

The Implementation of the BASEL III guidelines in Japan

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The logo for Bingham, consisting of the word "BINGHAM" in a bold, orange, sans-serif font. A thin vertical orange line extends downwards from the center of the letter "M".

I. Japanese BASEL III Framework: Summary

- Japan has implemented and will implement the Basel guidelines in order to cooperate with global efforts to maintain financial stability.
- The implementation of the Basel III guidelines in Japan complies with the international schedule; the Japanese Basel III framework applicable to internationally active banks (“**IAB**”) (“**International Standard**“) is effective from March 31, 2013 .
- As for domestic banks (“**DB**”), the Financial Services Agency of Japan (the “**JFSA**”) provided a slightly modified version of Basel III (“**Domestic Standard**“) taking into consideration their locally-based activities.
- Japanese Basel III for DBs is effective from March 31, 2014.

II. Definition of IAB and DB

- Internationally active banks (“**IAB**”) are defined as “those having a foreign branch or a foreign subsidiary”.
- International Standard is applicable to IABs.

- Domestic banks (“**DB**”) are defined as “those not having a foreign branch or a foreign subsidiary”.
- Domestic Standard is applicable to DBs.

III. Minimum Capital Requirement in Japan: Summary

International Standard

Basel 2

$$\frac{\text{Total Equity Capital (Tier 1+ Tier 2)}}{\text{Risk Asset}} \geq 8 \%$$



Basel 3

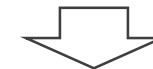
$$\frac{\text{Common Equity Tier 1 Capital}}{\text{Risk Asset}} \geq 4.5\% \text{ (minimum level)}$$

$$\frac{\text{Total Equity Capital (Tier 1+ Tier 2)}}{\text{Risk Asset}} \geq 8 \%$$

Domestic Standard

Basel 2

$$\frac{\text{Total Equity Capital (Tier 1+ Tier 2)}}{\text{Risk Asset}} \geq 4 \%$$



New Domestic Standard

$$\frac{\text{Core Capital} \times}{\text{Risk Asset}} \geq 4 \%$$

\times Core Capital = Common Equity + Retained Earnings
 + Preferred Stock with Mandatory Convertible provision
 +/- Adjustment · Deduction

IV. List of IABs and DBs: Summary

Internationally Active Banks and Domestic Banks (As of March 2014)	
Internationally Active Banks (IABs)	Domestic Banks (DBs)
1. Major Banks	
<ul style="list-style-type: none"> - The Bank of Tokyo-Mitsubishi UFJ, Ltd. - Sumitomo Mitsui Banking Corporation - Mizuho Bank, Ltd. 	<ul style="list-style-type: none"> - Resona Bank, Ltd. - Shinsei Bank, Limited - Aozora Bank, Ltd.
2. Trust Banks	
<ul style="list-style-type: none"> - Mitsubishi UFJ Trust and Banking Corporation - Sumitomo Mitsui Trust Bank, Limited - Mizuho Trust & Banking Co., Ltd. 	<ul style="list-style-type: none"> - The Nomura Trust and Banking Co., Ltd. Others, 13 banks in total
3. Local Banks	
<p>The Gunma Bank, Ltd., The Chiba Bank, Ltd., The Bank of Yokohama, Ltd., The Hachijuni Bank, Ltd., The Shizuoka Bank, Ltd., The Shiga Bank, Ltd., The Chugoku Bank, Ltd., The Yamaguchi Bank, Ltd., The Iyo Bank, Ltd., The Bank of Nagoya, Ltd.</p>	<ul style="list-style-type: none"> - The Joyo Bank, Ltd. - The Bank of Fukuoka, Ltd. - Saitama Resona Bank, Ltd. Others, 106 banks in total

V. Basel III regulatory consistency assessment (Level 2) Japan (1): Summary

- Reviewing the level of implementation of Basel III in Japan, the Basel Committee published the above titled report (the “**Basel III Japan Assessment**”) to make public its assessment up to October 2012.
- In the Basel III Japan Assessment, the Basel Committee gave Japan rankings of “Grade 3”, and “Compliant” or “Largely Compliant” in each detailed finding.

V. Basel III regulatory consistency assessment (Level 2) Japan (2): IAB/DB Issue

- Basel regulations do not provide any specific definition of internationally active banks.
- Generally speaking, the definition of an internationally active bank as “a bank that has overseas business locations” may seem in contradiction with the spirit of the Basel agreement because a purely domestic bank with no establishment abroad may still compete with foreign banks in foreign markets.
- However, in the case of Japan, the impact of this rather restrictive definition is not material, at least for now, as banks with noteworthy overseas operations are the internationally active banks with at least one subsidiary or branch abroad.

VI. Domestic Standard: Definition of “Core Capital”

- The total regulatory capital applicable to DBs is defined as “Core Capital”, which is an original concept in Japan.
- The basic elements and the condition to include such elements into Core Capital are more limited and restricted than the sum of Tier 1 and Tier 2 Capital.
- The framework of regulatory adjustment applicable to DBs harmonises with Basel III standards and International Standards.

VII. Impact of Basel III Implementation in Japan (1): Summary

1. Minimum capital requirements

It is generally believed that both IABs and DBs will likely satisfy applicable requirements, though some banks may have to struggle to meet the requirements.

2. Leverage ratio

According to a trial calculation by Mizuho Securities in March 2011, Japanese mega banks exceeded the requirements for leverage ratio under Basel III.

VII. Impact of Basel III Implementation in Japan (1): Summary

3. Counter Cyclical Capital Buffer and Capital Conservation Buffer

Japanese banks would be required to conduct further efforts:

- to increase profitability of banking business; and
- to reduce regulatory adjustments to Tier 1 or Tier 2 and/or high RWAs (which could have relatively high returns), and to achieve a reasonable balance between them.

VII. Impact of Basel III Implementation in Japan (2): Internationally Active Banks (IABs)

- It was anticipated that the ratio of regulatory adjustments to Common Equity Tier 1 deducted due to double gearing would be relatively high.
- However, the three mega banks announced in November 2012 that they expected to satisfy the minimum capital requirements of Basel III mainly due to the following reasons:
 - Japanese banks have invested in JGBs (Japanese Government Bonds) to reduce their RWAs; and
 - Japanese banks have increased their profits in the last few years.

VII. Impact of Basel III Implementation in Japan (3): Domestic Banks (DBs)

- There was a concern as to whether the international minimum requirements would be directly applied to DBs.
- However, it was determined that the 4% minimum capital ratio is to be kept.
- It is anticipated that DBs could satisfy the requirements due to the longer period of transitional arrangements.

Questions?

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