Self-Assessment of Asset Quality and Policies for Write-Offs and Reserves

Self-Assessment of asset quality is conducted in order to clarify the quality of assets as a preparatory step for making appropriate write-offs and transfers to reserves based on accounting and other principles. Under the Prompt Corrective Action System*1, banks carry out such assessments at their own responsibility as the basis for preparing financial statements that reflect the true quality of their assets.

In the process of Self-Assessment, DKB applies its own Credit Risk Rating System*2 and classifies all obligors into one of five classifications, namely, “Normal Obligors,” “Obligors under Close Observation,” “Obligors with Possible Bankruptcy,” “Obligors Substantially in Bankruptcy,” and “Obligors under Legal Bankruptcy Proceedings.” These are DKB’s Obligor Classifications.

After excluding claims against obligors in the “Normal Obligors” classification, the remaining claims are individually classified into Class I, II, III, and IV based on the degree of difficulty in collecting such loans and the risk of impairment of value. These are DKB’s Asset Classifications.

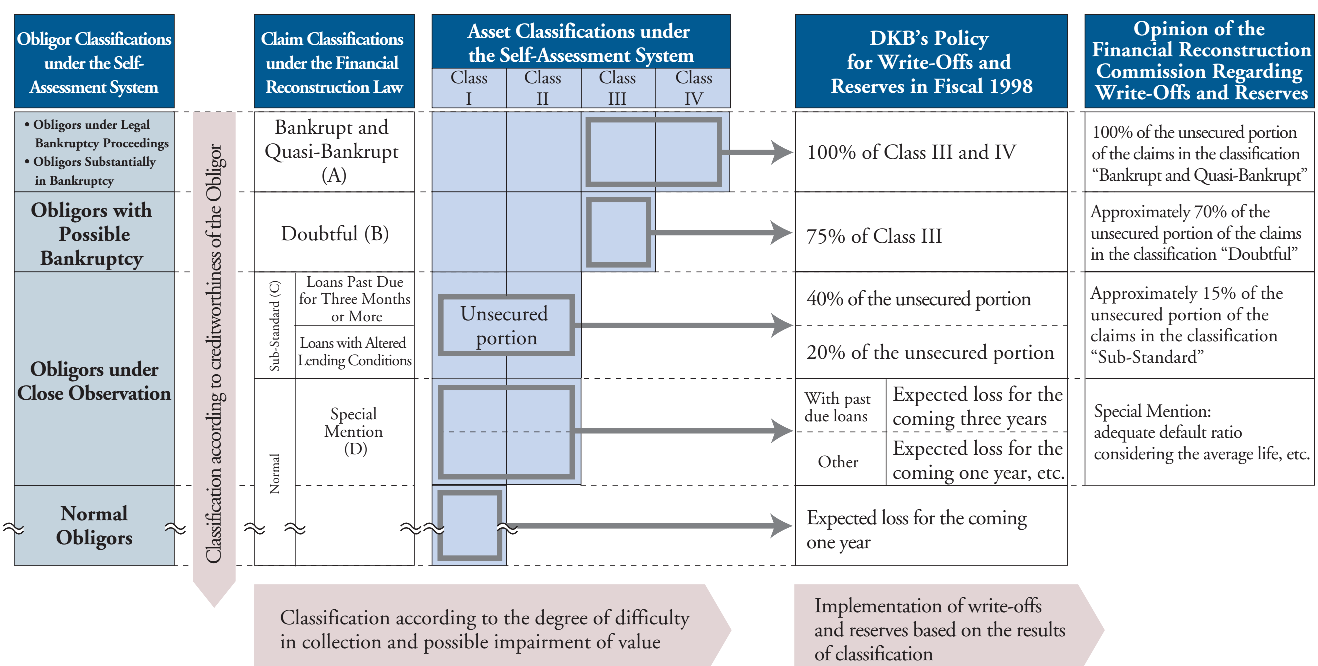
Specifically, such claims are classified on the basis of the expected usage, prospects for collection of the funds, amount of security in the form of collateral and guarantees and other factors.

Decisions on write-offs and reserves for possible loan losses are based on the matrix showing the positioning of the claim with respect to the Obligor Classification and the Asset Classification under the Self-Assessment.

For example, in fiscal 1998, for claims against obligors classified as “Obligors with Possible Bankruptcy,” specific reserves for possible loan losses were set aside equivalent to approximately 75% of their value in Class III.

The system for setting aside write-offs and reserves based on the Self-Assessment of asset quality was clarified legally with the implementation of the Bank Recapitalization Law in November 1998. This law requires banks to set aside appropriate reserves following the assessment of asset quality as stipulated in the Financial Reconstruction Law.

Policies for Write-Offs and Reserves



(A) Claims against Obligors under Bankruptcy, Reorganization and Similar Proceedings; (B) Claims against Obligors with Possible Bankruptcy; (C) Claims against Obligors under Special Attention; (D) Claims against Other Obligors under Close Observation

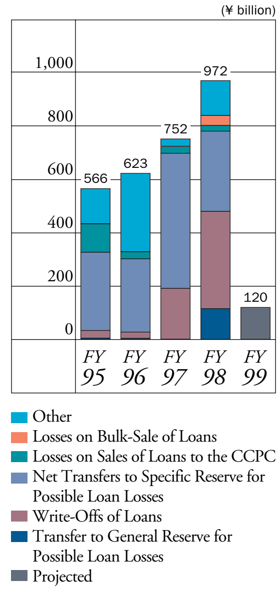
Measures to Deal with Problem Loans

In order to deal with problem loans during the fiscal year under review, DKB set aside reserves far larger than the amount under the previous criteria it adopted and accelerated the disposal of non-performing loans.

As a consequence, Write-Offs of Loans amounted to ¥365.1 billion, Net Transfer to Specific Reserve for Possible Loan Losses was ¥301.4 billion, and Transfer to Reserve for Specific Borrowers under Support amounted to ¥65.1 billion, bringing costs related to the disposal of non-performing loans to ¥856.4 billion. If the ¥115.5 billion of Transfer to General Reserve for Possible Loan Losses is included, total credit costs amounted to ¥972.0 billion.

Although trends in the economy, interest rates, land prices, and other variables are uncertain, credit costs in fiscal 1999, ending March 31, 2000, are expected to be substantially lower.

Credit-Related Costs



Risk-Managed Loans

To provide shareholders, investors, and depositors with information on the soundness of its asset portfolio, DKB has been disclosing Risk-Managed Loans under the voluntary criteria established by the Japanese Bankers Association. Accompanying the revision of the Banking Law Enforcement Regulations in December 1998, DKB began to disclose this information on a consolidated basis in addition to a non-consolidated basis beginning with the fiscal year ended March 31, 1999.

Non-Consolidated Statement of Income Summary

(¥ billion)

	Fiscal 1998	Fiscal 1997	Change
Net Operating Profit			
(Before Deduction of Transfer to General Reserve for Possible Loan Losses)	¥ 294.1	¥ 323.2	¥ (29.1)
Transfer to General Reserve for Possible Loan Losses (A)	115.5	0.1	115.3
Net Operating Profit	178.5	323.0	(144.4)
Net Other Profit/Loss	(783.0)	(478.0)	(305.0)
Net Profit/Losses Related to Stocks and Other Securities	102.4	292.8	(190.3)
Gains on Sales of Stocks	159.7	310.2	(150.4)
Losses on Sales of Stocks	38.7	15.0	23.7
Devaluation of Stocks	18.6	2.3	16.2
Losses on Bad Debt (B)	856.4	752.8	103.6
Write-Offs of Loans	365.1	191.1	173.9
Net Transfer to Specific Reserve for Possible Loan Losses*	301.4	507.7	(206.2)
Losses on Sales of Loans to the CCPC	21.4	25.5	(4.0)
Losses on Bulk-Sales of Loans	37.6	1.7	35.8
Transfer to Reserve for Losses on Loans Sold	49.5	11.0	38.4
Losses Due to Supporting Borrowers	—	7.5	(7.5)
Transfer to Reserve for Specific Borrowers under Support	65.1	—	65.1
Transfer to Reserve for Loans to Restructuring Countries	11.4	(0.4)	11.8
Losses on Sales of Other Loans, etc.	4.6	8.4	(3.7)
Other	(28.9)	(18.0)	(10.9)
Ordinary Profit/Loss	(604.4)	(154.9)	(449.5)
Net Extraordinary Profit/Loss	(49.9)	12.1	(62.1)
Income/Loss before Income Taxes and Others	(654.4)	(142.7)	(511.6)
Income Taxes and Others	5.0	3.6	1.4
Adjustment to Income Taxes and Others	(283.2)	—	(283.2)
Net Income/Loss	(376.1)	(146.4)	(229.7)
Total Credit Costs (A) + (B)	¥ 972.0	¥752.9	¥ 219.0

* For fiscal 1997, this was Net Transfer to Reserve for Special Purposes

Changes in the Criteria for Risk-Managed Loans

All non-accrual loans are classified as either Loans to Borrowers under Bankruptcy Proceedings or Non-Accrual Status Loans.

The standard for the non-accrual of interest receivable was a formal and objective standard based on tax law criteria*3. However, from the fiscal year ended March 31, 1999, DKB has adopted new criteria based on the Self-Assessment of asset quality instead of tax law criteria previously adopted and changed the standard for the non-accrual of interest receivable. As a result, all loans to obligors classified as “Obligors with Possible Bankruptcy,” “Obligors Substantially in Bankruptcy,” and “Obligors under Legal Bankruptcy Proceedings” are classified as non-accrual loans regardless of whether the loans are past due or not.

For this reason, certain loans which had not been classified as Loans to Borrowers under Bankruptcy Proceedings and Non-Accrual Status Loans under tax law criteria previously adopted were classified as such. In addition, certain loans formerly disclosed under Loans Past Due for Three Months or More and Loans with Altered Lending Conditions were reclassified as Loans to Borrowers under Bankruptcy Proceedings and Non-Accrual Status Loans.

Thus, under the new criteria, Risk-Managed Loans of the Parent, as of March 31, 1999, were as follows: Loans to Borrowers under Bankruptcy Proceedings, ¥196.3 billion; Non-Accrual Status Loans, ¥1,640.7 billion; Loans Past Due for Three Months or More, ¥38.2 billion; and Loans with Altered Lending Conditions, ¥329.4 billion. The total amount of Risk-Managed Loans was therefore ¥2,204.7 billion.

Under the previous criteria based on tax law criteria, amounts were as follows: Loans to Borrowers under Bankruptcy Proceedings, ¥130.0 billion; Non-Accrual Status Loans, ¥297.4 billion; Loans Past Due for Three Months or More, ¥120.7 billion; and Loans with Altered Lending Conditions, ¥377.5 billion. The total

(¥ billion)

Obligor Classification under the Self-Assessment	Obligors under Legal Bankruptcy Proceedings			Obligors Substantially in Bankruptcy/ Obligors with Possible Bankruptcy				Obligors under Close Observation		
New Criteria (Self-Assessment Basis) 2,204.7	Loans to Borrowers under Bankruptcy Proceedings 196.3			Non-Accrual Status Loans 1,640.7				Loans Past Due for Three Months or More 38.2	Loans with Altered Lending Conditions 329.4	(Normal)
Treatment of Interest Receivable under the New Criteria	Not Accrued			Not Accrued				Accrued		
Previous Criteria (Tax Law Basis) 925.7	Loans to Borrowers under Bankruptcy Proceedings 130.0 [Not Accrued]	(1) Loans with Altered Lending Conditions 29.9 [Accrued]	(2) Loans Not Formerly Classified as Risk-Managed Loans (36.3) [Accrued]	Non-Accrual Status Loans 297.4 [Not Accrued]	(3) Loans with Altered Lending Conditions 18.1 [Accrued]	(4) Loans Past Due for Three Months or More 82.5 [Accrued]	(5) Loans Not Formerly Classified as Risk Managed Loans (1,242.6) [Accrued]	Loans Past Due for Three Months or More 38.2 [Accrued]	Loans with Altered Lending Conditions 329.4 [Accrued]	(Normal) [Accrued]

Difference between Risk-Managed Loans under previous and new criteria: ¥1,279.0 billion

Descriptions in brackets show accounting treatment of interest receivable under the previous criteria.

Difference between Risk-Managed Loans under New and Previous Criteria

Loans Past Due for Three Months or More: Item (4) above

Under the previous criteria, loans in (4) were disclosed as Loans Past Due for Three Months or More. But, following Self-Assessments, these loans were classified as being outstanding to Obligors Substantially in Bankruptcy and Obligors with Possible Bankruptcy. Under the new criteria, these loans have been classified as Non-Accrual Status Loans.

Loans with Altered Lending Conditions: Items (1) and (3) above

Under the previous criteria, loans in (1) and (3) were disclosed as Loans with Altered Lending Conditions. But, following Self-Assessments loans in (1) were classified as being outstanding to Obligors under Legal Bankruptcy Proceedings and loans in (3) were classified as being outstanding to Obligors Substantially in Bankruptcy and Obligors with Possible Bankruptcy. Under the new criteria, these loans have been classified as Loans to Borrowers under Bankruptcy Proceedings and Non-Accrual Status Loans.

Difference between Risk-Managed Loans under Previous and New Criteria: Items (2) and (5) above

The difference between the amount of Risk-Managed Loans under the previous and new criteria is due to the change in the criteria for classifying loans as non-accrual from those based on the tax law criteria to one based on the result of DKB’s Self-Assessments. Those loans classified as being outstanding to Obligors under Bankruptcy Proceedings, Obligors Substantially in Bankruptcy, and Obligors with Possible Bankruptcy after Self-Assessments were all reclassified as non-accrual loans whether they were past due or not. As a result of this change in criteria and reclassification, Risk-Managed Loans increased ¥1,279.0 billion.

amount of Risk-Managed Loans under the previous criteria was therefore ¥925.7 billion, or ¥545.6 billion lower than for the previous fiscal year-end.

The figure for total Risk-Managed Loans for fiscal 1998 under the new criteria is ¥1,279.0 billion higher than the figure as calculated under the previous criteria. The major reason for this difference is the previously mentioned change in the criteria for non-accrual loans. Other factors include the implementation of more conservative Self-Assessments of loan quality as part of DKB's policy of enhancing the soundness of its operations.

Risk-Managed Loans on a Consolidated Basis

Risk-Managed Loans on a consolidated basis as of March 31, 1999, were as follows: Loans to Borrowers Under Bankruptcy Proceedings, ¥253.3 billion; Non-Accrual Status Loans, ¥1,843.9 billion; Loans Past Due for Three Months or More, ¥61.9 billion; and Loans with Altered Lending Conditions, ¥275.2 billion. The total amount of Risk-Managed Loans was therefore ¥2,434.5 billion, or ¥229.8 billion greater than such loans on a non-consolidated basis.

DKB conducted a major review of its consolidated subsidiaries and, based on the opinions of the Deliberation Council for Corporate Accounting and practical guidelines established by the Japanese Institute of Certified Public Accountants, shifted from formalized criteria to the principle of actual corporate control in determining the extent of coverage of consolidated accounts. As a result, the scope of consolidation was expanded to include DKB Finance Corporation and other companies under the effective control of DKB. The addition of these new consolidated subsidiaries resulted in an increase in Risk-Managed Loans of ¥150.0 billion.

Risk-Managed Loans on a Consolidated and Non-Consolidated Basis

(March 31, 1999) (¥ billion)

	Consolidated Basis	Non-Consolidated Basis	Change
Loans to Borrowers under Bankruptcy Proceedings	¥ 253.3	¥ 196.3	¥ 57.0
Non-Accrual Status Loans	1,843.9	1,640.7	203.2
Loans Past Due for Three Months or More	61.9	38.2	23.7
Loans with Altered Lending Conditions	275.2	329.4	(54.2)
Total	¥2,434.5	¥2,204.7	¥229.8

Disclosed Claims under the Financial Reconstruction Law

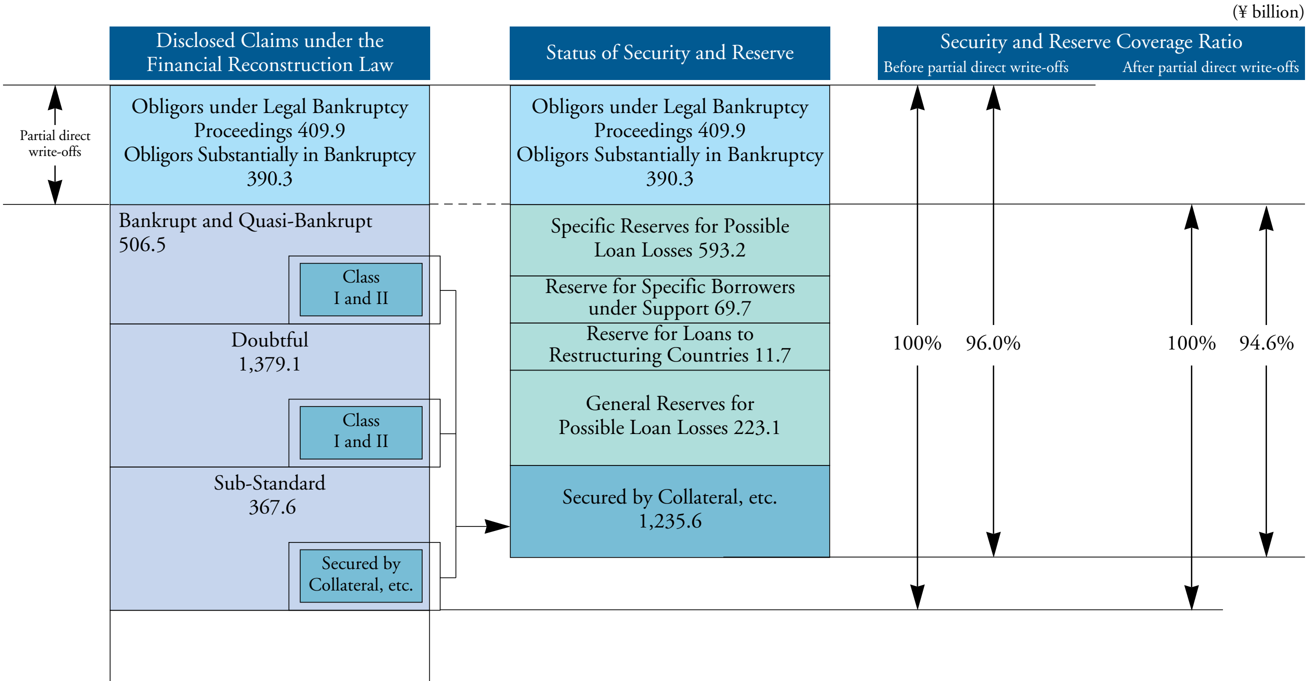
Under the Financial Reconstruction Law and the Financial Reconstruction Law Enforcement Regulations that were implemented in October 1998, banks are required to disclose their claims classified as follows based on the financial condition or earnings performance of each obligor: "Normal," "Sub-Standard," "Doubtful" and "Bankrupt and Quasi-Bankrupt."

Claims classified as "Bankrupt and Quasi-Bankrupt" correspond with the claims against "Obligors under Legal Bankruptcy Proceedings" and "Obligors Substantially in Bankruptcy" under the Self-Assessment Criteria. Similarly, claims classified as "Doubtful" correspond with claims against "Obligors with Possible Bankruptcy." Moreover, claims classified as "Sub-Standard" correspond with "Loans Past Due for Three Months or More" and "Loans with Altered Lending Conditions" among claims against "Obligors under Close Observation" under the Self-Assessment Criteria, and loans reclassified into these classifications are abstracted on an individual loan basis. Disclosed claims under the Financial Reconstruction Law were as follows: "Bankrupt and Quasi-Bankrupt," ¥506.5 billion; "Doubtful," ¥1,379.1 billion; and "Sub-Standard," ¥367.6 billion, for a total of ¥2,253.4 billion. In addition, the difference between the latter figure and the figure for Risk-Managed Loans under the new criteria, amounting to ¥48.6 billion, was due to the inclusion of acceptances and guarantees and certain other assets, other than loans, in the disclosed claims under the Financial Reconstruction Law, while Risk-Managed Loans include only loans.

Security and Reserve for Problem Loans

The secured portion of problem loans under the Financial Reconstruction Law criteria was ¥2,133.4 billion. These loans were covered by Reserves for Possible Loan Losses and Reserve for Specific Borrowers under Support amounting to ¥897.8 billion and collateral and guarantees amounting to ¥1,235.6 billion. The coverage ratio was 96.0% before partial direct write-offs*4 and 94.6% after partial direct write-offs. The totals for reserves include provisions against ordinary loans. If these amounts are excluded, the coverage ratio after partial direct write-offs was 88.3%.

Disclosed Claims under the Financial Reconstruction Law and Secured Status



Security and Reserve Coverage Ratio under the Financial Reconstruction Law

Before partial direct write-offs	96.0%
After partial direct write-offs	94.6%

The coverage ratio following exclusion of the portion of the General Reserve for Possible Loan Losses set aside against possible losses on normal loans was as follows:

After partial direct write-offs	88.3%

GLOSSARY

*1 **Prompt Corrective Action System** This is an accounting treatment in which the irrecoverable loan amount is eliminated from the balance sheet by offsetting it with reserves. This irrecoverable amount is loans to obligors classified as Obligors under Legal Bankruptcy Proceedings and Obligors Substantially in Bankruptcy less anticipated proceeds from the sale of collateral pledged against the loan and anticipated recoveries from guarantors of the loan. The irrecoverable amount is equivalent to the Class IV amount under the Self-Assessment System and is offset by transfers from Reserves for Possible Loan Losses.

*2 **Credit Risk Rating System** With the aim of structuring credit risk management systems that meet international standards, DKB has introduced a system to rank the credit risk of obligors based on an absolute and uniform standard. This is a first step toward a system that uniformly monitors and evaluates the credit risk for all its obligors and all types of credits on a bankwide basis and can be used to control credit risks.

*3 **Non-Accrual Loans Based on Tax Law Criteria** Under applicable tax law, it is permissible not to accrue interest receivable on loans in the circumstances listed below. Prior to the fiscal year under review, DKB determined whether or not to accrue interest receivable according to these tax law criteria.

1. Loans for which the loan agreement has expired
   (a) Loans for which the borrower has gone bankrupt under generally accepted criteria, including application for legal resolution of obligations under the Bankruptcy Law, Composition Law, and other applicable laws, and loans to borrowers that have had all transactions with banks suspended.
   (b) Loans for which the term of the loan agreement has expired.
2. Loans for which interest payments have been suspended in a meeting with creditors or other relevant parties.
3. Loans which have been past due for a substantial period
   Loans for which the contract date has not passed, but for which interest payments have been in arrears for six months or more.

*4 **Partial Direct Write-Offs** This is an accounting treatment in which the irrecoverable loan amount is eliminated from the balance sheet by offsetting it with reserves. This irrecoverable amount is loans to obligors classified as Obligors under Legal Bankruptcy Proceedings and Obligors Substantially in Bankruptcy less anticipated proceeds from the sales of collateral pledged against the loan and anticipated recoveries from guarantors of the loan The irrecoverable amount is equivalent to the Class IV amount under the Self-Assessment System and is offset by transfers from Reserves for Possible Loan Losses.

Definitions

SELF-ASSESSMENT	
Classification	**Obligors Basis**
Subject	**All Claims**
Obligor Classifications (A)	**Definitions (“Final Report” of the Working Group on Financial Inspection Manuals*)**
Obligors under Legal Bankruptcy Proceedings	Obligors who have already gone bankrupt, from both legal and practical perspectives.
Obligors Substantially in Bankruptcy	Obligors for which formal and legal bankruptcy causes have not yet occurred, but whose financial position are extremely distressed, and whose prospects for financial rehabilitation are so low as to render it substantially bankrupt.
Obligors with Possible Bankruptcy	Obligors who are not currently facing bankruptcy but are having business difficulties, and whose progress state of the business improvement plan or other measures are not satisfactory, so that there are a high probability that the obligor will go bankrupt.
Obligors under Close Observation	Obligors who require increased credit watching, including obligors with problematic loan conditions, such as interest suspended or reduced, obligors with problems in payment, such as those who are in arrears in the principal repayment or the interest payment, obligors whose business conditions are unstable or poor, and obligors who have problems in their financial conditions.
Normal Obligors	Obligors generally recognized to be experiencing good business conditions and having no significant financial problems.

THE FINANCIAL RECONSTRUCTION LAW		
Classification		**Obligors Basis (Claims basis as to Sub-Standard)**
Subject		**All Claims (Loans only as to Sub-Standard)**
Asset Classifications (B)		**Definitions (Article 4 of the Financial Reconstruction Law Enforcement Regulations)**
Bankrupt and Quasi-Bankrupt (Claims against Obligors under Bankruptcy, Reorganization and Similar Proceedings)		Claims against bankrupt obligors under bankruptcy, corporate reorganization, composition or any other equivalent procedures, and claims corresponding to the said conditions.
Doubtful (Claims against Obligors with Possible Bankruptcy)		Claims against obligors who are not currently bankrupt, but whose financial position and business results have deteriorated materially with a high probability that the principal and interest will not be paid in accordance with the contracts.
Sub-Standard (Claims against Obligors under Special Attention)		
	Loans Past Due for Three Months or More	Claims for which principal repayment or interest payment is in arrears for three months or more calculated from the next day of the contractual due date of payments.
	Loans with Altered Lending Conditions	Claims which are given a certain modification on the lending conditions in favor of the obligors for the purpose of restructuring and supporting the obligors in financial difficulties and for the purpose of progress in collection of the claims.
Normal (Claims against Normal Obligors)		Claims against obligors that are not experiencing any financial or management difficulties and are not included in the above-mentioned classification.

* **Financial Inspection Manuals** In April 1999, the Financial Supervisory Agency issued a Final Report of the Working Group on Financial Inspection Manuals that clearly states appropriate procedures for financial inspections. These manuals are the guidelines that inspectors use at the time of examinations of financial institutions. Moreover, these manuals require that banks should make efforts to establish sound and appropriate operations under the responsible management, taking the essence of the manual into consideration.

	RISK-MANAGED LOANS	
	Classification	**Claims Basis**
	Subject	**Loans Only**
(B) corresponds to (A)	**Loan Classifications**	**Definitions (Article 19, Section 2 of the Banking Law Enforcement Regulations)**
Claims against “Obligors under Legal Bankruptcy Proceedings” or claims against “Obligors Substantially in Bankruptcy”	Loans to Borrowers under Bankruptcy Proceedings	Loans to be non-accrual loans for which obligors are under bankruptcy, corporate reorganization, composition, or suspension of banking transaction.
	Non-Accrual Status Loans	Loans to be non-accrual loans for which there are no prospects for collection or repayment of principals or interest for which payment of principals or interest has not been received for a substantial period or for other reasons.
Claims against “Obligors with Possible Bankruptcy”		
“Loans Past Due for Three Months or More” or “Loans with Altered Lending Conditions” among claims against “Obligors under Close Observation”	Loans Past Due for Three Months or More	Loans for which payments of principals or interest have not been received for a period of three months or more beginning with the next business day following the last due date for such payment, and are not included in Loans to Borrowers under Bankruptcy Proceedings or Non-Accrual Status Loans.
	Loans with Altered Lending Conditions	Loans for which the Bank has provided more favorable terms and conditions—including reducing interest rates, rescheduling interest and principal payments, or the waving of claims on the borrower—to the borrower than those in original loan agreement, with the aim of providing restructuring assistance and support. Such loans exclude Loans to Borrowers under Bankruptcy Proceedings, Non-Accrual Status Loans, and Loans Past Due for Three Months or More.
Claims against “Normal Obligors” and claims in the classification “Obligors under Close Observation” exclusive of those corresponding to Sub-Standard		