the perspective of how to achieve the 2050 goal.</p>

Q.4	<p>On page 12 of the presentation material, there is a "virtuous circulation in the area of sustainability." Is only SuMi TRUST Group included in this value chain, or does the Group intend to expand it by inviting other financial institutions as well?</p>
A.4	<p>We are aiming not only to involve our group affiliates, but also to have other financial institutions to join.</p> <p>While we will naturally do what we can in each area, in specific areas such as climate change, which requires huge amount of capital, there is even less need to insist on self-financing approach in comparison to other areas.</p> <p>Although we have been active in this area in the past, we would like to create a larger circulation and positive impact on society by proactively working with partners that we can work with, such as collaborating with regional banks and developing new financial channels through DX.</p>

Q.5	<p>I would like to ask about measures that you believe will be effective in working together with industries with high carbon intensity to lower their footprint in order to achieve Scope 3 target.</p> <p>I would also like to know what you envision for impact equity investments, reduction of strategic shareholdings and other specific measures to reduce GHG in your own portfolio.</p>
A.5	<p>We are currently working towards compliance with the PCAF (Partnership for Carbon Accounting Financials) standard for the measurement of GHG emissions from our portfolio. According to this standard, the contribution of both strategic shareholdings and senior loans would be the same, so a technical answer would be that reducing senior loans would have a greater effect.</p> <p>However, this is also only an answer on paper, and in practice, the impact will vary from industry sector to industry sector. We believe that lowering the average emissions intensity of each company will be most effective, and SuMi TRUST Group is firmly committed to being involved in this effort.</p> <p>Using the knowledge of the TBF team, we have been supporting clients in their efforts to reduce their emissions intensity by setting ambitious targets and tracing them through positive impact financing, as well as providing financial support by ourselves and, in some cases, inviting investors from the start of demonstration experiments and projects that are not yet on a commercial footing.</p>

Q.6	<p>We would like to ask how you evaluate each of these measures will affect ROE, such as the increase in impact equity, the reduction of strategic shareholdings and other initiatives to lower carbon intensity.</p>
A.6	<p>Let me explain each time frame separately.</p> <p>First, impact equity investments do not generate returns in the short term. In the next medium-term management plan, which spans several years into the future, we will further promote our transition to product related finance and steadily continue activities that will have a direct effect on improving ROE, such as increasing arrangement fees by expanding distribution to investors.</p> <p>However, since such current efforts alone will eventually turn into a red ocean and profitability will deteriorate significantly, we will constantly work to develop blue oceans while utilizing the framework of TBF and impact equity investment. The assumption is that once the risk profile of the sector has been defined to some extent and approaches commercial viability, investors will be invited according to their risk tolerance, creating a pathway to the fee business for the sector.</p> <p>In addition, as shown on page 12 of the document, we believe that by eventually incorporating individual funds into this value chain, we can contribute to improving ROE by increasing fee revenues in asset management and asset administration business areas as well as proprietary loans and credit investments business.</p>

2. TBF business initiatives

Our Impact business and examples

(Respondent: Minoru Hayashida, Senior Manager, Sustainability Management Dept., SuMi TRUST Holdings)

Q.1	Regarding the project to identify CO2 emissions described on page 19, I would like to know who participated in the project, with what backgrounds, and the contributions they made to the project. Also, please let us know the challenges and breakthroughs recognized by the project members.
A.1	I majored in biophysics in graduate school and started my working career as a researcher at RIKEN after earning a Ph.D. degree in science. I then worked in the private sector in research and development, launching new businesses, and most recently as a venture capitalist. I have shifted from the field of technology to the field of finance. In this project, in addition to my background in chemistry, it was necessary to have a proper overview of the supply chain. And I believe that my experience and background in science were useful to this project.

Q.2	Which organization calculated life cycle GHG emissions?
A.2	This calculation is made by the "Japan Automobile Tire Association" as noted in the source. We suggested which stage in the product life cycle should be focused and tackled.

Q.3	Regarding the TBF team initiative, how is it advantageous from a financing perspective if you have knowledge of technology? For example, is it correct to understand that risk estimate can be decreased or cash flow forecast can be increased? Also, how often do you intend to implement the adequacy of valuations?
A.3	The main point is to be able to evaluate the business feasibility from a technical point of view. We believe that this will increase the probability of success of the investment.

Q.4	SuMi Trust has announced 0.5 trillion yen of impact equity investment and 2.0 trillion yen of external funding from investors as the financial targets, but I would like you to describe how you assess whether this is quite low or ambitious from a technology perspective.
A.4	It depends on how you look at it. In terms of overall environment-related projects, I believe that this level of financial investment is necessary. On the other hand, there is probably no financial institution in Japan that is ready to invest funds on this scale. From this perspective, it can be said that we have set a very substantial investment target.

Q.5	I believe that the areas in which the TBF team is involved are not so profitable at this moment. Will you challenge to achieve pricing that meets the risk, or will you focus on attaining volume first?
A.5	The level of return on loans and equity investments in projects in which the TBF team participates must be higher than for typical projects. We will aim for appropriate return against each risk.

Our hydrogen related business and strategy

Q.1	Are there any projects that the TBF team is involved in regarding GHG emissions reductions in the shipping sector? You explained that one of TBF's strengths is its ability to contact directly with R&D departments, I would like to know why a financial institution like SuMi Trust can have contact with those departments of clients.
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A.1	<p>(Mr. Hayashida's answer)</p> <p>The TBF team is not directly involved in the impact assessment for Anchorship Partners transaction. The shipping finance team of the Structured Finance Department at that time calculated the CO2 reductions for this project, and the TBF team has been working with the relevant departments to tackle the project while leveraging the company's strengths.</p> <p>Our relationship managers have made significant efforts to keep better relationship with clients as well as TBF team members utilize their previous business network.</p>
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Q.2	<p>I would like to know how you came to join SuMi TRUST and what attracted you to the company. Also, do you think there is still a possibility to increase the number of members with similar backgrounds?</p>
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A.2	<p>(Mr. Hayashida's answer)</p> <p>I worked in venture capital nine years ago. At that time, I heard the term "impact investing" and became interested in the idea of using impact as an axis for investment decisions in addition to the traditional risk and return. I wanted to challenge myself in this field, but venture capitalists cannot support clients after exit. I joined SMTB four years ago because I believe that a financial institution like SMTB can support its clients throughout their entire life cycles and stages. After joining the company, I planned and proposed impact investing. The firm has a very strong competitive edge in the private equity space. We interviewed about 20 investment managers who are making impact investments among overseas private equity firms and organized a framework for impact investment. Since then, we have been engaged in work related to impact evaluation and impact management support.</p> <p>(Respondent: Takahide Haneda, Senior Manager, Sustainability Management Dept., SuMi TRUST Holdings)</p> <p>I worked in the research lab of an energy company until a year and a half ago. At that time, I was researching innovative technologies in fuel cells and electrolysis systems and working with manufacturers to commercialize them. In the course of my work, I became acutely aware of the importance of finance. In addition, I realized that in the case of a manufacturing company, there are restrictions on the scope of activities and collaboration with rival companies, and that there are many obstacles other than technology. In order to solve these problems, I thought it was necessary for someone with a technical background like myself to work in the financial industry and become a bridge between manufacturing companies and financial institutions. As a result, I expect that financial institutions and operating companies will work together to efficiently promote commercialization and productization, and that this will be a breakthrough to achieve carbon neutrality, which is a challenging hurdle to overcome. In addition, since I moved to a financial institution, I have actually been able to realize collaboration between rival companies that we had never thought of by having our company, a bank, act as an intermediary from a neutral standpoint. I intend to continue this kind of value-added corporate support in the future.</p> <p>(Mr. Sato's answer to a possibility to expand the TBF team)</p> <p>Regarding the TBF team composition, there is a possibility that more members will join in the future. We are currently recruiting members for the TBF team and have plans to hire imminently. We would like to continue to strengthen the team.</p>
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