



Mizuho International plc
Pillar 3 Disclosure
for the year ended 31 March 2018

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1. Introduction

Objective

This document sets out disclosures in respect of Mizuho International plc (MHI) required under European Union (EU) CRD IV legislation, consisting of the Capital Requirements Regulation¹ (CRR) and the Capital Requirements Directive² (CRD).

Pillar 3 disclosures, as required under Part Eight of the CRR provide market participants with information on a firm's risk governance, risk management processes, risk exposures, and capital resources.

Directive imposed disclosure requirements are implemented within the UK through Prudential Regulation Authority (PRA) rules³. These disclosures provide market participants and other stakeholders with information in relation to a firm's governance and remuneration practices.

Regulatory information

MHI is authorised by the PRA and regulated by the Financial Conduct Authority (FCA) and the PRA. MHI is entered into the Financial Services Register and its register reference number is 119256.

Forward looking statements

Certain statements in this disclosure document are forward looking with respect to plans, goals and expectations relating to the future financial position, business performance and results of MHI. Although MHI believes that the expectations reflected in these forward-looking statements are reasonable, MHI can give no assurance that these expectations will prove to be an accurate reflection of actual results. Because these statements involve risks and uncertainties, actual results may differ materially from those expressed or implied by these forward-looking statements. MHI undertakes no obligation to update any forward-looking statements whether as a result of new information, future events or otherwise.

Overview of Basel framework and Pillar 3

The CRD IV legislation, designed to implement the Basel III reforms of the Basel Committee on Banking Supervision, came into force in the EU on 1 January 2014. However, certain aspects of CRD IV are subject to phased implementation and may also be dependent on final technical standards to be issued by the European Banking Authority (EBA) and adopted by the European Commission, and ultimately implemented in the UK.

Prudential requirements under the Basel framework are categorised under three pillars as described below.

Pillar 1 - Industry minimum capital requirements

Risk based requirements

The first pillar of the Basel framework focuses on the determination of minimum capital requirements applicable to all firms to support exposures to credit, counterparty credit, market and operational risks. Capital requirements may also be expressed as risk weighted assets (RWAs), being a notional amount 12.5 times the size of the capital requirement.

Risk based minimum capital requirements may be determined using a number of approaches. These are summarised below, together with the approach which has been adopted by MHI:

¹ Regulation (EU) No 575/2013 of the European Parliament and of the Council on prudential requirements for credit institutions and investment firms.

² Directive 2013/36/EU of the European Parliament and of the Council on the access to the activity of credit institutions and the prudential supervision of credit institutions and investment firms.

³ Section 4.3A.11 of the PRA's Senior Management Arrangements, Systems and Controls (SYSC) sourcebook.

Table 1: Basel Pillar 1 risk based approaches

| Approach | MHI | Summary |
|---------------------------------------|-----|--|
| Credit risk | | |
| Standardised approach | ✓ | <p>Standardised risk weightings are applied to credit risk exposures.</p> <p>Credit exposures in respect of counterparty risk must be calculated in accordance with prescribed methods, being either: mark-to-market, standardised, or the internal model method (IMM).</p> <p>Credit ratings supplied by external credit assessment institutions (ECAIs) are used to determine the appropriate risk weight to be applied to exposure amounts.</p> <p>Credit risk mitigation techniques are recognised.</p> |
| Internal ratings based (IRB) approach | ✗ | <p>There are two main IRB approaches for wholesale exposures:</p> <ul style="list-style-type: none"> - The foundation IRB approach allows banks to make their own internal assessment of a counterparty's probability of default (PD), but subjects their quantified estimates of exposure at default (EAD) and loss given default (LGD) to standard supervisory parameters. - The IRB advanced approach allows banks to use their own internal assessment in determining PD, quantifying EAD and LGD. |
| Counterparty credit risk | | |
| Mark-to-market method | ✓ | <p>Under this method an add-on for potential future exposure (PFE) is applied to the mark-to-market value of the instrument to give the overall exposure. Exposure value is then subject to risk-weighting under the Standardised Approach to determine capital requirement.</p> |
| Original Exposure method | ✗ | <p>Under this method the exposure value is calculated by multiplying the notional amount of the instrument by set percentages prescribed depending on maturity.</p> |
| Standardised method | ✗ | <p>The exposure value is calculated by applying a multiplier to the market value, dependent on the type of contract.</p> |
| Internal model method (IMM) | ✗ | <p>Under the IMM approach, the fair value on the balance sheet is replaced by an exposure value calculated using internal models.</p> |
| Market risk | | |
| Standardised approach | ✓ | <p>Requires the calculation of position risk requirements for each type of market risk within the trading book in accordance with standard rules.</p> |
| Internal models approach | ✗ | <p>Capital requirements are calculated using internal Value at Risk (VaR) models.</p> |
| Operational risk | | |
| Basic indicator approach | ✓ | <p>Capital requirements are calculated as 15% of three year average income.</p> |
| Standardised approach | ✗ | <p>Capital requirements are calculated from the three year average of aggregate risk weighted indicators. A firm's business must be split into defined business lines with specific risk weights applied to each business line.</p> |
| Advanced measurement approach | ✗ | <p>Capital requirements are calculated through the use of internal operational risk measurement systems.</p> |

Non-risk based requirements

Under CRD IV risk based requirements are supplemented by a leverage ratio, under which firms are required to maintain Tier 1 capital in excess of a minimum ratio to a gross measure of exposures. Exposures comprise on and off balance sheet items, calculated from the accounting balance sheet subject to a defined set of adjustments. Whereas risk-weighted capital ratios differentiate capital requirements according to estimates of the relative riskiness of different asset classes, a leverage ratio weights all assets equally. The leverage ratio is intended to limit the risk of excessive leverage across the banking sector and to reinforce risk based requirements with a simple backstop measure.

In accordance with CRD IV banks are required to publish their leverage ratios from 2015, with a binding requirement across the EU expected to come into force from 2020. Institutions will from this point be required to maintain capital in excess of the greater of the risk based and non-risk based requirements. MHI's current leverage ratio is provided in section 6 of this document.

Pillar 2 - Supervisory review process

The second pillar of the Basel framework is designed to assess the adequacy of a firm's capital resources by considering all material risks to the firm's business, including those not covered or adequately addressed by the first pillar, together with the impact upon the capital position that is forecast to occur using stressed macroeconomic scenarios.

Firms are required to conduct an Internal Capital Adequacy Assessment Process (ICAAP) at least annually to review their capital resources in light of material risks identified, and the outcome of stress testing procedures performed. This internal assessment is subject to the Supervisory Review and Evaluation Process (SREP) and forms part of the PRA's own assessment of the risks to which firms are exposed, their risk management and capital adequacy.

Following the SREP, the PRA sets firms a Pillar 2A capital requirement on an individual basis, for the amount and quantity of capital the PRA considers the firm must hold in addition to the capital it must hold to comply with the CRR (Pillar 1 capital) to meet the overall financial adequacy rule. The sum of Pillar 1 and Pillar 2A capital requirements is the firm's Total Capital Requirement (TCR). TCR is set as a percentage of RWAs.

The PRA may also notify firms of an amount and quality of capital, over and above the level of capital required to meet its TCR and over and above the CRD IV buffers (CCoB: Capital Conservation Buffer; CCyB: Countercyclical Capital Buffer), that should be held for the PRA buffer. In setting a PRA buffer for a firm the PRA will not just consider whether the firm would meet its CET1 capital requirements under the CRR and its Pillar 2A capital requirement in stress. Other factors informing the size of the PRA buffer include but are not limited to: the maximum change in capital resources and requirements under the stress; the firm's leverage ratio; the extent to which the firm has used up its CRD IV buffers; Tier 1 and total capital ratios; and the extent to which potentially significant risks are not captured fully as part of the stress. The PRA Buffer is set as a percentage of RWAs.

Pillar 3 - Market discipline

The third pillar of the Basel framework requires public disclosure surrounding a firm's risk governance, risk management practices, its approach to capital management, capital resources and Pillar 1 capital requirements. These disclosures are intended to foster market discipline in relation to a firm's risk management practices.

Notes on basis of preparation

Scope of consolidation

These disclosures are comprehensive and prepared in respect of MHI.

Basis of preparation

These disclosures have been prepared in accordance with regulatory capital adequacy concepts and rules rather than in accordance with accounting standards. Certain information provided within these disclosures is therefore not directly comparable with financial information contained within the annual financial statements.

The table below shows the relationship between MHI's accounting balance sheet categories and the calculation of RWAs by risk driver. The table does not include all inputs included in the calculation of RWAs, but is intended to provide an overview of the link between accounting and Pillar 1 regulatory measures:

Table 2: RWA calculation drivers split by balance sheet category

| Accounting balance sheet category | RWA risk type | | |
|--|---------------|--------------------------|-------------|
| | Credit risk | Counterparty credit risk | Market risk |
| Assets | | | |
| Reverse repurchase agreements | - | ✓ | ✓ |
| Debt and equity securities | - | - | ✓ |
| Derivative assets | - | ✓ | ✓ |
| Loans and advances to banks | ✓ | - | - |
| Shares in group undertakings | ✓ | - | - |
| Intangible fixed assets | - | - | - |
| Tangible fixed assets | ✓ | - | - |
| Other assets, prepayments and accrued income | ✓ | - | - |
| Liabilities and equity | | | |
| Deposits by banks | - | - | - |
| Customer accounts | - | - | - |
| Repurchase agreements | - | ✓ | ✓ |
| Short trading positions | - | - | ✓ |
| Derivative liabilities | - | ✓ | ✓ |
| Debt securities in issue | - | - | - |
| Subordinated debt | - | - | - |
| Other liabilities, provisions and accruals | - | - | ✓ |

Not all Pillar 3 disclosure requirements under CRD IV are applicable to MHI. In such instances no disclosure is presented within this document.

Location and verification

A standalone copy of these disclosures is located on MHI's website (www.mizuho-emea.com). These disclosures should be read in conjunction with the MHI financial statements for the year ended 31 March 2018, which are also published on this website.

Whilst the disclosures presented within this document do not require validation through external audit, they have been subject to internal governance procedures, including review and approval by MHI's Chief Financial Officer (CFO) and Chief Risk Officer (CRO) and the Board of Directors of MHI (the "Board").

Frequency of disclosure and comparative balances

Disclosures are provided in accordance with EBA guidelines, currently on an annual basis, and published as soon as practicable after the publication of the financial statements and, unless otherwise indicated, all current year figures are stated as at MHI's financial year end, 31 March 2018.

More frequent disclosures are provided in the event that a material change occurs to MHI's business.

Comparative balances as at 31 March 2017 have generally been presented within this document. Where required, comparative prior year values have been restated to align with the 2018 presentation of disclosures.

Immaterial disclosures

In line with Article 432 of the CRR, where the information required under a particular disclosure is considered by MHI to be immaterial, such disclosures have been omitted. The determination of immateriality is based upon the guidance issued by the EBA.

2. Corporate governance

Role of the Board

The MHI Board (the “Board”) has overall responsibility for the management of MHI, although certain matters are reserved to the shareholder whether under English law or by decision of the shareholder as set out in a Statement of Delegated Authority by the shareholder reviewed and approved by the shareholder on 16 February 2017 and by the Board on 23 February 2017. The role of the Board is to provide leadership of MHI within a framework of prudent and effective internal control, in order to maintain effective operations, control of financial affairs and compliance with law and regulation. The Board is responsible for the long term success of MHI and, to this end, sets the strategy and risk appetite for MHI, whilst ensuring that an effective risk management framework is maintained.

Certain matters are reserved for approval by the Board due to their significance. These matters include decisions concerning Board membership (subject to approval by the shareholder at an annual general shareholder meeting of the appointment / continuation in office of any Board member appointed during the previous year) and corporate governance, strategy, approval of risk appetite and risk management oversight, capital and liquidity matters, corporate structure, financial performance, remuneration policy and significant legal and regulatory matters. Matters not specifically reserved to the Board are delegated to MHI's executive officers.

Directors' responsibilities

Under UK company law, directors must promote corporate success by exercising independent judgement with reasonable care, skill and diligence, while having regard to the long-term consequences of their decisions.

Directors of UK regulated banks are also required by the PRA and FCA to act in accordance with their principles, including requirements in relation to observing proper standards of market conduct, dealing with regulators in an open and co-operative manner, taking reasonable steps to ensure that business is organised to facilitate effective control, and compliance with the regulatory system.

The principal roles on the Board and the responsibilities attaching to those roles are summarised below:

Table 3: Roles on the Board

| | |
|--|---|
| Chair of the Board | <ul style="list-style-type: none"> Leads the Board and sets / reviews the Board's agenda Facilitates engagement and participation from all Board members Ensures effective communication with MHI's shareholder Acts as Chair of the Nomination Committee |
| Chief Executive Officer (CEO) | <ul style="list-style-type: none"> Recommends MHI strategy to the Board Responsible for implementation of strategy and day-to-day management of MHI's affairs |
| Each Non-executive director | <ul style="list-style-type: none"> Offers constructive challenge to management and oversees achievement of agreed objectives Monitors operation of effective internal control and risk management |
| Senior independent non-executive directors | <ul style="list-style-type: none"> Acts as a sounding board for the Chair Available to act as an intermediary for other Board members and stakeholders |

Board composition

The Board is made up of a majority of non-executive directors. The importance of maintaining an appropriate balance of skills, experience, diversity and independence is recognised. The Nomination Committee will assess on an annual basis the structure, size and composition of the Board, together with the balance of knowledge, skills and experience of its members.

The Board composition at 31 March 2018 with regard to the balance of executive and non-executive membership is shown below:

Table 4: Board composition

| Board members | Number of individuals |
|---|-----------------------|
| Chair and independent non-executive directors | 4 |
| Other non-executive directors | 3 |
| Executive directors | 2 |
| Total | 9 |

MHI is committed to diversity and respects the diversity and individuality of all persons, irrespective of nationality, gender, age, career-level, or lifestyle. The Nomination Committee will recommend Board appointments on the basis of the benefits individual appointees can bring to the firm. This will take account of their knowledge, skills and experience measured against identified objective criteria, as well as the broader contribution they can make to the Board by widening the collective expertise and increasing the scope for effective challenge. The Nomination Committee has set an initial target for gender diversification on the Board at a minimum of 10% which has been met.

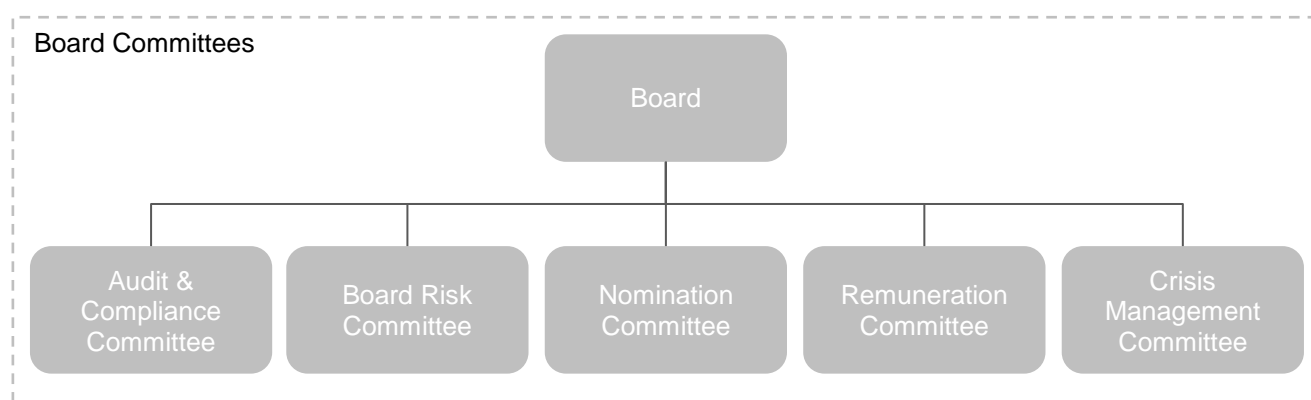
Directorships held by Board members are reviewed to ensure compliance with the PRA's requirements regarding the total number of such positions which may be held. As at 31 March 2018, the Board comprised nine members who held a total of 19⁴ directorships (inclusive of those held on the Board). The total of such directorships held by each individual director was in compliance with those requirements.

Board performance

Arrangements for induction of new Board members and ongoing training are in place to ensure that directors are fully informed of key business, legal and regulatory matters relevant to the performance of their roles. Review of Board performance and that of individual directors plays an important role in ensuring effective ongoing governance, and MHI has made arrangements for the Nomination Committee to conduct annual performance evaluations and to make recommendations to the Board arising out of these reviews.

Board committees

The Board has established a number of committees under the Board ("Board Committees") to enable detailed oversight of particular areas of Board responsibility and to facilitate oversight of senior management. Board and Board Committee meetings are held on a regular basis and sufficient time is allocated to ensure that relevant business is fully considered. The Board Committees are described below, together with a summary of their respective responsibilities:



⁴ This disclosure is given in accordance with the definition used in Article 91 of CRD IV and implemented by the PRA, whereby directorships in organisations which do not pursue predominantly commercial objectives are not counted and directorships held within the same group are counted as a single directorship.

Table 5: Board Committees

| | |
|------------------------------|---|
| Audit & Compliance Committee | <p>Reviews the appropriateness and completeness of the internal control framework, receives reports from internal and external auditors and monitors the progress of remedial action with regard to control weaknesses.</p> <p>Reviews arrangements established by management for compliance with regulatory requirements and reviews any matters of significance regarding MHI's relationship with its regulators.</p> |
| Board Risk Committee | <p>Makes recommendations to the Board concerning MHI's risk appetite and reviews the supporting Board level limit framework and key metrics.</p> <p>Evaluates and reports to the Board on matters concerning MHI's overall risk profile and performance against risk appetite, giving consideration to key trends and concentrations, compliance with limits and significant risk issues.</p> <p>The Committee evaluates MHI's governance, risk and control framework.</p> <p>Provides input to the Remuneration Committee with regard to appropriate risk adjustments to be made to remuneration packages.</p> |
| Nomination Committee | <p>Reviews and makes recommendations with regard to Board composition, performance, and Board and senior management succession planning.</p> <p>Selects and recommends to the Board candidates for membership in accordance with its assessment of the balance of skills, experience, diversity and independence to be maintained on the Board.</p> |
| Remuneration Committee | <p>Sets and recommends to the Board the objectives, principles and parameters of MHI's Remuneration Policy.</p> <p>Reviews the individual remuneration arrangements of senior staff having regard to the impact on behaviour, risk appetite and risk profile of these arrangements, and the degree to which performance assessment takes account of current and potential future risks.</p> |
| Crisis Management Committee | <p>Convened at the request of (i) any two of the CEO, CFO, CRO and Treasurer, (ii) the Risk Management Committee, (iii) the Chair of the Board, (iv) the Chair of the Board Risk Committee, or (v) the Senior Independent Non-Executive Director of the Board to resolve a crisis or threat situation.</p> |

3. Risk management framework

MHI maintains a prudent approach to risk to ensure that it can operate safely and to support sustainable business development in keeping with the Board's strategy. A culture which is supportive of strong risk management, in line with clear principles and tolerance for risk is led by the Board. MHI has a strong and independent Risk Management function responsible for the identification of MHI's principal risks, maintenance of risk control frameworks, and for keeping the Board informed of MHI's risk profile.

Risk culture

MHI believes that a strong risk management culture is essential to achieve its business objectives. With ultimate responsibility for risk governance throughout MHI, the Board embeds a strong risk management culture through the establishment of an independent Risk Management function which works closely with the business and treats risk management as a shared responsibility.

Risk principles

The Board has established clearly defined risk principles which describe MHI's key risk management objectives in support of its business strategy and are summarised below:

- Maintain a predictable cautious to moderate risk profile;
- Ensure that effective control of balance sheet usage and concentration risk is exercised, without tolerating breaches of MHI's limit framework;
- Preserve strong capital and liquidity ratios and comply with all regulatory requirements;
- Maintain a diversified funding strategy with regard to both the sources and tenor of funding;
- Ensure that remuneration arrangements are aligned to MHI's risk appetite.

Risk appetite

The Board's risk appetite describes the levels and types of risk that MHI is prepared to accept in pursuit of its business strategy. The risk appetite is prudently quantified with reference to scenario and stress testing, and is set so as to ensure that MHI is able to maintain a sound financial position throughout economic cycles.

The risk appetite is implemented through a supporting limit framework that ensures all material sources of risk are controlled in a manner consistent with the Board's overall risk tolerance. MHI has adopted a structured approach to limit management which ensures that limit reporting and oversight take place at the appropriate level within the organisation. The status of MHI's overall risk profile in relation to the risk appetite is overseen by the Board.

Risk governance and assigning responsibility

Three lines of defence

In keeping with MHI's risk culture, responsibilities for risk management are assigned to multiple functions within the organisation under the three lines of defence model, to ensure that MHI's risk management framework is robust and effective.

First line: Business and support functions which originate or accept risk are held responsible for the management and control of that risk in line with MHI's risk appetite, supporting limit framework and other related risk policies.

Second line: The second line of defence is provided by risk control functions which exercise independent oversight of the management of risk by those originating functions. The principal risk control functions comprise MHI's Risk Management and Compliance functions, supported by the Finance and Legal teams.

Third line: Independent and post-dated assurance with regard to the effectiveness of risk management strategies, policies and processes is provided by MHI's Internal Audit function and its external auditors.

Risk governance

The Board retains responsibility for approval of MHI's risk appetite, risk management oversight and capital and liquidity matters, including compliance with applicable regulation. The heads of the principal risk control functions, being the CRO and the Head of Compliance, are mandated through dual reporting lines to update and inform the relevant Board committees of matters relating to their functions and group wide risk management.

Responsibility for the day to day running of the business is delegated by the Board to MHI's CEO, who in turn mandates the heads of the principal control functions to assume responsibility for risk challenge and oversight.

Risk Management function and approach

MHI maintains a strong and independent Risk Management function which is headed by MHI's CRO. The function is mandated to oversee all material classes of risk to which MHI is exposed, other than conduct risks which are overseen by MHI's Compliance function.

The Risk Management function is structured to facilitate oversight of these principal risk classes and incorporates separate teams with responsibility for market, credit, liquidity, regulatory governance, and operational risk oversight. A common approach to risk oversight is adopted for each principal risk class, in accordance with risk policies established for those classes.

Risk identification and assessment

All material risk exposures are identified and recorded within MHI's risk register, whilst responsibility for the assessment of those risks resides with both the business and the risk control functions. Risks and sub-components of risk are assessed through the implementation of a variety of measures or metrics relevant to each risk class. Risk assessment measures are developed in accordance with accepted measurement methodologies for each class of risk, and the resulting assessments are classified according to severity, to provide clear identification of MHI's material exposures. Risk assessments are conducted in relation to both normal and stressed market conditions.

Control and mitigation

Risk exposures are managed by business and support functions using a range of techniques relevant to the individual risk class. Such techniques encompass market based hedging activities, credit risk mitigation techniques, diversification of funding sources and tenor, business continuity planning and the purchase of insurance.

Risk control limits and key risk indicators are established to ensure that risk exposures remain within specified levels, and that MHI is able to operate in accordance with its overall risk appetite. A comprehensive limit framework is maintained by risk class, with defined levels of authorisation to ensure that risk exposure levels are authorised and monitored at the appropriate level within MHI's governance hierarchy.

Monitoring and reporting

Reporting of risk exposures in relation to risk limits, and more broadly with regards to trends in MHI's risk profile and emerging risks, is performed by the Risk Management function (and by the Compliance function with regards to conduct related matters). Reporting is conducted in relation to all principal risk factors, and is designed to enable effective governance of MHI's risk profile. In particular the Board and the Board Risk Committee are regularly informed of MHI's risk exposures and compliance with risk limits.

In addition to monitoring current risk exposures, MHI also monitors potential future adverse developments by establishing early warning indicators whose breach may indicate deterioration in MHI's capital and liquidity strength. Monitoring and reporting the status of these early warning indicators forms part of MHI's contingency planning arrangements.

Strategy and planning

MHI conducts formal business planning on an annual basis, through which the Board's strategic objectives are developed into detailed business plans. Commercial objectives and plans are established for all significant business lines, and from these financial projections are developed, which take account of expected macroeconomic and market conditions.

MHI's risk appetite is also formally reviewed on an annual basis as part of the business planning cycle, to ensure that business strategy and risk management activities are aligned. Business plans are also reviewed by MHI's Risk Management function to ensure that planned developments are achievable given MHI's risk management capabilities, and to form a view with regard to the balance of risk and reward attributable to planned activities.

As part of its business planning activities MHI also conducts capital planning to ensure that an appropriate balance between capital resources and capital requirements is maintained through the planning cycle. As part of its capital planning framework, MHI utilises stress tests to ensure that it is able to maintain a sound financial position in the event of severe economic stress. Stress tests are developed based upon potential future scenarios, selected in the light of MHI's risk profile and plausible future market and economic developments. Stress tests are conducted so as to apply selected scenarios in a consistent manner to the market, credit and liquidity risks to which MHI is exposed and to take account of any concentrations of exposure.

Adequacy of risk management arrangements

MHI assesses the adequacy of its risk management framework and of the amount of capital and liquidity that it needs to hold in respect of its risk profile on an annual basis, or more frequently if required. This assessment is formally documented within MHI's ICAAP and Internal Liquidity Adequacy Assessment Process (ILAAP), and is approved by the Board.

MHI's most recent ICAAP and ILAAP concluded that the risk management arrangements adopted by MHI were adequate in relation to its risk profile and strategy. Further, through its risk management framework, risk appetite and limit framework, independent reviews and ongoing programme of enhancements, MHI confirms that its risk management is effective.

4. Risk profile

Risk profile

MHI's business strategy is based on the provision of intermediation services within the capital markets for MHI's international client base. In keeping with this overall strategy, MHI operates Investment Banking, and Markets and Products business lines. Investment Banking services chiefly comprise the underwriting and distribution of new debt and equity issuance on behalf of MHI's clients together with the provision of mergers & acquisition services. Within its Markets and Products division MHI acts as Mizuho Securities Co. Ltd.'s primary dealer and provider of secured financing in European debt securities, offers broking services in Japanese and Asian equities, and provides derivative risk management solutions to clients.

The Board requires that a cautious to moderate risk profile is maintained in pursuit of this strategy. MHI's Investment Banking and equity broking activities result in low levels of risk exposure as underwriting activity is predominantly conducted without accepting significant underwriting risk and equity broking activity does not expose MHI directly to equity market risk. Fixed income trading activities result in low to moderate levels of risk as MHI maintains sovereign, financial and corporate inventory, provides securities financing services, and offers predominantly vanilla and cleared derivative risk management solutions to clients.

The Board's risk appetite with respect to capital is quantified with reference to minimum capital requirements and stress testing, and ensures an appropriate surplus is maintained over MHI's assessed capital requirements; this includes regulatory TCR and capital buffers, ensuring that MHI meets the PRA's capital requirements on an ongoing basis. Aggregate risk appetite measure is supported by a range of supporting limits and metrics which facilitate the control of individual risk factors at a detailed operational level. Key regulatory metrics are shown below:

Table 6: Key regulatory metrics

| | 2018 £m | 2017 £m |
|---|------------|------------------|
| Available capital | | |
| Common Equity Tier 1 (CET1) | 690.9 | 658.3 |
| Tier 2 | 45.0 | 45.0 |
| Total capital | 735.9 | 703.3 |
| RWAs | | |
| Total RWAs | 2,257.0 | 2,002.2 |
| Risk-based capital ratios as a percentage of RWA | | |
| CET1 ratio | 30.6% | 32.9% |
| Tier 1 ratio | 30.6% | 32.9% |
| Total capital ratio | 32.6% | 35.1% |
| Additional CET1 buffer requirements as a percentage of RWA | | |
| CCoB requirement (2.5% from 2019) | 1.875% | 1.250% |
| Institution-specific CCyB requirement | 0.074% | 0.081% |
| Total of bank CET1 specific buffer requirements | 1.949% | 1.331% |
| EBA leverage ratio | | |
| Total EBA leverage ratio exposure measure | 15,347.8 | 15,108.3 |
| EBA leverage ratio | 4.50% | 4.36% |
| Liquidity Coverage Ratio⁵ (LCR) | | |
| Total High Quality Liquid Assets (HQLAs) | 1,996.8 | N/A ⁶ |
| Total net cash outflow | 517.3 | N/A |
| LCR | 396% | N/A |

Note: MHI does not currently apply IFRS, therefore fully loaded Expected Credit Loss (ECL) accounting model (IFRS9) values are not applicable and have not been disclosed.

⁵ These values and figures represent the simple average of month-end observations over the twelve months preceding 31 March 2018 as per the EBA guidance.

⁶ Not applicable as this disclosure is being made for the first time in 2018, for further details refer to Section 11 Liquidity Risk.

5. Capital resources

Capital ratios

MHI has continued to maintain capital resources significantly above the minimum requirements established by the Capital Requirements Regulation (EU) No 575/2013. MHI's ratio of tier 1 common equity to Pillar 1 RWAs is given below:

Table 7: Tier 1 capital ratios

| | 2018 | 2017 |
|----------------------|-------|-------|
| Tier 1 capital ratio | 30.6% | 32.9% |

Capital resources reconciliation

As at 31 March 2018, MHI's total capital resources consisted of £690.9m CET1, and £45m of Tier 2 capital.

The difference between total equity on an accounting basis and regulatory capital arises from regulatory adjustments, as shown below:

Table 8: Capital resources reconciliation

| | 2018 £m | 2017 £m |
|--|--------------|--------------|
| Share capital | 725.5 | 725.5 |
| Reserves | 36.1 | 10.9 |
| Total equity (Accounting) | 761.6 | 736.4 |
| Regulatory adjustments to accounting total equity | | |
| Prudent valuation adjustment | (4.7) | (6.6) |
| Intangible assets | (66.0) | (71.5) |
| Total CET1 | 690.9 | 658.3 |
| Total Tier 2 capital | 45.0 | 45.0 |
| Total capital resources (Regulatory) | 735.9 | 703.3 |

Table 9: Own Funds

| | 2018 £m | 2017 £m |
|--|----------------|----------------|
| CET1: instruments and reserves | | |
| 1 Capital instruments and the related share premium accounts | 725.5 | 725.5 |
| 2 Retained earnings | 39.8 | 12.2 |
| Previous years retained earnings | 12.2 | - |
| Profit or loss eligible | 27.6 | 12.2 |
| 3 Accumulated other comprehensive income (and other reserves) | (3.7) | (1.3) |
| 6 CET1 before regulatory adjustments | 761.6 | 736.4 |
| CET1: regulatory adjustments | | |
| 7 Additional value adjustments (negative amount) | (4.7) | (6.6) |
| 8 Intangible assets (net of related tax liability) (negative amount) | (66.0) | (71.5) |
| 28 Total regulatory adjustments to CET1 | (70.7) | (78.1) |
| 29 CET1 | 690.9 | 658.3 |
| 45 Tier 1 capital (T1 = CET1 + Additional Tier 1) | 690.9 | 658.3 |
| Tier 2 capital: instruments and provisions | | |
| 46 Capital instruments and the related share premium accounts | 45.0 | 45.0 |
| 51 Tier 2 capital before regulatory adjustments | 45.0 | 45.0 |
| Tier 2 capital: regulatory adjustments | | |
| 57 Total regulatory adjustments to Tier 2 capital | - | - |
| 58 Tier 2 capital | 45.0 | 45.0 |
| 59 Total capital (TC = CET1 + Tier 2) | 735.9 | 703.3 |
| 60 Total RWAs | 2,257.0 | 2,002.2 |
| Capital ratios and buffers | | |
| 61 CET1 (as a percentage of total risk exposure amount) | 30.6% | 32.9% |
| 62 Tier 1 (as a percentage of total risk exposure amount) | 30.6% | 32.9% |
| 63 Total capital (as a percentage of total risk exposure amount) | 32.6% | 35.1% |
| 64 Institution specific buffer requirement (CET1 requirement in accordance with article 92 (1) (a) plus CCoB and CCyB requirements, expressed as a percentage of risk exposure amount) | 1.95% | 1.33% |
| 65 of which: CCoB requirement | 1.875% | 1.250% |
| 66 of which: CCyB requirement | 0.074% | 0.081% |
| 68 CET1 available to meet buffers (as a percentage of risk exposure amount) ⁷ | 18.9% | 25.6% |

Note: Only rows relevant to MHI shown in Table 9, remaining rows from EBA disclosure template have been left out as these are nil rows.

⁷ At 31 March 2018, 62% of total CET1 was available to meet buffer requirements. This equates to 18.9% of CET1 as a percentage of risk exposure amounts. The disclosure for 2018 has been based on the PRA's TCR and PRA Buffer advice received in May 2018. In addition, in December 2017, the PRA also revised the definition of TCR. TCR is equal to the sum of the 8% Pillar 1 minimum capital requirement (CRR Article 92) plus any Pillar 2A requirement. The 2017 comparative calculated on the same basis as 2018 would be 19.6%.

6. Capital requirements

RWAs and Pillar 1 capital requirements

MHI's Pillar 1 capital requirements and RWAs as at 31 March 2018 are set out below by risk class. These requirements are further analysed in the following sections as referenced below:

Table 10: RWAs and Pillar 1 capital requirements

| | Section | 2018 RWAs £m | 2018 Pillar 1 capital requirements £m | 2017 RWAs £m | 2017 Pillar 1 capital requirements £m |
|---|---------|--------------------|--|--------------------|--|
| Interest rate position risk | 7 | 1,585.7 | 126.9 | 1,380.5 | 110.4 |
| Equity position risk | 7 | - | - | - | - |
| Foreign currency position risk | 7 | 13.0 | 1.0 | 12.9 | 1.0 |
| Market risk total | | 1,598.7 | 127.9 | 1,393.4 | 111.4 |
| Counterparty credit risk | 9 | 182.3 | 14.6 | 184.5 | 14.8 |
| Concentration risk | 8 | - | - | - | - |
| Credit risk | 8 | 98.7 | 7.9 | 117.7 | 9.5 |
| Credit risk total | | 281.0 | 22.5 | 302.1 | 24.2 |
| Operational risk | 10 | 377.3 | 30.2 | 306.7 | 24.5 |
| Total Pillar 1 capital requirement | | 2,257.0 | 180.6 | 2,002.2 | 160.1 |

Pillar 2 capital requirements

The PRA prescribes a TCR to firms as part of its supervision of the banking sector. MHI has been issued with a TCR by the PRA in May 2018 and maintains capital that exceeds this requirement. Applying TCR issued in May 2018 on 31 March 2018 data, MHI's TCR would have been £265.4m⁸. This was met entirely with CET1 capital.

The MHI ICAAP provides an assessment of risks not covered or not fully captured through Pillar 1 capital requirements together with Group's own quantification of those risks. MHI ensures that it maintains capital which also exceeds this internal assessment of risk exposures. Some of the key risks assessed within the ICAAP under Pillar 2A include:

Risks not fully captured under Pillar 1

- Operational risk - operational risk losses measured using MHI's internal approach to assessing potential operational risk scenarios.
- Concentration risk - the risk of additional losses arising due to a higher level of default correlation than is assumed in Pillar 1 approaches; for example, due to sectoral concentrations.
- Counterparty risk - additional counterparty risk exposure measured using MHI's credit portfolio model (Value at Risk calculated for the credit portfolio model).
- Market risk - additional market risk exposure calculated using market stress and issuer default scenarios measured at the 99th percentile.

Risks not included under Pillar 1

- Pension risk - the risk of additional defined benefit pension contributions arising due to adverse movements in

⁸ On 12 December 2017, the PRA issued MHI with Individual Capital Guidance (ICG). MHI's ICG as at 31 March 2018 was £298.5mn. MHI met the ICG with 100% CET1. On 25 May 2018, the PRA issued MHI with a TCR which modified the 12 December 2017 ICG.

market rates or increases in longevity.

- Liquidity risk - additional costs incurred in a liquidity stress scenario.
- Structural foreign exchange risk - the risk of deterioration of MHI's capital surplus due to the revaluation of non-sterling risk assets with regard to foreign exchange rates.
- Interest rate risk in the banking book - the risk of losses due to adverse interest rate movements which impact non-trading assets and liabilities.

The ICAAP forecasts capital requirements and capital resources under stressed scenarios, which enables MHI to make an internal assessment of the capital buffer required to ensure that it will continue to meet the PRA's capital requirements throughout the economic cycle. MHI maintains capital which exceeds the higher of the TCR and the PRA's requirements and its internal assessment of potential future capital needs.

CRD IV capital buffers

Introduction

Alongside the minimum capital requirements, CRD IV requires institutions to hold capital buffers that can be drawn down in times of economic stress to absorb losses. Specific capital buffers that MHI is required to hold include:

Capital conservation buffer (CCoB)

The CCoB is designed to ensure that institutions build up capital buffers outside of times of stress that can be drawn upon if required. The requirement is 2.5% of RWAs but has been phased in from 2016 in steps of 0.625% per annum to the full value in 2019. The CCoB at 31 March 2018 was 1.875%.

Countercyclical capital buffer (CCyB)

The CCyB is designed to require financial institutions to hold additional capital to reduce the build-up of systemic risk in a credit boom by providing additional loss absorbing capacity and acting as an incentive to limit further credit growth.

The following table shows all positive CCyB rates recognised or set by the Financial Policy Committee (FPC) on foreign exposures for UK firms in specific countries which are relevant to MHI at 31 March 2018.

Table 11: CCyB rates on foreign exposures set by the FPC

| Country | Current CCyB rate | Implementation date |
|----------------|-------------------|---------------------|
| Czech Republic | 0.50% | 01 January 2017 |
| Sweden | 2.00% | 19 March 2017 |
| Slovakia | 0.50% | 01 August 2017 |
| Iceland | 1.25% | 01 November 2017 |
| Norway | 2.00% | 31 December 2017 |
| Hong Kong | 1.88% | 01 January 2018 |

Each institution's specific CCyB rate is a weighted average of the CCyBs that apply in the jurisdictions where the institution's relevant credit exposures are located. The FPC is responsible for setting the UK CCyB rate (for credit exposures located in the UK), and has indicated that this will be set at 1% in normal economic conditions. Since 31 March 2018, the CCyB rate has been increased to 0.5% by the FPC (effective from 27 June 2018), with a further plan to increase it to 1%, effective from 28 November 2018. MHI continues to adhere to these buffer requirements.

Table 12 shows MHI's specific CCyB rate and requirement. The table is split down into:

- The total risk exposure amount, for exposures in all countries;
- The institution specific CCyB rate, which is MHI's weighted-average CCyB rate, calculated by multiplying the total exposure to each geographical area by the CCyB rate set for that region (including those countries with a CCyB rate set to zero); and
- The institution specific CCyB requirement, which is calculated by multiplying the above two figures together.

Table 12: Institution-specific CCyB

| CCyB metric | 2018 £m | 2017 £m |
|---------------------------------------|------------|------------|
| Total risk exposure amount | 2,257.0 | 2,002.2 |
| Institution-specific CCyB rate (%) | 0.074% | 0.081% |
| Institution-specific CCyB requirement | 1.67 | 1.62 |

As at 31 March 2018, geographical breakdown of credit exposures relevant for the calculation of the CCyB is shown in Table 13:

Table 13: Geographical breakdown of credit exposures relevant for the CCyB calculation

| Breakdown by country | General credit exposures | Trading book exposures | Own funds requirements | | Total | Own funds req. weights | CCyB rate |
|---------------------------|--------------------------|---|------------------------------------|--------------------------------|--------------|------------------------|------------|
| | Exposure value | Sum of long & short positions of trading book exposures | of which: General credit exposures | of which: General trading book | | | |
| | £m | £m | £m | £m | £m | | |
| | 010 | 030 | 080 | 090 | 070 | 110 | 120 |
| United Arab Emirates | 0.00 | 14.08 | 0.00 | 0.66 | 0.66 | 0.01 | - |
| Austria | 0.00 | 6.48 | 0.00 | 0.38 | 0.38 | 0.01 | - |
| Australia | 0.00 | 19.83 | 0.00 | 1.03 | 1.03 | 0.02 | - |
| Azerbaijan | 0.00 | 0.00 | 0.00 | 0.00 | 0.00 | 0.00 | - |
| Bahrain | 0.00 | 0.86 | 0.00 | 0.07 | 0.07 | 0.00 | - |
| Belgium | 0.00 | 13.72 | 0.00 | 0.47 | 0.47 | 0.01 | - |
| Bermuda | 0.00 | 2.39 | 0.00 | 0.04 | 0.04 | 0.00 | - |
| Canada | 0.00 | 13.86 | 0.00 | 0.42 | 0.42 | 0.01 | - |
| China | 0.00 | 0.54 | 0.00 | 0.01 | 0.01 | 0.00 | - |
| Czech Republic | 0.00 | 0.14 | 0.00 | 0.01 | 0.01 | 0.00 | 0.50% |
| Germany | 0.00 | 59.37 | 0.00 | 1.57 | 1.57 | 0.03 | - |
| Denmark | 0.00 | 5.83 | 0.00 | 0.47 | 0.47 | 0.01 | - |
| Estonia | 0.00 | 6.78 | 0.00 | 0.54 | 0.54 | 0.01 | - |
| Spain | 0.00 | 24.25 | 0.00 | 1.77 | 1.77 | 0.04 | - |
| Finland | 0.00 | 3.05 | 0.00 | 0.24 | 0.24 | 0.00 | - |
| France | 0.00 | 157.91 | 0.00 | 7.75 | 7.75 | 0.16 | - |
| United Kingdom | 87.58 | 74.49 | 7.03 | 3.72 | 10.75 | 0.22 | - |
| Hong Kong | 0.00 | 0.41 | 0.00 | 0.03 | 0.03 | 0.00 | 1.88% |
| Ireland | 0.00 | 12.41 | 0.00 | 0.83 | 0.83 | 0.02 | - |
| Italy | 0.00 | 47.18 | 0.00 | 2.25 | 2.25 | 0.05 | - |
| Japan | 6.06 | 5.20 | 0.48 | 0.10 | 0.59 | 0.01 | - |
| Jersey | 0.00 | 2.95 | 0.00 | 0.18 | 0.18 | 0.00 | - |
| Korea, Republic of | 0.02 | 0.50 | 0.00 | 0.00 | 0.01 | 0.00 | - |
| Cayman Islands | 2.81 | 9.05 | 0.22 | 0.15 | 0.37 | 0.01 | - |
| Luxembourg | 0.00 | 28.84 | 0.00 | 1.61 | 1.61 | 0.03 | - |
| Malaysia | 0.00 | 0.00 | 0.00 | 0.00 | 0.00 | 0.00 | - |
| Mexico | 0.00 | 0.49 | 0.00 | 0.01 | 0.01 | 0.00 | - |
| Netherlands | 0.28 | 155.78 | 0.02 | 6.70 | 6.72 | 0.14 | - |
| Norway | 0.00 | 2.78 | 0.00 | 0.02 | 0.02 | 0.00 | 2.00% |
| New Zealand | 0.00 | 5.44 | 0.00 | 0.44 | 0.44 | 0.01 | - |
| Panama | 0.00 | 6.27 | 0.00 | 0.10 | 0.10 | 0.00 | - |
| Portugal | 0.00 | 0.68 | 0.00 | 0.05 | 0.05 | 0.00 | - |
| Qatar | 0.00 | 0.17 | 0.00 | 0.00 | 0.00 | 0.00 | - |
| Sweden | 0.00 | 28.66 | 0.00 | 1.77 | 1.77 | 0.04 | 2.00% |
| Singapore | 0.00 | 0.61 | 0.00 | 0.05 | 0.05 | 0.00 | - |
| Taiwan, Province of China | 0.00 | 0.00 | 0.00 | 0.00 | 0.00 | 0.00 | - |
| United States | 0.15 | 213.50 | 0.01 | 7.82 | 7.84 | 0.16 | - |
| Virgin Islands, British | 0.22 | 5.36 | 0.02 | 0.25 | 0.27 | 0.01 | - |
| Total | 97.12 | 929.86 | 7.79 | 41.50 | 49.29 | | - |

Leverage ratio

Management of exposure to leverage forms part of MHI's business planning process and risk appetite framework. MHI's leverage ratio as at 31 March 2018 meets the expected future requirements set out above. MHI is committed to ensuring that full compliance with all relevant regulatory requirements is maintained.

The firm's leverage ratio is monitored on a daily basis and a Recovery Plan Early Warning Indicator has been established to ensure the firm's leverage balance sheet is sustainable and in line with the Board's Risk Appetite.

The leverage ratio over the reporting period has remained stable (31 March 2018: 4.50%; 31 March 2017: 4.36%).

Table 14: Summary reconciliation of accounting assets and leverage ratio exposures

| CRR leverage ratio exposure | 2018 £m | 2017 £m |
|---|--------------------|--------------------|
| Total assets as per published financial statements | 15,517.3 | 15,395.2 |
| Adjustment for entities which are consolidated for accounting purposes but are outside the scope of regulatory consolidation | - | - |
| (Adjustment for fiduciary assets recognised on the balance sheet pursuant to the applicable accounting framework but excluded from the leverage ratio total exposure measure in accordance with Article 429(13) of Regulation (EU) No 575/2013) | - | - |
| Adjustments for derivative financial instruments | (44.1) | (428.3) |
| Adjustment for securities financing transactions (SFTs) | (60.5) | 213.6 |
| Adjustments for off-balance sheet items (i.e. conversion to credit equivalent amounts of off-balance sheet exposures) | 5.8 | 5.9 |
| (Adjustment for intragroup exposures excluded from the leverage ratio total exposure measure in accordance with Article 429(7) of Regulation (EU) No 575/2013) | - | - |
| (Adjustment for exposure excluded from the leverage ratio total exposure measure in accordance with Article 429(14) of Regulation (EU) No 575/2013) | - | - |
| Other adjustments | (70.7) | (78.1) |
| Leverage ratio total exposure measure | 15,347.8 | 15,108.3 |

Table 15: Leverage ratio common disclosure

| | | 2018 £m | 2017 £m |
|--|---|-----------------|-----------------|
| On-balance sheet exposures (excluding derivatives and SFTs⁹) | | | |
| 1 | On-balance sheet items (excluding derivatives, SFTs and fiduciary assets, but including collateral) | 5,982.5 | 4,753.4 |
| 2 | (Asset amounts deducted in determining Tier 1 capital) | (70.7) | (78.1) |
| 3 | Total on-balance sheet exposures (excluding derivatives, SFT's and fiduciary assets) (sum of lines 1 and 2) | 5,911.8 | 4,675.3 |
| 4 | Replacement cost associated with <i>all</i> derivatives transactions (i.e. net of eligible cash variation margin) | 123.2 | 51.1 |
| 5 | Add-on amounts for PFE associated with all derivatives transactions (mark-to-market method) | 1,968.8 | 912.1 |
| EU-5a | Exposure determined under Original Exposure Method | - | - |
| 6 | Gross-up for derivatives collateral provided where deducted from the balance sheet assets pursuant to the applicable accounting framework | - | - |
| 7 | (Deductions of receivables assets for cash variation margin provided in derivatives transactions) | - | - |
| 8 | (Exempted CCP ¹⁰ leg of client-cleared trade exposures) | 0.0 | 0.0 |
| 9 | Adjusted effective notional amount of written credit derivatives | 115.6 | 559.7 |
| 10 | (Adjusted effective notional offsets and add-on deductions for written credit derivatives) | (115.6) | (452.8) |
| 11 | Total derivatives exposures (sum of lines 4 to 10) | 2,092.1 | 1,070.1 |
| SFT exposures | | | |
| 12 | Gross SFT assets (with no recognition of netting), after adjusting for sales accounting transactions | 15,828.1 | 16,558.8 |
| 13 | (Netted amounts of cash payables and cash receivables of gross SFT assets) | (8,660.6) | (7,425.8) |
| 14 | Counterparty credit risk exposure for SFT assets | 170.6 | 224.0 |
| EU-14a | Derogation for SFTs: Counterparty credit risk exposure in accordance with Articles 429b(4) and 222 Regulation (EU) No 575/2013 | 0.0 | 0.0 |
| 15 | Agent transaction exposures | 0.0 | 0.0 |
| EU-15a | (Exempted CCP leg of client-cleared SFT exposure) | 0.0 | 0.0 |
| 16 | Total securities financing transaction exposures (sum of lines 12 to 15a) | 7,338.1 | 9,357.0 |
| Other off-balance sheet exposures | | | |
| 17 | Off-balance sheet exposures at gross notional amount | 5.8 | 5.9 |
| 18 | (Adjustments for conversion to credit equivalent amounts) | (0.0) | 0.0 |
| 19 | Other off-balance sheet exposures (sum of lines 17 to 18) | 5.8 | 5.9 |
| Exempted exposures in accordance with Article 429(7) and (14) of Regulation (EU) No 575/2013 (on and off balance sheet) | | | |
| EU-19a | (Intragroup exposures (solo basis) exempted in accordance with Article 429(7) of Regulation (EU) No 575/2013 (on and off balance sheet)) | - | - |
| EU-19b | (Exposures exempted in accordance with Article 429 (14) of Regulation (EU) No 575/2013 (on and off balance sheet)) | - | - |
| Capital and total exposure measure | | | |
| 20 | Tier 1 capital | 690.9 | 658.3 |
| 21 | Leverage ratio total exposure measure (sum of lines 3,11, 16, 19, EU-19a and EU-19b) | 15,347.8 | 15,108.3 |
| Leverage ratio | | | |
| 22 | Leverage ratio | 4.50% | 4.36% |
| Choice on transitional arrangements and amount of derecognised fiduciary items | | | |
| EU-23 | Choice on transitional arrangements for the definition of the capital measure | Fully phased in | Fully phased in |
| EU-24 | Amount of derecognised fiduciary items in accordance with Article 429(11) of Regulation (EU) No 575/2013 | - | - |

⁹ SFTs: Securities Financing Transactions¹⁰ CCP: Central Counterparty

Table 16: Split-up of on balance sheet exposures (excluding derivatives, SFTs and exempted exposures)

| | | 2018 £m | 2017 £m |
|-------------|--|----------------|----------------|
| EU-1 | Total on-balance sheet exposures (excluding derivatives, SFTs, and exempted exposures), of which: | 5,982.5 | 4,753.4 |
| EU-2 | Trading book exposures | 5,608.1 | 4,419.4 |
| EU-3 | Banking book exposures ¹¹ , of which: | 374.5 | 334.0 |
| EU-4 | Covered bonds | - | - |
| EU-5 | Exposures treated as sovereigns | 234.5 | 114.1 |
| EU-6 | Exposures to regional governments, Multilateral Development Banks, international organisations and Public Sector Entities not treated as sovereigns | - | - |
| EU-7 | Institutions | 52.0 | 128.4 |
| EU-8 | Secured by mortgages of immovable properties | - | - |
| EU-9 | Retail exposures | - | - |
| EU-10 | Corporate | - | - |
| EU-11 | Exposures by default | - | - |
| EU-12 | Other exposures (e.g. equity, securitisations, and other non-credit obligation assets) | 88.0 | 91.5 |

¹¹ Banking Book exposures in the leverage ratio calculation are based on exposures subject to credit risk under the standardised approach. Exposures at default are derived by reducing gross exposures by allowable credit risk mitigation.

7. Market risk

Risk management

Market risk is the risk of financial loss or reduced valuation arising from adverse market movements (including changes in interest rates, foreign exchange rates, credit spreads, bond prices, equity prices and their associated volatilities). Credit valuation adjustments are considered within section 9 of this disclosure.

Market risk appetite is a component of MHI's overall risk appetite and is approved by the Board. MHI provides liquidity to customers of the wider Mizuho Financial Group, Inc. group of companies in European debt products, and holds inventory in its core product classes. MHI's market risk appetite is to maintain a cautious to moderate risk profile, whilst focusing upon client transaction flows in actively traded vanilla products.

MHI's market risk exposures arise principally from trading operations in government, supranational, sub-sovereign, agency, corporate debt instruments and derivatives. Exposures are partially mitigated through the execution of offsetting transactions in other debt instruments or through the use of hedging derivative contracts.

Market risk is managed in accordance with a variety of risk measures including sensitivity based measures (e.g. sensitivity to a basis point move in interest rates or credit spreads), VaR, and stress testing. Market risk limits are set and monitored using these measures as appropriate on a business line basis. Key risk exposures, which incorporate the effect of hedging activity, are monitored by MHI's Risk Management function on a daily basis.

Market risk exposure is routinely monitored by the Risk Management Committee, and is overseen by the Board Risk Committee and the Board. Significant exposures are escalated in accordance with an established market risk policy.

Balance sheet split of trading and banking books

Trading books comprise those positions that are held with trading intent or to hedge the trading book. In addition to these positions, the trading books also contain assets held as part of the high quality liquid asset portfolio for the purpose of managing liquidity risks and ensuring ongoing conformance with the LCR.

MHI's balance sheet is split between trading and non-trading, or 'banking', books as shown below:

Table 17: Balance sheet split by trading and banking books

| Balance sheet category | 2018 | 2018 | 2018 |
|--|--------------------|--------------------|-----------------|
| | Trading Book £m | Banking book £m | Total £m |
| Reverse repurchase agreements | 7,393.0 | - | 7,393.0 |
| Debt and equity securities | 5,249.0 | 0.7 | 5,249.7 |
| Derivative assets | 2,130.7 | 5.5 | 2,136.2 |
| Loans and advances to banks | - | 356.4 | 356.4 |
| Shares in group undertakings | - | 6.0 | 6.0 |
| Intangible fixed assets | - | 66.0 | 66.0 |
| Tangible fixed assets | - | 31.1 | 31.1 |
| Other assets, prepayments and accruals | 39.9 | 239.0 | 278.9 |
| Total assets | 14,812.6 | 704.7 | 15,517.3 |
| Deposits by banks | - | 398.0 | 398.0 |
| Customer accounts | - | 337.8 | 337.8 |
| Repurchase agreements | 5,163.3 | - | 5,163.3 |
| Short trading positions | 4,561.1 | - | 4,561.1 |
| Derivative liabilities | 2,026.2 | 4.4 | 2,030.6 |
| Debt securities in issue | - | 1,773.3 | 1,773.3 |
| Subordinated debt | - | 45.2 | 45.2 |
| Other liabilities, provisions and accruals | 36.9 | 409.5 | 446.4 |
| Total liabilities | 11,787.5 | 2,968.2 | 14,755.7 |

Internal risk measures

MHI has continued to manage its market risk at low levels over the past year, with average VaR of £1.7m (2017: £1.5m). The table below shows MHI's internal VaR measurement, determined using a 99th percentile confidence level over a one day time horizon, by risk factor:

Table 18: VaR by risk factor

| VaR by risk factor | 2018 | | | | 2017 | | | |
|-----------------------|-------------|---------------|------------|------------|-------------|---------------|------------|------------|
| | Close £m | Average £m | High £m | Low £m | Close £m | Average £m | High £m | Low £m |
| Interest rate risk | 0.8 | 0.9 | 2.3 | 0.6 | 0.9 | 0.8 | 2.1 | 0.4 |
| Credit spread risk | 1.3 | 1.7 | 3.0 | 0.6 | 1.4 | 1.1 | 2.0 | 0.4 |
| Equity risk | - | - | - | - | - | - | 0.3 | - |
| Foreign exchange risk | 0.1 | 0.1 | 0.3 | - | 0.4 | 0.2 | 0.5 | - |
| Total VaR | 1.2 | 1.7 | 2.6 | 1.0 | 1.8 | 1.5 | 2.1 | 0.8 |

Note: Total VaR assumes some diversification across risk types, and does thus not represent the simple sum of component risk factors.

Pillar 1 requirements by risk category

MHI's largest sources of market risk derive from general interest rate risk on debt instruments within its trading inventory of flow derivative instruments, and specific risk on debt instruments from the trading inventory of fixed income securities. Specific risk on debt instruments arising from the trading of fixed income securities represents exposure to risk factors related to the issuer relevant to the pricing of individual debt securities.

The table below shows MHI's Pillar 1 market risk capital requirements, calculated using the standardised approach by risk factor:

Table 19: Pillar 1 market risk under standardised approach

| Market risk under standardised approach | 2018 £m | 2017 £m |
|---|--------------|--------------|
| General interest rate risk - debt instruments | 70.8 | 56.8 |
| Specific risk - debt instruments | 56.1 | 53.6 |
| General interest rate risk - equity instruments | - | - |
| Specific risk - equity instruments | - | - |
| Foreign exchange risk | 1.0 | 1.0 |
| Total market risk | 127.9 | 111.4 |

Non-traded market risk

Market risk exposures which arise from non-trading activities are not captured or fully captured through Pillar 1 capital requirements, and thus attract Pillar 2 charges. The market risk exposures which arise in respect of non-trading activities are summarised below:

Table 20: Summary of non-traded market risk

| | Principal risk factors | | | |
|------------------|------------------------|-----------|---------------|--------|
| | Interest rate | Inflation | Credit spread | Equity |
| Non-trading book | ✓ | ✗ | ✗ | ✓ |
| Pension scheme | ✓ | ✓ | ✓ | ✓ |

Equity risk in the banking book

MHI's most significant non-trading equity asset constitutes a carried interest entitlement in a private equity healthcare fund, representing a contractual interest in the fund's performance in excess of predefined thresholds. This interest had a fair value of £0.5m as at 31 March 2018.

MHI maintains holdings of Mizuho Financial Group, Inc. shares in connection with share based remuneration arrangements as discussed in section 12.

The balance sheet value of non-trading equity investments is shown below by investment category. These holdings are recorded on the balance sheet at fair value, with revaluation gains taken through profit and loss:

Table 21: Banking book equity by category

| Banking book equity | 2018 Balance sheet value £m | 2017 Balance sheet value £m |
|----------------------------------|--|--|
| Private equity | 0.5 | 0.8 |
| Exchange traded | 6.2 | 6.0 |
| Other | - | - |
| Total banking book equity | 6.7 | 6.8 |

Interest rate risk in the banking book

The non-trading book principally comprises net balances of unsecured funding raised and managed by MHI's Treasury & Funding function in support of trading activities. Funding is raised across a range of maturities to ensure diversification of repayment risk and is issued on both a fixed and floating rate basis. MHI's policy is to minimise interest rate risk in the banking book through the use of derivative interest rate hedges, which leaves MHI exposed to falling short term interest rates. A summary of MHI's non-trading notional interest rate risk exposure by maturity band is included in Note 30B of the 31 March 2018 Financial Statements.

Pension scheme market risk

MHI sponsors one defined benefit pension plan, the Mizuho International plc Retirement Benefits Scheme (the "Scheme"). The Scheme closed to new members in 1996. Accrual of further liabilities ceased on the retirement of the last active member, prior to the 31 March 2009 actuarial valuation of the Scheme. The requirement to fund the Scheme is borne jointly by MHI and by DIAM International Limited in proportion to the historical association of Scheme members to those employers.

The Scheme's investment strategy is set by the Trustees, in consultation with MHI and recorded in the Scheme's Statement of Investment Principles. The strategy involves retaining longevity risk within the Scheme and holding a proportion of return seeking assets.

With regard to market risks, the Scheme's assets give rise to interest rate, credit spread and equity risk and the Scheme's liabilities give rise to interest rate and inflation risk.

8. Credit risk

Risk management

Credit risk is the risk of financial loss arising from the failure of a customer, client, issuer, or counterparty to meet its contractual obligations. MHI's activities that give rise to counterparty credit risk, such as securities financing, derivatives and securities trading which supports MHI's market-making are discussed in section 9 and the credit risk arising from exposure to issuers of traded debt is discussed within section 7.

Credit risk appetite forms a key component of MHI's overall risk appetite and is approved by the Board. MHI employs a number of metrics in support of this, which are used to limit and monitor the credit risk exposures in accordance with credit risk management policies.

Aside from those credit risks discussed in sections 7 and 9, the principal sources of non-trading credit risk exposures arise from funding operations through the placement of cash resources and deposits with third parties. Credit exposures also arise in the ordinary course of business through short term receivables and, in addition, Pillar 1 credit risk charges also apply to investments in fixed assets. MHI does not undertake commercial or retail lending activity and does not extend credit through the provision of guarantees.

Non-trading credit risk exposures are measured in accordance with balance sheet carrying values, after taking account of any applicable credit risk mitigation arrangements and adjustments for credit impairment.

Pillar 1 requirements

RWAs and Pillar 1 credit risk capital requirements calculated under the standardised approach are set out below:

Table 22: Credit risk RWAs and Pillar 1 capital requirements by exposure class

| | 2018 | | 2017 | |
|---|-------------|--|--------------|--|
| | RWAs £m | Pillar 1 capital requirements £m | RWAs £m | Pillar 1 capital requirements £m |
| Central government or central banks | - | - | - | - |
| Public sector entities | - | - | - | - |
| Multilateral development banks | - | - | - | - |
| Regional governments or local authorities | - | - | - | - |
| Institutions | 10.4 | 0.8 | 25.7 | 2.1 |
| Corporates | 0.0 | 0.0 | - | - |
| Equity | 7.1 | 0.6 | 6.9 | 0.6 |
| Other ¹² | 81.1 | 6.5 | 85.1 | 6.8 |
| Total | 98.7 | 7.9 | 117.7 | 9.5 |

Analysis of credit risk exposures

Credit risk exposures by credit quality

Credit risk exposures before and after credit risk mitigation (CRM) and RWAs by credit quality, in accordance with the credit quality steps used within the standardised approach, are given below.

Under the standardised approach, credit ratings assigned by credit rating agencies are used in the calculation of RWAs. The PRA determines which rating agencies may be used in the calculation of risk weights, of which MHI uses ratings assigned by Standard & Poor's Financial Services LLC (S&P), Moody's Investor Service, Inc. (Moody's) and Fitch Ratings, Inc. (Fitch). Credit exposures must be assigned to one of six credit quality steps if a rating is available. Risk weight percentages are assigned based on the credit quality step, exposure class and maturity of each credit exposure. Where an external credit rating is not available or where exposures exist to central counterparties, a default treatment is applied as specified by regulatory guidance.

Table 23: Credit risk exposures and RWAs by credit quality step

¹² 'Other' exposure class relates to items defined in article 134 of the CRR – tangible assets, and prepayments and accrued income for which counterparty cannot be determined.

| 2018 | | | | |
|-----------------------|-----------------------------|-------------|---------------------------|-------------|
| | Gross credit exposure £m | CRM £m | Net credit exposure £m | RWAs £m |
| Credit quality step 1 | 234.5 | - | 234.5 | - |
| Credit quality step 2 | 83.1 | 31.1 | 52.0 | 10.4 |
| Credit quality step 3 | 0.0 | - | - | 0.0 |
| Credit quality step 6 | 6.8 | - | 6.8 | 7.1 |
| Unrated | 81.1 | - | 81.1 | 81.1 |
| Total | 405.5 | 31.1 | 374.5 | 98.7 |

| 2017 | | | | |
|-----------------------|-----------------------------|-------------|---------------------------|--------------|
| | Gross credit exposure £m | CRM £m | Net credit exposure £m | RWAs £m |
| Credit quality step 1 | 114.1 | - | 114.1 | - |
| Credit quality step 2 | 196.0 | 67.6 | 128.4 | 25.7 |
| Credit quality step 3 | - | - | - | - |
| Credit quality step 6 | 0.8 | - | 0.8 | 1.3 |
| Unrated | 90.7 | - | 90.7 | 90.7 |
| Total | 401.6 | 67.6 | 334.0 | 117.7 |

Gross credit exposures by exposure class

Gross credit risk exposures, before the impact of credit risk mitigation, as at year end and averaged over the financial year are summarised below:

Table 24: Gross credit risk exposures by exposure class

| | 2018 | | 2017 | |
|---|---------------------------------|-------------------------------------|---------------------------------|-------------------------------------|
| | Average gross exposure £m | Year-end gross exposure £m | Average gross exposure £m | Year-end gross exposure £m |
| Central government or central banks | 122.6 | 234.5 | 106.2 | 114.1 |
| Public sector entities | - | - | - | - |
| Multilateral development banks | - | - | - | - |
| Regional governments or local authorities | - | - | - | - |
| Institutions | 128.0 | 83.1 | 123.5 | 195.9 |
| Corporates | 0.0 | 0.0 | - | - |
| Equity | 9.5 | 6.8 | 7.3 | 6.6 |
| Other | 76.8 | 81.1 | 84.3 | 85.0 |
| Total | 337.0 | 405.5 | 321.3 | 401.6 |

Geographic distribution of gross credit exposures

The geographic distribution of gross credit exposures as at 31 March 2018 is given below:

Table 25: Geographic distribution of gross credit risk exposures

| | 2018 | | | | | Total £m |
|---|--------------|-------------|-------------|--------------|-------------|--------------|
| | UK £m | Japan £m | US £m | Europe £m | Other £m | |
| Central government or central banks | 234.5 | - | - | - | - | 234.5 |
| Public sector entities | - | - | - | - | - | - |
| Multilateral development banks | - | - | - | - | - | - |
| Regional governments or local authorities | - | - | - | - | - | - |
| Institutions | 1.3 | 31.1 | 40.7 | 10.0 | 0.0 | 83.1 |
| Corporates | - | - | - | - | 0.0 | 0.0 |
| Equity | 0.6 | 6.1 | 0.2 | - | - | 6.8 |
| Other | 81.1 | - | - | - | - | 81.1 |
| Total credit risk exposure | 317.5 | 37.1 | 40.8 | 10.0 | 0.1 | 405.5 |

| | 2017 | | | | | Total £m |
|---|--------------|-------------|-------------|--------------|-------------|--------------|
| | UK £m | Japan £m | US £m | Europe £m | Other £m | |
| Central government or central banks | 114.1 | - | - | - | - | 114.1 |
| Public sector entities | - | - | - | - | - | - |
| Multilateral development banks | - | - | - | - | - | - |
| Regional governments or local authorities | - | - | - | - | - | - |
| Institutions | 30.5 | 67.6 | 84.7 | 13.1 | 0.0 | 196.0 |
| Corporates | - | - | - | - | 0.0 | 0.0 |
| Equity | 0.8 | 5.8 | - | - | - | 6.6 |
| Other | 85.0 | - | - | - | - | 85.0 |
| Total credit risk exposure | 230.4 | 73.4 | 84.7 | 13.1 | 0.1 | 401.6 |

Residual maturity of gross credit exposures

The residual maturity of gross credit exposures as at 31 March 2018 is given below:

Table 26: Residual maturity of gross credit risk exposures

| | 2018 | | | | Total £m |
|---|---------------------------|-----------------------|------------------------|------------------------|--------------|
| | Less than 1 year £m | 1 to 5 years £m | 5 to 10 years £m | Over 10 years £m | |
| Central government or central banks | 234.5 | - | - | - | 234.5 |
| Public sector entities | - | - | - | - | - |
| Multilateral development banks | - | - | - | - | - |
| Regional governments or local authorities | - | - | - | - | - |
| Institutions | 83.1 | - | - | - | 83.1 |
| Corporates | - | - | - | - | 0.0 |
| Equity | - | - | - | 6.8 | 6.8 |
| Other | 81.1 | - | - | - | 81.1 |
| Total credit risk exposure | 398.7 | - | - | 6.8 | 405.5 |

| | 2017 | | | | Total £m |
|---|---------------------------|-----------------------|------------------------|------------------------|--------------|
| | Less than 1 year £m | 1 to 5 years £m | 5 to 10 years £m | Over 10 years £m | |
| Central government or central banks | 114.1 | - | - | - | 114.1 |
| Public sector entities | - | - | - | - | - |
| Multilateral development banks | - | - | - | - | - |
| Regional governments or local authorities | - | - | - | - | - |
| Institutions | 196.0 | - | - | - | 196.0 |
| Corporates | 0.0 | - | - | - | 0.0 |
| Equity | - | - | - | 6.6 | 6.6 |
| Other | 85.0 | - | - | - | 85.0 |
| Total credit risk exposure | 395.0 | - | - | 6.6 | 401.6 |

Impairment adjustments

At each balance sheet date, MHI assesses whether those financial and other assets which are not accounted for at fair value through profit and loss are impaired. As at 31 March 2018, no adjustments in respect of asset impairment were made (31 March 2017: no impairment adjustments were made).

MHI's accounting policies concerning the treatment of impaired financial and non-financial assets are set out in its financial statements.

9. Counterparty credit risk

Risk management

Counterparty credit risk forms a key component of MHI's overall risk appetite, and is approved by the Board. MHI employs a number of metrics in support of this which are used to limit and monitor the credit risk exposures in accordance with credit risk management policies.

MHI is exposed to counterparty credit risk principally through derivative contracts and repurchase agreement contracts arising from its trading activities, and to a lesser extent from securities trading which supports MHI's market-making activities.

Counterparty credit risk methodology

Counterparty credit risk is assessed and limits are set in accordance with MHI's methodology. Exposure is evaluated by determining the potential size of counterparty exposures which may arise from transactions together with an assessment of the creditworthiness of the obligor.

The potential size of counterparty credit risk is a function of both current and potential future exposures. Potential future exposures to a counterparty default, which may arise through securities trading, derivatives, and repurchase agreement contracts, are estimated using historical volatilities of key pricing variables to those contracts over their remaining life.

Counterparty credit quality is assessed using external credit ratings where available, or alternatively an internal rating is assigned in accordance with internal credit rating methodology.

Counterparty credit limits are established in accordance with MHI's methodology for measuring counterparty credit risk, taking into account executed documentation with permissible netting and collateral management arrangements, and consistent with the overall credit risk appetite.

Counterparty credit risk mitigation

Risk mitigation techniques are used to reduce counterparty credit risks arising from MHI's activities. These techniques include the use of netting agreements, acceptance of collateral, application of haircuts, and execution of transactions with central counterparties, whereby credit risk to individual counterparties is replaced by exposure to a central counterparty.

Derivative and repurchase agreement trading activity is undertaken using netting agreements on a collateralised basis, unless exceptions are approved in accordance with credit risk policies. Collateral arrangements are governed by standard agreements (such as Credit Support Annexes to International Swaps and Derivatives Association (ISDA) Master Agreements and Global Master Repurchase Agreements). The forms of collateral which may be accepted are subject to MHI's internal credit risk policy, which seeks to ensure that in the event of counterparty default the value of collateral held is sufficient to compensate for losses arising from such default.

Repurchase agreement trading activity is principally conducted using high-quality government securities as collateral, and minimal use is made of sub-investment grade corporate securities as collateral. This is in line with MHI's requirement to only accept high quality collateral for margining purposes, which must be of at least of equivalent quality to the collateral of the underlying transaction. Collateral is revalued on a daily basis in accordance with collateral management procedures.

In order to recognise the effects of credit risk mitigation, a number of conditions must be met, and in particular agreements must be legally enforceable and legal title to collateral must be passed to MHI. Once these conditions are satisfied the effect of collateral is reflected through the reduction in the measure of credit exposure.

Credit valuation adjustments are established in accordance with valuation policies for derivative and repurchase agreement transactions. Credit valuation adjustments concerning individual counterparties are based upon the potential size of exposures to those counterparties, taking account of legally enforceable netting and collateral agreements, together with market pricing of the creditworthiness of those counterparties.

Correlated risk

Correlated or *wrong way* risk arises where the probability of counterparty default is positively correlated to the risk of the underlying transaction. MHI adopts an integrated market risk and credit risk stress testing methodology which highlights correlated exposures across a range of scenarios.

Credit risk policies have been implemented to mitigate *wrong way* risk which, for example, prohibit the acceptance of collateral issued by a connected entity to the transaction counterparty, and over-collateralisation. *Wrong way* risk is further controlled through the operation of a credit limit framework in respect of specific counterparties, groups of counterparties and countries.

Pillar 1 requirements

MHI's RWAs and Pillar 1 counterparty risk requirements, in respect of counterparty risk arising within trading and non-trading books, are set out below and are calculated using standardised methodology (e.g. mark-to-market method for derivative exposure):

Table 27: Counterparty credit RWAs and Pillar 1 capital requirements

| | 2018 | | 2017 | |
|--------------------------|------------|--|------------|--|
| | RWAs £m | Pillar 1 capital requirements £m | RWAs £m | Pillar 1 capital requirements £m |
| Counterparty credit risk | 182.3 | 14.6 | 184.5 | 14.8 |

Note: The total counterparty credit risk RWA and Pillar 1 capital requirement includes default funds, settlement risk and CVA capital requirement.

Analysis of counterparty risk exposures

RWAs and exposures by product type

An analysis of counterparty credit risk RWAs and exposures as at 31 March 2018 by product type is given below:

Table 28: Counterparty credit RWAs and exposures by product type

| | 2018 | | 2017 | |
|--------------------------------|--------------------|---|--------------|-------------------------------|
| | RWAs £m | Credit risk exposure ¹³ £m | RWAs £m | Credit risk exposure £m |
| Derivative contracts | 67.9 | 1,998.8 | 69.1 | 910.4 |
| Securities financing contracts | 55.2 | 325.7 | 45.0 | 471.0 |
| Other | 59.2 ¹⁴ | 66.4 ¹⁵ | 70.4 | 5.9 ¹⁶ |
| Total | 182.3 | 2,390.9 | 184.5 | 1,387.3 |

¹³ Credit risk exposure is shown as the credit exposure, calculated in accordance with Pillar 1 standardised rules using the mark-to-market approach, less deductions in respect of credit risk mitigation.

¹⁴ Includes a credit valuation adjustment charge, settlement and delivery risk charges, pre-funded default fund contributions and Treasury Default Loss Allocation Regime contribution.

¹⁵ Includes pre-funded default fund contributions and Treasury Default Loss Allocation Regime contribution.

¹⁶ The 2017 comparative calculated on the same basis as 2018 would be £57.9m.

Further analysis of credit risk exposure in respect of derivative contracts is given below, and shows the impact of netting benefits from legally enforceable netting agreements and collateral arrangements:

Table 29: Derivative counterparty credit risk exposures

| | 2018 Credit risk exposure £m | 2017 Credit risk exposure £m |
|---|---|---|
| Gross positive fair value of derivative contracts | 3,045.6 | 2,798.0 |
| Potential future credit exposure | 1,968.8 | 954.2 |
| Netting benefits | (2,724.5) | (2,457.3) |
| Netted credit exposure on derivative contracts | 2,289.9 | 1,294.9 |
| Collateral (held) / placed | (297.4) | (387.5) |
| Long settlement | 6.3 | 3.0 |
| Total net derivatives credit risk exposure | 1,998.8 | 910.4 |

Counterparty credit risk exposures by exposure class

An analysis of counterparty credit risk exposures as at 31 March 2018 by principal exposure class is given below:

Table 30: Counterparty credit risk exposures by exposure class

| | 2018 Credit risk exposure £m | 2017 Credit risk exposure £m |
|---|---|---|
| Central government or central banks | 56.5 | 45.1 |
| Public sector entities | 1.5 | 18.1 |
| Multilateral development banks | 27.3 | 26.1 |
| Regional governments or local authorities | - | - |
| Institutions | 2,296.5 | 1,291.8 |
| <i>Of which- CCPs</i> | <i>2,070.8</i> | <i>1,068.4</i> |
| Corporates | 9.1 | 0.3 |
| Equity | - | - |
| Other | - | - |
| Total | 2,390.9 | 1,381.4¹⁷ |

Counterparty credit risk exposures by credit quality

MHI has maintained a cautious approach with regard to the credit standing of its counterparties. An analysis of counterparty credit risk exposures as at 31 March 2018 by credit quality, in accordance with the credit quality steps used within the Pillar 1 Standardised Approach, is given below:

¹⁷ The 2017 disclosure excludes Treasury Default Loss Allocation Regime contribution.

Table 31: Counterparty credit risk exposures by credit quality step

| | 2018 | | | | | |
|---|----------------------|--------------|------------|------------|----------------|----------------|
| | Credit quality steps | | | | | Total £m |
| | 1 £m | 2 £m | 3 £m | 4 £m | Unrated £m | |
| Central government or central banks | 56.5 | - | 0.0 | - | - | 56.5 |
| Public sector entities | 1.5 | - | - | - | - | 1.5 |
| Multilateral development banks | 27.3 | - | - | - | - | 27.3 |
| Regional governments or local authorities | - | - | - | - | - | - |
| Institutions | - | 225.6 | - | 0.1 | 2,070.8 | 2,296.5 |
| <i>Of which- CCPs</i> | - | - | - | - | 2,070.8 | 2,070.8 |
| Corporates | - | - | 9.1 | - | - | 9.1 |
| Equity | - | - | - | - | - | - |
| Other | - | - | - | - | - | - |
| Total credit risk exposure | 85.3 | 225.6 | 9.2 | 0.1 | 2,070.8 | 2,390.9 |

| | 2017 | | | | | |
|---|----------------------|--------------|------------|----------|----------------|-----------------------------|
| | Credit quality steps | | | | | Total £m |
| | 1 £m | 2 £m | 3 £m | 4 £m | Unrated £m | |
| Central government or central banks | 45.0 | - | 0.1 | - | - | 45.1 |
| Public sector entities | 18.1 | - | - | - | - | 18.1 |
| Multilateral development banks | 26.1 | - | - | - | - | 26.1 |
| Regional governments or local authorities | - | - | - | - | - | - |
| Institutions | - | 223.4 | - | - | 1,068.4 | 1,291.8 |
| <i>Of which- CCPs</i> | - | - | - | - | 1,068.4 | 1,068.4 |
| Corporates | - | - | 0.3 | - | - | 0.3 |
| Equity | - | - | - | - | - | - |
| Other | - | - | - | - | - | - |
| Total credit risk exposure | 89.2 | 223.4 | 0.4 | - | 1,068.4 | 1,381.4¹⁸ |

External ratings are mapped to EBA prescribed credit quality step assessment scale and applied to exposures.

The counterparty credit risk exposures described in the analysis above include credit derivative contracts which give rise to counterparty credit risk exposure to the counterparty to the contract.

Notional value of credit derivative transactions

The following table shows the notional value of the credit derivative transactions outstanding as at 31 March 2018, arising in respect of MHI's own credit portfolio or through intermediation activities. Transactions in respect of MHI's own credit portfolio comprise both hedges of market risk associated with trading inventory and hedges used in connection with the issuance of structured notes:

Table 32: Notional value of credit derivative transactions

| Notional value of outstanding transactions | 2018 | | 2017 | |
|--|-------------------------------|--------------------------|-------------------------------|--------------------------|
| | Own credit portfolio | | Own credit portfolio | |
| | Protection purchased £m | Protection sold £m | Protection purchased £m | Protection sold £m |
| Credit default swaps | 122.7 | 115.6 | 597.6 | 559.7 |

¹⁸ The 2017 disclosure excludes Treasury Default Loss Allocation Regime contribution.

10. Operational risk

Risk management

Operational risk is the risk of financial loss resulting from inadequate or failed internal processes, people and systems or from external events.

Operational risk tolerance forms a component of MHI's overall risk appetite and is approved by the Board. MHI has no tolerance for inappropriate staff behaviour which may result in damage to its reputation or to the interests of its clients.

The principal operational risks to which MHI is exposed include technology failures (including cyber-attack), fraud, human error, the creation of unauthorised credit or market risks, regulatory breaches, and litigation.

Operational risk exposures are assessed and measured using a framework which includes: risk and control self-assessments, key risk indicators, internal loss event reporting, external loss event capture, and scenario stress testing.

MHI mitigates such risks through the maintenance of a comprehensive system of internal controls, which incorporates a strict segregation of duties between front and back office functions, the purchase of external insurance, and business continuity planning. Root cause analysis is undertaken to investigate internal instances of operational loss or near miss incidents. In cases where internal controls cannot be implemented to reduce operational risk to an acceptable level, consideration is given to avoiding or transferring the risk altogether.

Operational risk reporting is undertaken routinely to the Risk Management Committee and to the Operational Risk Committee. Significant matters are escalated to the Board Risk Committee and to the Board.

Pillar 1 requirements

As at 31 March 2018, the Pillar 1 capital requirement in respect of operational risk was £30.2m (2017: £24.5m) as calculated under the basic indicator approach.

11. Liquidity risk

Risk management

Liquidity risk is the risk that MHI does not have sufficient capital and funding resources to meet its financial contractual obligations as they fall due. Liquidity risk can result from a lack of availability of external funding, and the inability to convert securities into cash to meet near-term funding demands.

Strategies and processes in the management of liquidity risk

MHI's management of liquidity risk aims to ensure that there are sufficient liquid resources, both in amount and quality, to enable MHI to meet its financial contractual obligations as they fall due, even during times of idiosyncratic and / or market stress. MHI maintains liquidity in excess of its regulatory and internal risk appetite requirements.

MHI's business model is simple, largely cash-based, with derivatives predominantly being of a vanilla and cleared nature, has access to diverse funding sources, allocates costs to businesses in a transparent and effective way, and has a robust limit and control framework to protect against liquidity risks in excess of appetite.

MHI further mitigates liquidity risks through maintenance of HQLAs in a segregated portfolio under the control of its Treasury & Funding function, as well as holding additional HQLA-eligible unencumbered unsegregated assets also under the operational control of Treasury & Funding.

MHI performs stress testing of its liquidity risk position; a dynamic and forward looking approach is taken for MHI's internal liquidity stress scenarios and their underlying assumptions. Reporting of liquidity risks and associated stress testing is undertaken routinely by the Stress Testing Committee and the Risk Management Committee. Significant matters are escalated to the Board Risk Committee and the Board.

MHI also considers the effects of a downgrade in the rating of MHI and Mizuho Bank, Ltd., whose rating is referenced within the CSAs under which MHI may be required to pay collateral to its counterparties. Stress testing is conducted which incorporates the impact of a three notch downgrade in the ratings of MHI and Mizuho Bank, Ltd., and this modelling indicates that MHI has sufficient available liquidity resources to manage the cash requirements which may arise in such a situation.

Structure and organisation of the liquidity risk management function

Liquidity risk appetite is a component of MHI's overall risk appetite and is set and approved by the Board. The Board delegates responsibility over the day to day management of liquidity risk to the Executive Committee who in turn empower the Asset & Liability Committee with responsibility for the day to day management of liquidity risk. Responsibility for liquidity risk oversight is delegated to the Board Risk Committee, to which the CRO is primarily accountable to. The CRO is supported by Risk Management Department, and chairs the Risk Management Committee and Stress Testing Committee.

MHI adopts a "Three Lines of Defence" model in the management of liquidity risk:

- The First line of defence is primarily accountable for liquidity risk on an operational level. This is considered to comprise of Treasury & Funding and Operations.
- The Second line of defence is primarily accountable for liquidity risk oversight. This comprises Liquidity Risk Management and Regulatory Reporting.
- The Third line of defence provides assurance over MHI's risk management framework and is independent of both first and second lines of defence. This comprises of Internal Audit.

Scope and nature of liquidity risk reporting and measurement systems

Robust systems, procedures and policies ensure that liquidity regulatory reporting and risk oversight metrics are produced in compliance with the PRA's requirements.

Adequacy of liquidity risk management arrangements

MHI has produced and maintains an ILAAP document detailing how it assesses, quantifies, and manages the principal liquidity risks to which it is exposed. Further, it highlights MHI's approach to determining the minimum level of internal liquidity resources required to be maintained to mitigate those risks in line with its overall liquidity risk management and liquidity risk appetite approved by the Board.

The approval and overall ownership of the ILAAP is the responsibility of the Board of MHI. The leadership for preparation of the ILAAP document has been delegated to the CRO with support from the Risk Management Department, Finance, Regulatory Reporting, Treasury & Funding, Compliance, and impacted business areas. The document has been discussed and challenged by senior management, including the CEO, the CFO, the Head of Compliance and the Treasurer.

The ILAAP document is an integral part of MHI's liquidity management framework and informs the Board of the ongoing assessment and quantification of liquidity risks, how these are mitigated, and required liquidity resources. The CRO; through the Head of Regulatory & Liquidity Risk Management and supporting functions; is responsible for maintaining and updating the ILAAP document, monitoring MHI's liquidity adequacy, and ensuring that the ILAAP document is reflective of MHI's liquidity risk management at all times.

The ILAAP document is dynamic and updated at least annually, but also in line with changes in regulations, risk appetite, business model, and market conditions. The annual Board approval of the ILAAP, including statement of liquidity risk appetite, is taken as management's declaration and attestation of the adequacy of liquidity risk management systems and conformance with the overall liquidity adequacy rule.

Table 33: LCR disclosure template

| Scope of consolidation: solo | Total weighted value (average) | | | |
|--|---------------------------------------|-----------|-----------|-----------|
| Currency and units: £m | | | | |
| Quarter ending on | 30-Jun-17 | 30-Sep-17 | 31-Dec-17 | 31-Mar-18 |
| Number of data points used in the calculation of averages | 12 | 12 | 12 | 12 |
| | Total adjusted value | | | |
| Liquidity buffer | 2,068.2 | 1,987.2 | 1,975.7 | 1,996.8 |
| Total net cash outflows | 444.8 | 442.1 | 462.1 | 517.3 |
| LCR | 474.9% | 460.8% | 443.4% | 395.6% |

Note: These values and figures represent the simple average of month-end observations over the twelve months preceding quarter-end dates as per the EBA guidance.

Asset encumbrance

The secured and unsecured wholesale market, together with the debt issuance programme, is the prime funding source for MHI. MHI provides securities financing transactions and collateralised borrowing as part of its repurchase agreement business and these result in off-balance sheet encumbrance. Another form of encumbrance is pledging securities with central counterparties to facilitate trading activities and meet initial margin requirements. Assets on the balance sheet are considered encumbered when they have been pledged or used to secure or collateralise a transaction that impacts their transferability. Treasury & Funding control the funding strategies for MHI's assets and monitor asset encumbrance levels daily.

Encumbered and unencumbered assets for MHI as at 31 March 2018 are disclosed using median values. These median values are the rolling quarterly medians for June 2017, September 2017, December 2017 and March 2018.

Table 34: Encumbered and unencumbered assets

| As at 31 March 2018 ¹⁹ | | | | | | | | | |
|-----------------------------------|--|--------------------------------------|---|---------------------------------|---|--|-------------------------|-----------------------------------|-------------------------|
| | | Carrying amount of encumbered assets | | Fair value of encumbered assets | | Carrying amount of unencumbered assets | | Fair value of unencumbered assets | |
| | | | of which notionally eligible EHQLA and HQLA | | of which notionally eligible EHQLA and HQLA | | of which EHQLA and HQLA | | of which EHQLA and HQLA |
| £m | | 010 | 030 | 040 | 050 | 060 | 080 | 090 | 100 |
| 010 | Assets of the reporting institution | 2,584.1 | | | | 4,310.1 | | | |
| 030 | Equity instruments | | | | | 8.1 | | | - |
| 040 | Debt securities | 2,584.1 | | 2,598.5 | | 2,236.1 | | 2,270.7 | |
| 050 | of which: covered bonds | 7.7 | - | 7.8 | - | 40.7 | - | 41.0 | - |
| 060 | of which: asset-backed securities | - | - | - | - | - | - | - | - |
| 070 | of which: issued by general governments | 2,007.1 | - | 2,016.9 | - | 1,122.9 | - | 1,143.0 | - |
| 080 | of which: issued by financial corporations | 346.1 | - | 348.6 | - | 782.8 | - | 794.0 | - |
| 090 | of which: issued by non-financial corporations | 223.2 | - | 225.3 | - | 289.7 | - | 292.7 | - |
| 120 | Other assets | - | - | - | - | 2,066.0 | - | - | - |

EHQLA: assets of extremely high liquidity and credit quality

¹⁹ MHI will be required to report columns 030, 050, 080 and 100 from 31 March 2019 onwards.

| As at 31 March 2017 ²⁰ | | | | | | | | | |
|-----------------------------------|--|--------------------------------------|---|---------------------------------|---|--|-------------------------|-----------------------------------|-------------------------|
| | | Carrying amount of encumbered assets | | Fair value of encumbered assets | | Carrying amount of unencumbered assets | | Fair value of unencumbered assets | |
| | | 010 | of which notionally eligible EHQLA and HQLA | 040 | of which notionally eligible EHQLA and HQLA | 060 | of which EHQLA and HQLA | 090 | of which EHQLA and HQLA |
| | | | 030 | | 050 | | 080 | | 100 |
| 010 | Assets of the reporting institution | 2,481.0 | | | | 3,154.0 | | | |
| 030 | Equity instruments | - | - | - | - | 7.6 | - | - | - |
| 040 | Debt securities | 2,481.0 | | 2,500.7 | | 2,215.8 | | 2,269.7 | |
| 050 | of which: covered bonds | 2.3 | - | 2.3 | - | 20.1 | - | 20.3 | |
| 060 | of which: asset-backed securities | - | - | - | - | - | - | - | |
| 070 | of which: issued by general governments | 2,039.0 | - | 2,053.9 | - | 1,065.7 | - | 1,073.5 | |
| 080 | of which: issued by financial corporations | 225.8 | - | 228.3 | - | 868.5 | - | 911.5 | |
| 090 | of which: issued by non-financial corporations | 213.8 | - | 216.1 | - | 261.5 | - | 264.3 | |
| 120 | Other assets | - | - | - | - | 930.6 | - | - | |

²⁰ The 31 March 2017 figures which were based on average values have now been restated using median values.

Table 35: Collateral received²¹

| £m | | As at 31 March 2018 | | | | As at 31 March 2017 | | | |
|------------|---|--|--|---|--------------------------------|--|--|---|--------------------------------|
| | | Fair value of encumbered collateral received or own debt securities issued | | Unencumbered | | Fair value of encumbered collateral received or own debt securities issued | | Unencumbered | |
| | | | | Fair value of collateral received or own debt securities issued available for encumbrance | | | | Fair value of collateral received or own debt securities issued available for encumbrance | |
| | | 010 | of which notionally eligible EHQLA and HQLA 030 | 040 | of which EHQLA and HQLA 060 | 010 | of which notionally eligible EHQLA and HQLA 030 | 040 | of which EHQLA and HQLA 060 |
| 130 | Collateral received by the reporting institution | 16,163.5 | | 276.0 | | 16,545.7 | | 353.3 | 16,545.7 |
| 140 | Loans on demand | - | - | - | - | - | - | - | - |
| 150 | Equity instruments | 1.8 | - | 0.0 | - | 1.9 | - | 0.0 | 1.9 |
| 160 | Debt securities | 16,161.7 | | 276.0 | | 16,543.8 | | 353.2 | 16,543.8 |
| 170 | of which: covered bonds | 45.1 | - | 0.5 | - | 5.6 | - | 0.4 | 5.6 |
| 180 | of which: asset-backed securities | - | - | - | - | - | - | - | - |
| 190 | of which: issued by general governments | 15,258.8 | - | 213.3 | - | 15,655.4 | - | 288.6 | 15,655.4 |
| 200 | of which: issued by financial corporations | 530.7 | - | 23.2 | - | 528.1 | - | 23.2 | 528.1 |
| 210 | of which: issued by non-financial corporations | 327.1 | - | 39.0 | - | 354.6 | - | 41.1 | 354.6 |
| 220 | Loans and advances other than loans on demand | - | - | - | - | - | - | - | - |
| 230 | Other collateral received | - | - | - | - | - | - | - | - |
| 240 | Own debt securities issued other than own covered bonds or asset-backed securities | - | - | - | - | - | - | - | - |
| 241 | Own covered bonds and asset-backed securities issued and not yet pledged | - | - | - | - | - | - | 8.6 | - |
| 250 | Total assets, collateral received and own debt securities issued | 18,747.6 | - | - | - | - | - | - | - |

²¹ MHI will be required to report columns 030, 060 from 31 March 2019 onwards.

Table 36: Encumbered Assets/Collateral Received and Associated Liabilities

| | | As at 31 March 2018 | | As at 31 March 2017 | |
|-----|---|---|---|---|---|
| | | Matching liabilities, contingent liabilities or securities lent | Assets, collateral received and own debt securities issued other than covered bonds and ABSs encumbered | Matching liabilities, contingent liabilities or securities lent | Assets, collateral received and own debt securities issued other than covered bonds and ABSs encumbered |
| £m | | 010 | 030 | 010 | 030 |
| 010 | Carrying amount of selected financial liabilities | 13,304.4 | 13,690.5 | 13,222.7 | 13,698.0 |

ABSs: asset-backed securities

12. Remuneration

The Remuneration Committee (RemCo)

As part of MHI's corporate governance arrangements the Board has established a RemCo to approve remuneration policy and set specific remuneration at certain levels. RemCo members are appointed by the Board and solely comprise Non-Executive Directors; the committee reports to the Board through its Chair. The remuneration of MHI's Executive Directors is approved by the RemCo. The RemCo also approves the remuneration of Managing Directors and above and of Material Risk Takers (MRTs), a definition of which is set out below. Between 1 April 2017 and 31 March 2018, the RemCo held seven meetings.

Remuneration policy

MHI maintains a remuneration policy which applies to all employees together with staff seconded from affiliates within the Mizuho Financial Group, Inc. of companies. The policy takes into account the PRA and FCA's Remuneration Codes and related guidance, and is intended to promote effective risk management whilst retaining the flexibility to make changes dependent upon external factors including, but not limited to, future legislative or regulatory changes. The policy also provides a market based remuneration framework, which enables the Group to recruit and retain high calibre staff and promote fairness and consistency throughout the employment relationship whilst not compromising the Group's high standards of control and risk management.

The remuneration policy and its implementation are reviewed and approved by the RemCo from time to time and at least annually. Any changes to the policy will only take effect upon approval by the RemCo and will be subject to ratification by the Board. RemCo approved a revised remuneration policy during the meeting of 19 March 2018.

Material Risk Takers (MRTs)

MRTs are defined as staff whose professional activities can have a material impact on MHI's risk profile, taking into account the criteria set out in the EBA's Regulatory Technical Standard *CDR (EU) No 604/2014*.

A list of MRTs is held by MHI's Human Resources (HR) department. Employees that appear on this list are notified by HR of their status and of the implications of being defined as an MRT.

As at 31 March 2018 for the fiscal year 2017/18, 70 active members of staff were identified as MRTs.

Control functions

The compensation of employees engaged in control functions is based principally on the achievement of objectives linked to those functions and MHI performance. Compensation for the heads of those control functions is approved by the RemCo.

The link between pay and performance

The remuneration policy is designed to align employee rewards with performance and aims to protect and promote shareholder interests by incentivising staff to deliver sustained performance and create long-term value through delivery of MHI's goals. The policy also provides a market-competitive remuneration structure to attract and retain high calibre staff. The policy is reviewed at least annually and approved by the RemCo and the Board. The policy is made available to all employees on MHI's intranet site and when updated it is mandatory that all employees attest that they have read and understood the policy.

MHI remuneration policy states that variable remuneration awards are conditional, discretionary and contingent upon a sustainable and risk-adjusted performance, in excess of that required to fulfil the employee's job description as part of the employee's terms of employment. All staff (including Front Office revenue generating staff) performance is assessed on a range of both quantitative and qualitative measures. Awards of variable remuneration are capable of forfeiture or reduction at MHI's discretion, including down to zero.

Variable remuneration will be paid only if it is sustainable in the context of MHI's financial situation and is justified on the basis of individual, departmental, MHI or wider Mizuho Financial Group, Inc. performance.

A remuneration sub-group consisting of the Head of HR, the Head of Compliance, the CFO, the CRO and a representative from Internal Audit, meets regularly (generally before each RemCo meeting) to discuss a number of remuneration related matters including behaviour and conduct. The sub-group is involved in the process to review and set remuneration. Concerns regarding an individual's activities and / or conduct can be raised at any stage and are taken into account by management through the Balanced Scorecard Appraisal process; this is described in further detail below.

An evaluation committee, comprising Executive Committee members, meets on an annual basis to assess individual staff behaviours, the results of which form part of the appraisal and remuneration process. This is in addition to the specific involvement of the remuneration sub-group.

The RemCo will use information in respect of corporate performance and risk management to make informed decisions when reviewing the appropriateness of discretionary reward and specifically the remuneration of MRTs. The level of discretionary remuneration is agreed in consultation with MHI's parent company, Mizuho Securities Co., Ltd., with final approval by RemCo.

The staff appraisal system ensures that an individual's behaviour and their adherence to control and compliance requirements is taken into account, and that sole reliance is not placed on an individual's financial performance. The assessment is in the form of a Balanced Scorecard Appraisal. The Balanced Scorecard Appraisal consists of the following:

1. Financial, Strategic & Operational: this measures employees' performance against SMART objectives set at the beginning of the financial year; and
2. Culture, Conduct & Values: this comprises inputs from the remuneration sub-group, Internal Audit, and Front Office Supervisory Reporting, and is strongly linked to MHI's values (Speed, Innovative Spirit, Team Spirit, Passion and Customer First) through a competency framework.

The Balanced Scorecard Appraisal is used to determine the overall performance ratings and as a basis for determining any adjustments to individual discretionary remuneration awards, including malus and clawback. All permanent employees qualify for consideration of discretionary remuneration; no formulaic discretionary remuneration is awarded by MHI.

An employee's individual performance is measured on a rating scale of 1 (Poor performance) to 5 (Outstanding). An employee will not be assigned a rating higher than a 3 if they have not met their objectives including any financial targets. Where an appraisal rating is a 2 or lower then malus (up to 100%) may be applied to any discretionary remuneration awarded to the employee.

The design characteristics of the remuneration scheme

During the period in question variable remuneration for MRTs (who were not subject to the de minimis concession) was paid in cash and shares, with elements subject to deferral. MRTs that fell under the de minimis concession were paid in cash only. Variable remuneration is subject to the following design characteristics:

Risk adjustment

The level of discretionary remuneration is determined from performance figures which inherently factor in risk adjusted accounting measures; the level of discretionary remuneration is further adjusted for risk by the RemCo. The CRO attends RemCo and contributes to discussions on the size of overall discretionary remuneration relative to risk by reference to a number of metrics including adherence to MHI's risk appetite. The CRO and CFO (who also attend the RemCo on a regular basis) can recommend discretionary or formulaic adjustments to accrued discretionary remuneration at any point throughout the year via the RemCo or the Board Risk Committee where relevant performance metrics are discussed.

The Board and RemCo are of the view that a purely formulaic approach to discretionary remuneration adjustment is not suitable in any circumstances. In addition, MHI has been in an evolving process of revising its budget and strategy for future years, this means that a more flexible discretionary approach to adjusting discretionary remuneration is required e.g. for retaining and attracting key staff. Current potential discretionary adjustments include, but are not limited to, the cost of capital, cost of funding and potential long tail risks.

Deferral policy

During the financial year ending 31 March 2018, variable pay for MRTs and certain other staff was subject to a deferral plan. The deferral plan for MRTs (who were not subject to the de minimis concession) provided for deferral of between 40% and 60% of variable pay for a period of between three and seven years in line with the Remuneration Codes and subject to a MRTs categorisation (Senior Manager, Risk Manager or Other MRT). For all other staff subject to the deferral plan (and MRTs who fell under the de minimis concession), the deferral plan provided for cash deferrals of between 20% and 40% of variable pay over a prescribed threshold for a period of three years.

Malus: performance adjustment

A deferred award may be subject to adjustment (including forfeiture) as set out below and will only vest to the extent determined by the RemCo at its discretion, giving regard to such matters as it considers appropriate, including but not limited to:

1. In the case of all staff including MRTs, any restatement or recalculation of individual and/or departmental and/or MHI and/or Mizuho Financial Group, Inc. company financial performance (including but not limited to following the discovery of incorrect or false accounting); and/or
2. In the case of MRTs only:
 - whether vesting is (a) sustainable according to the financial situation of MHI, and/or (b) justified on the basis of individual and/or departmental and/or Group and/or Mizuho Financial Group, Inc. company performance; and/or
 - any assessment or reassessment of individual and/or departmental and/or Group and/or Mizuho Financial Group, Inc. company performance, (b) any evidence of an individual's misbehaviour and/or material error, (c) any material downturn in departmental and/or Group and/or Mizuho Financial Group, Inc. company financial performance, and/or (d) any material failure of risk management suffered by MHI and/or any Mizuho Financial Group, Inc. company and/or the individual's department; and/or
 - any conduct which the individual participated in and/or was responsible for and which resulted in significant losses to MHI and/or any Mizuho Financial Group, Inc. company and/or the individual's department, and/or (b) any failure of the individual to meet appropriate standards of fitness and/or propriety (including, without limitation, any such standards set by a regulator and/or MHI and/or any Mizuho Financial Group, Inc. company) and/or to comply with Group and/or Mizuho Financial Group, Inc. company policies; and/or
 - any misconduct and/or material failure of risk management which the individual could (a) reasonably be expected to be aware of but failed to take adequate steps to promptly identify, assess, report, escalate or address, and/or (b) by virtue of the individual's role or seniority, be deemed indirectly responsible and/or accountable for, including, without limitation, by virtue of being senior staff in charge of setting Group and/or Mizuho Financial Group, Inc. company culture and/or strategy; and/or
3. In the case of all staff including MRTs, any other circumstance(s) as required by law and/or any regulator.

Clawback

The Remuneration Codes require MHI to apply clawback to the variable remuneration of MRTs. The following provisions apply in respect of payments of all discretionary remuneration awards for a period of seven years after the date the award is made (which can be extended from seven to ten years for *Senior Managers* in certain circumstances where at the end of the normal seven year clawback period (i) MHI has commenced an internal inquiry into a possible material failure which could lead to clawback or (ii) a regulatory authority has notified MHI that it has commenced an investigation which could lead to clawback):

- An employee who is or becomes an MRT may be required to repay to MHI up to 100% of the gross amount of any non-deferred cash award, deferred cash award, non-deferred share award and/or deferred share award paid pursuant to a discretionary remuneration award in the event that the employee is involved in or is responsible for:
 - a. any misconduct and/or material failure of risk management suffered by MHI and/or the employee's department, including any misconduct and/or material failure of risk management which the employee could (i) reasonably be expected to have been aware of but failed to take adequate steps to promptly identify, assess, report, escalate or address, and/or (ii) by virtue of the employee's role or seniority, be deemed indirectly responsible or accountable for; and/or
 - b. conduct which results in significant losses to MHI and/or the employee's department; and/or
 - c. any restatement or recalculation of individual and/or departmental and MHI financial performance (including but not limited to following the discovery of incorrect or false accounting); and/or
 - d. any material error and/or any failure to meet appropriate standards of fitness and/or propriety (including, without limitation, any such standards set by a regulator and MHI) and/or to comply with MHI policies which apply to an employee; and/or

e. any other circumstance as required by law and/or any regulator.

- The RemCo, in its sole discretion shall determine whether and the extent to which some or all of any part of the discretionary remuneration award that has previously been paid must be repaid pursuant to these clawback provisions.
- An employee who accepts an award and is or becomes an MRT agrees that MHI shall be entitled to withhold or collect any repayment required pursuant to the clawback provisions (i) by deduction from any salary or other earnings or payments due to the employee at any time, (ii) directly from the employee by immediate payment in cleared funds or (iii) by selling some or all of any shares held on the employee's behalf.

Remuneration leverage

Remuneration leverage is the ratio of fixed to variable components of remuneration. MHI ensures that fixed and variable components of total remuneration are appropriately balanced and sets fixed remuneration at a level which permits a fully flexible discretionary remuneration policy (including the award of no variable remuneration in appropriate circumstances). For 2017/18, the maximum remuneration leverage ratio for all Front Office staff was set as 1:2 (Fixed : Variable), and for all support and control functions staff this was set at 1:1 (Fixed : Variable). In accordance with the Remuneration Codes, approval for the aforementioned ratios has been obtained from the shareholders.

Remuneration awards and expenditure

Aggregate MRT total remuneration by business area

Aggregate remuneration awards to MRTs by business area are shown below:

Table 37: Aggregate MRT remuneration by business area

| MRT aggregate remuneration | 2018 | 2017 |
|----------------------------|-------------------------------------|-------------------------------------|
| | Aggregate remuneration awards £m | Aggregate remuneration awards £m |
| Investment Banking | 5.2 | 5.8 |
| Markets and Products | 14.9 | 18.6 |
| Central functions | 14.8 | 12.5 |
| Total | 34.9 | 36.9 |

Aggregate remuneration of MRT by type of award

Aggregate remuneration awards in respect of MRT by type of award, split between senior management and other staff, are set out below:

Table 38: Aggregate MRT remuneration by type of award

| MRT aggregate remuneration | 2018 | | 2017 | |
|----------------------------|-------------------------|------------------|-------------------------|------------------|
| | Senior management £m | Other MRTs £m | Senior management £m | Other MRTs £m |
| Fixed remuneration | 6.8 | 13.1 | 7.6 | 13.6 |
| Variable remuneration: | 4.7 | 10.3 | 4.6 | 11.1 |
| Total remuneration | 11.5 | 23.4 | 12.2 | 24.7 |

The number of MRTs in respect of whom remuneration awards were made during the year is as follows:

Table 39: Number of MRTs subject to awards

| MRT staff numbers | 2018 | | 2017 | |
|--------------------------|--------------------------|-------------------|--------------------------|-------------------|
| | Senior management | Other MRTs | Senior management | Other MRTs |
| Number of staff | 19 | 51 | 21 | 52 |

Appendix 1 Main features of capital instruments

| # | Features | CET1 | Unsecured subordinated loan |
|-----------------------------|---|-----------------------------|--|
| 1 | Issuer | Mizuho International plc | Mizuho International plc |
| 2 | Unique identifier (e.g. CUSIP, ISIN, or Bloomberg identifier for private placement) | BBG000N27XG2 | N/A |
| 3 | Governing law(s) of the instrument | English Law | English Law |
| <i>Regulatory treatment</i> | | | |
| 4 | Transitional CRR rules | CET1 | Tier 2 |
| 5 | Post-transitional CRR rules | CET1 | Tier 2 |
| 6 | Eligible at solo/(sub-) consolidated/solo & (sub-) consolidated | Solo | Solo |
| 7 | Instrument type (types to be specified by each jurisdiction) | Common shares | Other Tier 2 instruments |
| 8 | Amount recognised in regulatory capital (currency in millions, as of most recent reporting date) | GBP 709.9 million | GBP 45 million |
| 9 | Nominal amount of instrument | GBP 709.9 million | GBP 45 million |
| 10 | Accounting classification | Shareholders' equity | Liability |
| 11 | Original date of issuance | N/A | 23/03/2015 |
| 12 | Perpetual or dated | Perpetual | Dated |
| 13 | Original maturity date | N/A | 22/03/2025 |
| 14 | Issuer call subject to prior supervisory approval | No | No |
| 15 | Optional call date, contingent call dates and redemption amount | N/A | N/A |
| 16 | Subsequent call dates, if applicable | N/A | N/A |
| <i>Coupons / dividends</i> | | | |
| 17 | Fixed or floating dividend/coupon | N/A | Floating |
| 18 | Coupon rate and any related index | N/A | 3 month LIBOR + margin |
| 19 | Existence of a dividend stopper | No | No |
| 20a | Fully discretionary, partially discretionary or mandatory (in terms of timing) | Fully discretionary | Mandatory |
| 20b | Fully discretionary, partially discretionary or mandatory (in terms of amount) | Fully discretionary | Mandatory |
| 21 | Existence of step up or other incentive to redeem | No | No |
| 22 | Noncumulative or cumulative | Non-cumulative | Non-cumulative |
| 23 | Convertible or non-convertible | Non-convertible | Non-convertible |
| 24 | If convertible, conversion trigger(s) | N/A | N/A |
| 25 | If convertible, fully or partially | N/A | N/A |
| 26 | If convertible, conversion rate | N/A | N/A |
| 27 | If convertible, mandatory or optional conversion | N/A | N/A |
| 28 | If convertible, specify instrument type convertible into | N/A | N/A |
| 29 | If convertible, specify issuer of instrument it converts into | N/A | N/A |
| 30 | Write-down feature | No | No |
| 31 | If write-down, write-down trigger(s) | N/A | N/A |
| 32 | If write-down, full or partial | N/A | N/A |
| 33 | If write-down, permanent or temporary | N/A | N/A |
| 34 | If temporary write-down, description of write-down mechanism | N/A | N/A |
| 35 | Position in subordination hierarchy in liquidation (specify instrument type immediately senior to instrument) | The most subordinated claim | Unsecured subordinated to the claims of all senior creditors |
| 36 | Non-compliant transitioned features | No | No |
| 37 | If yes, specify non-compliant features | N/A | N/A |