

Maximizing shareholder value is not going to be achieved by a single executive. The company's day-to-day activity is built on the activity of each and every employee, whose efforts are reflected in the company's business results. This is what leads to shareholder value. In FY 2005, the Daiwa Securities Group reported its best performance since the "bubble" era—a major feat and testimony to the efforts of all Group employees.

FY 2006 marks the beginning of the Group's new medium-term management plan, entitled "Passion for the Best 2008". My most important task as CEO is to create a corporate culture and working environment that enable employees to realize their full potential—one that makes them feel motivated and satisfied to work for the Daiwa Securities Group. I want to "fuel the passion" of employees to create the "greatest" organization possible and attract the type of people that can make the Group the best in the industry.

## 1. FY 2005 in Review

### Previous strategies bear fruit under improved business conditions

In FY 2005, we enjoyed a favorable macroeconomic environment and a vibrant equity market, which had a beneficial effect for our group business. The struggling Japanese economy finally made a breakthrough and forged ahead pushing real GDP growth to 3.2% for the fiscal year. The Nikkei 225 Average surged 46% during the 12 months, driven by overseas and individual investors. The average daily trading value on the Tokyo Stock Exchange jumped 68.7% year-on-year, to ¥2,404.5 billion—the highest in history.

The highlight of the year was the real takeoff of the "savings to investment" move by Japanese individuals, whose financial assets are estimated to total around ¥1,500 trillion. The era has arrived in which individuals understand the nature of taking risks and think seriously about managing their own assets. In the meantime, corporations, supported by solid performances, are expanding their operations and adopting a more aggressive investment approach, pursuing M&As and other proactive strategies.

FY 2005 was the final year of the Group's previous three-year management plan that began in April 2003. We are pleased to report that our results for the year greatly exceeded the targets set out in the



President and CEO

Shigeharu Suzuki

plan. For example, we posted a 2.2-fold increase in ordinary income to ¥260.6 billion—well above the plan’s target of ¥127.0 billion. In addition, consolidated return on equity (ROE) reached 19.4%— the highest among Japan’s top 3 securities houses, which I am most proud of.

## 2. From Previous to New Medium-term Management Plan

### FY 2005 Performance Highlights

Creating a unique retail business model: Offering both face-to-face and online services

In the retail securities business, we think it is crucial to provide services that reflect the customers’ perspective. With this in mind, Daiwa Securities offers two service “courses” to retail customers: “Daiwa Consulting” course, for those who desire face-to-face consulting, and “Daiwa Direct” course, for those who prefer online trading. Customers can choose the course that best suits their trading style. We believe that the exceptional features of our unique business model led us to the success in FY 2005.

Now let me briefly discuss the three fields we have been strategically focusing on over the past year.

First of all, with Daiwa Consulting, we proposed a wide spectrum of products and services to meet the specific needs of customers. These included various equity and bond type investment trusts, foreign bonds, and SMA (Separately Managed Account). During the period we also pursued an asset gathering sales style. We are confident that this concept has penetrated well into our sales force over the past year, which is very important for us going forward in establishing a win-win relationship with our clients. As a result, Daiwa Securities had ¥27.6 trillion of retail assets under custody at fiscal year-end, considerably higher than the ¥21.5 trillion target set under the previous medium-term plan. Notably, net assets of Daiwa Global Bond Fund, managed by Daiwa Asset Management, exceeded ¥1 trillion. It is now the second largest investment trust in Japan.

Secondly, with respect to Daiwa Direct, we introduced a flat-fee system, which became effective for margin transactions in May 2005 and for cash transactions in July 2005. We have also succeeded to establish a unique business model by utilizing our branch network and providing access to our analyst reports from Daiwa Institute of Research (DIR). This is only possible because we keep the online operation within Daiwa Securities and we believe it makes it difficult for dedicated online brokers to emulate. As a consequence, we reported substantial year-on-year gains in assets under custody, number of accounts, and online margin balance.

Thirdly, “Daiwa SMA”, our wrap account service for high-net-worth individuals, is enjoying a faster-than-expected growth. We think the performance-based fee scheme, and the “custom-built” service, as we do all from consulting to management within Daiwa Securities, are the two key factors to the success of this service. The contract assets under management of Daiwa SMA surged to ¥159.1 billion, well above our target of ¥100 billion, and placing Daiwa Securities at the top of the industry (based on the data released by the Japan Securities Investment Advisers Association, as of March 31, 2006).

### Wholesale and investment businesses: Increased earnings and presence

Daiwa Securities SMBC, which handles the Group's wholesale securities business, made significant progress in FY 2005. Taking full advantage of the formidable client base, built from our collaboration with Sumitomo Mitsui Banking Corporation, we stepped up cross-divisional activities, from underwriting and product development to brokerage. In particular, we expanded our business in providing high-value-added products, notably in structured bonds and derivatives, as well as financing vehicles utilizing SPS (Structured Principal Solution) Program. As a result, consolidated net gain on trading, mainly driven by Daiwa Securities SMBC, reached ¥224.9 billion, far surpassing the ¥140 billion target set under the previous medium-term plan. In the lead-manager league tables, we seized the No. 1 spot for IPOs, and for the third successive year in total corporate bonds.

We are also actively expanding our private equity investments that are mainly carried out by Daiwa Securities SMBC Principal Investments (Daiwa Securities SMBC PI). In FY2005, we made large-scale investments in companies such as SANYO Electric and Sumitomo Mitsui Construction. As a result, Daiwa Securities SMBC PI's fiscal year-end investment balance rose to ¥310 billion, highlighting our greatly enhanced presence in this field.

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### New medium-term management plan: Seeking to become "Japan's best securities group"

Building on this record of success, in April 2006 the Daiwa Securities Group stepped up efforts to cement its position as "Japan's best securities group." Specifically, we initiated a new Group's medium-term management plan, called "Passion for the Best 2008."

Under the new plan, we will further reinforce our earnings foundation by adding a fourth core segment—Investment—to our three current core activities in retail securities, wholesale securities, and asset management.

In quantitative terms, we are targeting consolidated ordinary income of ¥350 billion and consolidated ROE of 15% or higher for the year ending March 2009, the third and final period of the plan. Specific targets include ¥45 trillion or higher in retail assets under custody, the No. 1 rank in the league tables in the wholesale segment, equity investment trust assets of ¥11 trillion or higher in the asset management segment, and ¥5 trillion or higher in investment advisory assets. In qualitative terms, we intend to become "Japan's best" in every aspect, including customer satisfaction, legal and ethical compliance, corporate social responsibility (CSR), and information disclosure.

\* For details of the Group's new medium-term management plan, see p.28-33.

### 3. Earning the Public's Trust and Raising Corporate Value

#### Corporate governance

In 1999, we became Japan's first listed company to switch to a holding company structure. Prior to that time, we had already established an Advisory Board, which was followed by setting up the Compensation Committee in 2000. Two years later, in 2002 we appointed outside directors in an effort to further separate management and supervisory functions. As a natural progression, in 2004 we shifted to a "committee system" of corporate governance, thus clearly differentiating the business execution function from the supervision and evaluation functions. Accordingly, the Group has continued to build a highly transparent and impartial corporate governance framework. We have also worked hard to improve the quality of our internal control system. In FY 2005, for example, we set up a systems auditing framework within the internal audit division of the Group. We also established an information security management system and instituted measures to monitor and verify our responsiveness to the Personal Information Protection Law.

Ultimately, however, the goal of corporate governance is to "pinpoint and prevent systematic misconduct as well as arbitrary or uncontrolled actions by management, and to establish a trend in which all employees adhere to the Group's corporate principles". I believe that we will achieve this goal if we can ensure that all employees are constantly aware of social expectations, embrace their jobs with pride, and feel motivated to work at the Daiwa Securities Group. In my desire to promote such a mindset throughout the Group, I work year-round to visit our branches nationwide and speak directly to our employees.

#### CSR initiatives

I believe that the essence of corporate social responsibility (CSR) is to contribute to the creation of a better society through our regular business activities. Our role is to build bridges between companies seeking to raise funds and investors desiring more effective management of their assets. By satisfying the needs of both parties, we are performing a valuable public service by providing a function that supports smooth economic and social development. The public service attributes inherent in the securities business form the core of our CSR commitment. It is important that all employees fully appreciate the Group's social mission and perform their regular businesses accordingly.

Each year, we publish the Group's Sustainability Report. Our 2005 report won the Grand Prize for Sustainability Report (Minister of the Environment Awards), underlining the high official praise accorded to our CSR approach. Going forward, we will take CSR initiatives via our core business in an effort to support sound social development while raising the Group's evaluation in the eyes of the public.

### Return to shareholders

In FY 2005, Daiwa Securities Group Inc. declared an annual cash dividend of ¥34 per share, greatly exceeding the previous record of ¥14. We also achieved a dividend payout ratio of 32.2% in FY 2005, which is above our 30% target and at a level that we believe is satisfactory for our shareholders' expectations.

We regard ROE as one of the most important performance benchmarks that illustrate how efficiently we are utilizing our shareholders' capital. Under our new management plan, we are targeting consolidated ROE of 15% or higher, and to this end we will aggressively allocate capital to areas expected to generate high returns. In the absence of investment targets that enable us to raise corporate value, our policy is to actively return profits to shareholders.

### To shareholders, investors, and employees

From my perspective, conditions surrounding Japan's financial and capital markets are quite favorable. Given the acceleration of the "savings to investment" move, we have a growing opportunity to demonstrate our professionalism on our home ground—the equity field.

Meanwhile, I believe that Japanese companies, with recovering financial strength, will expand capital investments and adopt a more assertive approach to the capital market. This should lead, for example, to increases in M&As aimed at raising corporate value. Given this appropriate evolution of the capital market, the core foundation supporting the financial services sector is clearly shifting from traditional savings to the securities business—our home turf.

Improving business conditions, however, will also bring intensified competition. To win against our rivals while achieving sustained growth and raising corporate value, we must maintain a constant desire to improve and build on current achievements. As CEO, my responsibility is to provide a job environment that cultivates strong employee morale, enables workers to fully realize their creative potential, and helps them approach their jobs with passion and enthusiasm. If management and employees fail to unite and overcome formidable challenges, we cannot achieve major success.

We are steadily attaining the No. 1 position in many of our business fields. Backed by an unprecedented financial performance, I intend to forge ahead and make the Daiwa Securities Group into the "greatest" organization from the viewpoint of all stakeholders.

July 2006

**Shigeharu Suzuki**

President and CEO

Daiwa Securities Group Inc.

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