

■Date November 30th Monday 16:30-18:00

■Topic What does ROE stand for?! –What the data users expect of the accounting standard / disclosure rules when they calculate the indicator?–

1. The background of the topic “ROE”

Agenda Consultation discussion, Net income and Equity

/ IASB Board member, Mr. Ochi (Document 1)

2. Why do investors look ROE?

2.1 ROE on the Summary of Financial Results [Earning Digest to TSE], for News Media and for Equity analysts / Ms. Nakagawa (Document 2), Mr. Kubota (Document 3)

2.2 ROE for Fund managers / Mr. Kawakita (Document 4)

2.3 Proxy voting and ROE / Mr. Kimura (Document 5)

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3. Current situation and issues of ROE

3.1 ROE and Class shares / Mr. Yoshii (Document 7)

3.2 Current situation and issues of ROE Calculation / Mr. Nomura (Document 8),

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4. Improvement of accounting standards and disclosure for the appropriate usage of ROE

4.1 Company’s opinion for ROE Mr.Fukai (Document 10)

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Concerning of disclosure/Message for Agenda Consultation

■Documents

Agenda (included Document 1 – 11 )

Document 0 Agenda Consultation 2015 (English)

Document 2-1 Summary of Financial Results [Earning Digest to TSE] (Japanese)

Annual and 2<sup>nd</sup> quarter base on J-GAAP, USGAAP, and IFRS

Document 2-2 Summary of Financial Results [Earning Digest to TSE] (English)

Annual and 2<sup>nd</sup> quarter base on J-GAAP, USGAAP, and IFRS

Document 3-1 Sumitomo Riko ‘s Earning Digests which has changed from J-GAAP to IFRS

Document 4-1 Information of the investor who gave his comment for 2.2 of Today’s agenda. (Japanese)

Document 4-2 The same above (English)

Document 7-1 Sample : Mizuho FG Balance sheets from the securities report 2015 Mar. (both)

- Document 7-2 ROE difference between company announcement and Calculation from securities reports.
- Document 8-1 The amendment of the definition of Net Income (Japanese with English comment)
- Document 9-1 ROE distribution comparison of each combination of the numerators and denominators  
(Japanese with English comment)
- Document 11-1 Feedback sheet (Japanese)
- Document 12-1 Minutes of 5<sup>th</sup> workshop (Japanese)
- Document 12-2 Minutes of 5<sup>th</sup> workshop (English)

## ■Prelude · · · · Why we chose ROE for today's discussion

1. ROE is calculated by dividing the net profit by shareholders' equity. As both the numerator and denominator are topics of the agenda consultation, we would like to discuss on how ROE is being used and hope the discussion can be a good input for the agenda consultation. Regarding the calculation of ROE, we plan to discuss about whether non-controlling interests portion should be included in profit and what items else shall be included as equity.
2. On the other hand, we know that there are various ways to apply ROE to analysis. For example, some analysts use expected ROE while some use actual ROE and some will average the ROE over a few years before their analysis. Moreover, the case in Japan is an especially complicated one due to the submission timing difference of several reports (summary of financial results; Earning Digest to TSE and Audited financial statements; Securities Report to FSA) and the existence of several financial reporting standards. (In the past, there were also discussions on whether the non-consolidated financial statement or the consolidated financial statements shall be used for analysis)
3. These are not Japan-specific issues, in many other countries, companies are required by security regulators to disclose different reports at different times and report separate financial statements and consolidated financial statements in compliance with local GAAP and IFRS respectively. (Securities Exchange and data aggregator are collecting companies' earnings digests and providing data to the market). By understanding the problems existing in the current disclosure environment may also contribute to other projects including the disclosure initiative project and the digital reporting project.

## Document 1

### 1. The background of the topic "ROE"

Agenda Consultation discussion, Net income and Equity

IASB Board member, Mr. Ochi

Q1. Why Agenda consultation 2015 pickup "Net income" / "Equity" as the discussion topics? What are those issues?

A1. Regarding financial instruments which have characteristics of "equity" and influence the equity section of the balance sheet, IASB is aiming to have a "universal principle", under situations of expanding new types of financial instruments which are difficult to classify as either equity or debt. About the conceptual framework, since it was established in 1989, there are insufficient coverage. There are also parts which are unclear or does not catch up with the amendments / new standards. Now IASB is going to improve this framework. Next, Focusing on "Net income and OCI" being of particular interest. However, the consultation exposure draft avoided giving a clear definition of net income. It was expected to be discussed in the primary financial statements project.

Q2. What kind of discussions have already made?

A2. To put it simply, IASB recognized that the most important information for investors is "net income". Also, with regards to equity from the point of view of "what is equity", for example, we can say that equity is where one is not obliged to repay (claim) until a company is liquidated. The other concept is that the promise to pay with part of the company's resources (instead of the determined financial amount) could be considered a part of "equity".

Q3. How do you think those topics? What would you like to know from data users?

A3. I would like ask to the data users how you look at the contents of the equity.

In particular, we would like to ask whether the financial instruments needs adjustment or not when a company issues preferred stock or complex securities.

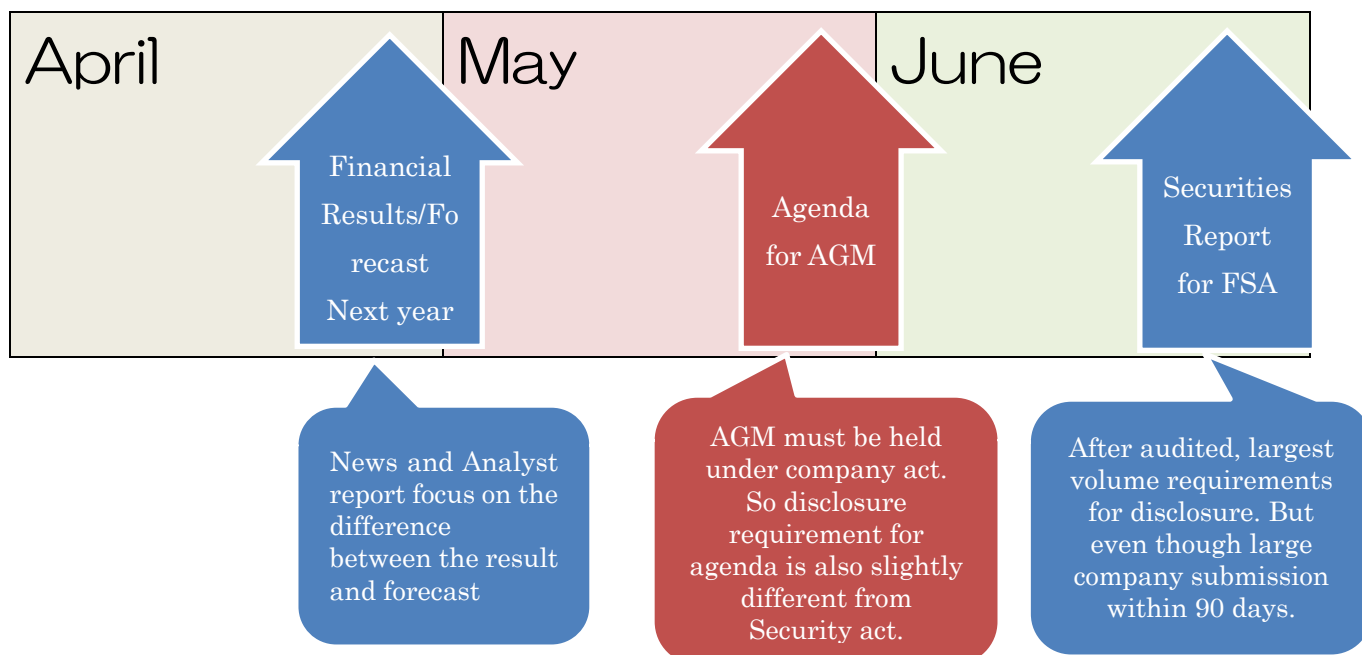
## Document 2

### 2. . Why do investors look ROE?

#### 2.1 ROE on the Summary of Financial Results [Earning Digest to TSE], for News Media

Jiji Press News Writer Ms.Nakagawa

Disclosure schedule (in case of March year-end companies)



- As News Media company, we are delivering the cause of moving stock prices
- We receive some amendment forecasts from company which will worse (better) result more than expected in March, April..
- Company makes announcement of the forecast of next year with its financial result. We broadcast how it change, also Q1~Q3 compares the forecast.
- We broadcast as news when 1) company makes change its forecast. 2) Company forecast becomes far from the consensus (forecast of analysts), 3) when the financial result becomes far different from forecast, The news will move the stock price.
- ROE disclosure on the financial result is only one time in the years. It is calculated by actual data. Company does not disclose forecast ROE. So news media make forecast ROE using forecast net income.. But news media can not obtain forecast equity. Some news media make original forecast “ROE”. (Not using company forecast net income)
- This table is the ROE ranking in the companies which have March year- end and belong to first section of Tokyo stock exchange. The company has high ROE seems to have poor equity, rather than high net income.

News of financial results at November 18<sup>th</sup>

ROE ranking (First section of Tokyo stock Exchange)

			*Net Income	ROE
1	66240	TABUCHI ELECTRIC Co., Ltd.	7,695	72.300
2	69110	New Japan Radio Co., Ltd.	4,580	58.800
3	46120	Nippon Paint Holdings Co., Ltd.	181,477	53.800
4	77090	Kubotek Corporation	535	53.600
5	15140	Sumiseki Holdings, Inc.	3,911	49.900
6	23710	Kakaku.com, Inc.	10,890	41.700
7	30920	Start today Co. Ltd.	8,999	40.400
8	58070	Totokumakisen Co., Ltd.	2,264	38.100
9	66200	Miyakoshi Holdings, Inc.	1,404	36.000
10	43440	Sourcenext Corp.	1,214	35.800

ROE Ranking (Ordinary over 500 billion)

			*Net Income	ROE
1	67230	Renesas Electronics Corporation	823	31.400
2	72700	Fuji Heavy Industries Ltd.	2,618	29.300
3	45680	Daiichi-Sankyo Company Ltd.	3,221	28.200
4	99840	Softbank Corp.	6,683	28.000
5	67240	Epson Corp.	1,125	26.300
6	95010	TEPCO	4,515	24.900
7	40420	Tosoh Corporation	622	24.500
8	18780	Daito Trust Construction Co., Ltd.	561	24.100
9	67700	Alps Electric Co., Ltd.	347	21.900
10	72610	Mazda Motor Corporation	1,588	20.800

ROE is calculated by TSE's definition / Net income is presented in million yen

\*Net Income= Profit attributable to owners of parent

SICCode	CompName			
6723	Renesas Electronics Corporation			
End date	Net income (million)	Owner's equity(million)	ROE	
2012/3/31	-62,600	217,958	-25	
2013/3/31	-167,581	66,744	-117.7	
2014/3/31	-5,291	214,601	-3.8	
2015/3/31	82,365	309,529	31.4	
<b>Average of 3 years</b>			<b>-30</b>	

## Document 3

### 2. . Why do investors look ROE?

#### 2.1 ROE on the Summary of Financial Results [Earning Digest to TSE], for Equity analysts

Rukuten Securities Inc. Mr.Kubota, CFA

Analysts pay attention to how the value of investment increases and therefore it is important to know the difference between forecast ROE and actual ROE, whether the actual ROE is an improvement or worsening result from the forecast ROE

ROE is decomposed as follow:

$$\text{ROE} = \text{Net Profit/Revenue} \times \text{Revenue /Total Assets} \times \text{Total Asset/Equity}$$

(Net Profit Ratio)                      (Return on Assets Ratio)                      (Financial Leverage)

In the 1980s, companies are keen on expanding businesses and are not interested in ROE. As expansion is the first priority of most companies, achieving high net profit ration and return on assets ratio are not business goals for many companies. Entering the 1990s, with decrease in the growth of the Japanese economy, companies start to focus more on net profit ratios and return on asset ratios. However, ROE is still not a common measurement at that time. On the other hand, companies were eager to constantly increase their equity ratio (to repay debts). It is difficult to judge that the repayment of debts is reducing investment value because at that time companies had too high financial leverage ratios.

However, even after 2000, when the financial conditions significantly improved, companies kept on to increase their equity ratios, shareholders began to disgruntled. Shareholders welcome restructuring of companies to improve the net profit ratios and return on assets ratio, but they are not happy with companies which buying back their own shares even if they already have a very high equity ratio. The purpose of share buybacks in the first half of 2000s was to absorb the elimination of cross-holding shares rather than to improve ROE.

From 2 years ago, companies started to set a business goal to improve ROE and they start to consider financial leverage as import as net profit ratio and return on asset ratio. Some companies started to perform share buyback to improve ROE.

The case of difficulty for comparison with previous years.

5191 Sumitomo Riko just adopt IFRS this year, its 1Q profit as IFRS became minus 0.4 billion from +1.5 billion plus last year. It included loss from subsidiary 2.3 billion last year came to “operating income” this year because of IFRS should include it. This year Sumitomo Riko plan to decrease this loss from subsidiary and recover profit. But I can not figure out this is actual base or not. IFRS do not allow to exclude extraordinary profit/loss for operating income, so that the up-down of the operating income must be fluctuated more. My analysis will suffer from it. Besides, It becomes more difficult to understand whether each quarter profit/ loss characteristic is temporarily or permanently at several years ago. Sector analyst can, but fund manager who is downloading data from information terminal, like me, can not have enough time.

IFRS does not allow company to amortize goodwill. And when company recognized the impairment, the data lose its continuity,, it also becomes barrier of my analysis.

I am aware that short-term borrowing and cash and equivalents are decreasing and asset also decreasing. If they are net, I have to be careful to see ROA.

➤ See Document 3-1 historical data of Sumitomo Riko.

## Document 4

### 2. . Why do investors look ROE?

#### 2.2 ROE for Fund managers

Mr.Kawakita former asset manager (Active fund)

As asset manager of active fund, I didn't ask company "improve ROE". I discussed their efficient financial structure and business strategy of improve profitability but did not require just improve ROE. If the companies which have low ROE and no chance of improvement, we don't need hold them.

I believe that ROE is the indicator for evaluate management performance, but not the indicator for investor when they make a decision to invest the company. Company uses it when they appeal their performance to investor, because management should evaluate how much profit they can earn (as R) against equity (E), but it is not reasonable for investor to decide investment using the indicator which doesn't include stock price (P). What we have to do is, checking ROE when company appeals high ROE. "Is there any unusual operation to make ROE higher?" Because, if company do something unusual operation for making ROE higher, it will not be sustainable. Investor should discuss sustainability of ROE, and we have to alert (show our worry) to company when they made unusual operation against equity only for high ROE.

In Japan, historically, Insurance companies or Pension fund association which doesn't have choice to sell, required improvement of ROE. (I think their requirement is reasonable, but active funds can take different way). At the same time, this is difficult to compare ROE in different countries' companies. It might be reasonable if we adjust inflation and accounting, but most of discussions are not adjust these. Some study shows that it is not big difference between Japanese companies' ROE and Western companies' after adjusted inflation.

Japan's equity market is a little different from Western countries' markets. Mean reversion of ROE is remarkable in Japan. Although we can see mean reversion of ROE also in Europe and the United States, Japan has a high volatility of profit. Therefore, asset managers of active fund in Japan make investments to capture mean reversion of ROE. In the results there is a remarkable tendency to invest low ROE companies than high ROE companies. (ROE has been stable negative factor in Japanese market).

**Former CIO(Chief investment officer) of the large asset management company Mr. Mizuno CFA**

**\* He is now choosing the DCF for long term investment**

The most important of calculation of ROE is Integrity of denominator and molecular.

When denominator takes Net asset attributable to non-controlling owners, molecular should be new net income.

But when denominator takes Shareholders' equity that is not included attributable to non-controlling owners, molecular should be old net income, "Profit attributable to owners of parent".

In case of NTT, subsidiary NTT docomo has large portion as attributable to non-controlling owners, it is good example to consider about this issue.

Please see Appendix 4-2 Interview to Mr.Mizuno



## Document 5

### 2. Why do investors look ROE?

#### 2.2 Proxy voting and ROE Mr. Kimura (Document 5)

Mr. Kimura, former Nomura Assets, former corporate governance director of Pension fund association

## ROE = Net Profit / Equity

### *What investors expect of Japanese companies*

#### Improvement of understanding of "shareholders (equity owners) value"

- improvement of understanding of owner's equity cost
- improvement of capital efficiency = increase of ROE, which results in investment return
- Equity owner's value(performance) linked remuneration
- Financing in consideration of equity owner's value (appropriate rules for MSCB, allocation of new shares to a third party)
- TOB policy in consideration of equity owner's value
- Protection for minority shareholders. (avoiding cross share holding etc)

▲ Pension Fund Association 2010

#### ■ The reason why Pension Fund Association use ROE

Since 1990s, especially between 2000 and 2002, Japanese stock market had remained at the low price level and Japanese pension funds suffered huge losses from investment which hit directly the pension assets. We shared the concerns that it would result in the collapse of the pension scheme. To avoid such consequence, we expect Japanese companies to challenge for improving

shareholders value.

As ROE is the return from the equity capital which shareholders invested, we believed that it must be closely related to the returns from the stock value increasing. Thus, we decided to adopt ROE criteria in the proxy voting, which was considered as the most appropriate benchmark index which indicates shareholders value. We believed that ROE is the proxy variable of equity owner's value.

#### **PFA Guidelines for Exercising Voting Rights (3) Appointment of directors**

**c. Oppose a proposal to reappoint a director when ROE has been less than 8% for the previous three consecutive years and there is no satisfactory explanation or action with respect to business plans and capital policies, including reasons and responses.**

The aim was that the companies should take into account the equity owners' value through considering ROE. We determined the "8%" target criteria for Japanese companies based on the factors which had lead by results of investor's consultation, and the studies such as the basic DDM model and refraction point in PBR. We recognised that it might be better to state "ROE exceeds the capital costs", as the ROE ratio varies according to the individual companies or sectors. However, to put a strong impact on ROE, we indicate a certain ratio such as 8%. When we published this voting guideline, we received much criticism from companies. Nevertheless, the companies who realised the importance of the dialogue with investors appreciated our approach. It follows that increasing number of companies have the ROE targets in their company strategies today.

# Document 6

## 2. Why do investors look ROE?

### 2.4 ROE for the JPX400 selection

Index Name	JPX-Nikkei Index 400 (JPX-Nikkei Index 400)
No. of Constituents	400 issues
Eligible Issues	TSE-listed issues (1st Section, 2nd Section, Mothers, JASDAQ)
Constituent Selection/Review Method	<p>[Selection Criteria]</p> <p>1. Screening</p> <p>a. Screening by Eligibility Criteria Issues are excluded from selection if they fall under any of the following criteria.</p> <ul style="list-style-type: none"> <li>- Listed for under 3 years (excluding technical listings)</li> <li>- Liabilities in excess of assets during any of the past 3 fiscal years</li> <li>- Operating deficit in all of the past 3 fiscal years</li> <li>- Overall deficit in all of the past 3 fiscal years</li> <li>- Designation as Security to be Delisted, etc.</li> </ul> <p>b. Screening by Market Liquidity Indicator The top 1000 issues will be selected from those eligible, excluding the above, in consideration of the following 2 items.</p> <ul style="list-style-type: none"> <li>- Trading value during the most recent 3 years</li> <li>- Market capitalization on the base date for selection</li> </ul> <p>2. Scoring based on Quantitative Indicators The 1,000 issues selected in (1) will be scored according to the ranking of the following 3 items. (1st: 1000 points – 1000th: 1 point). Then, overall score is determined by aggregating those ranking scores with the following weights. (There are handling rules for the overall scoring with negative ROE and operating profit.)</p> <ul style="list-style-type: none"> <li>- 3-year average ROE: 40%</li> <li>- 3-year cumulative operating profit: 40%</li> <li>- Market capitalization on the base date for selection: 20%</li> </ul> <p>3. Scoring based on Qualitative Factors Following the scoring in (2), issues will be further scored based on the following 3 items. This score is complementarily added to the quantitative scores explained above (2)*.</p> <ul style="list-style-type: none"> <li>- Appointment of Independent Outside Directors (at least 2)</li> <li>- Adoption or Scheduled Adoption of IFRS (pure IFRS)</li> <li>- Disclosure of English Earnings Information via TDnet (Company Announcements Distribution Service in English)</li> </ul> <p>* The score is determined so that at most around 10 constituents are different from those chosen with only quantitative score above (2).</p> <p><b>Determination of Constituents</b> Following scoring in (3), the 400 issues will be selected in descending order of high scores as constituents.</p> <p>[Buffer Rule] There is a preferential rule for previous year constituents. Constituents selected in the previous year will be selected as long as their scores are ranked within the top 440.</p> <p>[Constituent Review] A constituent review will be conducted on the last business day of August each year with the last business day of June as the base date. (The result of the constituent review will be announced on the 5th business day of August)</p>

Average ROE for 3 years = (Sum of Net income for 3 years) / (Sum of Owner's equity (Beginning and end year average) for 3 years) X 100

- In case of IFRS adoption companies, "Profit attributable to owners of parent" and "Total of equity (Equity attributable to owners of parent)" are used for ROE instead of "Net income" and "Shareholder's equity"

# Document7

## 3. Current situation and issues of ROE

### 3.1 ROE and Class shares

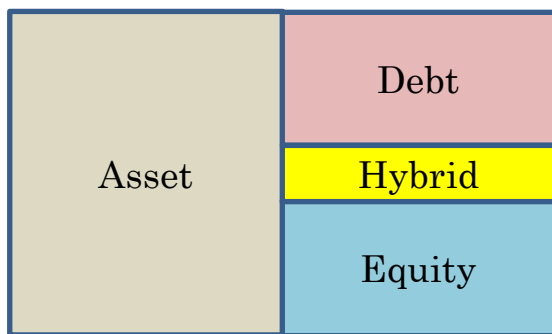
Daiwa Research Institute Mr.Yoshii

#### ▼Agenda Consultation 2015

#### Financial Instruments with Characteristics of Equity

A24 The classification of financial instruments as liabilities or equity in accordance with IAS 32 *Financial Instruments: Presentation* presents many challenges. The project is exploring whether the existing classification requirements in IAS 32 could be improved. In addition, the project is looking at what improvements could be made to the presentation and disclosure requirements for financial instruments with characteristics of equity. The timing of a Discussion Paper has yet to be determined.

There are financial instruments which belong to Equity / Debt in different cases, depend on accounting standards.



For example in case of Toyota AA class share  
IFRS categorized it in Debt  
US GAAP categorized it in Hybrid.  
J-GAAP categorized it in Equity  
Those classification affects on their indicators  
such as ROE.

#### Banks

➤ Disclosure regulation, form No.3 annual securities report  
...Regarding the net income to shareholders' equity ratio, there is no provisions for adjustment of preferred stock, etc.

➤ However, in the Banking Law Enforcement Regulations,

- The profit of the molecule must deduct the amount that is not attributable to common shareholders
- The denominator must deduct the outstanding preferred shares × issue price

◇ Mizuho FG

- Both denominator and molecule of ROE seems to exclude 11th 11 species preferred stock. (Same as EPS and BPS)
- ROE in the medium-term plan is not carried out the above adjustments

However, the denominator deducted net unrealized gains or loss on other securities.

◇ MUFG, SMFG doesn't have Preferred stock issued as Parent. (Holding company)

However, MUFG deducts the preferred shares outstanding at the beginning of the year. In addition, MUFG explained the definition of their own ROE,

$$\text{ROE} = (\text{Net income} - \text{Non-convertible preferred stock annual dividend}) /$$

(Total of Owner's equity - Number of Non-convertible preferred stock \* amount paid + The average value of the beginning and end of period, which is sum of foreign currency translation adjustment account)

...Net unrealized gains or loss on other securities, Deferred hedge gains and losses, and Adjusted cumulative for Retirement Benefits are not included.

- SMFG explains their own ROE used Shareholders' equity as denominator ( OCI is not included)

### Toyota Motor Co.

- ✧ AA class shares (the dividend preferred stock with voting rights. Stepwise priority dividend amount increasing. Cumulative and non-participatory), in the balance sheet of the US GAAP, it is recognized in the middle section of the capital and liabilities.
- ✧ Although it doesn't deduct preferred dividends from the net income as molecule, it should be deducted?

### Kyushu Electric Power Company, Inc.

- ✧ Dividend preferred stock (cumulative and non-participatory, no maturity, there is provision such as acquisition by cash)
  - No consideration on ROE in the securities report .
  - Taking consideration on EPS and BPS.

### Cyberdyne, Inc.

- ✧ They have Common stock and Class B shares.
- ✧ Class B shares is not a preferred stock, but it number of shares of each unit is one tenth. So it has 10 times voting rights of common stock.
- ✧ But it calculates EPS and BPS as same as common shares. ROE might be same.

### Sharp Corporation

- ✧ provides preferred shares to the bank by Debt Equity Swap.
- ✧ No consideration for ROE?

### Itoen

- ✧ Issued listed preferred stock, ROE does not include it

#### Comment from other Analyst

I'm calculating ROE by using PER and PBR that are adjusted the influence of class shares.

$$\begin{aligned} \text{ROE} &= \text{PBR ( Stock price / BPS )} \div \text{PER ( Stock Price / EPS )} \\ &= \text{EPS / BPS} \\ &= \text{Net income / Number of outstanding shares} \div \text{Net asset / Number of outstanding shares} \end{aligned}$$

EPS and BPS are required the adjustment the influence of class shares by accounting standard. In addition, I'm also calculating that assumes all shares convertible into common shares of convertible preferred stock

#### Comment from who can not attend today, Re-insurance company Ms.F CFA

There are a variety of assessment in the insurance company. For example, subordinated debt which is categorized as debt in JGAAP, but it is a part of capital in the classification of the solvency on the regulations. Thus, there are multiple different assessments for one item is in several different classifications in the company. Not only financial instruments, but also catastrophe reserve, price fluctuation reserve are debt in JGAAP, equity in IFRS. Moreover, they are capital in Japan's solvency.... On the other hand the equity of the insurance company becomes more important because they have to be enough amount against their taking risk.

Thus as a measure of internal managerial necessary, adjusted ROE is used. From the point of view above, I think that it might be difficult to assess the entire industries by one indicators defined by the accounting.

# Document 8

## 3. Current situation and issues of ROE

### 3.2 Current situation and issues of ROE Calculation

Nomura Securities Mr. Nomura

New “Net Income” doesn’t have appropriate “denominator” in the disclosure.

#### Calculation of ROE by Tokyo stock exchange

- $ROE = \text{Net income} / \{(\text{Net assets} - \text{Stock Warrant} - \text{attributable to non-controlling owners})\} \times 100(\%)$
- Net income divided by average of beginning and end year shareholders' equity. “Net asset minus (Stock Warrant and attributable to non-controlling owners)” becomes Owner’s equity, as “seed money” for how much earning for 1 years, that is the indicator of management efficiency. **(Tokyo stock Exchange HP)**

numerator of ROE

Net Profits attributable to parent company shareholders a	Net Profits attributable to non-controlling interests (NCI) x
y	z

a = Net Profits attributable to parent company shareholders

b = Net Profits = a+x

c = Comprehensive income attributable to parent company shareholders = a+y

c' = Comprehensive income attributable to non-controlling interests = x+z

d = Comprehensive income = c+c' = a+x+y+z

denominator of ROE

Owner's equity A	Non-controlling Interests (NCI) X+Z
Accumulated Other Comprehensive Income Y	

A = Owners' equity

B = (Calculation impossible)

C = Shareholder's equity = A+Y

D = Net Assets = A+X+Y+Z

# Document 9

## 3. Current situation and issues of ROE

### 3.3 ROE distribution comparison of each combination of the numerators and denominators

Toyo Keizai Mr.Hirota

We researched how different between ROE calculation of Tokyo Stock Exchange/JFSA and ROE calculation introduced at “3.2 Current situation and issues of ROE Calculation”.

**[Calculation]**

- ( a / A ) Net Profits attributable to parent company shareholders / Owner's equity  
= *excludes Accumulated other comprehensive income from denominator of p*
- ( b / B ) Net Profits / ( Owner's equity + Non-controlling Interests )  
= *includes Non-controlling Interests as a factor in ( a / A )*
- ( c / C ) Comprehensive income attributable to parent company shareholders / Shareholder's equity  
= *includes Other comprehensive income in numerator of P*
- ( d / D ) Comprehensive income / Net assets  
= *includes Non-controlling Interests as a factor in ( c / C )*

p = ( a / C ) Net Profits attributable to parent company shareholders / Shareholder's equity

- Median of general ROE(p) is 5.7%. Mean of general ROE is 6.3%. There is only 40% or less company could meet this percentage requirement if 8% of ROE is required in proxy voting policy.
- Calculation (a) and Calculation (b) are not so different from general ROE (p) as below chart. But still 70% of companies are higher % than general ROE (p).
- Median % of Calculation (c) and Calculation (d) have large different from general ROE (p) by 3.5%. It means other comprehensive income affects in numerator much more than denominator. Over 90% are larger than general ROE.

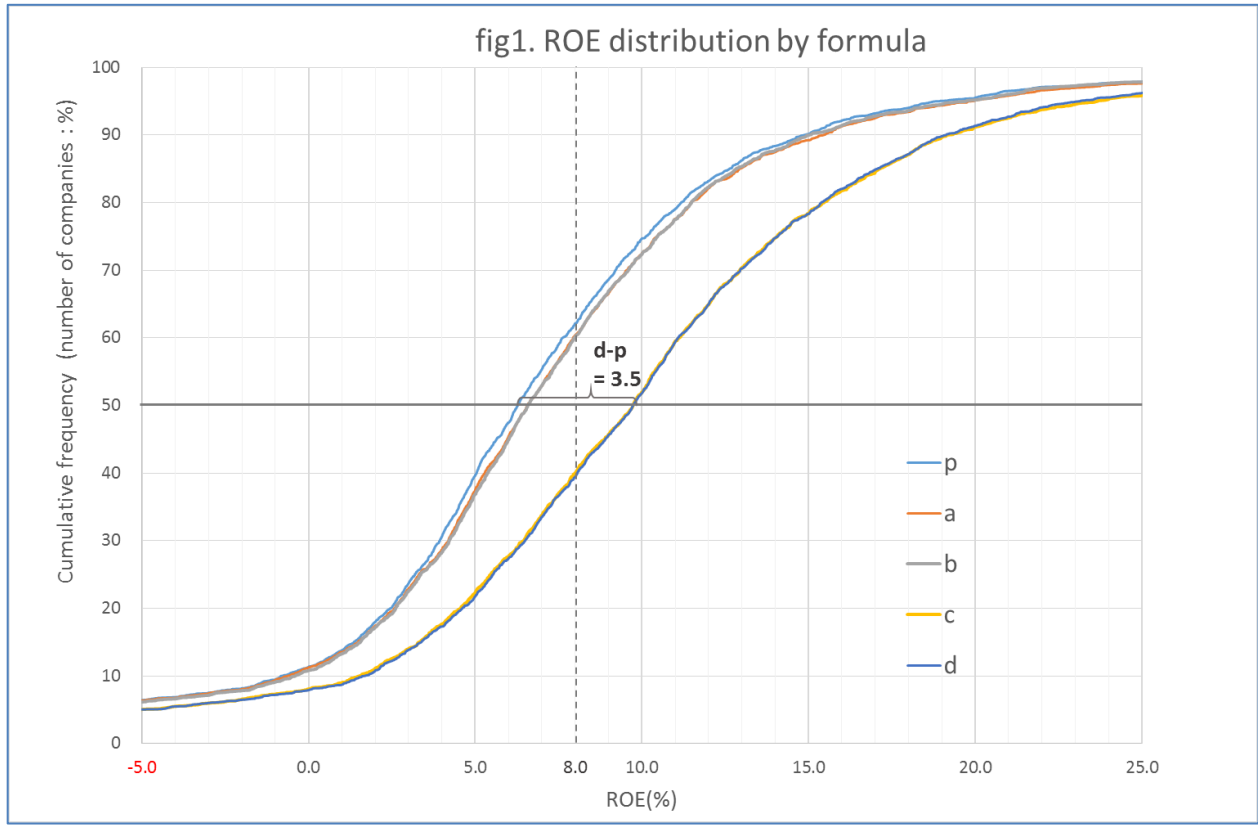


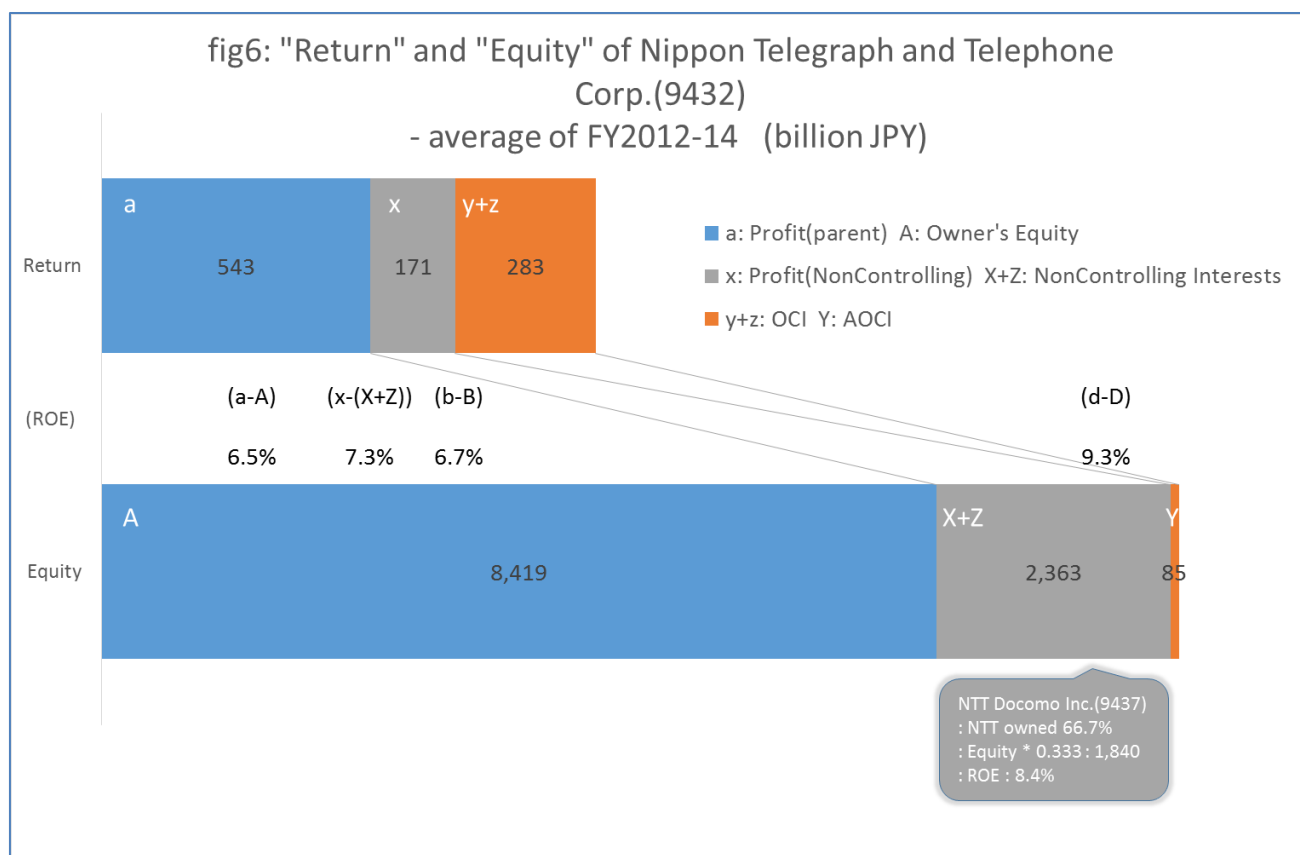
表 1 : 計算式別のROE統計値						
	社数 : num	p	a	b	c	d
中央値 : median (%)	2,693	6.3	6.6	6.6	9.7	9.7
平均値 : mean (%)		5.7	6.1	6.2	9.0	9.2
うちJPX400構成銘柄	388	11.4	11.8	11.7	16.7	16.6
現行ROE(p)より水準が高い会社 (%) : > p			70.9	68.6	94.3	92.8
現行ROE(p)と等しい (%) : = p			3.1	2.1	1.6	1.1
現行ROE(p)より水準が低い (%) : < p			26.0	29.3	4.2	6.2

**Source: TRENDPOT, TOYOKEIZAI Inc.**

\*東証1,2部, マザーズ, JASDAQへ上場している連結決算実施会社を対象に各社の直近3期平均ROEを集計

▲TSE's aggregation of ROE 3 years average, 1,2 section, Mothers, JASDAQ

- In other words, no much difference between Calculation (a) and general ROE when accumulated other comprehensive income is deducted from denominator of general ROE, and 3.5% increased from general ROE when accumulated other comprehensive income is added to numerator of Calculation (c).
- On other hands, Calculation (b) and (d) which is adjusted by attributable to non-controlling interests are not much different from calculations deducted attributable to non-controlling interests.
- In the case of Calculation (b) and (d), ROE values seem to be more volatile the attributable to non-controlling interests increases more in their capital. But it doesn't look like biased in either direction. (see fig.4, 5)
- NTT (9432) has large attributable to non-controlling interests for example. Because their main subsidiary, NTT Docomo, has larger ROE than parent NTT, NTT's ROE is higher when NTT include attributable to non-controlling interests in their calculation of ROE



## Document 10

### 4. Improvement of accounting standards and disclosure for the practical using of ROE

#### 4.1 Company's opinion for ROE

Mr. Fukai (Experienced IR, Management Planning Division, CFA)

- Companies adapted the target of ROE for responding to the request of investors. The targets has been set 5% or 10%.... Or 8 percent required by "Ito reports". Side-by-side feeling seems strong.
- Originally, individual companies are expected to estimate own cost of capital, and challenge to obtain higher ROE than it as much as possible. So, not only higher ROE, but also lower cost of capital is also important as corporate efforts. The goal is not only increasing the real number of ROE, would say to increase the gap between ROE and capital costs.
- Recognizing cost of capital of the company and using it for management decisions, investment decisions and evaluation performance have not been often yet, though there are exceptions such as some parts of large manufacturing companies and trading companies.
- In 90's, EVA was introduced in Japan. In the EVA approach, cost of capital is important management index. But only a few companies adopted it into their management system since then.. However, a subcommittee of the Japan Association of Corporate Directors, which was led by Professor Ito, released the research report in 2012. It referred that EVA is one of useful management tool. EVA might attract attention of Japanese managements again.

**EVA (Economic Value Added) = Net operating profit after tax – (costs of capital × Capital invested)**     **EVA is positive if "ROIC > Cost of Capital"**

- **ROE = Net operating profit after tax / Operating asset × (Operating asset / Shareholders' equity) = Net operating profit after tax margin × Financial leverage**  
**Shareholders' expectation is met if "ROE > Cost of Shareholder's Equity"**
- While companies try to increase ROE, profit margin and financial leverage could be improved. But if management pay attention to cost of capital for usual managerial decision, the speed of change could be accelerated. It would be idealistic that each company discloses capital cost for precondition of ROE target and discusses with investors. It will be difficult to make it requirement. But something to motivate voluntary disclosure is expected.
- In EU or US, concept of EVA is took into account when discussing Accounting standard and disclosure rules?
- There are some companies which use EVA and IFRS, like Kao and Asahi Glass. It is expected that EVA, ROE target and IFRS are organically linked and used for management in them.

Name	EVA	Adoption of IFRS	ROE Target	Others
Kao	○	From 2016	N/A	Estimate of next year's ROE is written on analyst meeting material.
Asahi Glass	○	From 2013	5 %	Mid-term ROE target is written on Financial report.



## Document 11

### 4. Improvement of accounting standards and disclosure for the practical using of ROE

#### 4.1 Discussion

#### **When you are focusing on number of ROE...**

Q1. What do you expect to the accounting standard? (Especially for IFRS. But if you have any requests to other accounting standard, please note them too)

Q2. What do you expect to the disclosure practice or rules?

(for example, disclose ROE under specific conditions for all companies, or disclose appropriate data as numerator and denominator for calculation of ROE, etc)

A2.1. It should be good for investors, if company disclose their own forecast ROE. However it must be high hurdle because company need to have their Capital policy for this year and have to disclose it.

Q3. Do you have any other comments for the accounting standard or disclosure practice regarding ROE?

#### **Please answer the following questions, if you manage database your own entity or belong to information providers....**

Q4. Do you have special treatment for calculation of ROE because different of accounting standers?

(for example, preparing different formula or managing items separately depends on accounting standard in your database, etc..)

A4.1 Regarding forecast ROE, we provide the consensus which is simple average of analysts' forecast ROE. Regarding actual ROE, we provide 2 types of data, 1. Company announcement, 2. Calculation in our company. About the 2nd item, we are careful that we take the same accounting term for numerators and denominators in order to adhere to the same definition. In addition, we adjust irregular accounting period as 12 months basis.

A4.2 Since both numerators and denominators are provided by XBRL in case of J-GAAP, we are calculating ROE using those data. In case of IFRS and US-GAAP companies, we are aggregating and calculating manually. However we are suffering from that sometimes the calculated ROE becomes different from company-announced ROE on the earning digest which submitted to TSE.

Q5, Do you have any other treatment for the differences of accounting standards?

(For example, to control companies which has already adopt IFRS9 or not in your database )

A5, Regarding actual ROE, there is a difference between calculated ROE by our company and the company-announced ROE, after adjusted irregular accounting period. There were 20 different companies in the First Section of the Tokyo Stock Exchange, in the latest case.

We haven't found the reason, yet. Whether company's mistake or our calculation wrong..