Daiwa's View

April BOJ *Financial System Report*

➢ Key is how to block negative feedback loop of "synergetic worsening of real economy and financial sector"

Fixed Income Research Section
FICC Research Dept.

Economist
Kenji Yamamoto
(81) 3 5555-8784
kenji.yamamoto@daiwa.co.jp

Daiwa Securities Co. Ltd.

April BOJ *Financial System Report*

Key is how to block negative feedback loop of "synergetic worsening of real economy and financial sector"

On 21 April, the BOJ announced its *Financial System Report (FSR)*. This report is issued by the Financial System and Bank Examination Department twice a year to assess the stability of the financial system. This time, the format and volume were changed, while the global outbreak of COVID-19 has been influencing global financial markets and the real economy significantly since late February 2020. The data was augmented by "information obtained from the BOJ's off-site monitoring."

In the previous two issues, the BOJ warned against the vulnerabilities of the financial system in the future by pointing out the "downtrends in the profitability and capital adequacy ratios of regional financial institutions" amid prolonged low interest rates and the decline in domestic deposit-taking and lending activities. In other words, the focus was put on the contagion risk from the financial sector to the real economy in the case of the prolongation of the financial environment of the time.

However, the global economy was suddenly hit by the COVID-19 pandemic, and it will likely become "the worst recession since the Great Depression (IMF)", meaning "the materialization of downside risks to the economy (previous *FSR*)." In such a situation, the theme of the latest *FSR* is how robust Japan's financial system will be against the "contagion risk from the real economy to the financial sector."

◆ April 2020 *Financial System Report*

・Despite undergoing great stress, Japan's financial system has been maintaining stability on the whole and continues to provide the funds essential for economic activities. Nevertheless, significant uncertainty remains about future developments regarding the global spread of COVID-19 and the resulting magnitude and duration of downward pressure on the real economy.

That said, the BOJ assessed the Japan's financial system as it has "been maintaining stability on the whole" similar to the previous issue. This is in line with BOJ governor Haruhiko Kuroda's greeting remark at the branch managers' meeting. Meanwhile, the report stated that the financial system is also "undergoing great stress."

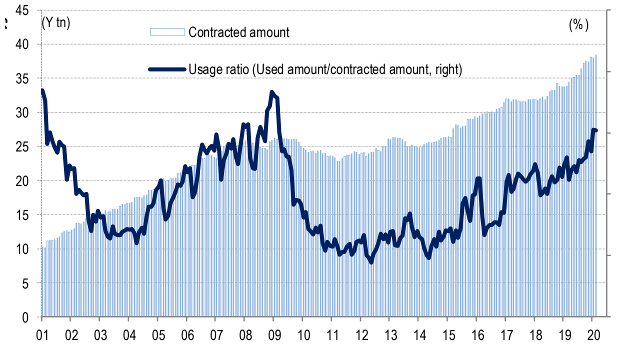
■ ◆BOJ governor Haruhiko Kuroda (9 Apr 2020)

・Investors' risk sentiment worsened and rapidly became unstable in the financial and capital markets at home and abroad. Amid aggressive responses by each nation's central bank, tension in the financial market has eased somewhat, but nervousness remains. The Japanese financial system is largely maintaining stability. However, looking at the financial environment, corporate financing is worsening.

In fact, the section of "current assessment" of the financial and capital markets and financial intermediation pointed out that "CP issuance rates are showing increases as of the beginning of April," and "the outbreak of COVID-19 has caused a sharp tightening of funding conditions, especially among small and micro nonmanufacturing firms with limited cash availability, particularly in such sectors as food services, accommodations, and retail," based on latest information (incl. that obtained from BOJ's off-site monitoring).

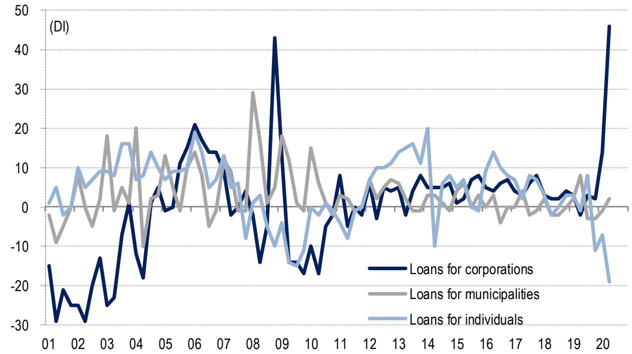
The report also says that "An increasing number of major firms have been taking actions to raise funds and establish or increase their commitment lines, some of which are led by precautionary motives to meet future needs." Such rapidly growing demand for loans is confirmed also by a surge in the DI to judge corporate loan demand in the BOJ's "Questionnaire survey on major banks' lending trends," announced on the same day.

Chart: Contracted Amount of Commitment Lines and Usage Ratio



Source: BOJ; compiled by Daiwa Securities.
Note: Feb 2020 data is the latest.

Chart: DI to Judge Loan Demand in Questionnaire Survey on Major Banks' Lending Trends



Source: BOJ; compiled by Daiwa Securities
Note: Latest figures are forecasts.

Regarding the global financial markets, the report says that "investors' increased preference for safe assets has accelerated the growing demand for US dollar cash. Against this background, US dollar funding premiums have spiked and strains in US money markets in particular have intensified," and "the global outbreak of COVID-19 has led to an increase in the drawdown of commitment lines, particularly by major firms overseas in such sectors as air transport, accommodations, automobiles, and their related retailers." As for procurement of the dollar, the US dollar liquidity swap line was expanded in March by major central banks led by the Fed. However, the report pointed out that "it is necessary to closely monitor the future lending attitudes and developments in profitability of Japanese banks, as the availability and costs of US dollar funding remain unstable due to strains in US dollar money markets" (refer to BOX at end of this report).

Under this recognition of the current condition, the main topic of the latest *FSR* is to assess the "implications and risks for financial stability arising from the COVID-19 outbreak" both in terms of quality and quantity. In particular, the major difference from previous reports is the emergence of the contagion risk from the "shock to the real economy (COVID-19 pandemic)" to the financial system.

In short, key is the degree of the risk that an "exogenetic shock" (deterioration of real economy) will turn to an "endogenous risk" via dysfunctinoal financial intermediation. In the latest *FSR*, the BOJ has warned against this negative feedback loop between the real economy and the financial sector, calling it a "synergistic worsening of the real economy and the financial sector."

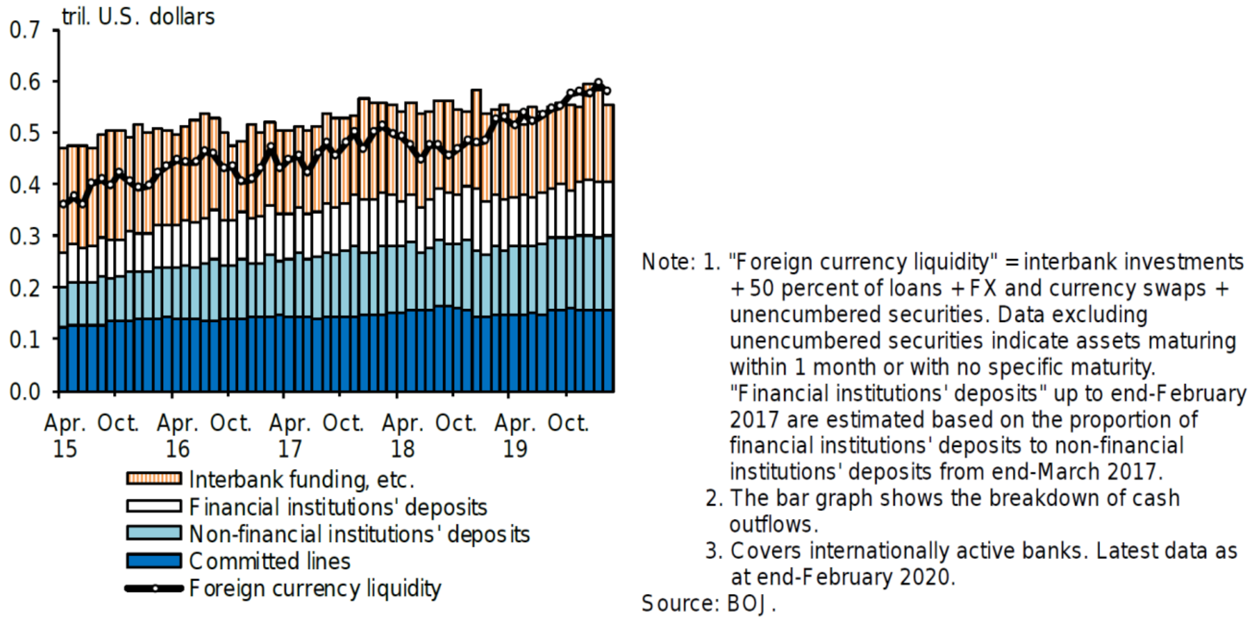
◆ **April 2020 *Financial System Report***

・The currently observed stress on the financial system originates from the shock to the real economy caused by the wide range of constraints on people's physical activities due to the disease outbreak. Thus, the root cause of the current stress and its transmission mechanism significantly differ from stresses in the past caused by the bursting of bubbles triggered by and resulting in the adjustment of financial imbalances.

The report pointed out three risks that could give rise to "synergistic worsening." Specifically, such risks are (1) a rise in credit costs due to economic downturns at home and abroad, (2) gains/losses on securities investment deteriorating due to substantial correction in financial markets, and (3) destabilization of foreign currency funding due to the tightening of foreign currency funding market.

The latter two are risks related to overseas investment. Amid the downtrend of domestic deposit-taking and lending activities, domestic financial institutions have recently been increasing investment/loans of overseas credit. Therefore, the correlation between the Japanese financial system and the global one has been strengthening, meaning that risks can propagate more easily between overseas and Japan's financial systems. In particular, as "it is of paramount importance to ensure foreign currency liquidity in times of stress," an urgent theme is to improve resilience to liquidity stress on dollar funding.

Chart: Resilience to Foreign Currency Liquidity Stress Among Major Banks

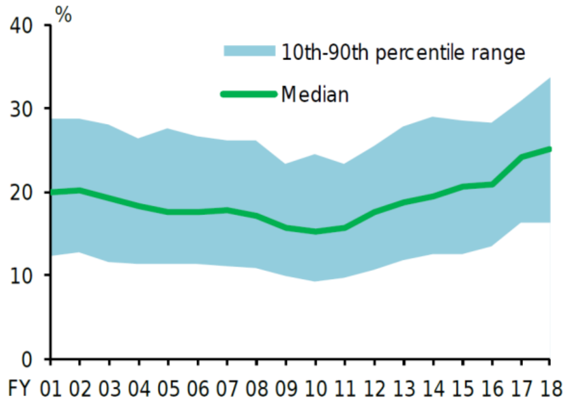


Source: Extracted from BOJ FSR (Apr 2020).

A big portion of the *FSR* is dedicated to the risk of an increase in credit costs from economic deterioration. For example, the previous *FSR* emphasized that credit costs have increased and that financial institutions need to pay more attention to the impact on credit costs from the realization of downside risks to the economy.

In its most recent report, it noted that with the COVID-19 pandemic having led to a realization of these downside risks to the economy, it has quickly become much harder for corporations to get funding, as described earlier. Furthermore, because in their reach for yield domestic financial institutions have more aggressively taken on risks, such as by lending to mid-risk companies, if the economy weakens at an accelerated rate there is a possibility that credit costs will increase beyond what has been provisioned for.

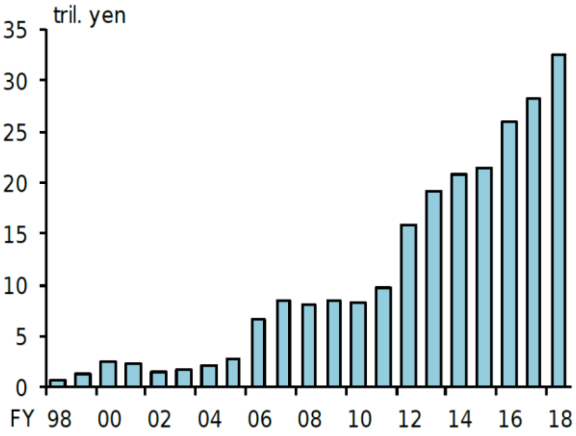
Chart: Loan Share of Low-Return Borrowers Among Financial Institutions



Note: Covers major banks and regional financial institutions.
Source: Teikoku Databank.

Source: Extracted from BOJ FSR (Apr 2020).

Chart: Amount of Firms' Goodwill



Note: Covers firms listed on the domestic stock exchanges.
Source: Development Bank of Japan.

Source: Extracted from BOJ FSR (Apr 2020).

The latest report also noted that in the real estate market, where lending has increased recently, the spread of the new coronavirus is causing risks to materialize through a softening of real estate supply-demand and decline in rental incomes, and that if an increase in lending on highly leveraged deals, such as for large M&A deals, triggers credit events, the risks could spread throughout the financial system via the corporate bond market.

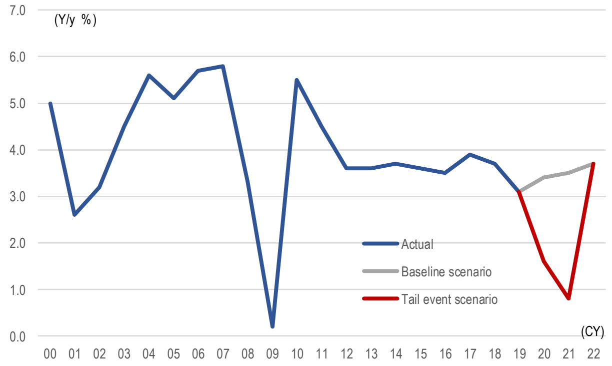
In other words, previous *FSR*s discussed the vulnerabilities brought by financial institutions' various efforts in search of yield aimed at avoiding declines in profitability and capital ratios caused by the prolonged low-rate environment, and the latest report warned strongly about the possibility of the exogenetic shock from the COVID-19 pandemic leading to the sudden eruption of the risks from these vulnerabilities.

While it makes a persuasive case for all of these risks, it is difficult to get across their extent and level of seriousness just by listing them. To do that, it uses a quantitative approach based on macro stress testing. As in previous reports, the BOJ looks at both a baseline scenario and a tail event scenario, and it found that even in a tail event scenario, which envisions an economic shock on the order of what occurred in the global financial crisis, Japan's financial institutions on the whole are highly resilient.

It is important to note regarding the stress tests, however, that the assumptions underlying the baseline scenario represent conditions that prevailed prior to COVID-19 becoming a pandemic, i.e., in January 2020. This means the tail event scenario is closer to being the baseline scenario, and given that many now expect this to result in the biggest downturn since the Great Depression, beyond the contraction caused by the global financial crisis, even the tail event scenario may be optimistic[1].

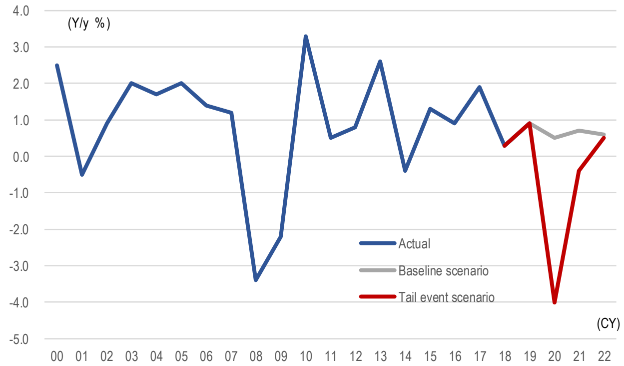
[1] Looking at the macro stress test data for each scenario, under the tail event scenario, the real economic growth of overseas economies is 1.6% in CY2020, while Japan's real GDP growth for FY2020 is -4.0%. In its *World Economic Outlook* published on 14 April, however, the IMF forecast real GDP growth of -3.0% for the world economy and -5.2% for Japan (in both cases for CY2020), worse than the BOJ's tail event scenario. The IMF also has three other scenarios more pessimistic than its baseline scenario.

Chart: Assumptions for Overseas Real GDP Growth Rate Under Stress Testing



Source: BOJ FSR (Apr 2020); compiled by Daiwa Securities.

Chart: Assumptions for Japan's Real GDP Growth Rate Under Stress Testing



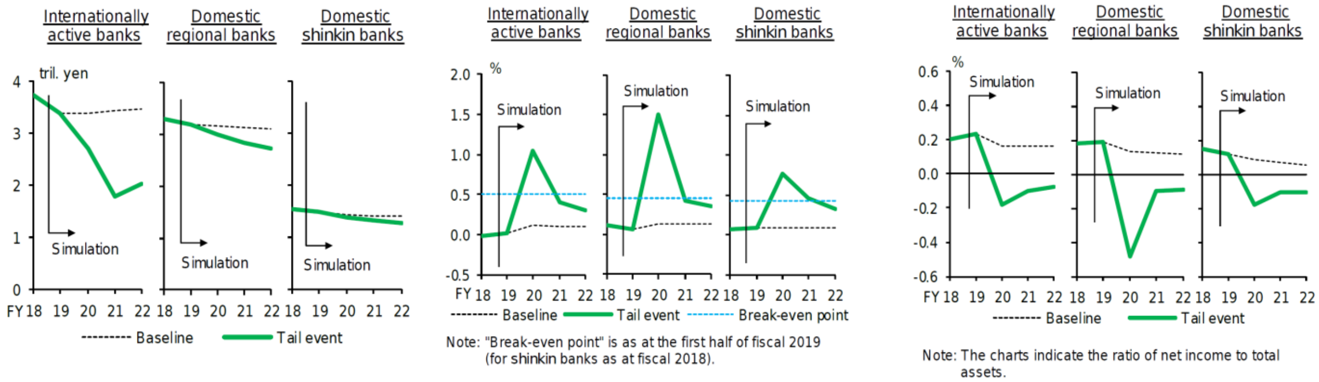
Source: BOJ FSR (Apr 2020); compiled by Daiwa Securities.

Under its tail event scenario, "net interest income declines substantially, reflecting sluggish loan demand and a narrowing of lending margins under the deterioration in the domestic and overseas economies." and "as a result, net income decreases substantially and remains in deficit for three consecutive years." The BOJ expects the worsening of credit costs ratios to be particularly bad for banks under domestic regulations, which have loan portfolios heavily weighted toward low-return borrowers, and sees those ratios rising to levels that are "high by historical standards."

Although the *FSR* does note that the decline in share prices and appreciation of the yen have not exceeded what occurred in the global financial crisis, it also notes that because the COVID-19 pandemic is an economic shock originating in the real economy, the source of stress and its transmission path is considerably different. This makes it necessary to keep in mind the possibility that risks will exceed the simulated results in this test.

Chart: Simulation Results of Macro Stress Testing

Net Interest Income | **Credit Cost Ratios** | **Net income**

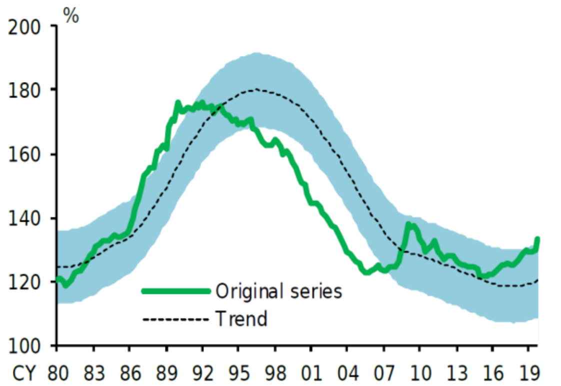


Source: Extracted from BOJ FSR (Apr 2020).

Additionally, in its heat map showing the extent of overheating in the financial cycle, the "total credit to GDP ratio" turned red for the first time since 1991. Much of this signal can be attributed to the large decline in the denominator, Oct-Dec 2019 GDP, caused in part by the consumption tax hike. As acknowledged in the *FSR*, however, the downward trend in this metric since the bursting of the economic bubble in the 1990s can be attributed to the declines in Japan's potential and expected growth rates.

That is, when considering the direction of the financial cycle, it is probably important to watch for whether the COVID-19 crisis leads to a further downward shift in Japan's potential and expected growth rates. The report also noted that financial institutions should cope with "challenges with regard to structural issues such as the prolonged low interest rate environment, the population decline, and excess savings in the corporate sector, the nature of which might be affected by changes in economic activity and corporate behavior due to the COVID-19 outbreak."

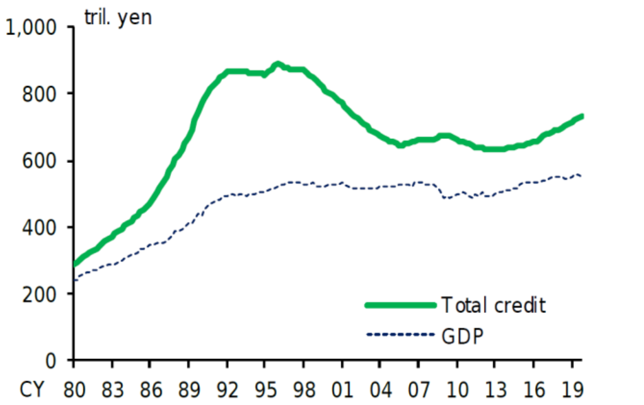
Chart: Total Credit to GDP Ratio



Note: 1. "Trend" is calculated using the one-sided HP filter. The shaded area indicates the root mean square of the deviation from the trend.
2. 4-quarter backward moving averages. Latest data as at the October-December quarter of 2019.
Source: Cabinet Office, "National accounts"; BOJ, "Flow of funds accounts."

Source: Extracted from BOJ FSR (Apr 2020).

Chart: Numerator and Denominator of Total Credit to GDP Ratio



Note: 1. "GDP" is in nominal terms.
2. Latest data as at the October-December quarter of 2019.
Source: Cabinet Office; BOJ.

Source: Extracted from BOJ FSR (Apr 2020).

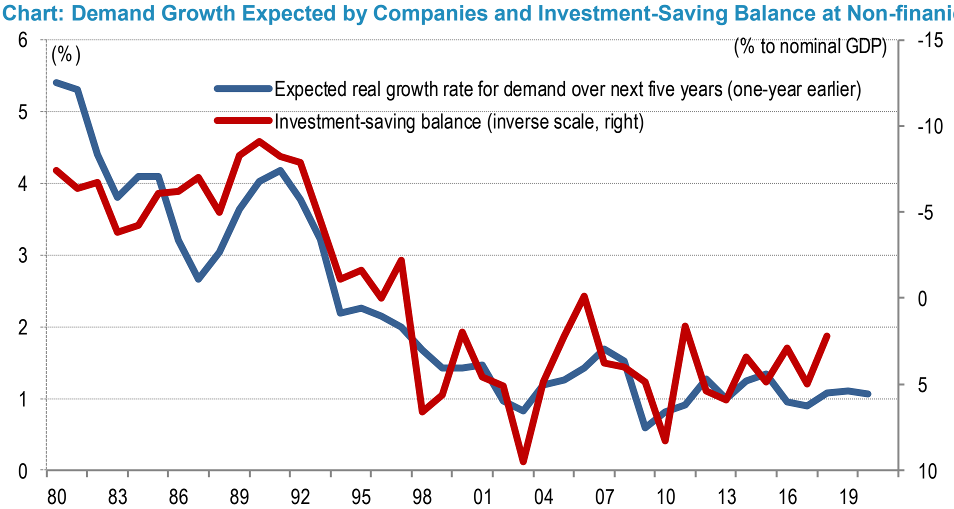
As was the case during Japan's lost two decades following the bursting of the bubble and also in the aftermath of the global financial crisis, the structural changes from corporations lowering their growth expectations and increasing their propensity to save are initially triggered by cyclical economic shocks. When such shocks last for an extended period, delaying the recovery from the recession following the shock, it causes permanent damage to GDP (the hysteresis effect).

◆ **April 2020 *Financial System Report***

・Domestic and overseas financial systems had accumulated various vulnerabilities due to the search for yield under the prolonged low interest rate environment, even before the outbreak of COVID-19. Should the substantial deterioration in the real economy be prolonged, full-fledged financial adjustments through such vulnerabilities could give rise to a negative feedback loop between the real economy and the financial sector.

The latest *FSR* expresses concern over prolonged negative impacts in many areas. It notes that "should the impact on the real economy be protracted, problems stemming from tightened liquidity conditions could turn into solvency problems," and that there are significant uncertainties over the duration of negative impacts on the real economy. Key to the crisis response from the government and the BOJ will be their efforts to break the negative feedback loop between the real economy and the financial sector.

Chart: Demand Growth Expected by Companies and Investment-Saving Balance at Non-financials

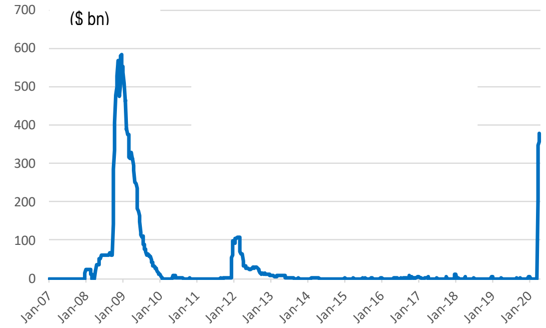


Source: Cabinet Office; compiled by Daiwa Securities.

BOX: USD Liquidity Swaps and BOJ's Balance Sheet

Major market disruptions since March have increased global demand for dollar liquidity and raised the cost of funding in dollars. To ensure that foreign central banks have access to dollar funding, the Fed responded by enhancing its existing USD swap lines and creating new ones, bringing the total number of central banks that have swap lines with the Fed to 14.

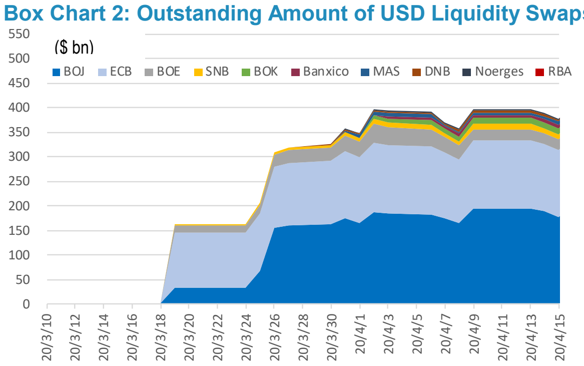
Box Chart 1: Outstanding Amount of USD Liquidity Swaps (weekly)



Source: Fed; compiled by Daiwa Securities.

According to data from the New York Federal Reserve Bank, ten central banks are currently using the swap lines, and the BOJ and ECB account for most of that use. The volume of this funding supplied to the BOJ shows how strong dollar funding demand from Japan's financial institutions was toward the end of the fiscal year, when the dollar funding environment was deteriorating.

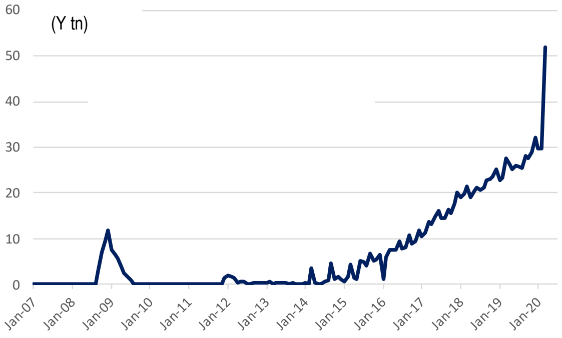
Box Chart 2: Outstanding Amount of USD Liquidity Swaps (by central bank, daily)



Source: NY Fed; compiled by Daiwa Securities.

Looking at this from the perspective of the BOJ's balance sheet, on the asset side there was a large increase in foreign currency reserves reflecting its supply of dollar funding to Japanese banks, while on the liability side there was a sharp increase in "other deposits," which are the corresponding JPY deposits from foreign central banks (in this case the Fed) held by the BOJ. Since Japanese banks do not have sufficient Japanese government securities as collateral to participate in these dollar operations, the BOJ lends that collateral through its Securities Lending to Provide Japanese Government Securities as Collateral for the US Dollar Funds-Supplying Operations. This program is roughly of an equal amount, creating a peculiar situation.

Box Chart 3: Other Deposits at BOJ Accounts



Source: BOJ; compiled by Daiwa Securities.

Explanatory Document of Unregistered Credit Ratings

In order to ensure the fairness and transparency in the markets, Credit Rating Agencies became subject to the Credit Rating Agencies' registration system based on the Financial Instruments and Exchange Act. In accordance with this Act, in soliciting customers, Financial Instruments Business Operators, etc. shall not use the credit ratings provided by unregistered Credit Rating Agencies without informing customers of the fact that those Credit Rating Agencies are not registered, and shall also inform customers of the significance and limitations of credit ratings, etc.

■ The Significance of Registration

Registered Credit Rating Agencies are subject to the following regulations:
1) Duty of good faith.
2) Establishment of control systems (fairness of the rating process, and prevention of conflicts of interest, etc.).
3) Prohibition of the ratings in cases where Credit Rating Agencies have a close relationship with the issuers of the financial instruments to be rated, etc.
4) Duty to disclose information (preparation and publication of rating policies, etc. and public disclosure of explanatory documents).

In addition to the above, Registered Credit Rating Agencies are subject to the supervision of the Financial Services Agency ("FSA"), and as such may be ordered to produce reports, be subject to on-site inspection, and be ordered to improve business operations, whereas unregistered Credit Rating Agencies are free from such regulations and supervision.

■ Credit Rating Agencies

[Standard & Poor's]

The Name of the Credit Rating Agencies group, etc

The name of the Credit Rating Agencies group: S&P Global Ratings ("Standard & Poor's")
The name and registration number of the Registered Credit Rating Agency in the group: S&P Global Ratings Japan Inc. (FSA commissioner (Rating) No.5)

How to acquire information related to an outline of the rating policies and methods adopted by the person who determines Credit Ratings

The information is posted under "Unregistered Rating Information" (http://www.standardandpoors.co.jp/unregistered) in the "Library and Regulations" section on the website of S&P Global Ratings Japan Inc. (http://www.standardandpoors.co.jp)

Assumptions, Significance and Limitations of Credit Ratings

Credit ratings assigned by Standard & Poor's are statements of opinion on the future credit quality of specific issuers or issues as of the date they are expressed and they are not indexes which show the probability of the occurrence of the failure to pay by the issuer or a specific debt and do not guarantee creditworthiness. Credit ratings are not a recommendation to purchase, sell or hold any securities, or a statement of market liquidity or prices in the secondary market of any issues.

Credit ratings may change depending on various factors, including issuers' performance, changes in external environment, performance of underlying assets, creditworthiness of counterparties and others. Standard & Poor's conducts rating analysis based on information it believes to be provided by the reliable source and assigns credit ratings only when it believes there is enough information in terms of quality and quantity to make a conclusion. However, Standard & Poor's does not perform an audit, due diligence or independent verification of any information it receives from the issuer or a third party, or guarantee its accuracy, completeness or timeliness of the results by using the information. Moreover, it needs to be noted that it may incur a potential risk due to the limitation of the historical data that are available for use depending on the rating.

This information is based on information Daiwa Securities Co. Ltd. has received from sources it believes to be reliable as of March 7th, 2017, but it does not guarantee accuracy or completeness of this information. For details, please refer to the website of S&P Global Ratings Japan Inc. (http://www.standardandpoors.co.jp)

[Moody's]

The Name of the Credit Rating Agencies Group, etc

The name of the Credit Rating Agencies group: Moody's Investors Service ("MIS")
The name and registration number of the Registered Credit Rating Agency in the group: Moody's Japan K.K. (FSA commissioner (Rating) No.2)

How to acquire information related to an outline of the rating policies and methods adopted by the person who determines Credit Ratings

The information is posted under "Unregistered Rating explanation" in the section on "The use of Ratings of Unregistered Agencies" on the website of Moody's Japan K.K. (The website can be viewed after clicking on "Credit Rating Business" on the Japanese version of Moody's website (https://www.moodys.com/pages/default_ja.aspx)

Assumptions, Significance and Limitations of Credit Ratings

Credit ratings are Moody's Investors Service's ("MIS") current opinions of the relative future credit risk of entities, credit commitments, or debt or debt-like securities. MIS defines credit risk as the risk that an entity may not meet its contractual, financial obligations as they come due and any estimated financial loss in the event of default. Credit ratings do not address any other risk, including but not limited to: liquidity risk, market value risk, or price volatility. Credit ratings do not constitute investment or financial advice, and credit ratings are not recommendations to purchase, sell, or hold particular securities. No warranty, express or implied, as to the accuracy, timeliness, completeness, merchantability or fitness for any particular purpose of any such rating or other opinion or information, is given or made by MIS in any form or manner whatsoever.

Based on the information received from issuers or from public sources, the credit risks of the issuers or obligations are assessed. MIS adopts all necessary measures so that the information it uses in assigning a credit rating is of sufficient quality and from sources MIS considers to be reliable. However, MIS is not an auditor and cannot in every instance independently verify or validate information received in the rating process.

This information is based on information Daiwa Securities Co. Ltd. has received from sources it believes to be reliable as of April 16th, 2018, but it does not guarantee accuracy or completeness of this information. For details, please refer to the website of Moody's Japan K.K. (https://www.moodys.com/pages/default_ja.aspx)

[Fitch]

The Name of the Credit Rating Agencies group, etc

The name of the Credit Rating Agencies group: Fitch Ratings ("Fitch")
The name and registration number of the Registered Credit Rating Agency in the group: Fitch Ratings Japan Limited (FSA commissioner (Rating) No.7)

How to acquire information related to an outline of the rating policies and methods adopted by the person who determines Credit Ratings

The information is posted under "Outline of Rating Policies" in the section of "Regulatory Affairs" on the website of Fitch Ratings Japan Limited (https://www.fitchratings.com/site/japan)

Assumptions, Significance and Limitations of Credit Ratings

Ratings assigned by Fitch are opinions based on established criteria and methodologies. Ratings are not facts, and therefore cannot be described as being "accurate" or "inaccurate". Credit ratings do not directly address any risk other than credit risk. Credit ratings do not comment on the adequacy of market price or market liquidity for rated instruments. Ratings are relative measures of risk; as a result, the assignment of ratings in the same category to entities and obligations may not fully reflect small differences in the degrees of risk. Credit ratings, as opinions on relative ranking of vulnerability to default, do not imply or convey a specific statistical probability of default.

In issuing and maintaining its ratings, Fitch relies on factual information it receives from issuers and underwriters and from other sources Fitch believes to be credible. Fitch conducts a reasonable investigation of the factual information relied upon by it in accordance with its ratings methodology, and obtains reasonable verification of that information from independent sources, to the extent such sources are available for a given security or in a given jurisdiction. The assignment of a rating to any issuer or any security should not be viewed as a guarantee of the accuracy, completeness, or timeliness of the information relied on in connection with the rating or the results obtained from the use of such information. If any such information should turn out to contain misrepresentations or to be otherwise misleading, the rating associated with that information may not be appropriate. Despite any verification of current facts, ratings can be affected by future events or conditions that were not anticipated at the time a rating was issued or affirmed.

For the details of assumption, purpose and restriction of credit ratings, please refer to "Definitions of ratings and other forms of opinion" on the website of Fitch Rating Japan Limited.

This information is based on information Daiwa Securities Co. Ltd. has received from sources it believes to be reliable as of September 27th, 2019, but it does not guarantee accuracy or completeness of this information. For details, please refer to the website of Fitch Rating Japan Limited (https://www.fitchratings.com/site/japan)

February 2020

IMPORTANT

Conflicts of Interest: Daiwa Securities Co. Ltd. may currently provide or may intend to provide investment banking services or other services to the company referred to in this report. In such cases, said services could give rise to conflicts of interest for Daiwa Securities Co. Ltd.

Daiwa Securities Co. Ltd. and Daiwa Securities Group Inc.: Daiwa Securities Co. Ltd. is a subsidiary of Daiwa Securities Group Inc.

Other Disclosures Concerning Individual Issues:
1) As of 26 April 2016, Daiwa Securities Co. Ltd., its parent company Daiwa Securities Group Inc., GMO Financial Holdings, Inc., and its subsidiary GMO CLICK Securities, Inc. concluded a basic agreement for the establishment of a business alliance between the four companies.
As of end-December 2017, Daiwa Securities Group Inc. owned shares in GMO Financial Holdings, Inc. equivalent to approximately 9.3% of the latter's outstanding shares. Given future developments in and benefits from the prospective business alliance, Daiwa Securities Group Inc. could boost its stake in GMO Financial Holdings, Inc. to up to 20% of outstanding shares.

2) Daiwa Real Estate Asset Management is a subsidiary of Daiwa Securities Group Inc. and serves as the asset management company for the following J-REITS: Daiwa Office Investment Corporation (8976), Daiwa Securities Living Investment Corporation (8986).

3) Samty Residential Investment became a consolidated subsidiary of Daiwa Securities Group Inc. effective 10 September 2019.

4) On 30 May 2019, Daiwa Securities Group Inc. formalized an equity/business alliance with Samty, and as of 14 June 2019 it owned 16.95% of shares outstanding in Samty along with convertible bonds with a par value of Y10bn. Conversion of all of said convertible bonds into common shares would bring the stake of Daiwa Securities Group Inc. in Samty to 27.28%.

5) Daiwa Securities Group Inc. and Credit Saison Co., Ltd. entered into a capital and business alliance, effective 5 September 2019. In line with this alliance, Daiwa Securities Group Inc. is to acquire up to 5.01% of Credit Saison's total common shares outstanding (excl. treasury shares; as of 31 Jul 2019).

6) NEC (6701): NOTICE REGARDING U.S. PERSONS: This report is not intended for distribution to or use by any person in the United States. Securities issued by NEC Corporation have been suspended from registration in the U.S. and are subject to an order of the U.S. Securities and Exchange Commission dated June 17, 2008, pursuant to Section 12(j) of the Securities Exchange Act of 1934. This document is not a recommendation or inducement of any purchase or sale of such securities by any person or entity located in the U.S. Daiwa Securities Co. Ltd. disclaims any responsibility to any such person with respect to the content of this document. Any U.S. person receiving a copy of this report should disregard it.

Notification items pursuant to Article 37 of the Financial Instruments and Exchange Law
(This Notification is only applicable to where report is distributed by Daiwa Securities Co. Ltd.)
If you decide to enter into a business arrangement with our company based on the information described in this report, we ask you to pay close attention to the following items.

- In addition to the purchase price of a financial instrument, our company will collect a trading commission* for each transaction as agreed beforehand with you. Since commissions may be included in the purchase price or may not be charged for certain transactions, we recommend that you confirm the commission for each transaction. In some cases, our company also may charge a maximum of ¥2 million per year as a standing proxy fee for our deposit of your securities, if you are a non-resident.
- For derivative and margin transactions etc., our company may require collateral or margin requirements in accordance with an agreement made beforehand with you. Ordinarily in such cases, the amount of the transaction will be in excess of the required collateral or margin requirements**.
- There is a risk that you will incur losses on your transactions due to changes in the market price of financial instruments based on fluctuations in interest rates, exchange rates, stock prices, real estate prices, commodity prices, and others. In addition, depending on the content of the transaction, the loss could exceed the amount of the collateral or margin requirements.
- There may be a difference between bid price etc. and ask price etc. of OTC derivatives handled by our company.
- Before engaging in any trading, please thoroughly confirm accounting and tax treatments regarding your trading in financial instruments with such experts as certified public accountants.

* The amount of the trading commission cannot be stated here in advance because it will be determined between our company and you based on current market conditions and the content of each transaction etc.
** The ratio of margin requirements etc. to the amount of the transaction cannot be stated here in advance because it will be determined between our company and you based on current market conditions and the content of each transaction etc.

When making an actual transaction, please be sure to carefully read the materials presented to you prior to the execution of agreement, and to take responsibility for your own decisions regarding the signing of the agreement with our company.

Corporate Name: Daiwa Securities Co. Ltd.
Registered: Financial Instruments Business Operator, Chief of Kanto Local Finance Bureau (Kin-sho) No.108
Memberships: Japan Securities Dealers Association, The Financial Futures Association of Japan, Japan Investment Advisers Association, Type II Financial Instruments Firms Association