Investor Relations Meeting for 1H of FY2022
Q&A Summary

Presenter
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Q1. Regarding fee income (page 11 of the IR presentation material), progress in the second quarter seems to be somewhat weaker than progress in the first quarter, while targets have been slightly revised. Please elaborate on the status of each business in terms of how strong or weak it has been progressing and the momentum it has demonstrated thus far. Also, over the course of the next medium-term management plan (MMP) period, can the Resona Group achieve growth in fee income at a pace exceeding the current annual plan target, namely, a 4.6% year-on-year increase?

A1. Our approach remains virtually unchanged, and our current performance is solid. Although our performance in the first quarter is indeed in excess of progress in the second quarter, this is primarily attributable to special factors seen in the first quarter, including an increase in dividends from group credit insurance on the back of a declining mortality rate, along with the conclusion of some major succession-related deals in the M&A and real estate fields.

We have pursued recurring fee income from both existing businesses, which are centered on face-to-face consulting aimed at addressing customer needs in-depth, and new businesses, including the financial digital platform. With these two types of businesses now complementing each other, we are finally seeing our hybrid business model complete.

The financial digital platform could possibly grow significantly should we succeed in gaining the participation of new partners from different sectors as well as a greater number of regional financial institutions. Meanwhile, our face-to-face businesses, such as succession-related, AUM and settlement, are expected to perform robustly. Although their individual potential may vary, we believe that, going forward, we will be able to further expand income from each.

Q2. Please share your thoughts as President regarding shareholder returns. We know that the Group's Common Equity Tier (CET) 1 capital ratio target remains largely unchanged at around 10% on the finalized Basel 3 basis. Even taking into account concerns regarding the U.S. economic recession, wouldn't it be advisable to materially revise this target? Furthermore, once the CET1 capital ratio target is met, the Group is expected to raise the total shareholder return ratio. What are your plans for raising this ratio? Do you intend to raise the total shareholder return ratio as a whole, or are you thinking of raising the dividend payout ratio, as well? Will you strive to raise these indicators while maintaining the CET1 capital ratio within the target range? Please elaborate on your thinking on this matter.

A2. We will engage in intensive discussions regarding capital management policies going forward, and we intend to announce our conclusions in conjunction with the announcement of the next MMP in 2023. In any case, we consider achieving a CET1 capital ratio of 10%, on the finalized Basel 3 basis, to be a major milestone.

Having completed full repayment of public funds in 2015, we have since accumulated capital, with our current CET1 capital ratio being 9.9% against our target of 10%. Thus, we are now confident about the robustness of our financial position, which underpins our ability to take on the challenge of developing new earnings pillars for the next generation via, for example, the pursuit of inorganic growth. Our policy is to undertake growth investment and shareholder return measures in a well-balanced manner that secures soundness. We will also consider increasing the content of shareholder returns.

Specific methods for shareholder returns, such as increasing dividends per share or undertaking share buybacks, will be a subject of future discussion. As we have stated previously, we believe that the current number of shares issued is still excessive in light of our need to secure flexibility in capital management. We will consider both increasing dividends per share and undertaking share buybacks with an eye to striking a balance between these two endeavors.

Q3. It was reported that the Group has completed measures aimed at restoring the soundness of its foreign bond portfolio as planned. Do you intend to now consider additional measures to replace this portfolio in light of the current interest rate environment?

A3. Measures aimed at restoring the soundness of our foreign bond portfolio have progressed in line with our plan. Compared with its status at the beginning of this year, the balance of foreign bonds declined by half, with the risk volume (BPV including hedging) having decreased 60% while the profit margin more than doubled. In sum, as the first step of restoring portfolio soundness, our measures have yielded some positive outcomes. Although the current environment remains quite uncertain, we believe that risk control is still possible. We are also aware of the importance of controlling the risk of negative spreads by, for example, addressing the issue of unrealized losses. We have made progress in this aspect, as well.

Along with these protective measures, we expect to have the opportunity to take a more aggressive stance as we move forward with a close eye on market trends. Specifically, we will be closely monitoring the status of the FF interest rate, U.S. employment rate, the CPI and other factors while striving to restructure our portfolio over the medium to long term. Our mode of portfolio management involves utilizing hedging and other tools in the course of replacing our portfolio with high-profit-margin stocks with optimal timing. Thus far, we have succeeded in securing a robust foundation supporting this approach. Looking ahead, we will leverage the advantages arising from taking a forward-looking approach to restoring portfolio soundness.

Q4. The Group has entered a new phase in which it is stepping up the utilization of capital. In this light, if the Group were to undertake growth investment, what are its target fields in terms of capital allocation? Please describe your plans for capital allocation in both organic and inorganic fields.

A4. First of all, we must pay close attention to risks arising from major changes in the rules of the game. Specifically, changes in value systems are now under way due to progress in digitalization and the growing public awareness of sustainability. It is important to stay apprised of how and when these changes affect society, industrial structure and customer operations. In the organic field, we will focus on providing financing and other solutions for SME customers to help them adapt to these changes.

On the other hand, our initiatives in the inorganic field largely hinge on identifying partners who possess a competitive edge and robust earnings power on a stand-alone basis. In this regard, we will not consider differences in sectors to be major restrictions. We will also focus on measuring partners' potential for generating synergies with the Resona Group. Therefore, we will pay close attention to their functions, customer bases, human resources and other aspects in the course of considering investment. Our goal is not merely forming business alliances. Rather, we will remain conscious of what value we can deliver to our customers through new business partnerships. We will always employ this perspective as we select our partner candidates.

Q5. The balance of loans and bills discounted as of September 30, 2022, presented on page 9 of the IR presentation material, is in excess of JPY40 trillion. In particular, lending in the corporate division seems to be buoyed by robust funding needs among both SMEs and large enterprises. Please share your impression on the current operating results. Please also describe, if any, changes in fundraising trends, for example, a shift from direct to indirect financing, among large enterprises.

A5. Despite the changing times, indirect financing still remains the mainstream method of fundraising, especially for SME customers. Achieving a balance of loans and bills discounted exceeding JPY40 trillion represents a major milestone for the Resona Group. Currently, funding demand among our customers has begun to pick up as they are in the process of recovery from the repercussions of the COVID-19 pandemic. Moreover, there has been gradual growth in funding needs associated with capital investment aimed at adapting to changes in society, including the transition to digitalization and sustainability. We see these trends as serving as a major tailwind. Looking at large enterprises, we feel that they are being affected by rises in interest rates in the bond market. This, in turn, is prompting them to review their debt portfolios.

Q6. Regarding the settlement business (page 27 of the IR presentation material), the Group has made progress in BtoC settlement. Now, could you please comment on the future potential of the BtoB settlement business? Specifically, please elaborate on your impressions from the launch of Resona One-Stop Payment. What are your thoughts on the potential of this service?

A6. The BtoB settlement market has been largely left untouched, despite its significant growth potential.

For example, fund settlement and fund management undertaken by departments charged with ordering and other relevant back-office operations can be digitized and, therefore, are good candidates for data-driven upgrading. This will provide us with unmistakable business opportunities. In this light, Resona One-Stop Payment will serve as a foremost solution for corporations seeking to address digitalization-related issues.

Recently, we announced an alliance with Digital Garage, Inc. This firm boasts outstanding capabilities regarding the provision of new corporate solutions in the fields of e-commerce and other non-face-to-face settlement. Today’s customer behavior is being characterized by the integration of online and physical payment, with boundaries between BtoB and BtoC settlement becoming increasingly obscured. Amid the ongoing transformation and integration of payment methods, our alliance with this firm is expected to constitute a key initiative in terms of expanding both the BtoB and BtoC settlement businesses.

Also, our recent achievements related to the Resona Cashless Platform (RCP) are presented on the bottom left corner of page 27.
Although RCP made a somewhat slow start, the number of stores that introduced it rose to 14,000. Looking ahead, we expect RCP to generate major business opportunities.

Q7. Please describe factors contributing to growth in the balance of loans and bills discounted. Could you name, if any, signs of positive changes affecting the profit margin associated with this balance? Please describe your thoughts in light of geographic locations, sectors, size of borrower corporations and highlights of their operating results, as well as such external factors as trends in funding demand and global interest rate environment.

A7. The balance of loans and bills discounted at the end of the first half of the fiscal year is presented on page 9 of the IR presentation material.
The major year-on-year increase (12%) in the balance of lending to “large companies and other” is attributable to both an increase in lending to large enterprises and an increase in that to national and local governments. Looking at the region-based breakdown, Resona Bank performed robustly in the Tokyo metropolitan area and thus achieved an increase of 1.7%, or approximately JPY320.0 billion in the regional balance of loans and bills discounted, compared with the same period of the previous fiscal year. Resona Bank similarly achieved an outstanding performance in the Kansai area, with its regional balance increasing 1.1%, or approximately JPY180.0 billion, year on year. By sector, we have seen increases of around JPY100.0 billion each in the wholesale and retail sector as well as in the public corporation sector (excluding the Ministry of Finance).
In terms of profit margin, we have long struggled in a harsh environment for corporate lending that dates back to the introduction of the negative interest rate policy. However, we have now begun seeing signs of recovery. With the profit margin currently staying flat, we hardly anticipate a major downturn going forward. Accordingly, we will strive to make improvements even as we accumulate a balance of high-quality lending upon confirming customer demand via consulting.
On the other hand, while the recurring profit margin for residential housing loans stands at around 96bps, the profit margin for newly extended residential housing loans amounts only to slightly more than 60bps. Given the situation, we believe that the profit margin of our portfolio of these loans is likely to decline 3bps to 4bps per year for the time being.

Q8. The Resona Group announced a policy of enhancing the content of shareholder returns as it looks toward the launch of the next MMP. In this light, do you have in mind any risk scenarios that could cause the Group to revise its shareholder return policy? What factors do you expect to affect the Group's initiatives to step up shareholder returns? For example, please describe the possible impact of major inorganic investment or substantial growth in unrealized losses on foreign bonds.

A8. We currently expect no major risk scenarios to come into play. However, we do consider credit-related costs to be a risk factor requiring attention. We need to closely assess the spillover effect of the depreciation of the yen, surging resource prices, supply chain restrictions and other factors that, in turn, could affect our SME customers through a variety of routes. We must determine the timing and magnitude of their impact. In Japan, we have already seen growing gaps between the corporate goods price index and the consumer price index. SMEs are especially susceptible to this phenomenon.

Credit-related costs recorded in the first half were around 20% of the annual plan, suggesting stability. Nevertheless, we will take a steadfast approach to managing signs of abnormalities as well as extending management support to customers whose operating results need to be improved even as we serve a "running partner" to our customers over the long term.

In the market division, although we still need to remain vigilant, risks in this field are well under control.

Our current performance is reliably positive. Overall, we do not anticipate the sudden emergence of major risks. Going forward, we will gear up the pace of growth in core income and thereby demonstrate robust operating results.

Q9. Resona Bank and Saitama Resona Bank have seen significant increases in their balance of lending to national and local governments, etc. Could you describe, if any, special factors leading to these increases?

A9. Saitama and Osaka are both our "home markets." These markets, in turn, position us to record a certain volume of lending to local governments on an annual basis. Moreover, the above increases in lending balance include emerging funding needs arising from the end of special banking operations aimed at helping businesses counter fallout from the COVID-19 pandemic.

Q10. The Group has recorded strong results in customer-segment businesses. Please explain the necessity of foreign bond investment and your concepts on this endeavor. While megabanks, which extend lending to overseas borrowers, need a certain volume of foreign bond holdings to secure collateral or liquidity, the Resona Group holds such bonds for the sole purpose of asset management. In no way do we intend to deny the significance of the market division, but we wonder if the Group really needs to engage in foreign bond investment, which involves both foreign exchange fluctuation and interest rate risks.

A10. As yields on Japanese government bonds (JGB) remain extremely low, we recognize a certain degree of necessity of engaging in foreign bond investment in order to obtain a buffer against external fluctuations on diverse fronts and to secure smooth access to the market.

Currently, we are seeing the growing likelihood of establishing a portfolio equipped with high profit margin and capable of yielding robust carry-forward profit over the medium to long term. Therefore, we have no intention to withdraw from foreign bond investment.

Of course, neither do we intend to take a huge risk in this field. However, we deem it important, as a financial institution, to maintain a certain volume of foreign bond holdings in the context of overall P/L and B/S management.

Q11. Do you intend to develop the international business into a growth driver for the medium to long term? Or, are you looking to develop this business for the sole purpose of securing effective collaboration with alliance partners and therefore not necessarily focused on establishing an extensive overseas branch network to facilitate a shift of the Resona Group itself into conformance with international banking standards?

A11. Having experienced the injection of public funds, the Resona Group has previously focused its management resources on the domestic banking business. This has made it possible to curb volatility in incomes and thus helped increase the stability of our repayment of public funds. Since the full repayment of public funds in 2015, we have seen the steady accumulation of capital. With this in mind, we will engage in discussions regarding the positioning of the international business, with an eye to determining a future time frame for the development of this business.

In Japan, the Tokyo metropolitan area and the Kansai area constitute two key markets. At the same time, we need to closely assess what we could possibly accomplish in growth markets in such regions as Southeast Asia. In the long term, we intend to consider business development in Asia.

Q12. Please describe the expected level of profit to be achieved over the course of the next MMP period, along with factors affecting operating results, especially key positive and negative factors on income fronts. Looking at long-term trends in KPIs (page 79), net income seems to have bottomed out in FY2021, suggesting a possible turnaround toward a growth track. Does it indicate that structural reforms have begun to take effect? Or, do you expect the plateau situation to continue unless the current environment undergoes major changes, for example, the reversal of Bank of Japan's monetary policies?

A12. We are not positioned to comment specifically on the next MMP as the plan is now in the process of discussion. However, we have seen steady outcomes from earnings structure reforms being undertaken over the medium to long term.

With regard to cost structure reforms, we are now in a period of massive cash outflows arising from digitalization-related investment. It is important to offset these outflows via the effect of digitalization and thus realize growth in operating results. In this regard, our progress has been steady. These reforms have begun to yield outcomes in a stable manner.

With regard to new challenges, we aim to take a balanced approach to developing a solid portfolio of new earnings pillars and, to this end, will discuss how to secure new sources of incomes from, for example, our financial digital platform, as well as how to achieve inorganic growth via capital utilization. We will disclose the details of these new endeavors at the announcement of the next MMP.

Q13. Regarding the international business, please elaborate on your vision, if any, for future business development in Asia. Although the Resona Group lacks experience in traditional commercial banking outside Japan, do you intend to explore the possibilities of conventional banking businesses for Japanese or local large enterprises? Or do you intend to make entries into the local markets in untraditional ways, for example, by taking on the form of a challenger bank or non-bank?

A13. We do not necessarily insist on banking. We believe that we will be able to secure growth opportunities arising from Southeast Asian markets in diverse ways. Therefore, we will not only consider investment in local banks but also develop our overall strategies based on the analysis of a broad range of growth factors in the Southeast Asian region.

Q14. Currently, a variety of initiatives, including the integration of face-to-face and digital channels (page 24) and the settlement business (page 27), are under way. Is it hard to disclose the quantitative effect of these initiatives on the basis of gross or net operating profit?

A14. Not really, for example, income from debit cards amounted to JPY2.3 billion in the first half. In terms of full-year operating results, we aim to secure around JPY5.0 billion in this field.

With regard to the integration of face-to-face and digital channels, securing customer connections via the Group App sets our businesses apart from the conventional banking business model. As presented on the right half of page 25, comparisons between the frequent users of the app and other users indicate that gross operating profit per person from transactions with the former group of users was 2.1 times higher than transactions with the latter group. Likewise, the average number of products used in transactions with the former group was 1.6 times higher. Moreover, the frequent users of the app recorded a 4.3 times higher usage rate for outgoing remittance and 17.3 times higher usage rate for Resona Debit Cards. As such, the advantages arising from the use of the app have been well confirmed. Although we have striven to determine the quantitative effects of our initiatives on a managerial accounting basis, we will endeavor to translate these factors into KPIs that can be publicly disclosed by the time we announce the next MMP.

As presented on the bottom right corner of page 25, digital transactions now account for 95% of new accounts opened for foreign currency deposits, 80% of freshly purchased investment trusts, and 75% of new applications for card loans, suggesting a strong shift toward digitalization. Ongoing progress in digitalization not only results in changes in customers' financial behavior but also enables us to exhaustively overhaul our cost structure. Looking ahead, we will promote internal discussions aimed at launching the numerical disclosure of KPIs centered on indicating these and other effects of digitalization.

Q15. The Group's financial digital platform seems to be focused on providing Banking as a Service (BaaS). Is my understanding correct? Also, what advantages can the Resona Group offer through the API connection?

A15. Our financial digital platform constitutes just a part of BaaS. We would rather emphasize the attractiveness of services and functions backed by partners from diverse range of sectors than merely the smoothness of our API connection. We consider these strengths, along with low-cost and swift platform connections encompassing customer bases of partner regional financial institutions, to be of great value.

On the right half of page 32, we feature our pathway toward the maximization of profit. At present, the number of app downloads via the Mebuki Financial Group amounts to 900,000, providing robust connections with customers of this partner. Meanwhile, Bank of Yokohama, another partner, has thus far contributed to an increase of more than JPY40.0 billion in the overall balance of the fund wrap through the API connection. These initiatives are thus enabling the Resona Group to expand its earnings base.

The API connection itself brings us no advantages. Rather, our framework for this platform business generates value. We will strive to increase this value through the API connection.

Q16. Earlier in the Q&A sessions, you commented on progress in controlling negative spread. Please elaborate on your thoughts on this matter. We assume that the Group's plan at the beginning of the fiscal year has factored in a certain volume of the costs associated with measures aimed at restoring the soundness of its foreign bond portfolio. After that, however, U.S. interest rates rose on an ongoing basis, making the current interest rate environment deviate from the Group's initial assumptions. In light of these circumstances, do you think that the Group's measures to restore portfolio soundness are now completed as planned? Don't you recognize any need for additional measures to be undertaken in the second half?

A16. Prior to undertaking measures to restore the soundness of our securities portfolio, our holdings included foreign bonds with profit margin of 1.5% or less, or nearly no profit margin at all. However, as we have divested foreign bonds with such low profit margins through the above measures, the overall profit margin of our foreign bond portfolio has now recovered to slightly below 3%. The current FF rate has been improved to approximately 4%. Although negative spreads still remain for some of our portfolio components, these factors are fully manageable.

Looking ahead, we will go on to push forward with restructuring our portfolio over the medium to long term as market interest rates stabilize. In the course of this restructuring, we will incorporate bonds with higher profit margins with the aim of improving the overall profit margin of our portfolio.

The balance of foreign bonds is now only half of the previous level. Accordingly, we are confident about our overall ability to exercise a robust grip over this portfolio within an appropriate time frame even as we utilize interest rate hedging and other tools.

Q17. Regarding lending to SMEs, the Resona Group is expected to meet emerging funding needs in fields of DX, succession, and other undertakings. On the other hand, some of these borrowers may face the need of debt reductions, and therefore be seeking relevant consulting from the Group going forward. When these future changes in the environment are taken into account, do you expect the balance of the Group's SME loans to increase? Or do you anticipate that the Group will rather shift toward risk aversion in this field?

A17. Circumstances surrounding our SME customers differ largely on a company-by-company basis, as do their initiatives to address such circumstances. For customers being negatively affected by the depreciation of the yen, surging resource prices and other changes in the external environment, we focus on extending management support to help them achieve early improvement in operating results via, for example, the enhanced management of signs of abnormalities. In light of this highly volatile environment, we will address customer needs with greater sensitivity.

At the same time, changes affecting our customers on diverse fronts are causing them to face new needs and issues. As we aim to become "retail No. 1," we intend to offer robust support via, for example, consulting, in order to help them navigate amid these changes. This is, we believe, our raison d'être. In the course of these pursuits, we will proactively accommodate their funding needs and aid them in capital enhancement and other financial efforts while steadily accumulating the balance of lending.

Q18. Although the Group has announced a capital and business alliance with Digital Garage, do you have a plan to form business alliances with other IT firms or regional financial institutions or will you take a more proactive stance toward investing capital in external partners in light of the Group's entering a new phase of capital utilization?

A18. While forming capital alliances remains a viable option, we also consider a range of other methods, including external collaboration that utilizes the financial digital platform but involves no capital relationship. We will consider our mode of alliance on a case-by-case basis.

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