

# 1H FY2018 Earnings Results Briefing

December 3, 2018



**CHUGOKU BANK**

## Summary of 1H FY2018 Earnings Results

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For inquiries regarding this document, please contact:

Management Planning Department, The Chugoku Bank, Ltd.

Mr. Fumiya / Mr. Umakoshi

TEL: +81-86-234-6519; FAX: +81-86-234-6587      Email: souki01@chugin.jp

# Section I

## Summary of 1H FY2018 Earnings Results

# 1H FY2018 Earnings Results –Summary–

[Non-consolidated] (100 million yen)	1H FY2015	1H FY2016	1H FY2017	1H FY2018	YoY	vs. Published*
Core business gross profit	436	409	401	396	-5	10
Interest income	358	334	338	329	-9	20
Fees and commissions	74	76	71	75	4	-1
Other operating income	3	-1	-7	-8	-1	-8
Expenses	277	281	287	272	-15	-11
Core business net profit	158	127	114	124	10	22
O H R ( % )	63.6	68.8	71.4	68.6	-2.8	-4.8
Credit expense (- is reversal (profit))	-26	-27	-26	2	28	3
Bond sales gains/redemption	4	7	-3	-3	-0	-3
Equity sales gains/redemption	26	9	4	3	-1	-8
Other	12	2	-2	9	11	8
Recurring profit	229	173	140	132	-8	16
Extraordinary gain/loss	-1	-1	-1	-1	0	0
Net income	155	121	98	94	-4	15
[Consolidated]						
Consolidated recurring profit	242	184	153	140	-13	20
Net income attributable to owners of parent	160	125	105	97	-8	18

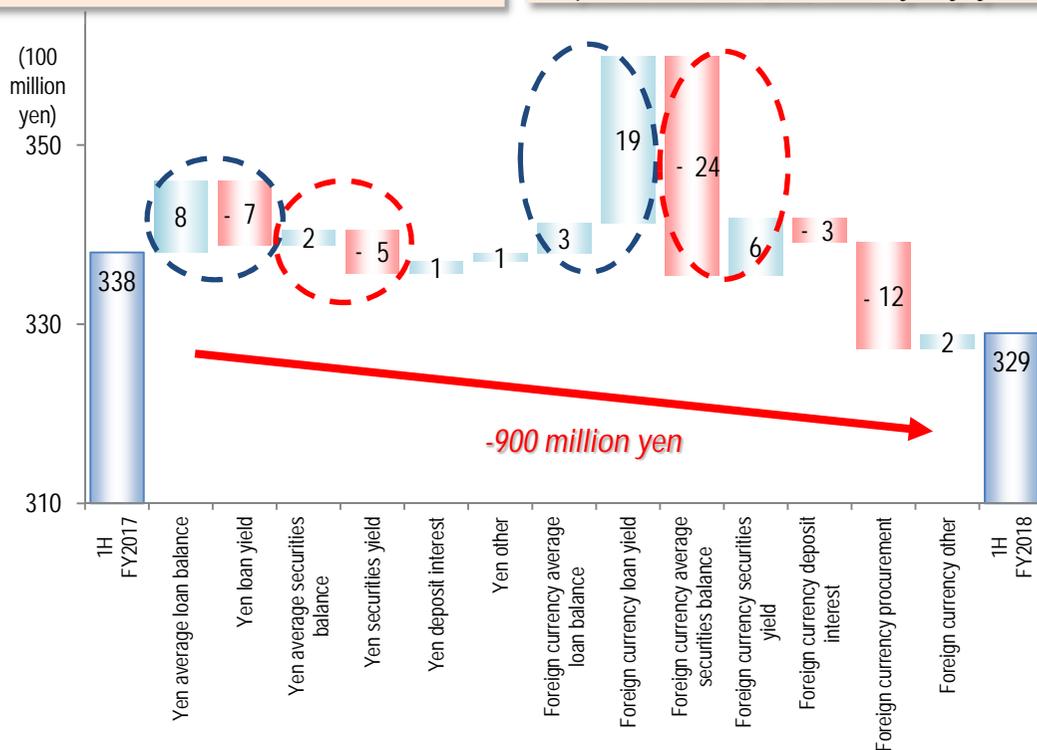
\* Forecast published on May 10, 2018

- Core business net profit increased by 1 billion yen year on year by covering the decrease in interest income with fees and commissions and cost reductions.
- Recurring profit decreased by 0.8 billion yen year on year due to a reversal of provisions for credit expense (mainly general provisions for doubtful receivables).

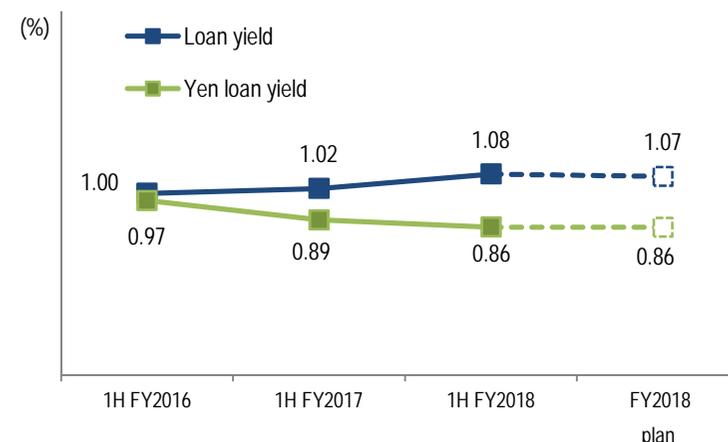
# 1H FY2018 Earnings Results –Change in Net Interest Income–

[Factors behind changes in net interest income]

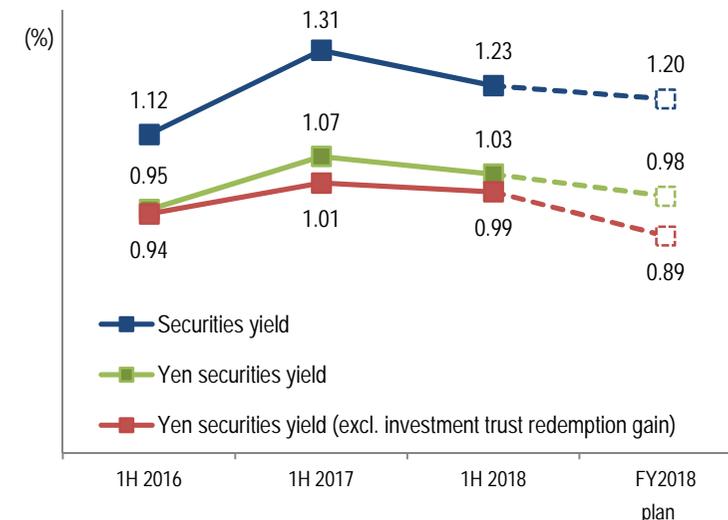
- Yen-based (-10 million yen year on year)**
  - Loan interest: +100 million yen yoy
  - Securities interest: -300 million yen yoy
  - Decrease in deposit interest: +100 million yen yoy
- Foreign currency-based (-900 million yen year on year)**
  - Loan interest: +2,200 million yen yoy
  - Securities interest: -1,800 million yen yoy
  - Increase in foreign currency procurement: -1,200 million yen yoy



[Loan yield]



[Securities yield]

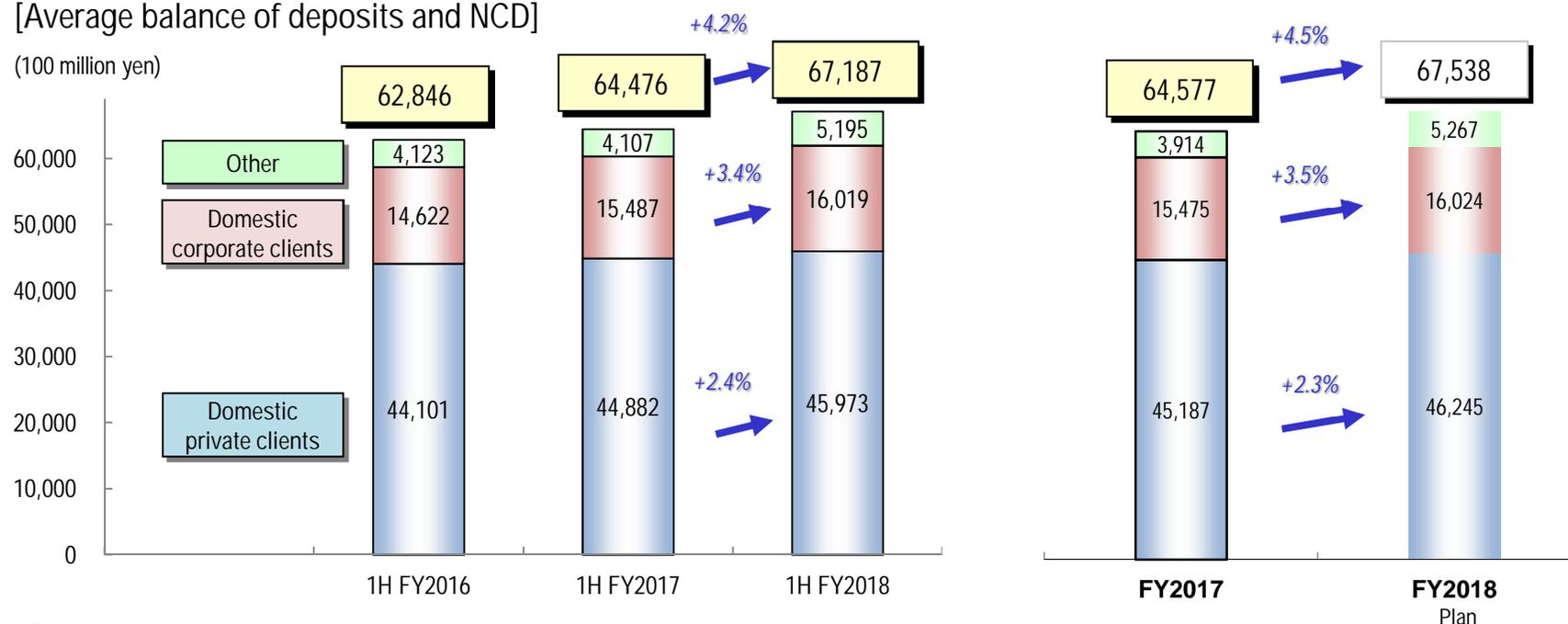


- Yen net interest income**
  - Loan interest: +100 million yen yoy since the drop in yield was covered by an increase in average balance
  - Securities interest: -300 million yen yoy mainly due to a drop in reinvestment yield
- Foreign currency net interest income**
  - Loan interest: +2,200 million yen yoy mainly due to a rise in yield on the back of a U.S. interest rate hike
  - Securities interest: -1,800 million yen yoy mainly due to a decrease in average balance owing to a reduction of balance

# 1H FY2018 Earnings Results –Major Accounts (1) Deposits & Assets in Custody– 中国銀行

[Average balance of deposits and NCD]

(100 million yen)



Ref: Balance of assets in custody

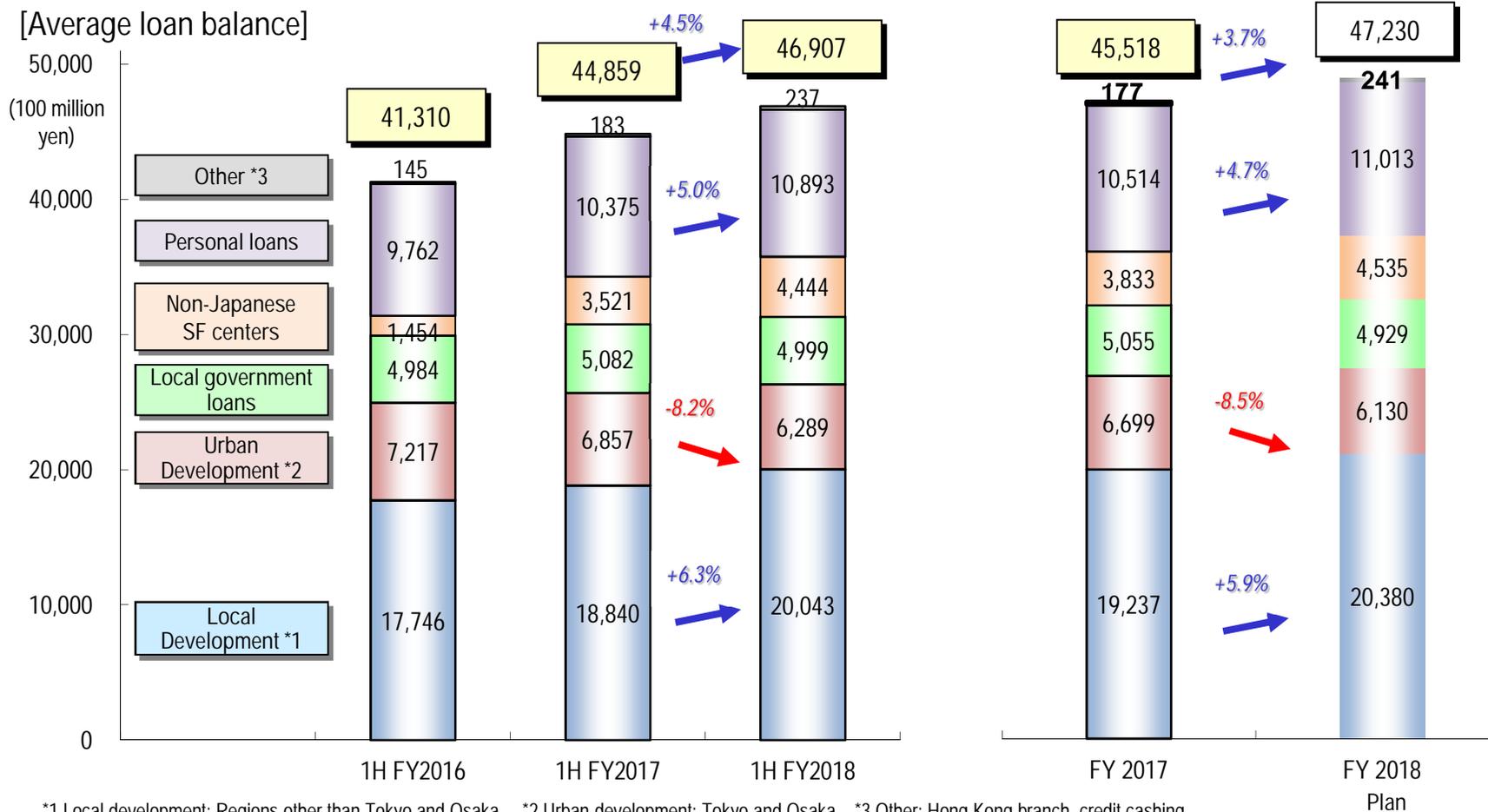
(100 million yen)	1H FY2016	1H FY2017	1H FY2018	
			Change	Change
Public bonds	2864	2931	67	-8
Investment trusts (1)	1574	1450	-124	-26
Financial instrument intermediary services	2061	1986	-75	-99
Investment trust portion (2)	862	766	-96	-111
Insurance	3447	3453	6	166
Bank parent	9946	9820	-126	33
Total investment trusts (1)+(2)	2436	2216	-220	-137
Chugin Securities	830	900	70	39

FY2017	FY2018 Plan	Change
2927	2927	0
1444	1472	28
1951	1859	-92
743	648	-95
3471	3664	193
9793	9922	129
2187	2120	-67
897	940	43

\* Public bonds are based on the value of the average balance. Investment trusts are based on the average balance of net assets. Financial instrument intermediary services are based on the average balance of the acquisition value. Insurance is based on the average balance taking into account cancellations. Chugin securities are based on the ending balance of bonds, equities and investment trusts.

- Private client deposits are growing steadily, maintaining the growth trend due to stable payment pipes (e.g., salary payment, pensions).
- Corporate client deposits continue to grow at a large pace on the back of robust corporate earnings.

# 1H FY2018 Earnings Results –Major Accounts (2) Loans–



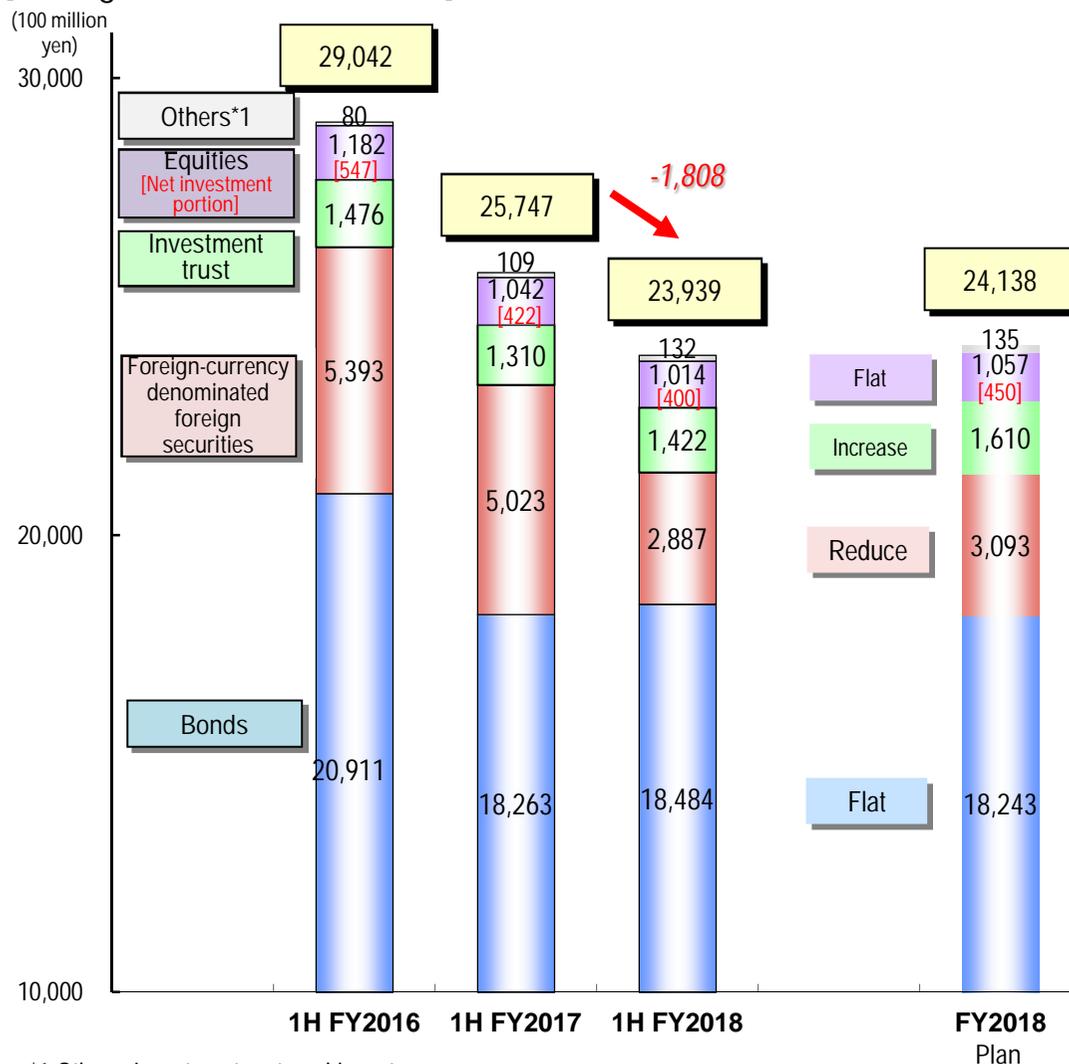
## [Loan/deposit ratio (ending balance basis)]

End of Sep. 2009	End of Sep. 2010	End of Sep. 2011	End of Sep. 2012	End of Sep. 2013	End of Sep. 2014	End of Sep. 2015	End of Sep. 2016	End of Sep. 2017	End of Sep. 2018
64.8%	63.0%	61.5%	61.4%	59.7%	61.0%	63.6%	67.4%	70.5%	70.2%

- In 1H FY2018, the annual growth rate of total loans was +4.5%, due to efforts to increase loans, mainly in local development.
- We will continue to strengthen loans by identifying and capturing fund demand.

# 1H FY2018 Earnings Results –Major Accounts (3) Securities–

[Average balance of securities]



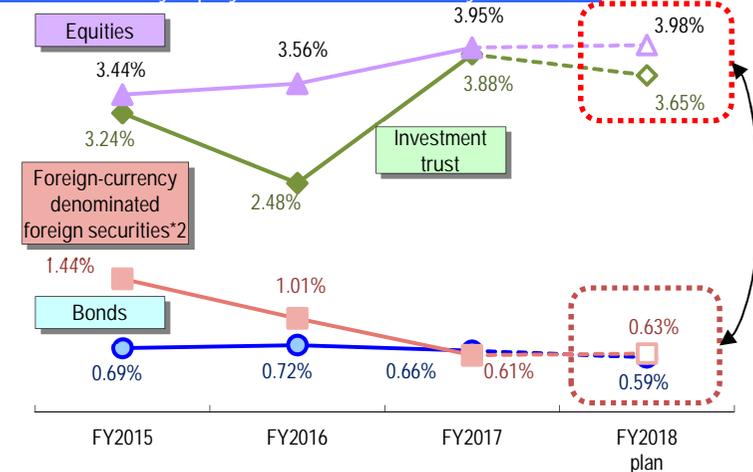
## Measures for improvement in management gains

Implement asset allocation investment with risk and return in mind

- Improve revenue by utilizing investment trusts (mainly equity assets).
- For foreign currency bonds, increase the percentage of variable bonds while reducing the balance.

## Yield and duration by type of investment asset

The drops in domestic and foreign bond yields were covered by equity and investment trust yields.



Duration	1H FY2016	1H FY2017	1H FY2018	FY2018 Plan
Bonds	5.8 years	4.8 years	5.0 years	4.9 years
Foreign currency bonds	5.1 years	3.8 years	4.7 years	4.4 years

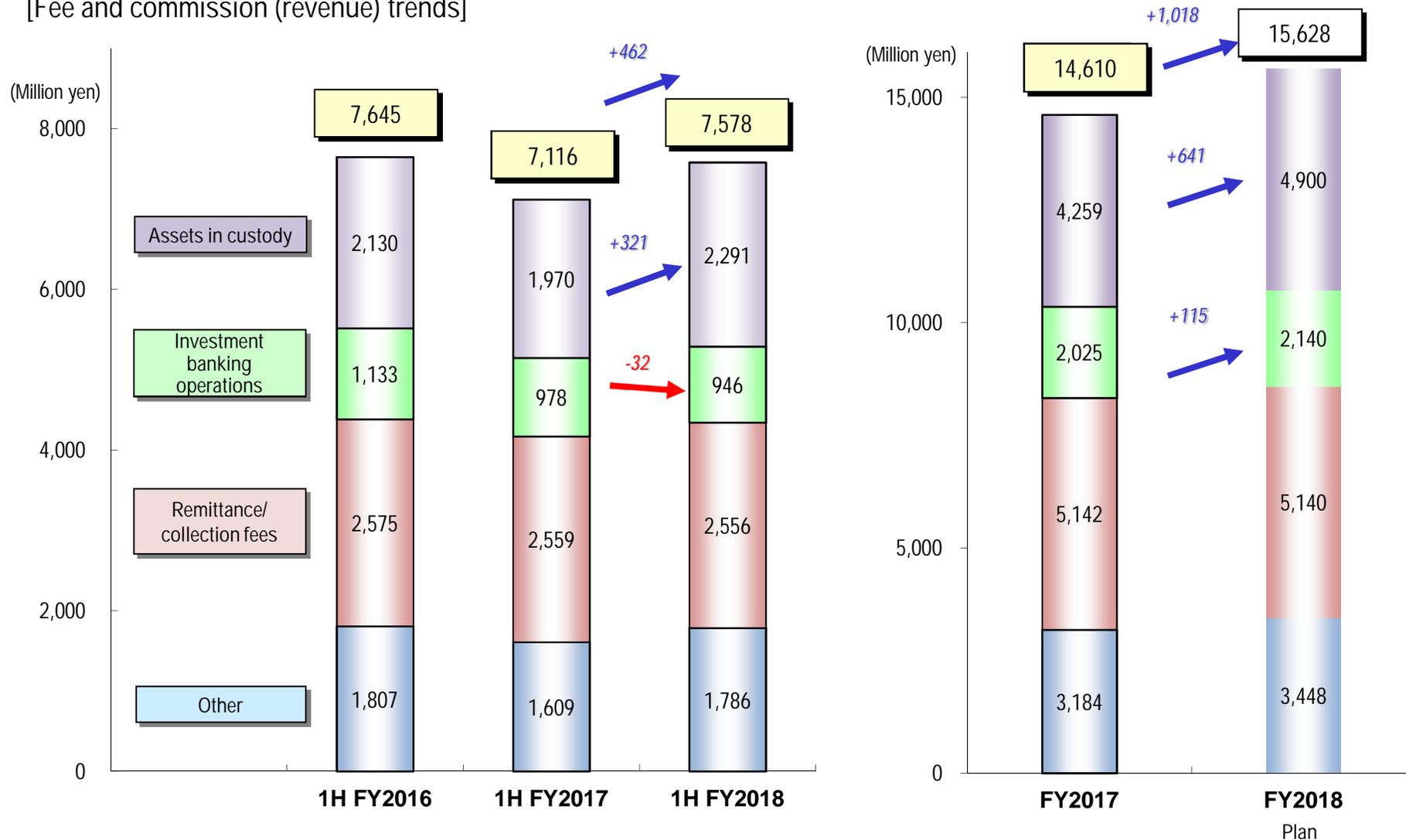
\*1 Others: Investment partnerships, etc.

\*2 Management-procurement spread for foreign-currency denominated foreign securities

- In 1H FY2018, the balance of foreign currency bonds was reduced to take interest rate risk into consideration when investing.
- We will continue to strengthen diversified investments and asset allocation investments while adjusting portfolios flexibly in accordance with the market environment.

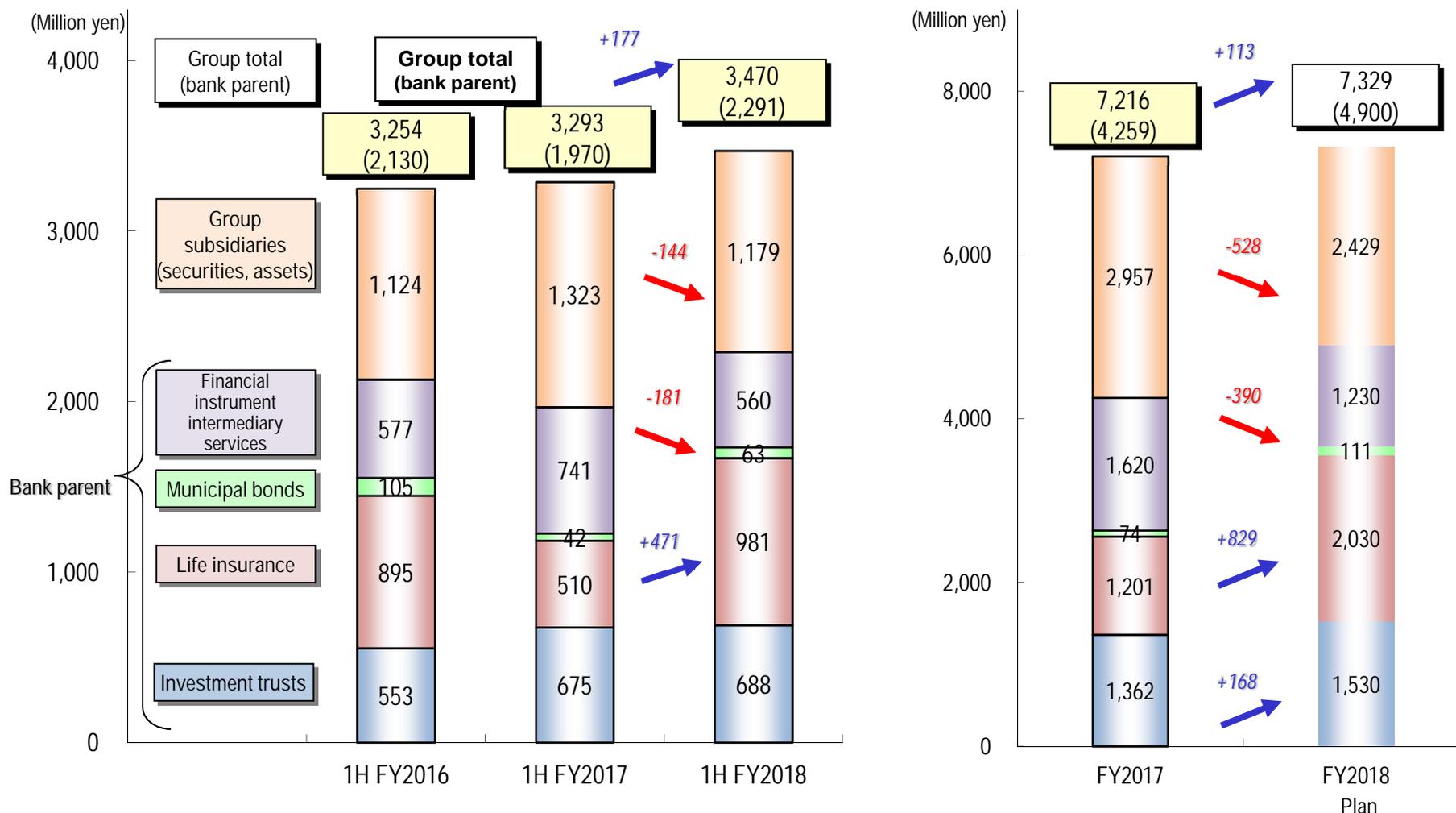
# 1H FY2018 Earnings Results –Change in Fees and Commissions–

[Fee and commission (revenue) trends]



• Fees and commissions revenue increased due to a rise in revenue related to assets in custody.

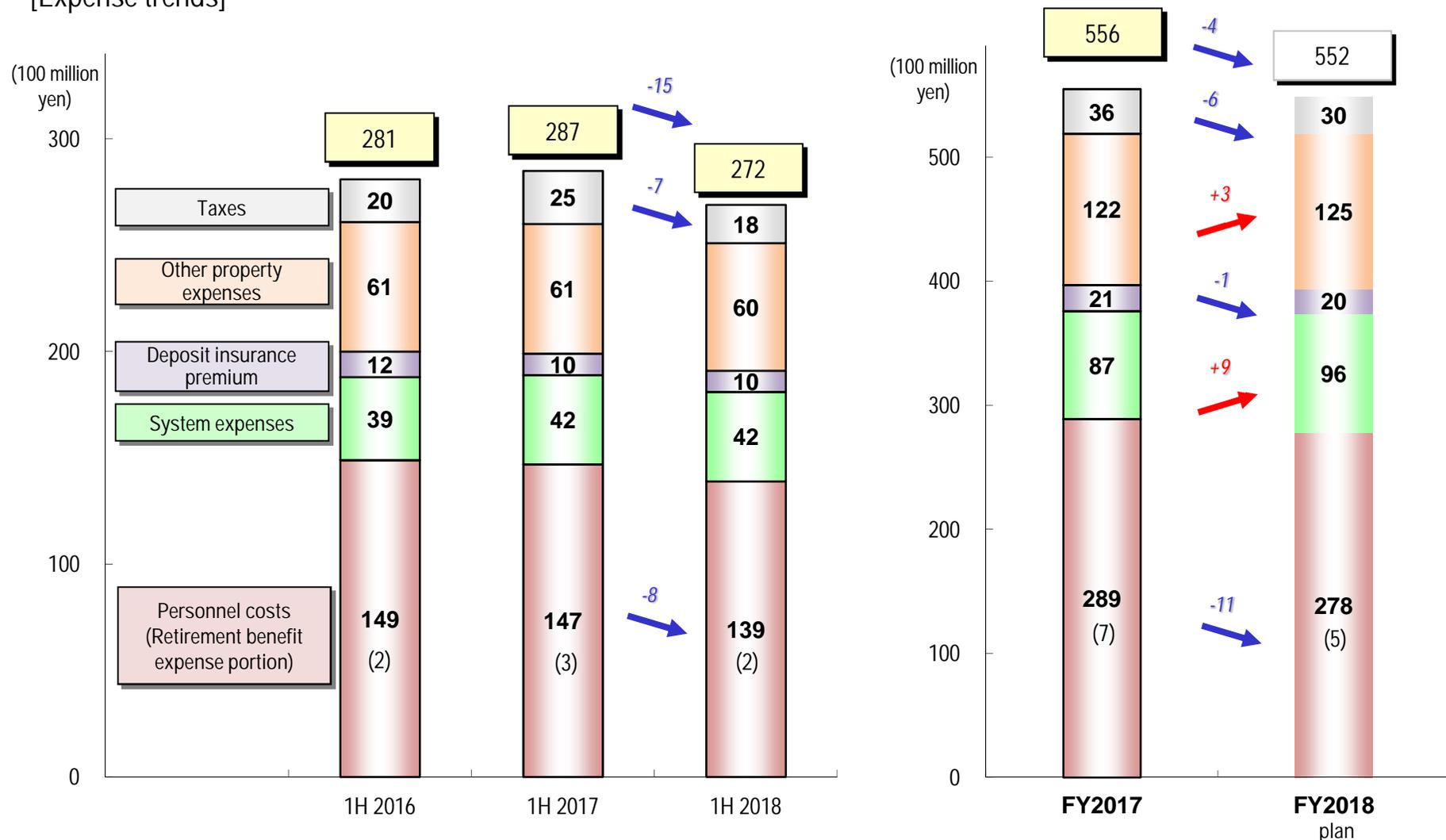
[Revenues related to assets in custody]



- Revenue from assets in custody increased due to a growth in life insurance revenue, despite a drop in financial instruments brokerage revenue on the back of stagnation and uncertainties in the stock market.

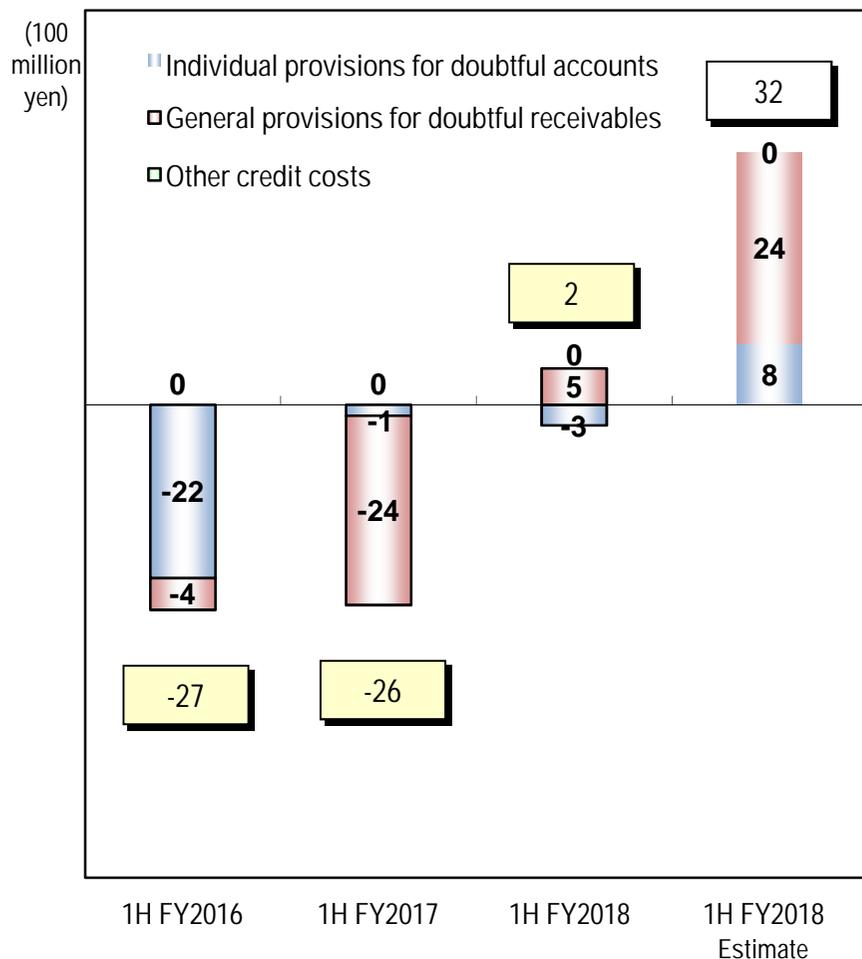
# 1H FY2018 Earnings Results –Change in Expenses–

[Expense trends]



- Personnel costs decreased significantly due to the spread of workstyle reforms as well as a reduction of and improved efficiency in operations.
- Tax decreased due to a drop in consumption tax relating to a new accounting system.

[Credit cost trends]

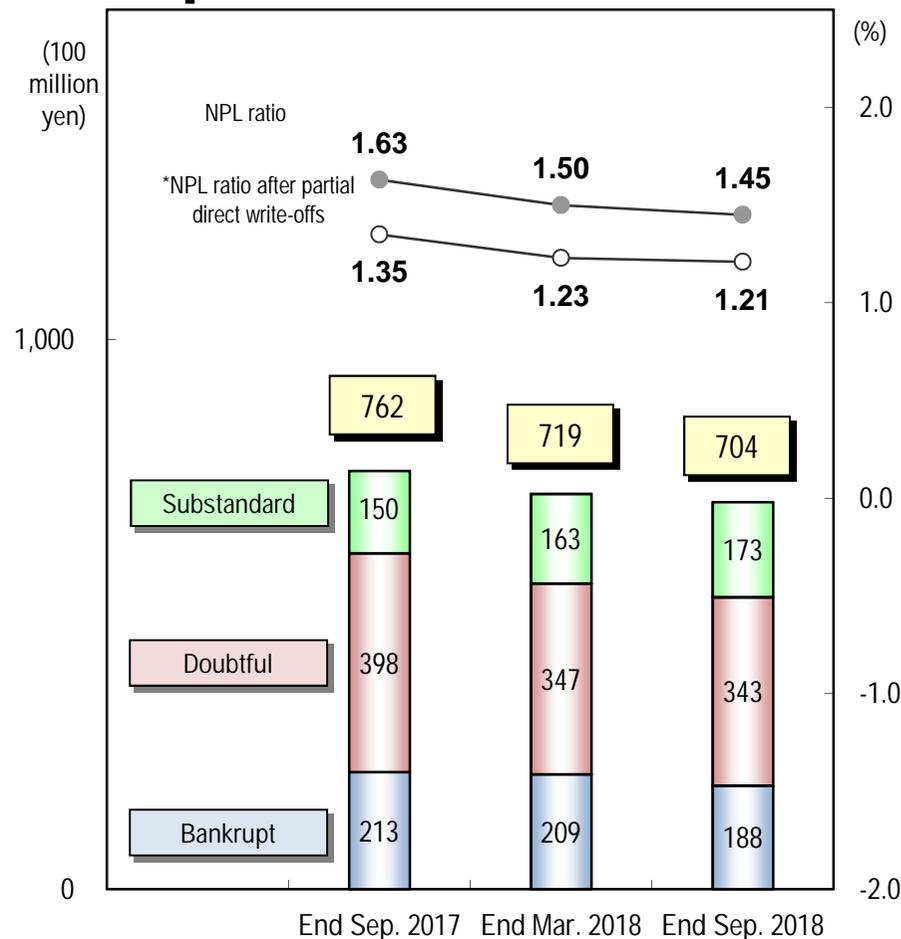


Credit cost = general provisions for doubtful receivables + individual provisions for doubtful accounts + loan write-offs + specific foreign borrowers + provisions for loss on claim sales + loss on claim sales - gain on reversal to loan loss account

Other credit costs = Loan loss write-offs, specific foreign borrowers, provisions for loss on claim sales, loss on claim sales

[Non-performing loan (NPL) trends]

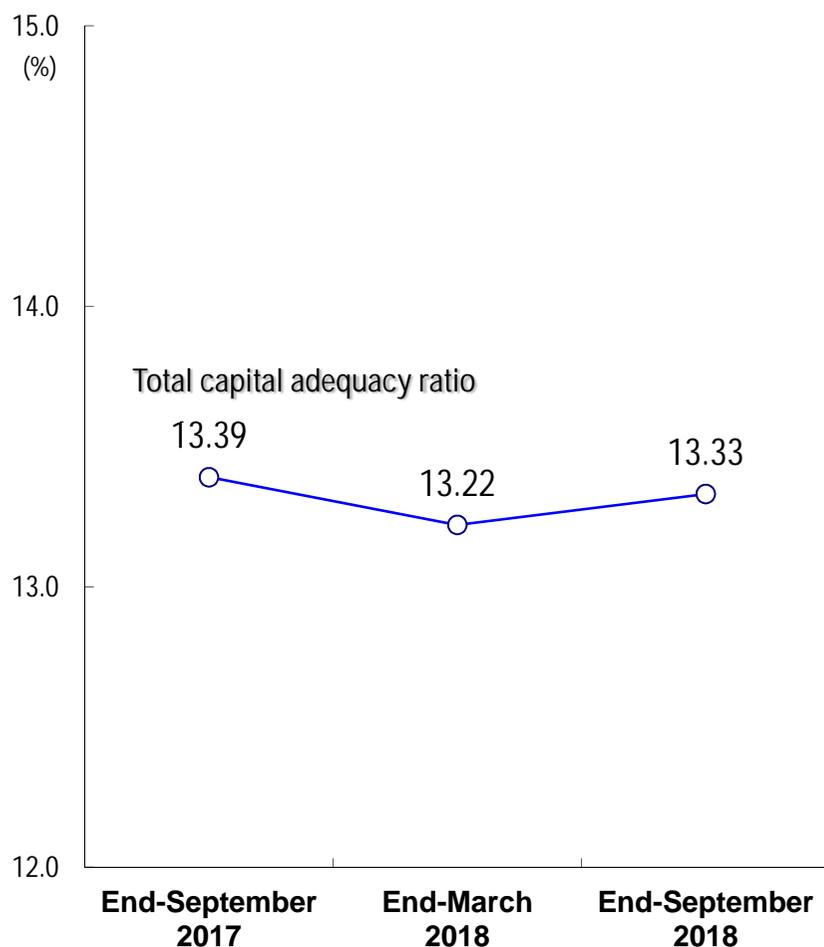
\*We do not implement partial direct write-offs.



- Credit cost increased due to the reversal of general provisions for doubtful receivables, although individual allowances for doubtful accounts continued to be reversed.
- With a continued decline in the NPL ratio, the quality of assets was maintained.

# 1H FY2018 Earnings Results –Capital Adequacy Ratio–

[Capital adequacy ratio (Basel III)  
(consolidated) trends]



[Capital adequacy (consolidated)]

(100 million yen)	FY2017	1H FY2018	YoY
Total equity	5,250	5,336	86
Tier 1, including common shares	5,247	5,334	87
Risk weighted assests, etc.	39,691	40,026	335
Credit risks	38,054	38,413	359
Operational risks	1,637	1,612	-25

[Other Basel regulations]

	FY2017	1H FY2018	<Regulatory standards>
Consolidated leverage ratio	6.03%	6.18%	3% or more
Consolidated liquidity coverage ratio (LCR)	142.9%	155.2%	90% or more

- The total capital adequacy ratio remained at a stable level.

## Section II

# FY2018 Forecasts and Major Initiatives

# FY2018 Forecast –Earnings Forecasts–

[Parent]	FY2017	FY2018		
(100 million yen)	Actual	Plan	YoY	Vs. published forecast at beginning of term
Core business gross profit	795	786	-9	19
Interest income	662	649	-13	38
Fees and commissions	146	156	10	-0
Other operating income	-12	-18	-6	-18
Expenses (-)	556	552	-4	-6
<b>Core business net profit</b>	<b>239</b>	<b>234</b>	<b>-5</b>	<b>26</b>

OHR (%)	69.9	70.2	0.3	-2.6
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Credit expense (+ is reversal (profit))	-17	32	49	12
Bond sales gains/redemption	-24	3	27	-7
Equity sales gains/redemption	44	15	-29	-8
Other	2	4	2	9
<b>Recurring profit</b>	<b>279</b>	<b>225</b>	<b>-54</b>	<b>10</b>
Extraordinary gain/loss	-1	-3	-2	1
<b>Net income</b>	<b>194</b>	<b>154</b>	<b>-40</b>	<b>7</b>

[Consolidated]				
<b>Consolidated recurring profit</b>	<b>309</b>	<b>242</b>	<b>-67</b>	<b>11</b>
Net income attributable to owners of parent	212	162	-50	8

(Year on year)

Profits are expected to drop due to an expected rise in credit cost.

(Vs. published forecast at beginning of term)

Profits are expected to increase from the forecast at the beginning of the term due to an increase in loan interest and a drop in foreign currency procurement cost.

■ Factors relating to changes in interest income, etc.

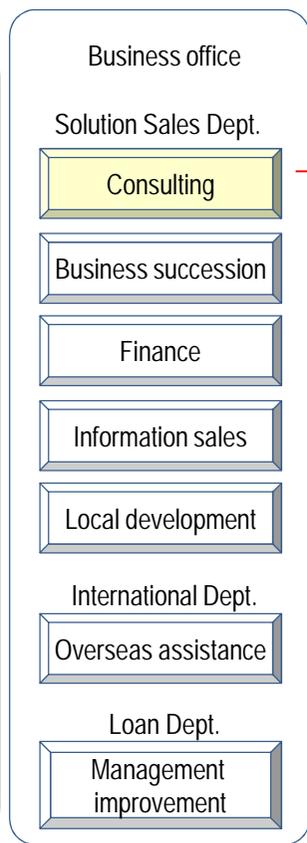
(100 million yen)

	Change (Impact on profit)	
	YoY	Vs. published forecast at beginning of term
Yen-based interest income	-0	+9
Loan interest	+2	+1
Securities interest & dividends	-6	+3
Others (e.g., swap cost)	+4	+5
Foreign currency interest income	-13	+28
Loan interest	+37	+8
Securities interest & dividends	-17	-8
Foreign currency procurement cost	-33	+29
<b>Total interest income</b>	<b>-13</b>	<b>+38</b>
Foreign currency procurement cost included in other business profit	+4	-15

# Improve the Quality of Services Provided —Advance Local Promotion Activities— 中国銀行

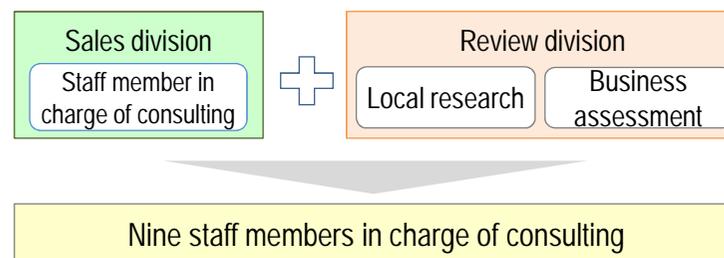
● Strengthen initiatives of “implementing business assessment” ⇒ “supporting through local promotion activities” ⇒ “problem solving through consulting” to enhance local development loans and the fee business.

[Overall image of initiatives for advancing local promotion activities]



[Commencement of business consulting operations]

Established in April 2018 by integrating the sales division and the review division

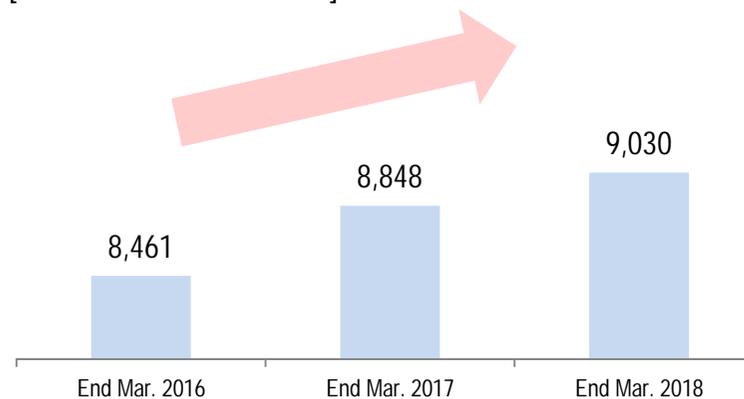


(Main activities)

- Assist formulation of medium-term management plan
- Assist the establishment of a personnel system and/or labor management system in accordance with workstyle reforms

Etc.

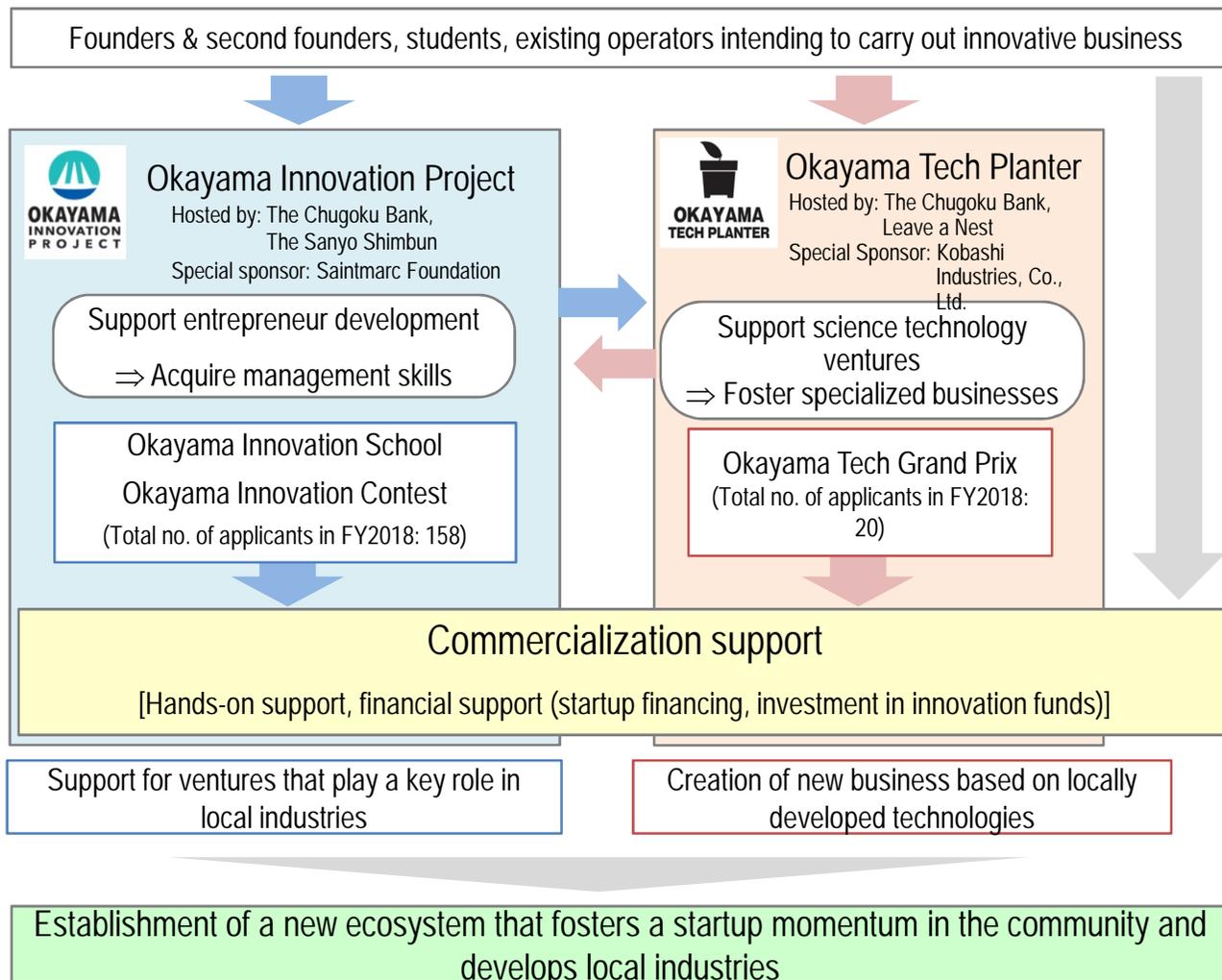
[Number of main clients]



# Improve the Quality of Services Provided —Initiatives in Open Innovation—

- Cooperate with local governments and private operators to build a startup support system around Chugoku Bank.
- Foster future core companies of the local community by discovering entrepreneurs at an early stage and providing hands-on support until commercialization.

[Startup support system]



(Initiatives in Innovation School/Contest)

Opening of Innovation School (10 courses in total)

Opened a school for students and persons wishing to start a company. The school offers management courses by company managers and business school lecturers through lectures and dialogue.

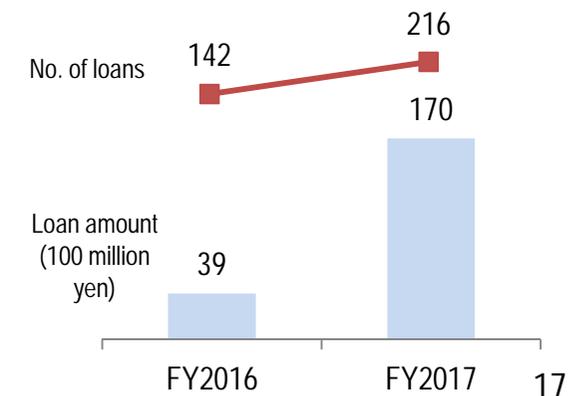


Innovation Contest (Once a year)

A contest by participants selected through screening. Offers brush-up support of business models to participants of the contest.



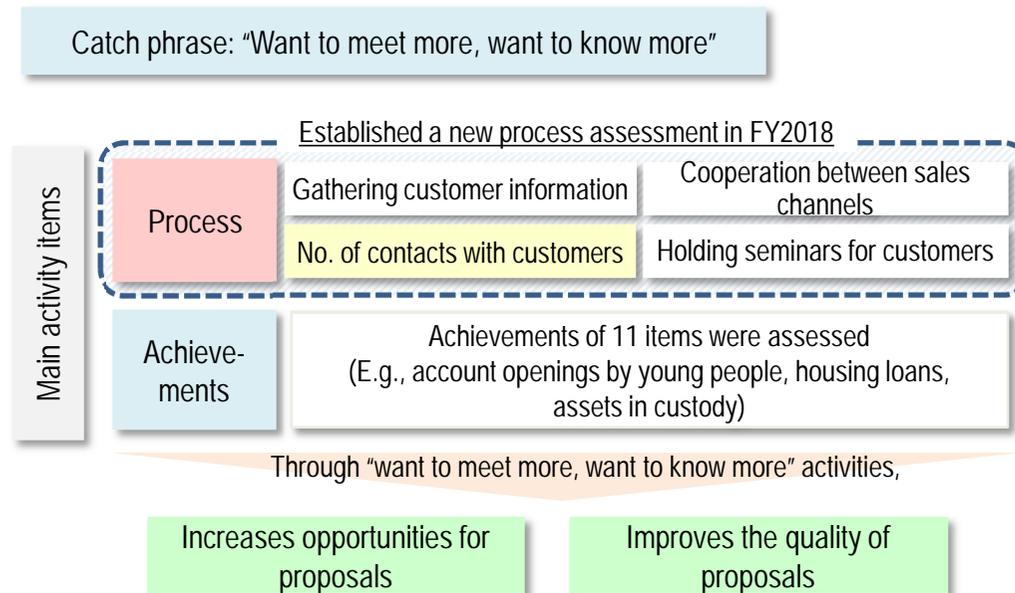
[Track record of startup support financing]



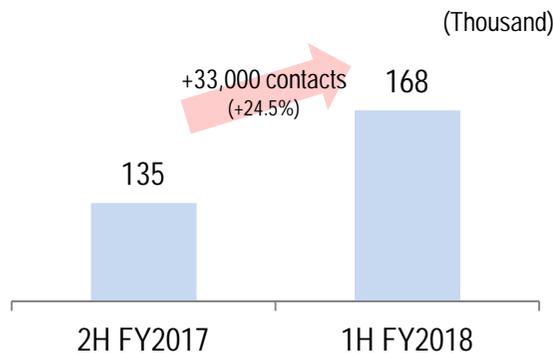
# Improve the Quality of Services Provided — Strengthening Sales Activities Based on Life Planning

- Contact with customers has increased due to the strengthening of “want to meet more, want to know more” activities.
- Face-to-face sales channels on holidays will be enhanced by the establishment of the Life Plan Center.

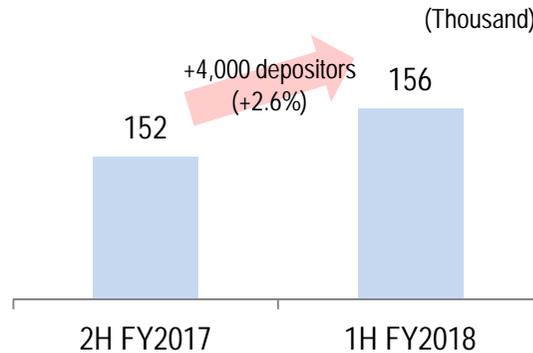
## [Life plan support activities]



[No. of contacts with customers]



[No. of depositors]



## [Establishment of Life Plan Center]

The Housing Loan Center is enhanced and renamed the Life Plan Center (three Centers in the prefecture).

### <Housing Loan Center>

- Consultation point for housing loans
- ⇒ Customers for housing loan contracts were the main visitors.

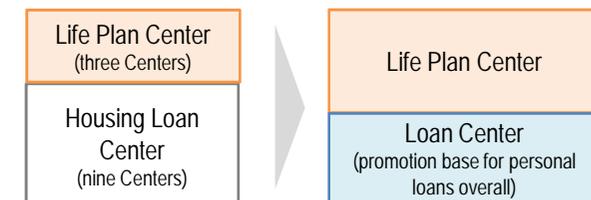
### <Life Plan Center>

- Consultation point for life planning
- ⇒ As the consultation point for loans, asset-building (e.g., iDeCo, installment-type NISA) and insurance, the center supports the life planning of all types of customers.

Examples of activities

- Information provision and needs stimulation through holiday seminars
- Periodic review of household finance of housing loan customers

The functions of the housing loan center will continue to be re-examined according to the market situation.

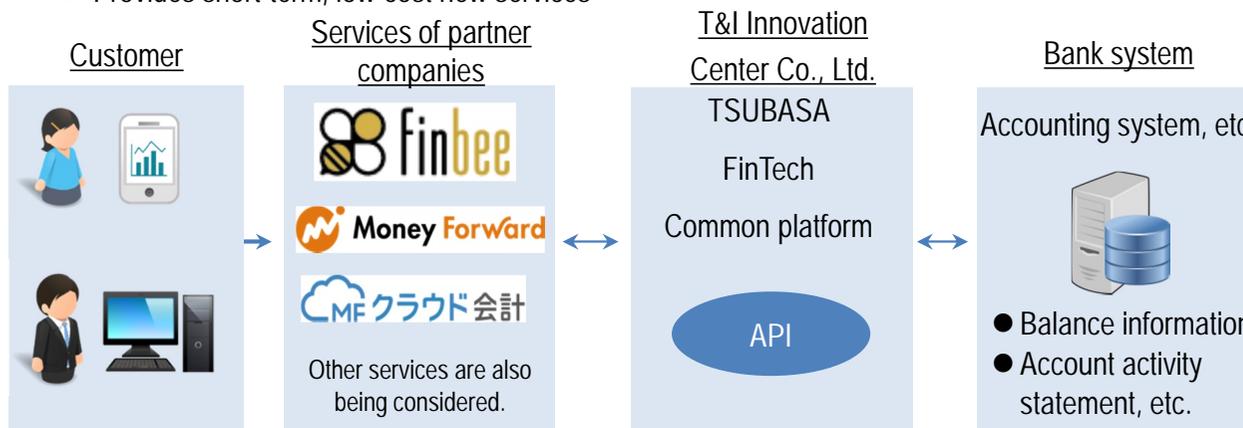


● Enhance services of non-face-to-face channels by utilizing IT channels and AI.

[Establishment of an open AI platform]

October 29, 2018 Start of service

- Provides high value-added services in collaboration with fintech companies
- Provides short-term, low-cost new services



[Utilization of AI, digitalization]

- Promote personal loans using AI

Analyzes big data (transaction statements) using AI

Determines the possibility of a deal and returns the promotion list

Telemarkets from call centers

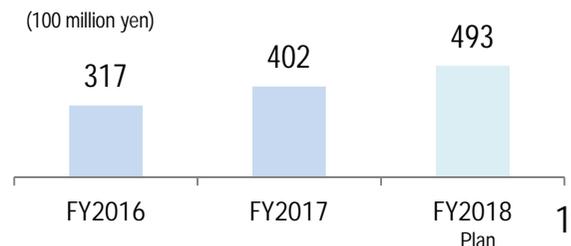


Preferentially approaches customers considered to have high financing needs and supports life planning

- Enables online completion of unsecured loans (scheduled in Jan. 2019)

Improves the convenience of customers by not requiring customers to visit a store or provide their signature/seal.

[Average balance of unsecured loans]



[FinTech Business Contest]

2nd "TSUBASA Alliance Finovation Challenge" (Host: T&I Innovation Center Co., Ltd.)

- Improving the convenience and safety of services for customers through digitalization
- Solving local issues and utilizing local resources with new technology  
⇒ To be held in March 2019; cooperation with participating companies is being considered.

(Performance of the 1st Challenge)  
No. of applications: 119 applications from 110 companies  
No. of companies for final presentation: 6



TSUBASA Alliance (co-host)	Special sponsors

● Formulate store/channel strategies according to changes in the environment and customer needs to increase contact with customers and improve the efficiency of store operation and store counters.

### [Review of store functions]

Environmental changes	<ul style="list-style-type: none"> <li>Population decrease</li> <li>Spread of IT channels ⇒ Changes in customer needs (Money transfers, payments, loan applications carried out online)</li> </ul>
	<div style="border: 1px solid black; border-radius: 15px; padding: 5px; display: inline-block;">Decrease in no. of visitors to stores</div>

Re-establish channels in accordance with changes in the environment and customer needs

- Strengthen the positioning of stores as a face-to-face channel with customers (enhance consultation).
  - Enhance non-face-to-face (e.g., IT) channels for customers whose needs are deposit/foreign exchange and loans.
- ⇒ Achieve operation that combines “increased contact with customers” and “improved efficiency of store operation.”

### (Store/channel strategy)

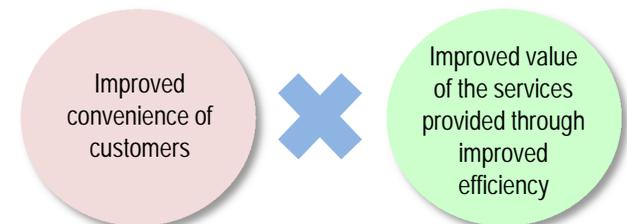
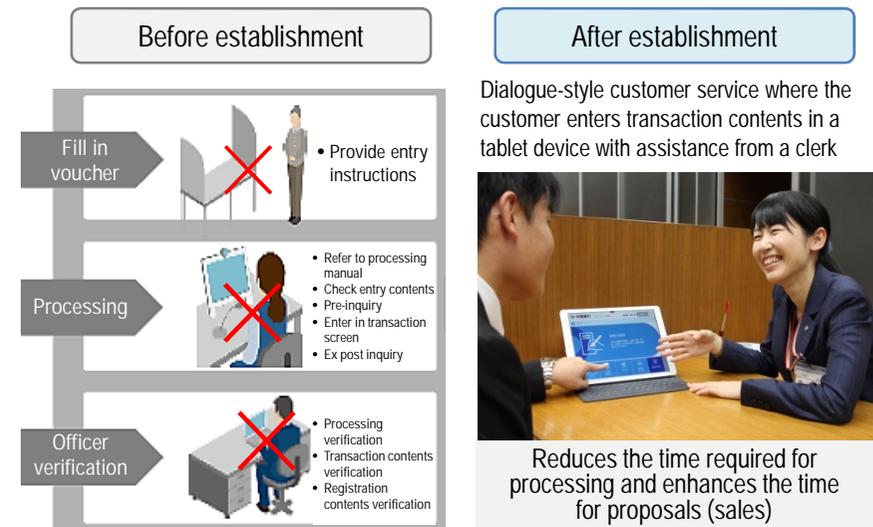
Strengthen sales	<ul style="list-style-type: none"> <li>Review store functions according to market attributes</li> <li>Strategically allocate personnel (quality, quantity)</li> </ul>
Improve CS	<ul style="list-style-type: none"> <li>Strengthen the functions of holiday channels by Life Plan Centers (review the functions of Housing Loan Centers)</li> <li>Enhance IT channel strategies</li> </ul>
Improve efficiency	<ul style="list-style-type: none"> <li>Expand the group sales system (stores specializing in personal loans, lightweight stores)</li> <li>Consider setting flexible business days and business hours</li> <li>Relocate/integrate stores based on a store-within-a-store method</li> </ul>

- Integration based on a store-within-a-store method  
A form of store integration where several branches carry out sales activities in one building  
Improve efficiency by relocating/integrating store functions without abolishing stores

### [Review of stores]

Establish counter reception tablet, “TSUBASA Smile” (scheduled May 2019)

Joint development by three TSUBASA banks—The Chugoku Bank, Chiba Bank and The Daishi Bank



- Generate sales personnel and time through thorough structural reforms, leading to enhancement of the top line and reduction of OHR.

## Headquarters

### Reduce operations of the headquarters, and implement workstyle reforms

- ✓ Introduce an electronic workflow system
  - ✓ Eliminate the use of paper by developing a wireless LAN environment and distributing tablet devices
- Increase in personnel during the current medium-term management plan period: 110 ⇒ Actual performance: Approx. 100

## Loans

### Operation of the Loan Administration Center

- ✓ The Loan Administration Center was established.
    - Centralization of loan administration work started in October. The process of centralization will be expanded to all offices by end of March 2020.
- Increase in personnel during the current medium-term management plan period: 40 (150 by end of March 2021) ⇒ Actual performance: Approx. 30

## Deposit & foreign exchange, store

### Execution of store operation reforms

- ✓ Improve operations through introduction of store tablets and significant simplification/centralization of administrative work
    - Reduce employees' administrative work at counters and have them concentrate on financial services
- Increase in personnel during the current medium-term management plan period: 30 ⇒ Actual performance: Approx. 30

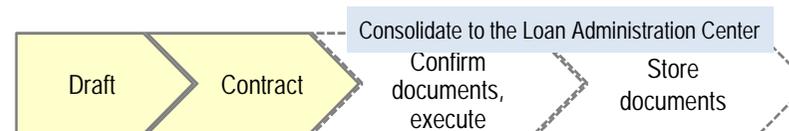
## Sales

### Execution of sales activity reforms

- ✓ Introduce tablets for negotiation
    - This enables access to information and sale of assets in custody during visits to customers, reducing the burden of administrative work upon returning to the office. Installed with a map information system, the tablets allow more efficient sales activities.
- ⇒ The no. of customer visits by external sales representatives is expected to increase by 30–40%.

## Image of the Loan Administration Center

### Work process of business offices up to the execution of loans

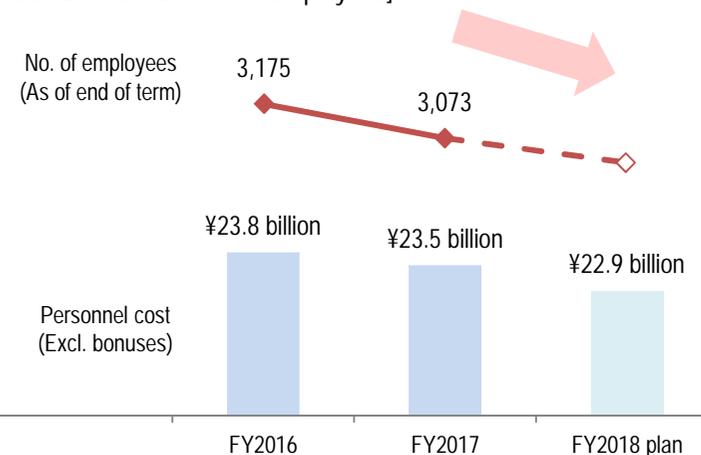


Reduce personnel in charge of loan administration at business offices ⇒ Re-allocate to sales

## Business offices

## Cost reduction effects

### [Personnel cost and no. of employees]



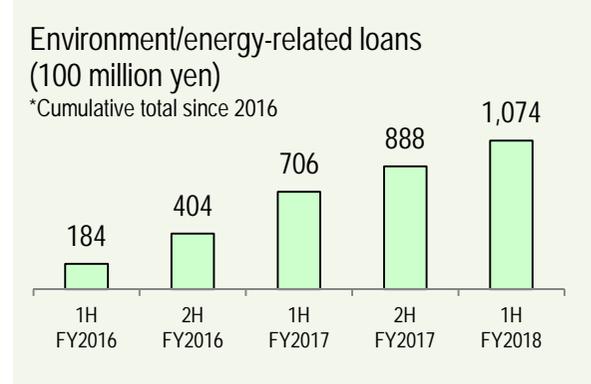
The FY2018 plan expects personnel cost to be reduced by 0.6 billion yen year on year, mainly due to personnel decrease (natural decrease) and reduction of overtime work through the reduction and improved efficiency of work.

● Aim for the long-term and sustainable improvement of corporate value through ESG initiatives.

## Environment

- Implement initiatives in environmental issues through conventional corporate activities.
- Consider the rise in renewable energy and agribusiness-related demand as a business opportunity and allocate personnel within the headquarters.
- Solve environmental issues through financial solutions.

\* Examples of solutions  
 Environment/energy-related loans, eco private placement bonds, sixth industry support, Chugin Argi-Support Fund, hosting various seminars

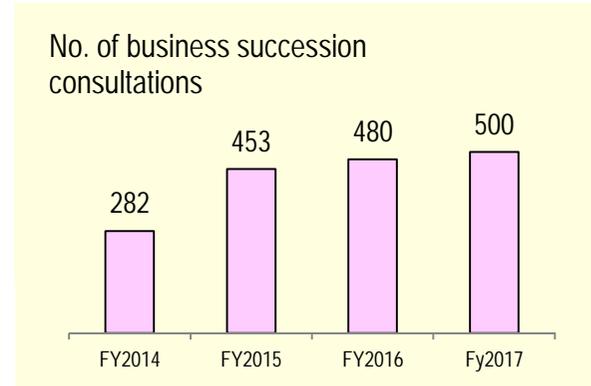
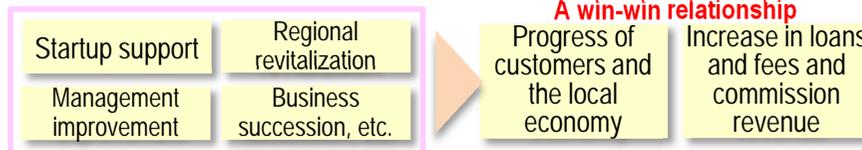


## Social



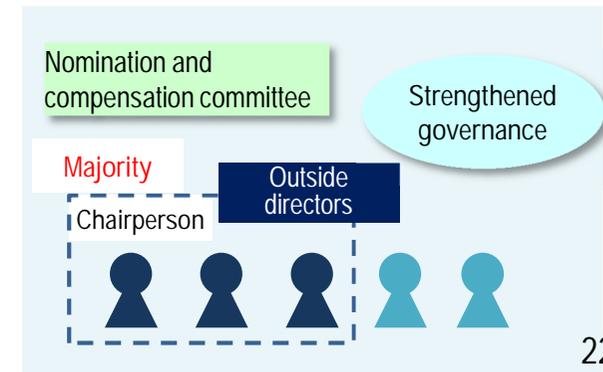
- Started local promotion activities in October 2015.

Local promotion activities : Positioned as a core business of the Bank and adopted in performance assessments



## Governance

- Percentage of outside directors: 35.3% (As of September 30, 2018)
- Established a nomination and compensation committee (December 22, 2017)
  - Chaired by an outside director, the committee carries out appropriate deliberations.
- Respond to the corporate governance code
  - Grasp capital costs → Consider reviewing the possession of strategically held stocks



# Impact of the 2018 Japan Floods and Initiatives of the Bank

The 2018 Japan Floods caused significant damage from floods and landslides in many regions, mainly in western Japan. Local economies were also affected by heavy rainfall, with some companies and individual businesses forced to temporarily suspend business. However, production activities recovered in general through swift restoration aid under cooperation between the government and the private sector. Consumer spending and capital expenditure were also robust, bringing the economy on a mild recovery path.

Damage in Okayama and Hiroshima Prefectures	Human damage	Okayama		Hiroshima		Damage to dwellings	Okayama		Hiroshima					
		Deaths	Missing	Serious/mild injuries	Complete collapse		Half collapse	Partial damage	Inundation above floor level	Inundation below floor level				
		66	3	161	108	6	127	4,822	3,282	1,118	2,731	2,926	6,116	5,009

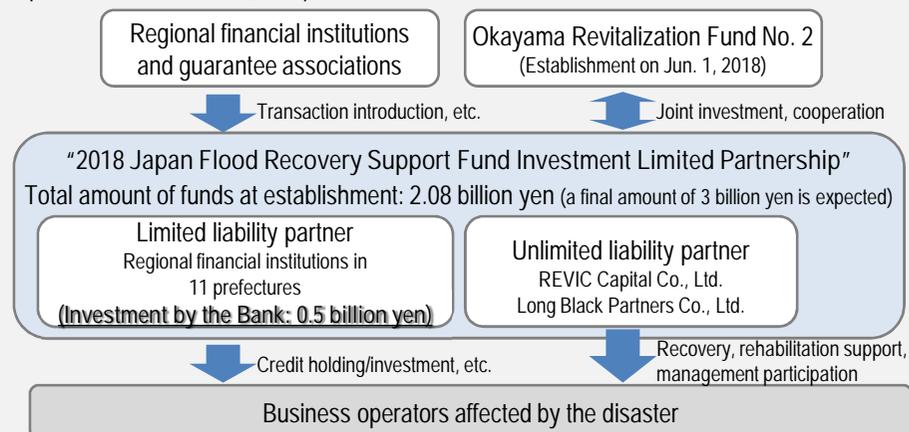
\* Published figures by Okayama and Hiroshima Prefectures as of Nov. 9, 2018

Damage to the Bank	Human damage	Store damage
	No deaths or missing persons	Five stores (the Mabi Branch, Hirajima Branch, Oda Office, Konkou Branch, and Yoshii Branch) were affected. ⇒ Four stores except for the Mabi Branch resumed operation on the following business day. The Mabi Branch operated at a temporary store but resumed operation at its original store on October 1.

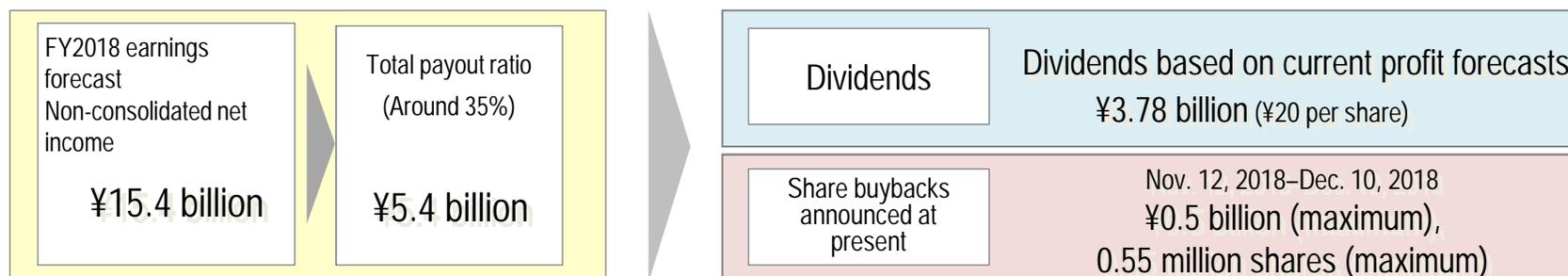
## [Major initiatives of the Bank]

- Initiatives in restoration assistance financing (e.g., business loans, housing loans, private placement bonds, etc.)
- Establishment of a syndicated loan system with the Japan Finance Corporation
- Group subsidy application support
- Establishment of a new financing system, the Chugin Group Subsidy Bridge Loan
  - Established a new bridge loan system to meet funding needs for the period between the decision of granting a Group subsidy and the granting of the subsidy
- Providing donations
- Support for the sites affected by the disaster
- ✓ Established a 2018 Japan Floods recovery support center within the headquarters
  - Consolidated the functions of the headquarters and departments and provided swift response to support early recovery and the restoration of customers

## ● Establishment of the 2018 Japan Flood Recovery Support Fund (establishment on Oct. 31, 2018)



Planning shareholder return of a 35% total payout ratio, which includes annual dividends (20 yen per share) and share buybacks



## [Shareholder returns]

	Non-consolidated net income [1]	Total dividends		Payout ratio [2] ÷ [1]	Share buybacks [3]	Total payout ratio ([2] + [3]) ÷ [1]
		Per share (interim)	[2]			
FY2018 (Plan)	154	¥20 (¥10)	37.8	24.5%	-	about 35%
FY2017	194	¥20 (¥10)	38.1	19.6%	30	35.1%
FY2016	190	¥20 (¥10)	38.5	20.3%	29	35.5%
FY2015	259	¥20 (¥10)	39.2	15.1%	52	35.2%
FY2014	209	¥18 (¥8)	35.6	17.0%	33	32.8%

\*Share buyback as a factor in calculating payout ratio: Calculated based on buybacks during one year from time of shareholders meeting.



This document includes forward-looking statements. These statements are not a guarantee of future performance, and involve risks and uncertainties. Note that future performance could possibly differ from the goals and targets herein due to factors, including changes in the business environment.