FY2016 Financial Results Investors' Meeting
(Held May 11, 2017) Q&A English Transcript

Q: Your Common Equity Tier 1 Capital Ratio is below 6% based on equity capital minus public funds. How do you intend to improve your total return ratio under these conditions?
A: The Bank's management team is expressing its intention to maintain or improve total shareholder return ratio. The Bank will determine shareholder returns based on the overall picture, including the operating environment and financial condition. Nonetheless, the Bank has been accumulating profit every year, which allows us to consider returning a part of the retained earnings to shareholders.

Q: What is the effect of calls for tighter regulation of excessive personal loans by the Japan Federation of Bar Associations and Japanese Bankers' Association on Shinsei Bank's card loan business?
A: The Bank manages *Shinsei Bank Card Loan – Lake* in a disciplined manner in compliance with the Money Lending Business Law. The Bank sees these developments as a step in the right direction for the market as a whole and is confident that it can harness its strengths in the business. We have no material impact on the growth momentum of the unsecured personal loan business.

Q: What is the risk of a rise in the ratio of loan loss write-offs in unsecured personal loans as the number of multiple debtors increases?
A: The Bank constantly monitors credit risk and so far has not noticed any signs of a sharp increase in loan losses stemming from multiple debts in its portfolio. The Bank assumes there will be some impact of credit risk on the operation of the Guarantee business, because it mainly complies with credit strategy of client financial institutions.

Q: What is the Bank's own assessment of "recurring profits" performance so far and performance relative to the original assumptions of the 3rd Medium-Term Management Plan (MTMP)?
A: The Bank's assessment is mixed. Priority businesses are progressing as expected. Loan balance trends in the Real Estate Finance business have diverged from initial assumptions, but this is due to taking a selective approach to lending in light of market conditions. The balance has not increased because of early redemption by many investors.
The Bank sees scope for improvement in other lending-related businesses, which have not progressed as well as expected, due in part to the effect of the negative interest rate policy.

Q: Are there any constraining factors for capital policy other than profit and capital?
A: The Bank declines to comment further on this matter.

Q: The Retail Banking business is continuing to make a loss. Is the Bank considering new ideas like procuring deposit funds mainly by Internet banking?
A: The roles of Retail Banking include procuring funds for the bank as a whole, providing asset management services to individual customers, and providing housing loans. Of these three, the cost of procuring funds should be tied to businesses that use the funds, but due to system and other limitations, it is difficult to allocate the cost precisely. The Bank is tackling the Retail Banking expense ratio as a management priority. The productivity enhancement project that we have unveiled is strongly focused on the retail business and offers many possibilities. Although some measures require investment, the Bank will adopt those with positive net present value.

Q: Do you expect revenue of *Shinsei Bank Card Loan – Lake* to grow to 30% of the total?
A: The Bank is unable to comment on specific target weightings at this stage, although we are confident that card loans are a business with growth potential. That being said, the Bank does not expect the domestic market to grow indefinitely. While we are now prioritizing growth, the Bank will explore opportunities to apply the skills and know-how nurtured in the unsecured personal loan business to small-lot finance businesses in Japan and overseas as the domestic market approaches saturation.

Q: What is the difference between "recurring profits" and "recurring/stable profits" (a key focus of the 3rd MTMP) in your FY16 results?
A: "Recurring profits" are recurring/stable profits minus profits from businesses with large market fluctuations such as the Treasury business. The Bank's "recurring profits" in FY16 is adjusted for profit from the sale of securities, which was substantial.
Q: Is the performance disparity between results and 3rd MTMP targets likely to constrain your shareholder returns policy?
A: The Bank will determine shareholder returns based on the overall picture, including the operating environment and financial condition at the time, regardless of any disparity between results and 3rd MTMP targets.

Q: You use the unfamiliar term "annual shareholder return plan" regarding your capital policy. Can you elaborate?
A: The Bank is using the term in the sense that it is considering shareholder returns as a total of share buybacks, dividends, etc. during the fiscal year.

Q: What is your roadmap for the repayment of public funds and progress in the second year of the 3rd MTMP?
A: The Bank's management is always aware of repayment of public funds, with the understanding that its main priority is to raise the share price and increase corporate value. The Bank expects that steady earnings performance as well as higher stock multiple will lead to improved share price valuations.

Q: What is the reason for such a solid balance sheet? The nonperforming loan ratio is extremely low. Although that means greater stability, is there any other reason?
A: The Bank is not running its operations with the intention of keeping a solid balance sheet. Most of the loans classified as nonperforming loans a long time ago turned out to be profitable recently. The Bank has taken a certain level of risk in growth businesses like Structured Finance and Consumer Finance. There is scope to consider effective ways to utilize capital such as shareholder returns, investing in business growth, inorganic growth, etc, at a time when the Bank is steadily increasing retained profit.

Q: FY17 targets are flat total revenue, higher expenses and flat final profit. The market likely reacted in disappointment today (May 11) as reflected in the sharp share price decline, because not only was there no share buyback announcement, but also there is no image of growth in the FY17 plan despite a higher balance of unsecured personal loans, which is a growth business. Is it accurate to say that the Bank expects profit growth in FY18 to be the same as growth of “recurring business profits”?
A: The Bank obviously understands that the market will react negatively on guidance of flat profits and no share buyback.
The Consumer Finance business does not contribute toward short-term growth of final profit, because credit costs arise as a forward expense during the growth phase. The same applies to the Structured Finance business. If the pace of growth becomes slow the final profit will be recorded.
Now is the time for increasing total revenue in these businesses. The Bank cannot afford to slow down its growth so that FY17 final profit appears to have increased. FY18 profit will also change depending on the performance of growth businesses.
The Bank expects a positive effect from sales recovery in asset management products and measures adopted by other businesses in addition to existing growth businesses. It is difficult to reflect in earnings estimates one-time factors, non-organic growth, and other factors that are difficult to quantify at this point in time.

Q: Is the current net credit cost ratio of 4.5% sustainable?
A: The Bank believes that a net credit cost ratio of 4–5% is reasonable. Although credit costs were relatively high in the Guarantee business in FY16, the credit model has been adjusted and its credit costs are under control.

Q: Your explanation of credit costs arising as a forward expense applies to part of the business that does not affect total revenue. I realize that it may be difficult to factor earnings other than “recurring business profits” into estimates because they are nonrecurring, but the market is paying attention to final profit (including one-time factors).
A: The Bank does not reflect in its earnings estimates factors that are not visible or those that are visible in terms of affecting performance, but are difficult to quantify. Obviously we will

incorporate the impact when it seems probable. Profit from the disposal of nonperforming loans is not zero, but is definitely shrinking.

Q: Please give us an organic description of group governance, including the Group Organizational Strategy Division, its relationship with the Group Business Strategy Division, and overview of Group Headquarters.
A: The Bank is starting up various projects with the purpose of improving productivity amid progressive commoditization of established businesses. The group's main subsidiaries are acquisitions and have been managed independently of each other. The Bank established a virtual headquarters on the assumption that integration of indirect functions would be highly effective for an organization of its size, in which the Group Organizational Strategy Division plays a leading role.
The Group Business Strategy Division reviews inorganic growth opportunities and business integration within the Group. The productivity enhancement project has had some positive effect on earnings. The Bank is aware of the need to express this effectively in FY17 guidance, but it does not believe in making short-term profit appear larger on paper at the price of medium- to long-term business growth.

Q: Is your credit rating a factor that limits inorganic growth? What are your thoughts on your credit rating?
A: The Bank's current rating is not a limitation. An A rating has a positive effect on market related business, but raising credit ratings is not a top management priority for us.

Q: What is the reason for not revising the FY18 net income target of the MTMP?
A: The Bank simply hasn't revised its FY18 profit plan. There is no other reason.

Q: Regarding the "optimization of the group's branch network across entities" objective of your productivity enhancement project, what do you expect to gain from this, considering that Shinsei Bank doesn't have that many branches?
A: The measure targets 700 unmanned Shinsei Financial branches as well as Shinsei Bank branches. The expression "across entities" means individual companies such as Shinsei Bank, Showa Leasing, and APLUS Financial can integrate business activities.

Q: Why have you added a slide on corporate tax to your presentation materials?
A: The Bank added the slides as supplementary information, because people often ask questions about it and the content is difficult to explain verbally.

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Q: Please explain the level of Kabarai (grey zone) reserve?

A: We maintain grey zone reserve in three entities, i.e. Shinsei Financial, Shinsei Personal Loan (Shinki) and APLUS FINANCIAL. Major exposure of grey zone amounts of the Kabarai reserve is Shinsei Financial. We believe that we have ample reserve in total. The number of the claims came down by 20% in FY2016 compared to the previous year, and we expect it to continue to decline in FY2017. When we look at reserve level of each entity we did not constitute a life-time reserve for Shinsei Personal Loan and APLUS FINANCIAL. Thus, we had to set aside the reserve for those two entities. But we have made a life-time reserve for Shinsei Financial.

Q: What level is that to avoid further addition of provision for the entities in FY2017?

A: There is 10 years statute of limitation from the last transaction date, and this issue has been around 10 years. Activities of law firms and judicial scriveners are not as active as in the previous years. If there is a clear trend that the grey zone claims are coming down rapidly, then the accountant would be comfortable in determining the appropriateness of the reserve.

Q: Why does credit provision seem high relative to your NPL ratio?

A: Our plan of net credit costs for FY2017 is JPY 32 billion which is flat as FY2016. We had JPY 3 billion of credit reserve in Institutional Business and JPY 29 billion in the Individual Business in FY2016. In FY2017 we expect unsecured loan asset growth needs additional JPY 2 billion of reserve. The composition for FY2017 is JPY 1 billion of credit reserve for the Institutional Business and JPY 31 billion from the Individual Business to accommodate the asset growth. We do not rely on any credit recovery from the Institutional Business as the NPL ratio is nearly zero.

Q: What is the main reason of the risk weighted assets increase? Why did the risk assets go up by switching the methodology from the Standard Approach (SA) to Foundation Internal Ratings-Based Approach (F-IRB)? Is there any plan for such changes next year to impact the risk weighted assets?

A: When switching from the Standard Approach to the Foundation Internal Rating-Based Approach, we are required close to JPY 200 billion in the Bank Lake business, which is the combination of the methodology changes and asset growth. It also increased by JPY 200 billion from asset growth in the Structured Finance. We do not envision such upward changes in risk assets pertaining to the methodology changes.

Q: Why can’t you layout the shareholder return to allocate certain percentage to share buyback and dividend? What causes the uncertainty?
A: Improvement of the shareholder return is one of the most important management issues. We seriously consider how to maintain or improve the total shareholder return ratio. It requires discussion with various stakeholders. Our management is expeditiously working on it.

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