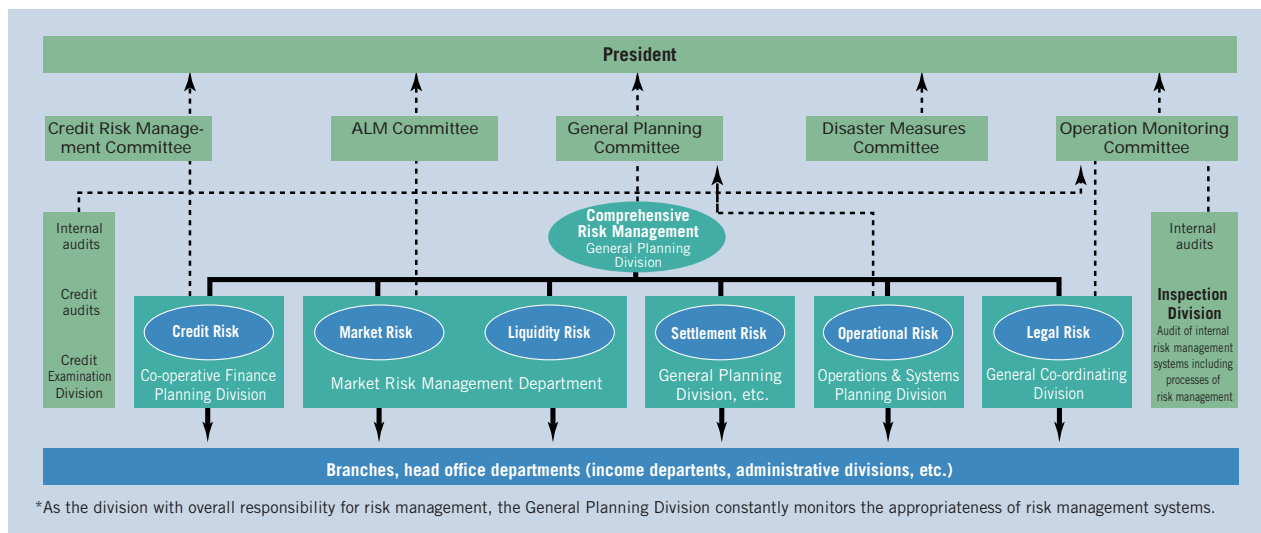


Risk Management

Financial institutions have been exposed to considerably diverse and complex risk factors such as credit risk, market risk, liquidity risk, and operational risk. The situation reflects liberalization and internationalization of the financial sector, and advances in financial technology. It is critical for financial institutions to manage these risks appropriately in order to maintain their financial soundness while responding to the increasingly diverse and sophisticated needs of their customers.

The Shoko Chukin Bank has strengthened its risk management systems by establishing departments responsible for the management of specific types of risk. Overall risk management is provided by the General Planning Division, which constantly monitors the other departments to ensure that risk management procedures are being implemented properly. The result is a robust and comprehensive risk management structure that provides total monitoring of the Bank's risk exposure.

Financial Institutions for SMEs in Japan



Definitions of Risk

Credit Risk

The risk of losses due to the reduction or elimination of asset value due to such factors as deterioration in the financial position of the borrower.

Market Risk

The risk of losses resulting from fluctuations in asset values due to shifts in interest rates, exchange rates, or the prices of securities.

Liquidity Risk

The risk that cash flows will become insufficient due to the inability to secure the required funds (cash flow risk), and the risk that market transactions will become impossible due to market disruptions (market liquidity risk)

Settlement Risk

The risk of losses resulting from failure to settle by the due date (categorized into credit risk, liquidity risk, operational

risk and legal risk, according to cause and characteristics of the problem).

Operational Risk

Operational risks are the risk of losses by financial institutions resulting from a failure, accident or fraud of management or staff (administrative risk), the risk of losses by financial institutions due to computer system failures, errors, and inadequacies (system risk), and the risk of losses due to serious threats (leaks, fraudulent use, erroneous operations, and deliberate acts) to the validity and reliability of essential information assets (information security risk).

Legal Risk

The risk of losses resulting from legal uncertainty about transactions or failure to comply with laws and regulations.

Credit Risk Management

The Shoko Chukin Bank bases its credit risk systems on expertise gained through many years of experience in working with SMEs. It is working to maintain and improve the quality of its loan assets by setting appropriate lending criteria and by ensuring that screening systems are properly applied.

Individual loan applications are screened under various criteria, such as the appropriateness of business and financial plans, repayment prospects, and collateral, as well as the future potential of the enterprise concerned. Each proposal is considered from a comprehensive range of perspectives, including the business and financial situations of customers, the quality of their management, and the level of their technological skills.

Lending to venture businesses, is subject to screening by the New Business Screening Committee. The Committee consists of outside members with industry expertise and the Bank's staff members who have skills in evaluating technology and knowledge in a specific industry.

Furthermore, the Shoko Chukin Bank uses self-assessment procedures to control and monitor credit risk. It has also introduced a 10-tier credit system based on its self-assessment criteria. This highly detailed system allows the Bank to assess the creditworthiness of SMEs using the most appropriate set of financial indicators selected from the many indicators available. The Shoko Chukin Bank's extensive experience of lending to SMEs is reflected in the system, which is designed to eliminate arbitrary decision-making by basing qualitative assessment on a uniform scoring system.

Credit screening is carried out by the Credit Group, which consists of Credit Divisions I, II and III and the Credit Data Monitoring Department. To ensure appropriate screening and control, the credit screening organization is completely independent from business divisions. The Shoko Chukin Bank is constantly working to maintain and improve the quality of loan assets.

Overall credit risk management is coordinated by

the Co-operative Finance Planning Division, which monitors credit screening and credit portfolios and works to enhance credit risk systems. At senior management level, the Credit Risk Management Committee analyzes credit portfolios from various perspectives, including creditworthiness and industry sectors. The aim of this committee is to maintain and improve the soundness of assets, mainly by distributing risk.

Employee training programs are designed to hone the credit screening skills of all staff at different levels.

Market Risk Management

Advances in financial technology and the expansion of market transactions have increased the exposure of financial institutions to a variety of market risks, including fluctuations in interest rates, exchange rates and share prices.

The Shoko Chukin Bank's approach to risk management in this area is defined in the Basic Policy on Market Risk Management. This policy defines the organizational structures, commissions, and managing methods as it relates to the management of market and liquidity risk. This risk management structure complies with guidelines published by the Japanese financial authorities and with the Accounting Standards for Financial Instruments, also known as market price accounting.

Asset and Liability Management (ALM)

The Shoko Chukin Bank uses funds raised primarily through long-term fixed-interest loans and 5-year interest-bearing debentures to provide a variety of financing services. Discrepancy between the terms over which funds are raised and invested causes an interest rate risk.

To maintain reasonable levels of revenue while managing these risks appropriately, the Shoko Chukin Bank uses a variety of asset and liability management (ALM) techniques. Assets and liabilities are analyzed from various perspectives, and swaps and other instruments are used to ensure integrated management of both on-and off-balance-sheet assets and liabilities.

The ALM Committee, consisted of senior management, hold a meeting every month to set policies to control the level of risk while gaining profit. The Committee takes into account the state of the economic and financial environment, the interest rate outlook, and the overall level of market risk affecting the Bank's on- and off-balance-sheet transactions.

1. Delta Analysis

This method provides an integrated measurement of interest rate risk in terms of changes in asset and liability values resulting from interest rate volatility. (Delta* = 10 basis point value)

*Delta analysis can also be used to monitor interest rate risk for each calculation period on the basis of grid point sensitivity.

2. Simulation Analyses

The Shoko Chukin Bank monitors medium-term period losses and gains and trends in the market values of assets and liabilities by combining its plans for the procurement of funds through loans, debentures and other means, and interest rate forecasting scenarios.

Market Business Operations

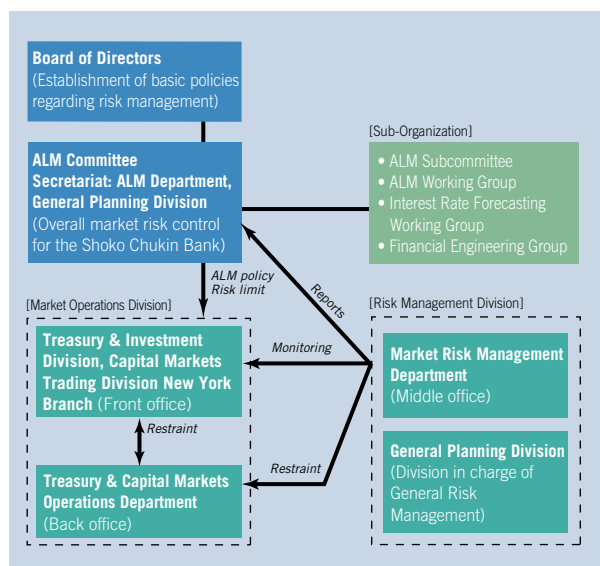
Market operations, including derivative transactions, are critical to control ALM risk and provide various financial

services to customers. Market operations are classified as banking operations and trading operations under the Bank's basic market risk management policy. The ALM Committee set the limit of risk capability for banking operations and the maximum loss allowed for trading operations. The committee monitors operations on a regular basis to ensure that these policies are being complied with properly. The Shoko Chukin Bank uses trading operations primarily to meet the market transaction needs of its customers.

The Shoko Chukin Bank has established a reciprocal checking system between front office departments, which are responsible for implementing transactions, and back office departments, which handle administrative tasks. In March 1998, the Bank further strengthened the risk management structure by establishing the Market Risk Management Department, a specialized department responsible for a "middle office" role.

The Market Risk Management Department monitors, quantifies and manages market risk using integrated risk management indicators, including delta and value at risk. In addition, it constantly monitors operations to ensure that the risk limits established by the ALM Committee are being complied with properly. The Department reports to senior management on a regular basis.

Management Systems for ALM and Market-related Risk



Managing Operational Risk

Operational risk is defined as administrative risk, system risk, and information security risk. The Operations & Systems Planning Division is responsible for managing and minimizing operational risk.

The Shoko Chukin Bank is making efforts to reduce administrative risk by introducing automated processing for the increasingly diverse range of products handled, and by using sophisticated auditing systems. It also provides in-depth employee education.

System risk is managed through efforts to ensure the stable operation of computer systems. Countermeasures include system redundancy, the establishment of back-up centers, and the implementation of breakdown drills.

The Shoko Chukin Bank has set a basic policy, specific criteria and administrative procedures concerning countermeasures against information security risk. To ensure an appropriate response, risk is classified based on such factors as importance of specific information assets, both information itself and information systems.

The Bank's contingency plans set clear operational priorities for the safety of customers and employees in the event of a disaster or other emergency.

Improving Internal Auditing Systems

The importance of internal control systems to avoid losses is increasing with the growing complexity and sophistication of financial transactions. Internal auditing systems are also an effective way to ensure that operations are being implemented efficiently and effectively in accordance with the directions set by management. The Credit Examination Division and the Inspection Division, which operate independently of all other head office sections, are in charge of conducting internal auditing and monitoring the Bank's internal management systems.

The Inspection Division verifies the effectiveness of internal management systems by inspecting the operations of branches and head office departments, and by auditing computer-related systems. These inspections cover a number of perspectives, including compliance with laws and internal regulations, the effectiveness of reciprocal checking systems based on internal inspections at the department and branch levels, and the adaptation of internal rules to environmental change. The aim of these inspections is to improve operations and prevent problems.

The task of the Credit Examination Division is to audit credit management procedures to ensure that self-assessment is being applied properly, and that credit ratings are accurate.

In fiscal 2000, the Shoko Chukin Bank established the Operation Auditing Committee. Its task is to discuss measures to improve operations and ensure compliance, based on the results of these internal audits.

The Shoko Chukin Bank is not subject to the statutory audit requirements set down in the Securities and Exchange Law and the Commercial Code Special Exception Law. However, it has commissioned the Chuo Aoyama Audit Corporation to audit its self-assessment of loans and other assets and its accounting procedures for financial instruments.

Compliance Systems

As a policy-based financial institution, the Shoko Chukin Bank fulfills an important role in society and has a special obligation to earn the confidence of the public by carrying out its activities fairly and appropriately. The Bank's operations must comply with all laws, regulations and rules. It ensures accountability by disclosing information and maintaining a high standard of transparency in its operations.

Reinforcement of compliance systems is an ongoing priority for the Shoko Chukin Bank. For example, the Bank has developed a solicitation policy based on the Law Concerning the Sale of Financial Products, which took effect in April 2001. It has also established procurement systems that comply with the Law Concerning the Promotion of Procurement of Environment-Friendly Products by the Government, which became fully effective in April 2001.

The Meaning of Compliance

The meaning of "compliance" indicates not only strict observance of laws, regulations and rules, but also conformance with accepted social norms.

Promoting Awareness of the Importance of Compliance

The Shoko Chukin Bank is working to increase awareness of the importance of compliance among its management and staff. For example, the president regularly emphasizes the Bank's commitment to full compliance at branch manager meetings.