

ECONOMIC AND FINANCIAL CONDITIONS

During Fiscal 2007, ended March 31, 2008, the ongoing global economic recovery was marred by signs that a slowdown was gaining ground. While the Chinese economy and other new economies continued to expand, the U.S. and European economies slowed through the second half of the fiscal year in response to the chaos in the financial markets triggered by the subprime loan problem.

The Japanese economy continued to enjoy a modest recovery, but in reaction to these global economic developments, it increasingly slowed through the second half of the fiscal year. The upturn in exports stalled somewhat, particular for exports to the United States, and industrial production lost its upward momentum and fell flat. Capital investment also softened on growing concerns over the economic outlook. After a sharp fall after the revised Building Standards Law took effect, housing investment showed signs of recovering, but then remained low. In the household sector, personal spending remained steady overall, attributable to modest improvements in the employment and income environment. During this period, consumer price growth expanded on the back of a jump in the price of raw materials such as crude oil and grains.

Economic sentiment continued to deteriorate for small and medium-sized enterprises (SMEs), and conditions became increasingly difficult for some industries relying on domestic demand. According to the Shoko Chukin Bank's "Monthly Survey of SME Business Sentiment," sales remained on an uptrend, but there were signs in some areas that demand had peaked. Moreover, the rise in input prices resulting from skyrocketing raw material prices was not fully passed on to sales prices, which continued to pressure profits. The SME Business Sentiment Index undercut the boom-or-bust threshold of 50 throughout the fiscal year. Given these conditions, the number of SME bankruptcies continued to increase.

On the financial front, the Bank of Japan (BOJ) held its policy rate steady in Fiscal 2007 in light of the chaos buffeting financial markets since summer and the heightened uncertainty over the economy's outlook. Long-term interest rates (newly issued 10-year Japanese government bond yields) rose to the mid 1.9% range at one point on heightened expectations in summer 2007 that the BOJ would raise policy rates. However, yields subsequently dropped and fell to around 1.3% at the end of the fiscal year.

The yen weakened against the dollar in summer 2007 as US long-term interest rates rose. However, the yen began to appreciate thereafter as investors unwound their yen carry trades, and in March 2008 the exchange rate briefly touched the ¥95/USD rate, the highest level in more than 12 years.

Stock prices rose from the start of the fiscal year through the summer, and set new highs for the year in early July. However, subsequently the stock market began to drop on growing concerns of a credit crunch in the U.S. financial market and worries that the strong yen would hurt corporate earnings, pushing the Nikkei Stock Average below the ¥12,000 range at one point in March 2008.

During this period, the Japanese government worked to ensure a smooth flow of funds and promote diversification in funding sources for SMEs—specifically, financing methods that were not overly dependent on collateral and personal guarantees. In addition, the government continued to support new business development by SMEs utilizing local resources as well as SMEs in the manufacturing sector taking advantage of advanced technology.

SUMMARY OF RESULTS

Loans

The balance of outstanding loans as of the end of Fiscal 2007 declined ¥240.2 billion, to ¥9,114.9 billion at year-end. The balance of loans through agencies, including credit cooperatives, totaled ¥9.7 billion. There were 150 agencies at fiscal year-end.

Debentures

Interest-bearing debentures decreased ¥227.0 billion compared with the previous year and discount debentures decreased ¥179.9 billion, for an overall decrease in the balance of debentures of ¥407.0 billion. As a result, the balance of debentures at year-end totaled ¥6,821.9 billion, a figure that includes ¥30.0 billion underwritten by the government.

Deposits and Negotiable Certificates of Deposit

The balance of deposits increased ¥115.1 billion, to ¥2,655.0 billion at the end of Fiscal 2007. Negotiable certificates of deposit decreased ¥2.7 billion compared with the previous year-end, to ¥9.9 billion.

Securities

Over-the-counter sales of government bonds and other securities amounted to ¥0.5 billion. Dealings in government bonds and other securities totaled ¥52.9 billion. The balance of trading securities at the end of Fiscal 2007 was less than ¥100 million.

Domestic and Foreign Exchange

Domestic exchange transactions in Fiscal 2007 totaled ¥24,317.5 billion. Foreign exchange transactions totaled US\$4,275 million.

Income and Expenditures

Total operating income amounted to ¥209.4 billion, while operating expenses totaled ¥192.1 billion, resulting in income before income taxes and others of ¥17.2 billion. Other gains amounted to ¥0.3 billion and other losses totaled ¥3.7 billion. Provision for income taxes amounted to ¥0.3 billion, and adjustment for income taxes totaled ¥8.4 billion. As a result, net income for the fiscal year amounted to ¥21.8 billion.

Issues to Address

With the aim of reciprocating its clients' trust and actively contributing to the growth and development of SMEs, the Bank strives to ensure that SMEs have smooth access to financing. The Bank also believes in the importance of reinforcing its business structure.

Consequently, the Bank will provide a stable supply of funds based on a long-term transaction stance and will serve as a safety net to counteract changes in SMEs' financial and economic environment, and will further enhance its efforts to revitalize companies by utilizing diverse recovery methods through new methods and cooperation with external organizations. In addition, the Bank will help raise its clients' corporate value by providing high-quality solutions for their management problems. The Bank will actively endeavor to augment its fund-raising base and build a solid management foundation, and will ensure thorough compliance and raise the sophistication of its internal management system to improve customer satisfaction and solidify the trust it has earned from society and its clients ahead of the transition to the privatization.

