

6. Sept.2010

Sirs and Mesdames:

I would like to present here my comments on “Consultative Documents, Countercyclical capital buffer proposal” released July 2010.

1. Regarding Principle 1

I am afraid the principle 1 in the consultative documents lacks insight into why it is important to prevent procyclical feed back to the economy induced by banking regulations. The mechanism of feed back is that when the economy slows down, the banking system incurs some losses, which decreases the capital and, thus, the lending capacity of the banking system, which, in turn, makes the economy insufficient of money and further slows down the economy. The latter half of the process is so-called “credit crunch”.

It should be shared here that the important point is to prevent “credit crunch” to avoid procyclical feed back to the economy. As long as the losses sustained by the banking system is not large enough to cause “credit crunch”, bank regulators do not need to worry about the procyclical movement and eventual catastrophic outcome.

Therefore, I would like to propose here that the Principle 1 should be amended as follows.

Principle 1. Buffer decisions should be guided by the objectives to be achieved by the buffer, namely to avoid credit crunch, which facilitates the procyclical feed back between the economy and the banking system and hurts the economy and the banking system to a catastrophic end.

2. Regarding credit-to-GDP

I would like to propose here that “credit capacity to GDP” ratio is more appropriate than “credit to GDP” ratio. Credit capacity can be calculated from the aggregate capital of the banking system.

If the objective of the new regulation is to avoid credit crunch, credit capacity is the most important number to monitor. As you look at the Japanese economy for the last 20 years, its slow growth in spite of excessive inflow of money by the central bank is mainly due to lost credit capacity of the Japanese banking system. I would like to point out here again the possible grave economic outcome of lack of credit capacity management and would like to draw your attention to the credit capacity figure. Thank you.

Sincerely,  
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