Interview With the COO/CFO

The Group Aims to Add ¥40 Billion to Earnings by Improving Organizational Efficiency

To fulfill our goal of building a robust business structure, the Daiwa Securities Group aims to make substantial improvements to profitability by promoting greater organizational efficiency. Specifically, by consolidating the administrative functions of Group companies and increasing front-office staff we plan to elevate revenues by ¥10 billion and reduce SG&A expenses by around ¥30 billion (base level, assuming a break-even ordinary income). These measures will improve the underlying profitability of the Group by a net ¥40 billion.

QUESTION: In July 2011, the Group announced plans to merge Daiwa Securities Co. Ltd. and Daiwa Securities Capital Markets Co. Ltd. What prompted this decision?

A. In 1999, the Daiwa Securities Group adopted a holding company structure and divided operations into a number of separate companies under the control of Daiwa Securities Group Inc. The three main corporations in the Group are the holding company itself, Daiwa Securities Co. Ltd., which oversees the Retail business, and Daiwa Securities Capital Markets Co. Ltd. (initially Daiwa Securities SB Capital Markets), which oversees the Wholesale business (formerly in a joint venture operation with the Sumitomo Mitsui Financial Group). In the decade since we adopted the holding company structure, however, the securities business has become increasingly technical and complex. As a result, each group subsidiary has been forced to increase its middle-office and back-office staff, creating a bloated administrative structure. The number of individual departments handling middle- and back-office procedures has expanded from 41 in April 1999 to 69 as of February 2011, and the number of employees swelled from approximately 1,400 to 2,050 in the same period.

In order to reform this administrative structure, in February 2011, we began a project to consolidate all back-office procedures for administrative functions. The first step in this consolidation process involved unifying the planning, personnel and finance divisions of the three main Group companies. By the end of June 2011, this effort had essentially consolidated 35 departments into 13. Approximately 250 employees were reassigned, mainly to positions in the sales division.

By April 2014, we intend to reduce personnel levels in these divisions to around 1,500. With the reorganization of administrative divisions at head offices and branch offices added up, approximately 700 employees will be reassigned to the sales division where their contributions are expected to boost revenues by around ¥10 billion annually.

The merger of Daiwa Securities and Daiwa Securities Capital Markets represents the next step in the consolidation process. The goal is to consolidate the two companies' inter-trading activities, eliminate duplication and cut costs. By expanding our consolidation effort to target front- and middle-office functions, as well as further cementing of back-office functions, we aim to make the entire management structure even more efficient.

QUESTION : Which specific cost items do you expect to reduce, and by how much?

A. We aim to cut costs by ¥30 billion per year over the medium term, focusing mainly on four cost categories: IT systems-related expenses, real-estate related expenses, overseas SG&A expenses, and other controllable expenses.

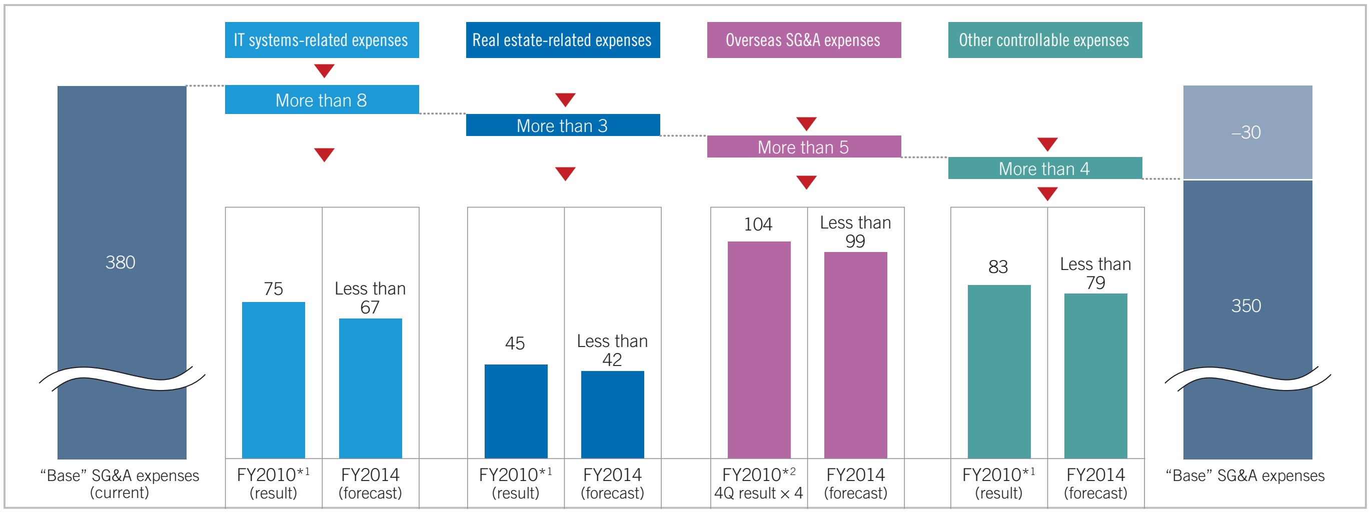
The first step in efforts to reduce IT systems-related costs will be to exercise greater selectivity in all future IT systems-related investment. Advances in the use of internal cloud computing should allow the Group to reduce operating costs. We hope to save more than ¥8 billion per year in this cost segment.

By consolidating the administrative functions of the three companies, some subsidiary company offices will be relocated to the head office building. These changes are expected to reduce costs by over ¥3 billion per year.

The Group plans to consolidate the administrative functions of overseas offices in much the same way that we are improving efficiency in domestic operations. This is expected to save over ¥5 billion. In addition, we plan to reduce advertising expenses, and other controllable expenses, while taking comprehensive steps to restrain costs related to the procurement of goods and services from companies outside the Group. This should contribute another ¥4 billion or more in cost savings.

The aforementioned items, which add up to ¥20 billion in overall cost savings, will be implemented over the course of a three-year plan that aims to meet these targets by FY2014. In addition, our plan to merge the two main securities subsidiaries, and to improve profitability in the wholesale business, is expected to contribute a further ¥10 billion in cost reductions over the medium term. This takes us to the target level of cutting ¥30 billion from base SG&A expenses.

Plans for Cutting SG&A Expenses
(¥ billion)



*1 SG&A expenses calculated on a consolidated basis, including overseas offices.
*2 Total for all overseas subsidiaries.

QUESTION: The Group's overall plan to build a robust business structure also includes revenue growth targets, adding up to an overall improvement of ¥100 billion in base earnings. Can you describe the timetable for this plan, including both cost cuts and revenue increases?

A. The diagram below shows our roadmap for earnings improvement. Phase 1 of the plan basically represents the current situation for the Group. Starting from the current "base level" of ¥380 billion in SG&A expenses, we have tried to develop a plan that will ensure that the company can break even at the ordinary income level, even in a "worst case" scenario, which involves severe stress to the business environment. Under such stress conditions we estimate that revenue could be reduced to a minimum of around ¥280 billion. Comparing these two figures, it becomes clear that we need to improve the overall earnings structure by ¥100 billion in order to achieve the goal of maintaining profitability under worst-case conditions. We plan to achieve this earnings improvement through measures such as the launch of Daiwa Next Bank, the Group-wide consolidation measures I mentioned earlier, and efforts to improve profitability at Daiwa Securities Capital Markets. We have nearly finished laying the foundation for our future earnings structure.

Phase 2 refers to our plans for the next three years: to consolidate middle- and back-office divisions, transfer personnel to the sales division, and expand the balance of customer assets, mainly in both bank savings accounts and mutual funds, in order to add ¥40 billion to "stable revenues." Together with the estimated ¥20 billion in SG&A savings, this represents a net improvement to our earnings base of some ¥60 billion.

Phase 3 represents our longer-term goal of adding another ¥30 billion to stable revenues from banking and mutual fund operations, and cutting SG&A expenses by an additional ¥10 billion. This would elevate base earnings by some ¥100 billion compared with the situation in Phase 1. Naturally, the pace of actual growth in earnings will depend on the condition of financial markets. These trends will also have some impact on how long it takes to complete Phase 3. However, we believe that the overall plan will be completed within three to five years.

Nobuyuki Iwamoto
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COO and CFO
Daiwa Securities Group Inc.

Outline of Measures to Improve Earnings Structure

Phase	Phase 1 (current)	Phase 2 (¥60 billion improvement)	Phase 3 (¥100 billion improvement)
Measures to improve earnings	•Launch of banking business •Group commences "Streamline Project" •Daiwa Capital Markets begins "Profit Improvement Project" •Group launches "Internal Reorganization Project"	•Balance of bank deposits ≧ ¥1.1 trillion •Approx. 700 employees reassigned •Reduce IT systems-related expenses •Reduce real-estate related expenses •Reduce other controllable expenses •Optimize overseas operations	•Balance of bank deposits ≧ ¥5 trillion •Increase balance of mutual fund assets at Daiwa Securities by ¥2 trillion •Increase total assets under management by ¥5 trillion