MUFG Investors Day 2019

Main Q&A

Retail & Commercial Banking Business Group (R&C)

Q : What is the key to ensuring the strengthening of the earning base?

A : One of the main reasons for the decline in the R&C's gross profits was a slowdown in investment products sales. It is, however, difficult to increase these sales substantially in the recent market environment and while we are in the process of aligning the sales structure with fiduciary duty.

In the wealth management business, we promote the profiling of each client's total assets that include not only financial assets but also real estate and shares in their own businesses. Of these, financial assets are primarily invested in bonds and thus do not contribute much to profits. On the other hand, considerable growth is seen in business succession and inheritance transactions that utilize clients' real estate and shares in their businesses. We will continue to work on cross transactions like these. In view of the size of the assets profiled, we believe there exists a considerable profit potential. Additionally, there are customer assets that are recognized as testamentary assets. We will strive to improve the wealth management business by not only harnessing asset management services but also pursuing all other available avenues.

Q : How would further deepening of negative interest rates affect the R&C?

A : It would affect loans and deposits differently. As lending spreads for newly executed corporate loans are on the rise, we do not assume that spreads would fall straight down as they did in the past. On the other hand, as deposit interest income would decrease, one of our challenges would be how to deal with domestic yen deposits. We consider it important to encourage customers to take a first step toward asset building by proposing fund-wrap and investment trust saving plans, for example. We implemented various measures, which have started to bear some fruit.

In addition, we believe there is room for reducing expenses, on which we are focusing our efforts. As the R&C was created by integrating two business segments—namely the retail and small-to-medium enterprise business segments—into one business group, operational overlaps still exist.

Q : How much expenses can you curtail by accelerating reductions in branches and workloads? And, what do the additional expense reduction measures under consideration entail specifically?

A : When drawing up the current medium-term business plan (MTBP), we planned to reduce the number of branches (around 500 at present) by 20%, which has now been revised up to 35%. While the number of conventional full-fledged branches has already been decided to be cut by half, we think there is room for further consideration as to whether the full-fledged branches that will remain should maintain the present branch model.

The rest of the full-fledged branches will be remodeled into branches specialized to features. We have already opened two light-weighted branches called "MUFG NEXT," and are considering the opening of a consulting office in the second half of fiscal 2019.

The effect of expense reduction was initially estimated to be about ¥36 billion over six years. However, the revision of the branch reduction ratio to 35% and other measures are expected to boost the effect to around ¥45 billion.

Furthermore, we are considering additional measures that are expected to deliver an approximately ¥10 billion reduction in expenses. These measures include reducing expenses through business process re-engineering as well as working to revise service fees.

Q : How much are the internet banking (Mitsubishi UFJ DIRECT) service and card shopping being used? And, how do you intend to increase the Mitsubishi UFJ DIRECT utilization rate and the volume of card shopping?

A : The utilization rate of the Mitsubishi UFJ DIRECT was 25% for fiscal 2018. In addition, we have been working to expand our digital channel, such as by releasing a smartphone app for various bank services. The sum of this app's usage and the aforementioned utilization rate indicates considerable progress in shifting to the digital channel. We will accelerate the channel shift by offering appealing services and providing an even better user interface and user experience.

With respect to card shopping, whereas transaction volumes have been steadily growing, our challenge is how to address the declining transaction fee rates. We are working to devise measures through ongoing discussion with the division responsible for digitalization.

Q : How are you prepared for nonfinancial firms' entry into the financial services industry?

A : We assume that nonfinancial firms' entry into the industry will reduce our opportunities to earn payment-related fees from individual customers. What we aspire to, however, is to be a platform provider for payment businesses. The fees to be earned from corporate customers participating in this platform may make up for the reduction in fees received from individual customers. In short, we anticipate that nonfinancial firms' entry into the industry may cause us to lose some but enable us to gain elsewhere.

Q : How are discussions on the integration of Mitsubishi UFJ NICOS (NICOS)'s systems developing?

A : NICOS running three separate systems for three credit card brands is an extremely inefficient practice. That is one of the reasons why its profitability is lower than that of the competitors. To address this challenge, we are working to integrate the company's systems.

Our discussions are based on two principles. One is to build a compact system, thereby increasing the likelihood of the success of system integration. The other is to simultaneously ensure stability that allows for safe and secure processing, and scalability that enables adapting to the changing environment, in light of the current situation where the greater use of cashless payments leads to exponential growth in the number of payment transactions. While meeting every single need is difficult, we believe satisfying these two principles is a must.

<u>Japanese Corporate & Investment Banking Business Group (JCIB)</u>

Q : At what pace will you reduce equity holdings going forward?

A : Whereas some companies still attach importance to cross-shareholdings and long-term relationships, we feel that, this year, the tide has turned and our corporate clients' ways of thinking have significantly changed. Japan's Corporate Governance Code was recently revised to ensure more rigorous and enhanced governance. This has helped advance dialogue between investors and corporations, and we have made our own efforts. As a result of these, we see a growing number of cases where clients, with whom negotiations previously reached an impasse, agree on selling or offer additional reductions.

Since fiscal 2015, we have sold equity holdings worth a cumulative total of around ¥600 billion. On top of this, agreement has been reached to date on the future sale of equity holdings worth an approximate total of ¥200 billion, which we call "the agreed amount." The sum of these comes to ¥800-plus billion, putting the goal of selling equity holdings worth ¥800 billion by the end of fiscal 2020 within reach. Although it is not that the entire agreed amount has been decided to be sold in the course of the current MTBP, we expect that we will be able to add a little more to the agreed amount as we are in the process of negotiating with various clients.

While the amount of equity holdings expected to be sold in each fiscal year cannot be disclosed as it depends on the capital policy of each client and the liquidity of equities, we will continue working to sell them in a timely manner.

Q : Will you accelerate the reduction of equity holdings in the future?

A : The risk weight for equities is set to be raised to 250% in stages. As a result, even if owning the equities of a client is economically rational at present, their risk-return profile will deteriorate in the future. Accordingly, the ongoing reduction of equity holdings is one of our Group's most fundamental policies.

Before anything else, we will advance negotiations with clients to achieve the goal of an ¥800 billion reduction ahead of schedule. We regard the reduction of equity holdings as a major challenge that must continue to be worked on going forward. Therefore, even if unable to sell in the course of the current MTBP, we will work to increase the agreed amount, at a faster pace if possible.

When executing the sale of equity holdings, care must be taken to ensure that the sale is in accord with the client's capital policy and will not cause the JCIB's profits and ROE to fall. By providing solutions that enhance the client's corporate governance system or facilitate its shareholder and investor relations activities, for instance, we will execute the sale without lowering the ROE. One of MUFG's strengths lies in the distinct securities and trust bank functions we have within the Group. We feel that we are in a phase where our comprehensive capabilities are tested.

Q : What are MUFG's strengths in, and outlook for profits from, transaction banking (TB)?

A : When compared with other Japanese banks, our strength lies in the extensiveness of networks, which is important to acquire deposits for settlement that are sticky and have low interest-rate sensitivity. In addition, we have intangible advantages such as strong regional networks made possible by our long history of operations.

On the other hand, it is challenging to compete against local banks due to their home ground advantage, which we will address by expanding and enhancing TB products. Besides, our global network is something local banks do not have and works in our favor. Given growing transactions between Asia and Europe, the United States, or Japan, the ability to provide value-added services together with those transactions is another advantage of ours.

The balance of non-JPY deposits has been increasing further since the beginning of fiscal 2019 while deposit margins have been widening compared to those in last year. In this environment, our profits are outperforming both the plan and the previous year's results. Although a decline in interest rates generally results in lower deposit interest income, we intend to minimize the impact of rate cuts by both increasing sticky deposits and changing deposit interest rates in tune with a decline in interest rate.

Q : How has the quality of the JCIB's asset changed? And, what is the outlook for credit costs?

A : Our credit quality is fairly sound at present. The stress tests we have conducted to assess various risks suggest that, within the scope of the currently anticipated risks, there is no likelihood of credit costs ballooning substantially. This is partly because large Japanese corporate clients become financially stronger and more risk-resistant. Nevertheless, as the credit cycle undoubtedly peaks now, we will proactively take necessary measures while remaining vigilant about signs of a cycle change.

The profitability of the JCIB's assets has considerably improved over the past year. In particular, non-JPY lending spread has improved owing to our stringent pricing management. JPY lending spread has also bottomed out. However, lending itself remains at a low level. If including profits from TB and solution business, profitability reaches an acceptable level; but we think it is still in the process of improvement.

<u>Global Corporate & Investment Banking Business Group (GCIB)</u>

Q : Could you explain the details of revisions to the impact on net operating profits estimated in the MTBP?

A : Page 23 of the presentation material shows the estimated impact on net operating profits over the remaining two years toward achieving the MTBP. The figures are smaller than the three-year impact presented last year because certain progress was made in fiscal 2018. We consider it vital to render the plan feasible by making revisions in light of progress in operating results and changes in the business environment. We therefore flexibly reallocated resources and targets, rather than sticking to the original plan, so as to make it more feasible to achieve the planned net operating profits and ROE for fiscal 2020.

The revisions made this time were aimed at increasing the feasibility of achieving the plan by reanalyzing the impact of our key initiatives, reclassifying those initiatives, and adjusting the targets to more realistic levels. With respect to "1: O&D on an integrated group-basis," we made steady progress in the areas of the primary O&D business, including business with investment grade corporates, and collaboration between the Bank and the Securities. On the other hand, the secondary business, including sales and trading (S&T) areas fell short of the plan. After reviewing the plan based on these results, we reached the conclusion that the potential shortfall against the plan could be made up for by the acquisition of two types of high-profitability assets—namely, the aviation finance business and the supply chain finance business—which resulted in the revision presented on the page. Another important factor is an interest rate trend. While the original plan was predicated on continuing a rate-hike phase, in reality we are now entering in the rate-cutting phase, which renders the planned net operating profits unattainable without changing the plan that assumed rate hikes. Therefore, based on the assumption that interest rates will either stay within a certain range or fall, we revised the plan concerning "3: Business platform to enable sustainable growth," which had mainly estimated the impact of obtaining non-JPY deposits, and allocated the shortage to other initiatives.

Q : Will you continue to reduce low-profitability assets?

A : For fiscal 2018, the GCIB posted year-on-year growth despite having disbursed necessary expenses. What greatly contributed to this was an improvement in portfolio returns, which was made possible primarily by reducing ¥800 billion of low-profitability assets. Consequently, the GCIB's return on risk-weighted assets (RORA) has improved dramatically over the past year.

If an asset does not exceed the RORA threshold set by the GCIB, it will be divested. When undertaking a new deal, exceeding the threshold is not the sole requirement; but also we screen deals rigorously to find those delivering high profitability or leading to ancillary businesses.

Q : What are your views on credit risk changes?

A : With regard to the United States, consumer spending is solid but cannot be viewed optimistically. We take a more cautious stance than last year. The upcoming presidential primaries will begin in February 2020. As US presidential election years tend to be years with less dramatic economic movement, a key point is what will happen during the period up to February 2020. Thereafter, how President Trump will run his campaign will be another key point.

Whereas corporate debt is on the rise, household borrowing is low. Jobs numbers fluctuate to some extent, but not significantly. While scarcely reported in the media, immigrants from Asia are increasing and their spending is solid. Various indicators suggest the US economy is stable, and we anticipate there will be no major crash.

Q : What are your thoughts on other regions?

A : We sense that in the past year or two, the Unites States, and China and the rest of Asia, started to become somewhat independent of each other. This does not mean, however, that the global economy would not be affected by a US recession. The important point to watch is the degree of localization—that is, the characteristics of each regional economy and its past and present susceptibility to US economic fluctuations. Taking into account the perspective of shifting from offshore to onshore, the GCIB manages operations and considers where to allocate its resources.

This is exactly the area in which MUFG can demonstrate its strength as a group having three onshore operations—in the United States, Asia, and Japan. In Asia, where more European companies are about to enter, we have Bank of Ayudhya (Krungsri) and Bank Danamon, thereby holding local currencies and networks. There are also companies that raise funds in Japan by means of samurai loans and bonds. We believe it is the GCIB's mission to operate business globally and to support and earn the trust of clients while striking a balance among our three onshore operations.

Q : Why is DVB Bank's average lending margin of new aviation finance approximately twice as high as the GCIB's average lending margin? Wouldn't that become a risk factor in a recession phase?

A : DVB Bank's aviation finance business is unique in that it covers both newly built aircraft and used aircraft traded in the secondary market. There are two reasons for the bank to be able to take this approach. Firstly, it has experts specializing in assessing the residual, or resale, value of aircraft, and also provides advice on aircraft repossession. The ability to assess aircraft's residual value means being able to understand what price is competitive, resulting in the bank's higher lending margin. Thanks to personnel with high expertise, there have rarely been irrecoverable loans in the aviation finance business. In addition, we now consider incorporating the collateral value of aircraft's residual value into the internal rating system, which is expected to lead to reducing risk-weighted assets and improving profitability. The second reason is the stability of collateral value. Aircraft manufacturers are limited to two major companies if excluding ones making small aircraft. As the number of new aircraft manufactured per annum has not been increasing much over the years, the market value of aircraft rarely falls. In fact, aircraft prices were stable even on Black Monday and during the 1997 Asian financial crisis and the 2008 global financial crisis. As these suggest, aircraft are recession-resistant assets, which is the reason that we decided to acquire the aviation finance business.

Global Commercial Banking Business Group (GCB)

Q : What are your views on risks associated with overseas business expansion? Also, how do you manage those risks?

A : We clearly identify near-term risks associated with overseas businesses while operating the banking business. Although some observers point out the risks involved in doing business in the ASEAN region, we feel that ASEAN nations have learned lessons from the Asian financial crisis and the global financial crisis, and taken necessary measures. MUFG Bank's branches in ASEAN nations are also prepared for risks, such as by shifting from USD-denominated businesses to ones denominated in local currencies. Our partner banks, which spread over four countries, form a highly diversified portfolio, with Krungsri and Bank Danamon focusing on consumers. Also, each of the four partner banks is managing their operations very conservatively. As no bank in the world can completely avoid risk, what matters is to minimize risk better than the competition. In that respect, Krungsri improved the non-performing loan ratio while the competitors' ratio deteriorated. Bank Danamon, too, has maintained a lower non-performing loan ratio than the competition.

With regard to how to address risks, we think our four partner banks in ASEAN have managed to control risks nimbly. When they see a risk materializing, they either release the gas pedal and apply the brakes, or increase loan prices when pressing the gas pedal. Our partner banks excel at, and have actually succeeded in, managing risks by flexibly switching from the gas pedal to the brakes, reviewing prices, and so forth. The global economy has cycles, which makes it difficult to win in an absolute sense. What is important therefore is to win in a relative sense. We believe MUFG is equipped to win in a relative sense.

Q : Could you explain the direction PurePoint Financial in the United States is heading? Also, how is the shift to the mobile channel progressing?

A : PurePoint's funding cost is high. As funding should be increased in proportion to growth in high-profitability assets, we do not intend to increase it in an undisciplined manner. On the asset side, MUFG Union Bank is gradually expanding unsecured consumer loans.

While digital banks are gaining their market share in the United States, MUFG Union Bank is focusing on building its brand by changing its mobile user interface and taking other initiatives with the aim of obtaining deposits through marketing prowess.

Q : How has MUFG Americas Holdings Corporation (MUAH) been progressing versus the plan?

A : Frankly, MUAH's progress has been challenging. With funding interest rates rising, asset-side interest rates ought to rise correspondingly. However, as MUAH holds a high proportion of residential mortgage assets and a far lower proportion of unsecured consumer loans relative to other US regional banks, it faces difficulty in increasing the net interest margin. This progress is unsatisfactory to us, of which MUAH is well aware. Given that top-line growth is difficult to achieve, we think expenses must be curtailed. We will continue to collaborate closely with US-based directors and management to address issues in a hands-on manner.

Q : Could you elaborate on synergies with partner banks?

A : Allow me to explain them using page 33 of the presentation material. MUFG's conventional businesses were limited to (1) deposits and (2) loans, while Krungsri provided (4) auto loans. What neither of us provided was (3) dealer finance, the business we have entered. To make the entry successful, we brought together the expertise of MUFG Bank's staff and of Krungsri's personnel, such as those in charge of auto loans and risk management; sought referrals from Japan-based clients; and deepened our industry knowledge by interviewing dealers on automotive sales. As a result, the business has been growing at approximately 60%. Although we initially had little knowledge, we grew dealer finance by building ties with clients through loans and proposing auto loans. These efforts, in turn, have led to a virtuous cycle in which dealers come to need further loans to finance their inventories. In other words, we have succeeded in creating a positive cycle by mobilizing ties with clients and industry expertise in each of the upstream, midstream, and downstream stages of the supply chain. We attribute this success to the hybrid functions of MUFG, which has close ties with auto manufacturers, and Krungsri, which provides loans to consumers and small-to-medium enterprises. We intend to utilize this successful model of Krungsri at Bank Danamon in the future.

Clearer examples are credit rating upgrades and the resultant falls in funding costs. Additionally, in the digital field, MUFG has greater expertise in business process reengineering and will share the knowledge with partner banks. We also plan to have Krungsri provide its superior auto-loan management scheme for Bank Danamon.

Q : How do you expect Bank Danamon’s business model to change going forward? And, with regard to the risk of goodwill impairment for Bank Danamon, what solutions are you considering?

A : Joining hands with MUFG has enabled Bank Danamon to initiate large deals, something it would have been difficult to do on its own. As a result, corporate loans have been growing. We also intend to expand auto loans, harnessing support from Krungsri and relations with Japanese corporate clients.

In the dealer finance business, we have created an interesting framework, whereby instead of simply providing a loan to a dealer, we structure the loan together with other two parties—that is, an anchor company like an auto manufacturers as well as the dealer. By MUFG and Bank Danamon working hand in hand, we are now equipped to provide services that could not be provided by Bank Danamon alone. This framework has been acclaimed by major global auto manufacturers, which have given us mandates. That way, the framework has steadily borne fruit. We are also expanding into areas that are new to Bank Danamon, such as transactions with employees of Japanese corporate clients. Through these initiatives, we intend to replicate at Bank Danamon the positive cycle that has been created at Krungsri.

(The paragraph immediately below is an explanation that supplements the answer given at the Investors Day meeting)

With respect to the impairment risk referred to in the question, we consider that Bank Danamon has been posting solid operating results, to begin with, and thus raises no concerns about financial soundness. MUFG's policy is to help Bank Danamon enhance its intrinsic value by exerting synergies and implementing other measures, without overreacting to changes in the stock price. We will continue endeavoring to maintain Bank Danamon's stock price at an appropriate level by clearly communicating the growth strategies explained above to external stakeholders and conducting proactive investor relations activities.

<u>Asset Management & Investor Services Business Group (AM/IS)</u>

Q : What is your evaluation of the global acquisitions carried out in the investor services business areas?

A : We first acquired Butterfield Fulcrum, a firm strong in hedge fund administration, in 2013. Then, after several minor acquisitions, we purchased UBS Asset Management's fund administration business, thereby laying the foundation for global investor services business. Thereafter, by adding the capabilities of administering private equity funds and US mutual funds, we now have a full suite of fund administration services.

Fund administration providers are classified into non-captive firms and banking companies. Many non-captive firms originated as information technology companies, subsequently obtaining fund administration capabilities through acquisitions. In contrast, the advantage of MUFG as a banking company is that it provides services as an investor services specialist while making the most of its strengths as a banking company. The acquisitions to date have enabled us to skillfully provide comprehensive services, not only banking but also meticulously tailored services.

The expense ratio of our investor services business worldwide has improved to about 71%, which we aim to reduce further to mid-60% range by utilizing the expertise of the recently acquired fund administration company that has strong information technology capabilities.

As these developments illustrate, value added by our past acquisitions is manifest.

Q : How should we view an ROE level of 20%? How should we evaluate it compared to other companies?

A : The AM/IS's ROE has historically trended around 20%. Although it is difficult to make comparisons with other companies due to the absence of comparables with a business portfolio similar to ours, we will continue to manage our businesses with an eye to 20%.

As for the expense ratio, our understanding is that the market average is around 70% both for investor services companies and asset management specialist firms overseas. The expense ratio of the entire AM/IS stands at approximately 60% while our overseas operations posting higher numbers and the domestic investor services and asset management businesses lower. The crux of the matter, therefore, is how much we will be able to reduce the overseas operations' expense ratio by applying our know-how.

Q : Is there a possibility to integrate your domestic asset management entities in the future?

A : MUFG has three asset management entities in Japan: Mitsubishi UFJ Trust & Banking Corporation; Mitsubishi UFJ Kokusai Asset Management, an investment management firm; and MU Investments, an active investment management boutique. This composition is derived from our determination to develop products in close proximity to clients. When developing an investment trust product, it is crucial to do so in close proximity to its vendors. In the pension business, we provide consulting on schemes and investment products as a package, which makes an accurate understanding of clients essential to providing better products. The integration of these entities would, on the other hand, offer the benefit of reducing costs. Having examined the pros and cons of the integration, we have reached the conclusion that, at present, providing products under the current three-entity format is the most desirable framework to our clients. This, however, does not preclude the possibility of reviewing these entities in the future in the event that greater cost synergies are expected and more products become common.

Q : Regarding the global asset management business strategy, what scale are you aiming for and when?

A : Our ultimate goal is to be ranked within the global top 15. We are currently ranked 39th worldwide, which we expect will go up to 30th or so after the acquisition of Colonial First State Global Asset Management (CFSGAM). In order to be ranked within the top 15, we need to increase our assets under management by about $500 billion, on top of the CFSGAM acquisition. Toward that end, we will first concentrate on closing the CFSGAM acquisition. The following step will be to acquire small asset managers, which is needed for us to develop experience in the management of overseas asset managers and the process of integrating new teams into our entities. Then we will consider another acquisition, which will require us to discuss various issues, such as whether the common platform should be used despite employing a different brand. These issues may be discussed when we draw up the next MTBP, if possible. In conducting the asset management business, we have always kept in mind that growing the business inorganically is no easy task. The CFSGAM acquisition reminds us of the importance of carefully moving things forward step by step.

<u>Global Markets Business Group</u>

Q : With respect to non-JPY funding, what are your views on the proportion of medium- to long-term funding?

A : We cover around 60% of loans by customer deposits, and the remaining 40% by medium- to long-term market funding, which offers stability but at the same time is a costly measure. We are considering the reduction of reliance on medium- to long-term currency swaps over the next several years. We intend to endeavor obtaining further customer deposits while also diversifying our funding measures and sources through the use of cross-currency repos and other means.

Q : Unrealized gains on foreign bonds seem to be increasing. What is your policy on the utilization of those gains going forward?

A : As of the end of March 2019, unrealized gains on domestic bonds, foreign bonds, and equities totaled approximately ¥500 billion. Now that European and US long-term interest rates are lower than at the end of March, we have even greater unrealized gains at present. In fiscal 2018, the share of gains on sales in treasury revenue was limited to about 20%. In fiscal 2019, we intend to increase this share taking into account the current level of unrealized gains. Furthermore, with a view to achieving the fiscal 2020 plan that assumes sharp profit growth, we will formulate our policy considering a balance between gains on sales and interest income. Given that recognizing gains on sales has an aspect of front-loading interest income, we will continue to fine-tune our treasury position while monitoring the latest financial condition and market environment.

Q : Do you leave the fiscal 2020 profit plan for treasury operations unrevised despite a significant change in the interest rate environment?

A : Although interest rate trends deviate from the scenario we envisioned at the time of drawing up the MTBP, we have managed to secure the level of unrealized gains that is close to that anticipated in our original plan. This has been made possible by harnessing our market expertise to foresee market changes and by nimbly fine-tuning our treasury position to adjust to those changes. In the case of treasury operations, however, it is vital to have the perspective of conducting stable financial management over the medium term. We will thus review the planned profits for fiscal 2020, considering various factors such as a balance between interest income and gains on sales, and levels of unrealized gains. Meanwhile, as the business environment is more challenging for sales and trading business than for treasury, we will review the cost structure but measures to make up for profits may also be needed. To reduce not only variable expenses but also core expenses, we will carry out our Global Markets 3.0 initiatives.

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