

Major Questions and Answers:
Press Conference for Fiscal 2000 Financial Results

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Place: Press Club in the Bank of Japan (Tokyo)

Announced by:

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<Credit Cost Related>

Q. What are the major factors behind the new occurrence of problem loans, amounting to around 700 billion yen?

A. The first factor is the deterioration of our assets. The Japanese economy continues to be sluggish, and financial conditions of borrowers are still getting worse. Under these circumstances, we have revised the classification of our borrowers, resulting in some of those loans being newly classified as problem loans. The second factor is that we took pro-active steps toward the resolution of the problem loan issue.

Q. How much assets do you think will newly deteriorate as problem loans this fiscal year?

A. We expect our annual credit cost to be around 400 billion yen. It is not easy to predict the amount of problem loans that will newly occur in the future, but we will take the required steps in order to dispose them within two to three years. Looking from the other side, to prevent the new occurrence of problem loans, we will have to engage in further conversation with our borrowers, and guide them to take concrete actions toward their revitalization.

Q. Is SMBC considering the adoption of stricter reserving policy rules? Another bank explained that they took some credit cost on Normal Borrowers as a result of stricter provisioning rules.

A. We do not know about the other bank's method of accounting for problem loans, so we cannot comment on it. Our reserve for Borrowers Requiring Caution is based on the actual default ratio, and we have no plan to change this criterion.

Q. SMBC's total problem loans and Substandard Assets decreased a little from last year, while another bank largely increased the amount in the past half year. How do you interpret this?

A. We do not know about the other bank's method of accounting for problem loans, so we cannot comment on it. Our self-assessment is based on an objective standard, is in compliance with the FSA's Inspection Manual, and was properly audited by Certified Public Accountants. We will continue to follow our standards.

Q. Are you going to take more hands-on control over Borrowers Requiring Caution?

A. We are already taking hands-on control over Borrowers Requiring Caution. Rather than taking more severe control over them, we will go into the specific steps to seek their restoration.

Q. What do you think about forgiving debt for a second time?

A. Personally, I do not believe that the second time is always unacceptable, although the first time is acceptable. When time has passed since the first debt waiver and the circumstances have changed, we believe it is possible to consider debt forgiveness on a case-by-case basis—provided that there is a rational plan for restructuring from that point on, the probability of collecting debt is higher, the cost to the Bank is less than it would be in an ordinary liquidation, and the responsibility of the borrower's management is reexamined.

Q. You mentioned that one of the reasons for the new occurrence of problem loans is the depressed economy. But on the other hand, some people see that the banks' self-assessment criteria were rather loose. What do you think of this?

A. I fully recognize that such a type of view exists. However, our self-assessment and provisioning are made with objective criteria, such as the actual default ratio and market value of real estates, and are subjected to an external audit. Thus, while it may have been difficult to incorporate future prospects in them, the write-offs and reserves were definitely strict at the time they were made.

Q. How much of the credit cost for this fiscal year will be used for the final disposal of problem loans?

A. In our rationalization plan, we forecasted the annual credit cost for this fiscal year to be 200 billion yen. Credit cost for the final disposal of the problem loans is included in this 200 billion yen. But our current forecast took into consideration the new guideline, which requires us to dispose Bankrupt and Quasi-Bankrupt Assets and Doubtful Assets within two to three years. Of the 400 billion yen of expected credit cost, nearly half is considered to derive from the acceleration of final disposal.

Q. It is being said that the final disposal of problem loans may result in massive unemployment. What do you think about this?

A. There are two different ways to look at: one way for the portion handled by promoting the rebuilding of the borrower, and a second way for the portion that we must abandon. Up until now, we have been talking with borrowers, and now we have to take the next step forward. When accelerating the final disposal of problem loans, we have to think about the social impact, the employment problem, the deflationary spiral, and other issues. The most fundamental thing that is needed is for the Bank and the borrower to speak frankly with each other. It is like a doctor-patient relationship. To be a good doctor, the Bank sometimes has to tell the patient harsh things. As a result, if a company that should be rebuilt then rebuilds itself, the impact on the economy is small. However, with loan disposal, rushing to sell land may affect land prices, and there may be an influence on the deflationary spiral. Bulk sale may also affect the price of credit. On the other hand, if companies with the potential to rebuild are allowed to go bankrupt, the impact on the economy will be large.

Q. So in the end, is your Bank not going to carry out final disposal of problem loans in light of these effects? Or will you still do it?

A. It is hard to give a clear-cut answer, but the Bank will be dealing with the situation strictly, adhering to its stance of telling borrowers what they need to be told, and having them do what needs to be done. We take seriously the fact that the problem loan issue and the development of guidelines for out-of-court reorganization have been included in the emergency economic measures. At the same time, we would like borrowers to be fully aware of the situation.

Q. Concerning the guidelines for out-of-court reorganization, what do you think about the time period for rebuilding? For example, I am doubtful that a 10-year restructuring plan is feasible.

A. The environment now is quite different than when the economy was always booming. The situation also depends on the industry and a company's position within its industry. Some think that we should set a certain limit on the number of years, but we have to think carefully about the current state of the economy and the industry. The time frame of the restructuring is one of the items that must be considered when conducting an out-of-court reorganization, but we think some flexibility is needed.

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Q. How much are the current unrealized gains and losses on securities for the new Bank?

A. Based on yesterday's Nikkei average, our net unrealized gains on listed stocks were approximately 500 billion yen. On April 1, the merger date, The Nikkei average was slightly under 13,000 yen, and the net unrealized gains were about 200 billion yen.

Q. Your outstanding balance of JGBs evidently increased. What do you think of the market risk associated with it?

A. The major reason for this increase can be attributed to the introduction of RTGS, which started at the beginning of this year. We decided to hold a certain amount of JGBs, mainly short-term bills with low price volatility, to use as the collateral for our overdraft line. Since these JGBs largely consist of short-term bills, the risk level measured by the Value-at-Risk method did not increase so much. We execute our ALM operation, watching these movements in the risk level.

Q. What is the outstanding balance of your stock portfolio? What is this fiscal year's target for unwinding cross-holding shares? How does the outstanding balance compare to your capital?

A. The new Bank has approximately 6 trillion yen of cross-holding shares. There is about 700 billion yen of associated companies' stocks in addition to that, so the total stock portfolio is about 6.7 trillion yen. Our current capital is 3.8 trillion yen, so our cross-holding shares is over 150% of the level of capital. We have an internal target for the unwinding of cross-holding shares, but we have decided not to disclose it. Basically, we would like to reduce our stock portfolio to the level of our capital. Regarding the time

span of this plan, we recognize that some people say three years would be too long. We will proceed with its execution, watching the market and gaining customer approval.

<Other>

Q. What is the amount of merger surplus?

A. Approximately 1,760 billion yen. The amount of Capital Stock succeeded from Sakura Bank was determined by the merger ratio of 1 to 0.6. The rest of Sakura's Stockholders' Equity was the merger surplus, which can be calculated by subtracting 523.9 billion of succeeded Capital Stock from the 2,281.2 billion yen of Sakura's total Stockholders' Equity. This is the amount of the so-called merger surplus. But according to our merger contract, Sakura's Earned Surplus Reserve, Land Revaluation Excess and Retained Earnings were to be succeeded at their current amount, so the actual capital that we could use as the merger surplus was the amount of Capital Surplus only.

Q. How do you evaluate the fact that Sakura's unrealized losses were wiped-off as a result of using the merger surplus?

A. On one hand, it is true that our capital decreased by 427 billion yen. But on the other side, gross unrealized loss of "Other Securities" and reevaluated land, and unrecognized obligation on the employee retirement plan were all disposed. Considering the high volatility of the current stock market, I believe this will lead to improvement in our financial strength.

Q. What is the Advisory Board? How does it serve an oversight function?

A. The Board of Directors oversees the running of operations in the Bank. The Advisory Board has more freedom; it is a body within the Bank where knowledgeable people from outside the Bank can express their opinions to the top management. We would like advice from a broader point of view—outside opinions about issues facing our Bank, our Bank's strategy, and other matters.