Q2 2014 Earnings Call

Company Participants

- Kengo Sakurada, President
- Shinji Tsuji, Senior Managing Executive Officer, Director
- Unidentified Speaker, Unknown

Other Participants

- Futoshi Sasaki, Analyst
- Hideyasu Ban, Analyst
- Jun Shiota, Analyst
- Masao Muraki, Analyst
- Natsumu Tsujino, Analyst
- Tatsuo Majima, Tokyo Securities Co. Ltd.
- Unidentified Participant, Analyst
- Wataru Otsuka, Analyst

Presentation

Kengo Sakurada {BIO 15149542 <GO>}

Good afternoon, ladies and gentlemen. My name is Sakurada, the President of NKSJ Group. Thank you, so much for attending our IR meeting today.

Our IR team had a conference call with you last week. And we had a Q&A session with you on that telephone conference call already. So we'd like to really simplify the explanation about the numbers. And I'm going to just hit the highlights for today.

As we disclosed last week, first of all, we revised our guidance for the full year upward in light of our current business improvement trends, as we disclosed last week.

Our new projections are, for net income, is JPY72 billion; and JPY128 billion for adjusted consolidated profit. We are making a good progress steadily towards achieving our targets for FY 2015.

Improvement in the combined ratio in domestic P&C business is outpacing the management plan. Against a plan of 6.7 points improvement in four years, we project to achieve 4.4 points improvement over the first two years up to this year, which is equivalent to two-thirds of the whole improvement planned.

In the core automobile insurance business, profitability is improving. And the loss ratio in the first half was improved by more than 5 points. There is a noticeable fall in the number of claims made.

In the domestic life business, we are continuing the shift to protection-type products and expansion in P&C sales channel. The preparation for the merger of two P&C companies, which is our unique strategy, is proceeding smoothly. There is no change to the merger synergy, as well as the scale and the timing of one-time costs.

The reduction in the exposure of strategic-holding stocks has progressed more than 50% compared to the fiscal year plan. Our dividend policy remains unchanged, which is JPY60 per share. Based on the upward revision of the full-year business forecast and the capital conditions, we will examine the option of stock buybacks.

Let me explain each point. Please turn to page 3. Here is the update on the progress of management plan.

We revised our adjusted consolidated profit forecast upward from JPY113.5 billion to JPY128 billion, up JPY15 billion. We project adjusted consolidated profit to improve farther, mainly in domestic P&C business, with the merger of two P&C companies to around JPY150 billion level.

We think we have more visibility of achieving our JPY215 billion. It doesn't include extraordinary losses and profits in this number. So as we mentioned earlier, we think we have more visibility of achieving our 2015 plan.

Please turn to page 4. This shows J-GAAP based performance trend.

Business improvement is proceeding ahead of our plan, with the upward guidance revision this time, although J-GAAP based profit level in FY 2014 is projected to be in line with our plan. Since there are one-time merger costs associated with the release of the integrated system, there is a possibility that it may be a temporary correction phase. However, the key message here is the fact that our fundamental earnings base is improving, as we saw in adjusted consolidated profit plan.

As for one-time merger costs, many of them will be posted as extraordinary losses. As a result, they do not impact adjusted consolidated profit, which is the fund available for shareholder returns.

Please turn to page 13. This slide shows the trend of the combined ratio in domestic P&C business.

In our current plan, we aim at reducing the combined ratio by 6.7 points over four years to 94.7%.

FY 2013, the second year of the plan, saw an increase in commissions due to the expansion in the reinsurance business. But combined ratio fell to 97%; contributed to improvements both in premiums and claims. We forecast to achieve 4.4 points improvement over the first two years of the plan, which is equivalent to two-thirds of the whole improvement planned.

We plan to improve furthermore by around 3 points through expense reduction as a result of the merger of two P&C companies. Towards FY 2015, we are determined to achieve the plan by implementing additional actions to improve profitability with consumption tax hike in mind.

Please turn to page 14. This page shows the trend of combined ratio of automobile insurance business, which is our core business.

In FY 2013, loss ratio has improved dramatically as a result of products and premium rate revisions, which will put the combined ratio 98.8% level, below 100%.

We think we have higher probability of achieving the plan of profit improvement in automobile insurance business. But we'd like to study necessary measures continuously by paying attention to rising trend of repair cost per claim, impact of consumption tax hike on the plan, etc.

Please go over to page 27.

NKSJ Himawari Life, the life business of the Group, is growing profitably, with uniquenesses in distribution channel and product mix. The main sales channel is cross-sales channel, making the use of our P&C insurance agency network where our strength lies, representing 62% of our total life sales.

On our product front, we have been focusing on high profitable protection-type products, such as medical and income compensation since 2008, which puts protection-type weight higher and higher every year to 51% currently. As a result of our high profitability product strategy, our new business margin is 9.4%, which is higher than that of our peers.

Please turn to page 28. This shows the new business margin. And this slide shows the trend of annualized premiums in force and MCEV.

As I mentioned earlier, tapping on the unique characteristics of our life business, as I explained on the previous page, both annualized premium in force and MCEV are steadily growing.

Please go over to page 29. This page shows trend of P&C channel mix, as well as protection-type product mix.

Our strategy to increase P&C channel mix is gradually bearing fruits. From 57.9% to 61.6%, the weight of P&C insurance channel has increased.

Sales competition in medical insurance business is becoming more intense. And it will be even more intense in the future. In this environment, the importance of P&C distribution channel, which has a strong grip on our customers, will be even higher, because they have the opportunity of contacting them. So the competitive edge of our P&C distribution channel will be even more useful in the future. And we are going to continue our steady effort to strengthen this channel even more.

Protection-type product mix on the basis of the number of policies in force is surely increasing. We plan to continue this profit-driven product strategy in the future.

Next topic is our overseas business. Please turn to page 35.

As I mentioned when we announced our plan, there is no change in our strategy and direction to promote overseas business. We continue to achieve growth by disciplined investment in our targeted markets we classified last year, such as commercial markets in Europe and the United States, as well as Brazil and Turkey.

We started to include Maritima in Brazil, one of our key regions, as a consolidated subsidiary in June this year. I attended a party of Maritima in Brazil celebrating the 70th anniversary. As the President of the holding Company, I made a speech at that celebration party. So that our Company is doing very well.

We continue to keep taking actions to enhance the presence of NKSJ Group in each region, as you can see on this page.

Please turn to page 38. Let me next explain our overseas assumed reinsurance business.

There is no change in our policy of making steady progress in the overseas reinsurance business while rigorously managing risks. We recalculated our overseas assumed reinsurance net premiums written. Reflecting our first half performance, we now project it to be JPY47 billion, up JPY13 billion year on year.

Our plan for the final year of the plan, which is 2015, the net premiums written in this business is JPY60 billion against which we are making good progress.

Please go over to page 40. This is the progress of the merger of the two P&C companies.

In one word, everything is very smooth. Prior to the Nippon [ph] merger in September 2014 as we announced, we will be integrating all levels of the Company structure in April 2014 so that the entire organization will be managed as one entity. As part of the practical merger, we have already unified offices and head office general managers in April this year. And have unified sales and claim office managers nationwide.

We plan to unify section managers as well in April next year, establishing the one-wheel [ph] structure. If market sees it appropriate, there will be more locations where we will unify the structures prior to the plan.

In any case, this one structure is not only helping the cost reduction through reduction of the number of the managers. But it is also helping to speed up the decision-making process significantly.

As we have already announced, we are recruiting voluntary early retirement scheme applicants. And development and testing for systems in division is making progress smoothly. We will have done all sorts of tasks necessary before the merger date so that merger date will come seamlessly.

Please turn to page 41. This is the situation of merger synergies and one-time merger costs.

In 2013, merger synergy will increase due to reduction of headcount. On the other hand, we expect one-time costs to slightly increase due to pre-emptive consolidation of offices. I'd like to remind you that what's happening is as we had expected. There is no major change with the scale and schedule of the plan for next year and after. Specifically, synergy effect will increase to JPY40 billion in 2014. And to JPY56 billion in fiscal year 2015.

Next, I'd like to talk about capital-related matters. Please turn to page 43.

This page is showing the situation of stock price and capital level. Since NKSJ was founded, share price has been trending below the net asset per share level. And it is my concern, as of the end of September, according to J-GAAP, net asset was JPY1.3 trillion. And adjusted consolidated net assets was JPY2.3 trillion; whereas as of today, the market GAAP [ph] was JPY1.2 trillion. So both from accounting standard point of view, as well as from economic value point of view, evaluation of NKSJ Holdings from the market is below the actual value of the Company.

As we have explained with earlier slides, earnings is on the recovery trend, even outpacing the medium-term management plan we have towards 2015. And we believe that there is high probability to achieve the targeted profit as well as ROE of the medium-term management plan.

We would like to show to the market the steady earnings recovery situation, as well as progress we are making towards financial target in order to improve the market devaluation of NKSJ Holdings.

On the next page, we are showing the capital management policy.

The basic policy of capital management has not changed since the founding of the NKSJ Group. By striking a balance of the three elements, namely maintaining financial soundness, improving capital efficiency and increasing shareholder return, we will aim to expand corporate value.

To represent those three elements simply with numbers and such, they are what you can see, with the underlying parts as follows; target credit rating of AA; ROE of 7%, or more; stable dividend payment; and total payout ratio of 50%. In order to achieve these targets, we simply need to reduce risk, or risk take appropriately. And do the right resource allocation.

Please turn to page 45. I'd like to confirm the value of the different categories that make up the adjusted consolidated net asset.

So as of the end of the September this year, it totaled to JPY2.3 trillion; and from the end of March, we increased it by over JPY100 billion.

Please turn to page 46. This is the situation of the capital and risk according to the economic value basis internal standard.

For measurement of risk, we use a confidence level equivalent to AA credit ratings, which is valued at a risk of 99.95%, which is a risk that will occur once every 2,000 years. The result of the calculation is as you can see on the graph. Capital buffer defined by the variance between the capital and risk is JPY800 billion; solvency ratio, which is capital divided by risk, is 150%.

Comparing this to the end of last fiscal year, increase in capital was mainly realized by increase in unrealized gains of stock holdings. On the other hand, because we have aggressively reduced strategic holding stocks, the increase in risk is limited and solvency is on the increase.

The buffer is on the trend to increase, because earnings is on the recovery trend. And stock price is rising. At the same time, we are also in a situation where we cannot ignore the negative impact coming from the stock market, such as fall share price. Therefore, we would like to monitor the stock market and grasp the right timing in selling down strategic holding stocks in order to reallocate capital to higher efficiency businesses.

Next page is about the asset management. Let me first explain about the asset management situation with the domestic non-life insurance business.

Basic policy of portfolio management for general account assets is diversified investment; and for savings-type account asset, ALM is executed, centering around yen-denominated fixed income asset in [ph] general account asset, while we are aggressively reducing strategic holding stocks.

Due to the stock market rally, the proportion of domestic equities has increased from the end of March to 35%. Therefore, in that sense, reduction of strategic holding stocks continues to be on the agenda and use that money for other types of investment.

For savings account asset, as you can see, the duration gap is five years versus six years. So there is a one-year duration gap. Then interest fluctuation risk is limited. Therefore, we are well managing the portfolio.

Next pages explains about our life insurance business.

The life insurance business has main product as a savings type of insurance and protection type of policies. We have a conservative stance in asset management, mainly by ALM execution. The yen-denominated assets are mainly JJBs [ph]. And asset liability duration gap is small. So we have a conservative portfolio with mitigated risk.

Going forward, we will be monitoring the interest rate movement and lengthen asset side [ph] duration so we can gradually minimize the duration gap. So by extending the duration on the asset side, as you can see, which is 12 years now, we will able to catch up with the duration on the liability side.

If you go to page 49, this is about the reducing of the strategic-holding stocks. Last year, we sold about JPY197.8 billion of strategic-holding stocks; and this year, we also plan to reduce a similar amount of strategic-holding stocks.

The amount of reduction in the first half of the year with spot sales was JPY43.7 billion. And with stock futures was JPY63.8 billion. So in total, we have reduced it by JPY107.5 billion. And we have achieved more than 50% of the planned reduction for the year.

Again, the gain from the security sales will make a major impact to the financial P&L. So we would like to closely monitor the stock market as we sell down these equities.

Lastly, I would like to mention about shareholder return.

As I mentioned in the very beginning, this year, we plan to maintain the dividend per share of JPY60 per share. As for the share buyback, it will be considered based on the fact that we made an upward revision to the full-year projection, as well as on the capital situation. For fiscal 2014 and after, we would like to minimally maintain the dividend payment of JPY60 per share so as to maintain stable dividend payment.

On top of that, we would like to be mindful of the capital situation. And we will keep the right balance between that versus investment and improving capital efficiency through growth investment. And we will consider the scale and method of shareholder return after that. For fiscal 2013, we will pay the interim dividend of JPY30 per share.

That concludes my part of the presentation. Thank you very much.

Questions And Answers

A - Unidentified Speaker

Now we'd like to open the floor for questions. When you have a question, would you please raise your hand and state your name and your company name?

Q - Masao Muraki {BIO 3318668 <GO>}

Masao Muraki, Deutsche Securities. I have two questions.

My first question is on page 13, which is about your plan of the combined ratio.

Your combined ratio is outpacing the plan in terms of the improvement pace. But as you can see on this page, there is a 3 points increase factor from the consumption tax hike with the combined ratio.

And the actions that you can take on the premium side and also on the expense side, what is your direction of the counter measure from the consumption tax hike? And although consumption tax hike is official. But are you going to change your management plan?

And my second question is about page 43. And you have shown the trend of your net asset value. And as you explained for long time, your PBR [ph] is below 1 [ph]. In your assessment, what is the discount factor putting the pressure on your stock price in general? Sometimes, it's because of the low ROE which is lower than cost of the capital, or simply about accounting method. No one can put a valuation on your stock based upon the financial reported numbers.

Or, as was pointed out by some foreign investors, you have a tail risk associated with long-term natural disasters such as fire and allied segment. So there is a potential tail risk which is becoming a discount factor which is depressing your stock price.

So there are various potential cases. But in your opinion what is your assessment or reasons why your stock price has been depressed for such a long time?

A - Shinji Tsuji {BIO 16148256 <GO>}

My name's Tsuji [ph] from Corporate Planning. I'm going to answer your first question, page 13, which is about the combined ratio.

As we mentioned when we disclosed our results of the first half, combined ratio of the automotive insurance business is improving very steadily. And in the future, our action towards the consumption tax hike is as follows.

The impact on the tax hike is not included in the management plan at the moment. According to our trial calculation, as we have explained in the past, in 2015, the impact will be JPY35 billion of the total Group. That is a result of our trial calculation of the Company.

And as you know, the insurance product is exempt from the consumption tax. However, as a matter of course, the cost, which is the claim or agency commission imposed of consumption tax. Therefore, we'd like to devise our pricing upward reflecting those cost increases.

But in the main core business of automobile insurance business, we had the division of drivers' ratings scheme last year. And we are seeing the benefit from that currently. We see a significant decrease of the number of small-scale petty claims. And in October last year, we had the start of this new driving ratings scheme.

So it depends on the timing of the impact, on our revenue from this division as policyholders gradually shift to the new revised table. So we have to really wait and see the specific impact from that.

But we have no intention to change our numerical targets in the management plan. Therefore, I would like to offset the negative factor by expense reduction and positive impact from the Drivers' Rating Scheme. We'd like to wait and see the specific positive impact from the Driver's rating scheme change. So we'd like to continuously study and scrutinize the numbers.

And answer to your second question is going to be provided by Mr. Sakurada.

A - Kengo Sakurada {BIO 15149542 <GO>}

Long-term stagnancy of BPS [ph], as you asked, is my headache. And this may sound like an excuse. But this is not our only the phenomenon of our Company. But you cannot name so many financial insurance -- financial organizations, as PBR is dramatically above 1. And over the past six months to one year, I had opportunities talking with overseas investors. And this point has been raised up very frequently. And always discussion ends up with talking about the share buyback. And these discussion points are as follows.

First, our low ROE. Putting aside the J-GAAP difference, or the definition of how we calculate a numerator and the denominator, even on the equal footing basis, our ROE is low. And if you look at other non-life companies and the life companies in Japan, we all face double structure issue. So what we can do is just to address this issue steadily.

And other than this low level of ROE, there is an issue of tail risk. And there are many investors who say that they feel that there are more natural disasters than before and that they feel that tail risk is larger than before. But I don't have a feeling that that's the factor that is making them reluctant investing in our stock.

Another factor for our industrial P&C and for some listed companies in the life business, there is strong co-relationship with Nikkei average. There is very high beta [ph] against Nikkei average. And our stock is almost like an investment trust. So beta is very high, or higher than 1. So when the total stock market moves, then our valuation moves accordingly.

Personally speaking, it's very difficult for the Company to control the beta. So what we can do as a company is to enhance our ROE. But we cannot dramatically increase ROE over one year or two years. But if you look at major European insurance players such as Allianz or Berkshire, especially if you look at players who are in the retail primary insurance segment, not B2B segment. And if they look at their performance over the past 10 to 20 years, there were some years when their PBR was below 1. So how did they improve their PBR?

When I look at what they did, they did ABCs [ph] of the business just like a textbook. So that's what we have to do as well. And those ABCs of the business that are included in the textbook are like actions that we explained today.

So there is no unique factor unique to NKSJ Group other than the beta issue. So we think we can address this issue as a company.

And about the share buyback, as I mentioned earlier, there is no clear yes or no at this point. But we made an upward finance projection revision. So by looking at the appropriate opportunities or timings of capital allocation, we'd like to live up to the expectation of our shareholders as much as we can.

Q - Masao Muraki {BIO 3318668 <GO>}

Thank you. So much. Let me ask you a follow-up question about my first question on page 13. This number does not include the impact from the consumption tax hike. But your target of 94.7%, which is below 95% for 2015, you're not going to change this plan.

There is a positive impact on the Drivers' Rating Scheme change. But are you going to scrutinize the number of specific impacts from the Drivers' Rating system? And rest will be adjusted by the price increase and you have no plan to change your medium-term business plan?

A - Unidentified Speaker

That's correct.

Q - Natsumu Tsujino {BIO 2234779 <GO>}

Tsujino, JPMorgan. I have three questions. My first question is regarding the net premium income, net premiums written and the growth rate for Sompo Japan and Nipponkoa and other companies. When I compare these different entities, Nipponkoa is lower than the others.

Prior to the merger, I know that the two companies were working on this. And is that why this is happening? Or having said that, the Nippon Japan and Sompo Japan added together, I think it's going to be a little bit below 1 plus 1 equals 2. So do I expect this to improve as the two entities actually merge?

My second question is about Himawari Life. In the slide, excluding the lump sum payment, the ANP [ph] of new policies is also increasing, as what you mentioned. However, in the third sector of products, the new policy ANP since last year has seen declining trend from last year. So in the third sector, are you selling less products which are lump sum payment and is that why this decline is occurring?

That's my second question.

And regarding Himawari Life, I have another question. Channel, sales channel, what's the channel situation? How much further can you strengthen this? So what is the ratio? I believe the ratio of life -- products for the P&C is improving. But including the P&C sales channel, as well as other sales channels, what areas of the sales channel can you strengthen going forward? In other words, what other areas and sales channel can you utilize or expand in the future. And what are you doing to do so?

And lastly, overseas business for the reinsurance assuming business, you are showing the top line growth. But is there any data that shows the profit level of the overseas reinsurance assumption business?

A - Unidentified Speaker

Let me answer that question. First of all, your first question was about net premiums written, the growth rate of different entities. And from the perspective of net premiums written growth, in this industry, auto policies, auto insurance, is experiencing hike in the premium rate.

The timing as well as the number of the hikes that take place, of course, may differ. Most recently at Sompo Japan and Nipponkoa, we raised the premium rate in April this year. And prior to that, in this industry, the peers raised their rates in October. And then they will do so again in October this year, or they have done so this year as well.

So looking at those timings, the level of the hike may make some difference to the growth in the net premiums written. And because of that, maybe we are less than the peers in the growth of the premium income.

And because we are expecting the merger. And the practical merger will take place effective of April next year, after we have merged the entities, there could be some share adjustment that may take place. And this is something to be seen in any industry. So I believe after we made that announcement, that it did take place.

Going forward, I think that the phenomenon is now done. And I think it's going to improve from here onwards.

Regarding Himawari Life, for the new policies, including third sector, the ANP growth is lack-lustering, as what you mentioned. On this point, as you know, the third-sector products and others, there is fierce competition taking place in the market. Especially after this fiscal year started with medical insurance, etc., the premium has been discounted. And there are peers who are attacking this area with price policy. So we are impacted by those moves.

Our strength is that we have the P&C channel and we have a good grip of the P&C policyholders. And we only have about 6% penetration of the life sales within the P&C channel. After the practical merger takes place, which is the P&C side. And then with Himawari Life within the same Group, we will be creating, or we have created a plan to strengthen the sales channel. And towards the end of March, we are already acting on those plans.

Another factor is that every company has been impacted by the lowering of the price in the industry. In Himawari Life, the premium level had not been revised for more than five years. Therefore, right now, we are preparing to revisit the premium level for Himawari Life.

So the P&C channel, strengthening of the P&C channel, from the P&C side, actually, although the branch managers have been put into one structure under the one-bill strategy; and the sales target originally for both Sompo Japan and Nipponkoa now have a combined sales target so that the two entities can cooperate and collaborate in achieving the sales target. And we're already doing this one year prior to the legal merger. And I'm sure we will see some good fruits coming out of this effort.

About the reinsurance assuming business overseas, the profitability of the reinsurance assumption business, when we show you [ph] on the combined ratio slide, if you look at the combined ratio improvement auto, combined ratio improved by 3 points and, therefore, reinsurance assumption business improved by 2percentage points for combined ratio. That was our plan.

Therefore, the profitability of the reinsurance assumption business is sure to be achieved to some extent. However, the nat cat loss does bring in some volatility to the business. If there is a large natural catastrophe, of course, our original plan for 2015 was JPY60 billion. And so it might diminish that profit. But of course, we have leveled such impact of the natural catastrophes in the plan.

For nat cat occurrence, in years with less nat cat, it expands profit. If we have a year with big nat cat such as hurricane, then that might blow off the entire profit. But towards 2015, we are expecting the leveled profit in the years included towards 2015.

I believe I covered all your questions.

Q - Natsumu Tsujino {BIO 2234779 <GO>}

For auto, looking at the number of vehicles, Nipponkoa is reducing its number of vehicles. So I believe that comes from the adjustment of market share. And I know I am still on this point. But for this fiscal year, you are already seeing that come through this year. Therefore, we will not see that impact next year. Is that correct?

A - Unidentified Speaker

That's right, because we did already announce about the decision and the announcement about the merger. So for such impacts that may come from the announcement, I am sure that has already come through and is diminishing.

For this year in October, looking at the situation in October this year, this is for non-fleet auto policy, number of policies, the vehicle number is actually on the increase. Towards the end of September, it was declining. However, if you combine SJ and NK, the number of policies for auto is now on the increase. And I believe it's going to continue to increase as a trend is what I believe.

Q - Unidentified Participant

Thank you.

Q - Wataru Otsuka {BIO 16340098 <GO>}

Wataru Otsuka, Nomura Securities. I have two questions. My first question is on the merger. On page 40/41, as it shows the merger plan, on page 40 specifically, actions to be implemented and actions that have been implemented are laid out. And among those actions, what were the positive factors and what were negative actions?

In other words, directors and sales forces are combining into one-wheel, one team. And there is confusion in the marketplace, or is it more positive offsetting all the negative factors?

And on page 41, you explained merger synergies and one-time merger costs. And one-time merger cost was increased and merger synergies also were revised up. So simply, if you add merger synergies and one-time merger costs together, it seems like synergies are larger now on a net basis. Am I right?

That's my first question.

And the second question is more qualitative question. As Mr. Sakurada mentioned, towards the achievement of the management plan, you feel that you have good probability of achieving the management plan. But specifically in P&C business and life business and overseas business, where do you see the higher possibility of achieving medium-term business plan? In what specific business areas?

A - Unidentified Speaker

Let me answer your first question, one-wheel strategy. There are positives and negatives. And sometimes, negatives became positives. And positives do not really become negatives usually. But simply put, the human resource HR area was the most impactful area, close to 30,000 employees.

I really think about the future of the Company and the symbolic, atmosphere [ph] symbolic trend, was the HR selection. Who is going to become the general manger? Who is going to be the head of sales; director representing sales over HR head? So it's very important for the Company to really select and decide right people.

In that process, myself and Mr. Futamiya [ph] shared our views together and we took a long time. And we really made this process very transparent. We asked third parties, such as consultants, to be included in this process. And they helped us evaluating people. And we got involved directly and we had discussion directly. And we evaluated each person.

So employees now know that this is a fair and open process that was positive. And secondly, they think -- they really agreed on what we did on that selection or evaluation process. So they may had some anxieties. But those anxieties are now gone with this fair and open process.

So selection of directors, selection of store managers were selected fairly. And that HR decision making was made quickly. So nobody is from either side, SK or NK, we are representing both companies now, we are working for the same company. And now we face more concrete challenges such as agency issues, such as non-exclusive agencies or exclusive agencies. So the challenges that we face now are more concrete.

In my opinion, there was no negative action. If I have to name one, as Mr. Tsuji mentioned, probably share adjustment happened partially. But share adjustment was less than we anticipated at the beginning.

And as we mentioned, merger synergies and one-time merger cost, both were devised upward. In terms of the one-time merger cost, it was due to the system-related cost. One-time system-related cost is going to occur earlier than planned. And secondly, the early retirement special program is going to be implemented additionally. And on the synergy side, we are going to see positive merger synergies ahead of our original plan. So the specific mechanism, or specific numbers, will be explained in more details later.

In the medium term and in the long term, what is my view of our performance in the future in P&C life and overseas? Probably, NKSJ Group is going to see the most contribution from overseas in terms of the top line growth and bottom line growth. But it depends on how we measure. Is it going to be measured by growth rates? If so, then this year, we see the most growth in Japan. First in P&C and life business in Japan, we would like to solidify this base, whole market business first.

For P&C business segment, at this point, I cannot say clearly. But I feel that it has bottomed out. There are some uncertainties such as consumption tax hike, frequency. And repair cost hike per unit per claim. But these are common issues faced by the industry; this is not unique to NKSJ. So with some time back, it should be recovered. So P&C is bottoming out. And I think we can secure 5% margin, as planned over time.

This is cyclical business. We are getting to the positive phase now. As Miss [ph] Tsujino asked, the price competition has started at faster speed than we anticipated in the life business. So in the life business, we have to really make sure that we improve our performance. If we really prioritize on the volume, it will hurt our bottom line profit. So we have to be prudent. So at the holdings level, Himawari Life, we are telling them not to be so aggressive on the pricing front. We have to strike a good balance.

In the future, as we expand our product line-ups in the life business, we have a good sales channel. We have sales channel presence in 35 prefectures out of 47. And we have sales channel which is very strong, with financial organization such as banks, regional banks. So non-savings type. Protection-type products will see needs in the future more and more. So I see there is a growth potential. But I cannot quantify this opportunity at this point.

Q - Wataru Otsuka {BIO 16340098 <GO>}

Thank you.

A - Unidentified Speaker

About the merger synergies and one-time merger costs. On the one-time merger cost side, in 2013, it increased due to the recruitment of the early special retirement program. So we have to pay JPY5.7 billion special premium to those retirees.

And versus the beginning of this fiscal year, the number of people for which we recruit for this program is larger. And we are consolidating agents or stores ahead of the original plan. That's one of the reasons.

And also, merger synergies were increased because of the following reasons.

First, we conducted early special retirement program last year. We asked for 400 people. But 470 people applied for this program and we accepted all applications. Therefore, the labor cost was decreased. So that's a positive merger synergy.

Q - Wataru Otsuka {BIO 16340098 <GO>}

Let me confirm one more thing. Mr. Sakurada mentioned that he felt that P&C was bottoming out. That's because new prices being penetrated well and agencies are working towards the revised pricing table?

A - Unidentified Speaker

Yes. In principle, that's correct. But if you look at the whole market, I think the sentiment of consumers in reaching for lower priced insurance products has changed. It has turned around. One of our Group companies, which is Saison Fire Company, is doing well. It's been accepted very positively by the market. But they are not offering the cheapest price in the industry. So price sentiment or price sensitivity has improved positively. I think they are more sensitive towards quality.

Q - Wataru Otsuka {BIO 16340098 <GO>}

Thank you.

Q - Jun Shiota {BIO 4127431 <GO>}

Shiota, Daiwa Securities. I have two questions for you. My first question is regarding shareholder return. If you go to page 50, you are showing the diagram for fiscal 2013, JPY60 per share of dividend payment; and shareholder return stock buyback is considered. And if you look at the bar for 2014, the size of the bar is quite similar. Then looking at the length of the bars beyond that, it looks like the bar is getting longer and longer.

Dividend plus share buyback, how do you see them to you? Because once you increase dividend, you cannot reduce dividend. So I guess shareholders have better reliance over dividend. However, looking at the length of the bars, what will be the timing, the right timing to see increase in dividend going forward? So from Mr. Sakurada, I'd like to know your thoughts over the dividend hike timing.

My second question is regarding that do have more accuracy in achieving the target for the medium-term management plan? Beyond the current MTP, ROE of 7% or more is beyond the current MTP. However, when you said that you need to mention ROE, I don't think you'll be satisfied just with 7% of ROE.

In actual value, P&C combined ratio of 95% or below, if this achieved, then what will be the level of the combined ratio to be achieved beyond MTP? Do you think you'll have more room to lower the combined ratio beyond 95%? So what is the profitability of the P&C business looking at the long-term horizon?

A - Kengo Sakurada {BIO 15149542 <GO>}

Thank you for your question. It was a very difficult question. For the first part of your question, it's not that we have something like a formula. So it is a concept of how we look at it. Right now, what we think is as follows. And the policy should not change so often. Let me give you that as a footnote before I answer.

We do exclude life adjusted profit. We take the consolidated adjusted profit, excluding life adjusted profit. And 50% of that is the total shareholder return. So that is the basic policy about shareholder return.

The consolidated adjusted profit, excluding life adjusted profit in value, how much of that is going to grow is part of your question. And that means we need to be raising ROE. And how you measure the return, the R part is, of course, on an adjusted basis. Therefore, it is different from the statutory accounting basis P&L.

The other important point is that when we exclude life adjusted profit from the calculation, do we exclude this part forever? Embedded value contribution to the P&L, once we become more clear, or once there is a wider understanding about the EV contribution to the P&L. And once EV becomes a more reliable calculation among the investor circle, then we might not exclude the entire life adjusted profit but we might consider a part of it or part of the EV to be part of the source for shareholder return. That is my personal view.

So how will that evolve over the medium to long term? Will I be satisfied with ROE of 7%? Obviously not. Of course, part of that depends on the calculation. But as it was mentioned with the BPS question, there is a double structure issue. And especially for financial institutions in retail business, how to raise profitability is an industry-wide issue. And especially us. Because we want to be strong in the retail area, this is obviously an issue for us.

So what is the specific ROE percentage that we want to target over the medium to long term? At least, we want to achieve double-digit ROE over the medium to long term.

Of course, there is a way to not go after scale by simply going after the percentage. So I do not intend to just stick only percentage. But in any case, 7% is not a satisfactory level.

The assumption behind that is the combined ratio as well as ROE. These are the two important indices. And beyond 95%, can we improve it much more? Because P&C insurance is so public in nature, we will never see a day when we have a combined ratio of 80% or 85%, because if we achieve such combined ratio, we have to be taking more risk or we have to be lowering the premium. There is a cyclicality involved in the market.

So I would say that in between 90% to 95% is a good level to be considered as the combined ratio in the future. Once we have 90% or 95% combined ratio, when you back calculate it, you can calculate the return. And also do another calculation to come up with the ROE.

If you do the math, you might say that, no, that will not get you to a double-digit ROE. Well you're only looking at the insurance side of the business. We have other businesses within the Group, such as financial business or services business. And these are the businesses that we want to nurture going forward as part of our medium-term management plan.

That is my answer to your question.

Q - Jun Shiota {BIO 4127431 <GO>}

On the first point, the share buyback versus dividend, if you compare the two, what your thoughts?

A - Unidentified Speaker

That theme, actually, I'm in charge of that theme. And I need to make many proposals to the Board of Directors meeting. And I will be responsible for that.

So stable dividend first of all is our basic policy. So it's not something that we make decision on every year or every time. However, for example, even if the payout ratio is below 50%, as long as it does not go below 50% over the medium to long term, that is not a problem to us.

So if you look at this MTP, for 2014 and 2015, I guess in 2015, excluding life, the adjusted profit will be about JPY100 billion. And 50% of that is going to be JPY50 billion. And so JPY60 can become JPY120 by math. But for 2010 and after, when we were even booking a loss, we paid out JPY80. So for 2014 and 2015, we were pre-emptively using the profit that we projecting to make in the future years back then.

For share buyback, the decision will be made in a flexible manner every time the time is right. Right now, it's not something that we have a decision to do so now. We will have to look at the profitability flow, the risk buffer, etc.. And make decisions from time to time.

What you have pointed out, some of the large factors, the reason we did share buyback this year, it was by about JPY8.3 billion. And the reason we did that is, first of all, looking at the risk buffer, overseas M&A, about JPY200 billion in size, was going to be executed. And that was part of the plan after the announcement of the merger.

And it's not that we have withdrawn that plan. Right now, we have about JPY50 billion to be the source of the shareholder return, including dividend increase.

Looking at the overseas companies, if we buy them with the PBR of 2 times or so, risk buffer would be required by about JPY100 billion. And if you look at the risk buffer, we have about JPY800 billion. And then that much money could be paid from that buffer.

For the selling down of strategic-holding stocks, the value of the stocks are sold. And 40% of that value is the risk that we will be able to mitigate. And so that reduces risk and increased risk buffer.

Driver Rating System change; the total effect coming from the Driver Rating System change has not come through fully yet. We also need to counter the rise in the consumption tax. And we need to put some measures to that after reading off the full impact coming from the Driver Rating System change. And all of those will be combined in a set and to be considered towards the end of the year. And after doing all that, we can finally make a decision about share buyback. That will be the flow of the process.

Of course, share buyback, we have done it by JPY8.3 billion. If we execute it, the risk buffer does get reduced. But by value, from the entire amount, this is not a huge weight. But there certainly is a managerial issue. And together with making managerial decisions about other matters, in a similar way, we want to be making decisions about share buyback.

Looking at the profitability situation, the economic situation, etc., the shareholder return plan will be made as part of the major management decision as we make on day-to-day business.

Thank you.

Q - Futoshi Sasaki {BIO 17564798 <GO>}

Sasaki, Mitsubishi UFJ Morgan Stanley Securities. I have two questions. My first question is about your stock repurchase. Earlier, you mentioned that you were going to make a decision by applying your common sense. But if you do so, for example, last year, you paid out about JPY8 billion in total. Is it possible for you to do the share repurchase exceeding that amount? Is that rational? Does that make sense to you?

That's my first question.

My second question is about the long-term profitability projection of automobile business segment. Japanese Government is trying to build a transportation infrastructure free of accidents. And by a large scale, by 2020, MLIT is going to build a significant infrastructure; and there may be more innovations, such as more automatic driving support systems. But how does that impact your profitability going forward on your automobile insurance business?

A - Unidentified Speaker

Let me answer your first question first about the size of the potential share buyback. We did JPY8.3 billion in share buyback last time. When we decreased our dividend from JPY80 to JPY60 per share, we allocated JPY20 difference for the share buyback. So in the future, or for 2014, we are going to study whether we are going to do share buyback or not based upon the performance of 2013.

So we would like to see how we perform in 2013. And the study of shareholder return specifically in 2014. So at this point, there is no set specific size. Our mind is very flat, is very open to whatever depending upon the performance.

And let me answer your second question. So your question was about self-driving vehicles; and I've been thinking about this. But a short answer to that question is that I don't know at this point. But what's clear at this point is that there are three methods for self-driving cars. First method is Google type, surrounding GPS technology. They use the map that is very close to real map; and utilizing GPS, the vehicles are self driven.

And the second method is Toyota or Honda method by communicating infrastructure, such as roads and streets.

And the third method is Nissan method, which is totally autonomous. And wherever you are in the world, your car can be driven automatically.

So among these three methods, we don't know, at this point what method is going to be adopted by the Japanese Government? That's something that we are going to discuss, or the Government is going to discuss. But when they choose one method among the three, for example, when they choose the other method, are they going to not need Nissan method or Google method at all? The answer is no. It takes time until they decide.

And when the number of self-driving cars increases, is that going to decrease the number of accidents? It's neither yes nor no. But the risk profile will be totally different.

So if the vehicles will be auto-driven vehicles, are we going to see no accidents at all? That's not correct. It depends on the risk. When an accident happens, who should be responsible for that? Is that the responsibility of the car maker, or is it the responsibility of the owner? Or is it the driver's fault? He or she could put their feet on the brake. But he or she didn't. Is that their fault?

So the product liability, this involves product liability whole matter as well, where or who should take the responsibility. So it depends on the kind of risks that we are talking about here. Is it going to be a brand new insurance? Or is it going to be continuation from the current insurance scheme? We don't know at this point. We are in the middle of that process.

I don't know how much of vehicles will be shifted to auto-driven vehicles. It's not 100% as a right of citizenship. The Government can't deprive people of the fun to drive. So is it going to be 20% auto vehicles? If that's the case, then they have to drive by looking at manually-driven vehicles. So there are prudent drivers, like myself. And there are wild drivers like my colleague, Mr. Tsuji. So I am fully supporting this auto driving scheme. But the quality, the nature of the risk may be changed.

So premium is not going to go down because of the less accidents. But there is a pre-crash system which is commercialized already, like EyeSight made by Fuji Heavy. And they are currently collecting the data with that device. So they can get other data, such as the vehicles with less probability of accident, or high probability of accidents. Then we can have a discount scheme depending upon the risk profile of vehicles.

But the data is not enormous yet that can be treated as low or large numbers. So it's a very tricky issue. But in the transition phase, we are going to see more visibility. We are talking about the phase of five years or 10 years.

I don't know if I answered your question correctly. But thank you so much.

Q - Tatsuo Majima {BIO 15338044 <GO>}

Majima, Tokai-Tokyo Research Center. As answer in factors [ph], you talked about the consumption tax as well as the effect of the new grade rating system. This may be another uncertain factor. It could be. And what I think is, the impact of the revision of the insurance business floor [ph]. For P&C agents, there will be requirement for information confirmation as well as intent confirmation of the policyholders. And also allowing the FSA to do an on-site inspection of the exclusive [ph] agents.

If it goes to the Diet within 2014, it may take effect as of 2014, which means that the revision of the law may take place within your medium-term management plan period. And will this require additional cost to the exclusive agents, or on your side in order to revise the systems? So this a cost incurring item? That is my question.

Also is that if the revision takes place in order to facilitate the autonomy of the agents, do you think it will be impactful enough to unwind the double structure that exists in the insurance industry?

Please answer two of my points.

Thank you.

A - Unidentified Speaker

To your first question, as of today, the specific impacts coming from the revision of the laws, especially the numerical impacts coming from the revision of the law, is still uncertain. Therefore, we have not done any specification. So we have not created any projections based on it. Therefore, our stance is to monitor the situation as it progresses.

To your second question. We are basically doing the same thing. So it will be an agenda item going forward.

Thank you.

Directly to the business plan, or will it get reflected on to the constat [ph] is what that Tsuji-san answered.

Another point about this revision is to educate the policyholders. It's not that we are looking down on them. But it's important for the policyholders to be assured about the quality of the agencies that they are buying policies from. I think it becomes a good chance for that to happen in the market, because up until now, it was the insurance companies through the agency channel to make them more autonomous in order to evade the double structure.

However, it is the policyholders who hold the abundance power because they pay the commission. But there's agency A and agency B; why is the cost so different between the two? And when they realize that, some major change might happen in the market. And if it leads to revision of the law, then I'm sure the framework will be re-set. And I'm sure that kind of move will happen; I think it should happen. And this is going to be a positive impact to the entire industry.

Did that answer your question?

Q - Hideyasu Ban {BIO 15250840 <GO>}

Ban, Morgan Stanley. I have two questions. I don't know how appropriate it is to be asking you about next year's business. But today, on page 41, you update us about the merger synergy and one-time merger cost. And if you compare the two numbers for next year, the difference is JPY33 billion. And I think this is going to be a factor to push down the profit next year.

And I know that the reported P&L numbers is not the most important number. However, there are index such as Nikkei 400 which decides what to be included based on the ROE. So I don't know how you regard the reported ROE. And also, when you have a factor to push down the profit by JPY33 billion, how you plan to fill that next year.

For the adjusted profit for fiscal 2014, I know that JPY150 billion of adjusted profit is on the horizon. For life EV, we will make up JPY100 billion; overseas will be about JPY10 billion. That means domestic P&C will be about JPY40 billion to JPY50 billion of adjusted profit. That means you need to make your top line to increase by about JPY20 billion in order to get to the adjusted profit.

It's only on the rough estimate. But if the price revision takes place in the early part of next year and will still make effect for the rest of the year, then would that be a significant factor? And with that possibility included, am I right in estimating that the domestic P&C adjusted profit for next year will be JPY40 billion to JPY50 billion? And what will be the steps of the process to get from this year to the JPY40 billion to JPY50 billion next year?

A - Unidentified Speaker

Let me answer that question for 2014. For fiscal 2014, synergy is JPY40 billion. The way we showed it that way, actually, was the first time that we've done so today, because up until now, we talked about JPY75 billion of one-time cost. That's all we had explained so far.

And what we have been saying is that with the practical merger, there will be more rationalization and more synergy to surface. Therefore, we have come to announce the synergy and cost in the way we did.

For one-time cost, it's going to get excluded from the adjusted profit; not the entire amount. But most of the amount will get booked as extraordinary loss. Therefore, the source of the shareholder return, which is adjusted profit, will not have the impact of the cost.

And in 2014, how do we secure the profit of the domestic P&C business? The heaviest factor is the consumption tax change. For this fiscal year, for claims reserve, although the claims payment may occur next year, then we will have to top that with consumption tax, higher consumption tax, in paying the claims, even if the provisioning wasn't this year.

Therefore, as I repeat, the grade rating system impact has to be fully understood. And we must also consider the pricing. And if necessary, we might have to do the price hike in order to counter the situation. However, it has not been decided. And going forward, we will take some time to study the issue.

No further questions? If not, we would like to close this IR meeting. Thank you. So much for attending our conference. Thank you.