Silchester International Investors LLP (“Silchester”), acting on behalf of its clients, is the owner of 9,933,400 shares in Chugoku Bank, Ltd (the “Bank”). This represents 5.1% of the Bank’s issued share capital. Silchester’s clients have been an owner of the Bank since 2007.

Silchester has engaged with the Bank’s management and Board of Directors for more than 14 years. Silchester wants the Bank to maintain a sound capital structure, grow its revenues, fees and commissions and downsize its high cost legacy infrastructure.

On 11th April 2022, Silchester announced that it would submit a special dividend resolution to the Bank. On 13th May 2022, the Bank confirmed that the resolution would be voted on at the Bank’s June AGM.

**Silchester’s resolution calls for the Bank’s shareholders to approve the payment of an additional special dividend of JP¥ 29 per share.**

If approved, the total dividend paid by the Bank for the financial year ended 31st March 2022 would be JP¥ 57 per share. This compares to the Bank’s full year earnings of JP¥ 98 per share.

On 13th May 2022, the Bank issued a statement opposing Silchester’s special dividend resolution. The Bank argued that Silchester’s proposal ‘is based on a short-term view which does not take into account potential changes in the business environment or the need for continuous investment in the business. The Bank plans to utilise its capital even more actively for the development of regional economy’. The Bank added that ‘the shareholder proposal has a risk of damaging the Bank’s corporate value in the medium to long term and the interest of all shareholders’.

**The Bank’s arguments misinterpret and misrepresent Silchester’s special dividend resolution.** The Bank and its Board of Directors don’t seem to understand that shareholders own the Bank and that shareholders can ultimately determine the Bank’s shareholder return policy. The Bank incorrectly states that Silchester is only focused on short term returns, notwithstanding the long term nature of Silchester’s ownership of the Bank. The Bank and its Board of Directors are seeking to retain capital – not to benefit the Bank, its stakeholders, regulators, customers or shareholders – but for the comfort of management.

Silchester’s special dividend request is based on a simple philosophy. Silchester would like the Bank to distribute ordinary and special dividends to shareholders that total:

- 100% of the annual dividend income that the Bank receives on its equity holdings; and,
- 50% of the net income from the Bank’s core banking business.

Silchester’s pay-out philosophy allows the Bank to complete periodic share repurchases if the Board of Directors determines that these repurchases are in the long-term interest of the Bank.

Silchester’s pay-out philosophy allows the Bank to improve its operating performance over time, enhance the Bank’s technology infrastructure, ensure a smooth digital transition, increase lending to the local community, promote sustainable finance and expand into adjacent businesses if these are expected to improve the Bank’s earnings and exceed its cost of capital.
Silchester’s approach ensures that the Bank retains a fair share of the available earnings generated by the Bank’s core lending and banking activities. Silchester’s approach allows shareholders to benefit from all dividend income collected on the Bank’s equity holdings.

The Bank intends to repurchase a total of JPY 2bn of shares with respect to the 31st March 2022 financial year and intends to pay JPY 28 per share of dividends. If the special dividend resolution is approved, the Bank will retain around 30% of its consolidated earnings for the 31st March 2022 financial year.

Silchester’s approach does not adversely impact the Bank’s financial solvency or the Bank’s ability to meet its obligations as a regional financial institution.

- The Bank’s capital adequacy ratio stands at 13.8%. This compares to an average capital adequacy ratio of 9.6% for Japan’s regional banks and a minimum regulatory requirement of 4%. Contrary to the Bank’s 13th May 2022 statement, the Bank’s solvency ratios will not decline following the payment of a special dividend.

- The Bank benefits from excess customer deposits. If the Bank wishes to increase lending volumes to individuals, local businesses and governmental bodies, it can do so. Any lending must be done prudently and profitably. Contrary to the Bank’s 13th May 2022 statement, the Bank’s ability to expand its lending book and meet community obligations will not be impaired following the payment of a special dividend.

- Silchester’s approach does not require the Bank to dispose of its equity holdings. Silchester is simply asking the Bank to distribute all dividends from these equity holdings to shareholders. If the Bank independently chooses to sell one or more of its equity holdings, the proceeds of these sales should be distributed to shareholders via special dividends or opportunistic share repurchases.

Silchester’s approach forces the Bank and its Board of Directors to adopt a more appropriate capital allocation discipline. This provides the following medium and long term benefits:

- The Bank is more likely to improve its ROE and cover its cost of capital. Over the past decade, the Bank has delivered a ROE of approximately 4.1%. The Bank’s ROE has lagged the ROEs delivered by other Japanese companies including other regional banks. The Bank’s poor ROE arises from disappointing earnings, an excessively high cost-income ratio and excess capital retention. A low ROE is harmful to the Bank’s owners, its stakeholders and the broader community. Low ROEs destroy corporate value over time.

- The Bank’s reputation will improve. The Bank hopes to provide financial consultancy services to local businesses. To do so, the Bank and its Board of Directors must be seen to be responsible stewards of capital. Responsible stewards of capital display appropriate capital allocation policies.

- The Bank will increase returns to shareholders via a combination of stable ordinary dividends and ad hoc special dividends. The Bank’s primary owners are Japanese. These include individuals, families, insurance companies, pension plans, corporations and government bodies. Many of these are located in the broader Okayama Prefecture. Japanese shareholders rely on the Bank to grow its dividends. Higher dividends allow shareholders to meet their own financial obligations.

Silchester encourages all shareholders to carefully consider the special dividend proposal. Silchester encourages all shareholders to vote in favour of the special dividend proposal. The special dividend proposal gives all shareholders the right to express their views on the performance of the Bank and its management. A vote in favour of the special dividend resolution provides the Board of Directors with guidance on the Bank’s future capital allocation policies and holds them accountable for its execution.

Please contact Tim Linehan (tlinehan@silchester.com) with questions on this press release.
**About Silchester**

Silchester is a UK based asset management firm. Silchester invests client moneys in publicly traded non-US equity securities using a bottom up, value based, investment approach. Silchester is a ‘long-only’ manager. Silchester does not short securities, utilise derivatives or invest in convertible instruments. Silchester seeks to invest in companies trading cheaply relative to their assets, earnings or dividends. Silchester has been invested in Japanese equity securities since 1995.

Silchester is the appointed investment manager for several large commingled funds. One of these commingled funds is the Silchester International Investors International Value Equity Trust. The Northern Trust Company acts as the custodian for this commingled fund. The Northern Trust Company holds the shares for this commingled fund in a nominee account called Northern Trust Company AVFC Re: Silchester International Investors International Value Equity Trust. The Northern Trust Company has provided Silchester with a power of attorney granting Silchester the authority, as investment manager, to introduce the special dividend proposal. The Northern Trust Company is not otherwise involved with this proposal.

Silchester is not an ‘activist’ investor. Silchester is a fiduciary for its client assets and takes its corporate governance obligations seriously. Silchester will engage with portfolio companies where appropriate.
Silchester International Investors LLP (“Silchester”), acting on behalf of its clients, is the owner of 9,933,400 shares in Chugoku Bank Ltd (the “Bank”). This represents 5.1% of the Bank’s issued share capital. Silchester’s clients have been owners of the Bank since 2007.

Silchester has engaged with the Bank’s management and Board of Directors for more than 14 years. Silchester wants the Bank to maintain a sound capital structure, grow its revenues, fees and commissions and downsize its high cost legacy infrastructure.

Silchester is disappointed to report that the Bank’s Board of Directors has failed to put an appropriate capital allocation discipline in place. This, coupled with operational inefficiencies, means that the Bank has failed to deliver a return on equity (“ROE”) approaching 10%. A low ROE is particularly harmful to the Bank’s owners. The Bank’s primary owners are Japanese. These include insurance companies, pension plans, corporate treasuries, government bodies and individuals. Japanese shareholders, like Silchester’s clients, rely on the Bank to grow its dividends and increase its ROE.

In the financial year ended 31st March 2021, the Bank earned JPY 14.4 billion of net income. The Bank generated a ROE below 3%. Of the JPY 14.4 billion, JPY 11.2 billion originated from the Bank’s core banking activities. JPY 3.2 billion was collected as dividend income on the Bank’s equity holdings. The Bank has a significant number of equity holdings that are not needed to maintain customer relationships. The value of these equity holdings is a significant proportion of the Bank’s current market capitalisation.

For the year ended 31st March 2022, the Bank is forecasting net income of JPY 17.9 billion. This will generate a ROE of around 3%. The Bank expects to receive JPY 3.3 billion from its equity holdings during the year ended 31st March 2022.

On 7th February 2022, Silchester formally asked that the Bank to modify its dividend distribution policy. To minimise further damage to the Bank and its owners, Silchester asked the Bank to distribute ordinary and special dividends to shareholders that total:

- 100% of the annual dividend income that the Bank receives on its equity holdings; and,
- 50% of the net income from the Bank’s core banking business.

Silchester’s proposed pay-out policy would ensure that the Bank retains a fair share of the available earnings generated by the Bank’s core lending and banking activities. It would give the Bank sufficient financial flexibility to expand its banking businesses. This dividend pay-out policy allows the Bank’s shareholders to benefit from all of the dividend income collected on the Bank’s equity holdings.

Adopting this dividend pay-out policy does not adversely affect the Bank and/or harm its future business prospects. It does not jeopardise the Bank’s ability to meet solvency requirements, to work with its customers and/or to meet its obligations to stakeholders in the broader Okayama Prefecture.

The Bank and its Board of Directors rejected Silchester’s request.

On 25th March 2022, the Bank announced that it would increase the final dividend for the 31st March 2022 financial year by JPY 5 per share. The Bank announced that a total of JPY 28 per share of dividends would be paid in a financial year where the Bank forecasts earnings of JPY 96 per share.
Following the 25th March 2022 revision, Silchester asked the Bank and its Board of Directors to adopt Silchester’s proposed pay-out policy, announce a further special dividend and/or a share buyback. The Bank and its Board of Directors rejected Silchester’s request.

**The Bank’s current dividend distribution policy is insufficient and, if uncorrected, will result in further harm to the Bank’s owners, including its Japanese shareholders.**

On 11th April 2022, Silchester submitted a formal demand letter to the Bank. Silchester’s demand letter requires the Bank to add a special dividend proposal to the agenda of the Bank’s annual general meeting which will occur in June 2022.

**If Silchester’s proposal is approved by shareholders, an additional special dividend of JP¥ 29 per share will be paid to all shareholders of record as of 30th September 2022.**

The total dividend paid by the Bank with respect to the financial year ended 31st March 2022 would be JP¥ 57 per share versus the Bank’s JP¥ 96 per share earnings forecast.

Silchester will work with the Bank to ensure that the special dividend proposal is properly presented in the Bank’s AGM material. Silchester has asked the Bank to publicly announce that Silchester has submitted the special dividend proposal. Silchester has asked the Bank to publish the contents of the demand letter by posting it on TDnet, the Bank’s website and/or by other equivalent means.

Silchester encourages all shareholders to carefully consider the special dividend proposal. Silchester encourages all shareholders to vote in favour of the special dividend proposal. The special dividend proposal will give all shareholders the right to express their views on the performance of the Bank and its management. A vote in favour of the special dividend resolution will provide the Board of Directors with guidance on the Bank’s future capital allocation and dividend distribution policies.

Please contact Tim Linehan (tlinehan@silchester.com) with questions on this press release.
About Silchester

Silchester is a UK based asset management firm. Silchester invests client moneys in publicly traded non-US equity securities using a bottom up, value based, investment approach. Silchester is a ‘long-only’ manager. Silchester does not short securities, utilise derivatives or invest in convertible instruments. Silchester seeks to invest in companies trading cheaply relative to their assets, earnings or dividends. Silchester has been invested in Japanese equity securities since 1995. As of 31st March 2022, Silchester has more than JP¥ 1.9 trillion of its client assets invested in equity securities issued by publicly traded Japanese companies.

Silchester is the appointed investment manager for several large commingled funds. One of these commingled funds is the Silchester International Investors International Value Equity Trust. The Northern Trust Company acts as the custodian for this commingled fund. The Northern Trust Company holds the shares for this commingled fund in a nominee account called Northern Trust Company AVFC Re: Silchester International Investors International Value Equity Trust. The Northern Trust Company has provided Silchester with a power of attorney granting Silchester the authority, as investment manager, to introduce the special dividend proposal. The Northern Trust Company is not otherwise involved with this proposal.

Silchester is not an ‘activist’ investor. Silchester is a fiduciary for its client assets and takes its corporate governance obligations seriously. Silchester will engage with portfolio companies where appropriate.

Silchester first invested in the Bank in October 2006. Silchester has regularly discussed the Bank’s operating performance and capital allocation with the Bank’s Board of Directors and senior management. Silchester has sought for these discussions to remain confidential between Silchester and the Bank. Silchester has been forced to make this proposal public because of the Bank’s unwillingness to seriously consider Silchester’s proposals.

As of 31st March 2022, Silchester can exercise control over 5.1% of the Bank’s issued share capital. The Silchester International Investors International Value Equity Trust holds over 2.2% of the Bank’s issued share capital and has done so continuously for over six (6) calendar months. Silchester’s clients are, collectively, the Bank’s largest shareholder.