

Message from the President



Enabling Everyone in Our Communities to Lead More Fulfilling Lives

2020 in Review

The year 2020 is certain to go down in history as a time during which the world encountered and confronted threats posed by the COVID-19 pandemic. With economic activity having consequently stagnated worldwide, Japan's GDP dropped by 4.8% relative to the previous year, culminating in the nation's first negative growth since 2009, 11 years ago.

Likewise, the atmosphere in Kyoto also changed dramatically. The situation has dealt a significant blow to many businesses, particularly those in the tourism sector as they encounter a situation where tourist spots have lost their vibrancy amid evaporating Japanese and overseas tourism demand.

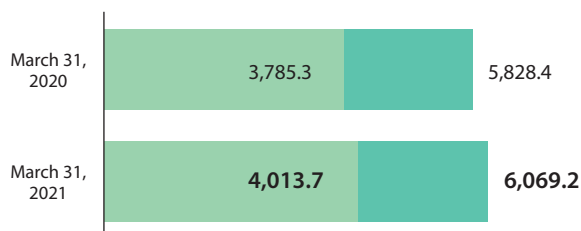
In the midst of a scenario where businesses continue to face inexplicable hardship, we are passionately rallying the entire Bank of Kyoto Group in helping prompt recovery of the local economy as quickly as possible premised on our strong belief that our role and mission as a regional financial institution calls for us to remain close to our customers and facilitate their business through our financial services.

Regional Financial Institutions Encountering Mounting Expectations

As business prospects of Japanese companies deteriorated overnight amid the rapid proliferation of the COVID-19 pandemic, such enterprises placed high hopes on the financial intermediary services of banks given their role in arranging prompt and flexible financing and providing a diverse range of business support. In 2020, the total outstanding balance of loans among banks across Japan increased by a substantial 5.3% over that of the previous year (in comparison with a year-on-year increase of 1.8% in 2019), thereby suggesting that the nation's banks were instrumental in propping up corporate financing. Likewise, the Bank of Kyoto has been supplying business financing to a wide range of enterprises, irrespective of their size or industry, which culminated in a balance of outstanding loans amounting to ¥6,069.2 billion as of March 31, 2021, thereby surpassing ¥6 trillion for the first time ever with our average loan balance for fiscal 2020 having increased by 8.9%

Loans (¥ billion)

Loans for SMEs



relative to the previous fiscal year (in comparison with a year-on-year increase of 3.6% in fiscal 2019).

The Bank formed its COVID-19 Pandemic Support Team laterally throughout the headquarters in June 2020, and has since been offering solutions to support clients who operate businesses. The team has consequently provided such support in more than 3,000 different cases as of March 31, 2021. We have accordingly been endeavoring to support the core businesses of our customers and provide them with solutions enlisting our increasingly robust consulting strengths, which has involved identifying a range of challenges in areas that include those pertaining to sales and customer outreach as well as concerns regarding business succession, new business development, administrative improvement and enhancement, and human resources.

In recent years, we have become capable of playing an active role in an increasingly extensive range of different fields amid deregulation with respect to the Bank of Kyoto Group's scope of business and investment. This is seemingly a sign of there being high expectations for regional financial institutions, and we accordingly hope to persist with efforts to actively expand our business domain going forward to also encompass the field of non-financial services.

Our efforts in this regard have involved establishing the Bank of Kyoto Next Fund business succession fund in March 2021. We have been addressing customer needs through our business succession support services thus far and have accordingly established this fund jointly with Bank of Kyoto Group company Kyogin Lease & Capital as the needs have been escalating largely due to COVID-19 and also because of a situation where companies are encountering an increasingly severe shortage of successors as the nation's population gets older. Going forward, we have opted to engage in ongoing investment targeting total investment of ¥10.0 billion over a 10-year period. In addition to facilitating seamless business succession, we will also strive to help companies increase their enterprise value by providing them with post-investment managerial support, while also drawing on offerings such as our professional recruitment services already underway.

Going forward, we aim to achieve growth serving as a comprehensive financial solutions provider by engaging in an expanding realm of business domains with such efforts underpinned by our analysis, particularly in terms of profitability encompassing effects of such solutions on regional economies in alignment with local circumstances and synergies with existing business operations.

Practices Aligned with Our Management Principle of "Serving the Prosperity of the Community"

Since its founding, the Bank has consistently endeavored to fulfill its role as a regional financial institution underpinned by its management principle of "Serving the Prosperity of the Community." That mindset permeates our entire workforce. For instance, on a daily basis our employees reflect on the Bank of Kyoto's ideals and meaning of existence serving as a regional financial institution, and furthermore exchange opinions from their respective points of view. One example of this is that our process of screening corporate loans involves having those in charge question one another in seeking to determine how best to make judgement calls as a locally based financial institution. We nurture a corporate culture whereby our employees naturally engage in practices espoused by our management principles in a manner that involves repeatedly performing such interactions throughout the organization, which seemingly reflects the notion that we tend to hire employees who as students originally aspired to serve their communities.

The first thing we did at the stage of drawing up our medium-term management plan initiated in fiscal 2020 was to gather feedback from all of our employees upon adopting a process whereby we sought to review their ideals with respect to how they envision the Bank. In so doing, we found that our employees express themselves in different ways as individuals, yet we reaffirmed the idea that they all share deep-seated desires to work "together with the community," and that they all in their own way embrace our management principle of "Serving the Prosperity of the Community," and that they furthermore put such ideals into practice in the course of performing work on a day-to-day basis. We intend to firmly tap into such desires of our employees, which will serve as a driving force in enabling the Bank to achieve further growth.

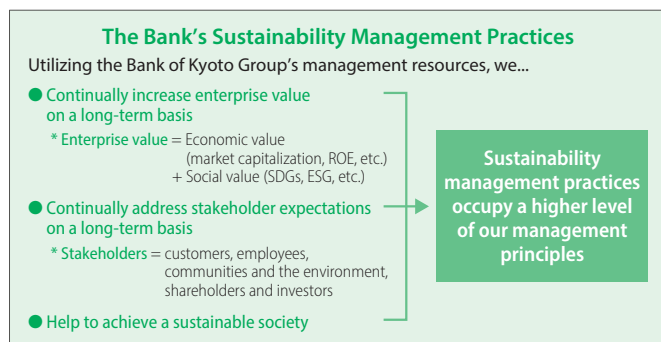
Promoting Sustainability Management

Having positioned sustainability management such that “sustainability management practices occupy a higher level of our management principles,” the Bank will seek solutions to both social challenges locally and environmental issues by engaging in specific initiatives geared to helping to achieve the Sustainable Development Goals (SDGs). The Bank has accordingly decided to set the aim of promoting sustainability management as a management objective amid a scenario of accelerating momentum toward making the notion of a sustainable society a reality, as embodied by the government’s goal of achieving carbon neutrality by 2050 (effectively zero greenhouse gas emissions). Whereas the Bank has been engaging in efforts of its own aligned with concepts underlying the SDGs given that it already embraces such ideals, it is now committed to forging ahead with management practices that are more in tune with society while enhancing its perspectives by conforming to international targets.

More specifically, we established the Sustainability Management Promotion Committee in January 2021 and have drawn up and released our Policy on Loans and Investments for Achieving a Sustainable Society. Our sustainability management practices will involve consistently maintaining inseparable ties between economic value and social value, while continuously working to increase enterprise value over the long term by striving to achieve improvement on both fronts. The committee will strive to ensure that the Bank addresses various sustainability-related issues encompassing the SDGs and environmental, social and governance (ESG) criteria through its core business operations. To such ends, the committee will seek to achieve more extensive understanding of social challenges, environmental issues and shareholder expectations, and will ensure that the Bank takes concrete action on an organization-wide basis.

Meanwhile, we have positioned the policy on loans and investments to serve as the Bank’s guiding principles for arranging loans and investments that adhere to sustainability management practices. We accordingly aim to create a positive future for our communities together with our customers backed by our management principles, which involves adhering to a basic approach that entails helping to bring about a sustainable society through the dual aims of “creating and increasing positive outcomes” while “reducing and avoiding negative outcomes” in a manner that involves addressing various economic, environmental and social challenges from the standpoint of a regional financial institution. We explicitly outline three initiatives for actively arranging loans and investments that result in “creating and increasing positive outcomes.” The first such initiative calls for “establishing local companies, generating innovation, and furnishing support for achieving growth.” In that regard, the Bank traditionally maintains a track record of facilitating venture businesses. Throughout the ages, innovation has always culminated in greater enterprise value for companies by increasing productivity and stimulating growth, while at the same time causing ripple effects beneficial to other companies, thereby giving rise to virtuous cycles of economic activity. Given that Japan has been subject to a low rate of potential growth due to its aging population, we hope to facilitate economic growth by prompting innovation among local companies.

The Bank has accordingly upgraded its operations by implementing funding schemes and other such initiatives in a manner that is in step with the times. As a result, since the year 2000 alone we have managed to invest a total of ¥5.6 billion in approximately 400 companies, about 30 of which have already gone public. Going forward, we intend to invest a further ¥5.0 billion over a period of about one decade.



Securities Held for Strategic Equity

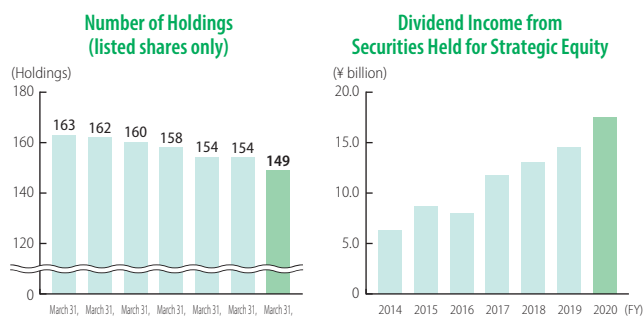
In recent years, we have been receiving an increasing number of inquiries particularly from investors regarding the Bank’s holdings of securities held for strategic equity. This warrants an explanation of the current situation, which is one whereby the Bank verifies the need for holding such equities based on factors that include the benefits and capital costs associated with ownership on a yearly basis, and confirms the economic rationale of such ownership. Consequently, the Bank has been gradually reducing its number of strategic equity holdings to the point where its portfolio at the end of the most recent fiscal year on March 31, 2021 contained 149 holdings, which is a decrease of 5 holdings compared to the previous fiscal year. Next, dividend income, which exemplifies benefits the Bank derives from its securities held for strategic equity, has been gradually increasing and reached a level exceeding ¥15.0 billion in fiscal 2020, thereby indicating that it significantly contributes to the Bank’s profits.

Among such holdings are shares from many listed companies located locally in Kyoto, which will be touched on shortly (pages 6 to 7), and companies that we have held since a time when the Bank acted to facilitate their growth. This involved offering financing as well as actively investing in such entities at a time when they were regarded as venture companies. Those former venture companies ended up achieving remarkable growth and went on to become world-renowned Kyoto companies. As such, the value of shares which the Bank held when the entities were venture companies has since increased dramatically, serving as a major source of the Bank’s profit and financial soundness.

Some investors have apparently described the Bank as an investment banking success story given this track record. However, we are a regional financial institution, not an investment bank. Whereas an investment bank would seek to maximize its own profits by selling holdings to reap the fruits of an investee’s growth, as a regional financial institution our first priority is that of considering how best to gain benefit from such results while maintaining holdings of Kyoto company shares when there is economic rationale for maintaining such holdings. We also prefer to ensure that the community, as well as the Bank, reaps such fruits of success in various ways. Premised on that desire, we seek to help bring about virtuous cycles in terms of sustainable growth of local companies and sustainable growth of local economies by actively investing in start-up support and business succession support.

On the other hand, we also deem it necessary to further reduce portfolio holdings by raising standards of economic rationale for maintaining holdings given significant changes in the business environment.

At any rate, the Bank’s securities held for strategic equity whose valuation gains exceed ¥1 trillion constitute important management resources for its operations. As such, management will accordingly strive to further seek the understanding among investors of the Bank, which focuses on enhancing engagement. At the same time, we will seek optimal solutions that are readily comprehensible across a wide range of stakeholders, which will also bring about an increase in the enterprise value of the Bank.



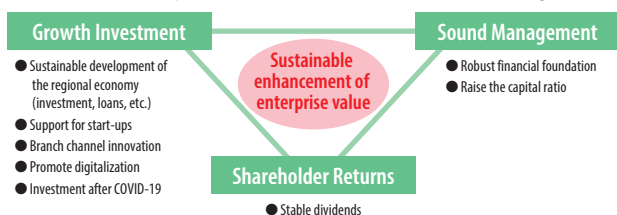
A Triple Balance: Growth Investments, Ensuring Sound Management, and Enhancing Shareholder Returns

In the management of a regional financial institution, we had long regarded the keys to continuously enhancing enterprise value to be deftly balancing growth investments, ensuring sound management, and enhancing shareholder returns.

In this environment, the current COVID-19 pandemic has brought home to me the relationship between the “role of a bank” during a sharp economic contraction and “ensuring soundness” in preparation. In cases where the economic environment for companies deteriorates suddenly, such as the recent COVID-19 shock, naturally it is the role of banks to support corporate liquidity until conditions recover. At the same time, banks bear the risk of a deterioration in their operating conditions due to future increases in the cost of credit. Nevertheless, I believe that regional financial institutions exist to support regional companies in withstanding adverse environments, regardless of future risks, in order to protect regional economies. However, to fulfill this role, banks themselves must have considerable strength. The Bank also recorded a significant increase in the cost of credit in its fiscal 2020 financial results compared to the level of an average year, but it was easily recovered by considering the robust financial foundation that the Bank has built up, and even if the economy were to take even longer than expected to recover, we would be able to continue supporting regional companies without any impact on our management framework. This past year has been a very real reminder that in order for banks to play their role during an economic recession, it is important that management strives to ensure sound management during ordinary times.

On the other hand, we have increased shareholder returns in line with our initial plan in order to meet the expectations of our shareholders. The Bank has long had a basic policy of returning a stable dividend, and from the fiscal year ended March 31, 2021 we have increased our guideline dividend payout ratio by 5 percentage points, from 25% to 30%.

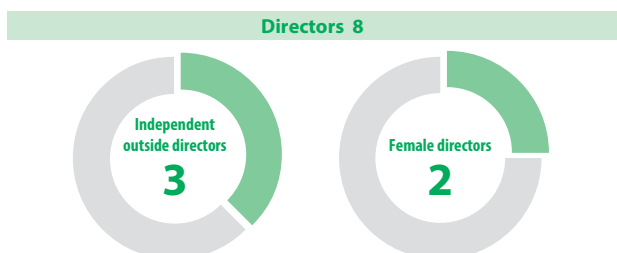
Turning to growth investments, we intend to focus on areas such as corporate financing and related investments, based on the realization that the sustainable development of the local economy will support the Bank’s growth. Of course, we will promote initiatives towards digitalization; and in line with our Policy on Loans and Investments for Achieving a Sustainable Society, we will also work proactively in support of start-ups, resolution of environmental issues including climate change risk reduction, and efforts to promote a focus on the SDGs and ESG in management.



Initiatives to Strengthen Governance

As part of establishing unwavering trust from all of its stakeholders, the Bank is working to strengthen corporate governance based on management transparency and soundness.

In order to streamline the Bank’s management structure, on June 29, 2021, we changed the composition of the directors, reducing the total number of directors to eight, including three outside directors. In addition, one of our outside directors has joined us after recently serving as a representative director for NTT DATA SYSTEM TECHNOLOGIES INC., bringing a wealth of experience as a corporate manager and wide-ranging, expert knowledge in the systems field to the Bank’s management.



Enabling Everyone in Our Communities to Lead More Fulfilling Lives

Recently, we have seen a growing movement towards promoting the SDGs and ESG, as well as thinking about the optimal benefit to the entire community in terms of three aspects: economy, environment, and society. The Japanese word for “economy” is said to derive from a classical Chinese phrase meaning “to fix the problems in society and relieve the hardship of people.” Economic growth and development are certainly important to the extent that they improve people’s lives, but economic growth itself is not the final goal by any means. For people to lead fulfilling lives, it is also important to have a natural environment in cities and regions, and a society that enables encounters and relationships between people. Rather than having an excessive bias towards the economy, it is necessary to think of the future of communities in terms of all three aspects. Many people have probably recognized that the COVID-19 pandemic has provided an admirable opportunity for many people to reaffirm that the environment and society contribute vitality and richness to their lives, helping them to notice the value of regions with abundant nature by moving out of the cities and to observe the value of face-to-face interaction by restricting contact between people.

Conversely, the services provided by the Bank can also be seen as an essential form of social capital for enabling everyone in communities to lead more fulfilling lives. Therefore, we place particular value on our branches, which provide a point of contact with our customers. The Bank is currently focusing on consulting services, such as corporate management, business succession, asset management, and inheritance measures. These services require an especially human touch to respond properly to customers’ issues, and I feel that our continued survival depends to a significant degree on our ability to provide them. Until now, we have served our customers as a wide-area regional bank by establishing branches closer to them and working to cultivate wider and deeper connections with them. We will utilize these branches to provide high-value-added services with a human touch that cannot be rivaled by other banks.

At the same time, the Bank is also working to provide more convenient and higher-quality services that are “digitally connected,” by connecting with all of our customers digitally. In the future, we believe that our real-world branches will receive fewer customer visits as customer contact points, but will actually play an even more important high-value-added role than before. On the other hand, we believe that digital transactions will not only increase in number as the services expand, but also that they will play a role in providing new services that leverage digital characteristics. The Bank has stated its aim is to achieve the best mix of face-to-face and digital services. We will build a business model that enables customers to choose between real (branch) service and digital service depending on which best meets their needs at the time. In doing so, we will work to enable customers to lead more fulfilling lives in terms of the financial aspect.

80th Founding Anniversary of the Bank

The Bank will mark its 80th founding anniversary in October 2021. Looking ahead to our 90th and 100th anniversaries and asking myself about the purpose for our existence as a corporation, it seems to me that everything really stems from our determination to work towards the realization of communities in which everyone can lead more fulfilling lives.

The Bank of Kyoto Group will continue its corporate activities aiming to achieve even greater growth, while taking a holistic perspective of optimizing the three aspects of economy, environment, and society, as we work together as one to enable everyone in our community to lead more fulfilling lives.

I would like to thank you for your continued support and kind consideration.

Nobuhiro Doi

Nobuhiro Doi
President
The Bank of Kyoto, Ltd.