Major Questions and Answers about The Financial Results of Fiscal 2002

Sumitomo Mitsui Financial Group, Inc. (SMFG) became the holding company of Sumitomo Mitsui Banking Corporation (SMBC) through a share transfer in December 2002. Figures for both SMFG and SMBC are stated in "Financial Results: Fiscal Year 2002 Supplementary Information".

For the sake of continuity, we have provided SMBC's non-consolidated figures including those for the former SMBC before the merger with Wakashio Bank.

1. SMBC's Earnings Results for FY2002

Q. What are the reasons for the year-over-year decrease in banking profit?

A. Banking profit was JPY 1,113.6 billion, which marks the achievement of more than JPY 1 trillion in banking profit for two consecutive fiscal years. Although it was a JPY 72.8 billion decrease on a year-over-year basis, the decrease was mainly due to the drop of JPY 220.0 billion in dividend income from overseas affiliates accounted in FY 2001. Gross banking profit decreased only by JPY 104.2 billion compared to the previous year, even with the large drop in the dividend income, because of the following factors:

First, non-interest profits contributed well in fields, such as sales of derivatives and loan syndications in the marketing units.

Second, the asset liability management (ALM) operations in the Treasury Unit worked effectively by utilizing the decline of interest rates in the Japanese, and other overseas markets.

Third, expenses fell by JPY 31.4 billion on a year-over-year basis to JPY 647.0 billion, in spite of the increase in expenses mainly due to IT systems integration after the merger between Sakura Bank and Sumitomo Bank, completed in the last fiscal year.

Q. What is the progress in improving the loan spread?

A. Regarding the improvement of the loan spread, the important part of the reexamination of domestic lending practices, the loan spread at the end of FY2002 has improved by 0.24% compared with the spread at previous fiscal year end for JPY 20 trillion in loans in the Middle Market Banking Unit which is in charge of banking business for small- and medium-sized enterprises. Specifically, the loan spread has improved by 0.40% compared with the one at the previous fiscal year end for JPY 11 trillion in loans to the targeted customers for the initiative during FY2002.

Q. Is your corporate restructuring progressing steadily?

A. In addition to on-going initiatives, such as, workforce streamlining and reduction in the number of domestic branches, we worked toward further efficiency in FY2002. As a result, the total expenses were JPY 647.0 billion, a JPY 31.4 billion reduction compared to the previous fiscal year and a JPY 161.6 billion reduction compared to FY1997, when expenses were the largest on record. As a result, the overhead ratio in FY2002 ended at 36.7%.

With respect to a further reduction in the number of domestic branches, upon the successful completion of the integration of domestic accounting systems, we integrated domestic branches substantially from 564 at the end of FY2001 to 403 branches at the end of FY2002 (including two combined branches), excluding branches of the former Wakashio Bank, and almost achieved our aim of a domestic 400-branches network. With respect to workforce streamlining, we are progressing in line with our original plan and the number of employees at the end of March 2003 was 23,401 excluding employees of the former Wakashio Bank.

2. SMBC's Asset Quality

Q. Please give an overview of the total credit cost for FY2002.

A. Total credit cost was JPY 1,074.5 billion, with no significant difference from that in the Revision of Forecasts for Consolidated Earnings and Dividends for FY2002, announced on April 4, 2003.

The breakdown of the credit cost is as follows: 1) approximately JPY 470.0 billion for the increase in credit cost from progress in restructuring the borrowers' businesses and in raising the reserve ratio for Borrowers Requiring Caution through the application of DCF method and others, 2) approximately JPY 300.0 billion for the credit cost related to a deterioration in the financial conditions of Borrowers Requiring Caution including Substandard Borrowers, and 3) approximately JPY 300.0 billion of the credit cost related to off-balancing.

Q. What is the reserve ratio for Substandard Borrowers after the application of DCF method? What is the reserve ratio for Borrowers Requiring Caution?

A. The reserve ratio of unsecured claims to all Substandard Borrowers was 33.7%, which increased by 11.9 percentage points compared to the last fiscal year end. The reserve ratio of unsecured claims to borrowers on the application of DCF method was approximately 37%.

The reserve ratio of unsecured claims to Borrowers Requiring Caution excluding claims to Substandard Borrowers was 12.8%, which increased by 3.4 percentage points compared to the last fiscal year end. The increases in the reserve ratios were due to bolstering the provision for risks of potential credit cost.

Q. What are the reasons for the decrease in problem assets based on the Financial Reconstruction Law?

A. While the amount of Doubtful Assets decreased by JPY 852.8 billion from the previous fiscal year end as a result of the progress in work-outs by sale and others for off-balancing and upward grade migration in borrower categories due to business restructuring and reorganization, Substandard Loans increased by JPY 167.1 billion from the previous fiscal year end, reflecting the sluggish Japanese economy, and as a result of upward grade migration in borrower categories due to business restructuring and reorganization; Bankrupt and quasi-Bankrupt Assets increased by JPY 26.6 billion from the previous fiscal year end.

Accordingly, total problem assets based on the Financial Reconstruction Law was JPY 5,261.3 billion, a decreased of JPY 659 billion from the previous fiscal year end.

3. SMBC's Balance Sheet

Q. What is the situation for the balance of loans and deposits?

A. The balance of loans as of March 31, 2003 decreased by approximately JPY 3 trillion from March 31, 2002. Details are as follows. 1) The balance of overseas loans decreased by JPY 2 trillion from March 31, 2002, as a result of the reduction in assets with low profitability. 2) The balance of domestic loans decreased by JPY 1 trillion from March 31, 2002, as a result of weak loan demand by corporations, aggressive progress in collection against problem loans, while we have undertaken initiatives to increase loans focusing on small- and medium-sized corporations, and, individuals, including housing loans.

The balance of deposits as of March 31, 2003 decreased by approximately JPY 3 trillion from March 31, 2002, as a result of the decrease in the balance of overseas deposits by JPY 4.3 trillion from March 31, 2002 due to a decrease in funding in overseas markets, although the balance of domestic individual and corporate client deposits increased from March 31, 2002.

Q. Are sales of cross-shareholdings progressing? What's your strategy for this fiscal year and hereafter?

A. We have reduced the amount of stock holdings by approximately JPY 1.1 trillion on a book value basis through sales to the Bank of Japan and others in FY2002. Moreover, we have substantially reduced the negative impact from the further sales of stock holdings against our profit by wiping out approximately JPY 700 billion of net unrealized loss on securities, utilizing the merger surplus through SMBC's merger with Wakashio Bank, and by exercising the impairment of approximately JPY 500 billion. Through the above actions, the amount of stock holdings at the fiscal year end, which needs to be reduced in accordance with the government guideline before the end of FY2004, has already been roughly equivalent to SMFG's consolidated Tier 1 capital.

We will reduce the book value of stock holdings further to the appropriate level for our capability to absorb risks, while avoiding any negative impact on the stock markets.

Q. Is there a large amount of cross-shareholdings between SMBC and life insurance companies?

A. Our decision regarding investments in foundation funds of life insurance companies has been made by the same criteria as for investments in other companies, based on economic rationality, and our investment in foundation funds of life insurance companies are not based on the intention of cross-shareholdings with them at all. Total amount of our investment to foundation funds of life insurance companies as of March 31, 2003 is JPY 168.7 billion.

Q. What is the amount of deferred tax assets? Isn't your estimate of the availability of deferred tax assets too optimistic?

A. While we have strictly estimated the availability of deferred tax assets up to now, for FY2002 we recognized the deferred tax assets based on a more conservative accounting standard, in accordance with the Program for Financial Revival announced by the Financial Service Agency in October 2002 and the policy guideline issued by the Japanese Institute of Certified Public Accountants.

As a result, we have written off the amount of deferred tax assets by JPY 454.7 billion to JPY 1,814.6 billion in SMBC on a non-consolidated basis as of March 31, 2003.

4. SMBC's Earnings Forecasts for FY2003

Q. What is your forecast for the banking profit for FY2003? Why is it forecast to be a decrease compared to the last fiscal year?

A. We forecast the banking profit for FY2003 to be JPY 1 trillion. We plan to further enhance the profitability of the marketing units in order to minimize the year-over-year decrease of gross banking profit up to around JPY 160 billion, mainly due to the conservative forecast for ALM operation profits in Treasury Unit, which have been contributing to the overall profit for FY2001 and FY2002.

In terms of expenses, we will realize the annual JPY 600 billion expense structure in FY2003, one year earlier than our original projection in the additional restructuring plan announced in July 2002, and reduce the annual expense by JPY 47 billion compared to last fiscal year. Consequently, the decrease of the banking profit for FY2003 will be limited to JPY 113.6 billion compared to FY2002.

Q. Please explain your management strategy for enhancement of profitability and expense reduction during FY2003.

A. We will continue our initiatives for optimizing the risk-return profile of our loan portfolio by increasing loan spreads; expanding credit-risk-taking in small- and middle-size enterprises, and loan syndications in corporate banking. In consumer banking, we will develop new business models, such as, consulting services, reinforce our competitive edges in the fields, such as, sales of investment trusts and investment pension funds, housing loans, and focus our management resources also in the field of consumer finance. Moreover, on the cost side, we will further extend our efforts for low cost operations through the integration of the systems development function within the group and through other additional initiatives aimed at more efficient office and operation management.

Q. What is your forecast for total credit cost for FY2003?

A. The total credit cost for FY2003 is forecast to be approximately JPY 650 billion. We forecast the cost related to off-balancing conservatively to be approximately JPY 250 billion. Regarding the credit cost related to a deterioration in the financial conditions of borrowers and to other factors, though we estimate it to substantially decrease due to our progress made in FY2002 and before, it is forecast to be approximately JPY 400 billion including the preparation for the provision for revitalization of Substandard Borrowers and effects of the unforeseen macro economic environment with continuous deflation. Anyway, while the total credit cost for FY2003 will decrease substantially compared to FY2002 due to the progress made in FY2001 and FY2002 in write-offs for large borrowers and the enhancement of the level of reserves, we will retain enough provision in order to ensure the achievement of our goal in reducing the problem asset ratio by half by the end of FY2004.

Q. What will be the amount of problem assets forecasted when SMBC achieves a reduction of the problem asset ratio by half.

A. We plan to reduce the amount of problem assets based on the Financial Reconstruction Law by approximately JPY 2.8 trillion within two years hereafter, to JPY 2.5 trillion at the end of FY2004. Accordingly, we estimate the problem asset ratio to be reduced by half to approximately 4% from 8.9% at the end of March, 2002. In detail, we will continue off-balancing through measures, such as, sale of Doubtful Assets and Bankrupt and Quasi-Bankrupt Assets. For Substandard Loans, we will accelerate our initiatives for revitalization and work-outs, including outright sales, by clarifying our policies to problem borrowers with the Asset Restructuring Unit, established in the last fiscal year, which will play a core role.

5. SMFG's Financials

Q. Please explain the breakdown of stockholders' equity at the end of FY2002.

A. Through events such as a merger and capital raising after the establishment in December last year, the term-end balance of items in stockholders' equity are as follows: JPY 1,247.7 billion for common stock, JPY 1,747.3 billion for capital surplus, JPY 161.5 billion for retained earnings, and JPY 3,156.1 billion for total stockholders' equity. Please see P. 19 of "Financial Results: Fiscal Year 2002 Supplementary Information" for details.

Q. Please give an overview of the earnings forecast for FY2003.

A. For SMFG on a consolidated basis for FY2003, the ordinary profit is forecasted to be JPY 320 billion, and net income to be JPY 150 billion. For SMFG on a non-consolidated basis for FY2003, operating income is forecasted to be JPY 55 billion, ordinary profit to be JPY 50 billion, and net income to be JPY 50 billion. Please see P. 22 of "Financial Results: Fiscal Year 2002 Supplementary Information" for details.