SONY

Financial Services Segment Small Meeting

March 27, 2024

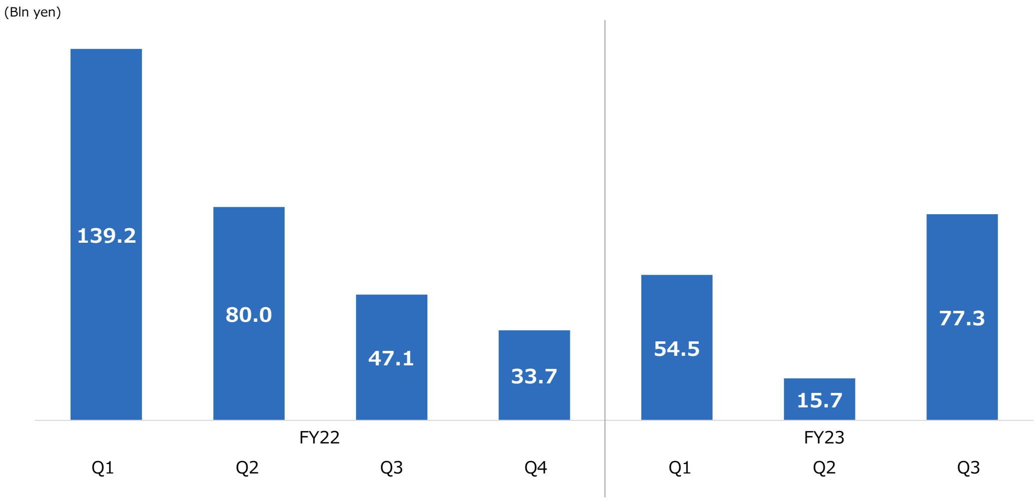
Sony Group Corporation

- Today, using the materials I have on hand, I will explain the fluctuations in operating income in the Financial Services segment as well as the landscape in which this is happening. Afterwards, we will have a question-and-answer session.
- We plan to disclosure the presentation materials on our website later.

Operating Income in Financial Services Segment

■ **Considerable fluctuations in operating income in the Financial Services segment following the adoption of IFRS 17**

Operating Income in the Financial Services Segment (IFRS 17)

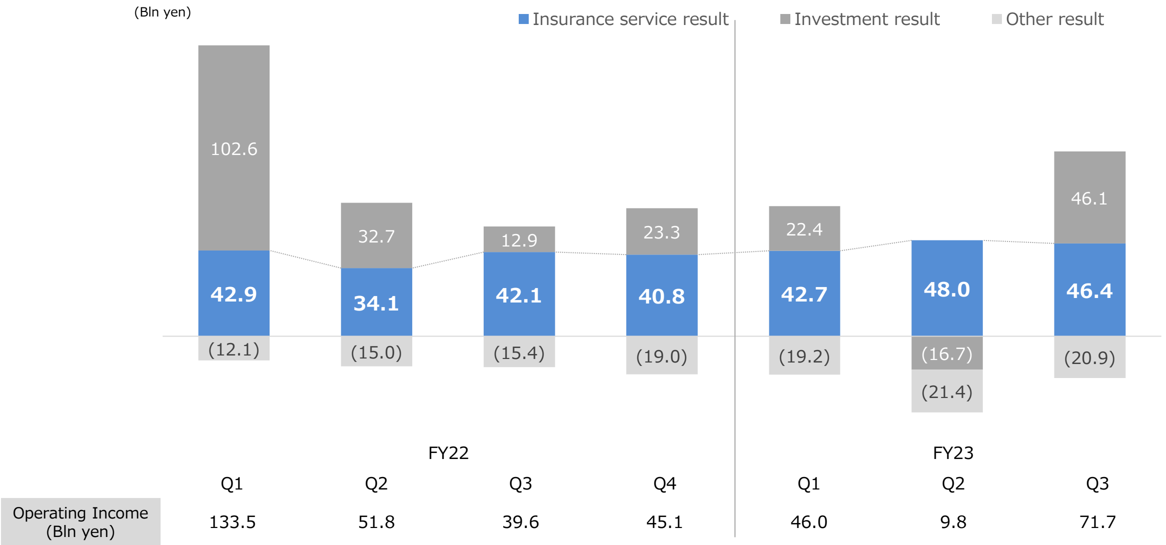


- This chart shows quarterly trends in operating income in the Financial Services segment after the adoption of International Financial Reporting Standards 17 ("IFRS 17").
- Operating income for the fiscal year ended March 31, 2024 decreased significantly in the second quarter, while increased significantly in the third quarter.
- This considerable change was caused by the significant impact of market fluctuations on Sony Life's operating income.

Operating Income for Sony Life

- **While large fluctuations were noted in operating income for Sony Life, which comprises the bulk of operating income for the Financial Services segment, insurance service result arising from the life insurance business has been stable.**

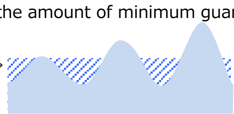
Breakdown of Operating Income for Sony Life (IFRS 17)



- This chart shows the trends of the breakdown of Sony Life's operating income.
- The operating income can be broadly divided into three components: insurance service result, investment result, and other result.
- Of these components, insurance service result, shown in blue, is profits related to Sony Life's core business as a life insurance company, which are insurance underwriting and payment. As shown in the chart, these profits have remained stable in response to Sony Life's business growth.
- Investment result, shown in dark gray, includes the effects of market fluctuations, and such fluctuations have become significant since the adoption of IFRS 17. We have previously explained that this profit fluctuation is mainly related to variable insurance, but I would like to explain what I mean by variable insurance.
- The breakdown on this slide is also disclosed in the supplemental information for the Consolidated Financial Results starting this fiscal year.

Distinct Features of Each Insurance Type

- **With variable insurance (with minimum guarantee), the company bears any portion of investment performance falling below the minimum guarantee.**

Insurance type	Insurance amount	Applicable asset account	Effect from market fluctuations / Attribution from investment performance
Fixed insurance	No change regardless of investment performance	General account	Small Effect appears on balance sheets
Variable insurance (without minimum guarantee)[1]	Changes based on investment performance	Separate account	Large Changes attributed to policyholder
Variable insurance (with minimum guarantee)[2]	Changes in response to investment performance but will not fall below certain amount (i.e., the amount of minimum guarantee) 	Separate account However, minimum guarantee is a general account	Large Company bears portion falling below the amount of minimum guarantee

1. Includes variable annuities such as SOVANI
2. In principle, death benefit and serious disability benefit only

- Sony Life handles two types of insurance: fixed insurance and variable insurance. Furthermore, among the different types of variable insurance, some include a minimum guarantee and some do not.

- Insurance companies manage assets using policyholder premiums received as their asset basis . The amount insured for fixed insurance is determined by the insurance contract and does not change in response to investment performance, but for variable insurance, the death/serious disability benefit and cash surrender value payouts fluctuate based on the performance of the investment.

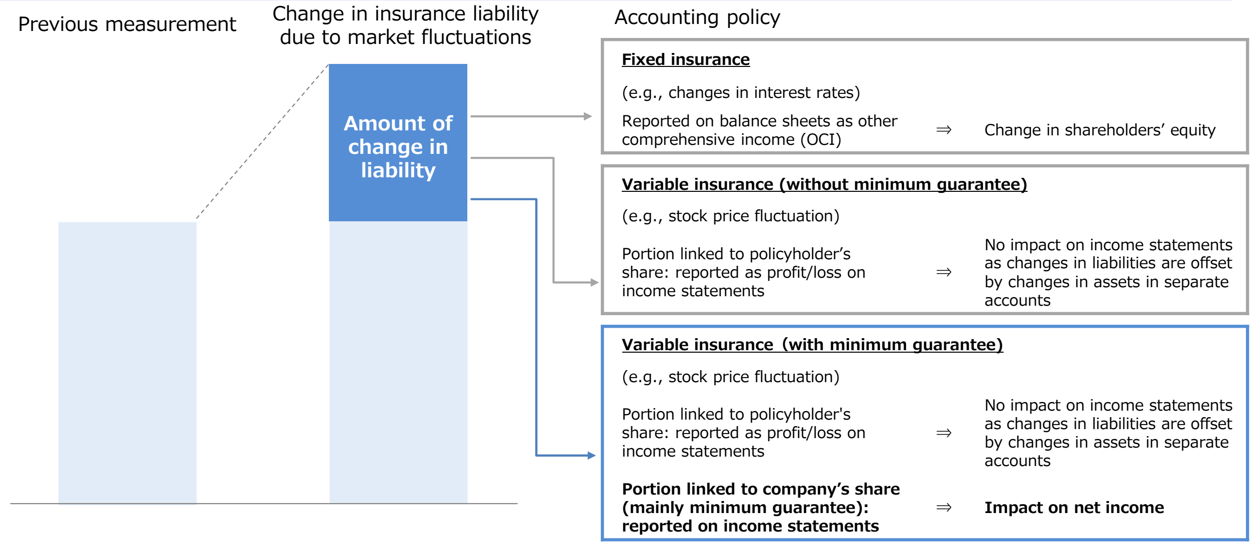
- There are two types of accounts in the life insurance company: the general account and separate accounts. Assets corresponding to some types of insurance, such as variable insurance, where investment performance is reflected in the insured amount, are managed separately from other accounts as separate accounts. As a principle, the gains and losses from such investments belong to the policyholder.

- Some variable insurance products provide a minimum guarantee, and if the amount of asset under management for insurance customers falls below the level of the minimum guarantee, Sony Life will bear the cost of the difference between the insurance claims and the minimum guarantee in order to guarantee the insurance payment amount.

- Since the assets corresponding to this minimum guarantee do not directly belong to the policyholder, such assets are managed with the general account.

Management under IFRS 17

- **Under IFRS 17, accounting policies differ based on insurance type.**
- **For variable insurance (with minimum guarantee), net income is affected since changes in insurance liability pertaining to the minimum guaranteed portion appear as profit/loss on income statements.**



- Under IFRS 17, insurance liabilities change due to the mark-to-market valuation done each period, and regarding how to reflect these changes in our accounting, we select and utilize accounting policies based on the type of insurance.

- For fixed insurance, if insurance liabilities change due to market fluctuations, they do not affect the profit and loss statement (the "PL") since such changes are recorded in the on the balance sheet as other comprehensive income.

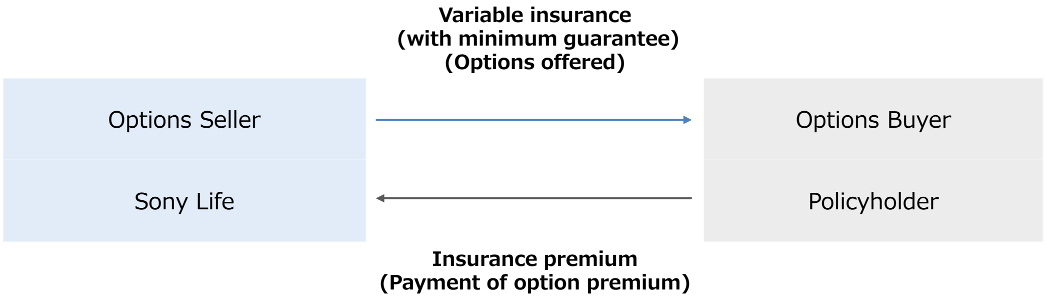
- In addition, for variable insurance without a minimum guarantee, changes in liabilities are recognized as profit or losses, but they are offset by changes in assets. Therefore, this does not affect the PL.

- On the other hand, for variable insurance with a minimum guarantee, if the portion of insurance liabilities pertaining to the minimum guarantee changes, such changes will be recorded as a change in net income.

Relationship Akin to Options Trading

- **If variable insurance (with minimum guarantee) is viewed as a type of option, the insurance premiums Sony Life collects as option seller are comparable to an options premiums.**

<u>**Relationship Akin to Options Trading**</u>

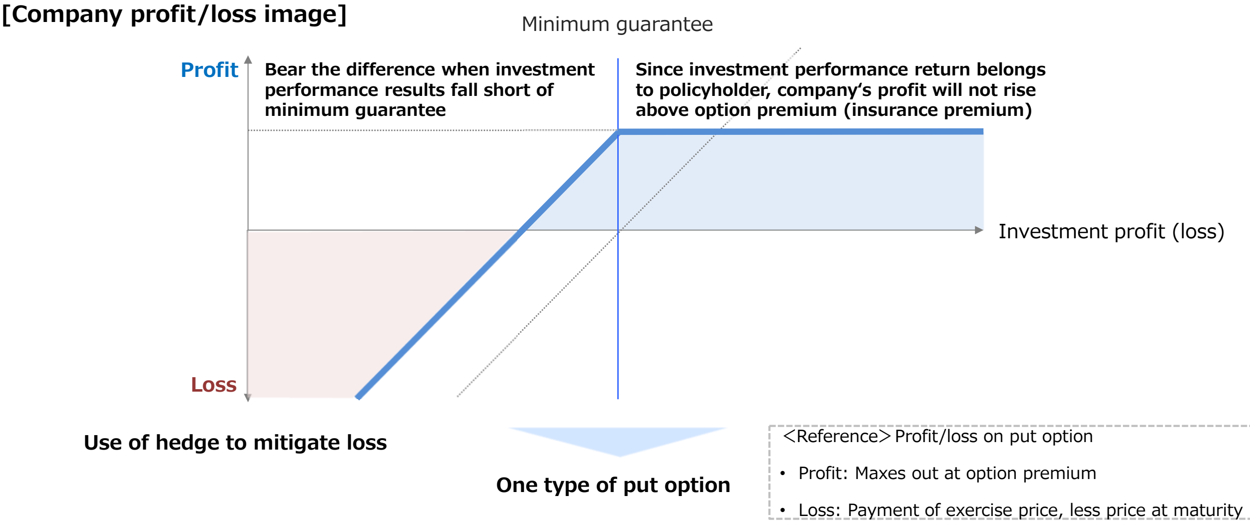


- The minimum guarantee is viewed as a type of option, and Sony Life, as an options seller, provides options to policyholders, who are options buyers, and we could say that, in return, Sony Life receives an insurance premium equivalent to the option premium.

Option-like Characteristic of Variable Insurance (with Minimum Guarantee)

■ **Variable insurance (with minimum guarantee) is a type of put option.**

Variable insurance (with minimum guarantee)
[Company profit/loss image]



<Reference> Profit/loss on put option

- Profit: Maxes out at option premium
- Loss: Payment of exercise price, less price at maturity

- This is an image of the changes in Sony Life's gains and losses that occur in variable insurance with a minimum guarantee.
- Sony Life's profit remains constant in the event that the investment performance significantly exceeds the minimum guarantee amount, since the return from investment performance belongs to the policyholder, but if it falls below the minimum guarantee amount, Sony Life must bear the difference between the minimum guarantee amount and the investment performance.
- Thus, variable insurance with a minimum guarantee has the characteristics of a put option, where the profit is limited to the option premium and losses increase when the amount falls below a certain threshold.
- Given this characteristic, Sony Life employs various hedging measures to limit its losses.

Key Factors in Market Fluctuation

- **Among market fluctuation factors, implied volatility is one such factor that is difficult to hedge.**

Key Market Fluctuation Factors and Corresponding Hedge Status

Hedge Applicable[1]

Fluctuation factors	Item risk	Hedge procedure
Interest rates	Interest decline	Fair value option (FVO) applied Bonds with selected bonds
Exchange rates	Yen appreciation	US treasury bond repurchase agreements, FX contracts
Stocks	Stock price drop	Stock index futures transactions

Hedge Not Applicable

Fluctuation factors	Item risk	Nature and response
Implied volatility	Rise in implied volatility for interest rates, stock prices, exchange rates	• Currently not hedged due to difficulty in applying hedge procedures • Because effect of implied volatility appears as valuation gain/loss arising from a type of option, risk decreases with approaching maturity
Inflation	Rise in inflation rate[2]	• Currently not hedged due to difficulty in applying hedge procedures

1. The portion attributable to the company as the minimum guarantee pertaining to variable insurance is covered
2. Rise in inflation rate negatively affects the income through an increase in anticipated future business expenses

See, Appendix: Rationale for for why Implied Volatility Hedging is Difficult

- This page shows the main factors influencing market fluctuations that impact variable insurance and how we hedge against them.

- While we have previously used various hedging methods for interest rates, foreign exchange rates, and stocks, we do not hedge against fluctuations in implied volatility or inflation rates since they are difficult to hedge through the market.

Impact of Fluctuations on Implied Volatility

- **In contrast to an increase in option price, when implied volatility increases, the insurance premium (equivalent to the option premium) remains fixed.**

Variable insurance
(with minimum guarantee)
(Options offered)

Options Seller	→ / ←	Options Buyer
Sony Life		Policyholder

Insurance premium
(Payment of option premium)

Effect When Implied Volatility Changes

Implied volatility	Option premium (insurance premium)	Option value for policyholder	
Rise ↑	**Fixed →**	**Rise ↑**	**Worsening profitability**
Fall ↓	Fixed →	Fall ↓	

- Among the items listed on the previous slide that are not subject to hedging, an increase in implied volatility in the market has a significant negative impact on profits and losses.
- This is due to the fact that while the insurance premiums that Sony Life receives from policyholders remain unchanged with a rise in implied volatility, the value of options held by policyholders increases.
- In particular, for whole-life variable insurance policies with lengthy contract terms, this variance in option value tends to be extremely large.

Current Issues and Countermeasures

- **Policies in force include substantial variable insurance (with minimum guarantee); market fluctuations could thus significantly impact on business results.**
- **We have been proceeding with revisions of product strategy, and considering more advanced hedge procedures and utilization of reinsurance.**

Background

In the past, whole-life insurance including variable insurance (with minimum guarantee) has been largely sold (approx. 40% of new policies in FY12 ((Annualized premium basis))

Management issues

Substantial portion of policy amount in force consists of variable insurance (with minimum guarantee)

--> Market fluctuations have a significant impact on business results

Measures

Revise product strategy --> Currently, whole-life insurance has declined to roughly 10% of new policies in FY22 (Annualized premium basis)
Consider more advanced hedging instruments
Consider utilization of reinsurance

- Market fluctuations of gains and losses related to minimum guarantees for variable insurance, as we have been discussing, have been influenced by insurance contracts acquired in the past.
- In the past, Sony Life sold many whole-life insurance products with long insurance periods. These accounted for approximately 40% of annualized premiums for new policies in the past.
- These include many of the variable whole-life insurance policies with a minimum guarantee that I mentioned earlier, and many of these policies are currently included in policies in force. Consequently, there has still been the impact of market fluctuations on gains and losses.
- As we look ahead to the partial spin-off and the listing of shares of Sony Financial Group Inc., a wholly-owned subsidiary of our Financial Services segment, we recognize that the scale of these fluctuations in profits and losses is a management issue.
- As a countermeasure, we revised our product strategy and have reduced the proportion of whole-life insurance in new policies to less than 10% in FY22.
- In addition, we have long been engaged in risk hedging efforts against fluctuations in interest rates, exchange rates, and stocks, but we are currently working to introduce methods that will repress fluctuations in gains and losses to improve hedge accuracy and to apply more effective hedging instruments for dealing with the impact of implied volatility.
- Furthermore, we are currently in the process of considering and preparing for the transfer of policies in force, or reinsurance transactions, which could be a more extensive measure.
- Going forward, while taking steps to reduce the impact of these market fluctuations, we aim to ensure stable insurance service result, which is the profit from the core business, as I mentioned at the beginning. We expect this to enable stable profit growth for the entire Financial Services business.
- This concludes my explanation. Thank you for your attention.