Nonperforming Loans

The Bank continually ensures the soundness of its assets by applying a three-step process to credit, mainly loans extended to various customers. The three steps are (1) assignment of internal ratings, (2) self-assessments and (3) write-offs and reserve provisions.

Framework for Ensuring Asset Soundness

(1) Assignment of Internal Ratings

The Bank assigns an internal rating to each debtor based on comprehensive qualitative and quantitative analysis of the debtor's condition. As part of the assessment process, internal ratings are reviewed "periodically" based on disclosed financial data and reviewed "as needed" in consideration of a change in the status of a debtor's creditworthiness.

Internal ratings are a core tool for daily credit management, including serving as the basis for the establishment of lending frameworks such as spread guidelines and a variety of credit ceilings.

Additionally, by continually compiling statistics on defaults among groups within the same internal rating, the Bank is able to calculate average default probabilities for each rating and use this as the base coefficient for quantifying credit risk.

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7</td><td>Standard debtors</td><td>Category I</td><td>Provisions to the general reserve for possible loan losses based on projected loss amount, calculated as credit exposure multiplied by the historical loss ratio.</td><td rowspan="2">General Reserve for Possible Loan Losses</td></tr>
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8-3</td><td>Substandard debtors
• Other substandard debtors
• Debtors under requirement of control</td><td>II</td><td>Provisions to the general reserve for possible loan losses based on the projected loss amount, calculated as credit exposure multiplied by the historical loss ratio for each group, which are categorized according to creditworthiness.

Substandard group further segmented into "other substandard debtors" and "debtors under requirement of control," with provisions based on the discounted cash flow (DCF) method for large loans to debtors, with additional consideration given to the financial condition and credit status of the latter subcategory.</td></tr>
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<tr><td>10-1</td><td>Debtors in default</td><td rowspan="2">For Category IV loans (portions determined to have zero value and/or be irrecoverable), the entire amount is basically removed from the balance sheet through direct write-offs, even if there are no related tax benefits. For Category III loans, provisions to the specific reserve for possible loan losses are made to cover the entire amount.</td></tr>
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(2) Self-Assessments

Self-assessments are conducted twice per year, in June and December. Also, necessary adjustments are made in March and September.

The self-assessment process first involves categorizing debtors based on their internal ratings. There are five categories: standard debtors, substandard debtors, doubtful debtors, debtors in default and debtors in bankruptcy. Next, individual loans are ranked in one of four categories in accordance with the risk of recovery and the danger of impairment.

(3) Write-Offs and Reserve Provisions

Write-offs and reserve provisions are made in accordance with the standards for each debtor category.

For claims on standard debtors and claims on substandard debtors, the Bank provisions the general reserve for possible loan losses based on the projected loss rate, which is determined from historical data for losses, including defaults, for each group. For some large loans to debtors under requirement of control, reserves are provisioned using the discounted cash flow (DCF) method. For claims on doubtful debtors and below, reserves are provisioned for respective loans based on the calculation of the necessary amount within Category III loans that are not guaranteed or collateralized.

Loan Disposal

Credit costs totaled ¥11 billion (US$104 million) in fiscal 2004, down approximately ¥40 billion from the previous fiscal year. Improvement in business conditions and repayments reduced the balances of claims on substandard debtors and claims on doubtful debtors, leading to a sharp decline in provisions to the general reserve for possible loan losses and the specific reserve for possible loan losses. Consequently, total reserves for possible loan losses were ¥314 billion (US$2,932 million).

The Bank is also proactively moving nonperforming loans off the balance sheet. In fiscal 2004, ¥218 billion (US$2,032 million) in such loans was taken off the balance sheet through sales and recovery. Meanwhile, the application of stricter standards in the determination of debtor categories added ¥102 billion (US$957 million) to the categories of doubtful debtors and below.

Debtor Classification

Standard debtors	Debtors with no particular financial or operating problems
Substandard debtors	Debtors that require close monitoring
Doubtful debtors	Debtors highly likely to fall into bankruptcy
Debtors in default	Debtors bankrupt in effect but not legally or formally
Debtors in bankruptcy	Debtors that are legally and formally bankrupt

Asset Categories

Category I	Assets with no problem being recovered
Category II	Assets at a higher-than-normal danger of not being recovered
Category III	Assets with significant concern about recovery and a high possibility of losses but viewed as a problem asset in terms of the rationally estimated loss amount
Category IV	Assets determined to be unrecoverable or have zero value

Credit Costs in Fiscal 2004 (On a Non-Consolidated Basis)

	Millions of Yen	Millions of U.S. Dollars
Loan write-offs	¥ 785	$ 7
Provisions to specific reserve for possible loan losses	3,163	29
Provisions to general reserve for possible loan losses	(16,184)	(151)
Provisions to reserve for specified overseas debts	(63)	(0)
Other	23,561	219
Total credit costs	¥11,263	$104

Disclosure of Nonperforming Loans

(1) Risk-Managed Loans

Risk-managed loans fall into one of four categories: (a) loans with principal or interest payments more than three months in arrears; (b) restructured loans (loans for which the terms and conditions of the original loan agreement are redrawn in the favor of the borrower, including reducing interest rates to support or help rehabilitate the debtor); (c) loans with principal or interest payments more than six months in arrears; and (d) loans to borrowers under bankruptcy proceedings.

As of March 31, 2005, risk-managed loans totaled ¥473 billion (US$4,414 million), or 3.02% of total loans outstanding. Compared with the previous fiscal year, total risk-managed loans declined ¥159 billion, with loans to borrowers under bankruptcy proceedings falling ¥2 billion, loans with principal and interest payments in arrears dropping ¥113 billion and restructured loans declining ¥43 billion.

Loans to overseas borrowers accounted for 2% of risk-managed loans, with ¥584 million (US$5 million) in Europe and ¥7 billion (US$65 million) in the United States.

(2) Disclosed Claims by the Financial Revitalization Law (Reference)

Under Article 6 of the Law Concerning Emergency Measures for Early Stabilization of Financial Functions (Law No. 132, 1998), banks are required to disclose nonperforming loans as follows: (a) claims on obligors under close observation (claims in this category basically include loans with principal or interest payments more than three months in arrears and restructured loans); (b) claims on obligors with bankruptcy imminent (claims on obligors who are not yet bankrupt but whose financial position and management performance are deteriorating) (it is highly likely that the principal and interest will become uncollectible); and (c) claims on obligors under legal bankruptcy proceedings and obligors substantially in bankruptcy (claims on obligors who are bankrupt or in the process of bankruptcy, reorganization or similar financial restructuring procedures as well as those in a similar condition).

Claims on obligors under legal bankruptcy proceedings and obligors substantially in bankruptcy totaled ¥7 billion (US$66 million); claims on obligors with bankruptcy imminent amounted to ¥245 billion (US$2,284 million); and claims on obligors under close observation totaled ¥231 billion (US$2,157 million), making a total of ¥483 billion (US$4,507 million), down ¥159 billion from the the previous fiscal year. The total coverage ratio for disclosed claims by the Financial Revitalization Law was 75.0% (calculated as the coverage amount, which is collateral, and guarantees plus the specific reserve for total loan losses plus the portion of the general reserve for possible loan losses attributable to claims on debtors under requirement of control divided by the total amount of disclosed claims).

Policy for Future Activities

The Bank will continue to apply its credit management processes—namely, assigning internal ratings, conducting self-assessments of assets and making write-offs and reserve provisions—in a timely and thoroughgoing manner. In cases where the Bank determines that rehabilitation of a debtor would be difficult even with the support of financial institutions and assistance in self-supporting efforts on the part of borrowers, the Bank will carry out final disposals by selling claims to the Resolution and Collection Corporation (RCC) and in the market.

The "Program for Financial Revival," unveiled in October 2002, is a road map for the stabilization of Japan's financial system, and it calls for the major banks to reduce their nonperforming loan ratios by approximately 50% by the end of fiscal 2004 through the application of stricter asset assessments. The Bank worked to reduce its nonperforming loan ratio in line with the basic policy of the financial authorities. The Bank is committed to maintaining and improving its nonperforming loan ratio through the steady disposal of nonperforming loans.

Additionally, the Bank will pursue appropriate risk management and steadily move nonperforming loans off the balance sheet. In conjunction with such actions, the Bank intends to step up its efforts to generate returns commensurate with risk by implementing more-advanced risk management methods. The Bank is also committed to sustaining the soundness of its assets as well as its profit performance.

Risk-Managed Loans (On a Non-Consolidated Basis)

As of March 31	Billions of Yen 2005	Billions of Yen 2004	Millions of U.S. Dollars 2005
Loans to Borrowers under Bankruptcy Proceedings	**¥ 1**	¥ 4	**$ 16**
Loans with Principal or Interest Payments More than Six Months in Arrears	**242**	355	**2,257**
Loans with Principal or Interest Payments More than Three Months in Arrears	**0**	0	**2**
Restructured Loans	**229**	273	**2,139**
Total	**¥473**	¥633	**$4,414**

Disclosed Claims by the Financial Revitalization Law (On a Non-Consolidated Basis)

As of March 31	Billions of Yen 2005	Billions of Yen 2004	Millions of U.S. Dollars 2005
Claims on Obligors under Legal Bankruptcy Proceedings and Obligors Substantially in Bankruptcy	**¥ 7**	¥ 6	**$ 66**
Claims on Obligors with Bankruptcy Imminent	**245**	360	**2,284**
Claims on Obligors under Close Observation	**231**	275	**2,157**
Total	**¥ 483**	¥ 642	**$ 4,507**
Claims on Ordinary Obligors	**¥15,432**	¥17,424	**$143,828**

Reserve for Possible Loan Losses (On a Non-Consolidated Basis)

As of March 31	Billions of Yen 2005	Billions of Yen 2004	Millions of U.S. Dollars 2005
General	**¥148**	¥164	**$1,385**
Specific	**165**	199	**1,541**
Reserve for Losses on Specified Overseas Debts	**0**	0	**6**
Total	**¥314**	¥365	**$2,932**