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## Revision to FY2023 Full-Year Earnings and Dividend Forecasts

TOKYO February 1, 2024 — Aozora Bank, Ltd. ('Aozora' or 'the Bank') today announced that its Board of Directors resolved to revise its FY2023 full-year earnings and dividend forecasts announced on May 17, 2023 as described below.

### 1. Revision to FY2023 Full-Year Earnings Forecast (April 1, 2023 to March 31, 2024)

#### Consolidated basis

(billion yen)	Ordinary profit	Profit attributable to owners of parent	Profit attributable to owners of parent per common share
Previous forecast	31.0	24.0	205.51 yen
Revised forecast	(49.0)	(28.0)	(239.76 yen)
Change	(80.0)	(52.0)	-
Percentage change	-	-	-

#### Non-consolidated basis

(billion yen)	Ordinary profit	Net income	Net income per common share
Previous forecast	27.0	19.0	162.69 yen
Revised forecast	(54.0)	(35.0)	(299.70 yen)
Change	(81.0)	(54.0)	-
Percentage change	-	-	-

### 2. Revision to FY2023 Dividend Forecast

Record date	Dividend per common share				Total
	June 30 (1 <sup>st</sup> quarter)	September 30 (2 <sup>nd</sup> quarter)	December 31 (3 <sup>rd</sup> quarter)	March 31 (4 <sup>th</sup> quarter)	
Previous Forecast for FY2023	/	/	-	-	154 yen
Revised Forecast for FY2023	/	/	/	0 yen	76 yen
Payments in FY2023	38 yen	38 yen	0 yen	/	/
(Reference) Payments in FY2022	38 yen	38 yen	38 yen	40 yen	154 yen

### 3. Reasons for Revision to Earnings Forecast

The Bank's customer-related business focusing on Aozora's Strategic Investments Business, which aims to serve customers in their three phases of "Fostering," "Change" and "Recovery," has been steadily growing under the Mid-term Plan "Aozora 2025" announced in May 2023.

Business-related profit (sum of business profit and gains/losses on stock transactions) from customer-related business was 36.4 billion yen in the first nine months of FY2023, and is expected to reach 44.0 billion yen for the full year, significantly exceeding the FY2022 result of 33.8 billion yen.

In order to establish a better foundation for the Aozora Group's growth in the next fiscal year and beyond, we have decided to take fundamental actions in FY2023 and significantly reduce future risks by addressing two balance sheet issues: (1) exposure to U.S. non-recourse office loan portfolio and (2) the restructuring of the securities portfolio.

#### (1) Additional reserves against U.S. non-recourse office loan portfolio

Due to higher U.S. interest rates and a shift to remote work accelerated by COVID-19, the U.S. office market continues to face adverse conditions combined with extremely low liquidity. While price discovery is anticipated to eventually improve with a gradual increase in office transactions on the back of an expected return-to-office movement as well as a pause in the rise in U.S. interest rates, our view is that it may take another year or two for the market to stabilize. With respect to office loans originated by Aozora, the recovery process has been bifurcated depending on region and the specific characteristics of the property. Given these circumstances, we decided to strengthen our reserves by making additional provisions to be more prepared for a potential increase in the number of workouts, including debt collection through a sale of the underlying property assets.

We have reevaluated all U.S. non-recourse office loans and reviewed property valuations from a forward-looking perspective, taking into account the risk of price declines over the next two years, in addition to the appraisal of properties based on current conditions. As a result of this process, credit-related expenses of 32.4 billion yen were recorded in the third quarter which included the maximum possible provision expected at this time. As a result, the loan loss reserve ratio for U.S. non-recourse office loans increased to 18.8% as of December 31, 2023, which we believe provides an adequate reserve level and minimize the risk of future losses.

#### (2) Acceleration of securities portfolio restructuring

With respect to unrealized losses on the securities portfolio, consisting mainly of foreign bonds, primarily due to the rise in U.S. interest rates we have decided to accelerate the disposition of securities with the aim to secure added flexibility in portfolio management and improve profitability in the next fiscal year and beyond.

We sold foreign currency ETFs in the third quarter and plan to sell a further portion of the remaining foreign currency ETFs and mortgage bonds. As a result, a loss of 11.1 billion yen was recorded in the third quarter and an additional loss of 29.8 billion yen is expected in the fourth quarter resulting in an expected loss of 41.0 billion yen in the second half.

Unrealized losses on securities were reduced from a net loss of 92.6 billion yen as of September 30, 2023 to a net loss of 81.5 billion yen as of December 31, 2023, and are expected to further improve to a net loss of 56.0 billion yen as of March 31, 2024, which will be a significant step toward the restructuring of the securities portfolio.

Please refer to the attached "Supplementary Material" for more detail.

#### **4. Reasons for Revision to Dividend Forecast**

In setting the FY2023 full-year dividend forecast, we had planned to provide a stable dividend based on the steady growth of our customer-related business and maintaining a sufficient capital adequacy ratio. However, while the customer-related business has been growing as anticipated, the consolidated capital adequacy ratio (domestic standards) and the CET1 ratio as of March 31, 2024 are expected to be approximately 8.8% and 6.6% respectively, temporarily falling below our target levels of 9% and 7%, respectively.

In order to retain capital for growth as well as to enhance our overall financial strength in the next fiscal year and beyond, we have decided to not pay a dividend for the third quarter and we are also now forecasting no dividend for the fourth quarter. As a result, the full-year dividend forecast for FY2023 has been revised downward to 76 yen per share.

We regret that we were not able to meet the expectations of our shareholders due to a failure to reach the initial dividend forecast. We would appreciate your understanding that this is a necessary step toward our steady business growth and stable dividend in the next fiscal year and beyond and kindly ask for your continued support.

#### **5. Business strategy for FY2024**

Our customer-related business focusing on Aozora's Strategic Investments Business have been experiencing steady growth. We anticipate achieving a net revenue of approximately 85.0 billion yen and profit attributable to owners of parent of approximately 17.0 billion yen for FY2024, driven by the overall growth of our business groups through the expansion of profitable businesses, the steady progress of GMO Aozora Net Bank (GANB) towards profitability, and signs of a positive outcome resulting from the structural reform in our retail business.

Due to progress in securities portfolio restructuring, we also expect that the unrealized losses on the securities portfolio to steadily decrease of a net loss of approximately 49.0 billion yen as of March 31, 2025.

Based on our capital policy of maintaining a proper balance among "stable shareholder returns" and "strategic investment," and "financial strength," we will strive to deliver a stable dividend by achieving steady growth in our customer-related business and maintaining a sufficient capital adequacy ratio.

With regard to the consolidated capital adequacy ratio which is expected to temporarily decline as of the end of March 2024, we plan to exceed 9% in terms of the domestic standard and 7% in terms of CET1 as of March 31, 2025 by taking measures including the accumulation of capital through improvement in business performance in the next fiscal year. In terms of shareholder returns, we aim to increase the FY2024 full-year dividend from the revised FY2023 dividend forecast of 76 yen per share.

We deeply regret the performance of this year and sincerely request the support of our stakeholders as we strive for growth under new management in the next fiscal year and beyond.

Forecasts and other forward-looking statements in this document are based on information currently available to the Bank and certain assumptions that the Bank deems reasonable, and are not intended to be a promise by the Bank that they will be achieved. Actual results may differ materially due to various factors.

## **Supplementary Material**

# FY2023 revised earnings and dividend forecasts (1)

## Earnings forecast

(billion yen)

		FY2023 initial forecast	FY2023 revised forecast	Change
<b>Consolidated</b>	Net revenue	86.0	51.0	-35.0
	Business profit*1	25.5	-8.0	-33.5
	Ordinary profit	31.0	-49.0	-80.0
	Profit attributable to owners of parent	24.0	-28.0	-52.0
<b>Non-consolidated</b>	Net revenue	70.0	34.0	-36.0
	Business profit (before general loan-loss reserves)	22.0	-13.0	-35.0
	Ordinary profit	27.0	-54.0	-81.0
	Net income	19.0	-35.0	-54.0

## Dividend forecast

	FY2023 initial forecast	FY2023 revised forecast
Full-year dividend per common share	154 yen	76 yen*2

## <Reference>

(billion yen)

	FY2021 results	FY2022 results	FY2023 projection
Business-related profit*3 (customer-related business excl. financial market-related and retail businesses)	29.4	33.8	44.0

\*1 Including gains/losses on equity method investments

\*2 No dividend to be paid for the 3<sup>rd</sup> quarter and no dividend is forecasted for the 4<sup>th</sup> quarter of FY2023

\*3 Business profit + Gains/losses on stock transactions

# FY2023 revised earnings and dividend forecasts (2)

- The Bank's customer-related business focusing on Aozora's Strategic Investments Business, which aims to serve customers in their three phases of "Fostering," "Change" and "Recovery," has been steadily growing under the Mid-term Plan "Aozora 2025" announced in May 2023. Business-related profit from customer-related business was 36.4 billion yen in the first nine months of FY2023, an increase of 9.8 billion yen year-on-year, and is expected to exceed the original full-year plan
- In order to establish a better foundation for growth in our customer-related business in the next fiscal year and beyond, Aozora has decided to take fundamental actions in FY2023 and significantly reduce risks by addressing two balance sheet issues: (1) exposure to U.S. non-recourse office loan portfolio and (2) the restructuring of the securities portfolio

## Earnings breakdown

(billion yen)	FY2022	FY2023				FY2023 2H Losses/expenses to be recognized
	Full-year	Interim results	3Q results	4Q projection	Revised forecast	
Net revenue	59.5	44.5	16.0	-9.6	51.0	
incl. financial market-related losses in 2H			-3.1	-29.8		Market-related -41.0
Business profit	2.5	15.6	1.6	-25.2	-8.0	
Credit-related expenses	-1.7	-9.9	-32.9	-0.0	-43.0	
incl. U.S. office loan-related expenses in 2H			-32.4	-		U.S. offices -32.4
Gains/losses on stock transactions	8.4	9.4	-7.8	0.4	2.0	
incl. financial market-related losses in 2H			-8.0	-		
Ordinary profit	7.3	14.3	-39.2	-24.2	-49.0	
Profit attributable to owners of parent	8.7	12.0	-26.7	-13.3	-28.0	

## Business-related profit\*

Customer-related business (excl. retail and financial market-related businesses)	33.8	29.5	6.8	7.7	44.0
Retail business	-5.2	-2.3	-0.7	-1.5	-4.5
Financial market-related business	-17.5	-2.2	-12.3	-31.0	-45.5

\* Business profit + Gains/losses on stock transactions  
Management accounting basis

# U.S. non-recourse office loans (1)

- Due to higher U.S. interest rates and a shift to remote work accelerated by COVID-19, the U.S. office market continues to face adverse conditions combined with extremely low liquidity. While price discovery is anticipated to eventually improve with a gradual increase in office transactions on the back of an expected return-to-office movement as well as a pause in the rise in U.S. interest rates, our view is that it may take another year or two for the market to stabilize
- With respect to office loans originated by Aozora, the recovery process has been bifurcated depending on region and the specific characteristics of the property. Given these circumstances, we reviewed property valuations from a forward-looking perspective and strengthened our reserves by making additional provisions as below to be more prepared for a potential increase in the number of workouts, including debt collection through a sale of the underlying property assets:
  1. We reevaluated all U.S. non-recourse office loans (47 borrowers) and reviewed property valuations, taking into account the risk of price declines over the next two years
  2. Following the above valuations, we downgraded borrowers of loans with an LTV of over 100% (and a high possibility of going into a workout process over the next two years) to NPLs, in principle, while taking into consideration factors including the specific characteristics of the property and regions
  3. We also applied a stress case scenario taking into account the impact of market volatility on the NPL borrowers and made additional provisions to loan loss reserves, accordingly

## Breakdown of Aozora's U.S. office loan portfolio by region (as of December 31, 2023)

	Non-performing loans			
	Number of transactions	Total outstandings (\$m)	Average LTV *2	% of valuation decline
New York		82	155%	-51%
Washington, D.C.		38	172%	-56%
Chicago		171	211%	-63%
Los Angeles		127	176%	-59%
San Francisco		79	168%	-59%
Other		220	163%	-56%
<b>Total NPLs *1</b>	<b>21</b>	<b>719</b>	<b>177%</b>	<b>-58%</b>
<b>Total Normal Loans</b>	<b>26</b>	<b>1,174</b>	<b>76%</b>	<b>-12%</b>
<b>Total</b>	<b>47</b>	<b>1,893</b>		

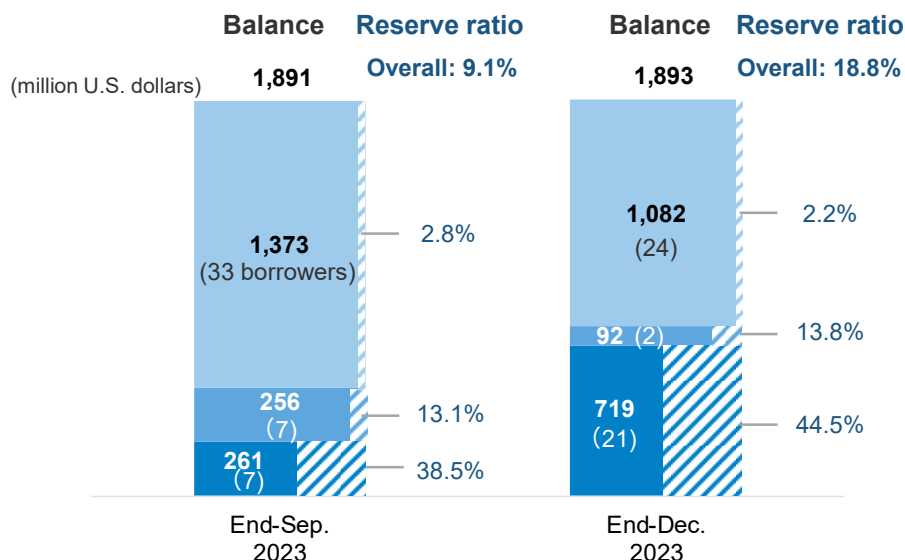
\*1 Including NPLs in the following seven cities/county: Atlanta, Arlington, Austin, Philadelphia, Orange County, Minneapolis and Seattle

\*2 Taking into account the risk of price declines over the next two years for NPLs

# U.S. non-recourse office loans (2)

- U.S. office loan outstandings were US\$ 1,893 million, which accounted for 6.6% of total loans
  - As described on page 4, we classified 21 borrowers with a total exposure of US\$ 719 million as NPLs. The ratio of NPLs to total claims was 38% (13.8% as of September 30, 2023)
  - An additional reserve of 32.4 billion yen (220 million on a U.S. dollar-basis) against the U.S. non-recourse office loan portfolio were provided in 3Q. The loan loss reserve ratio increased to 18.8%, which we believe provides an adequate reserve level and significantly reduces the risk of future losses

## Aozora's U.S. office loan portfolio



■ LTV: over 100% (NPLs) \* ■ LTV: 90-100% ■ LTV: less than 90%

\* U.S. office loans with an LTV of over 100% are classified as NPLs in principle  
(million U.S. dollars)

	End-Sep. 2023			End-Dec. 2023		
	Balance	Reserves	Reserve ratio*	Balance	Reserves	Reserve ratio*
LTV: less than 90%	1,373	37	2.8%	1,082	23	2.2%
LTV: 90-100%	256	33	13.1%	92	12	13.8%
LTV: over 100% (NPLs)	261	100	38.5%	719	320	44.5%
<b>Total</b>	<b>1,891</b>	<b>172</b>	<b>9.1%</b>	<b>1,893</b>	<b>357</b>	<b>18.8%</b>

\* Total exposure basis

## Credit-related expenses

(billion yen)

	FY2023 Interim	FY2023 3Q	FY2023 4Q projection	FY2023 projection
The Bank total	-9.9	-32.9	-0.0	-43.0
US office loan-related	-12.4	-32.4	-	-45.0

## Office market conditions by region (property leasing and trading trends)

New York	Office supply and demand in Manhattan is expected to recover earlier compared to other cities. The polarization of credit quality is increasing within the region due to fight-to-quality trends
Washington, D.C.	Property trading is relatively active, although there are disparities in areas (central district vs. submarkets) and properties (Class A vs. other classes)
Chicago	A considerable amount of time is required to recover supply and demand balances in urban areas. The volume of property sales remains very low
Los Angeles	More time is required to balance office supply and demand in central areas. Demand is expected to emerge for suburban properties
San Francisco	More time is required to activate property trading due to long-term imbalances in office supply and demand. Purchase and sales are beginning to emerge for medium/small-sized properties



# Securities portfolio restructuring

- With respect to unrealized losses on the securities portfolio, consisting mainly of foreign bonds, primarily due to the rise in U.S. interest rates we have decided to accelerate the disposition of securities with the aim to secure added flexibility in portfolio management and improve profitability in the next fiscal year and beyond
- We sold foreign currency ETFs in 3Q and plan to sell a further portion of the remaining foreign currency ETFs and MBS in 4Q. As a result, a loss of 11.1 billion yen (including losses from sale of 9.3 billion yen) was recorded in 3Q. An additional loss of 29.8 billion yen (including losses from sale of 26.7 billion yen) is expected in 4Q resulting in an expected loss of 41.0 billion yen including negative carry in 2H
- Unrealized losses on securities improved from a net loss of 92.6 billion yen as of September 30, 2023 to a net loss of 81.5 billion yen as of December 31, 2023, and are further expected to improve to a net loss of 56.0 billion yen as of March 31, 2024, which will be a significant step towards the restructuring of the securities portfolio
- Unrealized losses after the above disposition will mainly be from higher credit securities (U.S. and European government bonds, U.S. MBS and U.S. investment grade bonds ETFs, with minimum redemption risk
- Bond durations as of December 31, 2023 were 5 years for U.S. government bonds and 6 years for MBS

## Breakdown of loss-cuts in securities

ALM/securities *1		Balance *2, 3			Unrealized *4 gains/losses	Losses from sale/redemption	Unrealized *4 gains/losses	Losses from sale/redemption	Unrealized*4 gains/losses
		End-Sep. 2023	End-Dec. 2023	End-Mar. 2024 projection	End-Sep. 2023	FY2023 3Q	End-Dec. 2023	FY2023 4Q projection	End-Mar. 2024 projection
JGBs, municipal bonds	(billion yen)	37.8	36.9	36.9	(billion yen) -2.5	-	-2.9	-	-2.9
U.S. government bonds	US\$ million	1,550	1,550	1,550	(billion yen) -14.4	-	-15.7	-	-15.7
European government bonds	EUR million	405	405	405	(billion yen) -9.9	-	-10.1	-	-10.1
MBS	US\$ million	1,286	1,264	858	(billion yen) -42.9	-	-40.2	-15.4	-24.8
ETFs	US\$ million	1,101	851	465	(billion yen) -32.1	-9.3	-24.1	-10.2	-13.9
REITs	(billion yen)	8.7	4.3	4.3	(billion yen) -0.8	-	-0.5	-	-0.5
Investment trusts	(billion yen)	42.8	35.8	11.1	(billion yen) -3.2	-	-1.8	-1.1	-0.7
<b>Total</b>									
Overall securities	(billion yen)	1,395.2	1,375.9	1,164.1	(billion yen) -92.6	-9.3	-81.5	-26.7	-56.0

\*1 Management accounting basis

\*2 Balances are stated on an original currency basis in principle. REITs and investment trusts denominated in foreign currencies are stated on a yen basis.

\*3 Bonds are stated on face value. Other securities are stated on book value

\*4 Including hedging instruments

\*5 Based on an assumption that the financial environment and the Bank's portfolio will remain unchanged

Estimate for unrealized gains/losses\*4 as of March 31, 2025: approx. -49 billion yen\*5

# Business strategy for FY2024

## Earnings, Capital and Dividends

- Our customer-related businesses focusing on Aozora's Strategic Investments Business have been experiencing steady growth. We anticipate achieving net revenue of approx. 85.0 billion yen and profit attributable to owners of parent of approx. 17.0 billion yen for FY2024, driven by the overall growth of our business groups through the expansion of profitable businesses, the steady progress of GMO Aozora Net Bank (GANB) towards profitability, and signs of a positive outcome resulting from the structural reform in our retail business
- With regard to the consolidated capital adequacy ratio which is expected to temporarily decline as of the end of March 2024, we plan to exceed 9% in terms of the domestic standard and 7% in terms of CET1 as of March 31, 2025 by taking measures including the accumulation of capital through improvement in business performance in the next fiscal year
- We aim to increase the FY2024 full-year dividend from the revised FY2023 dividend forecast of 76 yen per share
- FY2024 earnings forecast will be provided as part of the announcement of FY2023 full-year earnings results scheduled for May 2024

### Net revenue, profit attributable to owners of parent and capital adequacy ratio

(billion yen)	FY2021 Full year	FY2022 Full year	FY2023 Full year forecast	FY2024 Full year plan
Net revenue	103.0	59.5	51.0	Approx. 85
Customer-related business	68.9	69.3	81.2	Approx. 85
incl. GANB	2.3	3.2	5.6	Approx. 8
Retail business	8.0	2.8	2.8	Approx. 4
Financial market-related business	25.9	-12.6	-33.0	Approx. -5
Profit attributable to owners of parent	35.0	8.7	-28.0	Approx. 17
	End-Mar. 2022	End-Mar. 2023	End-Mar. 2024 estimate	End-Mar. 2025 plan
Capital adequacy ratio	10.37%	9.43%	Approx. 8.8%	9% or higher
CET1 ratio (approximation)	9.3%	7.4%	Approx. 6.6%	7% or higher

## Customer-related business mainly driven by Aozora's Strategic Investments Business

The Bank strives to achieve steady growth in its customer-related business focusing on Aozora's Strategic Investments Business, which aims to serve customers in their three phases of "Fostering," "Change" and "Recovery," under the Mid-term Plan "Aozora 2025"

### Growth areas and business opportunities for FY2024

#### Fostering

#### Start-ups support (venture debt, GMO Aozora Net Bank)

- Enhance Aozora's start-ups support ecosystem framework across the Group with the aim to provide: (1) funding support through venture debt; (2) business support, including start-ups' creating open innovation with our corporate customers; and (3) human resources support
- Provide support for start-ups, including account openings by small businesses and start-ups, through GMO Aozora Net Bank

#### Change

#### Buyout business, environmental business, etc.

- Seize business opportunities, including buyout finance and business succession M&A, by capitalizing on the active M&A market
- Promote environmental finance and corporate finance that are instrumental in resolving customers' and society's challenges
- Support customers in enhancing their corporate value through the following three forms of investments: equity investments with a primary focus on engagement, structured equity investments and strategic investments

#### Recovery

#### Business recovery support

- Actively respond to business recovery finance needs that are growing on the back of the end of the government's COVID-19 related support as well as the expected normalization of the Bank of Japan's monetary policy, together with Aozora Loan Services as a leading company in the servicing industry