Question and Answers from May 27, 2014 IR Meeting

Management Plan

Q: You have said that your business plan running through until FY2015 is based on expanding the revenue base of the P&C operations. Over the medium term to 2020, which of your four businesses – domestic P&C, domestic life insurance, overseas, and financial services – will you target for growth? Or will you enter new business field? What is the medium-term outlook for the revenue base composition?

A. From a medium-term perspective running through to 2020, we may face greater price competitiveness in the P&C insurance business provided we are able to keep our combined ratio in the 90–95% range. The retail market will still be the major battleground within this business segment.

In terms of new risk developments, we expect to see the advent of autonomous car technology have an impact on the auto insurance market. Reduced accident rates and loss ratios should not only translate into lower premiums, but should also alter the nature of risk due to the question of whether liability will reside with the driver or the manufacturer. We think we will also develop insurance products for elderly society.

Natural disasters are our greatest concern in the domestic P&C business. There will be an impact if the scale of disaster-related damage we are seeing each year becomes the “new normal” for the sector.

Based on these medium- and long-term changes in the environment, we will focus not only on the domestic P&C and life insurance businesses, but also on service businesses where we can grow the customer base over time. For example, Group subsidiary Healthcare Frontier Japan has 45% of the market within the industry and services a customer base of 100,000 people each year. This yields not only cross-selling opportunities for Group life and non-life insurance policies, but also enables us to grow our total customer base. We have established a new business development division within the holding company to drive the Group’s creation of new business linked to the themes of safety, security and health. We will also consider suitable M&A opportunities in the service sector.

Domestic P&C Insurance Business

Q: Do you expect the merger of the two P&C insurers to create top-line synergies exclusive to the NKSJ Group?

A: We decided to merge the two insurers to reduce costs, and we expect the integration to do this. As we have indicated before, we forecast cost savings of ¥56 billion from the merger relative to FY2011. We should also see additional savings from FY2016 onwards once we phase out the Nipponkoa systems.

In top-line revenue terms, Sompo Japan and Nipponkoa started to integrate sales operations in FY2013, and as a result we have improved our market share and realized the top market share growth in last fiscal year. We also expect top-line synergies in the life insurance business by expanding our sales of medical insurance policies through the sales channels of Nipponkoa, and there could be similar opportunities in other insurance sectors.

Q: You are developing newly specialized auto insurance policies for electric vehicles that adjust premiums in line with the number of kilometers travelled. Are you looking to devise more advanced policies as well that reward safe drivers based on, for example, the number of times the brakes are applied sharply?

A: These policies need analysis of Big Data, in our view, which means gathering, analyzing and utilizing information in three stages. Currently we are at the data-gathering stage. In future, we plan to combine this information with our internal data on claim payouts to develop analytical algorithms that we could apply to the development of these types of insurance policies.

Domestic Life Insurance Business

Q: There is an assumption that price competition will accelerate in the domestic life insurance market going forward, among a range of major shifts. What strategy and products do you expect to see used in agency channels in the future?

A: We are already seeing price-based competition in third-sector policies, alongside changes in market conditions such as the development of mega-channels inside retail banks. We think that we could see price competition start to develop with first-sector policies as well. This reflects the high level of life insurance in Japan relative to per-capita GDP, as well as the regulatory drive to provide customers with greater transparency in life insurance sales. The emphasis these days is on rational design of policies based on customer self-appraisal of requirements.

Our focus going forward is to leverage the strong P&C insurance sales channel of Himawari Life to have customers select us as their insurer of choice for life and non-life policies. This means taking the time to provide a consulting service to customers on the total risk. We will grow our customer base if people respond favorably to this kind of approach. So we are developing the medical policies that we recently introduced so that we can try to help customers for our first-sector life policies work out exactly what their death protection and related insurance needs are.

Q: What proportions of sales do the P&C and agency channels account for within the overall life policy sales channels? Also, how are the new medical policies performing in sales terms?

A: Within Himawari Life's sales channels, the P&C channel is about 63% and, of that, the weight of professional agencies and trainees is a bit less than 45% combined. Professional agencies selling life policies account for roughly 20%.

We sold around 170,000 medical insurance policies in FY2013, but are targeting sales of 300,000 policies in FY2014 since we expect the new medical policies to prove popular. We sold around 10,000 policies in nine business days after the new product went on sale on May 2, and had reached sales of around 20,000 policies as of yesterday (May 26). So the sales began well.

Overseas Insurance Business

Q: You are planning to expand the Group's global reinsurance operations. What is your underwriting policy in the current soft market, and how will you incorporate Canopius?

A: Underwriting is growing in line with the plan, despite premium increases due to currency movements. We have now started to explore how to optimize the NKSJ Group's global reinsurance operations including Canopius. Overall, we see this as an area where we are likely to see more rapid growth in the future.

Canopius possesses advanced underwriting capacity and related know-how, which are translating into high performance at the moment. We are studying how best to make use of this specialist expertise, but it is clear to us that we must avoid any expansion strategy that sacrifices underwriting quality. The market for specialty lines of insurance is mainly in developed countries such as Europe and the US. We plan to expand the Group's overall presence in this field while managing any concentration of risks appropriately.

ERM, Capital Management

Q: Regarding the internal solvency margin ratio, has your revised internal risk model factored in natural disaster and long-term risks and risk-diversification effects? Also, why have you set a target range of 120–170% for this metric while it is still unclear how the international regulatory situation on solvency will develop?

A: We have revised our internal risk model to take account of risks that we previously left unrecognized. Note also that we have not counted the hybrid bond issue that we redeemed today (May 27) towards the capital base.

There has been little overall change in the internal solvency margin ratio due to the positive and negative risk variances largely cancelling out. In broad terms, we have seen risks decline in the domestic P&C business due to the disposal of strategic-holding stocks, while risks have increased in the overseas and life insurance segments. The target range ceiling of 170% is the internal solvency margin ratio if we hit our target of 7% for adjusted consolidated ROE, while the 120% floor value was set based on considerations of financial strength. We have also worked out contingency measures if the internal solvency margin ratio were to deviate from this range over the medium term.

We plan to re-examine the levels of ROE and capital we should be targeting once we see greater clarity in terms of international regulation of solvency issues.

Q: Is the disposal of strategic-holding stocks having any impact on top-line revenue? Do you expect to reduce these holdings any further in the future?

A. We have been reducing strategic-holding stocks only after discreet discussions with issuers to ensure there is no top-line impact. Forecasted figures for FY2014 takes into account further planned reductions in these stocks. Based on our ERM framework, we expect to review the holding level of strategic-holding stocks and study plans for further reductions and form a future management plan, including the revision of FY2015 plan. Our strategic-holding stocks are still about ¥1.5 trillion, while adjusted net assets for the two P&C insurers of about ¥1.7 trillion. At this stage we are considering a future target of reducing strategic-holding stocks to roughly 70% of adjusted net assets over the long term.

Shareholder Returns

Q: What are the chances of a dividend hike in future, and when might that happen?

A: Our capital management policies are focused on targeting a strong balance sheet equivalent to an AA credit rating, on improving capital efficiency to boost adjusted consolidated ROE to 7% or more, and on increasing total shareholder returns to the level of 50% of adjusted profit excluding life insurance over the medium term. Based on these policies, we plan to maintain dividend per share at ¥60 over the course of the current business plan that ends in FY2015. We will consider stock buybacks as well if we have the requisite capacity to return more capital to shareholders.

Q: You currently do not include the earnings of Himawari Life when calculating the fund for shareholder returns. Do you plan to factor in these earnings once the subsidiary becomes stably profitable according to J-GAAP?

A: International investors are usually of the view that earnings from life insurance operations should be an exceptional item in accounting profit terms. Moreover, we think it is appropriate to exclude Himawari Life from the shareholder returns calculation because the company is still in its growth phase. We do not plan to change this particular policy.

We will continue to review our policy on shareholder returns to ensure that it is appropriate for the Group as a whole.