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Q&A Summary

Presenters

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Q1. How would you assess the progress of initiatives undertaken by Resona Academy and what are your views on issues you are facing in this regard? Also, could you share your thoughts on new initiatives that may be launched at Resona Academy in the future?

A1. First of all, human resource development takes time. It’s been only a short time since the launch of Resona Academy, so we have yet to see results. Also, the academy’s policy is not to limit training to a certain period of time. Rather, trainees will be provided with various forms of ongoing assistance and education, even after they have completed formal programs. We will also strive to accept a growing number of trainees. Furthermore, we expect graduates to exercise leadership at their branches and train their colleagues in turn. Through these efforts, we aim to enhance skills of our human resources as a whole. In addition, the programs offered at the academy place emphasis on enhancing communication skills. We will focus on helping branch staff enhance their ability to accurately assess customer expectations and what they really want to know and then provide them with concise and convincing explanations. Although our conventional training programs have previously centered on imparting knowledge on products, we believe that, going forward, these programs must include such topics as the recognition of the global economic environment.

Q2. Fee income appears to be under pressure in such business areas as asset formation support. How are you tackling this issue?

A2. We are aware of such pressure, but at the same time we believe that there are plenty of rooms for renegotiations to receive commensurate fees for a number of services. In addition, we are determined to raise our capabilities to deliver value to our customers through such services as consulting. Take the Resona Cashless Platform (RCP) for example. Through the provision of the RCP, we are not only acting as an acquiring bank but also assisting our customers in their IT utilization efforts. In this way, we aim to add value to our services associated with upstream business process by helping secure connection with POS systems and financial accounting systems. In a magazine interview, I once commented that "Resona will become a company that provides IT-related business assistance." Our efforts in these fields will help us create new service value, which will, in turn, serve as a strong rationale for raising fees.

We are also aware of the importance of exercising strict cost control. In this light, we are reviewing our operations to determine what can be automated and what should be done by human operators. This will be essential to the optimization of the fees we receive from customers.

Q3. (Page 41 of the presentation material) Resona achieved its target CET1 ratio excluding net unrealized gains on available-for-sale securities. Could you share your views on capital adequacy? Please also give your thoughts on the targeted total shareholder return ratio vis-à-vis equity capital in relation to Resona's policy of allocating "equal weight" to the three items described in the presentation material.

A3. Evaluations of capital adequacy can vary with external conditions. Currently, global trends have become increasingly uncertain due to such factors as U.S.-China trade friction. Taking these factors into account, we must stay alert to a downward trend in corporate earnings. Although we believe that our current level of capital is in no way inadequate, we must nevertheless consider enhancing capital with an eye to addressing future uncertainties. We know that there are a wide variety of shareholder opinions regarding whether our total shareholder return ratio is high or low. In fiscal 2019, we expended ¥10 billion on share repurchases. Of course, most observers wouldn't deem this significant spending to secure shareholder returns. However, we believe that this move represents a step toward the further enhancement of shareholder returns, lifting them slightly above the "equal weight" allocation policy. We are grateful if our shareholders appreciate our efforts to reward them in this manner.

Q4. (Page 28 of the presentation material) How would you assess KMFG's interim results in terms of top-line income versus forecasts at the beginning of the fiscal year? Also, what do you aim to achieve under the next medium-term management plan?

A4. We believe that KMFG has yet to establish as robust an earnings structure as expected at the beginning of the fiscal year, overcoming the current interest rate environment and rectifying its current cost structure. However, Kansai Mirai Bank (KMB), a KMFG subsidiary, finished integrating its business processes and systems with those used by other Resona Group companies in October, successfully completing the foremost task for KMFG. Thanks to this accomplishment, the Resona Group and KMFG are now better positioned to operate in an integrated manner, especially in the Kansai area, and generate synergies for the future. I have a lot of opportunities to engage with KMFG employees myself and felt their growing expectations with regard to the Resona products they would be allowed to handle in such fields as business succession. Furthermore, KMFG has strengths in some fields, including consumer loans. We will therefore strive to ensure that KMFG and other Resona Group companies can mutually utilize each other's strengths.

Q5. With regard to measures aimed at enhancing shareholder returns, do you intend to increase annual dividends from the current ¥21 per share or undertake share repurchases in the future? What is your takeaway from your communications with investors, do they prefer higher dividends or share repurchases?

A5. Although we are frequently engaged in dialogue with investors, we are not positioned to name one measure over another as their preferred option. Some investors say that Resona should place emphasis on securing medium- to long-term profitability, while others argue in favor of an increase in dividends or share repurchases. Their opinions vary largely by individual. We will continue discussing what will be an appropriate shareholder return policy to be adopted in the next medium-term management plan period.

Q6. Please explain your views on the accounting methodology for recording the reserve for possible loan losses. Do you intend such reserve to account for a fixed ratio in the overall loan portfolio in light of prevailing macro economic and other conditions? Or, despite the great number of such loans held by Resona, do you intend to employ a bottom-up approach, assessing the status of each borrower and thus determining the amount of reserve? Which approach do you think is appropriate? What is your methodology of providing reserves for apartment loans?

A6. (Page 14 of the presentation material) In the first half, net addition to the general reserve for possible loan losses totaled ¥2.8 billion, reflecting the preemptive recording of a reserve and a decrease in reversal gains. However, the specific reserve for possible loan losses has not increased significantly from the same period of the previous fiscal year. We have also seen an ongoing downward trend in the volume of non-performing loans (NPLs).

Generally speaking, we believe that such reserves should be recorded in a way that helps us adapt to and is consistent with changes in the operating environment over the medium to long term. Based on this belief, we are sharply focused on “quality” in loan management.

Whether it be general or specific, a lender must choose the optimal type of reserve for possible loan losses in light of the probability of risk materialization and the magnitude of impact should the risk materialize. Accordingly, we record a general reserve, even when we have not seen any materialization of risk, with an eye to securing resilience against uncertain macro economic trends. Simultaneously, we record a specific reserve for possible loan losses whenever we identify a borrower facing a material risk in the course of assessing account status.

As for the preemptive recording of a reserve in the first half, we have increased the general reserve. This move was decided as part of our response to the announcement of the lengthened time frame for surveying and repairing apartments with defects. There are no other abnormalities. Once defects are repaired, apartment business may be operated continuously. The recording of a reserve is aimed at securing financial resilience. Currently, the outstanding apartment loan balance is approximately ¥480 billion on our part. Apartment loan portfolio in question is well-diversified and encompasses approximately 8,000 borrowers. In addition, the majority of properties are situated in favorable locations in the Tokyo metropolitan and Kinki areas, where the number of single-person households is expected to grow.

Moreover, many of properties with relatively higher defect ratios were constructed years ago. Typically, apartment loans furnished for these properties have been repaid. Although loans furnished more than 10 years ago account for around 28% of Resona’s overall apartment loan portfolio, nearly 70% of loans for the properties in question had been furnished over a decade ago. Also, the ratio of past-due loans among such loans amounts only to 0.07%, well below the 0.12 ratio of such loans to overall apartment loans. Likewise, the NPL ratio for these properties is only a half that of overall apartment loans.

Resona is sharply focused on “quality” in loan management. Our apartment loan screening criteria does not rely on a rent guarantee scheme and rather favors properties with higher operational profitability. With the coverage ratio in excess of 80%, our apartment loan borrowers consist mainly of wealthy individuals.

Q7. Some regional banks have petitioned the government for permission to offer real estate brokerage services. If they succeed in obtaining a go-ahead, what is the possible impact on the Resona Group?

A7. We have already been handling real estate brokerage services as part of our trust banking functions. We would be very happy if all of our 840 domestic bases, including those run by Group banks, were allowed to handle real estate brokerage. Although we are not positioned to know whether the government would intend to give permissions only to regional banks, KMFG could be one of beneficiaries. In sum, we will enjoy a significantly positive impact if this scenario comes into play.

Q8. Although Resona’s policy on promoting digitalization and executing the “Omni-Strategy” look to be on the right path, these initiatives have yet to yield positive quantitative effects on operating results. You recently downwardly revised forecasts for net interest income from loans and deposits, please explain the factors behind that revision. Also, Resona’s asset formation support business is currently facing strong headwinds. When do you think the business will bottom out? In fiscal 2019, the environment appears to be the harshest when looking at factors making it difficult to shift to a recurring fee business model. What is your outlook for fiscal 2020 and beyond?

A8. We have seen an improvement in lending spreads in corporate banking. Moreover, interest rates for newly furnished housing loans have been stabilized. Today, housing loans with interest rates of less than 40bp are available from some regional banks or online-based banks. In contrast, Resona is furnishing such loans with interest rates ranging from 65bp to 70bp while adding value to its loan services via the provision of peripheral insurance products. Thanks to these efforts, we have not seen a significant drop in interest rates for newly furnished loans, despite the growing weight of low-interest rate, commission fee-type housing loans.

The downward revision to our forecasts for the volume of loans and bills discounted, was mainly attributable to changes in the current business environment. Although the volume of funding for capital investment grew 2.2% in a year to Sep. 30, 2019, it has nevertheless declined from the growth observed for the previous year despite a continuously strong business sentiment toward capital investment. We have no intention to proactively decrease the volume of loans and bills discounted, but we will maintain a cautious stance while giving due consideration to the profitability and soundness of our portfolio.

With regard to the asset formation support business, we are striving to promote a shift to recurring fee-based products instead of providing sales commission fee-type products. We revised our forecasts for fee income mainly in the insurance field. It is difficult to predict when we could see an upturn in our fee income. As there are a number of uncertainties in the asset management environment, we are seeing a growing number of customers hesitant to entrust their assets due to growing volatility in the short term. Nevertheless, we believe that we still have opportunities to meet customer needs via the provision of fund wrap and other stability-oriented asset management products.

Q9. Please tell us your thoughts on the possibility that results may fail to meet forecasts. Historically, it has been rare for Resona to incur credit-related expenses that exactly match forecasts. However, in the first half of fiscal 2019, the Company did so. Furthermore, despite Resona's steady efforts to reduce policy-oriented stockholdings, its fiscal 2019 forecast for net gains on stocks totaling ¥31.5 billion seems to be on the high side, considering the Company's first half results. Should Resona fail to meet its forecast for this item, do you think the Company will be able to supplement the shortfall with another source of income?

A9. Our forecast for net gains on stocks is not solely dependent on sales of policy-oriented stocks. In terms of market operations, we are carefully assessing the trend in both stocks and bonds. With the aim of meeting the targeted level of profit, we will continuously work to optimize our portfolio in light of the latest market environment.

Q10. The recent revision of Japan's Civil Code is expected to make it easier for banks to revise terms and conditions for deposits. Given this, how possible do you think it will be to enact account maintenance fees? Since 2004, Resona's terms and conditions for deposits have included a clause requiring fees for the maintenance of dormant accounts. It appears to be rational for Resona to revise the terms and conditions applicable to those accounts opened before 2004 as well given the revision of the Civil Code. Although it can be assumed that the 2004 introduction of this clause was aimed at improving the economic efficiency of account maintenance, I would like to have your comments on this matter.

A10. Currently, we have not considered enacting account maintenance fees even if the law revision allows us to amend our terms and conditions. However, if app-based transactions one day account for the majority of our business, there will be notable gaps between costs associated with such transactions and costs for traditional paper- and book-based, over-the-counter transactions. We may, in the future, consider enacting a new kind of fees to fill these gaps. However, we have not actually discussed about the enactment of new fees.

We charge account maintenance fees for dormant accounts only when "there have been no transactions and the account balance remained less than ¥10,000 over the course of two years." Our purpose is not to charge fees, but to reduce the cost of account management. As a result, we have not been facing burdens of managing the great number of dormant accounts. In recent years, banks have been forced to bear a growing workload to prevent the illicit use of bank accounts. Charging fees for the maintenance of dormant accounts is also helping mitigate risks arising from and reduce costs for countermeasures against the illicit use of bank accounts.

Q11. The latest statistics suggest rising loan delinquency and bankruptcy rates among SMEs. This seems confusing as the economy has not gone particularly bad. Also, the lack of successors and human resources is hardly a new problem. What is your assessment on the cause of this phenomenon? Is it due to the abolition of the mandatory disclosure and reporting system based on the SME Finance Facilitation Act? Or, are there significant changes in ways borrowers fall into insolvency and thus cause Resona to record greater credit costs compared with the past?

A11. The probability of defaults ratio for Resona's entire loan portfolio has declined from the previous fiscal year. In addition, our assessment of the actual status of borrowers suggests no signs of such a phenomenon. However, as written in some newspaper articles on regional bank performance, there have been some borrowers that inflated their financial results. The statistics you've cited may somewhat be affected by these incidents. However, we don't believe that overall SME performance is significantly deteriorating, neither have we seen no specific signs of rapid deterioration in the environment.

Taking a look at the nationwide trend in SMEs, we have certainly seen a growing number of businesses choosing to close down due to human resource shortages or the lack of successors. However, this is different from defaulting. We are closely assessing the status of each borrower while maintaining optimal monitoring systems in light of sector- and region-specific conditions and lending scheme characteristics, with the aim of not missing any sign of abnormality. These practices enable us to quickly identify a borrower facing challenges and provide assistance in terms of management improvement or corporate rehabilitation. We will continue maintaining these practices.

Q12. KMFG recorded gains on cancellation of investment trusts totaling ¥1.5 billion. Of these, the amount posted by KMB totals ¥1.3 billion, or approximately 20% of its actual net operating profit. This seems disproportionally large. Please explain the positioning of gains from cancellation of investment trusts. Also, do you expect gains of this scale to be recorded going forward and to serve as an ongoing component of profit? At the end of the fiscal year, will these gains amount to ¥2 billion or so?

A12. KMFG's decision to record the gain was based on its recognition of the current market environment and the status of its portfolio. In general, KMFG's stance on market operations and risk handling is consistent with that of the Resona Group. We refrain from being overly dependent on market revenues while focusing on expanding fee businesses to strengthen our profit structure. This policy is universal to all Resona Group companies. Accordingly, we don't expect KMFG to be dependent on gains from cancellation of investment trusts in terms of the composition of profit.

Q13. (Page 28 of the presentation material, lower left) With regard to KMFG's staffing plan, how many people do you aim to allocate over the medium to long term? KMFG's head office staff accounted for approximately 30% of the overall headcount in the first half; however, some regional bank representatives told us that the average ratio of head office staff should be around 20%. We assume that the current increase in head office staff is due to the need to promote system integration. What are your future plans vis-à-vis head office staffing numbers at KMFG?

A13. At present, discussion with regard to the revision of medium-term staffing plan is under way. First and foremost, we need to verify the effectiveness of the new branch system in terms of operational efficiency to estimate the number of back office staff that can be reduced. In fiscal 2020, Resona Bank will be the first to introduce this system, which will, in turn, be rolled out throughout the Group. Furthermore, our plans call for the introduction of the digital service office (DSO) system. This system will take over all the complicated, time-consuming procedures that have been traditionally handled at branches and cannot be transferred to administrative centers. We must also verify the impact of the introduction of the DSO system if we were to give you specific number with regard to head office staffing.

However, we are certainly expecting the number of back office staff to decrease significantly over the medium to long term, given the ongoing trend toward digitalization. Moreover, although the size of the head office staff may seem to be disproportional, this is due in large part to a technical issue regarding the definition of head office staff. Specifically, our number includes Loan Plaza staff, who act in close collaboration with branch staff, and head office sales staff handling tasks that require highly specialized expertise, including those associated with RCP and M&A. The number of head office staff who operate in these professional fields may increase going forward.

Q14. (Page 24 of the presentation material) What will be the level of operating expenses currently hovering around ¥370 billion (Page 24, lower right) for the upcoming three- to five-year period including the investments on and cost-saving effects of the new branch system you have just mentioned?. Although current operating expenses are split approximately 50-50 between personnel and non-personnel, please give your projections with regard to the future composition of these costs.

A14. Both personnel and non-personnel expenses are on downward trends. This attests to the success of our longstanding cost-control efforts. However, constant spending on system-related tasks will remain necessary going forward. In the medium term, we expect a slight increase in non-personnel costs and a modest decrease in personnel costs. Therefore, we will focus on curbing growth in overall non-personnel costs.

Q15. (Page 34 of the presentation material) With regard to measures associated with promoting RCP, Resona's strength in the corporate sector is well understood. How do you intend to popularize Resona's cashless settlement services among individual users? According to a certain news outlet, the Japanese government is expected to initiate a measure to promote the use of the "My Number" card in 2020. Resona may face a need to take direct measures to encompass individual customers. Although this will cause the Company to incur some costs associated with the issuance of points and other loyalty benefits, I would like to hear your thoughts on whether Resona should maintain its current policy on individual customers or shift such policy.

A15. We are aware of the discussion regarding the possibility of the point system employing the "My Number" card. A system of this kind would require national infrastructure and carry significant importance. Accordingly, the handling of My Number cards will be a matter of critical importance to banking operations. This may also provide us with such benefits as making it easier to determine customer identity. Although we have not decided yet on our basic policy with regard to the utilization of My Number cards, efforts are now under way to secure our organizational responsiveness to the possible introduction of the aforementioned system.