



Round-Table Discussion with Outside Directors

# Reaching a New Stage as a Financial Conglomerate Through Investment for Growth

**Nakashima** Mr. Arthur M. Mitchel, Outside Director of Sumitomo Mitsui Financial Group, Ms. Eriko Sakurai, Outside Director of Sumitomo Mitsui Financial Group, and Mr. Isao Teshirogi, Outside Director of Sumitomo Mitsui Banking Corporation, have joined us today to discuss the vision that SMBC Group should be pursuing, with the focus being on the investment for growth we executed in FY2021. Thank you all for taking part in today's round-table discussion.

**Teshirogi** A year has passed since I was appointed as an outside director of Sumitomo Mitsui Banking Corporation. My impression during this time is that SMBC Group aggressively pursued investment opportunities to realize future growth. I was impressed that everyone was very familiar with the various processes, for example explaining the benefits, etc. of the M&A transaction to outside directors at Board of Director meetings.

**Nakashima** In FY2021, our investments exceeded ¥400 billion. This is only the second time in SMBC Group's history that such an amount has been used to fund acquisitions

in a single fiscal year. The first time was when we acquired SMBC Nikko Securities. If we look back at SMBC Group's M&A history, when Sumitomo Mitsui Banking Corporation was established in 2001 we announced our vision of becoming a financial conglomerate. Sumitomo Mitsui Financial Group was established the following year, and we engaged in M&A targeting domestic credit card companies, securities companies, and trust banks with the aim of expanding our businesses. It was never a case of only strengthening our core banking capabilities. We also proactively pursued overseas M&A opportunities and most recently, we acquired equity stakes in Fullerton India, FE Credit in Vietnam, and RCBC in the Philippines. We also entered into a strategic alliance with a U.S. firm Jefferies. As a result, while SMBC Group's overseas business at first only generated approximately 5% of the Group's total profit, our overseas business now generates approximately 30% of SMBC Group's total profit. The share of profit generated by SMBC Group's non-banking business has also risen from 20% to 40%. Could all of you kindly share how you evaluate SMBC Group's current business portfolio?

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**Mitchel** SMBC Group is making steady progress towards transforming itself into a financial conglomerate. I believe the profit contributions of SMBC Group's overseas business and non-banking businesses will undergo further growth. SMBC Group has the potential to not only play an important role in the Japanese economy, but also the global economy. As such, I look forward to seeing SMBC Group expand its global presence. I believe that the strategic alliance with Jefferies is a very good investment, as it will provide SMBC Group with a valuable foothold to further grow its overseas business. Having said this, I would like discussions to take place regarding how SMBC Group as a whole will strengthen its finance capabilities.

**Sakurai** I have been especially vocal in voicing my opinions regarding SMBC Group's overseas M&A strategy since I was told the reason for the offer to be an Outside Director was to help strengthen SMBC Group's global strategy. Mr. Nakashima, who at that time was the General Manager of the Corporate Planning Department, may recall that I meticulously confirmed the logic behind SMBC Group's acquisition of Bank BTPN by adopting the tone of "Why Indonesia?," "Why BTPN?," etc. I wanted to confirm



**Arthur M. Mitchel**

Outside Director,  
**Sumitomo Mitsui  
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the acquisition's consistency with SMBC Group's overall strategy. In other words, I wanted to confirm that executing the acquisition had not become the end goal. About five years ago, I asked Mr. Nakashima what sort of blueprints were being prepared for SMBC Group's global strategy. I believe SMBC Group's past M&A transactions are all consistent with the strategy that Mr. Nakashima kindly explained to me at that time. It is wonderful that SMBC Group has been able to expand its business portfolio in such a consistent manner.

**Teshirogi** When I look at SMBC Group's actions over the past few years, I can see that it is trying to proactively plant the seeds of its next stage of growth by capturing opportunities arising from growth in Asia. However, there is no guarantee

that all of SMBC Group's investments will be successful. Knowing when to step back is as important as knowing when to push forward. SMBC Group has proved its competence in this area through the past sale of its shares in Kansai regional banks and other arrangements. I look forward to seeing SMBC Group continue pursuing disciplined growth investments based on a clear set of investment criteria.

**Mitchel** I agree. Taking a disciplined approach is very important. However, given that the interests of numerous stakeholders often become intertwined with each other in an M&A transaction, the reality is that complying with set investment criteria is not an easy task. In the past, SMBC Group decided not to pursue an acquisition opportunity involving another financial institution. I feel that Japanese corporations often overpay in M&A transactions but, looking back, I feel that by walking away from that acquisition opportunity, SMBC Group was able to avoid such a situation. I believe that this case illustrates SMBC Group's ability to apply discipline to its M&A activities.

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**Nakashima** Of course, we have also experienced certain challenges. For example, two years after making our initial investment in Bank BTPN we had to book impairment losses. From the lessons learned from this experience, we focused on strengthening M&A governance. For example, we engaged in a comprehensive review of our due diligence process. We also made improvements from an organizational perspective, such as establishing the Business Development Department two years ago. The Department acts as SMBC Group's M&A execution team. While there is still much room for improvement, the progress we have made would not have been possible without the input of our Outside Directors. I am very grateful for your advice.

**Sakurai** I believe that SMBC Group has developed a good management system. Regular reviews of past investments for growth are conducted at Board of Director meetings, allowing us to discuss methods to improve those investments. If I were to suggest going forward, it would be the execution of initiatives to further enhance the synergies generated

by SMBC Group's M&A activities. This holds the key to SMBC Group realizing further global growth.

**Teshirogi** When carrying out its inorganic strategy, SMBC Group must clearly explain its overall strategy to investees while ensuring they understand the type of culture SMBC Group values. No sense of unity or synergy will be born without first completing this step. How strongly and clearly SMBC Group's vision is communicated to investees is a key factor in determining the success of M&A transactions.

**Nakashima** With the ongoing relaxation of COVID-19 related travel restrictions, I will coordinate with our Group CEO to engage in face-to-face meetings with the overseas companies in which we have acquired stakes, to further deepen communication and mutual understanding.

**Sakurai** PMI is an essential part of maximizing the benefits that arise from merging with or acquiring a corporation. The long-term success of the M&A transaction will greatly vary depending on how well PMI is

carried out during the first few years following the transaction. In this regard, I believe that SMBC Group's PMI capabilities have undergone significant improvement with the establishment of the Business Development Department and the increasing number of staff who are well versed in the conditions of the investees' home country, especially in Asia.

**Mitchel** In order to successfully expand its business portfolio, SMBC Group must hire staff with the appropriate skill sets. When entering a new business or territory via M&A, SMBC Group should carefully consider what type of personnel it requires before deciding on its M&A target.

**Nakashima** I completely agree. For example, if we were to expand our presence in the U.S. investment banking sector, we would need to hire outside personnel. However, given SMBC Group's current global position and scale of operations, hiring top tier personnel in this sector would be challenging. As such, our strategic partnership with Jefferies holds great significance, given the large number of Jefferies' personnel who possess the necessary skill sets.

**Teshirogi** Since the topic of global reputation has been brought up, I would like to make a suggestion. During Board of Director meetings, SMBC Group's businesses would often be compared to those of other Japanese megabanks. Is this comparison still relevant? Shouldn't SMBC Group be comparing itself to global corporations? By adopting this





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approach, I believe that the mindsets of SMBC Group employees will start to change from being domestically oriented to globally oriented, and that external entities will also start to view SMBC Group as being a global financial firm.

**Sakurai** Selecting companies for comparison with SMBC Group will be important. The same topic was raised by another outside director of another company where I used to serve as an Outside Director. External entities now compare that company with global corporations, rather than other Japanese corporations.

**Nakashima** In the past, Japanese megabanks pursued similar strategies. As such, comparisons with each other had value. However, this

is no longer the case. As the two of you have both pointed out, we need to change. Thank you for raising this point.

**Teshirogi** SMBC Group is currently implementing its Asia strategy, focusing on Indonesia, India, Vietnam, and the Philippines. However, I believe that our attention should also be directed to other developing economies. Discussions should take place regarding which new country SMBC Group should enter based on the country's economic growth, expected return on investment, and the contributions that SMBC Group can make to the country's development and growth. SMBC Group's Outside Directors come from a variety of backgrounds, and I believe it is possible to obtain a diverse range

of views and opinions. As such, I would like SMBC Group to develop new markets, even though a degree of risk may be involved, by engaging in robust discussions in Board of Director meetings. In addition, I believe that further discussions are required regarding SMBC Group's strategies in developed countries. We should discuss and determine which sectors can be classified as growth sectors and how we can capture their growth.

**Sakurai** I serve as the head of the Sustainability Committee, and I feel that the role the financial sector must play in sustainability is changing. However, since no clear solution has been reached, I would like the Sustainability Committee to engage in such discussions. It is also important that we do not solely focus on the growth opportunities; we must also pay close attention to the risks involved. Given Russia's recent invasion of Ukraine, the ability to accurately determine geopolitical risk is becoming very important.

**Nakashima** We must be careful when analyzing geopolitical risk, as there is a material difference in the impact on SMBC Group's business based on particular country or territory in question. For example, we could forecast with a degree of certainty the impact of Russia's invasion of Ukraine on SMBC Group's business, which was fairly limited compared to our total profit.

**Sakurai** I hear that U.S. corporations are engaging in very detailed scenario planning for countries and regions that could have a significant impact



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on their operations in the case of conflicts or etc. I am aware that SMBC Group has commenced such efforts, but I would like such scenario planning to be carried out with a greater sense of speed and urgency.

**Mitchel** I serve as an outside director at another firm, and they are also engaging in such discussions. In addition, as part of their long-term growth strategy they forecast the status of the market ten years from now, then back-cast to determine what sort of products and personnel are required. While it is easy for manufacturers to engage in such discussions, this is not the case for the financial sector. However, it is still necessary to think about the future shape of the financial sector.

**Nakashima** We are also engaging in such discussions, and they encompass a variety of scenarios. However, as Mr. Mitchel has stated, it is a challenge. Finance is a business that sustains the economy, so trying to predict the state of the financial sector ten years from now is very similar to trying to predict the state of the world ten years from now. However, just because this is the case does not mean that we do not have to try. Now, this slightly changes the perspective of our current discussion, but investment for growth is purely a method of applying our capital, and our capital policy is to balance the allocation of excess capital between investment for growth and shareholder returns. In my discussions with investors, I have repeatedly been told that SMBC Group's capital should be used to finance share buybacks, given that



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our PBR is less than 0.5, rather than applied to investment for growth. What are your opinions regarding this matter? As this is the last topic for today's round-table discussion, please share with us your frank and honest opinions.

**Teshirogi** Given the uncertainty and the speed at which the world is changing, I believe that a company risks being completely left behind if it cuts back on investing for growth. However, the company must engage in discussions with its various stakeholders. SMBC Group must conduct even closer discussions with its shareholders and investors before proceeding with further investment, and carefully explain that each investment for growth it pursues is crucial to become a financial institution with a global presence.

**Mitchel** I agree. I believe that, as Group CFO, Mr. Nakashima needs to adopt the perspective of SMBC Group's shareholders and investors when speaking at Board of Director meetings and Management Committee meetings. Based on this approach, selected investments for growth will be investments for which

investors' understanding and support can be obtained.

**Sakurai** I have faced similar questions in my discussions with investors. As Mr. Mitchel commented, my response is that the investment opportunities were selected after careful discussions based on investors' perspectives. I don't support investments that would only improve the share price, rather than contributing to future growth. As such, I hope to see SMBC Group steadily carry out the growth initiatives that it has decided upon.

**Nakashima** Please continue to provide me with your frank opinions as I will use your suggestions to enhance the quality of our dialogue with shareholders and investors while incorporating them into our global strategy. Thank you for sharing your valuable opinions with us today.