

Message from the CEO



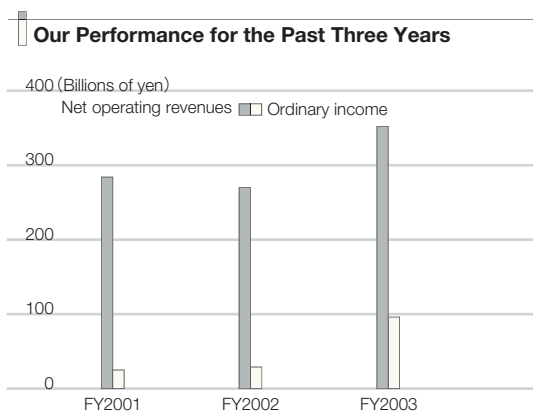
**We have a mission
to be accomplished
with confidence and pride.**

In June 2004, the CEO post of the Daiwa Securities Group was passed on from Yoshinari Hara (photo on right) to Shigeharu Suzuki (photo on left). During Mr. Hara's six-and-a-half-year tenure as CEO, the Group underwent various management reforms, including changes to its marketing system, management system, and balance sheet. We are now starting to see the results of these efforts and are confident that we will emerge as a winner in the second round of transformation of the financial services industry. We will accomplish this under a new management system by further differentiating ourselves from the competition, completing the move to a performance-based remuneration system, and gaining a firm grasp of our customers' diverse and complex needs.

Performance Highlights

Turnaround in Earnings

In FY 2003 ending March 31, 2004, consolidated net operating revenues rose by 30.1% to ¥352.4 billion. Ordinary income also showed a remarkable recovery, increasing by about 3.3 fold to ¥96.1 billion. I believe there are three major factors underlying this recovery in earnings. For a start, we benefited from an upturn in the external environment amid a rebound in the stock market and the overall economy. In addition to trading value on the First Section of the Tokyo Stock Exchange rising 57%, the earnings of Japanese companies improved dramatically and demand for raising funds expanded sharply.



Implementation of a well balanced offensive and defensive strategy will enable us to increase shareholders' equity regardless of the external environment.

The Success of Management Reforms That Balance Offensive and Defensive Strategies

The remaining two factors that contributed to the growth of the Daiwa Securities Group's earnings stemmed from our own efforts: First of all, as I will explain later, along with working to improve each of the Group's three functions of sales, the development and provision of products and services, and research, we have steadily and speedily implemented "forward-looking reforms" to systematically connect these three functions and enhance synergies.

Second, along with stabilizing our performance by converting fixed costs — especially personnel costs — into variable costs, we have worked to maximize our capital efficiency by streamlining assets that were not contributing to our main businesses and by reducing external debt. These factors coincided and led to significant improvements in our performance.

Balance Sheet Reforms Directed at Establishing a More Transparent and Solid Financial Base

Up to now, the Daiwa Securities Group has been working actively to reform its balance sheet and establish a transparent and solid financial base. In FY 2003, we posted an impairment loss of ¥12.7 billion resulting from the early adoption of accounting for impairment of fixed-assets two years ahead of the mandated deadline. With this move, we have been able to clear all foreseeable latent losses. This decision was made based on the confi-

dence we held in achieving future earnings becoming a firm conviction during the year in review. Going forwards, I believe that we will be able to steadily increase our capital base by continuing to generate profits.

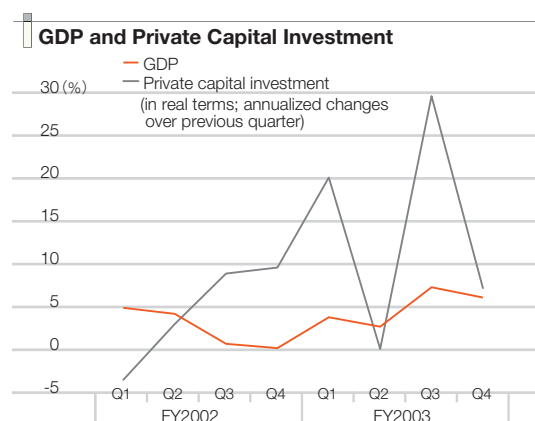
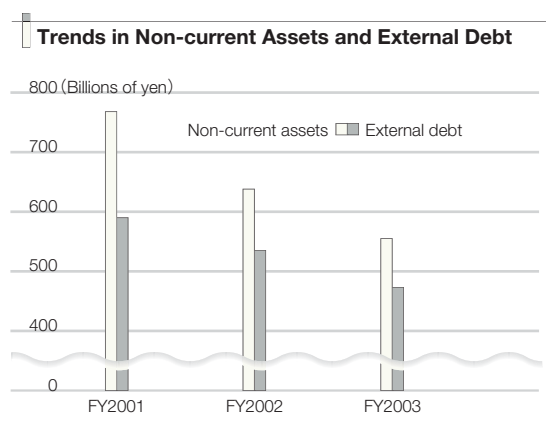
Seeds of Domestic Economic Growth

The Long-Awaited Breath of Growth

The Japanese economy has emerged from a long period of severe winter and is now well into spring. I believe this is because the various problems that had been weighing heavily on the economy — excessive debt in the private sector, non-performing loans, and deflation — are gradually being resolved. We are witnessing the emergence of some unprecedented changes in the recovery pattern of the Japanese economy. Previously, domestic companies aggressively cut costs to remain price competitive in existing markets. Now they are striving to grow by utilizing their unique technology to create new markets. One concrete example is the dramatic growth shown by the digital home electronics industry, an industry in which Japan is displaying strong originality and continues to be competitive in the global market.

Playing an Important Role in Circulating the Life Blood of the Economy

Sustained growth cannot be achieved with the return of just strength and spirit (i.e., confidence).



Source: Cabinet Office, Government of Japan

Never has there been a time when so much is expected of us.
Providing for customer needs is a direct contribution to the Japanese economy.

Only those who have steadily carried out the necessary reforms based on accurate foresight are eligible to emerge as one of the winners.

The life blood of the economy is money, and the smooth circulation of blood to deliver energy where it is needed is indispensable. Japan has reached the point where it must deliver funds to sectors of the economy where there is potential for growth. These include venture companies that are trying to expand based on their superior technology and services, and large corporations that have streamlined their businesses and achieved operational efficiency.

Let us now look at the situation of the provider of these funds. While the demand for new funds from companies is expanding along with the economic recovery, domestic companies as a whole still hold approximately ¥30 trillion in excess funds. As for individuals, of the ¥1.4 quadrillion in financial assets they own, nearly 60% are lying dormant in savings accounts. The circulation of money in the Japanese economy cannot be considered sufficient under these circumstances. This circulation cannot be improved by relying on indirect finance (i.e., the banks), which manages current deposits. In addition to the limited risks that the banks can shoulder, there is a lack of mechanism to deter violations of corporate governance. For the life blood of the economy to flow smoothly and to secure a corporate governance structure that fulfills appropriate risk and return requirements, the direct finance market must be fully operational. Our role and responsibility of developing market-based solutions that meet the needs of companies and investors are becoming increasingly large.

Bringing About Sustained Economic Growth in Japan

The growing need for smooth circulation of funds represents a major business opportunity for us. Now is the time to fulfill our underlying responsibility of contributing to the Japanese economy. Having solved the bad debt problems by the early 1990s, the United States, in part helped by the IT revolution, enjoyed more than 10 years of continued prosperity. The long-term economic growth achieved in the United States is now poised to come to Japan. Whether this actually happens rests on our shoulders.

Strategies of the Daiwa Securities Group

Capability to Take on Business Opportunities

“Opportunities” presents itself to all players in the industry, but only a few can take advantage of these opportunities. All companies have “responsibilities” but not necessarily all players can fulfill these responsibilities. I believe that in the end it all comes down to whether we were able to envision the changes in the economy, whether we have adopted the appropriate strategies, and whether we were able to execute accordingly.

We have been implementing our management reforms steadily and surely to be in the position to seize the major opportunities being made available in Japan and to become a player capable of fulfilling its responsibilities in helping to create an even larger trend.

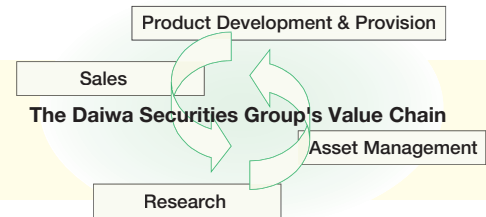
Strategy 1:

Differentiating Our Respective Strengths

Our strategy has been to grasp the diverse needs of our customers, to create high-quality products and services that meet these needs, and to provide these products and services in a timely manner. In carrying out this strategy we have had to differentiate ourselves from our rivals by (1) establishing a marketing structure that allows us to obtain a good grasp of our customers' varied needs, (2) securing “intelligence” (i.e., research and analysis capabilities) and creating a development structure that will enable us to create high-quality products and services, and (3) establishing a decision-making and command chain that enables us to react quickly.

As an example of the reforms to the marketing structure mentioned in (1) above, in the retail area we have established a new marketing structure. This combines an area marketing system (“Satellite Branch System”) with a multiple channel system (“Two-course” Service). In the wholesale area, we have established Japan's first investment bank formed through an alliance between a major securities company and a “megabank.”

Regarding the quality of “intelligence” mentioned in



(2), we worked to improve the Group's think tank (Daiwa Institute of Research Ltd. (DIR)) and asset management companies (Daiwa Asset Management Co. Ltd. (DAM) and Daiwa SB Investments Ltd. (Daiwa SB Investments)) by introducing performance-based remuneration systems. On the other hand, our wholesale company (Daiwa Securities SMBC Co. Ltd. (Daiwa Securities SMBC)) set up a division specializing in industry research (currently the Research & Advisory Department) consisting of a group of analysts with experience in various industries. Our efforts to improve quality have not been limited at the retail (Daiwa Securities Co. Ltd. (Daiwa Securities)) and wholesale companies. We have also been working to improve quality by strengthening training and education of all sales personnel. Finally, to deal with (3), we have delegated a wide range of authorities to the manager level.

I believe that all three of these reforms have helped to differentiate ourselves sufficiently from our competitors within the industry, owing to both the timing of their introduction as well as the speed and degree of implementation. In other words, our strategy has been to shift from the sell-side logic of aiming to be No.1 in transaction volume to the customer's perspective of aiming to be No.1 in terms of quality and productivity.

Strategy 2: Creating a "Value Chain"

Along with improving the three functions of sales, the development and provision of products and services, and research, we worked to maximize value by creating synergies among these functions. For example, while it is natural for Daiwa Securities and Daiwa Securities SMBC, the largest supplier of products, to work closely together, Daiwa Securities and our asset management companies, which develop and manage investment trusts, have also established close working relationships. Furthermore, Daiwa Securities SMBC and DIR work closely together to market to institutional investors. Within Daiwa Securities, we have created a new post of "internal wholesaler" when we introduced the Satellite Branch System. This post

was established to strengthen the ties between the branch offices and the Marketing Division at the head office. At Daiwa Securities SMBC, we combined the Fixed Income Division and the Derivatives and Structured Financial Products Division for this purpose.

Transforming Confidence into Conviction

No matter how rational a strategy may be, unless it achieves results it will be deemed worthless. I believe the strategies that the Daiwa Securities Group has implemented over the past few years with confidence are starting to steadily bear fruit. In particular, FY 2003 was the year when our confidence turned into conviction.

First, in FY 2003, Daiwa Securities' total assets under custody for the retail segment surpassed the level achieved during the so-called bubble years of the 1980s. Although the economy has recovered, the price level of the equity market is still far from where it was during the bubble period. Thus, I believe the high level of assets under custody that we have achieved indicates that the aforementioned reforms have been successful. At one point, it was said that full scale securities companies would fall into decline as companies specializing in on-line securities trading made aggressive advances. In fact, however, in FY 2003 Daiwa Securities ranked No.1 among the major securities companies and ranked high even compared with those specializing in on-line trading in the growth of on-line accounts.

In the wholesale business as well, we are steadily producing results. For instance, in the four years through FY 2003, our share of the Lead Manager League Tables rose from 18.2% to 22.2% for straight bonds, from 6.9% to 28.2% for primary and secondary equity offerings, and from 17.1% to 26.8% for IPOs. Notably, for three consecutive years from FY 2001 to FY 2003, we held the top share for lead manager of straight bonds.

We have also been able to improve our "intelligence," which I think of as the source of the Daiwa Securities Group's future growth. After improving its rating for three consecutive years, DIR finally reached the top of the analyst and economist

The reforms we have implemented have been successful and are now bearing fruit.

rankings in 2003. Furthermore, in asset management, Daiwa SB Investments was recognized for its asset management capabilities and was designated by Japan Post as the sole Japanese investment management company to manage the Japanese equity component of both the postal saving and postal life insurance funds. There is no doubt that these developments have led to an increase in assets under custody and an improvement in its earnings. I believe this represents a victory for both our differentiation and value chain strategies.

Addressing the Issues

We are confident, but we also remain vigilant. As I mentioned at the beginning of this message, the improvement in the market was a significant factor behind our earnings growth. Thus I do not believe that we can take credit for all that we have achieved so far. It is my duty as CEO to always have a good grasp of any remaining problems which may be hiding behind improvements in the external environment, to reflect upon how we can do better, and to plan the appropriate course of action.

1. Cultivating High Net-Worth and Corporate Clients at the Retail Business:

Appointment of Senior Consultants, Introduction of Wrap Accounts, Forming New Alliances in Response to the Lifting of the Ban on Securities Intermediation

Of the issues that we are now facing, the one that must be dealt with as a matter of urgency is the cultivation of high net-worth and corporate clients on the retail side. We have already implemented several measures with this in mind. One is the expansion of our tie-up with the Sumitomo Mitsui Banking Corporation, which has up to now centered on the wholesale business, to also include our retail arm, Daiwa Securities. The specific aim of this move was to cultivate corporate clients. In another example, during FY 2003 we selected 170 sales personnel with proven consulting capabilities,

and designated them as senior consultants. In April 2004, we appointed these consultants to branch offices in the major metropolitan areas. As a near-term goal, we intend to expand the number of these senior consultants to 600 by the end of FY 2005. Moreover, we have introduced wrap accounts to provide high value-added services. In addition, the ban that restricted banks from participating in the securities intermediation business is scheduled to be lifted in December 2004. Keeping this in mind, we are looking for possible tie-ups in this field with a number of financial institutions including regional banks, in addition to the non-financial corporations for which the ban has already been lifted.

2. Further Improving Our Abilities to Generate Profits from Trading

Over the past few years, the level and stability of revenues from our trading business have recovered rapidly. However, the gap between ourselves and the major competition in the industry has not yet narrowed to an acceptable level. In order to increase revenues generated from trading, we will of course need to raise our abilities to source transactions, but it is also important to enhance communication with customers to obtain a better grasp of their needs through such measures as expanding our stock lending business. The aforementioned reforms to our marketing system and our value chain strategy will most definitely lead to a further expansion in our client base. Thus, I would like to prioritize continuing and accelerating these basic strategies.

3. Revamping the Asset Management Business

As I have mentioned, our asset management business has been able to differentiate itself in pension fund management. But in investment trust management, we still have a long way to go. Nevertheless, with the efforts to enhance our cost efficiency now bearing fruit, and with the business environment hitting rock-bottom, the worst seems to be finally over. Asset management represents an extremely significant part of our business portfolio as a means to expand stable sources of earnings — or in other

Three ways we are cultivating high net-worth and corporate clients:

- deployment of senior consultants,
- development of a wrap account business, and
- forming alliances with a broad range of partners

words for the improvement to the quality of the Daiwa Securities Group's earnings. Furthermore, the influence this business has on the rest of the Group (value chain) cannot be ignored. We will work to improve the performance of funds under management and raise the company's profitability by reviewing the number of funds it manages. We will also change the attitudes of the fund managers by introducing a performance-based compensation scheme.

Corporate Governance

Shift to a "Committee System"

Listening to the market is a prerequisite for anybody working in the securities industry. Thus, I believe I am sufficiently aware of the concept of "corporate governance by shareholders." I also believe that the voice of the market is the most efficient means of measurement.

Up to now, corporate governance at the Daiwa Securities Group has been centered on the Board of Directors, which determines strategy, and the Management Committee and the Executive Committee, which implement corporate policy, supported by the Advisory Board and the Compensation Committee. From FY 2004, we have shifted to a Committee System that makes a clear distinction between the supervisory and executive roles of management. The Commercial Code requires that in moving to a Committee System we set up a Nominating Committee, Audit Committee, and Compensation Committee in which the majority of members must be outside directors. Our intention is to increase transparency of management through these supervisory functions.

CSR (Corporate Social Responsibility)

The phrase "corporate social responsibility" is not a new one. However, the acronym CSR is being used in a different fashion from before.

Our society and economy are currently going through major structural changes. Changes in perspectives are obvious, from that of producers to that of consumers, from public to private, and from development based on mass production and consumption to an emphasis on information and the environment. Needless to say, corporations have a major role to play in realizing this transition.

The Daiwa Securities Group is not passively accepting CSR as its "responsibility." Rather, we think of it as a strategy to actively build trust within our society. This is because companies that are successful in changing CSR into a competitive advantage will be able to achieve sustainable development by benefiting from the business opportunities amid the sweeping changes in the economy. In addition, CSR encompasses corporate governance in a broad sense of the word. Companies must be managed with consideration of how their business activities affect the economy, society, and environment to respond to the demands of their various stakeholders and earn their trust.

Based on this belief, the Daiwa Securities Group, in addition to activities that contribute to society, such as support for the arts and volunteer work, is working hard to carry out CSR through its mainstay securities business. We are putting a lot of effort into our SRI (socially responsible investment) funds, which invest in companies selected from a CSR perspective. We are also supporting programs that provide education for young people in economics and finance and engaging in joint research into leading-edge financial technology with universities and graduate schools.

To Our Shareholders and Investors

When the economy was booming, our existence was never in doubt despite the ups and downs in our profits. However, now that the economy is mature, we must achieve growth and stability by differentiation and by rigorously improving our operating efficiency. I believe this is crucial to increase our corporate value.

As I stated above, the various reforms that the Daiwa Securities Group implemented with a firm resolve are steadily bearing fruit. Up to now, the Daiwa Securities Group had a medium-term return-on-equity (ROE) target of 12%. However, with the rise in the book value ratio following the increase in our share price, the real return to our shareholders is below the nominal ROE. Taking this into consideration, I feel that we must raise our medium to long-term ROE target. For the time being, I envision this target to be about 15%.

The capital base of the Daiwa Securities Group has been weak up to now, but based on the results of our reforms, we expect to see an excess of capital going forwards. It is my duty as CEO to make sure that this excess capital does not lay idle by balancing investment in businesses with expectations of high returns and return to shareholders. In FY 2003, we raised our dividend by ¥4 to ¥10 per share in order to distribute to our shareholders some of the results we have attained.

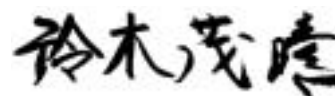
Message to Employees

My predecessor, Mr. Hara, under an unfavorable economic environment, focused his efforts on and was successful in strengthening the management foundations of the Daiwa Securities Group. My mission is to draw upon these foundations to take full advantage of the expanding business opportunities and to pursue aggressive and flexible management. Needless to say, it is the customers that make or break a company in the financial industry. In order to prevail over the competition and to earn the overwhelming support of customers, we must excel in the following two areas: the first is the possession of high level skills as financial professionals and the second is enthusiasm backed by pride. With this in mind, we will carry out extensive education and training to maximize your skills as professionals. In addition, we intend to raise motivation by promoting further reforms of the personnel and compensation system.

Our inherent DNA coupled with the highest level of professionalism will undoubtedly beat the competition, regardless of the environment surrounding our industry. Thus, to accomplish this aim, I will make speed a priority. I will also make sure my decisions are backed by strong theories and deep observations. And finally, I will make my decision making process transparent. Let us work hard together to ensure the prosperity of the Daiwa Securities Group.

July 2004

Shigeharu Suzuki
President and CEO
Daiwa Securities Group Inc.



**We are now in transition from a shortage of capital to a surplus.
Management will focus to avoid under-utilization of excess capital and increase ROE
through investment in businesses with expectations of high returns
and return of profits to our shareholders.**