

# **Business Report for Fiscal 2006**

**CRD (Credit Risk Database),  
A Limited Liability Intermediate Corporation**

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## I. Overview of Business Operations

### 1. Management stability of CRD (Credit Risk Database) and upgrading business operations structures

#### (1) Stabilization of CRD management

##### [1] Covering majority of domestic small and medium enterprises

As of the end of FY2006, the CRD database accumulated over 2.17 million debtors (after debtor identification of corporations and sole proprietors), covering more than half of the nation's small and medium enterprises. In terms of the number of financial statements, the database contained over 9.8 million cases (14.4 million original data before debtor identification, of which members of credit guarantee associations accounted for 8 million, and financial institutions for 6.4 million). Our database encompasses long-term series since 1995, with corporations, 5-year-or-over serial data accounting for 50%, and with sole proprietors, 3-year-or-over serial data accounting for 50% of records. Accordingly, we have come to pride ourselves on our predominant competitive edge as the nation's largest database for building and validating credit risk assessment models.

##### [2] Further upgrading the quality of accumulated data

As one of the crucial tasks in our business plans for FY2006, we proceeded with identifying quality problems within the accumulated data through general checkup and organized a response to each issue. In particular, we honed the reliability of accumulated data with member cooperation by i) reminding members to submit or complete their own information, ii) requesting members to update default information, iii) improving the data-cleansing process for debtor identification, iv) making arrangements so that the holding period of accumulated data could be extended from 10 years to 20 years, v) starting acceptance of data under new business sector codes from October 2006, and vi) conforming to the Corporate Law provisions for data processing.

##### [3] Stabilization of management and business activities

During FY2006, we successfully completed the alignment of various CRD services, especially of our basic services (statistical information, data sampling and credit risk scoring) and SME management support consulting services and other consulting. While our CRD models were incorporated into the SME credit insurance system; and so our membership has increased substantially from the outset of the fiscal year in the process, we characterized FY2006 as “the year when our management was put on a stable course.” Our annual membership fee, excepting for the initial year, was reduced from ¥3.2 million in FY2006 to ¥3 million in FY2007.

Stabilized management allowed our business activities to concentrate on providing our members with fuller services to meet a variety of high-level needs, such as contributing to the smooth implementation of the SME credit insurance system, or supporting intensified credit risk management.

#### (2) Reinforcement of our business operations structure

##### [1] Reinforcement of member support structure

We reinforced member support structures to provide better consulting services for meeting members'

new demands, for improving data quality, and for supporting intensified credit risk management, in addition to our regular services.

To respond to the diversified needs from our members, we bolstered our human resources to equip them with professional capabilities in credit risk management and statistical data analysis. We augmented staff in charge of local institutions to strengthen individual member services. At the outset of FY2007, our Executive Office was staffed by 3 full-time directors and 24 staffers (2 workers on loan and 3 contract workers).

Also from the outset of FY2006, we enhanced our IT system's performance by revising our system platforms and renovating operating soft wares. Moreover, we constructed member's information integration system, with the view of sustaining and improving member satisfaction through better communication with an increased number of members.

## [2] Strengthening of internal control and confidential information management

In FY2006, we developed a code of conduct for our executive staff, laying out mission statements and behavior guidelines. Our intention was to strengthen internal control on information security within the CRD Executive Office while keeping staff well-advised of "making the best possible effort to protect our database" and of "confidential information is the common property of all members." We enacted regulations for managing confidential information of which our management and staff members became more aware.

We reviewed how CRD sampling data was used by outsiders from the perspective of confidential information management and rigorously regulated the way CRD sampling data was provided to academic institutions, and audited how information was securitized at the outlets using data.

## (3) Slowdown in membership growth in the 2<sup>nd</sup> half

Due to the flexible application of segmented guarantee charge rates implemented in April 2006, the number of new members increased substantially at the outset of the fiscal year. It is a new increment of 32 members (31 regular members and 1 special member), amounting to a total of 193 fee members. However, since the 2<sup>nd</sup> half of the fiscal year, new memberships have leveled off; new members for FY2007 have remained four, indicating that total membership has reached a plateau.

From the trends in new memberships, our management environment has changed from the 4-year peak period from 2003 through 2006, when memberships were increasing yearly; we are now at a turning point to begin exploring a new phase in management without relying on increasing numbers of full members. Such understanding motivates us to upgrade services to be provided and develop new profitable businesses.

## 2. Upgrading member services to meet diversified and sophisticated needs

### (1) Smooth implementation of SME credit insurance system

#### [1] Supporting the application of flexible guarantee charge rates by credit guarantee corporations

Since April 2006, CRD Model 3 and Model 4 BS have been stipulated in the notification of the Ministry of Economy, Trade and Industry as credit risk measurement models under Article 9 (computation of

incidence rate of insured events) of the SME Credit Insurance Law Enforcement Regulations. They are utilized as assessment models to determine the insurance rate in accordance with incidence rates of insured events. Credit guarantee corporations also use these models as risk assessment models to assess guarantee charge rates.

With the CRD models playing such an official role, we periodically communicated with our members (credit guarantee corporations and financial institutions) about how to use the scoring model for computing credit guarantee charge rates, and asked how they used models or whether they had any problems in their implementation. We also provided training sessions for CRD Models 3 and 4 and answered inquiries on their applications. Furthermore, in line with the flexible application of credit guarantee charge rates, we developed our 8th version of the User Interface and provided an updated Model Applications Q&A manual for user convenience. We asked professional tax experts to be advisors for “the guidelines for SME accounting” in 2007.

## [2] SME management support and revitalization support

The SME Management Diagnosis System (MSS), as refined according to members' requirements, was utilized as a simple management-consulting tool by member SME operators. They used MSS in such manners, at many branches, as mailing output forms or reference documents for loan examinations. Use of the SME Revitalization Support System (CSS) has also expanded, as 48 SME revitalization support councils, etc., (54 licenses), 27 credit guarantee corporations (33 licenses) and 24 financial institutions (24 licenses) signed up contracts, with 2 credit guarantee corporations using it on an experimental basis as of the end of FY2006.

We held a series of sessions for both MSS and CSS training. In FY2006, 52 credit guarantee corporations, 147 participants as a total, attended MSS training seminars held under the auspices of the National Federation. A total of 120 participants partook in CSS training; 44 member institutions (60 participants) attended primary seminars, 31 members (40 participants) at intermediate seminars, and 15 members (20 participants) at advanced-practice seminars.

## (2) Upgraded support for intensified credit risk management

### [1] Strengthening of consulting services

“Intensification of credit risk management” has gained in significance and public attention, to satisfy “the new capital adequacy requirements” (hereinafter Basel II), regardless of the type or scale of financial institutions. Against this backdrop, upgrading our member services was the most essential task in our FY 2006 business plans.

We strengthened our credit risk management services by i) increasing staff with expertise in financial and credit risk management and upgrading consulting capabilities, ii) publishing the “CRD Utilization Manual” (3rd edition) to fully manage intensified credit risk (edited separately for credit guarantee corporations and financial institution members), iii) holding meetings to exchange information on specific themes of intensified credit risk management, iv) developing tools to support for portfolio analysis, etc.

### [2] Responding to the diversified individual needs of financial institution members

We energetically responded to the varied needs of our financial institution members by i) providing

advice daily on individual issues such as how to cope with Basel II requirements, ii) providing services for (re)constructing an internal rating system, iii) upgrading “mapping analysis for rating” using the CRD Model (actual results for FY2006: 14 members with a cumulative total of 18 cases), and iv) providing validation services using CRD data for an internal rating structure. We accomplished statistical validation of the internal rating system in a certain financial institution by extracting validation data analogous to her portfolio from our database.

In responding to the individual needs of credit guarantee corporation members, we endeavored to provide information on credit risk management methods relevant to their guaranteed assets.

### (3) Upgraded services for individual members

#### [1] Upgrading individual member services and scheduled visits to members by area representatives

We undertook scheduled visits to 188 members or 320 visits as a total, under the auspices of “trying to establish close communication with members, grasp accurately members' diversified needs, and provide services to maximize customer satisfaction” (228 visits for the previous fiscal year). We adopted this system in order to respond sensitively to our clients. At the outset of FY2007, seven staffs were serving members on a daily basis.

#### [2] Information services to members through information exchange meetings

Each area representative maintained daily contact with members, and supplied timely information. 72 members (107 participants) attended the 6th information exchange meetings held in July 2006, designed to exchange information among members and to brief them on timely and essential themes. We held a workshop, October 2006 for the 4<sup>th</sup> time, to assist with the expansion of research activities using CRD data. 18 members (54 participants) attended it.

We also started publishing, a quarterly magazine “Four Seasons” as a communication medium for members. The first issue was published in December 2006, followed by a second issued in March 2007.

#### [3] Diversified use of CRD services

Members utilized CRD data for various purposes throughout the year. Firstly, we released a credit risk assessment model in October designed specifically for the software industry. This model is characterized as integrating quantitative and qualitative assessments. Secondly, the “Macro Default Probability (MPD)” (formerly known as the “Macro Default Index”), studied on a full scale since FY2005, was completed for publication. This new regional macroeconomic indicator is expected to help provide speedy judgment on regional economic outlook and industry sector conditions. Thirdly, we furthered research on the model to project debt- collection rates and started out with a review of constructing the model for financial institution members. Fourthly, our CRD data were utilized to analyze innovation in service industry the “New Economic Growth Strategy”, compiled by the government in April. Our CRD data was utilized also in the first consulting research overseas conducted in Malaysia. Our services were increasingly utilized in various fields as the year progressed.