

Investor Meeting on Financial Results for 1H FY2022 (November 18, 2022)

Questions and Answers

(Respondent: Toru Takakura, President of SuMi TRUST Holdings
Masaya Yamashiro, Executive Officer of SuMi TRUST Holdings)

Q.1	SuMi TRUST's PBR ratio is below 1x. What is the reason for this and what do you think is necessary to gain market recognition?
A.1	<p>I would like to explain our efforts to enhance corporate value, which is described on page11 of the presentation material.</p> <p>With regard to ROE, we are working on a capital-light management approach, with a focus on increasing stable fee income without significantly increasing risk-weighted assets. On and after page12, we look back at the 10 years since our management integration and presented our track record of achieving profitable growth without a significant increase of risk-weighted assets. This strategy will remain largely unchanged in direction and we will continue to bolster fee-based businesses such as asset management, asset administration and real estate-related businesses.</p> <p>With regard to PER, the key point is how to raise investors' and society's expectations for our business growth. I have mentioned the key phrase "virtuous circulation of funds, assets and capital" on various occasions since assuming office as president in April 2021. If we can enhance this circulation, it will lead to the growth of our group, which conducts businesses at many contact points in the capital and asset markets. For a long time, it has been difficult for funds, assets and capital to be circulated in Japan, but we are finally beginning to see the impetus for this circulation.</p> <p>Among individual clients, the asset formation generation is showing a strong interest in investing through DC, and an increasing number of them are investing on their own. Pension plans such as iDeCo and NISA are also being enhanced. In the market for seniors, we have been receiving an increasing number of inquiries from baby boomers not only about inheritance, but also about asset management in the face of increasing longevity and asset administration in the event of unforeseen circumstances.</p> <p>For corporate clients, investments in decarbonization are about to generate huge domestic demand of funds for the first time in many years. With investor funds circulating firmly in the market to meet this demand, the Group's asset management and asset administration businesses also have a chance to grow.</p> <p>However, we have yet to raise investors' expectations sufficiently, partly because we have not been able to materialize measures for growth. We are currently discussing the next Medium-term Management Plan, which will start in the next fiscal year, and we would like to raise investors' expectations by demonstrating concrete measures in the future.</p> <p>I have repeatedly communicated within the company regarding my intention to raise PBR, which is currently around 0.6x, to more than 1x as soon as possible. I would like you to understand that the Group's various initiatives are based on the premise of aiming for a PBR of 1x or more.</p>

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Q.2	<p>What is your view of the immediate business environment, including the macroeconomic and credit cycle? What steps are you taking in terms of management posture, downside risks, and growth opportunities based on this perception?</p>
A.2	<p>Uncertainty about the future is increasing. In this presentation material, the readiness regarding risk is explained from page 7 onward. We transformed our risk control approach in fiscal year 2017. We hedge our stock price fluctuation risk with bear funds and have been reducing our strategic shareholdings. With regard to credit risk, we have been prudent in managing our balance sheet since our management integration without significantly expanding it. In the current fiscal year, in addition to the normal level of credit costs of -20.0 billion yen for the full year, we have set aside additional special loan loss provision for this risk. With regard to interest risk, we will continue to manage our operations by restraining bond investments and will not take any major risks in the future.</p> <p>Our group's business areas are well diversified. I believe that our business portfolio is well suited for the uncertain times ahead.</p> <p>One of the growth opportunities we expect to see in the future is the continuation of large-scale investments in decarbonization, both domestically and internationally. As companies move forward with their efforts to create a decarbonized society, we shall also take appropriate risks and make investments to create a situation where investors' funds can be circulated and generate solid returns. In this trend, our group will also secure growth opportunities in areas such as asset management and asset administration.</p>

Q.3	<p>I would like to ask about the Common Equity Tier 1 capital (CET1) ratio (finalized Basel3 basis). Even if the ratio recovers quickly through profit accumulation, etc. in the future, it was 9.3% at the end of September 2022, compared to the target level of 10%, giving the impression that the Company is back in the capital accumulation phase. Given the current uncertain environment, should we expect you to continue its cautious approach to capital utilization, such as investment for future growth or share repurchase? Also, assuming no M&A, to what extent should capital level recover for the Company to make share repurchases?</p>
A.3	<p>The decline in the CET1 ratio is largely due to the yen's depreciation that progressed in the first half of fiscal year 2022. However, the impact of the yen's depreciation is also within the expected buffer. We will continue to invest in growth, as we cannot reap the fruits of our efforts in the future without investments. We are also making investments in human capital, IT and digital technology. Trust Base Co., Ltd., a specialized digital company established last year, now has more than 100 employees, and various projects are in progress.</p> <p>The increase in risk-weighted assets is largely due to the foreign exchange impact on foreign currency denominated assets, including investments in Apollo related funds. We will continue to work on controlling risk-weighted assets as a whole. However, there is also a timing for investments, and it is not always a good idea to balance the increase or decrease in risk-weighted assets.</p> <p>We intend to manage our investments taking investment timing into consideration within our capital buffer. I explained last year that we have shifted from the capital accumulation phase to the capital utilization phase, and this recognition remains unchanged.</p> <p style="text-align: right;">(Continued to the next page)</p>

	Share repurchases will always be considered in the context of balancing investments for growth. In general, there are investments that produce immediate results and others that take time to produce results. For example, the collaboration with UBS is a case where the investment benefit is immediately visible. We will continue to balance growth investments and share repurchases in a variety of combinations.
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Q.4	For the next Medium-term Management Plan, you have capability to achieve ROE of 7.5%, and normally you would aim for a medium- to long-term target of 9%. However, given the current uncertain business environment, is 8% a realistic target level? In terms of business segments, which segment will lead future growth as a driver?
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A.4	<p>Raising PBR requires improving ROE, but we will continue to take a cautious stance on financial results, as we need to work on this while also protecting deposits from depositors. Our "Earning power" has definitely increased compared to the past. Looking back on the 10 years since our management integration, we have been able to shift from a state in which we relied to some extent on market-oriented businesses such as bond investments to a state in which we have a profit structure centered on client-oriented businesses. We have also made various investments for growth by the last fiscal year, and the results of these investments can be expected in the future.</p> <p>In the first half of fiscal year 2022, Asset management business has been struggling due to a decrease in market value, but other business segments have been performing well. In the second half of the year, each business segment has continued to perform well so far, and we expect an upward revision to our earnings forecast in the future. However, given the uncertain environment, we have decided not to revise our full-year forecast at this time.</p> <p>In the mid- to long-term, we would like to reach ROE of 9% first and we are working internally to achieve a structure that will enable us to aim for 10% or more. However, since business environment assumes to be very uncertain, it is difficult to provide specific figures at this time. Growth drivers are in the business areas of asset management and asset administration, which are also related to increased investment in future climate change. There are also significant business opportunities in inheritance and asset succession to the next generation due to the increase in longevity. In addition to 2,000 trillion yen in financial assets, individuals hold 1,000 trillion yen in real estate, and we see significant business opportunities in this domain for the next 10 to 15 years.</p>
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Q.5	<p>In the case of SuMi TRUST Group, the contribution from foreign currency translation adjustments included in CET1 capital is small compared to Japanese megabanks, so the negative impact of yen depreciation on the CET1 ratio appears to be relatively large.</p> <p>Are there any measures to reduce the impact of exchange rate fluctuations?</p>
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A.5	<p>As you mentioned, the impact of the yen's depreciation on our CET1 ratio is greater than that of the megabanks. Therefore, we are managing our capital buffer with this risk in mind and are conscious of this in our various daily operations.</p> <p style="text-align: right;">(Continued to the next page)</p>
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	<p>Since the yen's depreciation will affect the CET1 ratio mainly in the area of risk-weighted assets, I would like to explain the direction of risk-weighted assets as a whole. First of all, risk-weighted assets are expected to decline in line with our efforts for reduction of strategic shareholdings. Of the total loan portfolio of approximately 30 trillion yen, one-third (approximately 10 trillion yen) is yen-denominated mortgage loans, and the remaining 20 trillion yen is corporate lending, with foreign currency denominated loans accounting for approximately 6 trillion yen. Looking at corporate lending and product related, there has been a shift toward product related loans, and product related includes both yen and foreign currencies. However, since foreign currency loans currently offer higher returns relative to risk, the overall trend is toward product related loans in foreign currencies. This is one of the reasons why we are susceptible to the impact of the yen's depreciation. However, as we reallocate these loans in the credit portfolio, our policy is to control the overall amount of risk-weighted assets while taking the impact of the yen's depreciation into account.</p> <p>The current volatility in foreign exchange rates has increased, and we will continue to manage our operations while considering not only the possibility of further yen depreciation, but also the possibility that the yen may appreciate in some cases.</p> <p>It should be noted that the CET1 ratio based on the current rule is at 11.11% as of September end, which is an adequate level.</p> <p>The profit/loss impact of foreign exchange rate fluctuations would be an increase of approximately 6.0 billion yen in net business profit if the yen depreciated by 10 yen. With regard to asset reallocation, we reduced low-profitable foreign currency corporate lending in 2Q, improving the spread by about 3 bps on a managerial accounting basis. We will continue to respond to foreign exchange rate fluctuations, taking both positive and negative impacts on capital and profit/loss into account.</p>
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Q.6	In the first half of fiscal year 2022, fee income from real estate brokerage and corporate credit-related drove revenues. How do you see the sustainability of this trend?
A.6	<p>Fee income from asset management and asset administration is linked to the increase or decrease in the market value of assets under management and asset under custody. Therefore, it is susceptible to the impact of market fluctuations in stocks, bonds and foreign exchange rates. However, we recognize that the overall market size for asset management and asset administration is on an expansionary trend, as investment opportunities are increasing around the world toward carbon neutrality in the future, which will require much more investor funds.</p> <p>As for real estate brokerage business, we are focusing on domestic real estate, and we are not too concerned about forecast for this fiscal year since we have a reasonable pipeline. On the other hand, from the next fiscal year onward, although foreign investors still show strong interest in Japanese real estate due to the yen's depreciation, there are some cases where foreign investors are taking a wait-and-see attitude due to higher funding cost associated with the recent hikes of interest rates. Under the current unclear and uncertain environment, we believe that monitoring investor trends closely is one of the most important factors when we consider whether the strong performance of real estate brokerage business could be sustained.</p>

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Q.7	In the first half of fiscal year 2022, there were some impacts from the deterioration of profits derived from investment partnership that constitutes a part of net interest income and related profit, and other non-recurring profit. What is the current situation and outlook for the private asset investment environment?
A.7	<p>Private assets are divided into various asset classes. And even within private equity, there are deals that can generate cash at an early stage and those that have posted valuation gains due to future expectations. Currently, there has been an adjustment mainly in deals whose prices had been rising due to future expectations, but the prices of deals that are generating cash are stable due to expectations for stable growth. We have always emphasized diversification of investment portfolio in private assets. One of the main reasons for investing in the Apollo-related alternative asset portfolio was that, in addition to the diversification of the portfolio itself, it contained a reasonable number of asset classes in which we had not yet invested. As a result, we believe that our portfolio as a whole is more diversified than before.</p> <p>Given the current unclear and uncertain environment, it is difficult to provide a clear outlook for the future, but we recognize that public assets such as listed stocks and bonds may be in a phase where volatility is greater and risks are more likely to be realized. It is practically impossible to allocate all investments to private assets, and we believe it is appropriate to diversify the overall investment portfolio by combining public assets and private assets including corporate lending in a well-balanced manner.</p> <p>Accounting treatment for investments in Apollo-related alternative asset portfolios adopt J-GAAP. Therefore, changes in Net Asset Value are not recognized as revenue. In addition, since the company will not incur the burden of goodwill amortization, there is no material concern that this will cause a sudden negative financial impact.</p>

Q.8	Toward decarbonization, the financing needs in the form of sustainable finance or transition finance is expected to grow. On the other hand, if these financing methods are not expected to generate short-term returns and must be undertaken without regard to return to some extent, I am concerned that many of them may not be expected to generate sufficient returns on investment. In that case, investors would not provide sufficient funds and banks would have to respond the needs by their own financing. What are your thoughts on this?
A.8	<p>While the direction of investment in decarbonization is on an upward trajectory around the world, funds will not be attracted in low-return investments. This is the same for us. Investing in projects without an appropriate return will eventually reach its limits. We cannot achieve a globally decarbonized society unless we create a strong flow of investment with an appropriate return.</p> <p>On the other hand, it may take time to generate returns or to develop new technologies. As with government funds and donations, we will strive to provide funds through impact equity investments and other methods in the early stages of a project. By planting seeds, such as investments in the early stages, we believe we must create a circulation of funds so that investors can earn a return.</p>

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Q.9	<p>With regard to a regional ecosystem, I would like to ask what your uniqueness is in this field.</p> <p>What areas of business are you successfully able to engage in depth that would make you recognized as a priority partner by your cooperative partners?</p>
A.9	<p>In order to revitalize a region, it is important to involve many people and begin various initiatives. Local energy business will also be centered on local production for local consumption. If natural energy sources such as geothermal, solar, wind and hydropower could be utilized and locally produced for local consumption, the strength of the region would be enhanced.</p> <p>One of our strengths is our employees who can collaborate with our clients with deep knowledge on highly specialized technologies since we established Technology based Finance("TBF") team.</p> <p>TBF teams and relationship managers in charge of corporate clients are starting initiatives together with universities and companies in various regions of Japan. As for specific examples, please refer page 30.</p> <p>Collaboration with regional financial institutions is one of our advantages, and successfully we can keep and develop a win-win relationship with them. We hold monthly carbon neutral study meetings with almost all regional banks and can collaborate with them from the initial stages, sharing initiatives and ideas from each region.</p>

Q.10	<p>With regard to the timing of achieving a PBR of at least 1.0x, the expression was "in the medium term" this May, but this time it has been changed to "at the earliest time possible". I understood there might have been some changes in terms of the environment. I would like to ask how we should understand this difference of expression.</p>
A.10	<p>We are managing credit costs and net gains on stocks in a conservative manner. We booked special loan loss provision and realized losses from bear funds in fiscal year 2021. Net gains on stocks in the first half of fiscal year 2022 is almost zero. Assuming that credit costs are leveled and excluding net gains on stocks including loss of bear funds which is becoming manageable, our actual ROE is higher than before. And if gains from the sale of strategic shareholdings contribute in the future, ROE can be further improved.</p> <p>Considering these circumstances, I said "at the earliest time possible" with a slightly stronger tone than before. We would like to steadily promote the virtuous circulation of funds, assets and capital, and to earn the high expectations from the market by realizing the expansion of business markets in areas such as carbon neutrality.</p>

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.

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