Outside Director Roundtable Discussion

Taking on the Challenge of a New Stage Gunma Bank Evolves through Business Integration, Based on Its Purpose



Having completed the first year of the Mid-Term Business Plan "Growth with 'Purpose'," we asked Outside Directors how they evaluate the initiatives that the Gunma Bank has undertaken based on the Purpose and the effectiveness of its Board of Directors. In this roundtable discussion, we asked them to share their objective evaluation of these matters as well as their candid views on the challenges facing the Gunma Bank and the direction for sustainable corporate value enhancement, as the bank continues to evolve and take on the challenge of a new stage through the business integration with Daishi Hokuetsu Financial Group (hereinafter referred to as Daishi Hokuetsu FG).

Progress Evaluation of the Mid-Term Business Plan and Key Monitoring Points

——First, we would like to ask about the current situation. How would you evaluate the progress of the first year of the Mid-Term Business Plan "Growth with 'Purpose'"?

Mid-Term Business Plan is progressing steadily; it is important to measure achievement from the perspective of the Purpose rather than focusing solely on KPIs

Kondo The Mid-Term Business Plan is progressing steadily with tangible results. The achievements to date have been so remarkable that I even wonder whether such momentum can be sustained over the longer term. One of the Bank's strengths has been its consistent practice of pairing every reform initiative with complementary measures designed to address the challenges and unintended effects that may arise from the reform. For example, when reviewing its branch network, the Gunma Bank simultaneously rebuilt its "regional governance structure" to maintain responsiveness in the workplace. Likewise, when introducing profitability-focused "RORA management," the Bank established its "Purpose" in anticipation of the risk that excessive attention might be paid to numerical results alone. I believe, as a result, a "customer-oriented" decision-making mindset has become firmly embedded in every employee. Based on the Bank's track record of successfully balancing growth with solutions, I have strong confidence in the progress being made under the current Mid-Term Business Plan.

Kanai As Mr. Kondo noted, the Bank has performed steadily in terms of financial results. In addition to drastically transforming its earnings structure, the transition to "higher interest rates" has provided a tailwind, contributing significantly to profit growth. However, one thing I notice when asked to evaluate the progress of the Mid-Term Business Plan is that attention often tends to focus on profit metrics.

What we must not lose sight of is that the current Mid-Term Business Plan is founded on the "Purpose." I like the Gunma Bank Group's Purpose, "By connecting the strands of resources, people, and generations, we weave better futures for our communities," because I believe it embodies the very reason for the Gunma Bank's existence. To measure progress toward realizing the Purpose, the Bank has established sustainability indicators and "KPIs for Tsunagu." When viewed from the perspective of how far we have progressed toward realizing the Purpose, I believe we are still only halfway there.

As the business environment improved, a number of the targets set out in the Mid-Term Business Plan, including the profit targets, now appear likely to be achieved ahead of schedule. I will closely monitor not only financial targets but also indicators related to the Purpose and contributions to the local community, without losing sight of what was originally intended when the Mid-Term Business Plan was formulated.

Osugi Mr. Kanai commented that he likes the Gunma Bank Group's Purpose, but I would say that I "love" it. I expect the Purpose to serve as the guiding principle and spiritual backbone that will support the Bank's direction in the years to come. At the same time, I believe an upcoming major challenge will be how effectively we can ensure the Purpose permeates the organization and reaches every single employee.

Based on the Purpose, the Mid-Term Business Plan sets "Creating a virtuous cycle of social and economic values" as one of its basic policies. The underlying idea is that the Gunma Bank grows for the benefit of local communities, and that growth, in turn, contributes to the development of local communities. There may, of course, be situations in which the interests of the community (social value) and the Bank's interests (economic value) come into conflict. In such circumstances, however, prioritizing the pursuit of social value will ultimately lead to the expansion of the Bank's economic value over the medium to long term. I believe that our ability to maintain this conviction without wavering stems from having a firm guiding principle, the Purpose.

We must be highly sensitive to risks and adaptable to a changing environment especially when things are going well

Nishikawa Progress toward the numerical targets under the Mid-Term Business Plan is certainly on track. That said, from a different perspective, I believe there is still room for improvement in terms of whether the Bank is acting with sufficient speed and forward-looking perspective. Competition for deposits has intensified significantly against the backdrop of rising interest rates. The Bank needs to respond to these changes in a more timely and effective manner.

Particularly among younger generations, there is a growing tendency for customers to make full use of the Internet and choose financial institutions that offer more favorable terms. As the barriers to transferring funds have become significantly lower, it is important for the Bank to remain constantly attuned to customer behavior and to proactively consider and implement measures ahead of those changes as much as possible.

It is essential precisely when things are going well to remain highly sensitive to risks and respond swiftly to changes in the business environment. I would like to see the Bank broaden its perspective beyond its peers, looking not only across other industries and regions but also overseas, and approach challenges with a broader perspective and a higher vantage point. I believe that social value and economic value should ultimately be aligned. If we look toward the future of local communities and thoroughly consider "what the Bank can achieve for the community and how it can generate earnings," that process should make social value and economic value fully compatible.

Expectations for the Business Integration with Daishi Hokuetsu FG and Key Areas of Focus Going Forward

——The Bank reached a definitive agreement for business integration with Daishi Hokuetsu FG, and further details, including the integration structure, have now been disclosed. Please share your expectations for the integration and the key areas to which you will be paying particular attention.

Review management from the perspective of the original objectives of the business integration

Kanai One of the defining features of this business integration is that it is not a rescue-driven integration. Rather, it brings together two leading regional banks that are both operating successfully with solid business performance. This is a significant strength of the integration. At the same time, however, I cannot deny that the very fact that both companies are performing well creates the risk that the underlying realities may become less visible.

The most important aspect of the integration is the establishment of a holding company with a workforce of approximately 100 employees and the enhancement of its functions to enable effective top-down management. However, there is a risk that even if the organization slightly deviates from the management model originally envisioned, such deviations may be overlooked as "not a problem" when the

Group's overall earnings continue to grow. That is precisely why I believe it is important, even after the integration, to rigorously monitor progress against the original objectives while continually returning to the original intent of the integration and reminding ourselves of "what we set out to achieve in the first place."

Embrace Each Other's strengths to maximize top-line synergies

Osugi That is an important point. The objective of this business integration is to maximize top-line synergies.

The Bank excels in capital efficiency, while Daishi Hokuetsu FG has strengths in non-interest businesses. Both companies must leverage "the best of each other's strengths" to generate synergies and drive top-line growth. Achieving this will require an eager willingness on the part of both companies to learn from and actively absorb what the other does well. If the integration remains merely formal and the "Gunma Bank" and "Daishi Hokuetsu FG" continue to operate as separate entities, top-line synergies will never be realized. In my view, where management is truly tested will be how effectively it can manage the integration of the two companies.

Systematize management control practices

Nishikawa A strength in realizing the integration of the two companies lies in the Bank's management approach based on performance indicators such as ROE and RORA. The success of the business integration largely depends on how effectively these management practices can be embedded across the Group as a whole.

Management control is fundamentally about how to "systematize" superior know-how. For example, Daishi Hokuetsu FG is often regarded as having a particular strength in non-interest businesses. It is important to thoroughly analyze the sources of that strength, then "visualize" and "systematize" them.

Once such mechanisms are in place and the results become visible, it will create a tangible success story demonstrating that "the strengths of Daishi Hokuetsu FG has been successfully replicated within the Gunma Bank." This would give employees in the workplace a strong sense of confidence and accomplishment. I believe that through this process, it is important to create a virtuous cycle in which both companies enhance their earnings capabilities.

Osugi For such a framework to function effectively, it is important not only to have an eager willingness to learn from and adopt each other's strengths, but also to maintain a sense of "humility." Because this is a business integration between two successful institutions, there is always a risk that each side may become overly attached to its own ways of doing things. Approaching the integration with humility and a willingness to learn from one another will surely create a virtuous cycle.

Evaluation of the Effectiveness of Governance (the Board of Directors) and Challenges

——How would you evaluate the effectiveness of the governance? For example, what discussions took place within the Board of Directors regarding important matters such as the business integration?

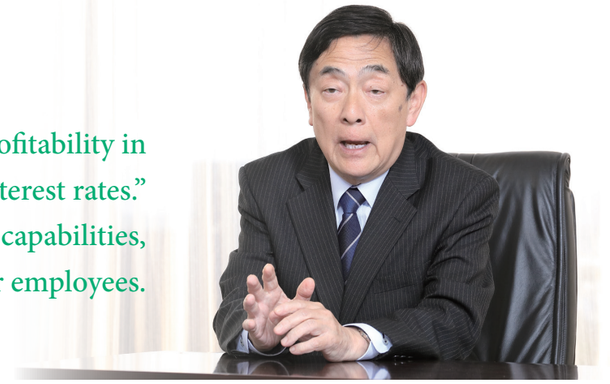
Diversity is ensured, and constructive tension with management is maintained

Kondo I assess the Bank's governance as highly effective. Mechanisms have been established to enhance effectiveness, and the PDCA cycle is being implemented in a disciplined manner. The effectiveness evaluation of the Board of Directors is also working well, and management provides appropriate feedback and follows up with concrete actions in response to views expressed by outside directors.

Another strength is the diversity of the outside directors. The four outside directors, each with a different professional background, contribute insightful discussions grounded in their respective experience and knowledge. I believe we have succeeded in maintaining an appropriate level of constructive tension with management.



We are still only halfway to realizing the Purpose.
Stay committed to the initial vision, rather than being satisfied with short-term profit.



Scale directly drives profitability in a "world with interest rates."
Strengthen pricing capabilities, especially among younger employees.

Governance means examining the logic behind management decision-making

Nishikawa With respect to the business integration, there were no significant differences of opinion within the Board of Directors. This was because the rationale for the integration, as well as the process leading up to the decision, was logical, persuasive and highly transparent.

Following the Bank's participation in the TSUBASA Alliance in 2020 and the formation of the Gunma and Daishi Hokuetsu Alliance in 2021, we held discussions regarding the future direction of the Bank's core banking system. Some expressed the view that "maintaining the Bank's proprietary system might be sufficient." However, I argued that "the direction should be examined from multiple perspectives, taking into account the various possibilities that could arise in the future."

Governance means examining whether management decisions are made through a sound and logical decision-making process. With respect to this business integration, I was able to sufficiently verify that process, and as a result, I had no particular objections to the decision.

Ensure that means do not become ends in themselves

Kanai As I commented in this roundtable discussion last year, many executives aspire to expand their organizations. In the course of our recent discussion, a vision of "becoming a company with a market capitalization of 1 trillion yen" was also presented. Pursuing a 1 trillion-yen market capitalization carries significant meaning in terms of enhancing presence in the capital markets, including among overseas investors. However, it would be counterproductive if that target were to become an end in itself. As an outside director, I intend to continue raising this question at Board of Directors meetings, reminding ourselves of the original purpose of the integration: "to expand our scale in order to make an even greater contribution to the local community."

Holding small meetings led by outside directors

Osugi In January, the Bank held its first small meeting led by outside directors, attended by Mr. Kondo and Ms. Nishikawa. The participating analysts responded very positively, particularly to the candid and insightful explanations the outside directors provided as experts in manufacturing and systems, which extended well beyond the scope of banking. In fact, participants commented that "it was extremely valuable to see that the outside directors were able to express their views to management openly and without hesitation (demonstrating that governance functions effectively)." Initiatives that place outside directors in direct dialogue with analysts in this manner reflect management's confidence in the Bank's governance and serve, at the same time, as compelling evidence that it is functioning as intended.

Challenges Facing Gunma Bank and Direction Ahead

——What would you identify as the challenges facing the Gunma Bank? Please share your views on the Gunma Bank's future direction and the role it should play going forward.

Pursuing scale and expanding data reach are keys to survival

Osugi A common challenge facing financial institutions, not only regional banks but also megabanks, is the decline in pricing capabilities.

In banking, "price" refers to interest rates, in other words, the pricing of financial products and services, and is one of the most important factors determining profitability. However, since the collapse of the bubble economy, Japan has experienced more than three decades of effectively zero inflation, resulting in a prolonged "zero-interest-rate world." As a consequence, I am concerned that the industry as a whole may have experienced a weakening of its ability to strategically set interest rates.

The Bank's upcoming challenge is how to secure appropriate levels of profitability in a "world with interest rates." In such an environment, scale is directly linked to earnings. From this perspective, the business integration with Daishi Hokuetsu FG represents a highly rational



Think how to effectively integrate
digital transformation and AI into operations.
Build genuine capabilities for
a sustainable regional future.

management decision. However, many of the Bank's younger employees have limited experience in negotiating increases in interest rates. Enhancing their pricing capabilities will therefore be critical, and if the Bank succeeds in strengthening these capabilities, it will be well positioned to gain a competitive advantage with regard to profitability.

Nishikawa The mission of regional banks, needless to say, is to revitalize local economies and contribute to their sustainable development.

I place strong emphasis on the use of systems in management, and from that perspective, I believe a challenge is how effectively the Bank can incorporate digital transformation and AI into its operations in order to support the sustainability of local communities. For example, the Bank promotes support for SMEs and digital transformation initiatives in Gunma Prefecture. However, it is now an era in which anyone can use AI to easily create websites and other basic digital tools. Against this backdrop, the challenge is how to promote meaningful digital transformation in the region. Rather than offering only superficial support, the Bank must build "genuine capabilities."

With AI, the volume and quality of training data are directly linked to the accuracy of outputs. The business integration with Daishi Hokuetsu FG will provide us with data from Niigata Prefecture. As a new financial group rooted in the regional economies of Gunma and Niigata, rather than urban centers, bringing together data from both regions will enable us to think thoroughly, based on data, "what kind of management approach is best suited to local communities." This will allow for more regionally grounded analysis that is not biased toward urban areas, thereby enabling the formulation of more effective and practical measures. I hope that, with this forward-looking perspective, the Gunma Bank will evolve into a "bank that can design regionally rooted management based on data."

Demonstrating awareness and acting as a leader among local financial institutions

Kondo I believe it is important for the Bank, as a regional bank, to carefully consider the "role to play in the local community" and translate that understanding into action. For example, from the perspective of AI, as Ms. Nishikawa mentioned earlier, I would like the Bank's employees to develop a deep understanding of AI technologies and applications so that they can provide practical advice enabling SME customers to improve productivity through the effective use of AI. In addition, a strong sense of responsibility as a leader among regional financial institutions is essential. We can enhance the overall productivity of businesses within Gunma Prefecture by bringing together small-scale businesses that may find it difficult to continue operating independently, and by creating a function similar to a "regional management office." I also expect the Bank to exercise leadership by working closely with shinkin banks and credit unions.

Long-term succession planning and talent development beyond reliance on top leadership

Kanai The key to the Bank's future growth and contribution to the local community lies in "people," and how it advances succession planning and human capital development is critically important. At present, the Gunma Bank is steadily progressing under the strong leadership of the President, and confidence in the current management structure remains unwavering. At the same time, looking ahead to the eventual leadership transition, the stronger the leadership of the current top management is, the more carefully we need to consider how to pass the baton to the next generation. While leveraging the strengths of top leadership, I believe a key theme going forward will be how to further draw out the capabilities of the middle-management layer that will lead the next era.

Osugi In this regard, the four of us share a common view that it is important to continuously monitor whether there is an open organizational culture and whether communication within the organization is being conducted smoothly.

Kanai The importance of succession planning and human capital development has also been actively discussed at the Nomination Advisory Committee, and we have received explanations from the President regarding the development of future management talent. Whether the potential candidates will grow into true leaders is a topic of strong interest both inside and outside the Bank, and I intend to continue closely monitoring the progress.

The Role That Outside Directors Should Fulfill to Further Enhance Corporate Value

——Lastly, please share your views on the role that outside directors should fulfill to further enhance corporate value.

Contribute to enhancing corporate value of Gunma Bank through creative discussions with an external perspective

Kanai I feel that the environment for us as outside directors to express our views and raise issues is very well established. Within that framework, I intend to act as an "outsider" with an external perspective, and at times to deliberately throw small "stones" into the organization, carefully monitoring how the organization absorbs or reacts to them.

Osugi The roles of outside directors are "supervision" and "advice." However, I believe that the more essential function that only outside directors can truly fulfill is "supervision." In most cases, inside directors are placed in an executive hierarchy relative to top management, and for that reason it is in practice not easy for inside directors to appropriately exercise a "supervisory" function over top management. "Supervision," in essence, means pointing out, without hesitation and without being constrained by authority or hierarchy, that "something is wrong." I intend to remain firmly committed to this principle and continue to express my views clearly whenever necessary.

Meanwhile, in normal times, we will work in close alignment and cooperation with management, sharing the same objective of "effectively enhancing the Bank's corporate value." In this context, what is particularly important is the Chairperson's leadership as exercised by the President, who serves as Chairperson of the Board of Directors. We, as outside directors, will respond to that leadership and are committed to providing constructive insights that contribute to the enhancement of corporate value.

Nishikawa I consider the Board of Directors to be a forum for "creative discussion," where we work together to make the Gunma Bank a better institution. In that setting, I would like to leverage my skills and strengths while also bringing in a range of perspectives, including global viewpoints and insights from other industries, what Mr. Kanai earlier referred to as "stones," without hesitation. At times, this may involve pointing out uncomfortable truths. However, based on a relationship of trust with management, I would like to continue engaging in constructive discussions aimed at further improving the Bank.

——We would like to ask Mr. Kondo, who is stepping down, to share a message of support for the future of the Gunma Bank.

Turn the business integration into an engine for regional revitalization

Kondo Even after stepping down from my position, I will continue to strongly support the Bank. Over the past decade, the Bank has achieved reforms at a pace that has clearly outperformed other regional banks. Building on this foundation, the integration with Daishi Hokuetsu FG marks the beginning of a new phase of challenges in regional revitalization that goes beyond the traditional regional banking model.

I sincerely hope that the new financial group, following the integration, will play an even greater role than before and serve as a new engine driving the regional economy forward.

Mutual respect is essential in business integration.
Develop a strong sense of responsibility
as a regional leader and take on
a new phase of regional revitalization.

