

Special Feature II.

New Medium-term Management Plan - “Best Brand Daiwa 2005”

We will step up our pursuit of “quality-driven” growth and strive to differentiate ourselves from our competitors by implementing a strategy focused on “quality” and “productivity.” This decision is based on the following three factors: (1) diversification of customer demand, (2) increased competition, and (3) the lessons we learned in reviewing our performance under the previous medium-term management plan.

We will step up development and improve deliverability of high value-added products and services, by strengthening the marketing structure in our retail securities business and promoting intra-group cooperation in our wholesale securities and asset management businesses.

In the wholesale securities business, we will enhance our presence in the corporate restructuring field, by taking advantage of both the vast opportunities offered by the current business conditions and the superiority of our position in this field.

We aim to win the unreserved trust of all our stakeholders, by making further improvements to our management system, centering on personnel management and corporate governance.

We will strive to raise capital efficiency and increase our ability to withstand turbulent economic conditions.

Our ultimate goal is to make ourselves indispensable to all of our stakeholders.



Our Assumptions for the Business Environment over the Next Three Years

Sluggish Economic Conditions and Deflation to Continue

In FY 2002, Japan's real GDP showed signs of a recovery after posting negative growth in FY 2001, thanks mainly to a quick expansion of exports in the first half of the fiscal year. However, due to delays in structural reform and deregulation, there were no signs of a recovery in domestic demand. In the meantime, the U.S. economy, which had absorbed the bulk of Japanese exports, suffered a slow-down, while in Europe, business confidence in Germany and other countries started to wane. Reflecting these conditions, Japan's industrial production year on year growth rate started to fall from the fourth quarter of FY 2002, while capital investments continued to be sluggish.

In our view, the current economic cycle can be characterized as follows: (1) the recovery was short-lived and peaked out at a low-level, and (2) there was only moderate pressure to adjust inventories. Consequently, we do not believe the current cycle will be subject to any serious economic adjustments. That said, however, we see no major driving force that could bring about an economic recovery. Accordingly, our view is that severe economic conditions accompanied by persist-

ent deflation are likely to continue for the time being.

The Challenging Environment Is Providing Us with New Business Opportunities

Given this difficult business environment, we believe that corporate reorganization and the reworking of balance sheets will accelerate. In addition, with no upsurge in domestic demand in the horizon, many companies have surplus capital as a result of their hesitancy to make any capital investments. These companies, in the meanwhile, are reducing their external debt and buying back shares, but further down the road we believe they will have a greater need to manage their surplus capital.

Due to uncertainty regarding employment and the pension scheme, rising medical expenses and the absence of confidence in future income growth, individuals' appetite for high risk financial products is unlikely to grow suddenly. Nevertheless, owing to the prolonged ultra-low interest rate environment, we are seeing a gradual shift of funds away from risk-free financial products to products with prospects for higher returns, especially among the elder generation.

Backbone of the New Medium-Term Management Plan

Lessons Learned from the Previous Medium-term Management Plan and Business Environment

We have created a new medium-term management plan titled "Best Brand Daiwa 2005" for the three year period from FY 2003 to FY 2005. In forging the future of the Daiwa Securities Group, we have incorporated the following three elements into our medium-term management plan: (1) the strengths and weaknesses of

the Daiwa Securities Group, that were revealed as a result of our reflections on the previous medium-term management plan; (2) our business environment assumptions for three years; and (3) the fundamental strategies and principles of the Daiwa Securities Group.

Becoming the Customers' First Choice

With competition intensifying, a business strategy that lacks a strong customer orientation is unlikely to meet with success.

In an era when customers have access to a wide range of information through the Internet and other media, it is obvious that it is the customer who chooses the company, not the company that chooses what to sell and to whom. This is why the Daiwa Securities Group's brand management, which has been based on improving customer satisfaction, is exactly what is needed in the current times. Moreover, as mentioned in our summary analysis of the previous medium-term management plan, we are aware that one reason why we were unable to record satisfactory results in our retail operations and in trading was because our organization was unable to provide customers with products and services that meet their needs.

Aiming to Be "Number One in Quality" and "Number One in Productivity" through Quality-driven Growth

The most important feature of our new medium-term management plan is "quality-driven growth." Specifically, our goal is to be "number one in quality" and "number one in productivity."

As we mentioned in Special Feature I, our marketing strategy did not pay enough

attention to the needs of our customers, which is why our previous medium-term management plan lacked success in some areas. In other words, we deviated from some of our pro-customer ideals and strategies that we should have adhered to, and instead merely tried to increase the immediate volume of business.

In the business world, making objective judgments about "quality" is ultimately in the hands of the customer. But no matter how good the quality might be, the notion itself becomes meaningless if customer needs are not dealt with precisely and rapidly. Given the tough business climate prevailing in Japan, it goes without saying that there are limits in the investment of management capital, including increasing headcount. The situation, therefore, calls for increased productivity, so that we can offer our clients high-quality products and services that meet their needs quickly and accurately. This is the reason why we are aiming to be number one in both quality and productivity.

The Daiwa Securities Group intends to push forward with these goals over the next three years. In our opinion, the results of our efforts will come to be reflected in our earnings.

Action Plan

Five Main Issues

Below we present an explanation of our action plan for achieving quality-driven growth. As part of this plan, we have identified five main issues that need to be addressed over the next three years.

The first is our retail securities business. Our main objective here is to overhaul its marketing structure and achieve quality-driven growth.

The second issue concerns strengthening the development and deliverability of value-added products and services in our wholesale and asset management operations. This goal cannot be achieved by

these two operations alone; all members of the Group must cooperate in developing the necessary products and services as well as in collecting customer feedback through marketing efforts and post-sales follow up.

The third issue involves increasing our presence in business opportunities related to corporate restructuring. Our previous medium-term management plan did help boost our presence in this area, but we aim to do better. One way we can achieve this is by further improving intra-group cooperation and by strengthening our collaborative business alliance with

Sumitomo Mitsui Banking Corporation.

The fourth issue is the enhancement of our human resource management system and the fifth is enhancing our corporate governance. These enhancements will enable us to secure the trust of all who have a stake in our company, most importantly, our shareholders, customers and employees, and bring us closer to our goal of being "number one in quality."

1. Strengthening Our Retail Securities Business

We plan to expand and reinforce the marketing system for our retail securities business. To accomplish this, we have formulated a five-point action plan.

(1) Marketing Based on the Satellite Branch System

The first part of this plan is the reconstruction of our marketing structure and improvement of the feedback mechanism, through the Satellite Branch System. The Satellite Branch System, which we briefly mentioned in Special Feature I, was introduced in July 2002 in the Tokyo metropolitan area and the Osaka region. This new system has been successful so far, enabling us to compile a useful database by identifying area-specific customer needs and characteristics. We believe that the success of the new marketing system should help to make Daiwa Securities an attractive choice among retail investors. In February 2003, as the second phase, the system was introduced in the Nagoya region. The know-how and knowledge that the Satellite Branch System places in our hands will be used extensively at our nationwide retail branch network. Furthermore, we are accelerating the delegation of authority to area managers. This will enable the area managers to provide products and services in response to the diverse and unique needs of customers in a timely fashion. At the same time, having the area managers submit semi-annual

reports will give management the means of reviewing the strategies and performance of each area.

(2) Introduction of Sales Specialist Position (in-house certification)

The second point is the introduction of the position of sales specialist. We plan to implement an in-house certification system. Under this system, employees will be given training to increase their knowledge in areas such as asset management and taxation. Marketing representatives who pass the exams will be assigned to branches as certified sales specialists to serve as consultants and further their involvement in the management and investment of our customers' assets. In this way, we can provide higher quality services and increase the level of customer satisfaction.

(3) Reforming Sales Channels

The third point is the reform of sales channels at Daiwa Securities. Up to now, Daiwa Securities has operated three sales channels: (1) over-the-counter sales (Daiwa Consulting), (2) a call center (Daiwa Call) and (3) the Internet (Daiwa Net). Each channel provided a different level of service and had a different fee structure. Of the three channels, we combined Daiwa Net and Daiwa Call into "Daiwa Direct" in May 2003 and moved to a two course structure. The main purpose of this reform was to provide a higher level of service. Before the reforms, customers were restricted in the products they could transact in according to channels. For instance, customers were unable to buy or sell certain investment trusts, overseas stocks, cumulative stock investments and bonds via Daiwa Net, and foreign currency-denominated bonds via Daiwa Call. Under the two course system, customers are free to enter into transaction in most products that we offer, regardless of the course. Furthermore, the range of services has

been expanded to meet the customers' needs.

In order to offer more information on our website, we have started to make prospectuses available there as well. Above all, we believe that we have made both courses more user friendly by streamlining our services. The only difference in service between the two courses is regarding consultation on investment.

(4) New Services That Reflect Customer Transaction Volumes

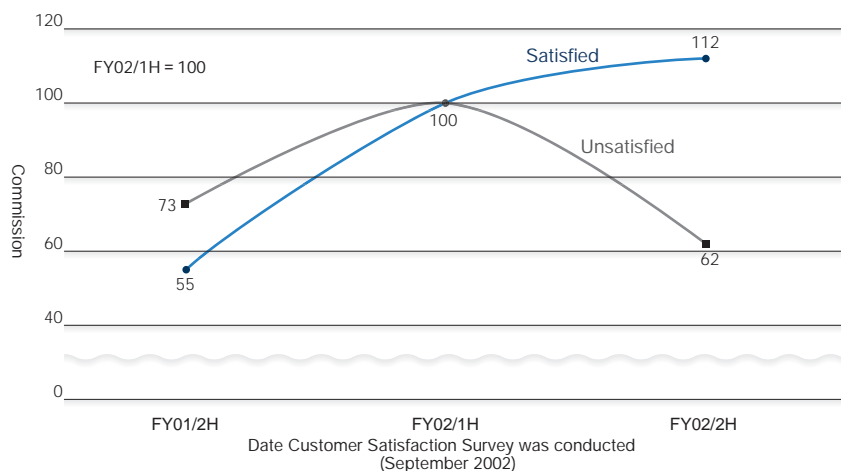
The fourth point is the introduction of the “Daiwa Comprehensive Account Service (Cash Management Program) Port One” in December 2002. Port One features the Daiwa Point Program, a mileage-like program. Under the Daiwa Point Program, customers accumulate points based on their assets under custody with Daiwa Securities and the value of commissions generated and bonds purchased. The point program provides “preferential service,” which includes a waiver of the account management fee, and an “exchange service” through which accumulated points can be exchanged for various merchandise.

Introducing the point program has enabled us to provide greater benefits to customers who appreciate the value of our products and services. In other words, customers will benefit from bringing their assets to Daiwa Securities and, by doing so, will be able to benefit from the higher quality of services that we are able to offer. This will all lead to higher customer satisfaction.

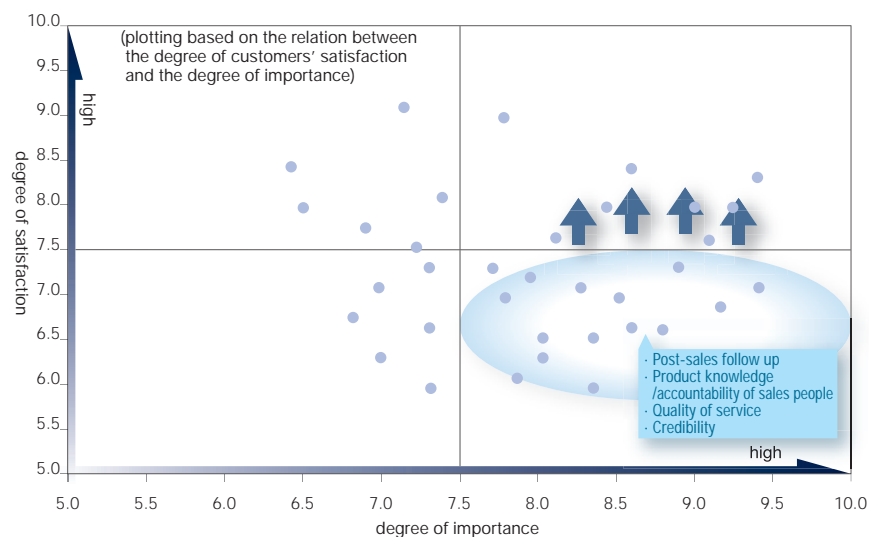
(5) Enhancing Post-sales Follow up

The fifth is enhancing post-sales follow up. As part of our branding activities started in FY 2000, the Daiwa Securities Group has twice conducted a customer satisfaction survey. Our analysis of the surveys reveals a correlation between customer satisfaction and the frequency

Trend in Commission Based on Level of Customer Satisfaction



Results of Our 2nd Branding Survey (Conducted in September 2002)



and volume of transactions (see above graph). We also discovered that we were not able to satisfy our customers in certain service fields, although the customers considered these as important. Post-sales follow up was one of them.

Based on these findings, we believe that we must not only strengthen our product development (i.e., the “entry” side) but also provide adequate post-sales services (the “exit” side); this will lead to better quality products and services through greater added value and differentiation from our competitors. The results of our surveys suggest that conducting surveys to understand what leads to customer satisfaction is extremely important. Henceforth, we are considering shorten-

ing the interval between surveys as well as instituting regular monitoring by including customer feedback forms in our account balance statements.

2. Enhancing the Development and Deliverability of Value-added Products and Services

A Challenging Environment

As we mentioned in Special Feature I, the net gain on trading securities in FY 2002 recovered to grow 48% year over year, but the level of gains was far short of our target. In the asset management business operated by Daiwa Asset Management Co. Ltd. (DAM) and Daiwa SB Investments Ltd. (Daiwa SB Investments), the business environment remains difficult. Particularly for DAM, management trust fee revenues from bond investment trusts declined as a result of the prolonged zero-interest rate environment while sales of Japanese equity related investment trust products dropped sharply. Moreover, as a result of the bankruptcy of Enron in the U.S., DAM experienced a 60% decline in the amount of bond investment trusts under management over the three-year period from the end of FY 1999 to the end of FY 2002.

Strengthening Our Product Development Capabilities

In our trading business operations, we believe it is necessary to expand businesses related to foreign currency-denominated bonds and structured bonds, the demand for which has been increasing recently. Therefore, we will continue to make investments in computer systems that handle our trading business. Over the next three years, we plan to reduce the Group's investment in IT by 23% over the actual amount of investment made during our previous medium-term management plan, but the investment level at Daiwa Securities SMBC will remain essentially

unchanged.

Also, in the asset management business, of the 200 funds managed by DAM and under review, we intend to reduce the number of funds to around 150 over the next three years, in keeping with our goal of improving our investment performance by using resources more efficiently.

Cooperation within the Group Is Essential to Making Improvements

It will be not enough just to strengthen our product development capabilities in the wholesale securities and asset management businesses. More so than our other operations, the sales departments are capable of quickly and accurately understanding customer needs and obtaining feedback from customers about our products. In short, therefore, it will be vital to secure cooperation from our sales division in order to improve our product development capabilities. We plan to strengthen our trading and asset management businesses by enhancing coordination among group companies, especially with Daiwa Securities and Daiwa Securities SMBC. One specific measure we already took in February 2003 was the creation of a financial product research team within Daiwa Securities' Product Planning Department.

3. Building a Stronger Presence in the Corporate Restructuring Field

Finding Ways to Take Advantage of Favorable Trends

As we explained in Special Feature I, our new business activities in the investment banking field showed strong growth over the three-year period covered by our previous medium-term management plan. We intend to continue to develop these businesses by steadily tapping into corporate needs for restructuring and revitalization, balance sheet reform and investment of capital. One of our focal points is

increasing our presence in the corporate restructuring area. Strengthening our relationship with Sumitomo Mitsui Banking Corporation lies at the core of this strategy.

M&A and principal finance, which are the central businesses involved in the revitalization of the Japanese economy, have shown strong growth over the last three years. We expect these businesses to continue to have excellent growth potential. Our target is to increase revenues from M&A related business by two fold and principal finance business by 60% in the next three years.

4. Enhancement of the Human Resource Management System

Reform of Compensation Practices

We will strengthen our human resource management system by focusing on (1) enhancement of performance-based evaluation system (2) providing diverse career options (3) implementing a fair evaluation system and (4) improving the quality of human resources. With regard to the reform of our employee compensation system, which we first announced in March 2003, we plan to take three specific steps: First, we will introduce a compensation system based on work classifications. Second, we will increase the number of steps in our monthly salary evaluation to 16 from the current 11. Third, we will introduce a “senior work system” and transfer our general career employees (sogoshoku) aged 55 and above to senior employment ranks. In addition, we plan a thorough review of regular increases in base salaries during FY 2005, a practice that we already abolished for management level employees.

Aiming for Broad and Fair Employee Appraisals

To transform our compensation system, we need to set up a more detailed job per-

formance evaluation system that our employees find convincing. A system that relies solely on supervisor evaluations is inadequate to measure employee performance accurately. It is essential to introduce a thorough evaluation program that also includes input from subordinates and other divisions. We are also considering implementing a monitoring system through which we can solicit customer feedback. Furthermore, we will proceed with giving more detailed evaluative feedback to our employees in order to maintain the fairness of the evaluation process and increase employee confidence in its effectiveness.

High-quality Services Come from High-quality Employees

Improving the quality of our personnel is integral to raising the quality of our products and services. As we later describe in the section on our “Group Management System” (from page 31), we plan to strengthen our human resources and bolster career management through a wide variety of training programs.

No Change to the Total Headcount, but More Use of Part-timers Will Improve Efficiency

According to our consolidated-level employment plan (which includes Daiwa SB Investments and security advisors) for the next three years, the total number of employees, including both full-timers and part-timers, will remain largely unchanged. However, we plan to reduce the number of full-time employees by 400 and raise the percentage of part-timers who handle office work from the current 40% to more than 50% over the next three years. In doing so, we believe we can convert more of our fixed personnel costs to variable costs.

5. Upgrading Our Corporate Governance System

Ensuring Better Brand Management

We are committed to continue upgrading our corporate governance structure and to ensure that our brand management strategy is well executed. For this purpose, our chief focus will be to (1) increase the number of outside directors on our Board, (2) move to a "committee system," (3) fully equip the Group with internal controls, (4) establish the Daiwa Securities Group Corporate Governance Principle, and (5) introduce a new executive compensation system linked to shareholders value. Details regarding these initiatives are explained in the section, "Group Management System".

Improving our corporate governance structure is also necessary to enhance compliance. During FY 2002, we experienced several regrettable incidents that were a complete deviation from the Daiwa Securities Group's goal of management based on building a brand. These incidents included cases of insider trading that caused administrative sanctions to be placed on Daiwa Securities SMBC. To prevent a reoccurrence of these incidents and to regain the trust of our stakeholders, Group companies have reestablished internal rules and upgraded their training programs.

Balance Sheet Reform and Continued Cost Controls

Management of External Debt and Risk Assets

While we did not include balance sheet reform and the continuation of cost controls among the five important issues contained in our new medium-term management plan, we will continue to push forward in these areas so as to attain less-volatile business results and improve our capital efficiency. Balance sheet reform will involve a tighter squeeze on external debt and risk assets in non-core business areas. We hope to reduce our external debt by around ¥120 billion over the next three years by, in part, boosting revenues via qualitative improvements and making use of commitment facilities. We plan to decrease our non-core business related risk assets by about ¥100 billion.

Making Our Cost Structure Better Able to Withstand Turbulent Business Conditions

Our basic approach towards costs will be tighter controls, but much depends on business conditions. As we explained earlier, we plan to convert more of our cost base to variable costs so as to be better protected from the ups and downs of the business environment. On the other hand, we intend to make ¥70 billion worth of IT-related investments over the next three years, compared with the total amount of ¥91 billion invested during our previous medium-term management plan. Within a limited investment framework, we will focus on areas that lead to improvements in quality and productivity.