

## DaltonInvestments

The Board of Directors  
Shinsei Bank, Limited  
Nihonbashi Muromachi Nomura Building,  
4-3, Nihonbashi-muromachi 2-chome,  
Chuo-ku, Tokyo, Japan

March 16, 2017

Dear Sirs:

Thank you very much for your continuing efforts to enhance the value of Shinsei Bank and for your openness in engaging with shareholders. As fully engaged minority shareholders, we are writing this letter to express our appreciation as well as to share our views. In aggregate, across all of the accounts for which we have responsibility, Dalton Investments LLC and its affiliates and advisory clients (together "Dalton") currently own 2.3% of the shares of Shinsei Bank. Our clients include the permanent endowments of major universities, hospitals, foundations and museums, as well as the pension funds of working men and women in North America and Europe. These clients have entrusted us to be wise stewards of their capital.

The year 2016 witnessed huge upsets in world politics as well as in capital markets, resulting in a downturn in the share prices of Japanese banking stocks, that was further compounded by introduction by the Bank of Japan (BOJ) of negative interest rates. This confluence of events provided us with a wonderful opportunity to buy Shinsei Bank shares for our clients at attractive prices. Our purchase of a stake in Shinsei Bank was not based merely on price. Rather it was dependent also on our respect for the management of Shinsei Bank. This has been repeatedly demonstrated by its impressive track record of building respected and unique business franchises such as the consumer finance franchise represented by the "Lake" brand, as well as by the bank's robust capital base that provides the flexibility to pursue various strategic initiatives. We believe the young and bright management team, possessed of global vision, will continue to drive the future success of Shinsei Bank.

Unlike other Japanese banks with few attractive opportunities for capital allocation, Shinsei Bank will be able to use capital effectively for growing its consumer finance businesses. With that said, we nonetheless believe the bank today is massively overcapitalized. The bank has ample reserves in its consumer finance businesses, significant unrealized tax losses, and a Consolidated Core Capital Adequacy Ratio of 14 percent—one of the highest in the world among international banks. By any measure, Shinsei Bank has substantial excess equity capital. Our appraisal is that the bank is worth at least Y850bn, based on (a) the sum of Net Present Value of cash flow from businesses (approx. Y500bn, excluding impact of tax assets) and (b) excess capital of at least Y350bn. The current appraisal by the stock market of the company is only Y570 billion. This represents a huge discount to fair value. We would not be at all surprised to see a stock price at twice current market levels given the growth and potential synergies between the consumer finance and banking businesses.

We consider the discount to fair value more attributable to the lack of recognition of excess capital held by the bank rather than to its business operations. This view is supported by relatively low historical shareholder returns and the uncertainty related to the repayment of public funds arising from the bailout.

The combination of ample excess capital and a cheap share price leads to a simple, logical conclusion: a large scale stock buyback to create value for all shareholders. The conclusion holds regardless of the existence of the government as a large shareholder because the interests of all stakeholders - the government (as a guardian of national wealth), management, and minority shareholders are, or should be, aligned. A substantial repurchase of the bank's shares would drive up the bank's book value per share, the reported earnings per share and the return on equity. All of these metrics, in turn would lead to a higher share price over time. All stakeholders would benefit.

Therefore, we ponder the following question: 'Why didn't share buybacks occur when alluringly attractive opportunities present themselves, as they did last year?' We are aware of Yen 10 billion in buybacks last year, and the recently announced additional Yen 2.5 billion buyback; but those are negligible amounts compared to our estimates of excess capital of Yen 350 billion. As a shareholder, this is the biggest puzzle and the greatest risk of the investment we have made on behalf of our clients.

We are concerned that perhaps the government is preventing the use of excess capital to buy back stock because of unrealistic price targets of Yen 745 per share before allowing management the flexibility to make the buyback and thus to act in the best interests of all shareholders. Or, perhaps the government is waiting for more advantageous conditions of exit, such as using an exchange offer of preferred securities for common shares. While we understand that the preservation of national wealth is of critical importance to the government, we question if a fixed price objective should be placed ahead of economic rationality and the interests of minority shareholders. Doing so would leave an indelible stigma on the reputation of Japanese capital markets and inflict enormous damage to the highly respected corporate governance reform efforts of the current administration. We would like to ask the board of bright directors not to yield to such government pressure (if it exists).

We would like to make two proposals for consideration.

### **1. 200bn Yen share buyback program**

Buybacks are less common in Japan than in the United States. But, in our view, we think that the example of the case of American International Group ("AIG") in the US is particularly relevant and compelling. Doubtless you will recall that AIG was rescued by the United States Government, acting through the Federal Reserve and the Treasury in the fall of 2008 at the height of the global financial crisis. The government made available substantial lines of credit and acquired 80% of the outstanding shares of the company. After new management was installed, the company was cleansed of its questionable assets and the operations rationalized. The share price responded and began to climb. But there was still a large amount of negative sentiment surrounding the company because of the government's large ownership position. Because the stock price was at a substantial discount to the company's book value, the management realized that it could repurchase shares and compound book value quickly. This, in turn, would attract investors who would increase the share price and help close the gap between share price and book value per share. And, importantly, this increase would stimulate demand for shares and allow the government to sell its stake in the company.

None of this happened immediately—it took several years and several enormous buybacks that collectively shrunk the shares outstanding dramatically. But the important point is that the management worked together with the government and the regulators, as well as with representatives from minority

shareholders to make this happen. It was truly a winning formula that benefited AIG, its shareholders, and the government.

We would like to propose that the bank implement a Yen 200 billion share buyback program. As discussed, we believe the excess capital of the bank amounts to Yen 350 billion based on the reasoning that:

- (1) 10% Tier 1 ratio, together with a rational rebalancing of risk assets, will provide sufficient capital to sustain and grow current businesses, and
- (2) roughly 50% of off-balance tax losses carried forward should be regarded as virtual shareholder's equity.

Our proposal of Yen 200 billion also reflects approx. Yen 264 billion retained earnings at the parent company level (as of March 2016), but the capacity could be expanded to Y300bn with a 2-3 year time horizon as the bank continues to retain more earnings.

Of course, the announcement of such a large stock buyback program could have a material impact on the share price, so the planning and operation must be executed very carefully. On the other hand, there are no guarantees that such an attractive environment for price buybacks will last for long and thus time is of the essence. We estimate Yen 200 billion in share buybacks at current prices will raise the BPS to Yen 340 from current Yen 286, but the outcome will be reduced to Yen 300 if the stock price goes up to 250yen. (See [Appendix 1.](#)) We believe that flexible and aggressive implementation of share buybacks at attractive prices will reward ALL shareholders as well as fulfill social responsibilities through repayment of public funds.

## **2. Implementation of Restricted Stock Compensation**

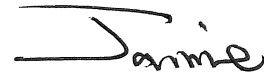
At the risk of repeating ourselves, we believe that alignment of the interests of all stake holders is a key driver to accelerating the effort for the repayment of public funds. In this light, while we are aware most directors own some shares of the bank, we believe this ownership does not rise to a sufficient level to foster a sense of ownership, with the possible exception of Mr. Christopher Flowers' holdings. Thus, we would like to recommend that the board implement Restricted Stock Compensation, which was permitted in Japan in April 2016 thanks to the initiatives of Ministry of Economy, Trade and Industry (METI) and the government. Among the various forms of stock compensation, we particularly like Restricted Stock as it gives the holder ownership from day one through voting rights and dividends.

If directors accumulate ownership to a significant level – desirably at the level of 3 to 5 times of their annual base remuneration – over the next 10 years, we believe that it will be a significant driving force not only for repayment of the public funds in near future, but also for long-term improvement of shareholder value by transforming the bank from government-controlled into a bank managed by a group of entrepreneurs with sound alignment of interests with other shareholders. Also we believe such benefit of alignment is applicable to Independent Outside Directors.

Needless to say, implementation of long-term performance based compensation is one of the important requests from the government in its corporate governance reform package, and we hope the bank will respond at its earliest convenience.

Please feel free to contact us if there is anything you might wish to discuss arising from this letter. We look forward to continuing our dialogue with you.

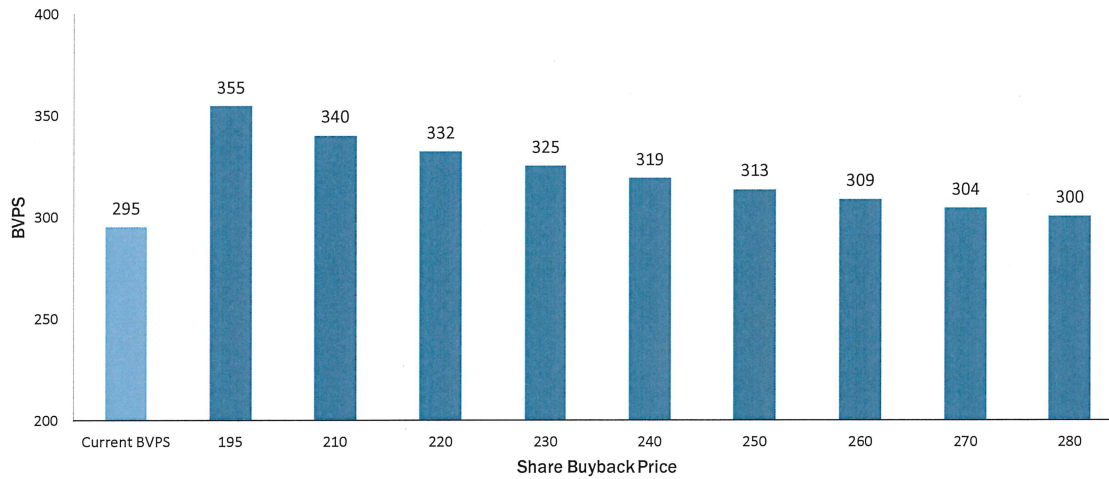
Sincerely yours,

A handwritten signature in black ink that reads "James". The signature is stylized with a long horizontal stroke at the beginning and a cursive "ames" following.

James B. Rosenwald III  
Co-Founder and Co-Managing Member  
Dalton Investments LLC

## Appendix I: Impact of Share Buyback

Impact of ¥200BN Share Buyback  
Current Estimated Book Value Per Share (BVPS): ¥286



Notes: Numbers of shares are calculated as Y200bn divided by share price.

## Appendix II: Japanese Translation<sup>1</sup>

株式会社新生銀行  
取締役御中

親愛なる貴社取締役の皆様、日頃より普段の企業価値向上への取り組み頂き、また株主に対しては積極的な対話の機会を賜り誠にありがとうございます。弊社は、関係会社保有分も含め、投資受託者として貴行発行株式済株式数のうち合計約 2.3%保有しております。私共の主な顧客は北米・欧州の年金基金、及び病院・大学・美術館の基金で構成されております。私共はこれら顧客の信任の下、お預かりした資金の最善の運用に努めております。

2016 年は世界の政治情勢及び国内の金融マーケット環境が目まぐるしく変化した 1 年でしたが、加えて銀行株は日本銀行によるマイナス金利政策の導入の影響も受け大幅に下落致しました。これらは私共にとっては貴社株式を素晴らしい価格で購入できた、素晴らしい機会となりました。しかしながら私共の購入動機は単に株価の変動に依拠したわけではございません。寧ろ、私共はレイクをはじめとするコンシューマーファイナンスの素晴らしいフランチャイズと、様々な経営戦略の実施を可能とする強固な資本基盤を築き上げたご経営陣のご実績を高く評価申し上げております。また皆様は国内業界と比較しても大変若く、グローバルな知見に富んだ有能なご経営陣である事は、今後の貴社の更なる発展の原動力になると信じております。

きわめて限定的な投融資機会しか持たない他の国内銀行と比べ、貴社は成長著しいコンシューマーファイナンスに今後更なる資本配賦の余地があると存じます。しかしながら、国際金融機関の中でも最も高い水準にある 14% に上る連結コア自己資本比率、加えてコンシューマーファイナンス分野での潤沢な引当や税務上繰越欠損金への保守的な引き当てを考えれば相当規模の余剰資本があると私共は考えております。株式評価については様々な考え方があろうかと存じますが、私共は貴行の企業価値を保守的に見積もっても将来収益の現在価値（5,000 億円程度、引当金繰り戻しによる利益底上げ効果を除く）と余剰資本（少なくとも 3,500 億円程度）の合計 8,500 億円程度と考えております。これは現実の時価総額 5,700 億円と大きなかい離があります。更にコンシューマーファイナンスの成長余地や銀行事業とのシナジーも考えれば、株価が現在の倍であっても過大評価ではないと考えます。

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<sup>1</sup> This letter is presented both in an official English version and in unofficial and courtesy Japanese translation. The translation is provided for informational purposes only and for ease of reference. In the event of any ambiguity about the meaning of certain translated terms or of any discrepancy between the official English version of the letter and the Translations, the English version of the letter shall prevail.

私共はディスカウントの源泉は前者、つまりビジネスそのものの評価というよりは後者の余剰資本の価値が適性に反映されていないためと考えております。その背景にはこれまでの貴社の配当・自己株買いが極めて保守的であったこと、加えて残存する公的資金への懸念とその返済シナリオが示されていない事への懸念が影響しているものと考えます。

余剰資本と割安な株価という2つの条件が重なれば本来経営者がとるべき行動はたった一つ、大規模な自社株買いです。この結論は政府が貴社の大株主であることを勘案しても変わりはありません。大規模な自己株買いを通じた一株当たり純資産及び利益の向上、そして結果としての株価の向上による恩恵は（国民財産の守護者としての）政府、経営者、少数株主すべてのステークホルダーが等しく享受するものです。

それが故に「なぜ昨年の様な絶好のチャンスに具体的なアクションが見られなかったのか？」その答えを私共は未だ発見できておりません。勿論貴社が100億円の自己株買いを昨年行った事（そして最近25億円の発表を行われたこと）は承知しておりますが、その規模は私共が3,500億円と推計する貴社の余剰資本規模に比べれば無視しうるものです。私共は株主として最大のミステリーであり、かつ顧客資金の受託者として最大のリスクをここに感じています。

我々が懸念するのは政府が現実的とはいいがたい一株745円の目標に固執し、経営者がすべての株主の利益を追求する裁量を奪っている、または普通株と優先証券のエクステンジオファー等を通じて政府だけに有利なエグジットを提供する事を要求しているのではないかという点です。国民の税金を原資とする公的資金の回収が極めて重要な課題であることは私共も理解しますが、仮にこの目的が経済合理性と少数株主の利益を犠牲にして行われるのであれば、日本の資本市場に拭い去れない汚点を残し、かつこれまで高い評価を集めてきた現政権主導のコーポレートガバナンス改革の努力も無に帰すでしょう。聡明な取締役の皆様がその様なプレッシャー（もし存在するとすれば、ですが）に屈しないことをお願いするとともに、対案として2つのご提案を差し上げたいと思います。

## 1. 2,000億円規模の自社株買いプログラム実施

日本において自社株買いは米国ほど活発には見られませんが、我々は米国のAIG(American International Group)の事例が貴社にとって最も適切かつ参考になると考えております。ご存知の通り、AIGは2008年秋の国際金融危機の最中、連邦準備銀行及び米国財務省を通じて、米国政府の救済を受けました。この際、政府は大規模な与信枠をAIGに提供し、発行済株式数の約80%の株式を取得しています。その後経営陣の刷新、不良資産の処理・業務改善が遂行され、株価も呼応して形で

上昇し始めましたが、それでも政府による AIG 株式の大量保有は株価の大きな重石となり続けました。このような状況下、経営陣は一株当たり純資産に対して大幅に割安な株価を活用すること、すなわち自社株買いを通じて一株当たり純資産を急速に高める戦略を実行したのです。この施策が投資家の評価を受け株価上昇をもたらし、結果として一株当たり純資産と株価のかい離の解消をサポートしました。そして重要な点として、株に対する買い需要が生み出され、政府の持分解消を容易にできたのです。

これらは一度に起こった事ではございません。複数回にわたる巨額な自社株買いの繰り返し行い、発行済株数を劇的な減少が達成されるまでには数年の歳月がかかっています。しかし、私共は経営陣が政府、当局、そして少数株主との協調によって成し遂げられたものであることを強調したく存じます。AIG のケースはすべてのステークホルダーが報われた事例と言えるかと思えます。

今回、私共は 2,000 億円規模の自己株買いをご提案致します。上記に述べました通り私共は 3,500 億円程度の余剰資本があると考えます。これは、

- (1) 適性なリスクアセットの入れ替えを進めれば、現行のビジネスは 10%程度の Tier 1 比率で十分維持・成長可能という想定、及び
- (2) ほぼ 100%引き当てられている繰越欠損金は貴社の収益力にかんがみればその 50%分程度は株主資本とみて良いだろうという想定

に基づきます。またこの提案は、貴社単体の利益剰余金が約 2,640 億円（2016 年 3 月末時点）という現実を踏まえてこの水準をご提案しておりますが、この規模は今後 2-3 年という時間軸では 3,000 億円まで引き上げることも可能でしょう。

勿論自己株買いのアナウンスメントが株価に与える影響も無視できるものではありませんので、実際の運用（期間・回数）については慎重に模索する必要があります。しかしながら一方で現在の様な自己株買いを行う上で魅力的な株価水準がいつまで続くかは保証の限りではありません。現行の株価で自己株買いを行った場合、2,000 億円の自己株買いで計算上 340 円程度まで一株当たり純資産を高める事ができる一方、仮に 250 円まで株価が上昇した場合、その効果はほぼ 300 円まで減殺されます。私共は、株価が低迷した際の機動的かつ積極的な自己株買いがすべてのステークホルダーに平等に報い、また長期的にも公的資金の返済という社会的責任を果たす道程となるものと信じております。



## 2. 株式報酬制度の導入

くどい様ですが私共はすべてのステークホルダーの利益が共有されることが大事であり、それによって公的資金返済に向けた力強い推進力が生まれると考えます。この点、貴社取締役の大半は株式を所有されてはおりますが、その水準については社外役員のクリストファー・フラワーズ様を除き、オーナー精神を醸成するレベルには至っていないのではないのでしょうか。このような問題意識に基づき、私共は2016年4月より政府・経済産業省の後押しにより可能となった譲渡制限株式を利用した株式報酬の導入をお勧め致します。もちろん株式報酬制度には色々な類型がございますが、私共は受け取ったその日から議決権と配当を受け取る権利が発生する譲渡制限株式がオーナーシップ醸成の観点から最も素晴らしい制度だと考えます。

仮に今後10年程度の時間軸で取締役の皆様の株式所有が意義ある水準に達すれば（固定報酬の3-5年分相当が望ましいと考えますが）、その効用は公的資金返済という短期の目標達成にとどまりません。貴社を政府支配下の銀行から株主と健全な形で利益を共有する企業家集団が統治する銀行へと変革し、長期的な株主価値向上に向けた推進力となるでしょう。尚、私共はこうした報酬制度が社内のご経営者のみならず独立社外役員の皆様に対しても適用される事が望ましいと考えます。

言うまでもなく経営陣報酬に中長期的な会社業績を反映させ、健全な企業家精神の発揮に資するようなインセンティブ付けを行うことは現政権のコーポレートガバナンス改革の中でも重要なリクエストの1つです。近い将来、貴社の対応が進むことをご期待申し上げます。

今回のレターについてご不明な点がございましたら遠慮なくお問い合わせください。引き続き対話の機会を頂ける事を心より楽しみにしております。

親愛の念を込めまして