

## Major questions and answers at SMBC Group IR Day 2018

1. **Naoki Tamura,**  
**Senior Managing Executive Officer,**  
**Retail Business Unit**

**Q1. It seems that SMBC has been promoting retail branch reorganization with more speed than the other mega banks in Japan. What are the reasons for this? Are there any plans to reduce the number of branches?**

A1. There are two major reasons. One is that we are trying to improve cost efficiency at branches by reducing costs required for basic banking services such as deposit and transactions, whose profitability are very low, to the minimum. The other reason is to transform all the branches to next-generation branches at an early stage in order to promote digital transactions. This is because digitalization, in our belief, will begin to spread at an accelerated pace, once it reaches a certain penetration rate.

We plan to maintain the number of branches since we consider that face-to-face contact points with customers continue to be important for consultation in the wealth management business. What is important is not about reducing the number of branches, but to improve efficiency at branches. We will address initiatives to reduce cost while at the same time adopt paperless, cashless and other digital technologies.

**Q2. What measures are you taking to increase the utilization rate for digital channels?**

A2. Our target is to increase the utilization rate for digital channels to 40% by FY3/20, which is the final year of our Medium-Term Management Plan. This target has been set based on the idea of increasing the ratio to the level of advanced countries in Asia. Last autumn, our team visited banks in Europe and had discussions on how they promoted digitalization. This revealed that the use of digital channels became popular in Europe not because the use of internet in Europe was high from the beginning. Rather, it increased gradually as bank employees explained the procedure of conducting digital transactions to each of their customers when they visited the banks. Thus, along with sophisticating and improving our smartphone apps, we will follow suit of European banks and increase the utilization rate steadily through diligent efforts including having our employees explain how to use the apps to customers at our branches.

**Q3. How does the shift to a cashless society impact the credit card business?**

A3. China's rapid shift towards a cashless society was driven by Alipay and WeChat Pay, but this was because the credit card system was not developed that broadly in China. Japan, on the other hand, has a well-established credit card system like the U.S. Therefore, whatever payment method drives Japan's shift to a cashless society, we expect that the existing system for credit cards will be utilized for these transactions. Under SMBC Group, we have Sumitomo Mitsui Card Company and Cedyna as leading credit card companies of both issuing and acquiring businesses in Japan. Therefore, it would be a big business opportunity for us when the progress of the shift to a cashless society increases the use of credit cards.

In Japan, there are already many different payment methods, including credit cards, debit cards, e-money and QR codes. We consider that the possibility of these methods to be consolidated into any one of them is low. For this reason, we aim to take the initiative to promote the shift to a cashless society in Japan, by providing (a) users with services which enable them to pay anytime, anywhere and by preferred method and (b) business operators with services which enable them to support users' payment through a single terminal. In other words, we will take the initiative to lead the transition to a cashless payment society in Japan by comprehensively meeting the needs of both users and business operators.

**Q4. How would the voluntary restrictions on card loans impact the lending and guarantee businesses?**

A4. In order to ensure further protection of borrowers, we reviewed the way our advertising and screening schemes are being operated, based on the agreed arrangements within the Japanese Bankers Association. Through this review, the outstanding balance of card loans at SMBC decreased. However, the outstanding balances at SMBC Consumer Finance and SMBC Mobit have been growing, offsetting the decrease at SMBC. As a result, the outstanding balance at SMBC Group as a whole is increasing. As to the guarantee business at SMBC Consumer Finance, the loan guarantee amount has been increasing, despite the voluntary restrictions by regional banks. This is because the regional banks just started their card loan business and is still growing.

However, the rate of increase in the outstanding balance of card loans is smaller than expected in the Medium-Term Management Plan. We are working to achieve the goal of bottom line profit set in the Medium-Term Management Plan through expense control and lower default rates with stricter screening criteria.

**2. Manabu Narita,  
Deputy President and Executive Officer,  
Wholesale Business Unit**

**Q1. What is the outlook for interest earned on loans and bills discounted for domestic corporations?**

A1. The rate of interest earned on domestic loans of SMBC is continuing to decline, but is still higher than that of other banks. The decline is largely due to the impact of repayment and refinancing of high-yield loans conducted in the past. However, while the spread on new loans is almost at the same level as that on a stock basis, room for further decline of loan spread has become quite limited. This is because we are focusing on expanding high-value-added loans, and by offering added values, we aim to eliminate competition and secure higher loan spread. Through these efforts, we would like to end the decline in interest earned on loans by the end of this Medium-Term Management Plan.

**Q2. What efforts are being made at front offices to improve profitability?**

A2. As part of the efforts to improve profitability, front offices are creating account plans for each customer. This does not mean that we will terminate transactions with unprofitable customers. Rather, it means that we will make efforts as a group to address the challenge of how we could improve the profitability of such customers. At the same time, we should be careful not to make employees at front offices feel intimidated and fall into a diminishing equilibrium made by the term "Discipline." This is the reason why we are promoting the market leader strategy and focusing on high-value-added loans. As a result, we were able to increase the outstanding balance of loans to mid-sized corporations and SMEs without lowering the spread in April and May. We will maintain this policy going forward and endeavor to further improve profitability.

**Q3. Regarding the real estate-related business of SMBC Trust Bank, what are the factors for the smaller profit compared to the other trust banks, and what measures are you planning to take?**

A3. With respect to the real estate brokerage service, we consider that the biggest factor for the profit difference is the size of the dedicated workforce. Although there is plenty of room to improve market share by approaching SMBC's customer base, SMBC Trust Bank did not have the workforce to realize such potential. Based on

this recognition, SMBC Trust Bank has been increasing personnel for the brokerage business and finally established a workforce large enough to earn a gross profit of around ¥10 billion. In addition, SMBC Trust Bank launched the asset management business in February 2017, and now has the full lineup of functions for the real estate-related business.

The ratio of customers in SMBC's entire customer base with whom SMBC Trust Bank has business with is yet very low, which implies plenty of room for SMBC Trust Bank to expand the ratio going forward.

**Q4. Is there any impact of the corporate governance code on the reduction of strategic shareholdings? How will you make up for the loss in dividend income caused by such reduction?**

A4. We have made steady progress in the reduction of strategic shareholdings since 2015. In order to achieve a further reduction, we need to proceed with it under mutual understanding, which can be achieved by communicating well with each customer looking at their capital policy. While the impact of the amendment of the corporate governance code is yet to be identified at this point, the implementation of the code has definitely changed the awareness of our customers. SMBC Nikko Securities' solution including block offer and other services is being well received by our customers and we are hoping to accelerate the reduction in strategic shareholdings while maintaining a win-win relationship with them.

As for the expected loss in dividend income, we consider that it can easily be made up by increasing asset-light income.

**Q5. One year has passed since the introduction of the group-wide business unit. Have you seen any changes in the awareness of employees?**

A5. Changes are definitely felt, as implied by the results of the survey for employees conducted in December last year. According to the survey, 80% of the employees have become more aware of the group-wide sales promotion. At the same time, the survey also clarified a challenge for us since only about 30% of all employees answered that they actually noticed the effects of the group-wide sales promotion. One major factor for this result is that, although the number of tossups (business referrals) has been increasing, most of these potential transactions have not been monetized. Therefore I think there is plenty of room for further improvement.

**3. Masahiko Oshima,  
Senior Managing Executive Officer,  
International Business Unit**

**Q1. Please tell us about the business opportunities and credit risks anticipated in each region in the coming three years.**

A1. As for the Americas, the economy seems to be stronger than shown in the economic indicators. A major potential risk is the intensifying trade war between the U.S. and other countries. However, as to the financial industry, although the market is vast and strictly regulated, the probability is high for us to expand income if rules are complied with and ample cost is spent to establish a framework to do business in the market. From this perspective, we consider that expanding business in the Americas is an important step in pursuing the growth of SMBC Group.

Economic situations in Europe are inferior to that of the Americas or Asia, partly due to increased uncertainty regarding Brexit and other EU-related issues. However, we are not betting on the strong macro economic growth. Rather, our business opportunities lie when large local banks become relatively weak along with the economy since our major customers are global companies and large local companies who are less immune to the influence of local economic conditions. We do not expect that the said risks will lead to a major crisis. We intend to seek opportunities in asset acquisition and other areas selectively to enhance our strengths.

We recognize that Asia is one of the fast growing markets in the world and has plenty of room for further growth. We will steadily promote our strategy to realize Asia-centric operations, which is one of our key initiatives. We do not deny the possibility that the emerging economies will be affected to some extent by the normalization of interest rates in Europe and the U.S. At present, assuming a certain level of downside risk, we are conducting business carefully within that range. On the other hand, if the environment gets more severe, such situation may turn out to be a great opportunity for us. We will accelerate the growth of our business when such golden opportunity arrives.

As to the credit environment, there are no risks that we are particularly concerned about at present. After the bankruptcy of Lehman Brothers, a safety net was built, and the regulations on leverage have become more stringent as well as risks associated with securitization transactions have become visible. Considering these factors, I personally think that it is unlikely that a major crisis with the magnitude as large as the Lehman Crisis will occur again. What we have to worry about the most

is the sudden moves in the emerging countries. The risk for us is that unexpected events involving fluctuation of resource price/currency, geopolitical risk and others occur in a complex form at an unexpected place and time. Therefore, we must always be prepared to confront situations when such unexpected risks materialize. It is important to enhance our sensitivity to various subtle changes and to have the ability to revise portfolios flexibly and promptly when a major event occurs. In this sense, we are promoting distribution of assets in our O&D business and expansion of direct contact with investors.

**Q2. What is the reason for the little increase in high profit assets in FY3/18?**

A2. We learned painful lessons from the past experience involving high profit assets. That is, if we obtain such assets without accurate understanding of the risk environment, it will cause us trouble later on. For example, LBOs for middle cap companies are in a dangerous level according to our criteria, since the degree of leverage has risen significantly. Since we are a major player in this field in the U.K., we are approached on almost all transactions in the early stages. We put all transactions through a very strict screening process and in this fiscal year, the transactions that our front offices decided to pursue accounted for only 9% of all the transactions brought to our attention. We are not trying to be cautious with every single opportunity, but we do not intend to increase risk-weighted assets without careful consideration either. Our policy is to be on the safe side at the expense of the speed of asset accumulation when we feel that the risk is too large.

**Q3. From the perspective of risk-weighted asset control, how will you achieve balance between assets to be distributed in the O&D business and those to be held on your balance sheet?**

A3. Our policy differs from that of investment banks. From the standpoint of managing the direction of projects by maintaining relationships with borrowers, we have set a basic policy to hold a certain percentage of total assets at any point in time, rather than distributing all the originated assets. In project finance, in particular, we consider that holding a certain percentage of assets gives us advantage in order to promote the business continuously, in both the terms of maintaining relationships with borrowers and gaining trust from investors.

**Q4. What is attractive about the Indonesian market where you are promoting the multi-franchise strategy? Other than Indonesia, which countries are you focusing on?**

A4. Indonesia has a population of 260 million people and is enjoying rapid economic growth. The country provides a foothold into the Islamic world, and has a culture that is relatively approachable for us. Excluding Indonesia, the country we focus on the most is Vietnam. We have a 15% ownership of VIETNAM EXIMBANK and have sent some personnel to the bank as directors. Vietnam has a population of about 90 million people with a high level of education. Since Vietnam has an ideal demographic pyramid as Indonesia does, we consider that it has a large potential for its macro-economic growth. We will first grow the business in Indonesia and Vietnam. After that we plan to expand the business into India, the Philippines, Thailand, Malaysia and other parts of Asia.

**Q5. Who are the depositors of the foreign currency deposits? Will the balance of foreign currency deposits grow at the same pace as in the past?**

A5. The customer base of foreign currency deposits is becoming diverse and spreading out to include large European and U.S. companies, central banks and fund-based investors. Our focus in the past few years have been on aggregating oil money from the Middle East and other regions. In addition, we have been focusing on becoming an account bank when executing project finance and other large-scale financing. By doing so, we have been able to steadily increase management accounts, in which deposits are pooled in preparation for payment to projects, thereby succeeding in aggregating highly sticky deposits.

We are hoping to maintain the current growth rate of the balance of foreign currency deposits, but I am hearing from the front offices that it is not going to be easy. What we are focusing on under these circumstances is to promote cross-selling through the implementation of CMS and other means and thereby to increase highly sticky current deposits. While quantity is of course important, we put emphasis on pursuing the “quality” of deposits and increase stable deposits that will not get withdrawn under stress situations.

**4. Hiroshi Munemasa,  
Senior Managing Executive Officer,  
Global Markets Business Unit**

**Q1. What are SMBC Group's strengths in S&T compared to its competitors?**

A1. SMBC Group's strength is the ability to analyze extensive data collected from within and outside the group and to propose solutions developed by leveraging our knowledge and insight as a market player. While some are still in a pilot phase, we believe that if we continue these efforts, we will be able to utilize SMBC Group's customer base as the strength of the S&T business.

**Q2. What do you think would be the future outlook of BOJ's monetary policy?**

A2. I personally consider that if all the factors, i.e. (a) the U.S. political risks being cleared, (b) the U.S. economy turning up again after the midterm election, triggering a risk-on market led by the U.S. stock market, (c) the acceleration of the FED's pace of raising interest rates, (d) the bottoming out of the decline in the consumer price index in Japan with the decline of yen and gets momentum toward 1%, are in place, then the BOJ may consider revising the framework of its monetary policy before the inflation target of 2% is achieved. The process that I presume begins with increasing the interest rate for the 10-year zone in yield curve control, followed by decreasing the purchase amount of JGB gradually and ends with terminating the negative interest rate policy.

**Q3. What would be the impact of the U.S.-China trade friction on the future real economy?**

A3. We are considering wide-ranging scenarios for the U.S.-China trade friction. One is a mild scenario in which the friction ends in a battle of words and is settled toward the U.S. midterm election. In a much more radical scenario, which could also be assumed, trade transactions decrease to the extent of impacting the real economy, and eventually result in a revision of the monetary policy leading to a complete change in market conditions. Unfortunately, since the behavior of President Trump is unpredictable, the discussion prevailing in SMBC Group is in favor of reactive actions, rather than proactive ones.



**Q4. The basis swap cost is currently stable at a low level. Do you expect this trend to continue in the future?**

A4. We are watching this trend a little cautiously. At this point, it is not moving toward a decline in the credit cycle, but we could hardly foresee as to until when this state will continue. In response to these circumstances, we slightly increased funding from the second half of FY3/18 until to date.

**5. Masayuki Matsumoto,  
Outside Director**

**Q1. How does the bank's governance differ from that of the companies you worked for?**

A1. One of the differences is that regulations on banks extend widely and are more stringent. This is probably because banks have a significant impact on people's lives and the national economy. It is, therefore, very important for banks to earn a decent income while complying with regulations. Another difference is that risk factors are extremely diverse and global and they surge over to a bank in a highly complex manner. To confront such risks, we need to collect and analyze information carefully and take countermeasures promptly.

**Q2. As an outside director, what do you consider is the strength of SMBC Group?**

A2. The strength of SMBC Group is that it has potential for creating new businesses by organically associating the potential abilities held by each group company. When SMBC Group introduced the group-wide business unit last fiscal year to shift to cross-functional management, I thought that it would take a considerable amount of time before penetrating throughout the entire organization. However, when I talked with the front offices, I found that the system was firmly fixed and is already achieving satisfactory results, much faster than I had expected. I believe that new businesses are likely to be created if we accelerate these initiatives.

**Q3. As an outside director, what is your opinion regarding the reduction of strategic shareholdings?**

A3. Since risks are inherent in shareholdings including strategic shareholdings, financial institutions must work to reduce such risks. Based on this concept, SMBC Group developed and is executing its reduction plan targeting 2020. As to the shares to be held continuously, we need to investigate each one of them from the standpoint of finding a decent reason to keep them, such as their returns and stability. Strategic shareholding is a result of the history and various experiences accumulated between customers during the course of doing business with them. When selling such shares, I think it important to fully analyze the anticipated impact and discuss with customers in a polite and careful manner.

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