

Our current medium-term management plan, “Passion for the Best” 2008, encapsulates the Group’s business strategy and management goals for the period from FY 2006 to FY 2008. Under this plan, the Group will focus its full energies in an effort to “build Japan’s best securities group on a foundation of customer trust and employee commitment.”

During FY 2006, the first year of this plan, we once again verified the vast potential that the Group possesses. It is clear that the Group is now well on the way to unleashing this potential fully, as we move confidently towards our goals.

## On Track to Being the Best



Shigeharu Suzuki

*President and CEO*

## Message from the CEO

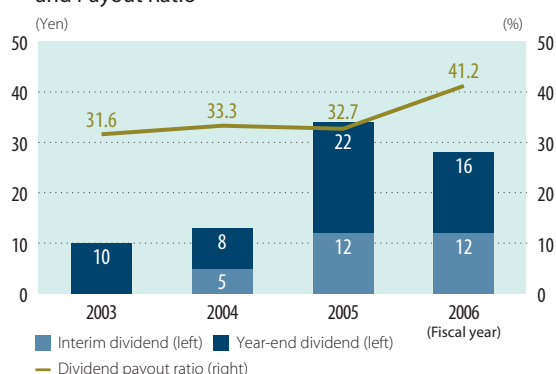
### Responding Confidently to the Challenges of FY 2006

Based solely on the headline figures in the FY 2006 earnings statement, our performance during the year was not entirely satisfying. However, in terms of the progress that the Daiwa Securities Group made toward medium-term management goals, I think the tally of achievements was quite impressive.

Consolidated earnings figures for FY 2006 show that net operating revenues for the Daiwa Securities Group declined 9% year on year, to ¥526.7 billion, ordinary income dropped 25%, to ¥195.4 billion, and net income was down 34% from the previous year, to ¥92.7 billion. This mainly reflects conditions in the Japanese stock market, which spent much of the year in a correction phase and saw a particularly dramatic drop in the small-cap and venture stock markets. As a result, brokerage commissions from individual investors decreased, as did profits from equity trading. Nevertheless, we were able to maintain a consolidated ROE for the Group of 10.8%, which put us in the top spot among major domestic securities companies, in terms of profitability, for the third year in a row. The Group paid an annual dividend of ¥28 per share in FY 2006, while the dividend payout ratio was 41.2%—well above our 30% payout ratio guideline.

Although our earnings performance was modest in FY 2006, we made a fine start in pursuit of the targets laid out in the Group's medium-term management plan, "Passion for the Best" 2008. In the first year of the plan, we made even more progress towards these targets than initially expected. I would like to use this opportunity to point out some of the important achievements that the Group made in its core businesses during FY 2006, and describe to you, our stakeholders, the many opportunities that our medium-term business plan will unlock for the Daiwa Securities Group, so that you may share my confidence and optimism as we progress towards these goals.

Annual Dividends Paid by Daiwa Securities Group Inc. and Payout Ratio



Notes: 1. The Group began paying an interim dividend for the first time in FY 2004.  
2. Dividend payout ratio = Dividends per share / Consolidated net income per share

### Dramatic Revenue Increases in the Asset Management and Investment Divisions

Although domestic stock trading by individual investors declined in FY 2006, the market for investment trusts was extremely active. Assets under management in publicly offered investment trusts grew by ¥16 trillion year on year in FY 2005, and added a further ¥14 trillion in FY 2006, raising the total balance to ¥72.5 trillion at the end of March 2007. Clearly, Japanese individuals are starting to shift a part of their estimated ¥1,536 trillion financial assets into these investments. The favorable trend had a strong impact on the asset management operations of the Daiwa Securities Group, boosting assets under management of both equity-type investment trusts and foreign bond-type investment trusts. A dramatic rise in the balance of assets in the Group's equity investment trusts contributed to sharp revenue growth in the asset management division.

Meanwhile, the Group's investment division has been steadily increasing its direct investments. The total investment amount expanded to ¥356.0 billion as of March 2007, and some of the private equity investments that the Group has made are starting to pay favorable returns.

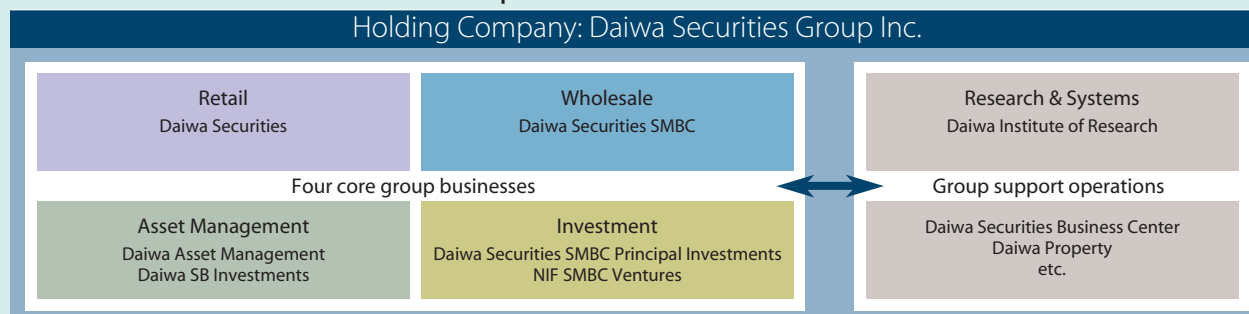
The growth achieved by these two divisions is producing a much better earnings balance among the four core business divisions. This has contributed greatly to our efforts to establish a broad, diverse and stable earnings base.

### Assets Under Custody in the Retail Division Rising Steadily

Although income from equity brokerage commissions may have declined in FY 2006, several core businesses in the retail division registered solid growth during the period. Agency commissions from investment trusts increased, as did the balance of margin positions outstanding in the Group's online trading business—"Daiwa Direct." In addition, "Daiwa SMA\*," our wrap account service for high-net-worth individuals, registered a clear increase in contract assets under management. Agency commission income from investment trust assets, in particular, has risen to over ¥3.0 billion a month; this is an income stream that we expect to remain steady, regardless of the short-term ups and downs of the stock market.

\* SMA=Separately Managed Account; an asset management service with a discretionary investment contract or an investment advisory service

#### Business Structure of the Daiwa Securities Group



### Investment Banking Business Demonstrating its Ability to Propose Financing Solutions

Daiwa Securities SMBC, which oversees our wholesale securities operations, has been working to improve its ability to offer investment banking solutions. Perhaps the best example of our accomplishments in this area is Daiwa Securities SMBC's support for a hybrid securities product issued by Nippon Steel. Utilizing internal financial engineering technology, Daiwa Securities SMBC has successfully developed this hybrid securities product, a new type of financial instrument that has received positive reviews from the customer. The advice that we provided helped Nippon Steel successfully raise ¥300 billion. In this way, we demonstrated our ability to propose innovative solutions that help clients address even complex financing needs. Because of this, and other successful investment banking deals, Daiwa Securities SMBC was recognized by THOMSON DealWatch as the FY 2006 "House of the Year," in the overall category. Clearly, Daiwa Securities SMBC is establishing itself as a highly innovative, comprehensive investment bank, not only in the eyes of customers in Japan, but world-wide.

## Favorable Business Conditions Offer Continuing Support

In FY 2006, Japan's capital markets continued their steady and brisk expansion. The shift of individual assets from savings to investment, in particular, continues to support the Daiwa Securities Group's growth.

Although I have pointed this out many times before, the current condition of Japan's financial markets is an extremely important factor which benefits the entire domestic securities industry. One of the basic assumptions underlying the goals of our medium-term management plan is that these favorable conditions will continue. During FY 2006, the stock market actually registered a slight decline over the course of the fiscal year, but trading value on the TSE First Section reached a record high of ¥600 trillion. By comparison, at the peak of Japan's economic bubble, trading value was only a shade over ¥300 trillion. This should give you some idea of the rapid growth that Japan's stock market is currently experiencing.

There is also an abundance of macroeconomic data which points to the probability that Japan's capital markets will continue growing. According to the Group's research arm, Daiwa Institute of Research, ordinary income at the top 300 listed corporations in Japan increased in FY 2006 for the fifth year in a row, and it appears likely that profit growth will continue this year and beyond.

Meanwhile, the market for mergers and acquisitions conducted by Japanese companies is growing by leaps and bounds every year. In 2006, there were 2,775 M&A deals carried out in Japan, more than four times the number of cases registered ten years ago. The total value of these deals soared past the ¥15 trillion mark. This shows that Japanese companies now

view M&A activity as a commonplace management tool. However, Japan still lags behind compared with the situation in other advanced economies. Relatively speaking, the M&A era in Japan has only just begun, and I strongly expect to see this activity become even more prevalent in the future.

While the trends mentioned previously are sure to benefit Japanese securities companies, by far the most important boon to the securities industry in recent years has been the shift of individual assets from savings to investment, which continued to accelerate in FY 2006. As of March 2007, private individuals held an estimated ¥1,536 trillion in financial assets, an increase of roughly 1% compared with March 2006. The share of these assets held in cash and deposits stood at 50.1%, a year-on-year decline of 0.6 percentage points, while individual holdings of bonds, investment trusts and equities accounted for a combined 19.5%, up 0.3 percentage points. A simple calculation based on the estimated total suggests that individual investors poured ¥5 trillion into these investments during FY 2006. Even so, Japanese individuals still keep a far larger share of their assets in cash and deposits than people in most other countries. We expect the percentage of assets invested in negotiable securities to continue rising over the coming years. This shift from savings to investment is a trend that the government itself is promoting, and securities groups such as the Daiwa Securities Group have an important role to play in supporting this trend.

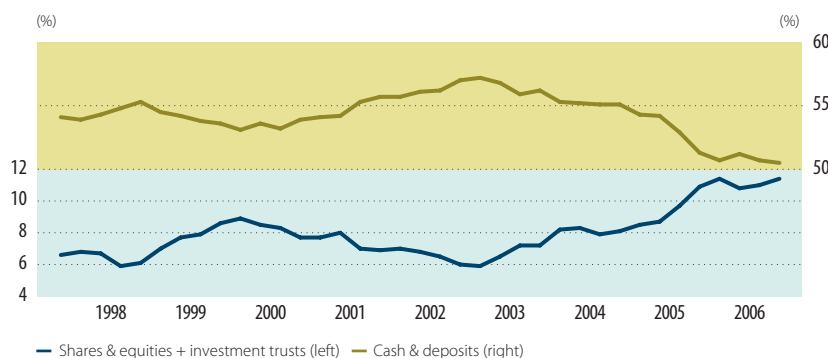
## Business Expansion in FY 2007

In FY 2007, each business division of the Group will work to meet ambitious targets, as we seek to carry out our medium-term management plan, "Passion for the Best" 2008.

Although our achievements in FY 2006 and the benefits of continued market expansion give us cause for optimism, each division will redouble their efforts to promote growth in FY 2007.

In the retail division, we will try to increase the balance of customer assets dramatically. The Daiwa Securities Group has many competitive advantages in this segment, including

Securities and Cash & Deposits as a Share of Total Household Financial Assets

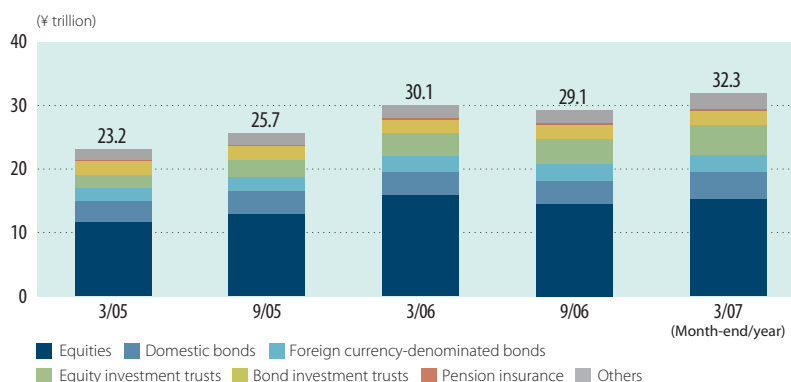


popular investment trusts and a dominant market share of the wrap account business via “Daiwa SMA.” In FY 2006 we launched several new services for retail clients, such as the securities-backed loan business. In these ways, we are trying to turn market events—the rising number of individuals reaching retirement age, and plans to introduce fully electronic stock certificates—into opportunities for business growth. In the online trading business, past efforts by some players to compete on the basis of commission rates are now giving way to competition based on added value. In response, we are expanding our presence in the market with “Daiwa Direct,” a service that seeks to merge the advantages of Internet trading and branch office support in order to provide higher levels of customer service.

In the wholesale business we are continuing to aim for the top spot, with the goal of earning recognition as number one in the league tables for equity financing, debt financing and M&A deals. Daiwa Securities SMBC enjoys extensive cooperation and support from Sumitomo Mitsui Banking Corporation, which it will continue to use in FY 2007 to improve the solutions capabilities of its M&A support and other investment banking operations. Meanwhile, we are expanding the range of financial products handled by our trading operations, and working to strengthen our Asia-related operations.

The asset management division enjoyed remarkable growth in FY 2006, and as assets continue to flow into the market, we expect the positive trend to continue. For this reason, we have raised the targets contained in our medium-term management plan to pursue more ambitious goals. The ordinary income target for Daiwa Asset Management and Daiwa SB Investments was raised from a combined total of at least ¥21 billion to at least ¥30 billion, and the target for total assets under management of equity investment trusts at the two companies was increased from at least ¥11 trillion to at least ¥14 trillion. We are working to further strengthen product development capabilities and asset management skills, while seeking to provide a higher level of service to Daiwa Securities, banks and other sales channels. In addition, during FY 2006, we established Daiwa Fund Consulting Co. Ltd., a subsidiary which evaluates investment funds. In FY 2007, this new company will help the Group to develop even more new investment trust products.

Daiwa Securities: Customer Assets Under Custody



In the investment division, Daiwa Securities SMBC Principal Investments is starting to harvest the fruits of past investment, and taking measures to ensure that this business will provide a stable stream of earnings in the future. In FY 2006, we established a new private equity subsidiary in the Asia-Oceania region, EMP-Daiwa Capital Asia Limited. This company will help us transplant the successful investment operations that we have developed in Japan to overseas markets.

## Higher Corporate Value Depends on Higher Employee Motivation

I believe that the most important mission of company management is to raise employee satisfaction and enthusiasm to the highest level possible. Employee motivation is the wellspring of a company's competitiveness.

I believe that a company's value is founded on the quality and enthusiasm of its employees. This is particularly true in the financial industry. For this reason, I consider measures to motivate employees, and provide them with a comfortable, stimulating work environment, to be the most important task of the management. I am confident that money is not the only factor in motivating employees. They also require a sense of trust in their company, a feeling of self-confidence and self-respect, and a close identification and feeling of camaraderie with their co-workers; indeed, these factors can be much more important than monetary compensation, when it comes to motivating employees.

The important question is how to convey this philosophy and message to employees effectively. One example of a way in which we are trying to promote a sense of trust and camaraderie is to involve each employee's family members in our company functions—for example, by inviting the family members of award recipients to various award ceremonies—and to promote broader relationships not only between management and employees, but with family members as well. We are also making use of the Group's broadcast media abilities, which are the most well developed of any Japanese securities group. We produce and broadcast "in-house TV programs" which tell staff at every office in the country about the direction management is taking.

Although loyalty and camaraderie are often viewed as areas where Japanese companies excel, in recent years company management, in general, has not been very proactive in conveying their high regard for employees. In Japan today, there is intense competition—even across industry sectors—to attract top-quality personnel from a shrinking labor pool. For Japanese companies to remain competitive in the future, it is essential that their investments in employees match those of any top-ranked global corporation. I am confident that the Daiwa Securities Group has addressed these issues more effectively, and more promptly, than any of our rivals.

## Aiming to Be the Best in Japan


Rising competition is actually contributing to growth in Japan's financial markets, and should be viewed as a boon to the Daiwa Securities Group. Thanks to the enthusiasm of our employees and the support of our stakeholders, we are steadily advancing towards the goal of being "the Best."

FY 2007 dawned with the news of Citigroup's take-over bid of the Nikko Cordial Corporation. The increased participation of foreign-based financial institutions in the Japanese market, and the steady disappearance of boundaries which once divided the financial industry into rigidly separate segments, are propelling consolidation and making the Japanese financial industry an increasingly competitive environment.

However, I welcome these changes, since the rising number of competitors reflects the growth of Japan's financial markets, and the evolution of Japan's securities industry, to become the core of the financial industry. This is Daiwa Securities Group's home domain, and I believe that we have the accumulated experience, knowhow and vision to emerge as the dominant player in this market.

Our role, as management of the Daiwa Securities Group, is to make the most of the favorable trends that our industry is currently experiencing, and translate the market's growth into rising corporate value. Accordingly, we will prepare the foundation on which our employees, through their devotion to the company and their strong individual ambition, can continue to build the company from strength to strength. Through these collaborative efforts and achievements of the management and employees, the Daiwa Securities Group intends to earn and to justify the trust and support of our stakeholders, so that together, we can realize the goal of becoming Japan's best securities group.

July 2007



Shigeharu Suzuki, President and CEO  
Daiwa Securities Group Inc.