Upgrading Risk Management

Basic Risk Management Stance

In today's environment, characterized by ongoing liberalization and internationalization of financial services and development of financial and information technology, the risks confronting banks are growing more varied and complex.

Against this backdrop, it is crucial for banks to appropriately manage and control risks according to the attributes of specific business tasks and risks, in order to enhance corporate value while maintaining soundness and reliability of management.

We have positioned the appropriate management of risk as a top management priority, and the Board of Directors has formulated "Basic Policy of Risk Management." Based on this policy, we engage in management of risks and work to establish and reinforce a risk management framework.

In addition to controlling specific types of risks, such as credit risk, market risk, and liquidity risk, we also need to comprehensively identify risks confronting the entire bank, and control them in gross by means such as comparing the magnitude of risks with the Bank's management strength. To this end, we established the Risk Management Department. As the entity in charge of controlling risks concerning the entire bank in gross, this department is developing frameworks to allow integrated risk management. In these ways, we are working to reinforce management of various risks and undertake integrated risk management at more advanced level.

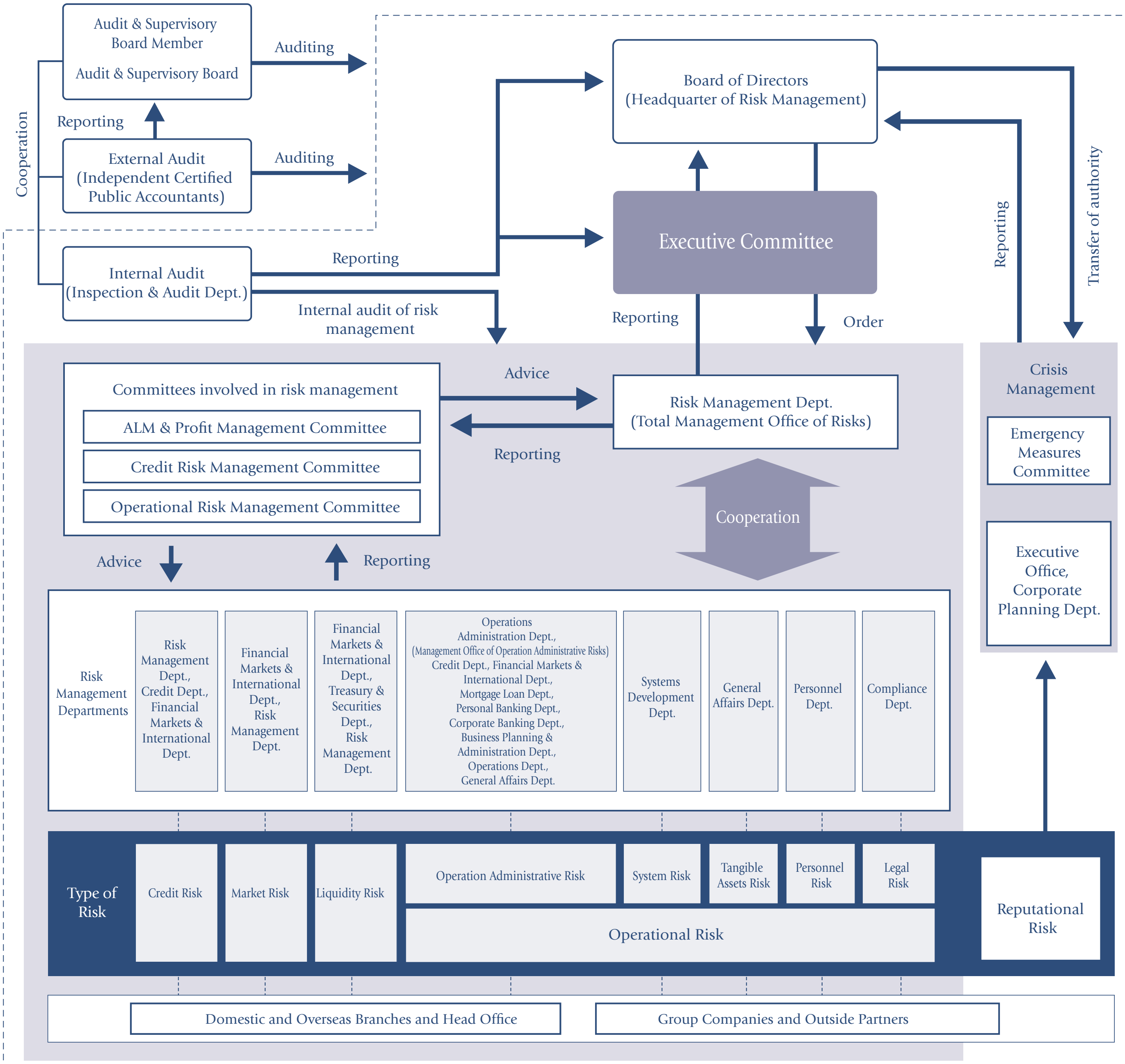
Further, Inspection & Audit Department conducts internal audit to evaluate the appropriateness of development of the risk management framework and the functional effectiveness thereof.

Integrated Risk Management

The Bank has adopted an "integrated risk management system" that measures risk exposure of risks such as credit risk, market risk, and other risks confronting the Bank by categories using unified framework (such as VaR), and compare them in gross with the management strength (equity capital).

In specific, we control risks by determining in the Board of Directors held in every half fiscal year the risk capital allocation by each risk category utilizing the amount calculated by deducting valuation and translation adjustments from Common Equity Tier 1 capital as the capital allocation resource.

With regard to the status of the risk exposure, the risk management departments monitor and check periodically whether the risk exposure is within the allocated risk capital. Current risk conditions are reported to top management on a monthly basis through the ALM & Profit Management Committee and Executive Committee.



Audit & Supervisory Board Member
Audit & Supervisory Board
Auditing
Reporting
Cooperation
External Audit (Independent Certified Public Accountants)
Auditing
Internal Audit (Inspection & Audit Dept.)
Reporting
Internal audit of risk management
Board of Directors (Headquarter of Risk Management)
Executive Committee
Reporting
Order
Reporting
Transfer of authority
Committees involved in risk management
ALM & Profit Management Committee
Credit Risk Management Committee
Operational Risk Management Committee
Advice
Reporting
Risk Management Dept. (Total Management Office of Risks)
Cooperation
Crisis Management
Emergency Measures Committee
Executive Office, Corporate Planning Dept.
Advice
Reporting
Risk Management Departments
Risk Management Dept., Credit Dept., Financial Markets & International Dept.
Financial Markets & International Dept., Risk Management Dept.
Financial Markets & International Dept., Treasury & Securities Dept., Risk Management Dept.
Operations Administration Dept., (Management Office of Operation Administrative Risks) Credit Dept., Financial Markets & International Dept., Mortgage Loan Dept., Personal Banking Dept., Corporate Banking Dept., Business Planning & Administration Dept., Operations Dept., General Affairs Dept.
Systems Development Dept.
General Affairs Dept.
Personnel Dept.
Compliance Dept.
Type of Risk
Credit Risk
Market Risk
Liquidity Risk
Operation Administrative Risk
System Risk
Tangible Assets Risk
Personnel Risk
Legal Risk
Operational Risk
Reputational Risk
Domestic and Overseas Branches and Head Office
Group Companies and Outside Partners

Credit Risk Management

Credit risk refers to the risk of the Bank incurring a loss as a result of default on the payment of interest or return/redemption of the principal as agreed upon by a client or issuer of securities due to such factors as deterioration in business performance.

At the Bank, loan assets account for the majority of credit risk, so ensuring the soundness of loan assets into the future is a critical objective for credit risk management.

Credit Risk Management Stance

Strict credit risk management requires mutual-checking among departments exposed to credit risk. The Bank is structured in a manner that makes checking functions work all the time: the Risk Management Department—which is independent of the business promotion division and the screening division—plans and verifies management systems that are vital to credit risk management, including systems for credit rating, self-assessment of the Bank's assets and write-off/reserve provisioning.

The Bank has also established the Credit Risk Management Committee, consisting of directors in charge of the Risk Management Department and general managers in charge of relevant departments. The Committee discusses and examines the status of bank-wide credit risks and important issues cutting across organizational boundaries to develop a common awareness of credit risks.

Individual Credit Screening and Management Stance

Having established the basic policy for its lending business in the form of "Credit Policy," the Bank is striving to accumulate sound loan assets and prevent non-performing loans from arising while existing harmoniously with local communities and complying with laws and regulations, etc.

When providing a loan, the Bank endeavors to facilitate the supply of funds to meet the sound demand for finance by making accurate and strict judgments on the purpose of use of funds, the financial sources for repayment, etc. in the loan application based on a comprehensive evaluation of quantitative aspects such as the financial position of clients, as well as qualitative aspects such as industry trends and growth potential. We are also developing a screening system and an education and training framework, in addition to enhancing system support.

After providing a loan, we strive to prevent loan assets from deteriorating by enhancing our stance to monitoring and managing business performance throughout the fiscal year so that changes in the business climate, etc. can be identified quickly and prompt responses can be taken, while deepening our relationship with clients. Furthermore, we have established the "Judgment Office" in the Credit Department, which is staffed by professionals with extensive experience in assessing the fiscal health of businesses, who provide finely-tuned support to clients in making managerial and financial improvements.

Credit Rating System and Self-assessment System

The Bank's "Credit Rating System" is an intra-bank system designed to determine credit risk in an objective manner, and consists of the "Borrower Rating System," "Retail Pool Management System," etc.

On the basis of the internal criterion, the "Borrower Rating System" rates the creditworthiness of clients based on an internal rating scale of 1 to 15. The ratings framework is consistent with borrower classification used in the self-assessment of assets, and is used in loan classification tasks that serve as the basis for calculating Reserves for Possible Loan Losses. It is also widely used in credit risk management operations in general, as a benchmark for management in the lending business as well as an indicator for the measurement of credit risk exposure, risk-return management, etc.

"Self-assessment" is conducted for the purpose of examining assets held by the Bank on an individual basis, and accurately identifying the Bank's actual asset position. It is an important means of managing credit risks. Self-assessment involves dividing borrowers into five borrower categories according to the internal borrower rating, and rating their assets on a scale of 1 to 4 according to their recoverability and the extent of risk of loss of value. The amount of future loss is estimated according to the rating, and accounted for as Reserves for Possible Loan Losses.

Measurement of Credit Risk Exposure and Loan Portfolio Management

The Risk Management Department conducts statistical analyses of default rates and loan coverage to measure credit risk exposure. Credit risk exposure quantifies losses that might arise in the future from the loan portfolio exposed to credit risks such as loan assets, and is utilized in the management of loan portfolios and the allocation of risk capital.

In managing loan portfolios, we analyze credit risk exposure, in addition to analyzing trends in loan portfolios and identifying issues based on monitoring aimed at preventing the concentration of credit in particular sectors and the simulation of risks being realized, in pursuit of more advanced credit risk management.

Market Risk Management

Market risk refers to the risk of the Bank incurring losses due to fluctuations in interest rates, foreign exchange rates, share prices, and other market factors. The Bank manages such market risk together with market liquidity risk.

The organization of departments in charge of market transactions is structured in such a way that they check each other: the Treasury & Securities Department serves as the front office department in charge of transactions, whereas the Financial Markets & International Department serves as the middle-office and back-office department in charge of risk management and administrative processing.

The Bank's basic policy is to appropriately control risks by recognizing the significance of the effect of market fluctuations on its management. Investments especially in bonds, shares, etc. are exposed to risks of price fluctuations, so these transactions are performed within appropriate bounds in terms of scale subject to adequate risk management.

At present, the Bank mainly uses VaR as an indicator tool for measuring and analyzing market risk. In addition, it controls and analyzes the market risk through monitoring valuation gain or loss, utilizing risk indicators such as BPV and outlier standard, and by observing the degree to which market factor fluctuations affect profit and gain for the period and on the capital adequacy ratio, etc. These analysis results are reported to the ALM & Profit Management Committee and Executive Committee.

Evaluations of interest rate risk may significantly differ depending on the recognition of maturity for floating deposit that consists of demand deposit and saving deposit, etc. The Bank uses the Core Deposit Internal Model for the estimation of material maturity regarding liquid deposit.

Liquidity Risk Management

Liquidity risk consists of cash flow risk and market liquidity risk.

Cash flow risk refers to the risk of the Bank incurring a loss due to difficulties in securing necessary funds or as a result of raising funds at high interest rates because of discrepancies between the timings of investment and funding, the unexpected outflow of funds and other such reasons.

With respect to cash flow risk, the Bank determines the department in charge of cash flow management, which rigorously manages cash flow periodically (e.g., daily, weekly, monthly) including its overseas bases. In addition, the ALM & Profit Management Committee, which is convened each month, takes every precaution to facilitate cash flow by identifying and analyzing the cash flow status, the balance between investing and funding, interest rate movements and other factors.

Moreover, the Bank conducts a stress test based on a scenario with the certain amount of deposit cancellation and confirms that the Bank has sufficient assets with high liquidity such as national government bonds to cope with those transactions every half fiscal year, and reports the result to the ALM & Profit Management Committee and Executive Committee.

We have also prepared a "Contingency Plan" to prepare against emergencies, and are taking every precaution including developing systems that enable us to respond appropriately to a wide range of scenarios.

Market liquidity risk refers to the risk of incurring a loss due to not being able to perform transactions because of market turmoil, etc. or as a result of being forced to trade at severely unfavorable prices compared to normal circumstances when selling assets, etc.

Market liquidity risk is managed together with market risk management.

Operational Risk Management

Operational risk refers to the risk of the Bank incurring a loss as a result of inadequate banking operation processes, inadequate activities conducted by executives, employees, temporary staff or other workers or inadequate systems, or due to an external event. In order to effectively manage such risk according to the organizational structure and the nature of operations, the Bank divides operational risk into five categories: (1) administrative risk, (2) system risk, (3) tangible asset risk, (4) human risk, and (5) legal risk.

The "Basic Policy of Risk Management" and the "Basic Rules for Operational Risk Management," both of which were formulated by the Board of Directors and prescribe the basics of operational risk management, stipulate that the director in charge of the Risk Management Department be responsible for overseeing operational risk management in general, and that the Risk Management Department be the department in charge of integrated operational risk management. Under the instructions and supervision of the director in charge, the Risk Management Department plans and oversees operational risk management overall, while each risk-management-related department manages its own risks from a more technical perspective.

In addition, the Bank has established the Operational Risk Management Committee as an organization for deliberating important matters pertaining to operational risk.

As the specific method for managing operational risk, the Bank has introduced the structure of Risk Control Self Assessment (RCSA) and manages operational risk in a comprehensive manner accordingly. The Bank also manages administrative risk, system risk, and other types of risks individually.

Administrative risk refers to the risk of incurring a loss due to an executive, employee, etc. failing to perform administrative processes accurately, causing an accident, engaging in misconduct, etc.

At the Bank, each and every employee is striving to execute administrative processes more rigorously based on his/her commitment to executing them with precision at all times according to the basic principles, in order to maintain and improve the level of trust placed in us by our customers. We are also working to prevent administrative mishaps and improve overall administrative quality based on internal checking efforts, by such means as the departments of the head office in charge of administration visiting the branches and giving administrative guidance to them, the Inspection & Audit Department conducting on-site audits in the head office's departments as well as the branches, and the branches conducting self-inspection.

System risk refers to the risk of customers and the Bank incurring a loss due to inadequacies in the system such as the failure and malfunctioning of a computer system, or the unauthorized use of computers.

We take various safety measures against foreseeable risks: we conduct quality control of software based on thorough testing, and take measures against unauthorized access and computer virus intrusion to prevent information leakage, in addition to taking safety measures at the facility level, including owing a computer center equipped with seismic-isolated floors, uninterrupted power supplies and other disaster-proofing facilities as well as securing a backup center. To prepare against accidents, we have devised a "Contingency Plan" and are taking every precaution.

With respect to tangible asset risk, human risk, and legal risk, the Bank has assigned the departments in charge of playing a central role in managing these respective risks.

Crisis Management

The Bank has prepared a "Contingency Plan" aimed at ensuring uninterrupted operations in times of unprecedented events, such as natural disasters, criminal activities, computer system breakdown, the spread of rumors, and the outbreak of new-type influenza. This plan is designed to help the Bank respond appropriately to such events and minimize their impact on its operations.

To address the occurrence of major large-scale events, the Bank will convene its "Emergency Measures Committee" to gather information and issue guidance and instructions in a unified manner. In addition, the Bank is working to strengthen its crisis management system, including by holding regular training drills based on its "Contingency Plan," and by periodically reviewing that plan.

Upgrading Compliance

To become a bank that is high evaluated from customers and shareholders, the Bank needs to establish "compliance system" that serves as the foundation for the sound business operations.

In strong recognition of the social responsibility and public mission that financial institutions need to perform, the Bank regards the enhancement of compliance as one of the most important management issues and strives for the strict observance of laws, regulations, rules and social norms and the enforcement of corporate ethics through day-to-day operations.

Compliance System

Under the Board of Directors, which serves as the supreme body responsible for compliance, the Bank has established the Compliance Committee, which is entrusted by the Board of Directors to deliberate important matters related to compliance. In addition, we have assigned Compliance Supervisors and Compliance Officers in all of our departments and branches, who are working to strictly enforce compliance by fostering compliance awareness and providing educational guidance.

The Compliance Department, as the compliance oversight department, centralizes the management of compliance-related matters and thereby strives to develop and establish a compliance system and a customer protection management system.

Compliance put into Practice

In order to fulfill our "Corporate Philosophy," we have stipulated the "Corporate Ethics" as our basic policy for compliance, and the "Code of Conduct" as our compliance standard.

Having distributed the "Corporate Ethics," the "Code of Conduct" and the "Compliance Guidelines" (a one-stop summary of matters deemed necessary for putting compliance into practice) to all executives and employees, we are working to strictly enforce compliance in practice.

Our efforts to further enhance and reinforce compliance in practice include implementing the "Compliance Program," which is a practical plan for the enriching of compliance systems and established every year by the Board of Directors, to take concrete compliance measures based on the plan, holding training sessions in each department and branch, inspecting and monitoring the compliance status by using special "Checklists," and giving advice and guidance by visiting branches.

Details of Corporate Ethics and Code of Conduct

Corporate Ethics

1. Awareness of social responsibility and public mission
2. Strict compliance with laws, regulations and rules
3. Transparent management that is open to the public
4. Confrontation with antisocial forces

Code of Conduct

1. Understand and comply with laws, regulations and rules
2. Maintain and improve credibility
3. Report, contact and consult
4. Distinguish between business and personal affairs
5. Deal with customers in good faith
6. Take a resolute stance against antisocial forces
7. Strictly manage customer information
8. Prevent money laundering

Customer Protection Efforts

We have published the "Policy for Managing Customer Protection, etc." as our policy for improving customer protection and convenience. Additionally, in an effort to improve and establish our management systems, we have appointed persons at each department and branch to make sure that thorough explanations are given to customers and that inquiries, requests, complaints, etc., from customers are appropriately handled.

The Bank has concluded an agreement concerning complaint handling and dispute resolution procedures with the Japanese Bankers Association, a certified alternative dispute resolution body under the Banking Act. The Japanese Bankers Association, from a fair and neutral standpoint, takes initiatives to resolve complaints filed and requests for dispute resolutions received from customers regarding bank operations.

Managing Information on Customers

With respect to personal information, we have published the "Privacy Policy" as our policy for efforts to properly protect and use personal information. We have also appointed officers, etc., responsible for managing and overseeing customer information including personal information in the entire Bank, to seek to strictly enforce security management measures, and to develop and establish management frameworks including those for the supervision of contractors.

Policy for Managing Customer Protection

The Bank will make the following efforts in good faith, and endeavor to ensure business operations from the viewpoint of customers in order to protect customers and improve convenience.

In this Policy, “customers” shall refer to “people who are already performing transactions with the Bank and people who are thinking about performing transactions with the Bank in the future,” “transactions” shall refer to “lending transactions (loan agreements and associated collateral/guarantee agreements), acceptance of deposits, etc., product sale, brokering, solicitation and other transactions performed between customers and the Bank,” and “operations” shall refer to “various operations concerning transactions.”

1. The Bank will make its executives and officers gain sufficient knowledge of operations and provide appropriate and sufficient information to customers. The Bank will also provide a proper and adequate explanation of transactions or products according to laws and regulations, etc.
2. The Bank will properly deal with inquiries, comments, etc. from customers in a sincere manner, and will examine the approach of operations and make improvements from the viewpoint of customers in order to satisfy customers.

In addition, the Bank will properly deal with disputes arising from our customers.

3. The Bank will properly obtain information on customers in compliance with laws and regulations, etc., and will properly manage such information by taking measures to prevent unauthorized access, information leakage, etc.
4. If the Bank outsources its operations, the Bank will select a contractor with the ability to execute such operations with precision so that information on customers will be protected and customers will be treated properly, and will properly manage outsourced operations by such means as conducting monitoring periodically or whenever necessary.
5. The Bank will appropriately manage customer transactions and prevent unfair impairment of customer interests by such means as identifying in advance transactions that may result in a conflict of interests between the Bank and its customers or among the customers of the Bank, and establishing and implementing a management method.
6. In addition to the above, the Bank will properly manage operations deemed necessary for the purpose of protecting customers and improving convenience.

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Compliance System