March 29, 2016
Bank of Japan

On-Site Examination Policy for Fiscal 2016

1. On-Site Examination by the Bank of Japan

The Bank of Japan (hereinafter, the Bank) formulates the on-site examination policy every fiscal year based on the decision of the Policy Board.[1] This document, "On-Site Examination Policy for Fiscal 2016" briefly reviews on-site examinations carried out in fiscal 2015 and outlines the basic approach and key issues in the conduct of on-site examinations in fiscal 2016. The Bank will conduct on-site examinations in fiscal 2016 on the basis of this document.

2. On-Site Examinations in Fiscal 2015 and General Observations

(1) On-Site Examinations in Fiscal 2015

The Bank carried out on-site examinations of 78 financial institutions in fiscal 2015: 30 domestically licensed banks, 36 *shinkin* banks, and 12 other institutions, including securities companies as well as Japanese branches and subsidiaries of foreign banks.[2]

[1] The Bank of Japan Act stipulates that "the content of a contract concerning on-site examinations" and "important matters concerning the implementation of on-site examinations for each business year" shall be determined by the Policy Board (Article 15, paragraph 2, item v).

[2] "Securities companies" in this document refers to firms that conduct securities-related business activities among those classified as Type I Financial Instruments Business in Article 28 of the Financial Instruments and Exchange Act.

Number of Financial Institutions Examined

	Fiscal 2013	Fiscal 2014	Fiscal 2015
Domestically licensed banks	29	33	30
Shinkin banks	55	40	36
Other institutions	26	12	12
Total	110	85	78

(2) Issues Observed in On-Site Examinations

In the fiscal 2015 on-site examinations, the Bank sought to adequately grasp financial institutions' business operations and the state of their property and examined the effectiveness of risk management conducted in accordance with their risk profiles.

As Japan's economy has continued its moderate recovery trend, financial institutions have taken a more active risk-taking stance, particularly in terms of loans and/or securities investment. Nevertheless, their capital bases relative to risks have been adequate in general, and their capacity to absorb losses has continued to be high.

Regarding risk management, individual financial institutions have continued to improve their management frameworks, but some of them needed to strengthen management in accordance with the accumulation and diversification of risks due to enhancing their loans in Japan and overseas as well as their market investments, including foreign currency-denominated ones.

Moreover, from the perspective of responding to structural changes in the financial system, major financial institutions have continued with their international business expansion and group-based business strategies, making it more important to appropriately grasp and manage complex and global risks. In this situation, some faced challenges in terms of their impact assessment and study of countermeasures on the assumption of stress events. On the other hand, the core profitability of regional financial institutions is generally on a declining trend, and it has become increasingly important to stabilize and improve their long-term profitability -- while helping to raise the growth potential of local areas -- as population declines are expected to occur in many regions. Nevertheless, only some of them have made progress in their specific study of long-term business strategies, taking into account the awareness of such an environment (see Appendix for major issues).

3. On-Site Examination Policy for Fiscal 2016

(1) Basic Approach

Financial institutions are expected to contribute to corporate and household economic activities and, ultimately, increase the growth potential on both the national and regional levels by ensuring the appropriate functioning of financial intermediation. Finance has a major role to play in addressing the challenges faced by the Japanese economy, including economic globalization as well as the decline in and aging of the population, and thereby creating a vigorous industrial structure. To perform this role in the current economic environment, financial institutions need to adopt a positive approach toward risk taking based on solid financial bases and clearly defined business strategies. It is essential for them to appropriately manage risks as well as stabilize and improve their profitability in order to maintain the soundness of their management while taking such a risk-taking stance. The importance of such efforts is expected to increase with the Bank's introduction of "Quantitative and Qualitative Monetary Easing with a Negative Interest Rate."

Against this background, and based on the challenges identified in the fiscal 2015 on-site examinations, the Bank will take the following points into account in the fiscal 2016 on-site examinations.[3]

First, the Bank will confirm how the board of directors or other relevant body (hereinafter, the board of directors) of financial institutions recognizes the external environment including financial and economic conditions, and examine their business strategies based on such recognition. The Bank will then grasp the financial institutions' current and future risk profiles, including the quality of their asset portfolios and the structure of assets and liabilities, by such means as assessing their assets and examining their securities investments and new businesses. The Bank will examine the risks associated with the rapid expansion of overseas business in recent years, from a broad perspective including credit risks and the stability of foreign currency funding, taking into account overseas economic conditions and the foreign currency funding environment. Regarding market investment, the Bank will examine risks involved in securities portfolios by risk factor.

Second, the Bank will examine financial institutions' resilience against risks. Specifically, it will examine whether the board of directors is properly involved in ensuring that (1) risk awareness is sufficiently shared when formulating business strategies or plans, (2) risk-taking policies compatible with the financial institutions' financial bases are formulated and risk management frameworks suitable to such policies are developed, (3) risk-taking policies or risk management frameworks are reviewed in response to changes in the external environment, and (4) risk management is effective. The Bank also will examine the

[3] In doing so, the *Financial System Report* will be referred to for analysis and evaluation of risks in the overall financial system in Japan.

functioning of bodies such as the board of directors, including various committees, the board of auditors, and internal audits.

Third, the Bank will examine the impact on financial institutions' profit and financial bases and responses in the event of changes in financial and economic conditions or stresses in accordance with the situation regarding the institutions' management and business.

Major financial institutions now have an increasingly significant impact on financial markets and the economy, as their profit sources and risks have become more diverse and complex through active expansion internationally and provision of a wide range of financial services on a group basis. In this context, the Bank will examine the impact and responses on the assumption of stress events, as well as the routes by which risk spreads and potential effects through credit provision relationships with other domestic and overseas major financial institutions.

The core profitability of regional financial institutions is generally on a declining trend, and population declines are expected to occur in many regions. In this context, the Bank will place more emphasis than before on the assessment of profitability. Specifically, it will run profit simulations assuming several scenarios including downside risks. In addition, the Bank will review the prospects for the regional economies, their customer base and profitability in the longer term, as well as their awareness of issues and management policies based on such prospects. In doing so, it will enhance its interaction with regional financial institutions on the direction of business management from a wide perspective including their asset-liability management, income/expense profiles, channel strategies, and utilization of information technologies.

Fourth, the Bank will strive to conduct its on-site examinations more efficiently under the framework of "risk-based on-site examinations" employed since fiscal 2008. With regard to financial institutions that provide a wide range of financial services through group entities, it will endeavor to grasp their relationships with major group companies and the actual business conditions of the group as a whole. Moreover, the Bank will enhance its on-site examinations of overseas branches through means including more specific field work, given the increased weight of international businesses. To enhance the effectiveness of on-site examinations, the Bank will interview the internal auditors of financial institutions before visiting their premises, and will continue to strengthen the linkage between on-site examinations and off-site monitoring.

(2) Key Issues in the Conduct of On-Site Examinations

In conducting on-site examinations, the Bank, based on the aforementioned basic approach, will focus particularly on the following issues. In doing so, it will examine and review various aspects of financial institutions in a flexible and effective manner in accordance with their business and their risk-taking attitude.

a. Business Management

Ensuring the Effectiveness of Internal Control

To ensure the effectiveness of risk management, internal control frameworks at financial institutions need to function effectively.

In the fiscal 2016 on-site examinations, the Bank will examine the following: (1) whether the board of directors has provided risk management frameworks and oversees the implementation appropriately; (2) whether senior management executes operations in accordance with the risk-taking policy determined by the board of directors and manages risks; and (3) whether senior management provides reports appropriately so that the board of directors can oversee the risk management practice.[4] In doing so, the Bank also will examine (4) the effectiveness of the group-wide business management of financial institutions, including overseas branches and subsidiaries, which offer a wide range of financial services on a group basis.

Proactive Improvement of Risk Management with Internal Audits

Internal audits provide a basis for ensuring the proper conduct of business operations and play an important role in promoting the proactive improvement of risk management. For this reason, the board of directors needs to be aware of the importance of internal audits and ensure their effectiveness. Also, the internal auditors need to evaluate the effectiveness of risk management and other control functions and report to the board of directors as appropriate from an independent and objective standpoint.

In the fiscal 2016 on-site examinations, the Bank will examine the following: (1) whether the board of directors appropriately decides the scope of internal audits and allocates audit resources based on the risk assessment; (2) whether the internal auditors adequately audit businesses, including those of overseas entities and subsidiaries; and (3) whether the board of directors makes the most of auditors' recommendations regarding their business management.

[4] In the on-site examinations, the Bank will refer to the "Corporate governance principles for banks" issued by the Basel Committee on Banking Supervision in July 2015.

Business Management Based on an Optimal Balance between Financial Bases and Risk Taking

To ensure the sustainable and stable functioning of financial intermediation, it is important for financial institutions to strike the right balance between financial bases and risk taking. In particular, major financial institutions need to conduct appropriate risk management while securing sufficient equity capital and liquidity, so that they can provide important financial functions continuously without relying on public support measures even under stress situations, taking into account the global efforts to solve the "too big to fail" problem. In this regard, it is effective to analyze the impact of any materialization of risk and systematically review the risk-taking policy and risk management frameworks based on the results.

In the fiscal 2016 on-site examinations, with regard to major financial institutions, the Bank will examine the following with regard to stress testing: (1) involvement of the board of directors and control functions of sections in charge; (2) sufficiency of scenarios and coverage of the subjects of the stress testing based on financial institutions' risk profiles and business strategies; (3) verification systems for models and data; and (4) frameworks to reflect test results of business operations and risk management. The Bank will then confirm the board of directors' awareness with regard to assessing the sufficiency of quality/quantity of the equity capital and the capital policy based on this assessment, taking into account the results of stress testing and responses to international financial regulations, and provide the necessary recommendations. The Bank also will examine progress with the establishment of the framework for controlling risk taking and management comprehensively based on the institutions' business strategies, including the risk appetite framework. Regarding Global Systemically Important Financial Institutions (G-SIFIs) and major financial institutions equivalent to them, the Bank will examine the effectiveness of the recovery plans and contingency plans.

With regard to overseas G-SIFIs' Japanese branches, the Bank will examine whether they have established an appropriate management framework, while understanding the roles of Japanese branches within their group, particularly in transactions, bookings, and risk management. On this basis, it will examine (1) impacts on Japanese branches under the assumption of stress events for the group as a whole and responses to them, and (2) the situations for Japanese branches within the recovery plans, including the involvement of Japanese branches in these matters. Moreover, regarding those branches with corporate status in Japan, the Bank also will examine the support system provided by headquarters in the event of deterioration in business conditions.

With regard to regional financial institutions, the Bank will run profit simulations under several scenarios including downside risks for the coming three years or so, to assess the economic value of the institutions' asset holdings and the impact on the asset and liability structure. On this basis, the Bank will confirm the board of directors' awareness of the assessment of the sufficiency of quality/quantity of the equity capital and the capital policy based on this assessment, as well as other issues for business management, and provide the necessary recommendations. In addition, it will examine the following: (1) whether the adequacy of the risk-taking policy, business operation, and risk management frameworks are verified through the frameworks of asset-liability management (ALM) and risk capital allocation; (2) whether necessary reviews are conducted based on the verification results; and (3) whether they analyze the possible impact on financial bases and profits in the event of abrupt changes in financial and economic conditions, and consider appropriate responses.

Furthermore, the Bank will confirm with the board of directors longer-term prospects for the regional economies and for regional financial institutions' customer bases and profitability, as well as their awareness of issues and management policies based on such prospects. Through such examination and confirmation, the Bank will enhance its interaction with regional financial institutions on the direction of business management from a wide perspective including their asset-liability management, income/expense profiles, channel strategies, and utilization of information technologies.

Development of Management Information Systems

It is important for financial institutions to appropriately set up and employ mechanisms to gather the information necessary to manage business operations and risks. For financial institutions that actively expand their international businesses and offer a wide range of financial services on a group basis, it is important to appropriately assess in a timely manner various risks that extend over regions.

In the fiscal 2016 on-site examinations, mainly with regard to major financial institutions, the Bank will examine (1) whether they have appropriately set up mechanisms to gather the necessary information, including those for information infrastructure such as the management information system (MIS), and (2) whether the reliability and timeliness of information are ensured. With regard to major financial institutions, the Bank also will examine (3) the routes by which risk spreads as well as potential effects through fund transactions and credit provision relationships with other major domestic and overseas financial institutions.

b. Credit Risk Management

Appropriate Credit Screening and Monitoring, and Establishment of a Framework Compatible with Lending Strategies

Financial institutions need to appropriately assess the business conditions of borrowing firms in terms of credit screening and follow-up monitoring, and ensure that credit screening and monitoring frameworks compatible with their lending strategies are in place.

In the fiscal 2016 on-site examinations, the Bank will examine the following: (1) whether financial institutions properly conduct credit screening of borrowing firms based on sufficient research and analysis of the business conditions of these firms; (2) whether financial institutions have developed follow-up monitoring frameworks to promptly grasp changes in the creditworthiness of borrowing firms; and (3), in particular, whether financial institutions have a deep understanding of the current conditions of large-risk borrowers and take proper measures in credit risk management. In addition, with regard to the business sectors and regions in which financial institutions are easing their lending stances, including sectors related to real estate as well as medical and nursing care, the Bank will examine (4) whether financial institutions properly assess the viability of borrowing firms' business in conducting credit screening and management, taking account of such factors as lending periods and the business characteristics, and (5) whether they conduct an institutional review of the profitability of such efforts.

Support for Enhancing the Vitality of Firms

Financial institutions are expected to contribute to enhancing the vitality of firms by continuously supporting borrowing firms' efforts to resolve their management challenges.

In the fiscal 2016 on-site examinations, the Bank will examine (1) whether financial institutions adequately analyze the current business conditions and future prospects of the borrowing firms and share an awareness of the management challenges concerning the borrowers, and (2) whether financial institutions offer advice, recommendations, and necessary support to help borrowers overcome challenges including fostering of growth businesses and reforming of business structures. Furthermore, the Bank will examine, with regard to borrowers with unstable business conditions, (3) whether financial institutions take initiatives toward more drastic solutions for management challenges by cooperating with other financial institutions and outside specialists, and (4) whether credit risk management measures are carried out as appropriate.

Strengthening the Management of Large Exposures/Concentration Risk

Financial institutions' equity capital and profits may be significantly affected by a worsening of the business conditions of large-lot borrowers, or by the materialization of risks in their credit portfolios with common risk characteristics. For this reason, financial institutions need to properly grasp and control large exposures/concentration risk inherent in their credit portfolios. In particular, as major financial institutions have been actively engaged in efforts such as M&A-related businesses, overseas resource development, and project financing -- including the provision of commitment lines -- in recent years, it has become increasingly important to manage large exposures/concentration risk.

In the fiscal 2016 on-site examinations, the Bank will examine the following in particular: (1) whether financial institutions properly grasp the status of large exposures/concentration risk, using measures such as stress testing, and (2) whether financial institutions have developed frameworks to control large exposures/concentration risk taking into account their equity capital, etc. while ensuring their effectiveness.

Strengthening the Management of Credit Exposure with Respect to Overseas Businesses

Major financial institutions are making efforts to expand their overseas businesses to support the global expansion of Japanese companies' activities and to capture the financial needs in other countries. Some regional financial institutions have increased credit to their existing customers taking into account the business expansion of these customers' overseas subsidiaries. In this context, it has become increasingly important for financial institutions to manage credit exposures with respect to overseas businesses.

In the fiscal 2016 on-site examinations of major financial institutions with large overseas exposures, the Bank will (1) conduct an in-depth examination on the quality of overseas exposures by examining the institutions' self-assessment of their exposures. It also will examine the following: (2) whether financial institutions have put in place an adequate framework for credit screening and management for areas on which they focus -- such as cross-border M&A-related and overseas resource development -- and for the management of large exposures, mainly to non-Japanese firms, considering the differences in legislations and infrastructure depending on the country and the country risk; (3) whether financial institutions' headquarters have set out rules for credit risk management including reporting procedures that apply on a global basis and appropriately monitor the status of compliance with such rules; and (4) whether the headquarters adequately review credit risk-taking policies on a global basis by making use of stress testing. The Bank will check whether regional financial institutions comprehend the business conditions of borrowing firms that have major overseas businesses.

c. Market Risk Management

Adequate Involvement of the Board of Directors in Market Risk Management

The board of directors needs to be adequately involved in developing risk-taking policies and risk management frameworks, examining the investment situation. In this regard, it is important to be accurately aware of market risk associated with securities portfolios and off-balance transactions, and to ensure the optimal balance between equity capital and risks.

In the fiscal 2016 on-site examinations, the Bank will examine the following: (1) whether the board of directors has clearly set out risk-taking policies, thereby having investment plans formulated in view of the optimal balance between equity capital and risks; (2) whether the board of directors has developed risk management frameworks in accordance with these policies and plans and reviews the frameworks as appropriate; and (3) whether the board of directors holds discussions and reaches adequate decisions in a timely and appropriate manner based on reports on market developments and risks in the event of abrupt changes in the financial and economic conditions.

Conduct of Risk Management Compatible with Investment Strategies and Methods

The targets and methods of market risk management need to be in line with the risk profiles of the securities portfolios and off-balance transactions and investment methods.

In the fiscal 2016 on-site examinations, the Bank will examine the following: (1) whether financial institutions appropriately identify and analyze risks, by looking at risk factors involved in their securities and portfolios as a whole, including the risks of individual financial products and transactions such as their credit risk, foreign exchange risk, and stock price risk, in addition to interest rate risk; (2) whether risk management division properly monitors the market prices of securities, the amount of risk associated with securities holdings, and observance of various limits in accordance with the risk characteristics and investment methods; and (3) whether the adequacy and limitations of the risk measuring methods are examined regularly through, for example, the conduct of back testing, and necessary measures are taken. In doing so, the Bank also will examine as necessary (4) whether frameworks of risk management function effectively in each phase of the stress scenarios.

In recent years, major financial institutions, among others, have announced a scheduled reduction of strategic stockholdings in their basic approach to corporate governance.

In the fiscal 2016 on-site examinations, the Bank will examine specific policies on reductions and status of implementations, in accordance with the risk posed by strategic stockholdings to equity capital.

d. Liquidity Risk Management

Liquidity Risk Management Based on Risk Profiles

To ensure stable liquidity management, it is necessary for financial institutions to (1) properly grasp the liquidity risk profiles associated with funding and investment portfolios, (2) set risk limits in accordance with their funding capability, (3) establish a framework for monitoring and controlling risks to observe the limits, and (4) understand the funding conditions including their funding bases, markets, and their own ratings and stock price changes in normal times while establishing a framework to respond promptly to changes in the environment by ensuring sufficient liquidity reserves for emergencies.

In the fiscal 2016 on-site examinations, the Bank will examine the situation of liquidity risk management, including that of foreign currency, from the above-mentioned standpoint.

Ensuring the Effectiveness of Global Liquidity Risk Management

It is important for internationally active financial institutions to implement appropriate management of foreign currency liquidity risks, including local currency risks, as well as enhance stable funding bases, at their overseas branches and at their financial groups as a whole.

In the fiscal 2016 on-site examinations, the Bank will examine the following, taking into account the recent rise in foreign currency funding costs: (1) whether financial institutions appropriately and in a timely manner grasp the current and prospective funding conditions in terms of different currencies and locations, ensuring smooth communication between the headquarters and each overseas branch, and (2) whether they disperse and diversify, across their financial groups as a whole, funding sources for the stable procurement of foreign currencies and review this dispersion and diversification carefully. The Bank also will examine the sufficiency of stress testing and the effectiveness of liquidity contingency plans, as responses to stress, including (3) whether the conduct of stress testing is consistent across their financial group and (4) whether financial institutions assume specific amounts of foreign currency outflow with the lapse of time, secure funding tools, and conduct an institutional review of their appropriateness.

e. Operational Risk Management[5]

Ensuring the Effectiveness of Proactive Risk Management Cycles

The operational risks inherent in the business processing of financial institutions may be diverse. In such a context, financial institutions need to identify the operational risks, focusing on those involving greater losses and impacts on business management in the event of the materialization of risk, and establish a management framework. In this regard, it also is necessary to make further improvements while verifying the effectiveness of the measures taken.

In the fiscal 2016 on-site examinations, the Bank will examine (1) stability of the business processing and target operations that involve greater losses and impacts on business management in the event of the materialization of risk. It also will examine whether financial institutions identify risk management issues through a survey of the processing of operations and analysis of fraud and accidents, and take effective remedial steps against such events. The Bank also will examine (2) whether financial institutions recognize changes in their risk profiles through changes in the surrounding environment, their business reprocessing, and expansion into new business areas, and then review their management frameworks.

Establishment and Strengthening of IT Risk Management Frameworks

To ensure the reliability and security of IT systems, financial institutions need to ensure the effectiveness of (1) measures to prevent IT system failures and recovery frameworks in the event of a failure, (2) project management, (3) information security management, and (4) management of contractors.

[5] In on-site examinations, operational risk refers to risks related to overall business operations, including, for example, risks related to business procedures, compliance, IT systems, and business continuity.

In the fiscal 2016 on-site examinations, the Bank will examine the above-mentioned points covering critical IT systems. In this regard, it also will examine, with regard to information security management and the management of providers of outsourced services, whether financial institutions have secured the effectiveness of management frameworks for confidential information about customers, for example.

Establishment and Strengthening of Cyber Security Management Frameworks

Ensuring cyber security is important in providing financial services utilizing IT.

In the fiscal 2016 on-site examinations, the Bank will examine measures to prevent cyber attacks and limit damage caused by such attacks on critical systems and external networks connected to these systems, taking into account individual financial institutions' businesses and presence in the payment and settlement systems. Specifically, the Bank will examine (1) whether financial institutions have taken measures to prevent/detect such attacks and (2) whether financial institutions have established frameworks and contingency plans in preparation for the occurrence of cyber incidents. In doing so, the Bank also will examine (3) whether financial institutions are collecting and sharing cyber security information, including external information, and (4) whether the board of directors is appropriately involved in establishing and operating these management frameworks, including the allocation of necessary business resources.

Strengthening of Business Continuity Management and Enhancement of Its Effectiveness

The development of effective business continuity management is important to ensuring individual financial institutions' critical operations, as well as the smooth functioning of the payment and settlement systems in Japan.

In the fiscal 2016 on-site examinations, the Bank will examine, taking account of each financial institution's types of business, as well as its presence in payment and settlement systems and in their respective regions, (1) the sufficiency and consistency of business continuity plans, (2) the securing of business resources such as staff, workplaces, and IT systems, and (3) the effectiveness of business continuity management through training. The Bank also will examine (4) whether business continuity management is reviewed properly based on environmental changes or other relevant factors.

(3) On-Site Examination Management

The basic approach of the Bank's on-site examinations is to intensively and comprehensively investigate and assess, through on-site visits over a period of about three weeks, the business conditions and risk management frameworks of financial institutions. In this regard, the Bank will continue to conduct "risk-based on-site examinations," which have been implemented since fiscal 2008, from the perspective of taking measures in a flexible and effective manner based on the risk conditions of financial institutions. The frequency, length, and scope of such examinations, as well as the number of examiners involved, will be determined on the basis of a comprehensive assessment from two perspectives: (1) the impact on the financial system of the materialization of risks for a particular financial institution and (2) the financial soundness of the financial institution, such as its financial bases and the degree of risk taking. In fiscal 2016, the Bank will step up its efforts to significantly improve the efficiency of on-site examinations. In this regard, the Bank will conduct the assessment of assets and field work for domestic branches in a more prioritized manner.

With regard to financial institutions that provide a wide range of financial services through group entities, the Bank will endeavor to grasp their relationships with major group companies and the actual business conditions of the group as a whole. Moreover, it will enhance its on-site examinations of overseas branches through means including more specific field work, given the increased weight of international businesses.

To further enhance the effectiveness of on-site examinations, the Bank, when necessary, will interview examinee institutions' internal auditors to grasp the institutions' risk profiles and other facts before visiting their premises. It also will continue to strengthen the linkage between its on-site examinations and off-site monitoring. In addition, the Bank aims to share its awareness and strengthen cooperation with overseas regulators, mainly on issues common to internationally active financial institutions.

The Bank will work to enhance its communication with examinee institutions and continue to take appropriate actions to gain their full understanding of and trust in the examination process and results. In the above process, the Bank will improve on-site examination procedures by responding to opinions and requests gathered from examinee institutions through a post-examination survey.

(Appendix)

Major Risk Management Issues Observed in the Fiscal 2015 On-Site Examinations

1. Business Management

Ensuring the Effectiveness of Internal Control

Some financial institutions did not have a sufficient grasp of actual business conditions for the operations of their subsidiaries, including overseas entities.

Proactive Improvement of Risk Management with Internal Audits

Some financial institutions needed to improve their implementation of audits taking account of their risk profiles and audits of highly professional risk fields at their headquarters. In addition, some financial institutions did not implement sufficient improvements based on the audit results.

Business Management Based on an Optimal Balance between Profitability/Equity Capital and Risk Taking

Some major financial institutions needed to improve their stress testing and study of countermeasures based on risk profiles and business strategies.

Some regional financial institutions needed to gain a better grasp of the impact of changes in their asset/liability and interest rates on profitability/equity capital, particularly through their ALM. In addition, while many regional financial institutions are concerned about declines in the sizes of their customer bases in the longer term, only some of them are conducting detailed/quantitative analyses of their future asset/liability and income/expense profiles and considering appropriate responses.

Development of Management Information Systems

Some financial institutions needed more sufficient frameworks to set up a management information system.

2. Credit Risk Management

Appropriate Credit Screening and Monitoring, and Establishment of a Framework Compatible with Lending Strategies

Some financial institutions needed to improve their screening/monitoring taking into account the prolonged credit period and business characteristics, as well as their comprehension of the current conditions of borrowers, while (1) promoting loans to real estate leasing, as well as medical and nursing care, and (2) increasing loans to firms categorized in the lower "normal" category or in the "need attention" category. In addition, (3) some financial institutions needed to improve their monitoring and analysis of portfolios while focusing on increasing housing loans.

Support for Enhancing the Vitality of Firms

With regard to support for enhancing the vitality of firms, some financial institutions needed to take initiatives toward more drastic solutions for borrowers with unstable business conditions.

Strengthening the Management of Large Exposures/Concentration Risk

While financial institutions maintained an active lending stance, some were moving toward larger or concentrated credit exposures. Under these circumstances, some financial institutions needed to deepen their understanding of the current business conditions of large-lot borrowers and enhance organized discussions to deal with them. Some financial institutions needed to improve their comprehension of concentration risk.

Strengthening the Management of Credit Exposure with Respect to Overseas Businesses

While financial institutions were actively extending overseas loans, some needed to improve their credit screening/monitoring of non-Japanese companies. Some financial institutions needed to improve their comprehension of current business conditions of their borrowing firms' overseas subsidiaries, including their financial situation.

3. Market Risk Management

Adequate Involvement of the Board of Directors in Market Risk Management

When developing and changing their investment plans, some financial institutions needed to increase involvement of their boards of directors for risk verifications based on equity capital. In addition, some financial institutions needed to more adequately develop and review their risk management frameworks in accordance with their risk-taking policies.

Conduct of Risk Management Compatible with Investment Strategies and Methods

While making more active investments in markets, including those denominated in foreign currencies, some financial institutions needed to improve their identification and monitoring of risks in accordance with new investments. In addition, some needed to improve their understanding of the impact of stress events on their future profits.

4. Liquidity Risk Management

Ensuring the Effectiveness of Global Liquidity Risk Management

Some internationally active financial institutions needed to improve their institutional reviews of possible foreign currency funding under stress and management frameworks for funding by currencies. In addition, some regional financial institutions needed to improve in particular their business reports on foreign currency liquidity risks and reviews on the stability of foreign currency funding. Furthermore, some Japanese branches of overseas G-SIFIs needed to improve their understanding of funding in yen for the whole group.

5. Operational Risk Management

Ensuring the Effectiveness of Proactive Risk Management Cycles

Some financial institutions needed to improve their identification of key risks through comprehension of the actual business operation situations and ensuring the effectiveness of measures to prevent accidents and other such incidents from reoccurring. In addition, some financial institutions needed to improve the development and review of their management framework according to changes in business processing as a result of enhanced business promotion and management streamlining, management of customer information, or management of transactions with antisocial forces.

Establishment and Strengthening of IT Risk Management Frameworks

Some financial institutions did not have a sufficient grasp of actual business conditions or a sufficient risk assessment with regard to system-related operations, including providers of outsourced services and overseas branches, and needed to improve risk control over leakage of important information. In addition, some financial institutions needed to improve their management of cyber security, particularly against unauthorized access by outsiders.

Strengthening of Business Continuity Management and Enhancement of Its Effectiveness

Some financial institutions needed to improve the effectiveness of their business continuity management through sufficient and consistent business continuity plans, securing business resources such as necessary staff for business continuation, and enhancing the content of their training.