BOJ Reports & Research Papers

Financial System Report Annex Series

Financial System Report – Annex

Financial Results of Japan's Banks for Fiscal 2018

FINANCIAL SYSTEM AND BANK EXAMINATION DEPARTMENT
BANK OF JAPAN

SEPTEMBER 2019

The total of major banks, regional banks, and *shinkin* banks covered in this *Report* is as follows (as at March 31, 2019).

Major banks comprise the following 10 banks: Mizuho Bank; MUFG Bank; Sumitomo Mitsui Banking Corporation; Resona Bank; Saitama Resona Bank; Mitsubishi UFJ Trust and Banking Corporation; Mizuho Trust and Banking Company; Sumitomo Mitsui Trust Bank; Shinsei Bank; and Aozora Bank. Regional banks comprise the 64 member banks of the Regional Banks Association of Japan (Regional banks I) and the 40 member banks of the Second Association of Regional Banks (Regional banks II). *Shinkin* banks are the 251 *shinkin* banks that hold current accounts at the Bank of Japan.

Financial Institutions Divisions I and II
Financial System and Bank Examination Department, Bank of Japan
post.fsbe2@boj.or.jp

Background

The Bank of Japan issues the *Financial System Report* semi-annually with the objectives of assessing the stability of Japan's financial system from a macroprudential perspective and enhancing communication with concerned parties with respect to financial stability issues. The *Report* provides a regular and comprehensive assessment of the financial system.

The *Financial System Report Annex Series* supplements the *Financial System Report* by providing more detailed analysis and insight into a selected topic. This paper covers the financial results of Japan's banks for fiscal 2018 to provide an annual analysis.

Abstract

The characteristics of the financial results of Japan's banks for fiscal 2018 are summarized in the three paragraphs below.

First, net income decreased for all types of banks: major banks, regional banks, and *shinkin* banks. For all types of banks, net income was pushed down mainly by the continued shrinking of domestic lending margins and the upward turn in credit costs.

Second, pre-provision net revenue (PPNR) (excluding trading income), which shows core profitability, continued to follow a declining trend for all types of banks, while that for *shinkin* banks, which was at the lowest level since the bursting of the bubble economy, increased slightly. PPNR (excluding trading income) was pushed down by declines both in loan-related net interest income owing to shrinking domestic lending margins and in net non-interest income mainly due to weak sales of investment trusts. A decline in securities-related income at regional banks also pushed down their PPNR (excluding trading income).

Third, the capital adequacy ratios of financial institutions have been sufficiently above the regulatory requirements, although they have declined moderately.

Contents

I. Outline of Financial Results of Japan's Banks for Fiscal 2018[1]

A. Profits and Losses

Net income for fiscal 2018 at major financial groups was about 2.1 trillion yen, decreasing by 23.4 percent from the previous year. The factors behind the decline in net income were (1) a continued decline in net interest income owing to the shrinking domestic lending margins, (2) a decline in net non-interest income mainly due to weak sales of investment trusts and improved valuation methods of derivatives, (3) an increase in credit costs mainly caused by loan-loss provisions to domestic and overseas exposures to some large companies, and (4) an increase in realized losses on securities holdings. Meanwhile, one-time losses incurred by a financial group led to a larger decline in net income. For details regarding the income structures of major financial groups, see Box 1.

Net income for fiscal 2018 at major banks (on a non-consolidated basis) was about 1.5 trillion yen, a decrease of 30.0 percent from the previous year.

I-A-1: Main profit and loss items at major financial groups and banks

100 mil.yen,%

	Major Financial Groups			Major Banks (non-consolidated)		
	FY2018	y/y chg.	y/y % chg.	FY2018	y/y chg.	y/y % chg.
Net interest income	47,718	-588	-1.2	33,925	-399	-1.2
Net non-interest income	53,242	-1,418	-2.6	22,286	-1,820	-7.6
General and administrative expenses	-68,385	+557	-0.8	-37,227	+94	-0.3
PPNR (excluding trading income)	36,681	-489	-1.3	18,984	-2,125	-10.1
Realized gains/losses on bondholdings	-802	-705	——	-608	-486	——
Realized gains/losses on stockholdings	5,404	-225	——	3,875	-2,244	——
Credit costs	-1,703	-1,755	——	1,176	-1,764	——
(Credit cost ratio)	——	——	——	(-4bp)	(+6bp)	——
Other profit and loss items	-9,905	-6,014	——	-5,057	-1,990	——
Net income before income taxes	29,675	-9,187	-23.6	18,369	-8,608	-31.9
Tax-related expenses	-6,587	+1,883	-22.2	-3,716	+2,339	-38.6
Net income	21,334	-6,519	-23.4	14,653	-6,269	-30.0

Notes: 1. Regarding credit costs, negative numbers represent a rise in costs while positive numbers represent an increase in reversals.
2. For major financial groups, PPNR (excluding trading income) includes profits/losses on investments in affiliates. Some items for which there exist no data based on financial groups are calculated using banks' data on a non-consolidated basis.

Sources: Published accounts of each financial group; BOJ.

[1] Figures provided in Chapters I and II are calculated on a non-consolidated basis unless otherwise noted.

Net income for fiscal 2018 at regional banks was about 0.7 trillion yen, a 20.8 percent decline from the previous year. The decline in net income was attributed to (1) a continued decline in net interest income owing to shrinking domestic lending margins, (2) a decline in net non-interest income mainly due to weak sales of investment trusts, and (3) an increase in credit costs. On the other hand, the level of net income was supported by a decline in general and administrative expenses as well as a decrease in the amount by which realized losses exceeded gains on bondholdings.

Net income for fiscal 2018 at *shinkin* banks was about 0.2 trillion yen, a decrease of 12.1 percent from the previous year. This was attributed not only to a continued decline in net interest income due to shrinking lending margins but also to an increase in credit costs and a decrease in the amount by which realized gains exceeded losses on stockholdings. On the other hand, the level of net income was supported by a decline in general and administrative expenses.

I-A-2: Main profit and loss items at regional banks and *shinkin* banks

100 mil.yen,%

	Regional banks (non-consolidated)			*Shinkin* banks		
	FY2018	y/y chg.	y/y % chg.	FY2018	y/y chg.	y/y % chg.
Net interest income	36,306	-1,052	-2.8	15,374	-70	-0.5
Net non-interest income	5,104	-259	-4.8	572	-73	-11.2
General and administrative expenses	-29,268	+524	-1.8	-12,932	+248	-1.9
PPNR (excluding trading income)	12,142	-787	-6.1	3,015	+106	+3.7
Realized gains/losses on bondholdings	-313	+874	——	378	-44	——
Realized gains/losses on stockholdings	2,493	-108	——	340	-199	——
Credit costs	-3,288	-2,238	——	-483	-273	——
(Credit cost ratio)	(13bp)	(+9bp)	——	(7bp)	(+4bp)	——
Other profit and loss items	-155	+14	——	-167	-19	——
Net income before income taxes	10,880	-2,245	-17.1	3,082	-430	-12.2
Tax-related expenses	-3,702	-31	+0.8	-761	+110	-12.7
Net income	7,465	-1,957	-20.8	2,321	-319	-12.1

Note: Regarding credit costs, negative numbers represent a rise in costs while positive numbers represent an increase in reversals. From fiscal 2018, the definition of credit costs has been clarified, adding up the year-on-year change in the negative values of credit costs: a decrease of 3,000 million yen and 7,100 million yen for regional banks and *shinkin* banks, respectively.

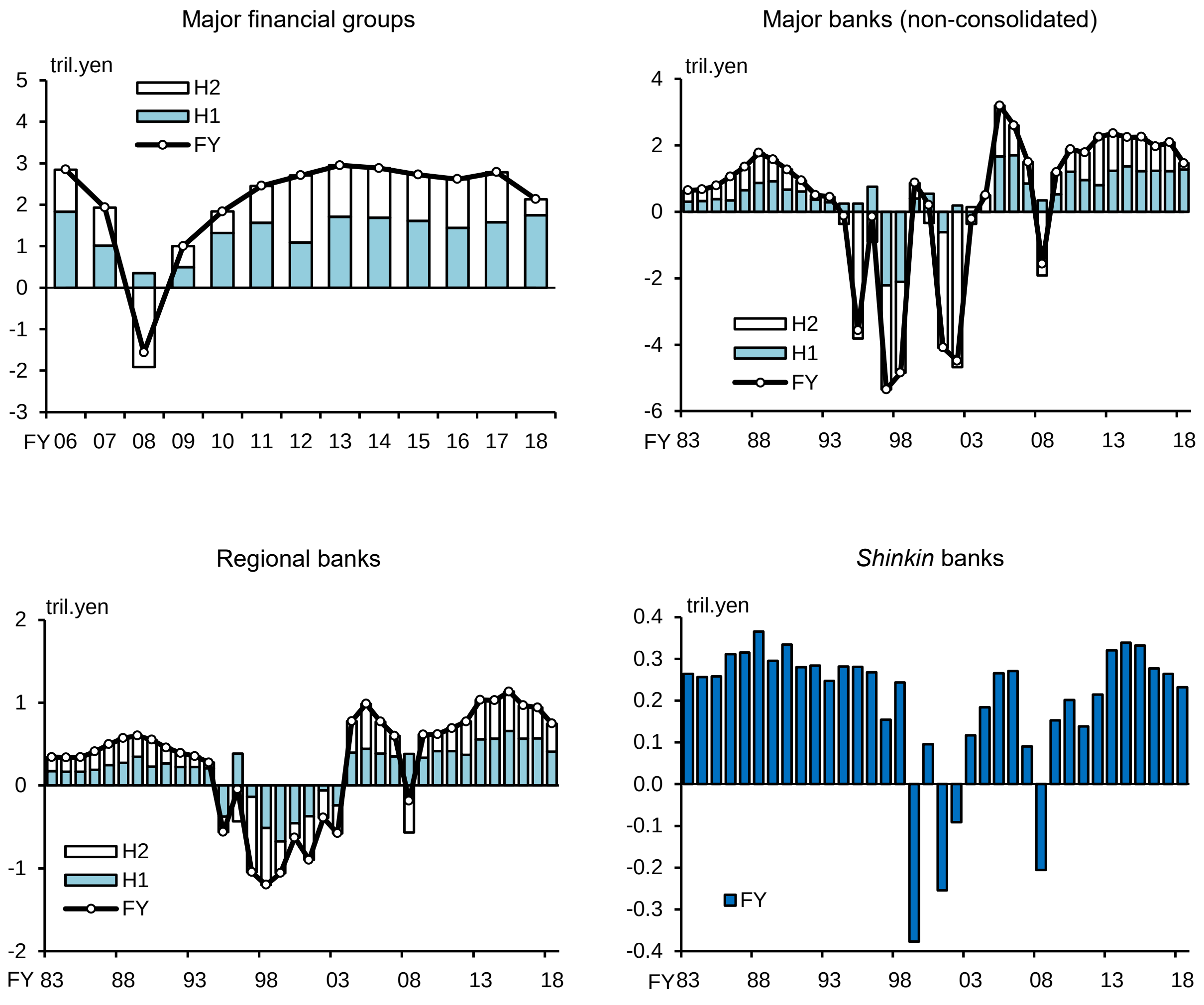
Source: BOJ.

B. Profit Levels from a Long-Term Perspective

Net income for fiscal 2018 for major banks turned down both on a consolidated and non-consolidated basis. Net income for regional banks and *shinkin* banks declined for the third and fourth consecutive year, respectively.

From a longer-term perspective, the net income levels for all types of banks bear comparison with those before the failure of Lehman Brothers and even before the bursting of Japan's bubble economy in the early 1990s.

I-B-1: Net income

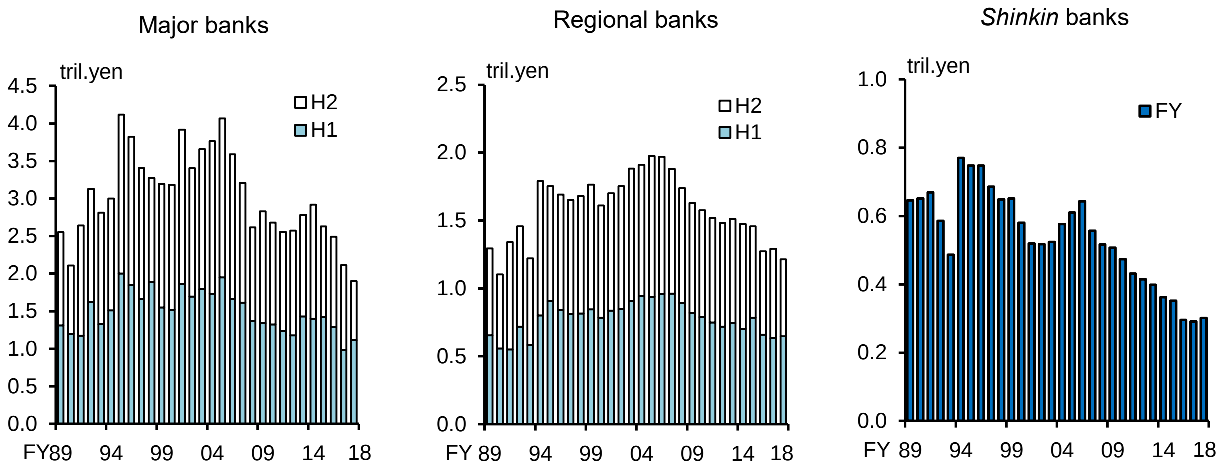


Source: BOJ.

With regard to core profitability, PPNR (excluding trading income) at major banks for fiscal 2018 marked a decline of 10.1 percent, decreasing for the fourth consecutive year, and registered only around 70 percent of the level seen four years ago. At regional banks, PPNR (excluding trading income) showed a decrease of 6.1 percent from the previous year, turning down again. At *shinkin* banks, such profits marked a small increase of 3.7 percent from the previous year.

From a longer-term perspective, amid the continued decline in domestic net interest income, the levels of PPNR (excluding trading income) for all types of banks remain on a downward trend and are at their lowest level since the bursting of the bubble economy.

I-B-2: PPNR (excluding trading income)



Source: BOJ.

C. Balance Sheets

Looking at developments in balance sheets for fiscal 2018 at major banks, total assets increased by 24.9 trillion yen as cash and due from banks, including current account balances at the Bank of Japan, loans, and foreign securities, increased. On the liability side, the main increase was in deposits.

I-C-1: Main balance sheet items of major banks

tril.yen

	End-Mar. 2019	y/y chg.	Change from end-Sep. 2018		End-Mar. 2019	y/y chg.	Change from end-Sep. 2018
Loans and bills discounted	312.5	+8.4	+1.1	Deposits + NCD	528.4	+25.2	+15.4
Domestic business sector	213.7	+3.1	+3.3	Domestic business sector	418.6	+13.8	+9.5
International business sector	98.9	+5.3	-2.2	International business sector	109.8	+11.5	+5.9
Securities	130.4	+0.1	-2.0	Loans from BOJ	24.1	-1.9	-0.9
JGBs	44.4	-6.4	-2.9	Due to trust accounts	16.7	+0.9	+1.0
Stocks	16.0	-1.8	-1.9	Other liabilities	131.4	+1.0	-8.5
Foreign securities	49.8	+6.2	+1.6	Total liabilities	700.6	+25.2	+6.9
Cash and due from banks	202.2	+14.0	+4.9	Total net assets	34.0	-0.3	-0.6
Other assets	89.5	+2.5	+2.3	Retained earnings	12.7	+0.4	-0.2
Total assets	734.6	+24.9	+6.3	Net unrealized gains/losses on securities	5.8	-0.5	-0.4

Source: BOJ.

Total assets at regional banks increased by 7.3 trillion yen as loans as well as cash and due from banks, including current account balances at the Bank of Japan, increased while Japanese government bonds (JGBs) decreased. On the liability side, the main increase was in deposits.

I-C-2: Main balance sheet items of regional banks

tril.yen

	End-Mar. 2019	y/y chg.	Change from end-Sep. 2018		End-Mar. 2019	y/y chg.	Change from end-Sep. 2018
Loans and bills discounted	262.0	+8.6	+4.9	Deposits + NCD	345.5	+4.9	+2.8
Securities	79.9	-5.7	-4.9	Current deposits	187.4	+9.0	+7.4
JGBs	19.2	-5.7	-3.7	Other liabilities	35.8	+2.4	-0.1
Cash and due from banks	49.9	+4.1	+3.0	Total liabilities	381.4	+7.3	+2.6
Other assets	12.1	+0.3	-0.6	Total net assets	22.5	+0.0	-0.3
Total assets	403.9	+7.3	+2.3	Net unrealized gains/losses on securities	3.5	-0.4	-0.4

Source: BOJ.

With regard to *shinkin* banks, total assets increased by 3.0 trillion yen as cash and due from banks, loans, and securities excluding JGBs increased. On the liability side, the main increase was in deposits.

I-C-3: Main balance sheet items of *shinkin* banks

tril.yen

	End-Mar. 2019	y/y chg.		End-Mar. 2019	y/y chg.
Loans and bills discounted	71.7	+1.0	Deposits + NCD	142.9	+2.5
Securities	43.1	+0.7	Current deposits	54.5	+3.2
JGBs	6.8	-0.9	Other liabilities	4.7	+0.2
Cash and due from banks	38.9	+1.2	Total liabilities	147.5	+2.7
Other assets	3.1	+0.1	Total net assets	9.2	+0.3
Total assets	156.7	+3.0	Net unrealized gains/losses on securities	0.8	+0.1

Source: BOJ.

II. Financial Results of Japan's Major Banks and Regional Banks for Fiscal 2018

This chapter analyzes banks' core profitability (net interest income, net non-interest income, and general and administrative expenses), realized and unrealized gains/losses on securities holdings, credit costs and non-performing loans, as well as capital adequacy ratios. The financial results of *shinkin* banks are analyzed in Chapter III.

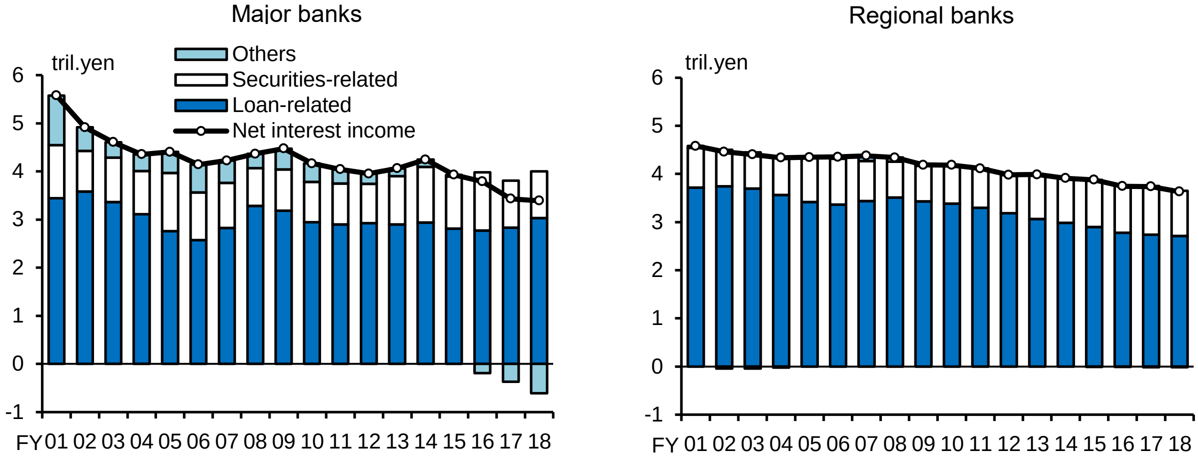
A. Core Profitability

1. Net Interest Income

Net interest income at major banks for fiscal 2018 decreased by 1.2 percent from the previous year. In the domestic business sector, securities-related income increased owing to the rise in stock dividend yields, while loan-related income continued to decrease due to narrowing interest rate spreads on loans. On the other hand, in the international business sector, loan-related income continued to increase.

Net interest income at regional banks for fiscal 2018 marked a 2.8 percent decline from the previous year. Loan-related income continued to decrease due to narrowing interest rate spreads on loans, and securities-related income also declined reflecting the redemption of JGBs with relatively high yields.

II-A-1: Net interest income



Note: Loan-related = (average loans outstanding) * (interest rate spreads on loans). Securities-related = (average outstanding securities holdings) * (interest rate spreads on securities).

Source: BOJ.

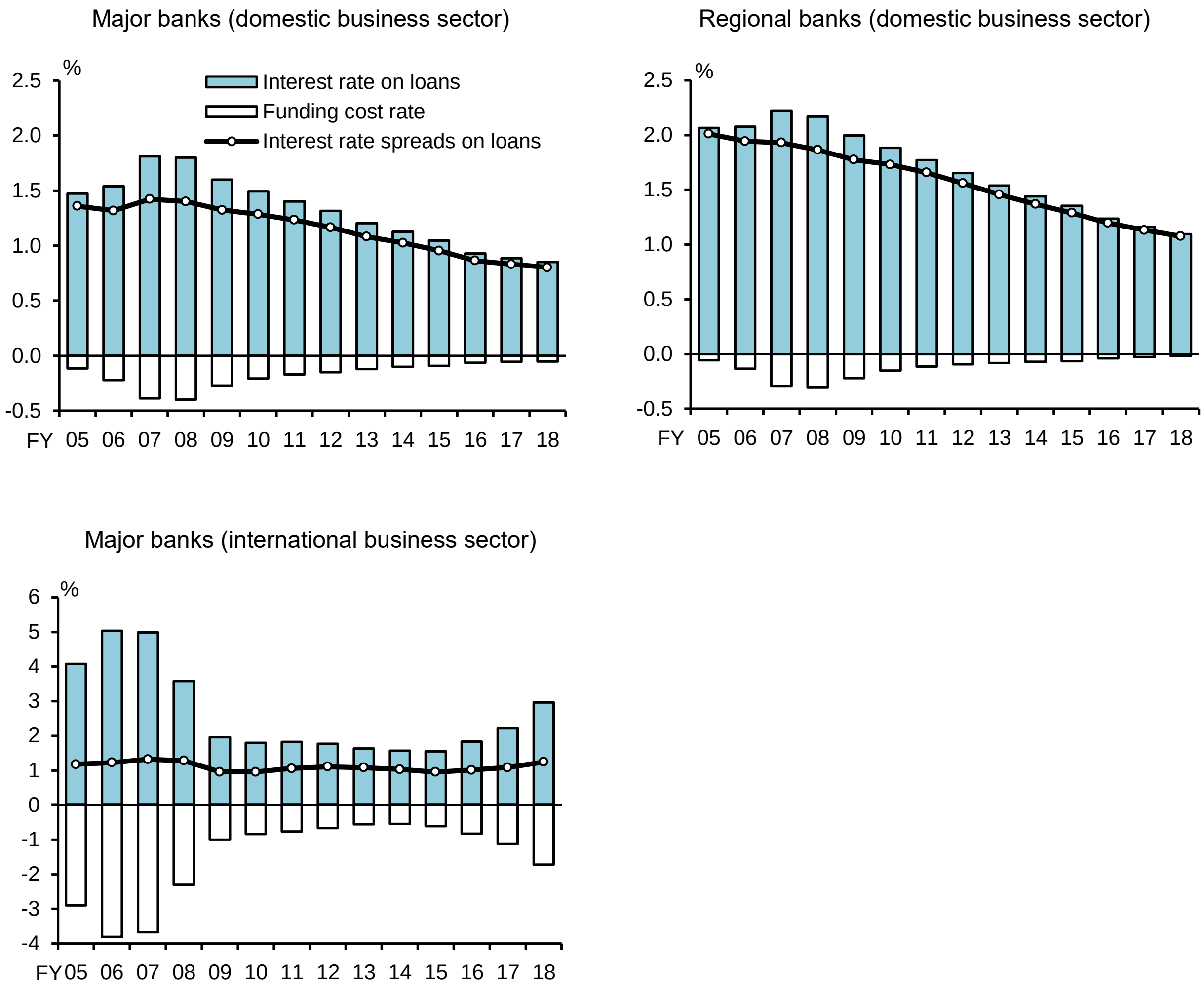
2. Interest Rate Spreads on Loans and Loans Outstanding

(1) Interest Rate Spreads on Loans

Interest rate spreads on loans in the domestic business sector continued to narrow at both major banks and regional banks as the decline in interest rates on loans exceeded the decline in funding rates under the prolonged low interest rate environment.

Interest rate spreads on loans in the international business sector at major banks were more or less unchanged as both interest rates on loans and funding increased, reflecting policy rate hikes in the United States.

II-A-2: Interest rate spreads on loans

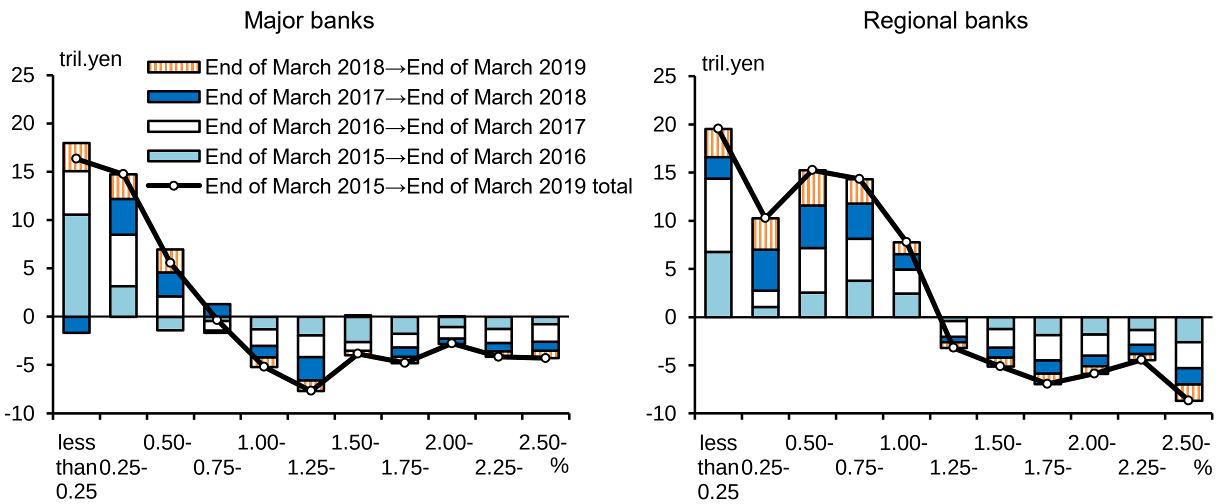


Note: In calculating the interest rate spreads, interest expenses on interest rate swaps are deducted from funding costs.
Source: BOJ.

(2) Loans Outstanding by Lending Rate

Looking at developments in loans outstanding by lending rate (yen loans in domestic branches) at both major banks and regional banks, those with low lending rates continued to increase.

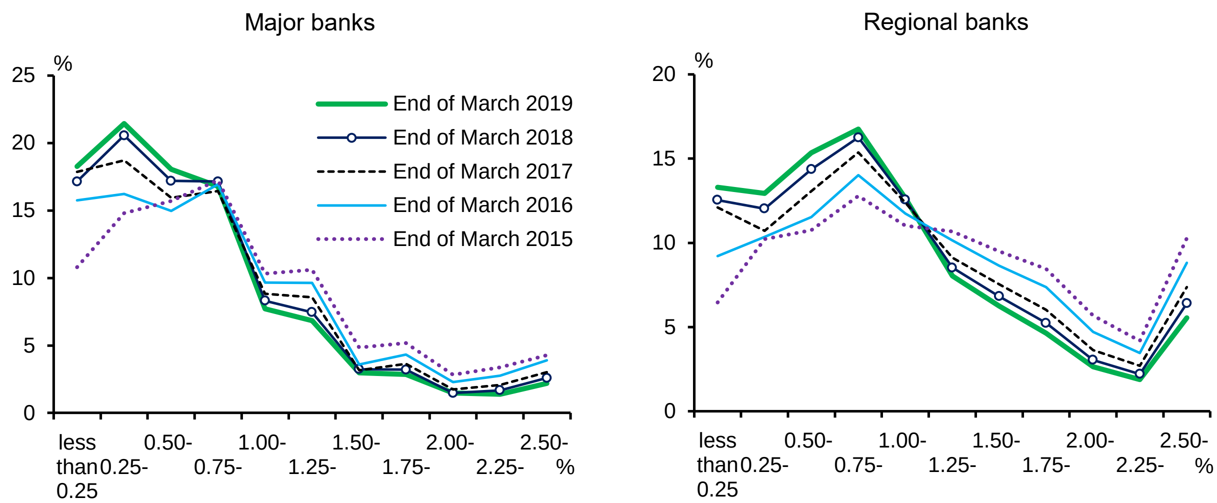
II-A-3: Changes in loans outstanding by lending rate (from the end of March 2015 to the end of March 2019)



Note: The data are for yen loans outstanding in the domestic business sector (excluding loans to the financial sector) based on the amount outstanding at month-end.

Source: BOJ.

II-A-4: Changes in proportion of loans outstanding by lending rate (from the end of March 2015 to the end of March 2019)



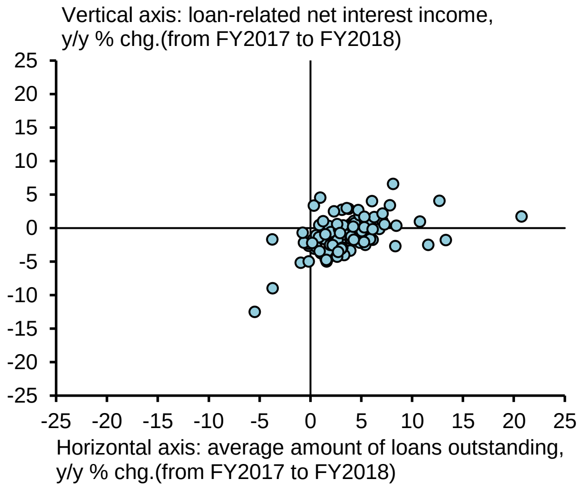
Note: The data are for yen loans outstanding in the domestic business sector (excluding loans to the financial sector) based on the amount outstanding at month-end.

Source: BOJ.

(3) Factors behind Changes in Loan-Related Net Interest Income (Loan Outstanding and Interest Rate Spread)

Looking at the changes in net interest income from domestic lending activities (= loans outstanding * interest rate spreads on loans) over the last year, most banks faced a decrease in net income, although their loans outstanding increased. This suggests that a narrowing of interest rate spreads on loans is continuing to push down net income.

II-A-5: Relationship between changes in loans outstanding and loan-related net interest income (major and regional banks, domestic business sector)



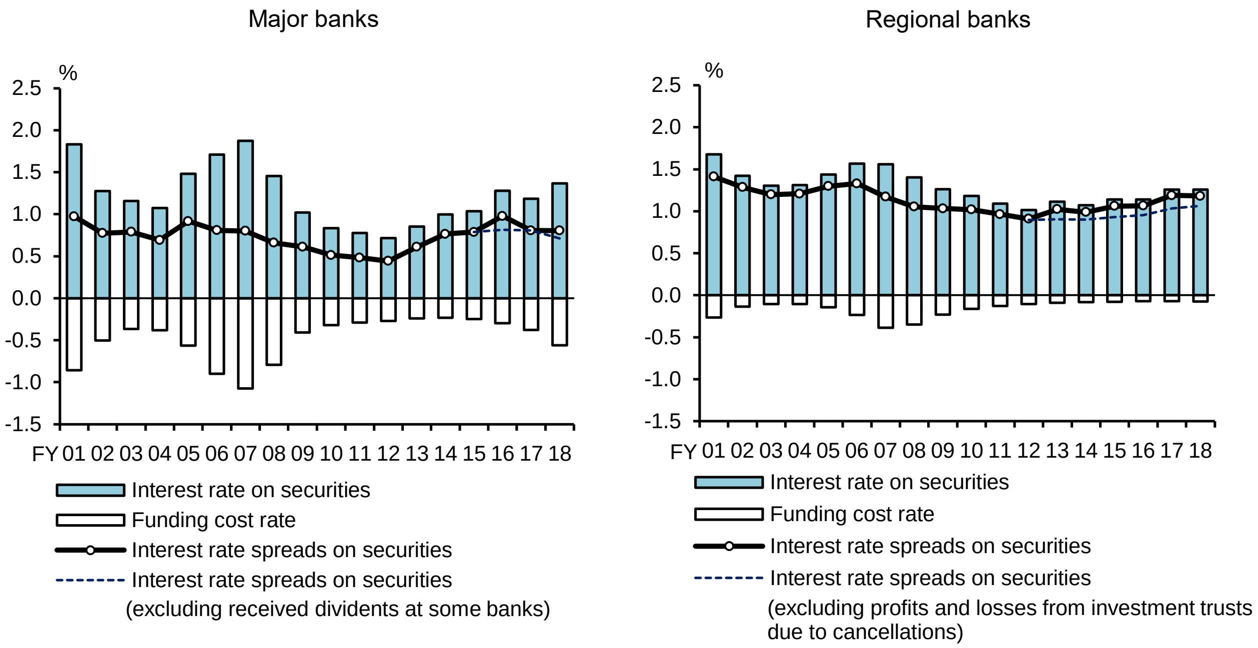
Notes: 1. The data for loans outstanding do not include foreign currency-denominated impact loans.
2. Loan-related net interest income = (average amount of loans outstanding) * (interest rate spreads on loans).
3. Some banks with special factors, such as mergers and acquisitions, are excluded.

Source: BOJ.

3. Interest Rate Spreads on Securities

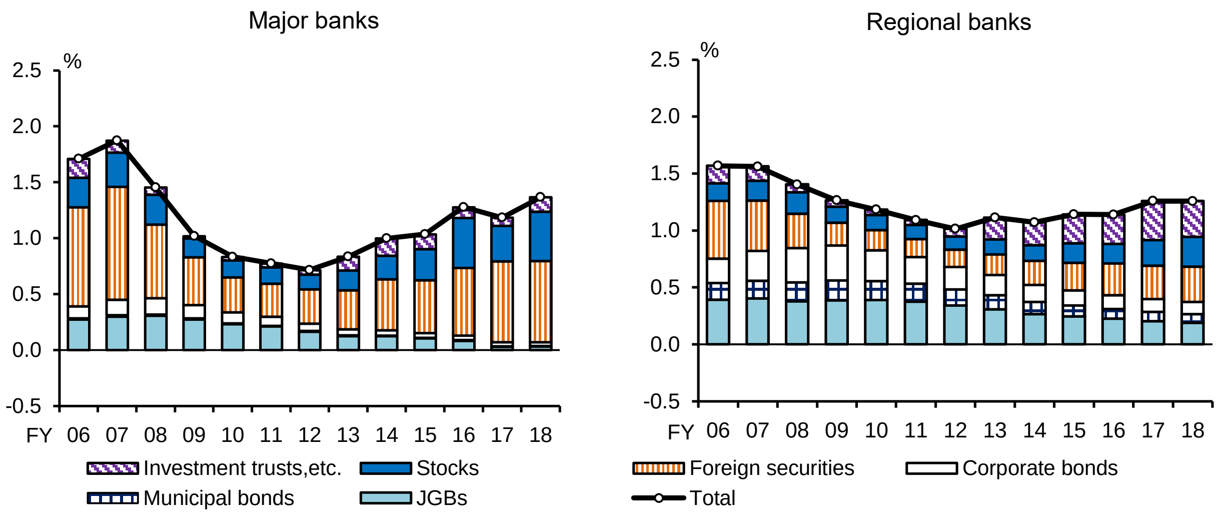
Interest rate spreads on securities were more or less unchanged on the whole at major banks as stock yields rose on the back of favorable corporate results, while foreign-currency funding rates increased. Such spreads on securities at regional banks were also more or less unchanged.

II-A-6: Interest rate spreads on securities



Note: In calculating the interest rate spreads, interest expenses on interest rate swaps are deducted from funding costs.
Source: BOJ.

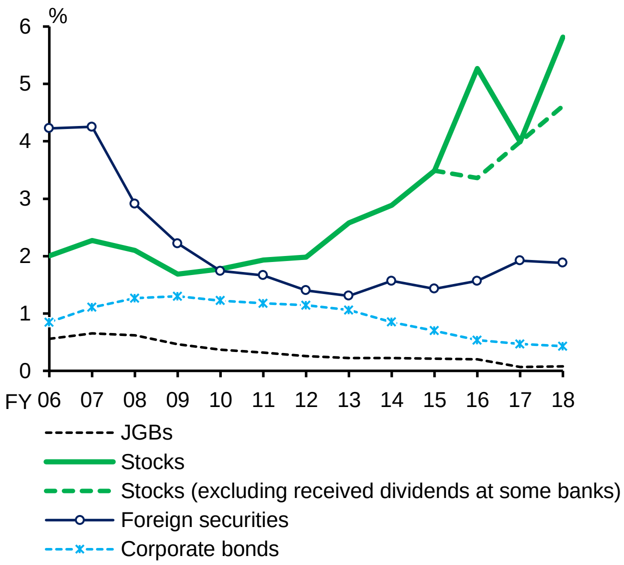
II-A-7: Decomposition of interest rate spreads on securities by product type

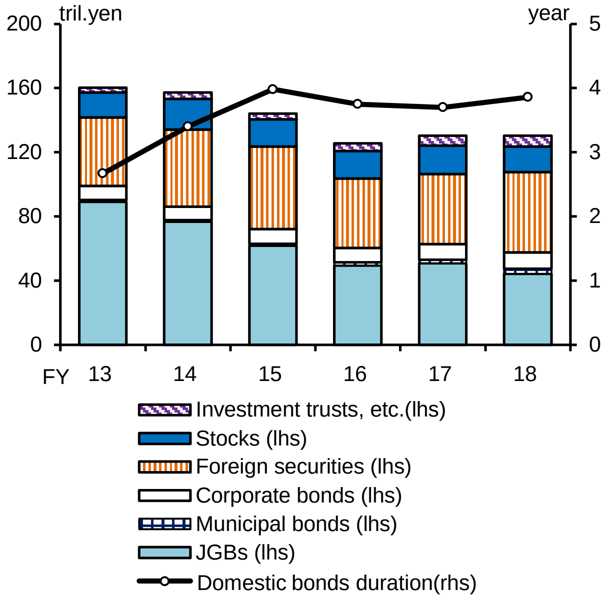


Notes: 1. Some banks are excluded due to a lack of time-series data.
2. For major banks, the rises in interest rate spreads on stocks in fiscal 2016 and 2018 reflect received dividends from subsidiaries at some banks.
Source: BOJ.

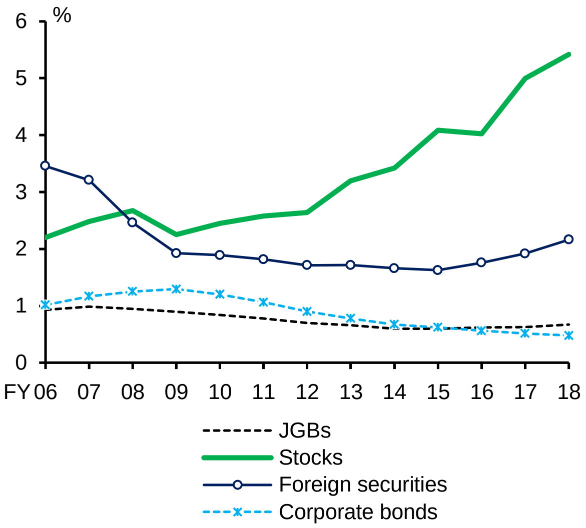
II-A-8: Interest rates on securities holdings and amounts outstanding by product type (at month-end)

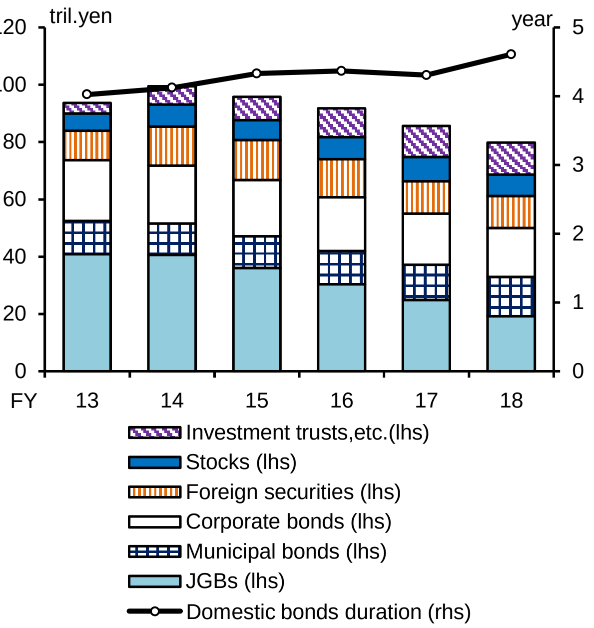
Major banks





Regional banks



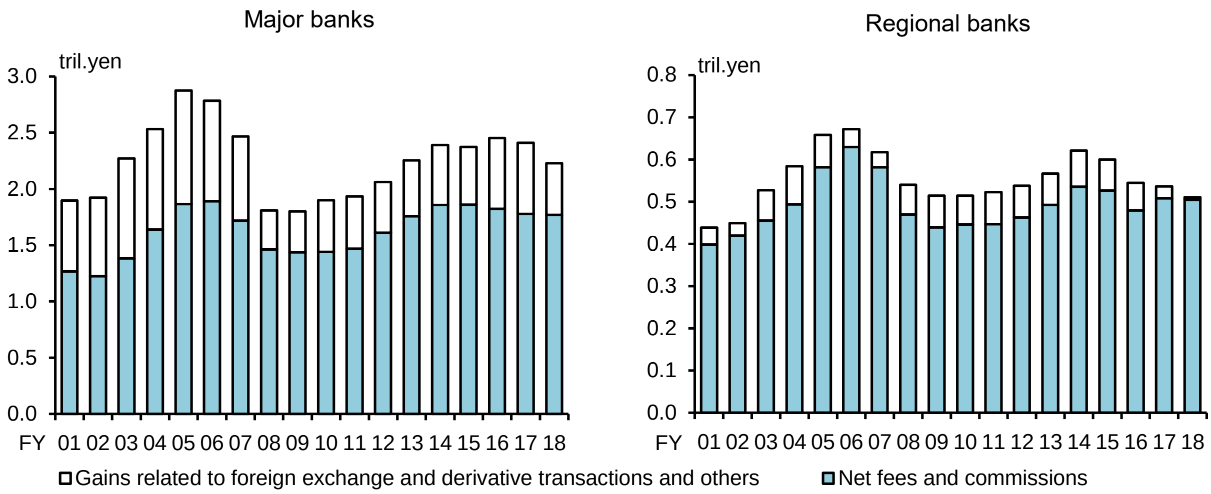


Note: In calculating interest rates, some banks are excluded due to a lack of time-series data.
Source: BOJ.

4. Net Non-Interest Income

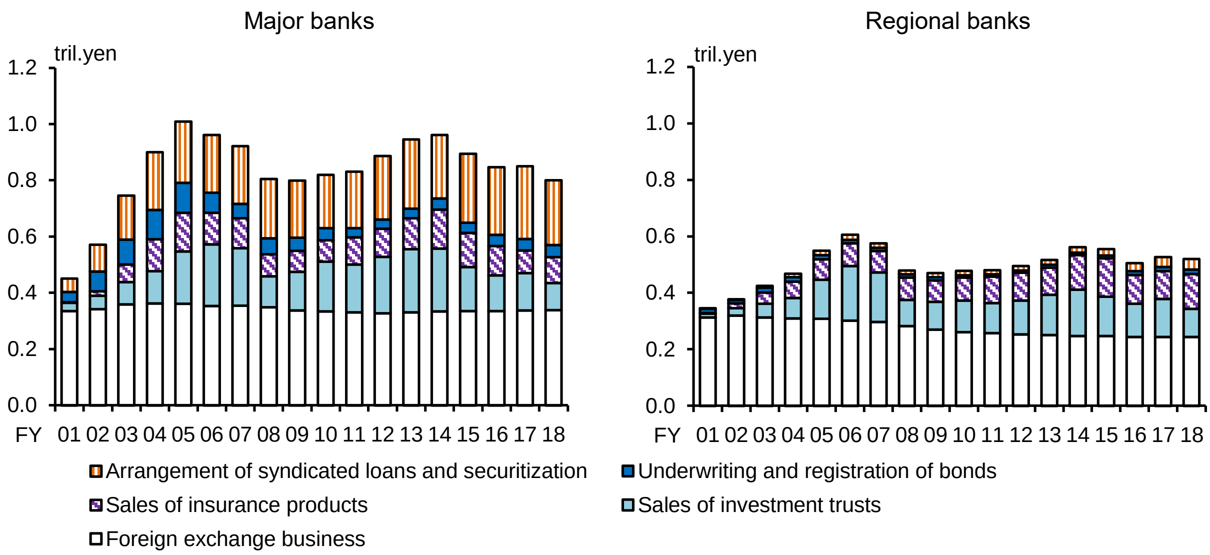
Net non-interest income decreased by 7.6 percent from the previous year at major banks. Specifically, gains related to foreign exchange and derivative transactions decreased mainly due to improved valuation methods of derivatives, while income from fees and commissions was more or less unchanged as the international business sector saw an increase in income from fees and commissions associated with deposits and lending, while the domestic business sector saw weak sales of investment trusts. Net non-interest income at regional banks decreased by 4.8 percent from the previous year, due to declines both in income from fees and commissions and in gains related to foreign exchange and derivative transactions.

II-A-9: Net non-interest income



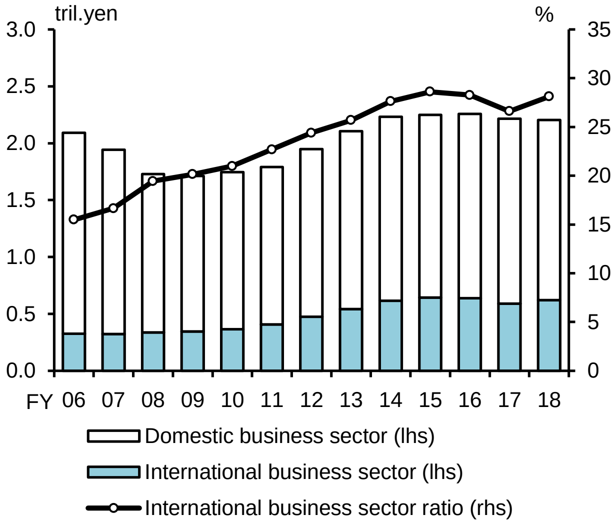
Source: BOJ.

II-A-10: Income from fees and commissions (domestic business sector)



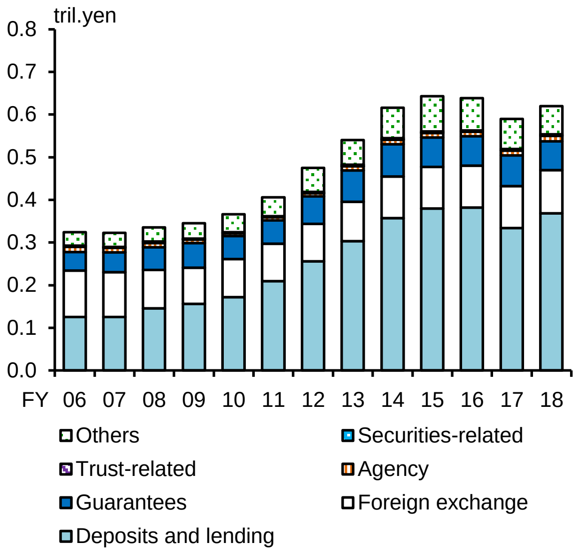
Note: Among items of income from fees and commissions, the 5 items listed above are counted.
Source: BOJ.

II-A-11: Income from fees and commissions at major banks (by domestic and international business sector)



Source: BOJ.

II-A-12: Income from fees and commissions in the international business sector at major banks



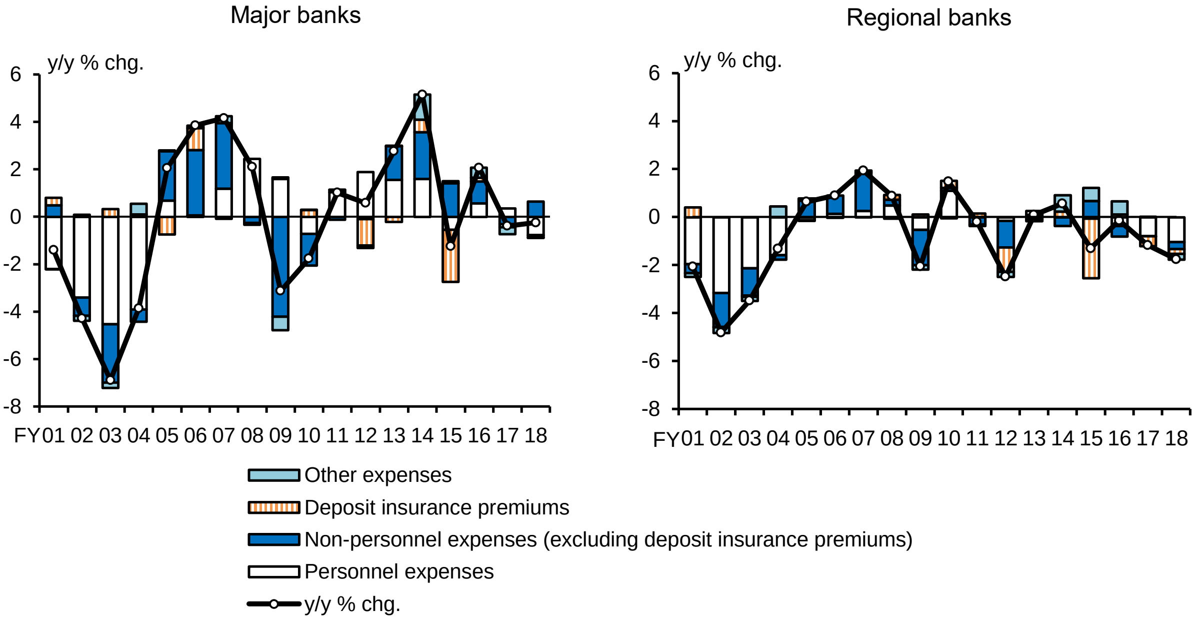
Note: The figures are categorized based on each bank's internal definition. "Deposits and lending" includes income from fees and commissions related to the arrangement of syndicated loans, commitment lines, securitization, and M&A transactions.

Source: BOJ.

5. General and Administrative Expenses

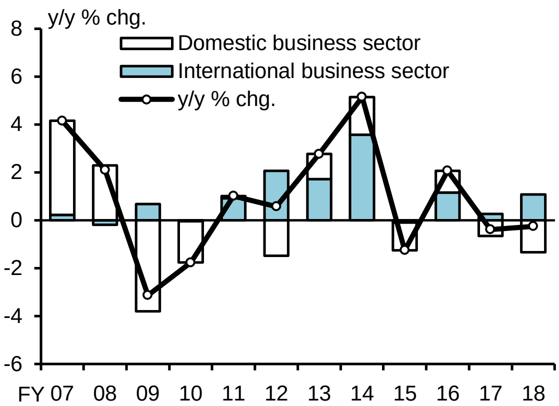
General and administrative expenses at major banks were more or less unchanged, marking a decline of 0.3 percent from the previous year; they decreased in the domestic business sector, while increasing in the international business sector. At regional banks, general and administrative expenses decreased by 1.8 percent from the previous year due to a decline in personnel expenses. While gross operating profits decreased at both major and regional banks, the overhead cost ratio (= overhead costs / gross operating profits) at major banks continued to increase due to their overhead costs remaining unchanged, and such ratio at regional banks was unchanged as their overhead costs decreased.

II-A-13: Decomposition of general and administrative expenses



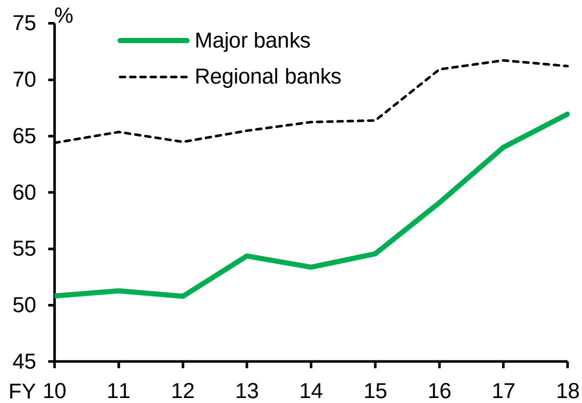
Source: BOJ.

II-A-14: Decomposition of changes in general and administrative expenses by domestic and international business sector at major banks



Source: BOJ.

II-A-15: Overhead cost ratios



Note: Overhead cost ratios = overhead costs / gross operating profits.

Source: BOJ.

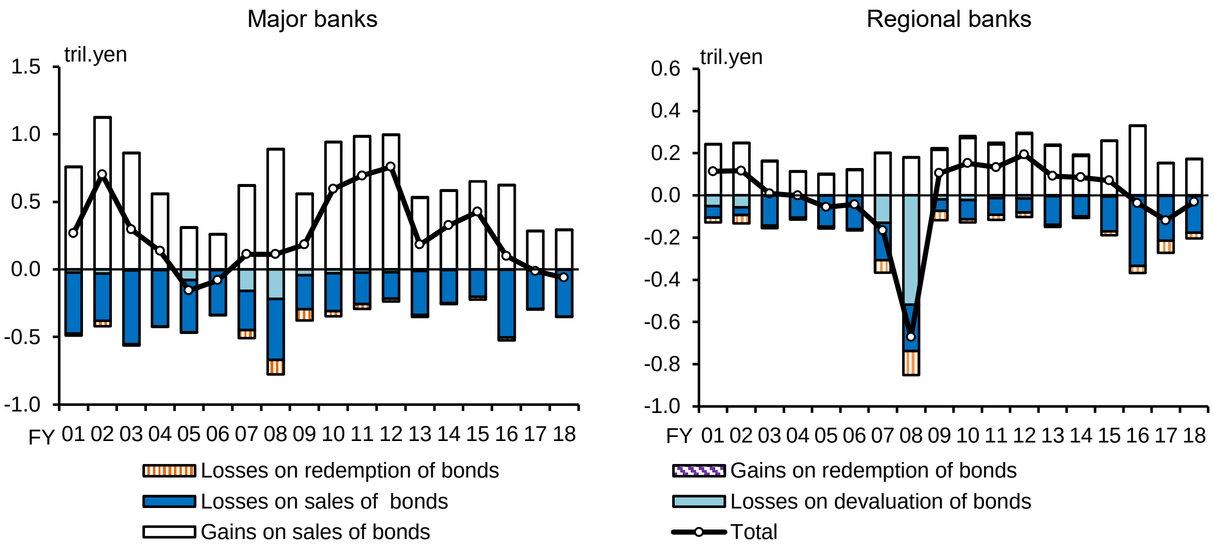
B. Realized and Unrealized Gains/Losses on Securities Holdings

1. Realized Gains/Losses on Securities Holdings

With regard to realized gains/losses on bondholdings, the extent to which such losses exceeded gains expanded at major banks due to further losses from sales of foreign securities, including loss-cutting sales to enhance the soundness of their portfolios. Realized losses continued to exceed gains at regional banks, but to a lesser extent.

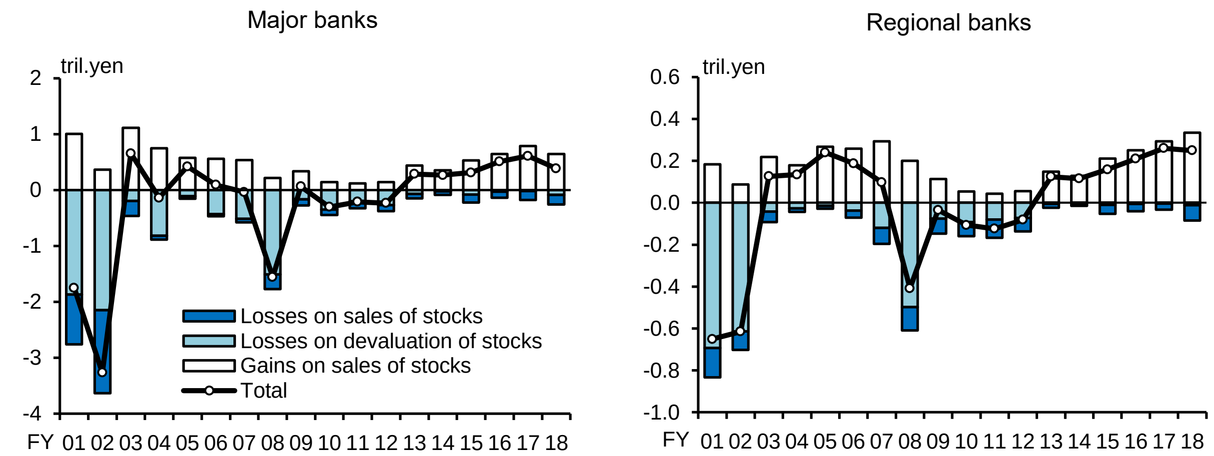
As for realized gains/losses on stockholdings, the extent to which such gains exceeded losses turned down at both major banks and regional banks due in part to the stock price decline at the end of 2018, despite the continued reduction in strategic holdings and the sales of ETFs to realize gains.

II-B-1: Realized gains/losses on bondholdings



Source: BOJ.

II-B-2: Realized gains/losses on stockholdings

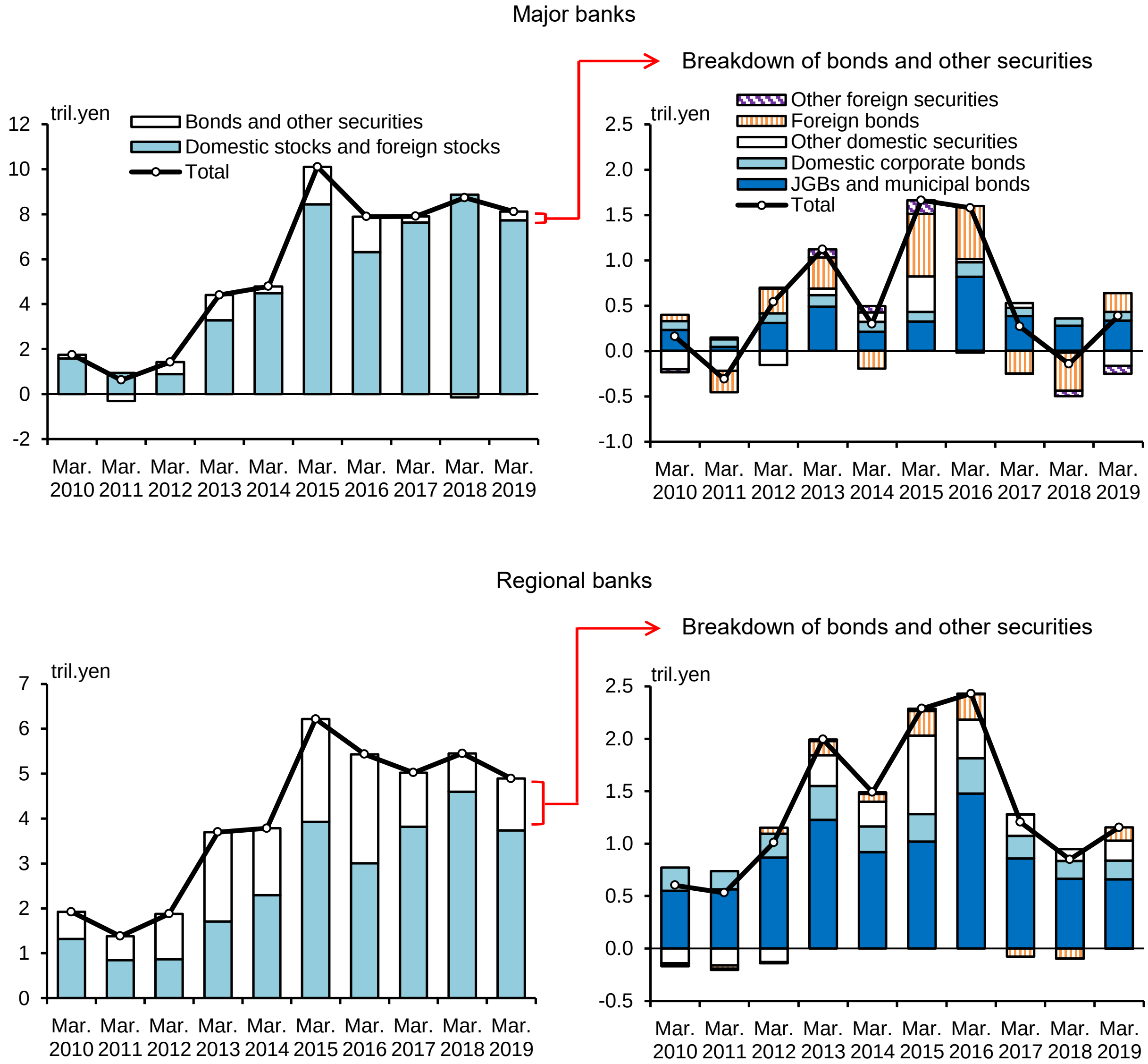


Source: BOJ.

2. Unrealized Gains/Losses on Securities Holdings

Looking at unrealized gains/losses on available-for-sale securities holdings as of the end of March 2019, the extent to which unrealized gains exceeded losses remained high both at major and regional banks, but decreased from the end of March 2018 to about 8 trillion yen at major banks and about 5 trillion yen at regional banks. Looking more closely at the breakdown, the extent to which unrealized gains in stockholdings exceeded losses, which accounts for a large share of the total gains on securities holdings, decreased as the amount outstanding was reduced due to the sales of strategic shareholdings and as stock prices declined. On the other hand, unrealized gains/losses on holdings of "bonds and other securities" turned positive at major banks and the extent to which unrealized gains exceeded losses increased at regional banks. This is because unrealized gains/losses on foreign bondholdings turned positive due to a decline in long-term interest rates.

II-B-3: Unrealized gains/losses on available-for-sale securities holdings



Note: The breakdown of bonds and other securities at both major and regional banks is shown on the right. "Other domestic securities" and "other foreign securities" include investment trusts and funds.
Source: BOJ.

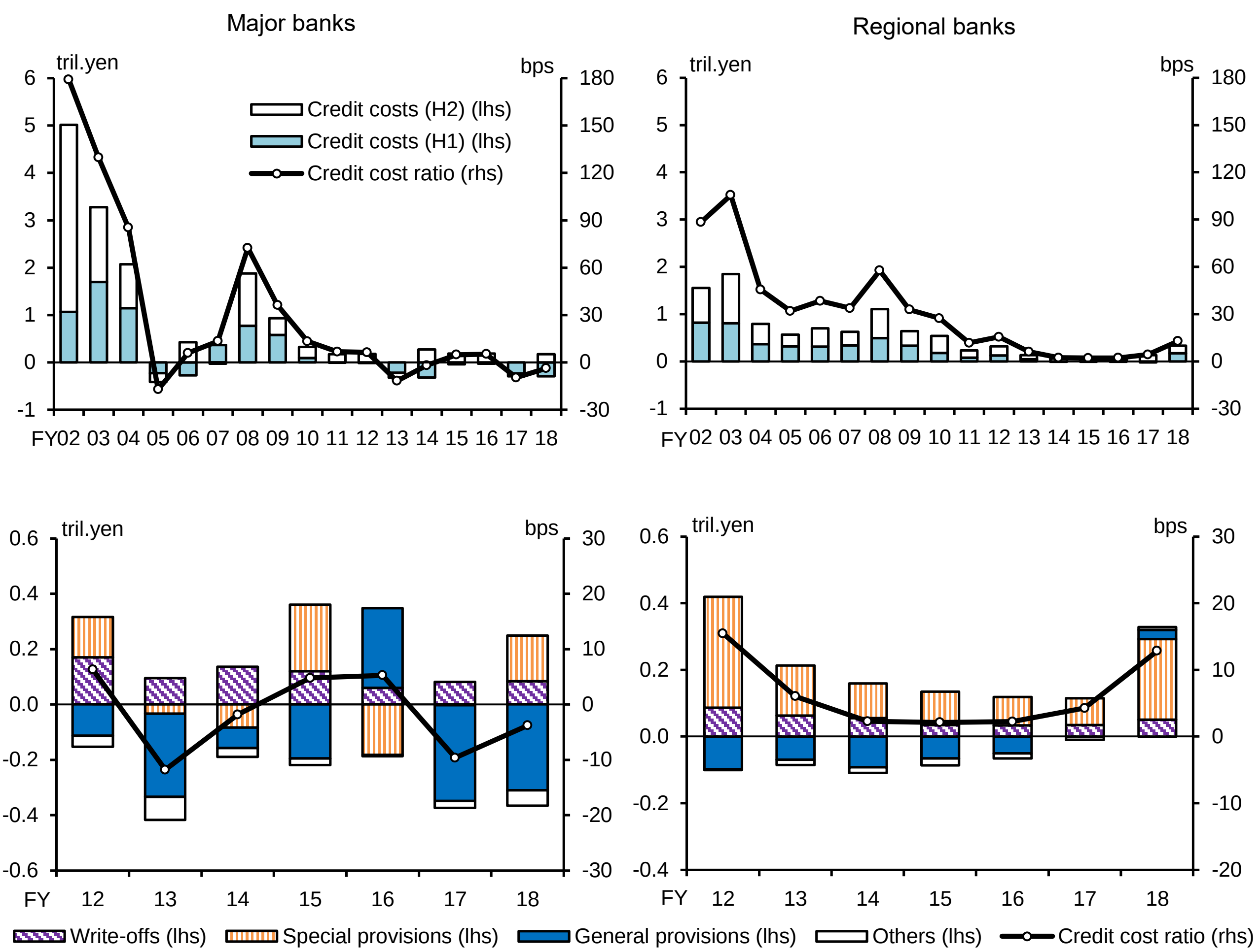
C. Credit Costs and Non-Performing Loans

1. Credit Costs

Looking at credit costs, major banks recorded smaller reversals of credit costs as there were loan-loss provisions to domestic and overseas exposures to some large companies, while there were reversals -- smaller than in the previous year -- of loan-loss provisions to certain large companies. Credit costs at regional banks increased due to high credit costs incurred by a bank and loan-loss provisions to some large companies.

The credit cost ratio (= credit costs / total loans outstanding) was minus 4 basis points (reversals) at major banks and 13 basis points at regional banks.

II-C-1: Credit costs and credit cost ratios

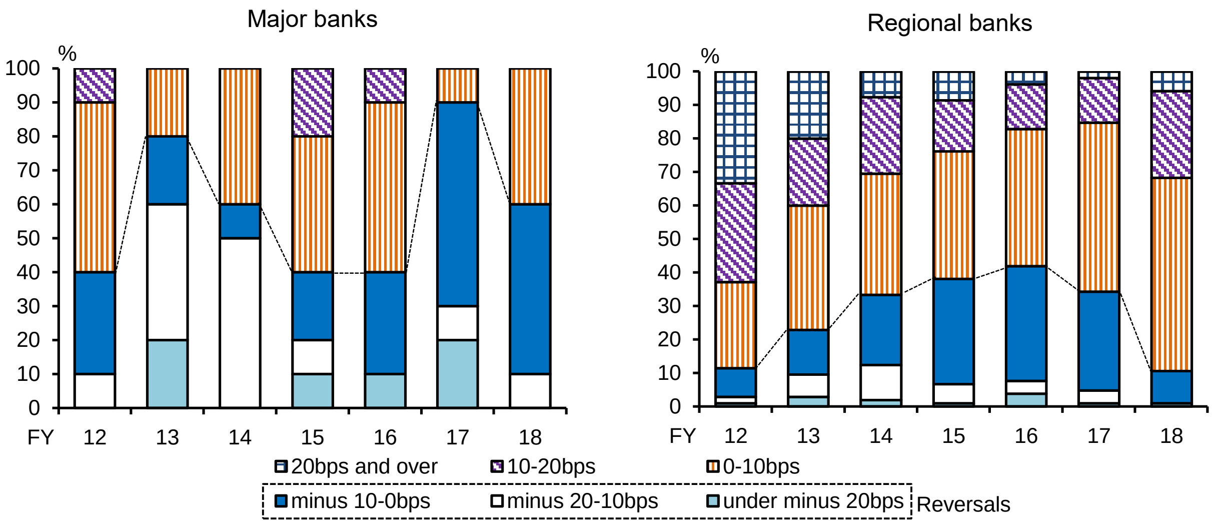


Notes: 1. From fiscal 2018, the definition of credit costs has been clarified so that the definition for regional banks has changed somewhat from fiscal 2017.
2. The lower charts show the breakdown of credit costs at major banks and regional banks, respectively.

Source: BOJ.

The distribution of credit cost ratios among banks showed that, at major banks, the share of those with credit costs reversed decreased from the previous year but remained high, accounting for 60 percent of the total, and there were no banks with credit costs 10 basis points or greater. For regional banks, the share of those with credit costs reversed decreased to 10 percent of the total, and the share of banks with credit costs 10 basis points or greater, which had continued to decrease, turned up.

II-C-2: Credit cost ratio distribution



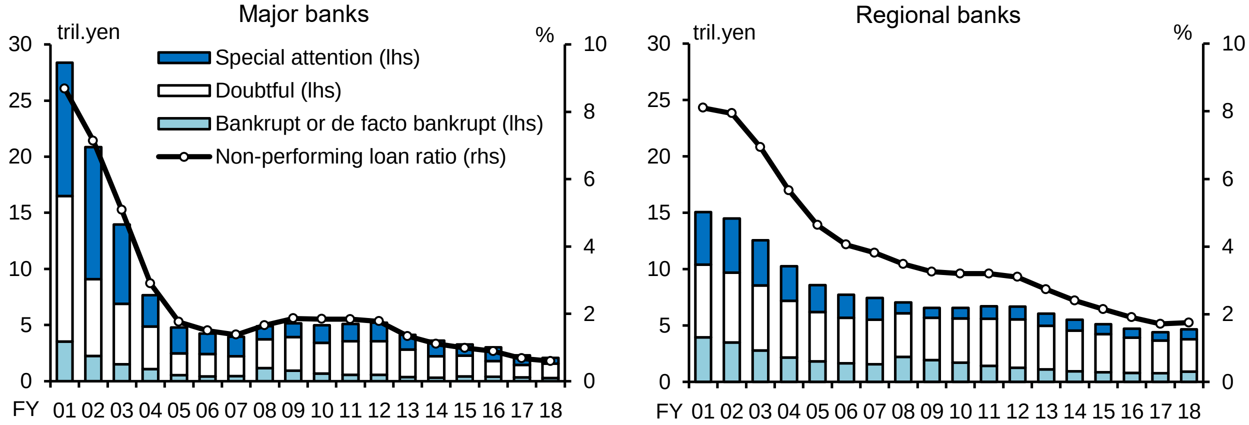
Note: Proportion of the number of banks by credit cost ratio.
Source: BOJ.

2. Non-Performing Loans

The non-performing loan (NPL) ratio at major banks continued to follow a moderate declining trend, and reached its lowest level since fiscal 2001, when the relevant data were first recorded. Meanwhile, the NPL ratios for overseas loans at the three major banks remained at low levels. The NPL ratio at regional banks remained low, but turned up slightly due to the deterioration of business conditions at some large companies.

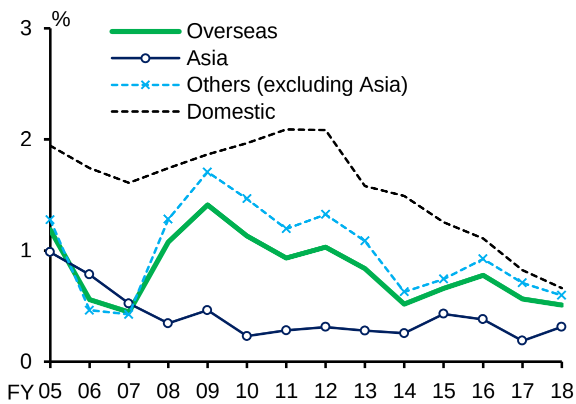
Looking at the proportion of loans outstanding by borrower classification, the ratio of normal loans at both major banks and regional banks remained high, exceeding 95 percent at major banks and marking almost 90 percent at regional banks, although the ratio at regional banks turned down slightly.

II-C-3: Non-performing loans outstanding and non-performing loan ratios



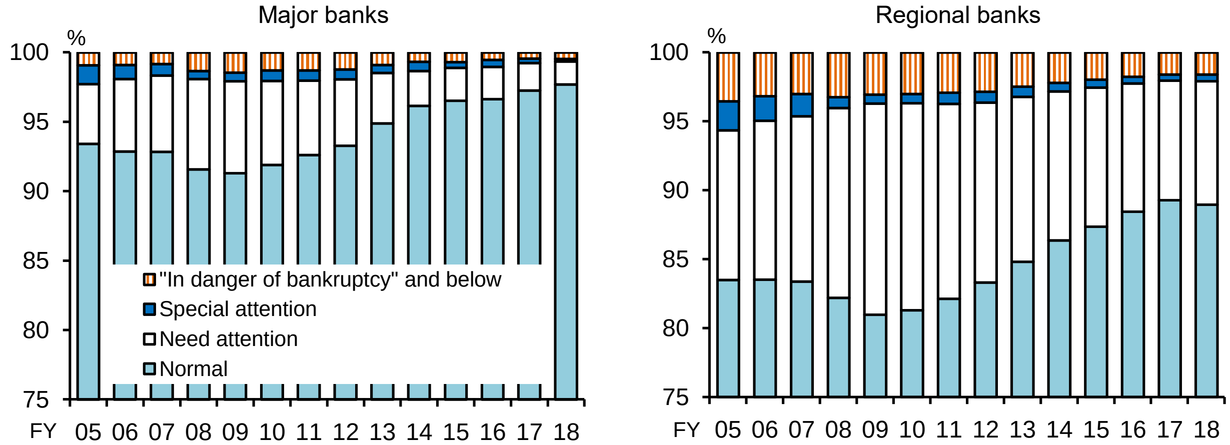
Source: BOJ.

II-C-4: Non-performing overseas loan ratios (three major banks)



Source: Published accounts of each bank.

II-C-5: Proportion of loans outstanding by borrower classification



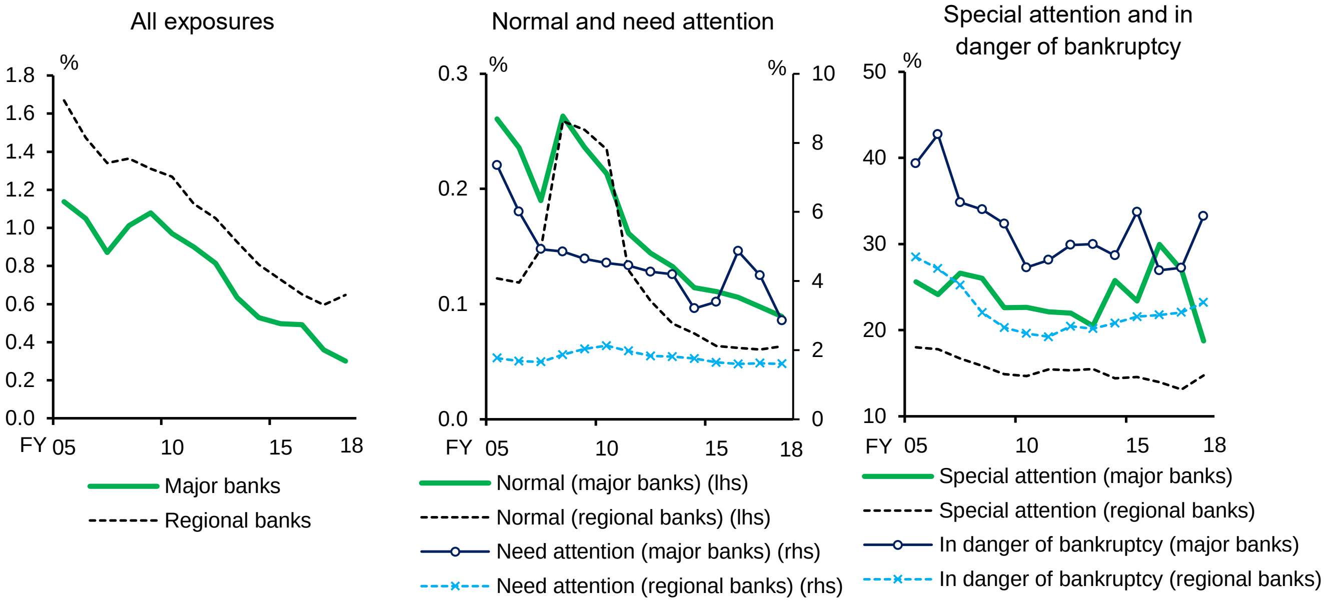
Note: The data are calculated on a write-off basis.
Source: BOJ.

3. Loan-Loss Provisions

(1) Loan-Loss Provision Ratios

The average loan-loss provision ratio for all exposures at major banks decreased from the previous year due to a somewhat large decline in the loan-loss provision ratio for loans requiring "special attention." Such ratio at regional banks turned up due to a rise in loan-loss provision ratios for normal loans and loans requiring "special attention."

II-C-6: Loan-loss provision ratios

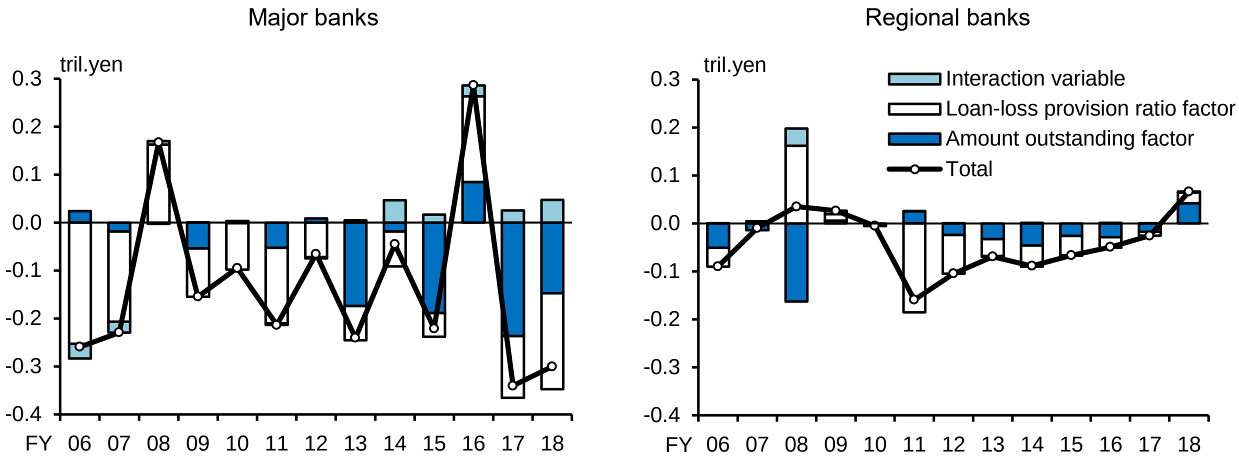


Notes: 1. The data include loans to which the discounted cash flow method is applied.
2. The loan-loss provision ratio is calculated as loan-loss provisions divided by the total amount of claims (not the uncovered amount of claims).
Source: BOJ.

(2) Outstanding Amount of Loan-Loss Provisions

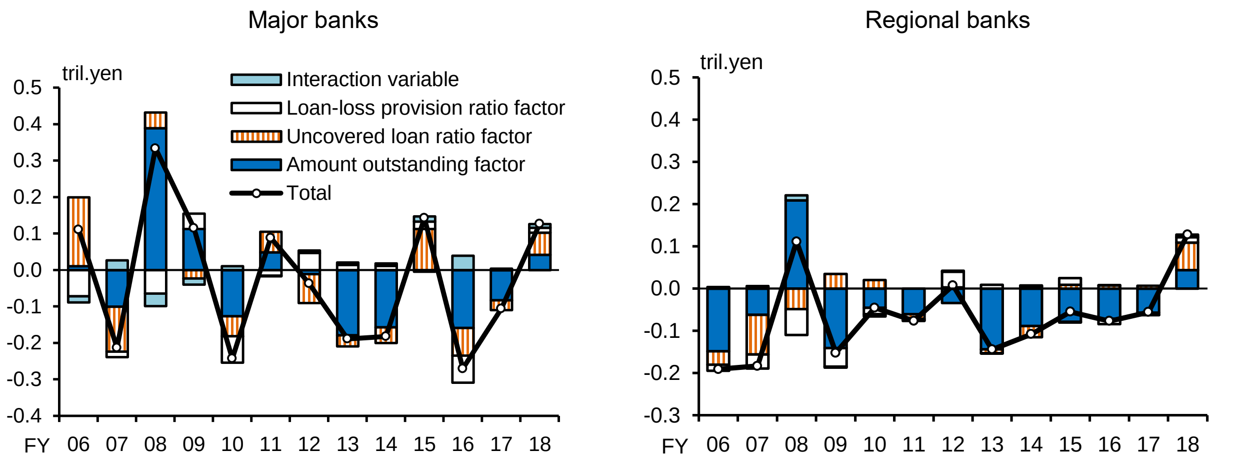
Looking at the outstanding amount of loan-loss provisions, general provisions continued to decline, while special provisions turned up at major banks due to a downgrading of the borrower classification for uncovered domestic exposures to some large companies. Both general provisions and special provisions turned up at regional banks.

II-C-7: Decomposition of outstanding amount of general loan-loss provisions



Note: Each factor represents the sum of the amount calculated by borrower classification.
Source: BOJ.

II-C-8: Decomposition of outstanding amount of special loan-loss provisions



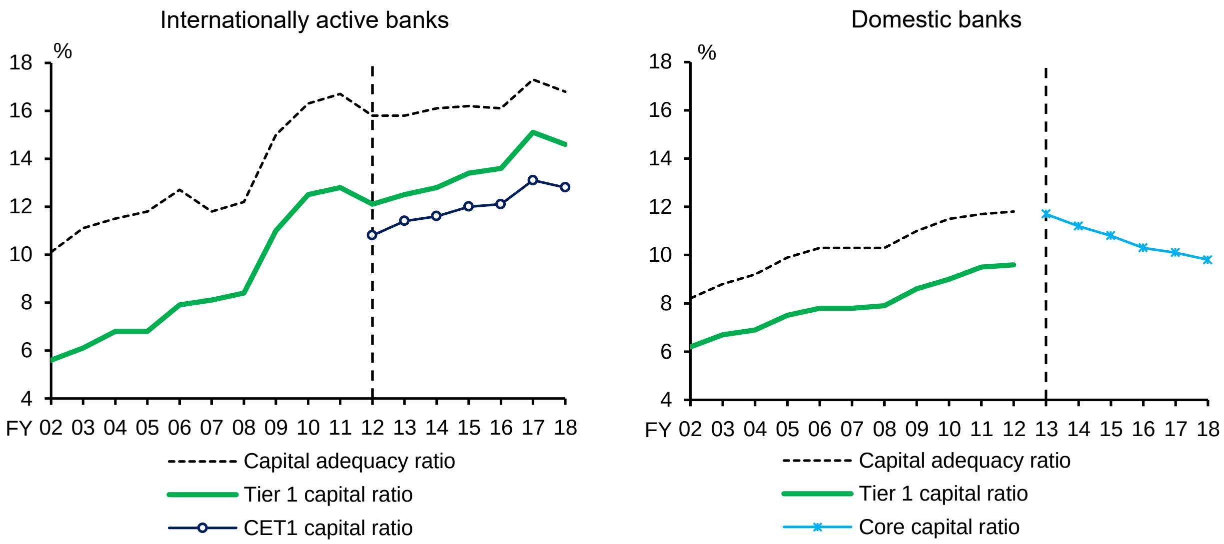
Note: Each factor represents the sum of the amount calculated by borrower classification.
Source: BOJ.

D. Capital Adequacy Ratios

On a consolidated basis, both the common equity Tier 1 capital ratio (CET1 capital ratio) and the capital adequacy ratio of internationally active banks remained high, but turned down as (1) the amount of capital decreased, due to both a pause in the accumulation of retained earnings caused by lower profits and a decline in unrealized gains on available-for-sale securities holdings, which are included in CET1 capital, while (2) risk-weighted assets increased.

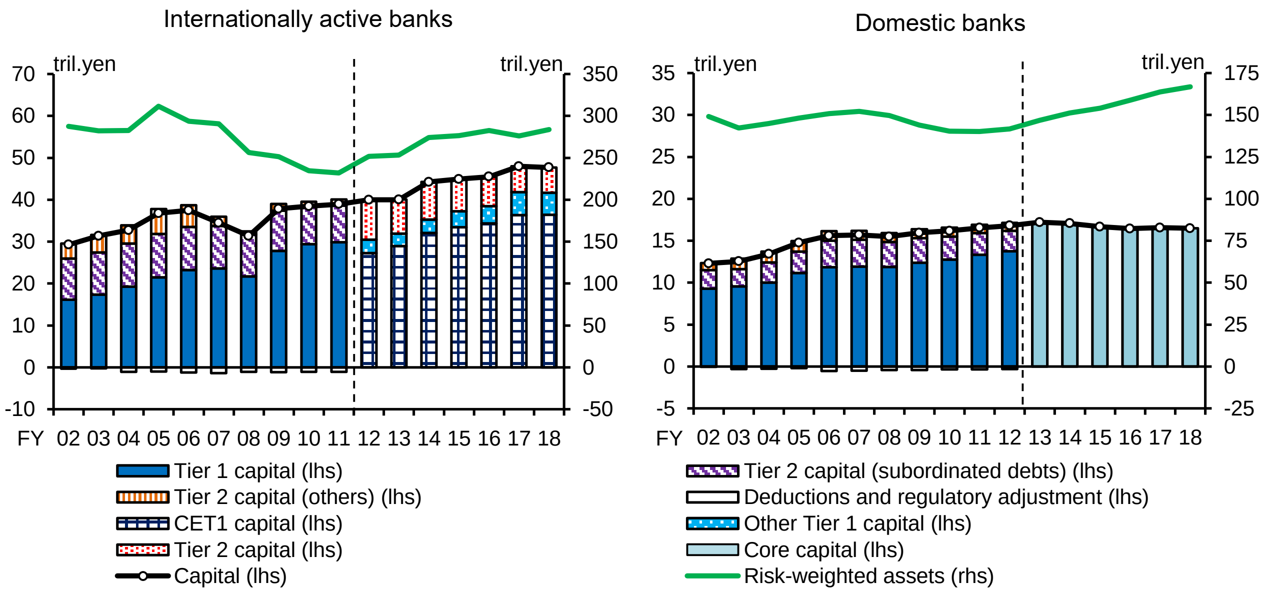
At domestic banks, the capital adequacy ratio continued to decline as (1) the amount of capital decreased, with the arrangements for these banks to phase in the Basel III requirements continuing to be gradually removed (the proportion of instruments that can be included in capital was reduced), and due in part to continued payouts to shareholders despite declining profits (see Box 2 for details), while (2) risk-weighted assets increased.

II-D-1: Capital adequacy ratios



Source: BOJ.

II-D-2: Capital components and risk-weighted assets



Note: Since fiscal 2013, the numerator of the capital adequacy ratio at domestic banks has been referred to as "core capital" in order to distinguish the definition of "capital" in the current Financial Services Agency public notice from that in the former public notice (the same applies to Chart III-D-2).

Source: BOJ.

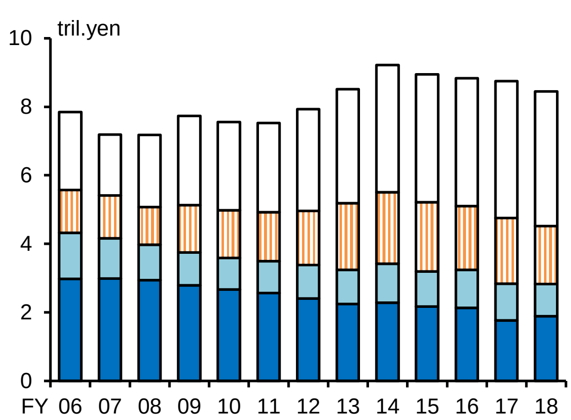
Box 1: Income structures of major financial groups

The income structures of major financial groups have changed over approximately the past 10 years. Among the three major financial groups, banks (the sum of commercial banks and trust banks) -- which form the core of financial groups -- on a non-consolidated basis have seen increases in net non-interest income in the domestic business sector and income in the international business sector, while net interest income in the domestic business sector has continued to follow a declining trend. Furthermore, group companies' profits have increased and contributed to raising the profit levels of individual financial groups as a whole.

Looking at group companies' contribution to consolidated profits for fiscal 2018 by type of group company, PPNR (excluding trading income), which shows core profitability, was pushed up by nonbanks and overseas subsidiaries and affiliates.

Although these types of companies have continuously been incurring certain credit costs and some nonbanks incurred one-time losses in fiscal 2018, net income was also pushed up by group companies' profits.

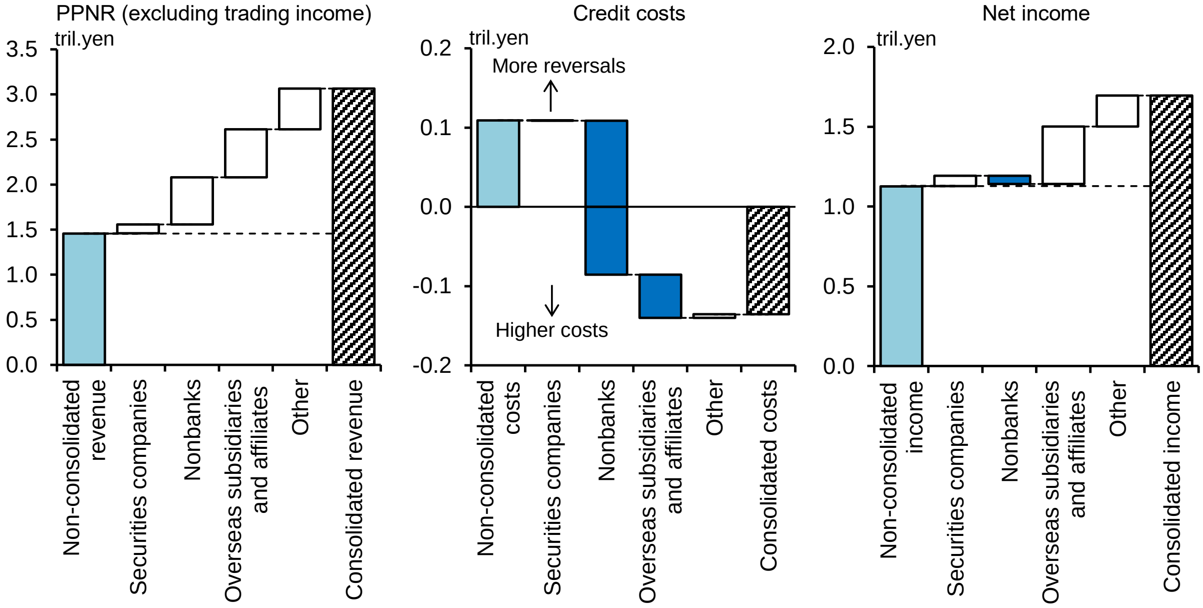
B1-1: Gross operating profits from core business of the three major financial groups



Notes: 1. Gross operating profits from core business = gross operating profits - realized gains/losses on bondholdings.
2. Banks' data (on a non-consolidated basis) are the sum of commercial banks and trust banks. The same applies to the charts below.

Sources: Published accounts of each financial group; BOJ.

B1-2: Breakdown of difference between consolidated and non-consolidated data for the three major financial groups in fiscal 2018



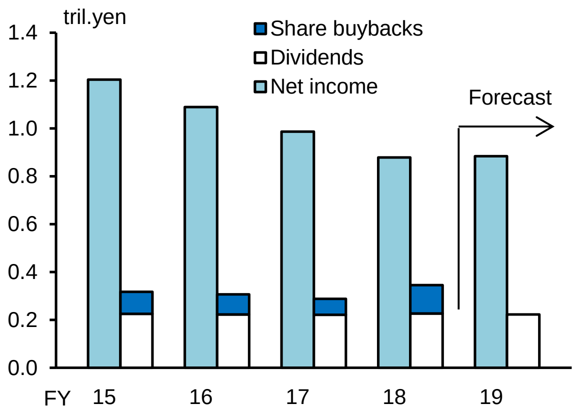
Sources: Published accounts of each financial group; BOJ.

Box 2: Payouts to shareholders by regional banks

A large number of regional banks prioritize stable dividend payouts despite a decline in their profitability and some regional banks buyback their shares.

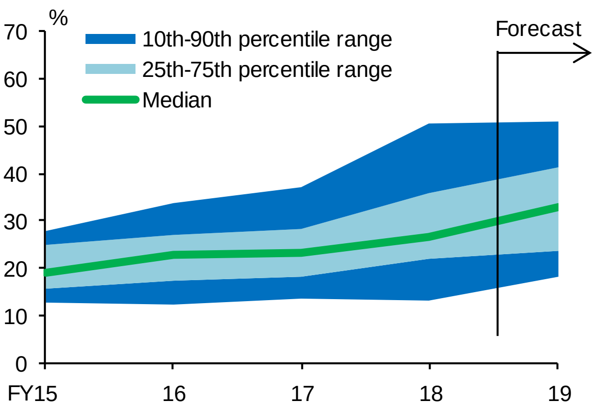
As a result, both dividend payout ratios and total payout ratios among regional banks have been trending upward and their distributions have been skewed upward. This trend is likely to largely continue in fiscal 2019.

B2-1: Net income and payouts to shareholders of regional banks



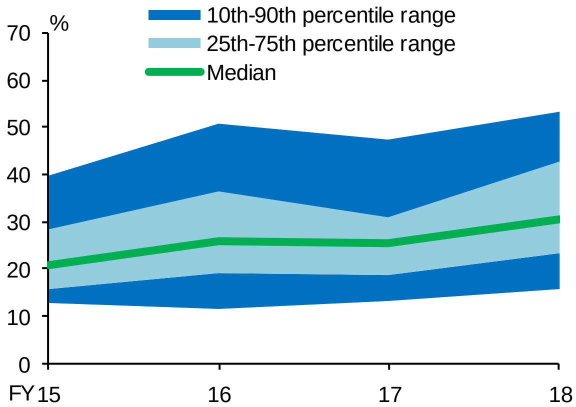
Notes: 1. The data are on a consolidated basis of banks or holding companies.
2. The data for the fiscal 2019 forecast are published by each bank and holding company, excluding the data for share buybacks.
3. The data for share buybacks include those for the repayment of public funds.
Source: BOJ.

B2-2: Dividend payout ratios of regional banks



Notes: 1. Dividend payout ratio = dividends / net income.
2. The data for the fiscal 2019 forecast are published by each bank and holding company.
Source: BOJ.

B2-3: Total payout ratios of regional banks



Note: Total payout ratio = (dividends + share buybacks) / net income.
Source: BOJ.

III. Financial Results of Japan's *Shinkin* Banks for Fiscal 2018

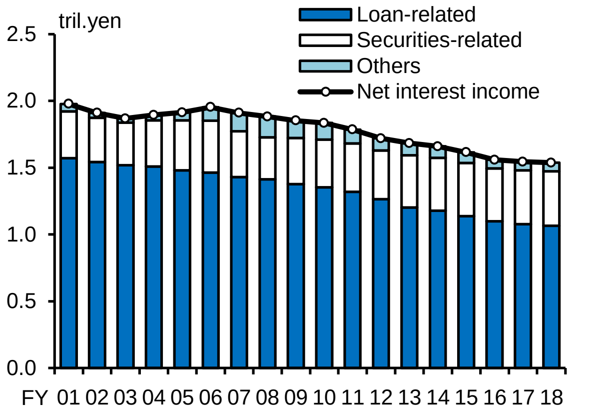
This chapter analyzes *shinkin* banks' core profitability (net interest income, net non-interest income, and general and administrative expenses), realized and unrealized gains/losses on securities holdings, credit costs and non-performing loans, as well as capital adequacy ratios.

A. Core Profitability

1. Net Interest Income

Net interest income continued to decrease as the impact of narrowing interest rate spreads on loans was larger than that of an increase in loans outstanding.

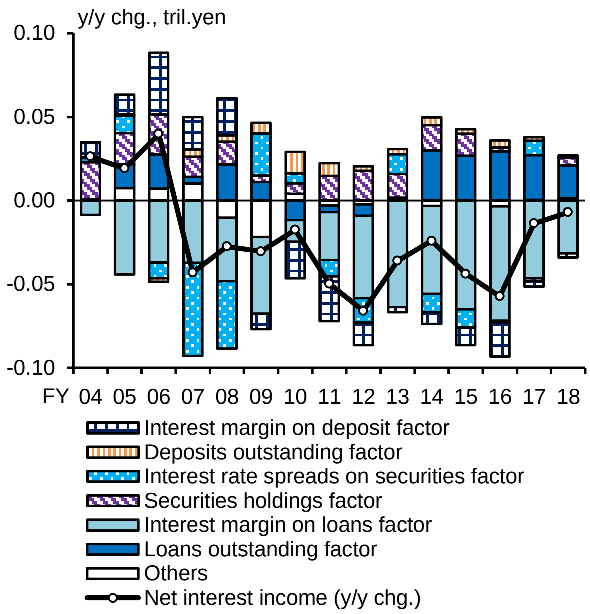
III-A-1: Net interest income



Notes: 1. "Others" includes interest income on deposits at the *Shinkin* Central Bank and at the Bank of Japan.
2. Loan-related = (average loans outstanding) * (interest rate spreads on loans). Securities-related = (average outstanding securities holdings) * (interest rate spreads on securities).

Source: BOJ.

III-A-2: Decomposition of net interest income (change from a year earlier)



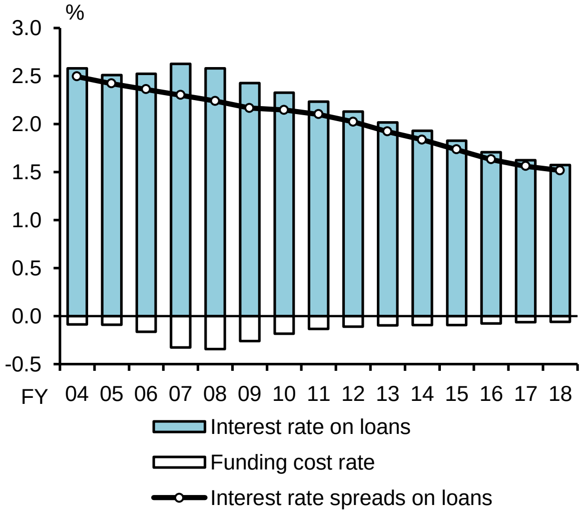
Source: BOJ.

2. Interest Rate Spreads on Loans and Loans Outstanding

(1) Interest Rate Spreads on Loans

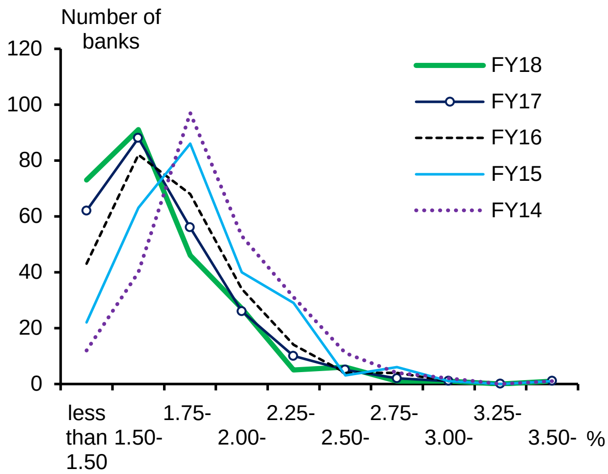
Interest rate spreads on loans continued to narrow due to a decline in lending rates. The distribution of interest rate spreads for individual *shinkin* banks also continued to shrink on the whole.

III-A-3: Interest rate spreads on loans



Note: In calculating the interest rate spreads, interest expenses on interest rate swaps are deducted from funding costs.
Source: BOJ.

III-A-4: Distribution of interest rate spreads on loans

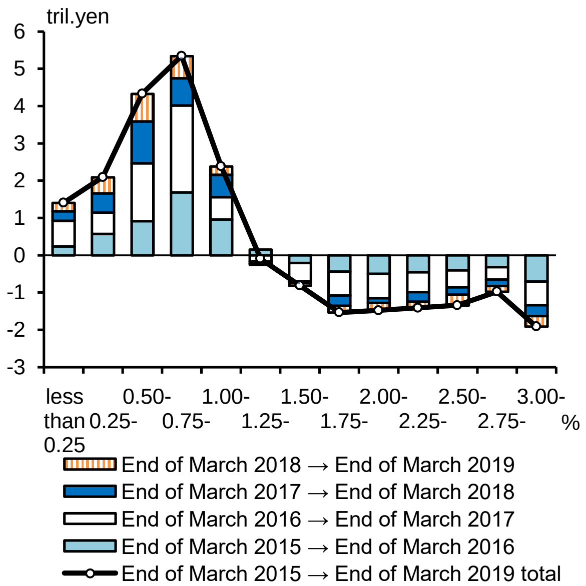


Note: In calculating the interest rate spreads, interest expenses on interest rate swaps are deducted from funding costs.
Source: BOJ.

(2) Loans Outstanding by Lending Rate

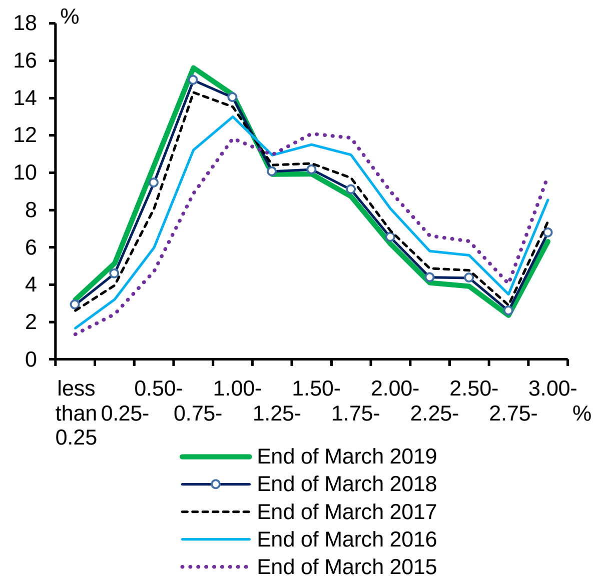
Looking at developments in loans outstanding, those with low lending rates continued to increase.

III-A-5: Changes in loans outstanding by lending rate (from the end of March 2015 to the end of March 2019)



Source: BOJ.

III-A-6: Changes in proportion of loans outstanding by lending rate (from the end of March 2015 to the end of March 2019)

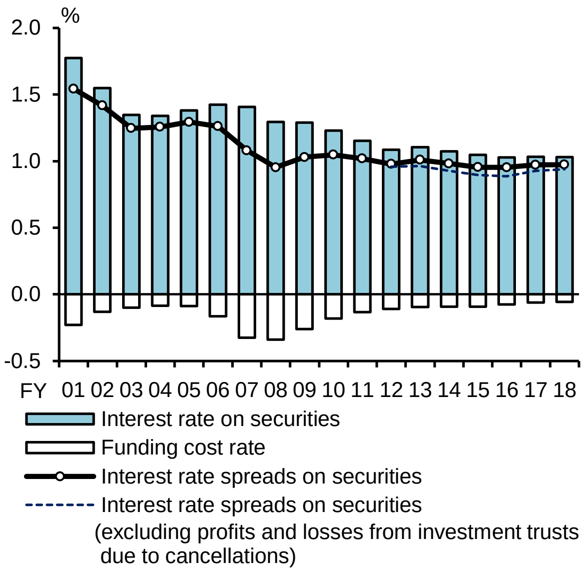


Source: BOJ.

3. Interest Rate Spreads on Securities

Interest rate spreads on securities were more or less unchanged on the whole.

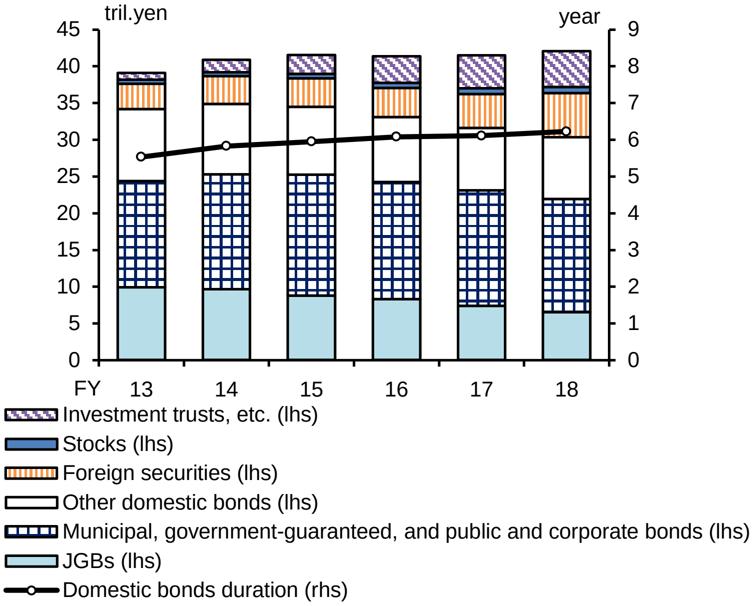
III-A-7: Interest rate spreads on securities



Note: In calculating the interest rate spreads, interest expenses on interest rate swaps are deducted from funding costs.

Source: BOJ.

III-A-8: Amounts outstanding and duration of securities by product type

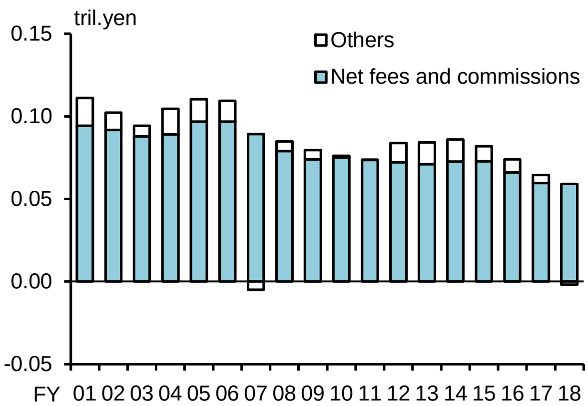


Source: BOJ.

4. Net Non-Interest Income

Net non-interest income decreased due to weakness in sales of investment trusts.

III-A-9: Net non-interest income

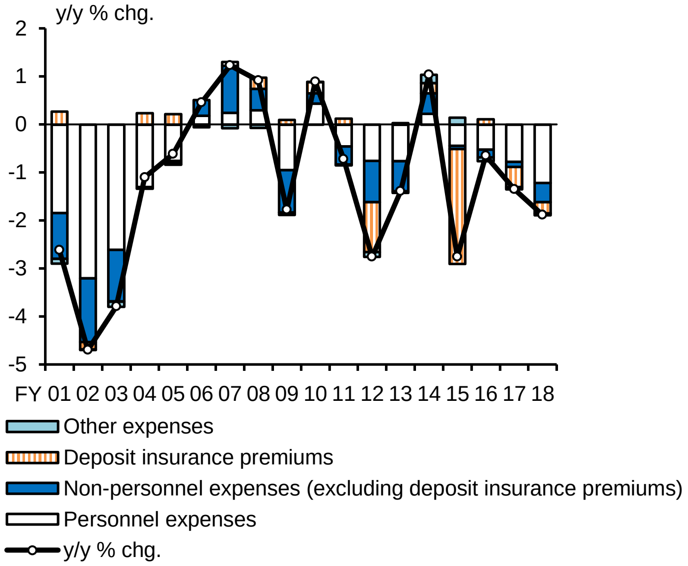


Source: BOJ.

5. General and Administrative Expenses

General and administrative expenses decreased, particularly with respect to personnel expenses.

III-A-10: Decomposition of general and administrative expenses



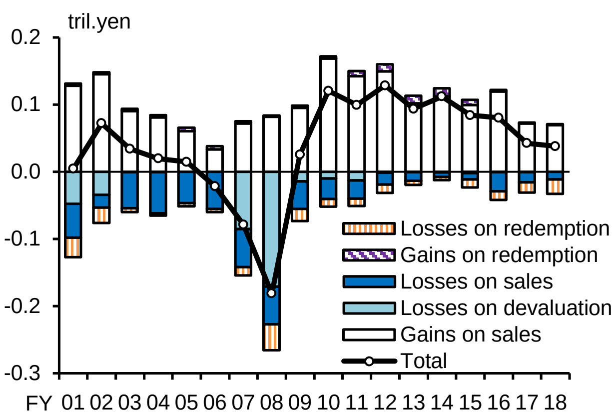
Source: BOJ.

B. Realized and Unrealized Gains/Losses on Securities Holdings

1. Realized Gains/Losses on Securities Holdings

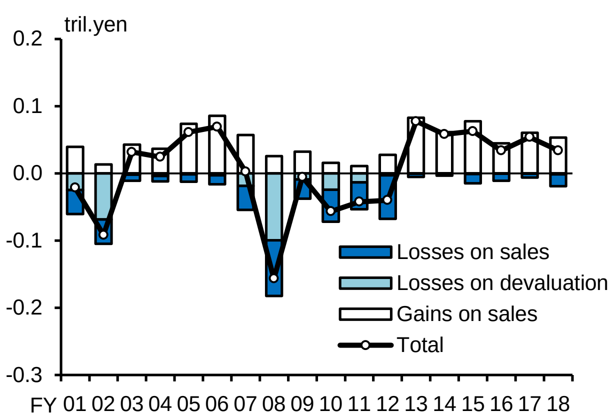
Looking at realized gains/losses on bondholdings, the extent to which gains exceeded losses was around the same as the previous year. On the other hand, for those on stockholdings, the extent to which gains exceeded losses was less than in the previous year.

III-B-1: Realized gains/losses on bondholdings



Source: BOJ.

III-B-2: Realized gains/losses on stockholdings

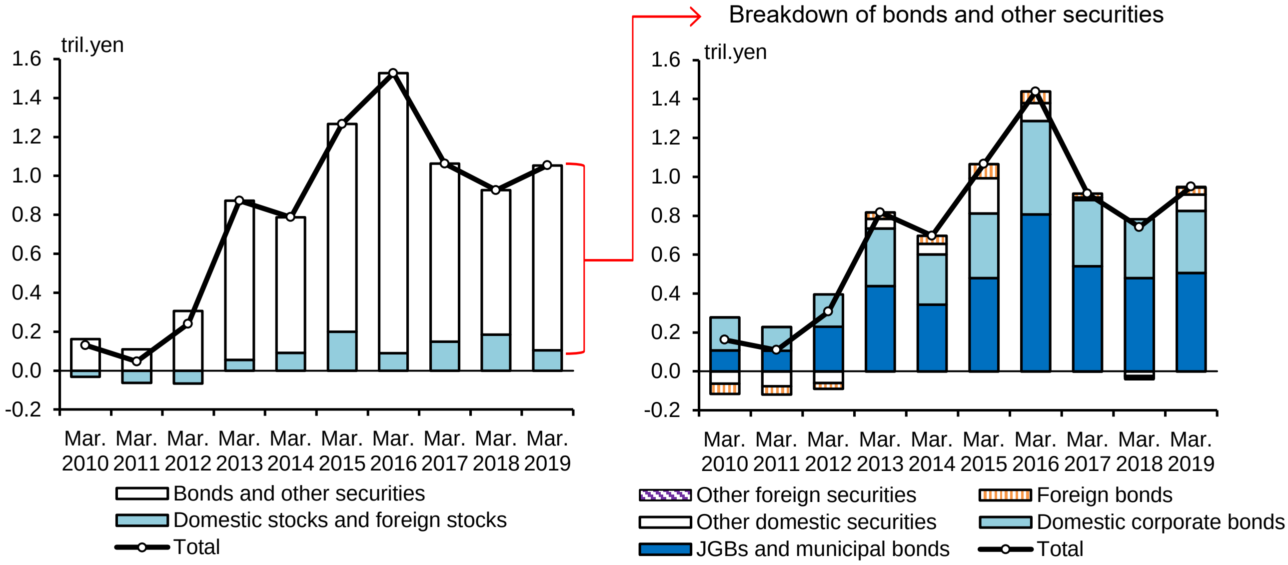


Source: BOJ.

2. Unrealized Gains/Losses on Securities Holdings

Looking at unrealized gains/losses on available-for-sale securities holdings as of the end of March 2019 for bondholdings, which accounted for a large share of the total gains on securities holdings, the extent to which gains exceeded losses expanded due to a decline in domestic and overseas interest rates.

III-B-3: Unrealized gains/losses on available-for-sale securities holdings



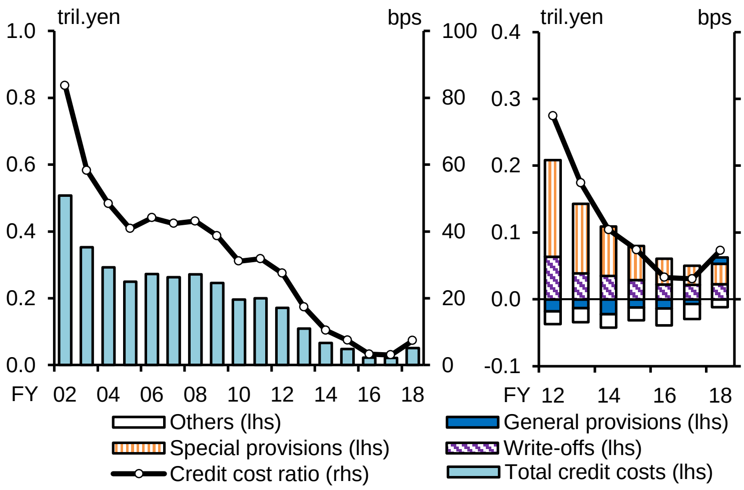
Note: "Other domestic securities" and "other foreign securities" include investment trusts and funds.
Source: BOJ.

C. Credit Costs and Non-Performing Loans

1. Credit Costs

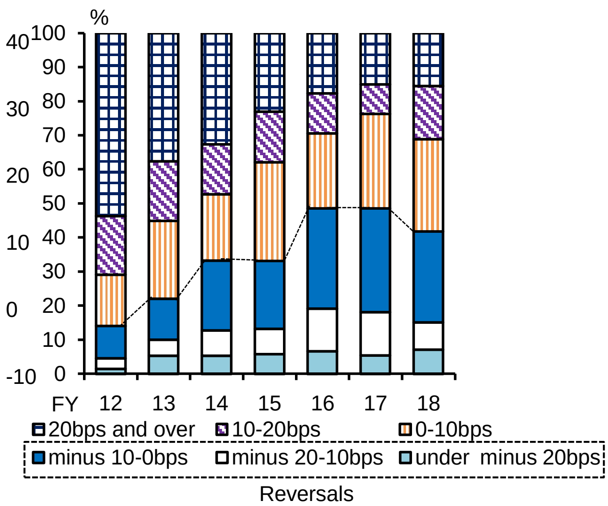
Credit costs increased for the first time in seven years as general loan-loss provisions turned positive following the reversals until the previous year. Looking at the distribution of credit cost ratios among *shinkin* banks, the share of banks with credit costs reversed decreased somewhat, and the share of banks with credit costs 10 basis points or greater increased.

III-C-1: Credit costs and credit cost ratio



Source: BOJ.

III-C-2: Distribution of credit cost ratios

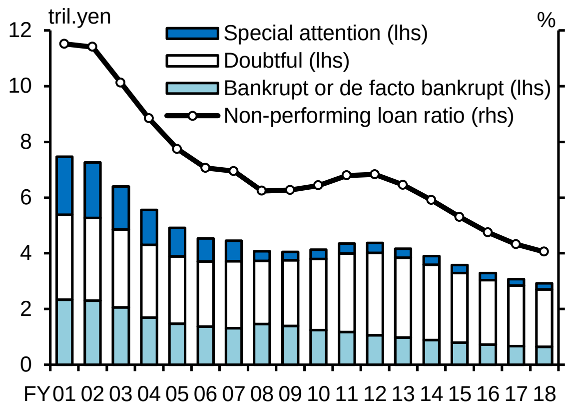


Note: Proportion of number of banks by credit cost ratio.
Source: BOJ.

2. Non-Performing Loans

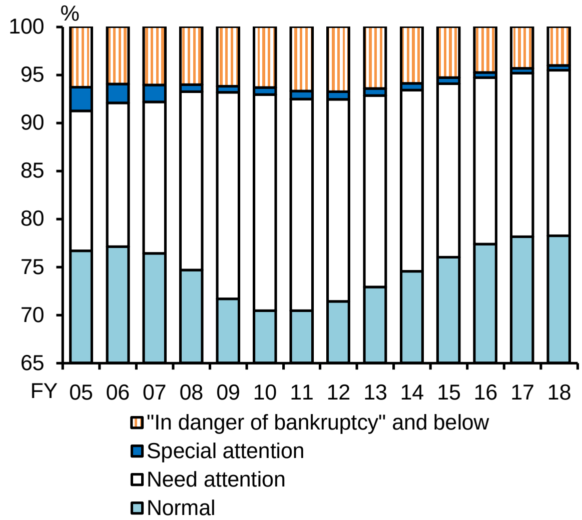
The NPL ratio continued to decline moderately and reached its lowest level since fiscal 2001, when the relevant data were first recorded. The proportion of loans outstanding for normal loans remained large.

III-C-3: Non-performing loans outstanding and non-performing loan ratios



Source: BOJ.

III-C-4: Proportion of loans outstanding by borrower classification



Note: The data are calculated on a write-off basis.
Source: BOJ.

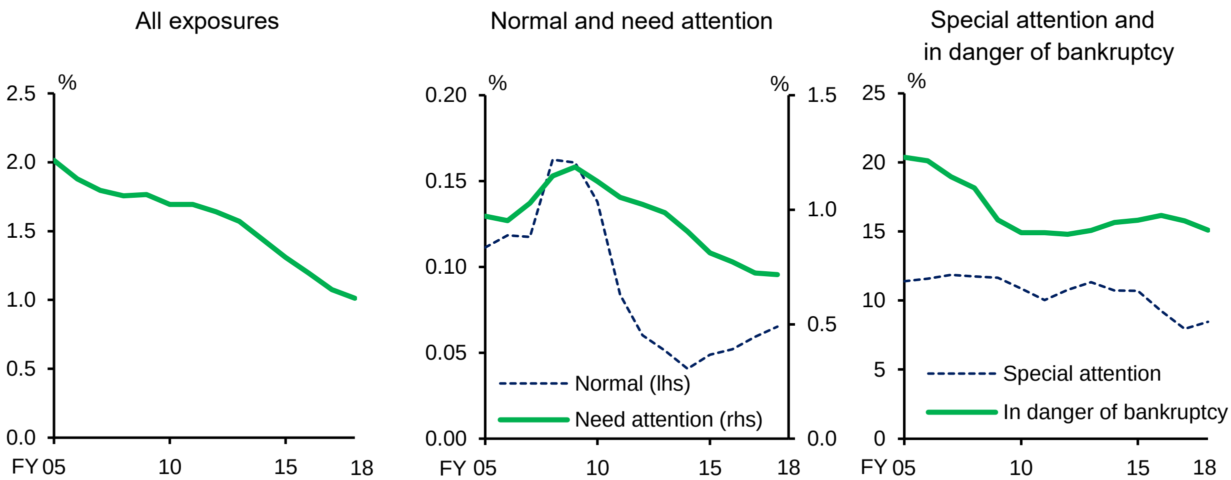
3. Loan-Loss Provisions

(1) Loan-Loss Provision Ratios

The average loan-loss provision ratio for all exposures continued to decline.

Looking at loan-loss provisions by borrower classification, the loan-loss provision ratio for normal loans continued to increase and the ratio for loans requiring "special attention," which had continued to decline, turned up.

III-C-5: Loan-loss provision ratios

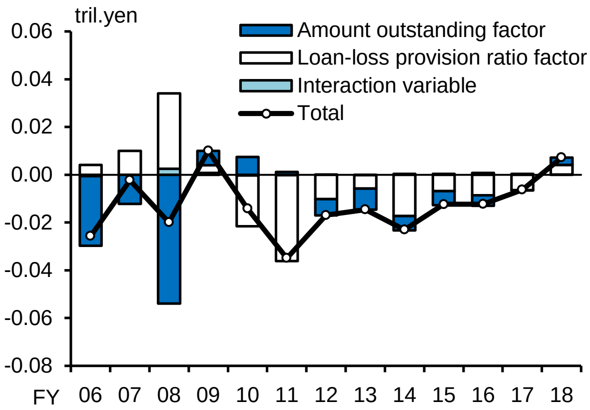


Notes: 1. The data include loans to which the discounted cash flow method is applied.
2. The loan-loss provision ratio is calculated as loan-loss provisions divided by the total amount of claims (not the uncovered amount of claims).
Source: BOJ.

(2) Outstanding Amount of Loan-Loss Provisions

As for the outstanding amount of loan-loss provisions, general provisions turned up due to an increase in the outstanding amount of "need attention" loans and a rise in the loan-loss provision ratio for normal loans. Special provisions continued to decrease mainly due to the decline in the outstanding amount of loans requiring special provisions.

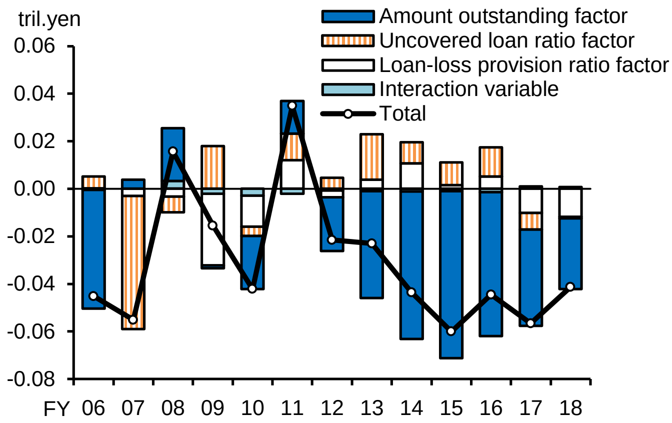
III-C-6: Decomposition of the outstanding amount of general loan-loss provisions



Note: Each factor represents the sum of the amount calculated by borrower classification.

Source: BOJ.

III-C-7: Decomposition of the outstanding amount of special loan-loss provisions



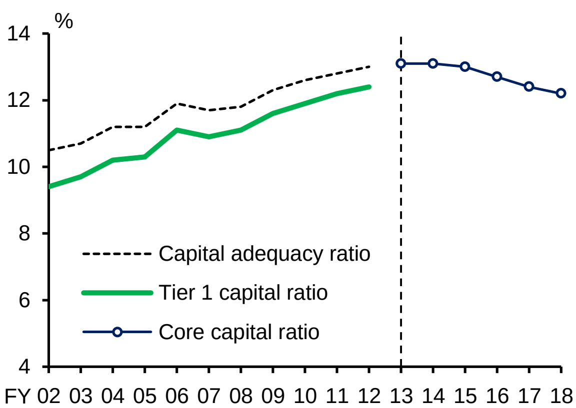
Note: Each factor represents the sum of the amount calculated by borrower classification.

Source: BOJ.

D. Capital Adequacy Ratios

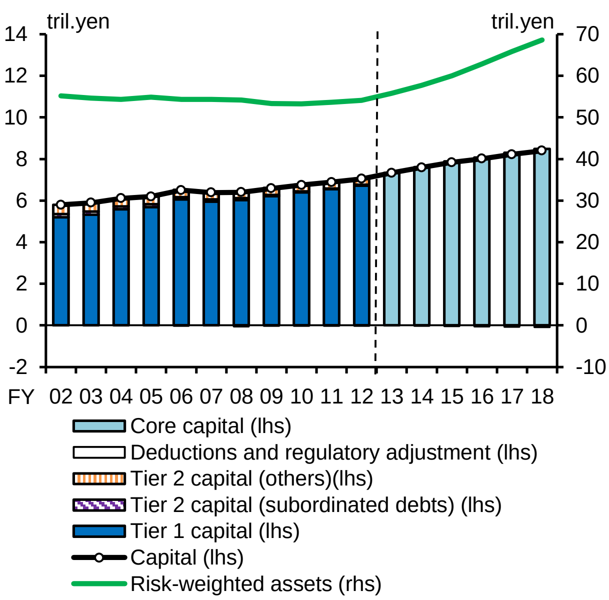
The capital adequacy ratio decreased slightly. The amount of capital increased, mainly due to the accumulation of retained earnings, but this was outpaced by an increase in risk-weighted assets.

III-D-1: Capital adequacy ratios



Source: BOJ.

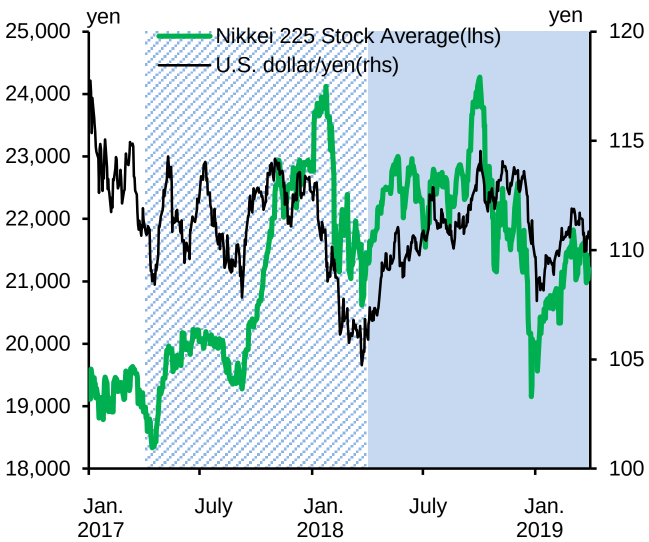
III-D-2: Capital components and risk-weighted assets



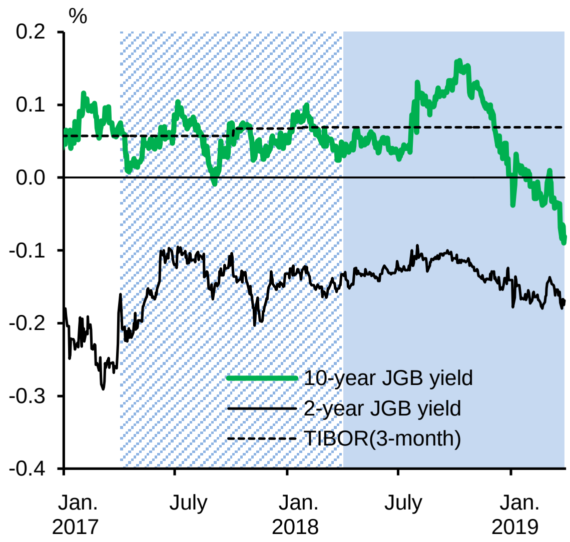
Source: BOJ.

Reference: Developments in Financial Markets

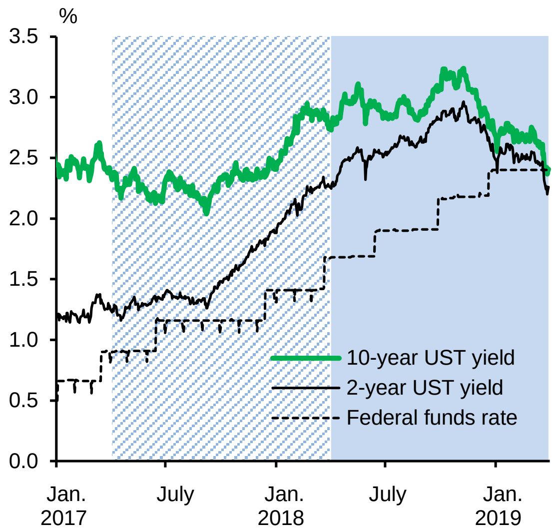
▽ Nikkei 225 Stock Average and foreign exchange rates



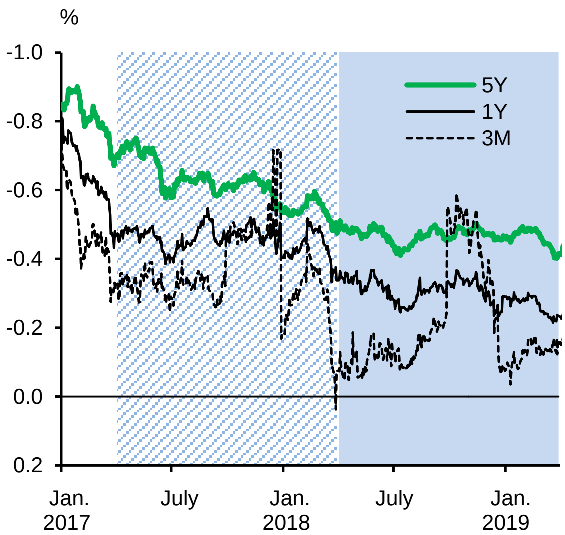
▽ JGB yields, etc.



▽ U.S. treasury yields, etc.



▽ U.S. dollar funding premiums



Notes: 1. Latest data as at end-March 2019. U.S. dollar funding premiums indicate the additional interest costs on U.S. dollar LIBOR in financing U.S. dollar funds collateralized by yen funds. 3M dollar funding premiums, which are expressed in opposite signs, show U.S. dollar funding costs on U.S. dollar LIBOR spreads through currency and foreign exchange swaps. Both 1Y and 5Y dollar funding premiums are U.S. dollar/yen cross-currency basis swaps.

2. The lightly shaded areas show the data in fiscal 2017. The darker shaded areas show the data in fiscal 2018.

Source: Bloomberg.

Glossary

Financial statements of financial institutions

Net income = operating profits from core business + realized gains/losses on stockholdings + realized gains/losses on bondholdings – credit costs ± others (such as extraordinary gains/losses)

Operating profits from core business = pre-provision net revenue (PPNR) (excluding trading income) = net interest income + net non-interest income – general and administrative expenses

Net interest income = interest income – interest expenses

Net non-interest income = net fees and commissions + profits on specified transactions + other operating profits – realized gains/losses on bondholdings

Realized gains/losses on stockholdings = gains on sales of stocks – losses on sales of stocks – losses on devaluation of stocks

Realized gains/losses on bondholdings = gains on sales of bonds + gains on redemption of bonds – losses on sales of bonds – losses on redemption of bonds – losses on devaluation of bonds

Credit costs = loan-loss provisions + write-offs + losses on credit sales – recoveries of write-offs

Credit cost ratio = credit costs / total loans outstanding

Capital adequacy ratios of internationally active banks

Common equity Tier 1 (CET1) capital ratio = CET1 capital / risky assets

CET1 capital comprises common equities and retained earnings.

Risky assets are financial institutions' risk-weighted assets.

Tier 1 capital ratio = Tier 1 capital / risky assets

Tier 1 capital includes CET1 capital and equities such as preferred equities that meet certain conditions.

Total capital adequacy ratio = Total capital / risky assets

Total capital includes Tier 1 capital and subordinated bonds that meet certain conditions.

Capital adequacy ratios of domestic banks

Core capital ratio = core capital / risky assets

Core capital includes common equities and retained earnings as well as equities such as preferred equities that meet certain conditions.

Risky assets are financial institutions' risk-weighted assets.