FY2018 Interim Results Presentation

Main Q&A

Q : Please share the future outlook for profit from the Global Markets Business Group.

A : Thus far, the Global Markets Business Group has recorded considerable profit by successfully seizing opportunities arising from downturns in interest rates. Although this success contributed to MUFG's efforts to strengthen its capital base, it is not possible and even dangerous to expect such level of profits from treasury operations as we posted in the past, given the current market environment.

Looking ahead, higher market volatility is expected, so we believe that taking excessive risk is not a right decision. Accordingly, we will manage our treasury operations by taking into account market movements and a broad range of market trends. More specifically, we will not only pay attention to interest rates but also give comprehensive consideration to overall investment portfolios including equities and credits, taking into account the correlation between these investments. We will also utilize hedging. In these ways, we aim to switch to a more stable approach.

We anticipate that the next time interest rates fall our treasury operations will encounter another opportunity to reclaim their profitability. Although individual views vary about exactly when this opportunity will arise, we will abstain from taking excessive risk, instead reshuffling and optimizing our current portfolios in preparation for future opportunities. Once we see interest rates fall, we will do our best to secure higher profit than what is currently possible.

At the same time, we are experiencing a year-on-year decrease in net operating profit from customer segment operations. Strengthening these operations is another major theme the Global Markets Business Group must address. Although we grappled with a harsh market environment during the interim period of fiscal 2018, we are determined to transform this business group, allowing it to yield greater profit from services targeting institutional investors. To this end, we will take a unique approach that MUFG alone is capable of pursuing.

Q : Could you explain MUFG's stance on non-JPY funding? Specifically, we would like you to elaborate on this from a perspective of securing quality, profitability and sufficient amounts.

A : As stated on page 14 of the presentation material, we think that the composition of non-JPY loans and funding portfolios is relatively stable. With regard to currency swaps, we are aware that there are diverse opinions on them. However, given the considerable yen-denominated surplus in the domestic market, we believe that we should not give up utilizing this currency altogether. Rather, we think that we should, to a certain degree, utilize this surplus while maintaining an appropriate framework for liquidity risk management. In addition, we will ensure stable funding via the use of medium- to long-term currency swaps and avoid an excessive increase in their volume.

As for non-JPY funding, customer deposits play a key role. While there is a sense of crisis due to a decrease in the balance of these deposits, one of the factors driving this decrease includes a growing trend toward investment products, rather than deposits, due to an improvement in investment yields. The tight demand-supply balance of the U.S. dollar in markets around the globe also contributed to the decrease in the deposit balance. These factors not only affected MUFG but also caused problems for U.S. financial institutions. In response, we will capture “sticky” customer deposits by utilizing MUFG Union Bank. We will also secure deposits from customers of our transaction banking (TB) services. Although we believe our TB has to be made even stronger, it has already begun attracting non-Japanese customers, such as those based in the United States, in addition to Japanese customers. This is thanks to MUFG’s technological advances. Furthermore, we have secured a certain volume of non-JPY deposits from customers in the investor services (IS) field. We may consider utilizing these deposits. In line with the current medium-term business plan (MTBP), we place particular focus on increasing transactions with financial institutions along with expanding corporate transactions. These efforts, in turn, help us secure greater liquidity.

Q : What lessons did you learn from the plunge in MUFG’s stock price following the previous financial results announcement in May? Also, please share your thoughts behind the most recent shareholder returns announcement and other messages to investors.

A : Admittedly, our stock price has been stagnant since the financial results announcement in May. Looking back, I would name three takeaways.

First, the way I explained at the financial results presentation meeting in May was not good enough. Although we subsequently provided supplementary information delineating the timeline for our dividend payout ratio, our explanation was not sufficient in some respects.

Second, the announcement in May was also intended to share our sense of urgency with stakeholders. With an eye to our long-term goals over the next six years, we consider the first two years a particularly crucial period in terms of the success of structural reforms. This was the message we aimed to convey via the announcement. An unprecedented approach is absolutely required to assure success in these two years and this must be understood by all stakeholders. Therefore, we sought to secure investor understanding that our management approach is driven by a sense of urgency, in addition to ensuring that each employee shares management’s views on where MUFG is now and where it needs to be.

Third, although we have upwardly revised our fiscal 2018 profit target, this has something to do with the way we incorporate an estimation of credit costs into initial target, which is somewhat daunting task. Previously, we took an approach to incorporate credit costs only after internal credit assessments are finalized. Going forward, we will carefully examine whether or not to change this approach.

Now, I would like to share my thoughts behind the most recent shareholder returns announcement. First and foremost, we have frequently engaged with shareholders and investors, pursuing open dialogue, which often addressed in-depth matters. We gave due consideration to their voices before announcing the content on shareholder returns of this time. On the other hand and despite speculation to the contrary, we made no revision whatsoever to our basic policies for shareholder returns. We have been telling that we aim to steadily increase dividends and raise our dividend payout ratio to 40% within six years. Accordingly, the increase in dividends per share would not be surprising. As for the share repurchases of up to ¥100.0 billion, this was resolved by taking into account greater-than-expected performance, leading to upward revisions in our full-year profit target, as well as deliberation on the conformity with our three criteria for share repurchases as stated on page 53 of the presentation material. Furthermore, the Board of Directors carefully discussed this matter, reaching the conclusion that this is in line with our basic policies for shareholder returns.

In summary, although we regularly engage with shareholders and investors and take heed of their feedback, we have not changed our basic policies for shareholder returns.

Q : How do you evaluate progress in the MTBP? Please provide us with your observation from a short-term and medium- to long-term perspective. Also, do you think that the ideal corporate culture and the behavior are as fully embraced by employees as you expected?

A : Overall, we believe that we made a good start in the MTBP. Although we had concerns about certain factors, after having finished the interim period, we found some of these factors were not as serious as anticipated. For example, the integration of the corporate lending businesses of the Bank and the Trust Bank began yielding positive outcomes in many ways. Despite the potential for issues associated with this integration, our organization is now able to function in exactly the way we had envisioned. This integration has also positively affected our numerical performance. Our initiatives related to the IS business have yielded positive results, too. Although their contribution to consolidated performance has yet to be significant, these businesses achieved a 20% year-on-year increase in net operating profits. This is working pretty well in light of our overarching objective of shifting from our conventional business model, which was dependent on interest income, to a new business model based on recurring revenues from fees and commissions. With regard to the asset management (AM) business, we drastically shifted our focus to the acquisition of majority equity stakes. Although the recent strategic acquisition is the initial step, we consider it a significant one. We also made progress in the pursuit of digital technology, the streamlining of branch operations and the restructuring of branch properties owned by MUFG.

On the other hand, we are facing three issues in the course of the implementation of the MTBP.

First, we aim to achieve a successful shift of our wealth management (WM) business model. We must break away from the conventional business model, which is dependent on fees and commissions related to sales activities of investment products, and establish a new business model centered on asset management and advisory services. This requires the development of infrastructure and systems as well as employee education. These will not be that easy. Although we aim to raise net operating profits from the WM business by ¥50.0 billion in six years, we must exert considerable efforts to this end.

Second, the Global Corporate & Investment Banking (GCIB) Business Group has encountered temporary stagnation. Unless it makes successful adjustments going forward, this business group will not reach its targets under the MTBP. Although progress had been made in such measures as the formulation of finance policies and the integration of primary businesses under the Bank and the Securities business, these also require considerable efforts.

Lastly, we face a challenge in the institutional investors business. Although our performance in the IS field is favorable, we have met some difficulties in sales & trading (S&T) operations. Currently, we are advancing the development of the organizational structure by, for example, assigning some individuals dual-hatted positions that concurrently serve the Bank and the Securities business, as well as by appointing Global Heads of business lines.

Looking at the mindset embraced by 150,000 employees across the MUFG Group, it is clear that they are increasingly sharing management's sense of urgency. I am rather worried, however, that I might not be eloquent enough in communicating our ambitions and the future goals Group members must envision. We are pursuing the Re-Imagining Strategy, whose title represents our intention to transform ourselves. I will therefore redouble efforts to effectively convey my thoughts on our future outlook and goals to all employees.

Q : In addition to current U.S.-China trade tension, there are a number of factors giving rise to a growing sense of uncertainty in Europe and emerging countries. Please provide your insights on future global situations, the timing of potential credit cycle changes, and the possible impacts of these factors on MUFG's operations.

A : Absolutely, there are a growing number of factors causing a sense of uncertainty. For example, trade policies executed by the Trump administration may result in a backlash against the U.S. economy, leading not only to an economic downturn in the United States but also to spillover effects that would, in turn, harm the global economy as a whole. We also have some concerns over U.S. financial policies and believe that we must prepare for interest rate hikes. In particular, a change in credit cycles can be triggered by a rise in U.S. interest rates. Although the timing of this change cannot be readily predicted, we think we may possibly confront this issue in the second half of the current MTBP. It may begin to occur that certain factors that went unnoticed by anyone were, in hindsight, actually signs of critical changes, while the factors may seem to be irrelevant to economic downturn at this stage. Accordingly, we will keep watchful eyes on the possible emergence of such signs.

In line with the MTBP, we intend to expand the scope of our risk profile to cover non-investment grade loans. This may appear to be a contrarian move given the current trend. However, we gave due consideration to our medium- to long-term strategies spanning a period of three to six years, and have concluded that we should diversify our business portfolios. Paying close attention to credit cycles, we will prudently push forward with our initiatives along with the formulation of risk management frameworks and portfolio policies.

With regard to risks associated with emerging countries, both Bank of Ayudhya and Bank Danamon would be affected by the change in credit cycles. However, the development of risk management frameworks has been under way at these two partner banks with the full involvement of MUFG. When regional economies deteriorate, we will swiftly implement countermeasures by employing their expertise. Going forward, we aim to adjust MUFG's risk profile by applying a medium- to long-term perspective focused on the development of optimal management frameworks and the realization of positive effects of dispersed portfolios.

We are also aware of the potential for temporary downsides with our initiatives. However, in order for MUFG to secure future growth, we must take these possibilities into account and push ahead with the MTBP while striving to minimize risks.

In addition, Colonial First State Global Asset Management, which we have recently announced to acquire, is distinctively resilient as for the performance within unfavorable market condition.

Q : Since the beginning of fiscal 2018, it seems that MUFG is losing the balance of triangle representing capital policy, especially between shareholder returns and strategic investment. We believe MUFG should increase shareholder returns while taking a stricter stance to screening strategic investment. What's your opinion?

A : Going forward, we will face several factors that will negatively affect our Common Equity Tier 1 (CET1) Capital ratio. For example, we anticipate the termination of exceptional treatment with regard to MUFG's investment in Morgan Stanley in five years. This will reduce our CET1 capital ratio by approximately 0.9%. As we have repeatedly stated, we aim to maintain a single A rating and, to this end, we must constantly strive to strengthen our equity capital.

Meanwhile, the current Basel III regulations mandate that we have a large adjustment for transitional floor, but no floor adjustment under the regulations will be required on finalized Basel III reforms basis. As a result, we expect these reforms to temporarily help raise the CET1 capital ratio. Taking these factors into account, we believe that we have some leeway. We would like you to rest assured that MUFG's capital will remain robust despite some negative factors.

Moving on, I would like to discuss the acquisition of the AM firm. We have a business group in each of the four quadrants of a matrix based on "Japanese" or "non-Japanese" and "large corporations" or "retail and SMEs." In addition, we are strongly committed to strengthening AM/IS businesses. From a perspective of stabilizing our business portfolio, we aim not only to focus on the banking business but also to secure our presence in the active AM business where we foresee a market growth. Although it might take some time to achieve target ROI, our underlying approach to the AM business is focused on creating a major business pillar over the long term. Of course, this does not mean that we will limitlessly seek for expansion. Rather, we will promote it with carefully screening each opportunity.

Q : We suspect that MUFG's expense ratio is going to deteriorate. Also, if the Company's initial investment plan has not been fully executed, neither structural reforms nor transformation initiatives would take full effect. What's your opinion on these risks?

A : The costs for digital technology and other expenses for structural reform initiatives being implemented during the last six months have not been significant. We have yet to undertake major investments for structural reforms. Going forward, you should expect that MUFG will make forward-looking investments.

On the other hand, efforts are now under way to reduce legacy assets via the recording of one-off costs. We began this initiative in fiscal 2017 with the impairment of domestic branches. In addition to the impairment losses, we also anticipate the recording of one-off losses for structural reforms in the second half of fiscal 2018 in connection with the optimization of strategic investments.

These are examples of structural reforms we have advanced thus far, but these initiatives have not yet been posted on profits and losses. Looking ahead, we are committed to updating our investors on the numerical effects of our initiatives every six months. We have a number of initiatives on track. We of course expect that we will see a positive impact before too long.

Q : Please tell us about progress in the reduction of risk-weighted assets (RWAs) and the recycling of the portfolio. Also, please provide us with updates on MUFG's initiatives to strengthen profitability and the current status of lending spreads.

A : We need to transform our Global CIB business, which has been a lending champion, into a provider of comprehensive financial services. To this end, we will continue to strengthen the origination & distribution while enhancing its product lineup further. At the same time, we will scrutinize and reduce its legacy assets. More specifically, we will set KPIs associated with the reduction of low-profitability assets and the review of customer composition, thereby assessing the progress of our initiatives in a periodic manner. With regard to overseas loans, we no longer see the growth we enjoyed previously and have now switched to a more restrictive lending approach. This approach has emerged as we began placing stronger emphasis on the efficient use of RWAs.

Meanwhile, how we launch the WM business is a matter of importance in domestic operations. We have consistently maintained robust transactions with large Japanese corporations, including those operating in overseas markets. Although differences in overseas yields between lending and deposit rates are increasing gradually, this increase is largely attributable to the effect of pricing revisions of loans to Japanese corporations in overseas markets.

In addition, we believe that the Global Commercial Banking (GCB) Business Group will grow steadily. If I were to name some issues it is confronting, I would say we must strive to change MUFG Union Bank’s business structure. In particular, enhancing profitability from its regional banking operations in the U.S. West Coast is essential. Recently, we have announced the acquisition of an M&A boutique. This move is intended to expand MUFG Union Bank’s SME finance services. In the consumer finance field, we consider launching an unsecured consumer loan business. Business restructuring via these measures is a major theme for the GCB Business Group and I believe it will provide us with growth opportunities. As such, we made some progress in our initiatives to raise top-line revenues in each segment.

Q : Could you tell us your future outlook on the impact of digital strategies being executed by banks in the financial industry? Also, please tell us your opinions about what changes MUFG has to make in terms of its positioning in the industry.

A : Previously, existing financial institutions have monopolized certain business areas, such as payment, preventing other types of firms from yielding profit from these operations. However, we think that going forward, these business areas will be eroded by new competitors making entries from different sectors. In Japan, our revenues from bank remittance and transfer fees might be partially captured by new players. Accordingly, we feel an urgent need for countermeasures. Part of our revenues from consumer lending may also be eroded by competitors.

On the other hand, we expect no significant change in corporate transactions. Although our operations will be more or less affected by the introduction of new database tools, such as those aimed at analyzing credit status and matching M&A deal candidates, we believe that our in-depth expertise in complicated transactions will remain a key component. There would be no major change in these operations, which are ultimately dependent on humans charged with making business decisions in the course of face-to-face dialogue with customers.

Neither do we think that our S&T operations will be eroded by the emergence of FinTech. Rather, we anticipate increasing convergence of technologies due to the widespread digitalization of interbank transactions. With this in mind, we will shape our model for digitalization and, to this end, place our focus on identifying MUFG's distinctive strengths that provide competitive advantage in the institutional investors business.

In addition, it is obvious that MUFG must collaborate with FinTech players. However, we will also be exposed to significant threats due to the emergence of BigTechs. Therefore, we must seek out mutually beneficial alliances while, as necessary, implementing measures to counter new threats. We are also considering creating innovative data-driven services that our competitors are not capable of providing. One such service is an "information trust platform," a recently announced initiative that leverages MUFG's unique strength. While a great number of business operators are in need of customer data, there is a call for strict measures to safeguard privacy information. Existing financial institutions, including MUFG, have earned the public trust and confidence requisite for this kind of business model, and are thus capable of meeting these two separate requirements. This model is also based on the application of our longstanding know-how with regard to the protection, management and utilization of customer assets. Currently, a number of similar initiatives are under way at business units across the Group. While ensuring that these initiatives are being executed in line with our overarching strategies, we will promote digitalization in a way that only MUFG is capable of doing.

Meanwhile, through collaboration with Akamai Technologies, Inc., we aim to create an unconventional platform business outside of the aforementioned initiatives. In Japan, interbank settlement has been executed via platforms run by the Japanese Bankers Association and the Bank of Japan. Overseas, the Society for Worldwide Interbank Financial Telecommunication (SWIFT) provides a similar platform. However, we intend to create a new platform. We will begin by handling credit card settlement and are expecting this platform to provide us with a great breadth of opportunities. We will utilize and expand MUFG's existing foundations in a way that fills the future needs of the general public as a whole. That's how MUFG will look in the future.

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