Comments on the Consultative Document of the Basel Committee on Banking Supervision
"Revisions to the Standardised Approach for Credit Risk"

March 27, 2015

The Japan Chamber of Commerce and Industry

The Japan Chamber of Commerce and Industry has a great concern with "Revisions to the Standardised Approach for Credit Risk" released by the Basel Committee on Banking Supervision.

We hope that our comments below will be of assistance to the discussion towards the finalization of the rules at the Basel Committee on Banking Supervision.

1. Impact on small and medium-sized entities (SMEs)
   - The voices of industry side, especially SMEs, in each country should be heard carefully. The proposed revisions of the standardized approach will not only impact on the management and behavior of financial institutions but also have an immense impact on the corporates including SMEs. In order to realize sustainable and inclusive growth of world economy, we should secure the lending to SMEs is provided smoothly and stably.

2. Exposures to corporates
   - The majority of Japanese SMEs do not qualify for inclusion in the Committee's definition of "regulatory retail" (the criteria including exposures up to the threshold of EUR 1 million), thereby the exposures to those SMEs are categorized as "Exposures to corporates." Therefore, the revisions to the "Exposures to corporates" will impact on SMEs.
   - The Consultative Document proposes the adoption of revenue as a risk driver, whereby risk weights would be determined in such a way that the smaller the revenue the higher the risk weights would be. The correlation between the risk and the size of revenue is not revealed. On the contrary, the ratio of bankruptcy of smaller SMEs (the number of employees are under 20) is 0.0028 % in 2014, which is same as the one of larger SMEs in Japan. In general, the number of employees is proportional to the size of revenue; therefore, it is inappropriate to utilize revenue as a risk driver.
   - In addition, the adoption of profitability as a risk driver would also be inappropriate. For example, long term investment contributes corporates' (especially a SME's) soundness of management rather than short-term profitability.
   - The risk weights on corporates should not be determined by applying a specific set of risk drivers in a mechanistic manner; essentially it is appropriate that they should be assessed based on diverse aspects. (In this light, credit ratings and credit assessments conducted by credit rating agencies that have satisfied certain criteria are deemed to have maintained certain levels of reliability.)
   - It is observed that well proven, appropriate and easily applicable methods of credit assessment and credit ratings for SMEs have been deployed by most financial institutions in Japan. This sophisticated approach should be applied in this revision. At least, the rule should be varied, in accordance with the actual circumstances of the respective countries.

3. The risk level is different in respective countries

- The risk level of corporates is very different from country to country and this difference should be reflected to the revision. The default risk of SMEs in Japan is 0.0028 %, which is much lower than the one of the other countries. SMEs, in particular, mainly operate within their respective countries. Therefore, it would be reasonable to constitute a system which would allow for each country to establish its own standards.
- In light of the above, it is only reasonable that qualifications for inclusion in “regulatory retail” (EUR 1 million, etc.) be determined in accordance with the actual circumstances of the respective countries.