

Balance Sheet (as of March 31, 2011)

(Millions of yen)

	2011		2011
Assets		Liabilities	
Cash and due from banks	978,074	Borrowed money	5,502,495
Cash	0	Borrowings	5,502,495
Due from banks	978,074	Bonds payable	2,703,551
Securities	76,453	Other liabilities	71,181
Other securities	76,453	Accrued expenses	29,911
Loans and bills discounted	8,376,794	Unearned revenue	38,881
Loans on deeds	8,376,794	Derivatives other than for trading-liabilities	1,899
Other assets	1,001,457	Lease obligations	290
Prepaid expenses	234	Other	198
Accrued income	29,379	Provision for bonuses	465
Derivatives other than for trading-assets	966,988	Provision for directors' bonuses	6
Other	4,855	Provision for retirement benefits	12,135
Property, plant and equipment	37,664	Provision for directors' retirement benefits	28
Buildings	3,488	Acceptances and guarantees	2,443,266
Land	33,881	Total liabilities	10,733,129
Lease assets	58	Net assets	
Construction in progress	2	Capital stock	1,091,000
Other	233	Retained earnings	801,398
Intangible assets	2,349	Legal retained earnings	742,615
Software	2,116	Other retained earnings	58,783
Lease assets	218	Retained earnings brought forward	58,783
Other	14	Total shareholders' equity	1,892,398
Customers' liabilities for acceptances and guarantees	2,443,266	Valuation difference on available-for-sale securities	(1,665)
Allowance for loan losses	(134,417)	Deferred gains or losses on hedges	157,781
		Total valuation and translation adjustments	156,115
		Total net assets	2,048,513
Total assets	12,781,643	Total liabilities and net assets	12,781,643

Japan Finance Corporation
ACCOUNT FOR JBIC OPERATIONS

Statement of Operations (Year ended March 31, 2011)

(Millions of yen)

	2011
Ordinary income	197,217
Interest income	178,661
Interest on loans and discounts	122,329
Interest and dividends on securities	48
Interest on deposits with banks	1,199
Interest on interest swaps	55,061
Other interest income	22
Fees and commissions	13,183
Other fees and commissions	13,183
Other ordinary income	74
Other	74
Other income	5,298
Other	5,298
Ordinary expenses	147,576
Interest expenses	118,777
Interest on borrowings and rediscounts	55,696
Interest on bonds	63,081
Fees and commissions payments	1,332
Other fees and commissions	1,332
Other ordinary expenses	3,370
Loss on foreign exchange transactions	2,501
Amortization of bond issuance cost	651
Expenses on derivatives other than for trading or hedging	8
Other	209
General and administrative expenses	15,861
Other expenses	8,233
Written-off loans	8,232
Other	0
Ordinary profit	49,641
Extraordinary income	9,142
Gain on disposal of noncurrent assets	0
Reversal of allowance for loan losses	8,715
Recoveries of written-off claims	425
Extraordinary losses	0
Loss on disposal of noncurrent assets	0
Net income	58,783

Japan Finance Corporation
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Statement of Changes in Net Assets (Year ended March 31, 2011)

(Millions of yen)

	2011		2011
Shareholders' equity		Deferred gains or losses on hedges	
Capital stock		Balance at the end of previous period	140,795
Balance at the end of previous period	1,055,500	Changes of items during the period	
Changes of items during the period		Net changes of items other than shareholders' equity	16,985
Issuance of new shares	35,500	Total changes of items during the period	16,985
Total changes of items during the period	35,500	Balance at the end of current period	157,781
Balance at the end of current period	1,091,000	Total valuation and translation adjustments	
Retained earnings		Balance at the end of previous period	140,107
Legal retained earnings		Changes of items during the period	
Balance at the end of previous period	726,011	Net changes of items other than shareholders' equity	16,007
Changes of items during the period		Total changes of items during the period	16,007
Provision of legal retained earnings	16,603	Balance at the end of current period	156,115
Total changes of items during the period	16,603	Total net assets	
Balance at the end of current period	742,615	Balance at the end of previous period	1,954,826
Other retained earnings		Changes of items during the period	
Retained earnings brought forward		Issuance of new shares	35,500
Balance at the end of previous period	33,207	Payment to the national treasury	(16,603)
Changes of items during the period		Net income (loss)	58,783
Provision of legal retained earnings	(16,603)	Net changes of items other than shareholders' equity	16,007
Payment to the national treasury	(16,603)	Total changes of items during the period	93,687
Net income (loss)	58,783	Balance at the end of current period	2,048,513
Total changes of items during the period	25,575		
Balance at the end of current period	58,783		
Total retained earnings			
Balance at the end of previous period	759,218		

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Changes of items during the period	
Payment to the national treasury	(16,603)
Net income (loss)	58,783
Total changes of items during the period	42,179
Balance at the end of current period	801,398
Total shareholders' equity	
Balance at the end of previous period	1,814,718
Changes of items during the period	
Issuance of new shares	35,500
Payment to the national treasury	(16,603)
Net income (loss)	58,783
Total changes of items during the period	77,679
Balance at the end of current period	1,892,398
Valuation and translation adjustments	
Valuation difference on available-for-sale securities	
Balance at the end of previous period	(687)
Changes of items during the period	
Net changes of items other than shareholders' equity	(977)
Total changes of items during the period	(977)
Balance at the end of current period	(1,665)

Notes to Financial Statements

ACCOUNT FOR JBIC OPERATIONS

Amounts presented are rounded down to the nearest million yen.

1. Significant accounting policies

(a) Securities

Held-to-maturity securities are carried at amortized cost based on the moving average method. Investments in affiliates are carried at cost based on the moving average method. Available-for-sale securities, which have readily determinable fair value are stated at fair value with changes in net unrealized gains or losses, included directly in Net assets. Available-for-sale securities whose fair value is extremely difficult to be determined are carried at cost based on the moving average method.

(b) Valuation method for derivative financial instruments

Derivative financial instruments are carried at fair value.

(c) Depreciation basis for fixed assets

(i) Property, plant and equipment (except for lease assets)

Tangible fixed assets are depreciated under the declining-balance method over their useful economic lives except for buildings (excluding installed facilities) which are depreciated under the straight-line method.

Amortization is based on the following range of estimated useful lives:

Buildings: 2 years to 50 years

Other: 2 years to 20 years

(ii) Intangible assets (except for lease assets)

Amortization of intangible fixed assets is computed by the straight-line method. Software used by JFC is amortized over its useful life (5years).

(iii) Lease assets

Lease assets in “property, plant and equipment” or “intangible assets,” under finance leases that do not involve transfer of ownership to the lessee are amortized under the straight-line method over the lease term. Depreciation for lease assets is calculated with zero residual value being assigned to the asset.

(d) Method of amortization for deferred assets

Bond issuance costs are expensed as incurred.

(e) Foreign currency translation and revaluation method

JFC maintains its accounting records in Japanese yen. Assets and liabilities denominated in foreign currencies are mostly translated into Japanese yen at the market exchange rate prevailing at the fiscal year end.

(f) Accounting policy for reserves

(i) Allowance for loan losses

The allowance for loan losses is maintained in accordance with internally established standards.

The allowance for claims on debtors who are legally bankrupt (“Bankrupt borrowers”) or substantially bankrupt (“Substantially bankrupt borrowers”) is provided based on the outstanding balance after the write-offs described in the followings and the deductions of the amount expected to be collected through the disposal of collateral and execution of guarantees.

The allowance for claims on debtors who are not legally bankrupt but are likely to become bankrupt (“Potentially bankrupt borrowers”) is provided based on an assessment of the overall solvency of the debtors after deducting the amount expected to be collected through the disposal of collateral and the execution of guarantees.

The allowance for claims on debtors other than Bankrupt borrowers, Substantially bankrupt borrowers and Potentially bankrupt borrowers is provided primarily based on the default rate, which is calculated based on the actual defaults during a certain period in the past.

The allowance for possible losses on specific overseas loans is provided based on the expected loss amount taking into consideration the political and economic situations of these countries.

All claims are assessed initially by the operational departments and subsequently by risk evaluation departments based on internal rules for self-assessment of asset quality. The risk evaluation department, which is independent from the operational departments, reviews these self-assessments, and the allowance is provided based on the results of the assessments.

With respect to claims with collateral or guarantees on debtors who are legally or substantially bankrupt (Bankrupt borrowers and Substantially bankrupt borrowers), the residual booked amount of the claims after deduction of the amount which is deemed collectible through the disposal of collateral or the execution of guarantees is written-off. The amount of accumulated write-off is ¥8,232 million.

(ii) Provision for bonuses

The “provision for bonuses” is calculated and provided for based on the estimated amounts of future payments attributable to the services that have been rendered by employees to the date of the balance sheet.

(iii) Provision for directors’ bonuses

The “provision for directors’ bonuses” is calculated and provided for based on the estimated amounts of future payments attributable to the services that have been rendered by directors to the

date of the balance sheet.

(iv) Provision for retirement benefits

The “provision for retirement benefits” represents the future payment for pension and retirement benefits to employees, and is accrued based on the projected benefit obligations and the estimated pension plan assets at the fiscal period end.

Unrecognized prior service costs are recognized as income or expense by the straight-line method over a certain number of years; 10 years within the average remaining work period of employees at the year of occurrence.

Unrecognized actuarial differences are recognized as income or expense from the following fiscal year by the straight-line method over a period up to a maximum of 10 years within the average remaining service period of employees of the respective fiscal year.

(v) Provision for directors’ retirement benefits

The “provision for directors’ retirement benefits,” which provides for future retirement pension payments to directors, corporate auditors and executive officers, is recognized at the amount accrued at the end of the fiscal year.

(g) Accounting for hedging transactions

(i) Accounting for hedges of interest rate risk

(a) Hedge accounting

JFC used derivatives for interest rate risk hedging purposes under the deferral method.

(b) Hedging instruments and hedged items

Hedging instruments: interest rate swaps

Hedged items: loans, borrowings, bonds and notes

(c) Hedging policy

JFC enters into hedging transactions up to the amount of the underlying hedged assets and liabilities.

(d) Assessment of hedge effectiveness

JFC assesses the effectiveness of designated hedges by measuring and comparing the change of fair value or cumulative change of cash flows of both hedging instruments and corresponding hedged items from the date of inception of the hedges to the assessment date.

(ii) Accounting for hedges of foreign exchange risk

Hedge instruments used to hedge foreign exchange risks associated with various foreign currency denominated monetary assets and liabilities are accounted for using the deferral method, in accordance with the standard treatment of The Japanese Institute of Certified Public Accountants (JICPA) Industry Audit Committee Report No. 25.

The effectiveness of the hedging instruments described above, such as currency swaps, foreign

exchange forward contracts and similar transactions, used for hedging the foreign exchange risks of loans and bills discounted, borrowings, and bonds payable denominated in foreign currencies, is assessed by comparing the foreign currency position of the hedged loans and bills discounted, borrowings, and bonds payable with that of the hedging instruments. An asset and liability denominated in foreign currency for which currency swap is used to hedge the foreign currency fluctuations are translated at the contracted rate if the currency swap qualifies for hedge accounting.

(h) Consumption and other taxes

Consumption taxes and local consumption taxes (“consumption taxes”) are excluded from transaction amounts. Amounts of nondeductible consumption taxes related to property, plant and equipment are expensed as incurred.

Change in accounting policy

(Accounting standard for equity method of accounting for investments)

ASBJ Statement No. 16, Accounting Standard for Equity Method of Accounting for Investments, issued on March 10, 2008, and ASBJ Practical Issue Task Force (PITF) No. 24 Practical Solution on Unification of Accounting Policies Applied to Associates Accounted for Using the Equity Method, issued on March 10, 2008, have been adopted commencing with this fiscal year end.

(Accounting standard for asset retirement obligations)

ASBJ Statement No. 18, Accounting Standard for Asset Retirement Obligations, issued on March 31, 2008, and ASBJ Guidance No. 21, Guidance on Accounting Standard for Asset Retirement Obligations, issued on March 31, 2008, have been adopted commencing with this fiscal year end.

Note that this adoption does not have any impacts on income or expense.

2. Equity securities of or investment in affiliates

Equity securities of or investment in affiliates is ¥52,193 million.

3. Loans

All loans entered into are loans on deeds. The amounts reported in the balance sheet include the followings:

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(Millions of yen)

	As of March 31, 2011 Account for JBIC Operations
Bankrupt loans	8,969
Non-accrual loans	97,717
Loans with interest or principal repayments more than three months on arrears	—
Restructured loans	187,046
Total	293,733

(Note) The description of the following five accounts, Securitization Support Programs (Purchase-type operation), Credit Insurance Programs, Finance Operations for Facilitating Realignment of United States Forces in Japan, Operations to Facilitate Crisis Responses, and Operations to Facilitate Specific Business Promotion are omitted since there are no balance in these accounts.

- (a) “Bankrupt loans” are loans, defined in Article 96, Paragraph 1, Item 3 and 4 of the corporate Tax Law Enforcement Ordinance (Government Ordinance No. 97), on which accrued interest income is not recognized as there is substantial uncertainty over the ultimate collectability of either principal or interest because they have been in arrears for a considerable period of time or for other reasons.
- (b) “Non-accrual loans” are loans on which accrued interest income is not recognized, although this excludes Bankrupt loans and the loans on which interest payments are deferred in order to support the borrowers’ recovery from financial difficulties.
- (c) “Loans with interest or principal repayments more than three months in arrears” are loans whose principal or interest payment is more than three months in arrears, and which do not fall under the category of “Bankrupt loans” and “Non-accrual loans”
- (d) “Restructured loans” are loans whose repayment terms and conditions have been amended in favor of the borrowers (e.g. reduction of or exemption from the stated interest rate, the deferral of interest payments, the extension of principal repayments or renunciation of claims) in order to support the borrowers’ recovery from financial difficulties, and which do not fall under the category of “Bankrupt loans”, “Non-accrual loans”, and “Loans with interest or principal repayments more than three months in arrears”.
- (e) The amounts of loans indicated in the table above are the gross amounts prior to the deduction of allowance for possible loan losses.

JFC, as a policy, does not pay down loans in part or in full immediately after the execution of the loan agreements, but instead makes disbursement, in accordance with the progress of the underlying projects. These undisbursed amounts are not included in the loans on deed in the Balance Sheet. The balance of unpaid amounts as of March 31, 2011 is ¥875,019 million.

4. Assets pledged as collateral

Pursuant to Article 52 of the JFC Act, assets of JFC are pledged as general collateral for all bonds issued by JFC (which include JBIC Operating Account bonds to a total amount ¥2,703,551 million.)

5. Accumulated depreciation of fixed assets

Accumulated depreciation of fixed assets amounted to ¥1,337 million.

6. Net assets per share

Net assets per share is ¥1.87.

7. Restriction in dividend distribution

JFC is restricted in its dividend distribution pursuant to Article 47 of the JFC Act^{*1}. In the event that the amount of the retained earnings brought forward in the balance sheet exceeds zero in each account related to the operations^{*2} listed in each Item of Article 41 hereof, JFC shall accumulate, as a reserve, the amount calculated in accordance with the standards prescribed by a Cabinet Order to the extent that it reaches the certain amount, and if there is still a surplus, JFC shall pay such surplus into the national treasury within 3 months after closing date.

In the event that the amount of the retained earnings brought forward falls below zero in each account set forth in the preceding paragraph, legal capital surplus and legal retained earnings shall be transferred to retained earnings brought forward to the extent that the amount of retained earnings brought forward becomes zero.

*1 Including instances deemed applicable by the replacement of terms pursuant to the provisions of Article 22 (1) of the Act on Special Measures Concerning Smooth Implementation of Realignment of United States Forces in Japan (Act No. 67; 2007) and instances deemed applicable by the replacement of terms pursuant to the provisions of Article 17 of the Act on the Promotion of Businesses to Develop and Manufacture Energy and Environmentally Friendly Products (Act No. 38; 2010).

*2 Including instances deemed applicable by the replacement of terms pursuant to the provisions of Article 17 of the Act on the Promotion of Businesses to Develop and Manufacture Energy and Environmentally Friendly Products (Act No. 38; 2010) and operations listed in Article 16 of the Act on Special Measures concerning Smooth Implementation of Realignment of United States Forces in Japan [hereafter referred to as “operations listed under each section of Article 41 of the same law.”

8. The account title and the amount related to transactions with affiliates

Ordinary income–Other income–Other: ¥2,210 million

9. Net income per share

Net income per share is ¥0.05.

10. Issued shares

For the fiscal year ended March 31, 2011, types and number of issued shares are as follows:

(Unit: shares)

Types	The number of stocks at beginning of the fiscal year	Increase during the fiscal year	Decrease during the fiscal year	The number of stocks at the end of the fiscal year
Common stocks	1,055,500,000,000	35,500,000,000	—	1,091,000,000,000

(Note) Increases is due to the issuance of 35,500,000,000 shares.

11. Financial instruments and related disclosure

1. Status of financial instruments

(1) Initiatives for financial instruments

Based on the JFC Act, we are a governmental financial institution founded for the purpose of supplementing the financing conducted by general financial institutions and contributing to the development of the Japanese and global economic society and the improvement of the lifestyle of citizens.

The budget required for governmental financial operations is decided on by the Diet of Japan, and business plans and financial plans (funds through borrowing from the fiscal investment funds and loans, bonds and investments from the general account, equity participation, etc.) are appended to the budget and submitted to the Diet of Japan.

These operations are classified into Micro Business and Individual Operations, Agriculture, Forestry, Fisheries and Food Business Operations, SME Loan Programs and Securitization Support Programs (Guarantee-type Operation), Securitization Support Programs (Purchase-type Operation), Credit Insurance Programs, JBIC Operations, Financial Operations for Facilitating Realignment of United States Forces in Japan, Operations to Facilitate Crisis Responses, and Operations to Facilitate Specific Business Promotion. Accounts are made for each classification (“operation account”) for accounting treatment.

The funds procured by JFC through borrowing from the fiscal investment funds and loans, bonds and investments from the general account are managed separately by each operational account. In principle, it is assumed that funds intended for one operation account will not be used for another operation account. Accordingly, ALM (asset and liability management) is conducted for the risks associated with financial assets and liabilities for each operation account. Note that financial instruments that can be used for the management of surplus funds are limited to extremely safe instruments such as Japanese government bonds, etc., as stipulated by The JFC Act.

The purpose of the Account for JBIC Operations is to conduct the financing required for “Promoting overseas development and acquisition of strategically important natural resources to Japan”, “Maintaining and improving the international competitiveness of Japanese industries”,

“Promoting overseas projects for conserving the global environment, such as mitigating global warming”, and “Taking appropriate measures with respect to disruptions to international financial order”. Principal operations consist of export loans, import loans, investment financing, financing for business development and capital investment (including guarantees expect for “capital investment”). To conduct these operations funds are raised through borrowing from the fiscal investment funds and loans and the issuing of bonds. ALM (asset and liability management) is conducted for financial assets and liabilities in this account that are subject to interest-rate and currency fluctuations to ensure that interest-rate and currency fluctuations do not have an adverse effect on these operations. Also, derivative transactions are conducted for the purpose of mitigating risk inherent in foreign currency denominated transactions.

(2) Types of financial instruments and risks

The financial assets and liabilities owned by JFC are managed in separate operation accounts.

The assets in this account mainly include loans to borrowers in Japan and overseas, and securities, and liabilities mainly include borrowings and bonds. The associated risks are described below.

(a) Credit risk

Credit risk is the risk that the account will suffer losses if the financial condition of the borrower deteriorates and the value of assets (including off-balance sheet assets) decrease or disappear.

The credit risks associated with this account include sovereign risk, country risk, corporate risk, and project risk. Characteristic of support for overseas economic transactions conducted in this account, much financing is conducted for overseas governments, governmental institutions, and overseas corporations. Much of the credit risk associated with the credit provided typically consists of sovereign or country risk.

As a result, if the financial condition of the individual borrower significantly deteriorates due to political and economic trends in the borrower’s country or region, the performance and financial condition of these operations can be adversely affected.

(Note) Sovereign risk refers to risk associated with credit supplied to foreign governments, country risk refers to risk associated with the country in which the corporation or project is located (risk in addition to corporate risk or project risk associated with the country in which the corporation or the project is located), corporate risk refers to the risk associated with credit to corporations, and project risk refers to the risk that the cash flow of an underlying project will not perform as planned in the case of project finance where the repayment of the borrowing is primarily secured by the cash flow of the project to which credit is supplied.

(b) Market risk

Market risk is the risk that the value of assets and liabilities (including off-balance sheet assets) will fluctuate and losses will be suffered, or profits derived from assets and liabilities (including off-balance sheet assets) will fluctuate and losses will be suffered due to the fluctuation of various market risk factors such as interest rates, exchange rates, etc.

The market risk associated with this account mainly consists of exchange rate risk and interest rate risk, and losses could be suffered from these risks from market fluctuations. However, in principle, these risks are mitigated through interest rate swaps, currency swaps, and forward exchange transactions.

In this account hedge accounting is used for interest rate hedges, where the hedging instruments are interest rate swaps to hedge the market fluctuation risk associated with loans, borrowed money and bonds. The effectiveness of the hedges is assessed by measuring and comparing the change in fair value or cumulative change in cash flows of both hedging instruments and corresponding hedged items from the date of inception of the hedges to the assessment date.

In this account hedge accounting is used for foreign exchange hedges, where currency swaps and foreign exchange forward contracts are used to hedge items such as loans, borrowings, and bonds for exchange rate fluctuation risk. The effectiveness of the hedging currency-swaps and forward contracts, hedging the foreign exchange risks of monetary assets and liabilities denominated in foreign currencies, is assessed by comparing the foreign currency position of the hedged monetary assets and liabilities with that of the hedging instruments.

(c) Liquidity risk

Long-term and stable funds, such as fiscal loan funds, government-backed bonds, and FILP agency bonds, are secured to finance this account and deposits are not accepted, with the result that JFC considers liquidity risk to be limited. However, financing costs could increase due to market disturbances and unexpected events.

(3) Risk management structure for financial instruments

JFC has a Corporate Governance Committee established to properly conduct management in order to comprehensively handle risks faced, including risks associated with financial instruments, to ensure the sustained and stable realization of the financing policies of the function.

For each type of risk, management policies and procedures have been created to handle the specific types of credit risks, market risks, and liquidity risks for financing associated with each operation, and a structure has been established to smoothly handle these tasks in each operation.

The risk management structure for these operations is described below.

(a) Credit risk management

The basis of credit risk management is centered on individual credit management based on the creditworthiness of the borrower during the credit approval process.

When a new credit application is processed, the relevant finance departments (sales promotion department) and credit departments collect and analyze information on the borrower. The overseas representative offices also play a part in collecting information on foreign governments and corporations. Credit appraisal takes place based on the information that has been gathered and analyzed, with the different departments ensuring appropriate check throughout the process, leading to the final decision by the management.

For lending to foreign governments and corporations, JFC makes most use of its position as a public institution and exchanges views and information with governments and other authorities in recipient countries, international institutions such as the IMF and the World Bank, other regional development banks and official export credit agencies as well as private financial institutions in the industrial countries. Using all these channels, JFC evaluates sovereign or country risk (in addition to corporate risk and project risk associated with the country in which the corporation is located) based on a broad range of information on government and government agency borrowers as well as political and economic conditions in their countries.

The relevant finance departments and credit departments conduct proper credit risk management based on the credit risk rating system for segmented risk categories and the asset self assessment system based on the Financial Inspection Manual. In addition, an Integrated Risk Management Committee is held regularly to report the status of credit management to the management. The credit management situation is also checked by an independent auditing department.

In addition, a claims protection mechanism exists based on an international framework unique to official creditors that is not contained in private sector financial institutions, for official claims on foreign governments. This mechanism consists of international financial assistance upon international approval by the Paris Club, an international group focusing on debt, to allow the debtor country to continue debt repayment when the debtor country becomes temporarily unable to service its debt due to economic conditions. As part of this international financial assistance, the debtor country conducts an economic reform program upon agreement with the IMF in order to secure the ability to sustainably service its debt. In view of JFC's position as a public financial institution, it will use the framework of the Paris Club to preserve its official claims on foreign governments.

Besides the individual credit management outlined above, credit risks are quantified to assess

the overall risk of the portfolio in these operations. To quantify credit risks, it is important to take into account the characteristic of the loan portfolio, that there are a significant proportion of long-term loans and loans involving sovereign risk or country risk. Also to be taken into account is the mechanism of securing assets, such as the framework of international financial assistance to debtor countries through the Paris Club, which is unique to official creditors. This account uses a unique model to quantify the credit risk taking account of the above explained elements and measures amount of credit risk, which are utilized for credit risk management.

(b) Market risk management

ALM is used to manage exchange rate risk and interest rate risk for these operations. Market risk management protocols contain detailed stipulations of risk management methods and procedures, which are used by the ALM Committee to assess and confirm the execution of ALM, and for discussions concerning future responses. In addition, monitoring is conducted through gap analysis and interest rate sensitivity analysis as well as Value at Risk (“VaR”) to comprehensively assess the interest and terms of financial assets and liabilities. The results are regularly reported to the ALM Committee

The basic policy for managing exchange rate risk and interest rate risk in these operations is described below.

(i) Exchange rate risk

Foreign currency-denominated loans conducted in these operations involve risks related to exchange rate fluctuations.

We have a consistent policy of managing this risk by fully hedging this risk exposure through the use of currency swaps and forward foreign exchange transactions.

(ii) Interest rate risk

Interest rate risk arises from exposure to market interest rate fluctuations for yen-denominated loan and foreign currency-denominated loan operations and the policy for managing interest rate risk is described below.

① Yen-denominated loan operations

For the most part, funding for yen-denominated loans is managed at fixed-rate interest. Currently, interest rate risk for yen-denominated loans is limited since maturity of loans and the related funding arrangements are generally matched. In addition, swaps are used to hedge interest rate risk for portions of loans that are thought to have high exposures to interest rate fluctuation risk.

② Foreign currency-denominated loan operations

For foreign currency-denominated loan operations, interest rate risk is hedged through the application of a consistent policy of using interest rate swaps and managing funds with floating interest rates for both loans and related funding arrangements.

(iii) Status of market risk

These operations only maintain a banking account and do not have financial instruments in a trading account. While these operations are managed by hedging operation in principle, as stated previously, market risk, such as Value at Risk is measured in order to ascertain fair value assessment and risks inherent. The following represents the status of market risk in these operations in the current fiscal year as calculated using Value at Risk (VaR).

(a) VaR status (Fiscal year ended March 31, 2011)

- (1) Interest rate VaR: 69.7 billions of yen
- (2) Exchange rate VaR: 45.9 billions of yen

(b) VaR measurement model

- (1) Interest rate VaR: Historical model
- (2) Exchange rate VaR: Variance-covariance model

Quantitative standards: ① Confidence Interval: 99%; ② Holding period: 1 year; ③ Observation period: 5 years

(c) Risk management using VaR

VaR is a market risk measure that assesses the maximum possible profits or losses that could be incurred due to market movements within a certain period of time (or holding period) and degree of possibility (or confidence interval). These are derived statistically by employing the theory of possibility distribution based on historical market movements of interest rates or exchange rates, etc. over a specific period in the past (or observation period).

This measurement assumes actual market trends and the theory of probability distribution. Based on the possibility that future market trends could deviate from these assumptions, a back-test is performed to cross-check the model-measured interest rate VaR with actual profits or losses, in order to confirm the effectiveness of market risk measurements using VaR. In addition, a stress test, which goes beyond the probability distribution of historical market movements is conducted in order to capture risks from multifaceted perspectives.

The following bullet points represent general shortcomings of VaR models.

- Model-measured VaR may differ depending on the confidence interval, holding period, or observation period.
- The VaR value represents the maximum fluctuation of a mark-to-market profit or loss at the time of the measurement. This does not guarantee that the fluctuation will be within the limit as predicted at some future point in time, since conditions precedent, such as market trends, will vary during the time horizon.
- The VaR indicates the maximum value based on specific conditions precedent. As such, it is imperative to consider that model-measured VaR may underestimate the potential losses when using VaR as a risk management indicator in practice.

(c) Liquidity risk management related to fund procurement

Long-term and stable funds such as fiscal loan funds, government-backed bonds, and FILP agency bonds are used to finance these operations and deposits are not accepted.

Cash flows are assessed and proper measures including establishing overdraft facility accounts with multiple private sector financial institutions are taken to maintain daily cash flows for proper risk management.

(d) Derivatives transactions

A protocol of internal checks with separate divisions executing transactions, assessing the effectiveness of hedges, and conducting office management has been established for derivatives transactions, and these transactions are conducted according to derivatives-related regulations.

(4) Supplementary explanation concerning fair value of financial instruments

The fair value of financial instruments includes amounts based on market value and amounts that have been reasonably estimated when no market value is available. Set valuation inputs are used for the calculation of this amount, and if different valuation inputs are used the resulting amount could vary.

2. Fair value of financial instruments

The amount in the balance sheet at March 31, 2011, and the related fair value, and difference is as follows. Note that unlisted securities and partnership investments whose fair value is extremely difficult to be determined are not included in the following chart (refer to note 2).

Japan Finance Corporation
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(Millions of yen)

	Amount on Balance Sheet	Fair value	Difference
(1) Cash and due from banks	978,074	978,074	—
(2) Securities			
Available-for sale securities	3,800	3,800	—
(3) Loans and bills discounted	8,376,794		
Allowance for loan losses ^{(*)1}	(120,414)		
	8,256,380	8,324,476	68,096
Total assets	9,238,255	9,306,351	68,096
(1) Borrowings	5,502,495	5,599,191	96,696
(2) Bonds payable	2,703,551	2,774,959	71,407
Total liabilities	8,206,046	8,374,150	168,104
Derivative transactions ^{(*)2}			
Derivative transactions not qualifying for hedge accounting	(4)	(4)	—
Derivative transactions qualifying for hedge accounting	965,093	965,093	—
Total derivative transactions	965,089	965,089	—

(*)1 General allowance for loan losses, specific allowance for loan losses and allowance for possible loan losses on specific overseas loan have been deducted from loans.

(*)2 Derivative recorded in “other assets and other liabilities” are collectively displayed.

The net values of assets and liabilities arising from derivative transactions are displayed. The figures in parenthesis indicate net liabilities.

(Note 1) Valuation methodologies used for estimating fair values for financial instruments

Assets

(1) Cash and due from banks

For due from banks that do not mature or have a maturity under 3 months, the carrying amount is used as fair value because fair value resembles the carrying amount.

(2) Securities

The fair value of “Available-for sale securities” is based on the price that is indicated from other financial institution.

(3) Loans and bills discounted

For loans with variable interest rates an amount calculated by the floating rate note method to reflect market interest rates over the short term is used for fair value.

For loans with fixed interest, the total principal and interest is discounted by a risk free rate that incorporates the default ratio and coverage ratio to calculate fair value. However for obligations on bankrupt borrowers, substantially bankrupt borrowers, and potentially bankrupt borrowers allowance for loan losses is calculated based on the expected collectable amount from the collateral or guarantee. Fair value approximates the amount on the balance sheet on the closing date after a deduction has been made for allowance for loan losses, so this amount is used for fair value.

Liabilities

(1) Borrowings

Borrowings with variable interest rates indicate that short-term market interest rates and the credit conditions of JFC are not significantly altered by borrowings. Therefore, the carrying amount is used as fair value because it is considered that the carrying amount approximates the fair value. For borrowings with a fixed interest rate, in principle, fair value is calculated by discounting the principal and interest of the borrowings by the risk free rate (the standard Japanese government bond rate) based on the set period of loan.

(2) Bonds payable

Market value is used for fair value of bonds.

Derivative transactions

Derivative transactions consist of interest rate-related transactions (interest rate swap) and currency-related transactions (currency swap and forward exchange contract). Calculation of fair value is based on the discounted cash flow.

(Note 2) Financial instruments that are recognized to be extremely difficult to be determined fair value are as follows.

They are not included in Fair value of financial instruments.

(Millions of yen)

Classification	Carrying amount on balance sheet
1) Unlisted stocks ^{(*)1}	19,907
2) Partnership investments ^{(*)2}	52,746
Total	72,653

(*)1 Since unlisted stocks do not have quoted market prices available and fair value is extremely difficult to be determined, fair values are

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not stated.

(*2) For partnership investments composed of unlisted stocks that do not have quoted market prices available and for which fair value is extremely difficult to be determined fair values are not stated.

(Note 3) Redemption schedule for receivables and redeemable securities with future redemption dates

(Millions of yen)

	Maturities within one year	Maturities after one year but within three years	Maturities after three years but within five years	Maturities after five years but within seven years	Maturities after seven years but within ten years	Maturities after ten years
Due from banks ^(*1)	978,074	—	—	—	—	—
Securities ^(*2) Available-for sale securities	—	1,192	2,607	—	—	—
Loans and bills discounted ^(*2)	1,078,144	1,970,380	2,275,246	951,556	1,081,671	910,789
Total	2,056,218	1,971,572	2,277,853	951,556	1,081,671	910,789

(*1) Demand deposits contained within due from banks are stated as “Maturities within one year”.

(*2) Within loans and securities, claims against bankrupt borrowers, substantially bankrupt borrowers, and potentially bankrupt borrowers contains an amount of ¥109,005 million that is not expected to be redeemed and not included in the table above.

(Note 4) Redemption schedule for bonds and borrowings with future redemption dates

(Millions of yen)

	Maturities within one year	Maturities after one year but within three years	Maturities after three years but within five years	Maturities after five years but within seven years	Maturities after seven years but within ten years	Maturiti es after ten years
Borrowings	367,683	1,204,243	2,478,286	1,072,471	379,812	—
Bonds payable	503,387	1,094,772	837,187	150,000	100,000	20,000
Total	871,070	2,299,015	3,315,473	1,222,471	479,812	20,000

12. Market value of securities

In addition to “Other securities” on the balance sheet, transferable deposits in “Due from banks” are also included.

The market value of securities at March 31, 2011 is as follows:

(a) Equity securities of or investment in subsidiaries and affiliates

(Note) These are equity securities of, or investment in, subsidiaries and affiliates whose fair value is extremely difficult to be determined.

	Carrying amount on balance sheet (Millions of yen)
Equity securities of or investment in affiliates	52,193

They have no quoted market price and their fair value is extremely difficult to be determined.

(b) Available-for-sale securities

	Type	Carrying amount on the balance sheet (Millions of yen)	Acquisition cost (Millions of yen)	Difference (Millions of yen)
Securities whose carrying amount does not exceed their acquisition cost	Others	503,800	503,800	—

(Note) Available-for-sale securities whose fair value is extremely difficult to be determined

	Carrying amount on the balance sheet (Millions of yen)
Others	
Unlisted foreign stocks	15,095
Unlisted Japanese securities	224
Unlisted foreign securities	5,139

These are not included in the above table of “Available-for-sale securities” because there are no quoted market prices available and it is extremely difficult to determine the fair value of these securities.

13. Deferred tax accounting

JFC does not apply deferred tax accounting since JFC is a nontaxable entity classified in the Article 2 (5)

of the Corporation Tax Act (Act No. 34; 1965).

14. Retirement benefits

JFC has a defined benefit pension plan comprising of a welfare pension fund plan and a lump-sum severance indemnity plan.

(a) The funded status of the pension plans

	March 31, 2011 (Millions of yen)
Projected benefit obligations (A)	(16,969)
Fair value of plan assets (B)	4,134
Unfunded pension obligations (C)=(A)+(B)	(12,834)
Unrecognized prior service costs (D)	81
Actuarial unrecognized difference (E)	617
Net amount recognized on the balance sheet (F)=(C)+(D)+(E)	(12,135)
Prepaid pension cost (G)	—
Provision for retirement benefits (H)=(F)–(G)	(12,135)

(b) Component of pension cost

	March 31, 2011 (Millions of yen)
Service cost	545
Interest cost	334
Expected return on plan assets	(83)
Amortization of prior service cost accounted for as expense	0
Actuarial differences accounted for as expense	89
Other costs	—
Net pensions cost	886

(Note) Employee contributions to pension funds have been deducted from the service cost.

(c) Principal assumptions made

	March 31, 2011
Discount rate	2.0%
Expected rate of return on plan assets	2.0%
Method of attributing the projected benefits to periods of services	Straight-line basis
Terms to amortize unrecognized prior service costs	10 years
Terms to amortize actuarial unrecognized differences	10 years

15. Profit and loss on equity method

Investment in affiliates	¥52,193 million
Investment in affiliates (equity method)	¥52,292 million
Profit or Loss of Investment in affiliates (equity method)	¥98 million

16. Related party transaction

Related party transactions in the fiscal year ended March 31, 2011 are as follows:

Transactions with parent company and major shareholder companies

(Millions of yen)

	Corporate name	Ratio to Total Voting Rights (%)	Relation with related parties	Transactions	Amounts of transactions	Items	Balance as of March 31, 2011
Principal shareholder	Ministry of Finance (Minister of Finance) (Note i)	100 (Direct)	Administration for policy based financing	Underwriting of capital increase (Note i)	35,500	—	—
				Receipt of funds (Note ii)	1,014,444	Borrowings	5,502,495
				Repayment of borrowing	626,657		
				Payment of interest on borrowings	55,696	Accrued expenses	13,863
				Guarantee for corporate bonds (Note iii)	1,633,712	—	—

(Note)

- (i) The underwriting of capital increase represents the increase in capital through shareholder allocation by JFC at an allocation amount of ¥1 per share.
- (ii) The receipts of funds represents borrowing under the FILP, and for this borrowing, the interest rates are applied under the FILP agreement.
- (iii) No guarantee fee has been paid for the guarantee of bonds.
- (iv) Figures in the table above do not include consumption taxes.

17. Subsequent events

The Japan Bank for International Cooperation Act (hereafter, the “New JBIC Act”) was passed on April 28, 2011 at the 177th ordinary session of the Diet. Based on this Act, on April 1, 2012, JBIC will be separated from JFC to form Japan Bank for International Cooperation Co., Ltd. (hereafter “New JBIC”), and effective on the same date, JFC’s JBIC Operations and Finance Operations for Facilitating Realignment of United States Forces in Japan will be transferred to the New JBIC.

JFC will underwrite the stock of the New JBIC, and will transfer this stock without compensation to the government of Japanese at the time the New JBIC is established on April 1, 2012. Effective the same day, assets and liabilities relating to JFC’s JBIC operations and Financial Operations for Facilitating Realignment of United States Forces in Japan will be succeeded by the New JBIC. The amount of assets and liabilities to be succeeded will be the assessed amount as determined by an evaluation committee based on the New JBIC Act. After the establishment of the New JBIC, profit and loss relating to JFC’s JBIC Operations and Finance Operations for Facilitating Realignment of United States Forces in Japan will no longer be recognized as profit and loss of JFC. Note that there is no impact on cash flows of Account for JBIC operations, Financial Account Related to the Financial Operations for Facilitating Realignment of United States Forces in Japan, or the New JBIC.