“Japan’s Experience of Transitioning from Blanket Guarantee to Limited Coverage”

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MEASURES IN THE CURRENT FINANCIAL CRISIS

“Direct Depositors Protection in the Crisis”

- Increasing Deposit Insurance coverage levels (all insured deposits/ specific categories)
- Newly announced deposit insurance program (e.g. Australia, New Zealand)
- Temporary blanket guarantees (all liabilities/ all deposits/ specific deposit categories)
**MEASURES IN THE CURRENT FINANCIAL CRISIS**

**“Blanket Guarantee and Coverage Increase”**

-Asia/Pacific-

- Temporary blanket guarantee on deposits or significant increase in coverage limit: Australia, Hong Kong, Indonesia, Malaysia, Taiwan, Thailand, Singapore

- Philippines: charter changes to increase coverage from PHP250,000 to PHP500,000

- Korea: coverage extended to foreign currency deposits

-US-

- Temporary coverage increase

- Optional programs for coverage expansion
MEASURES IN THE CURRENT FINANCIAL CRISIS

“Blanket Guarantee and Coverage Increase”

-Europe-

- Blanket Guarantee (Austria, Denmark, Germany, Greece, Hungary, Iceland, Ireland, Slovakia, Slovenia)
- Coverage Increase significantly above the EU minimum (Belgium, Lithuania, Luxemburg, Netherlands, Portugal, Spain)
- Coverage Increase to an amount closer to the EU minimum level of EUR 50,000 (Bulgaria, Czech Republic, Estonia, Finland, Hungary, Romania, Sweden, UK)
- EU directive on coverage level and payout delay in process
It is obvious that no country will keep current blanket guarantee provisions.

Policymakers and deposit insurers must apply effective exit strategies so as to avoid further financial instability.
A prompt removal of blanket guarantee and transition to limited coverage are the general rules when situations allow. The set of IADI Core Principles says;

"IADI’s Core Principle #10"

"(T)he transition should be as rapid as a country’s circumstances permit. Blanket guarantees can have a number of adverse effects if retained too long, notably moral hazard. Policymakers should pay particular attention to public attitudes and expectations during the transition period."
Countries transitioning from a blanket guarantee will need to consider three special issues. 

- Public attitudes and expectations
- The capacity of banking system to fund a new deposit insurance system
- How fast the transition should proceed

<Explanation and supporting guidance: Core Principle #10>
**JAPAN’S EXPERIENCE: TRANSITIONING FROM BLANKET GUARANTEE**

<table>
<thead>
<tr>
<th>Period</th>
<th>Duration</th>
<th>Date</th>
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<tbody>
<tr>
<td><strong>Original period</strong></td>
<td>5 years</td>
<td>(from June 1996 to April 2001)</td>
</tr>
<tr>
<td><strong>First (full) extension</strong></td>
<td>1 year</td>
<td>(to April 2002)</td>
</tr>
<tr>
<td><strong>Second (partial) extension</strong></td>
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<td>(for deposits payable on demand)</td>
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<td></td>
</tr>
<tr>
<td><strong>Third (partial) extension</strong></td>
<td>2 years</td>
<td>(to April 2005)</td>
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<td><strong>Complete resumption of limited coverage</strong></td>
<td>April 2005</td>
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With the introduction of permanent full coverage for “deposit for payment and settlement” and “specified settlement obligations”
JAPAN’S EXPERIENCE: TRANSITIONING FROM BLANKET GUARANTEE


<table>
<thead>
<tr>
<th>Deposit Payable on Demand</th>
<th>Current Deposits</th>
<th>Limited Coverage (JPY 10 mil)</th>
<th>Full Coverage</th>
<th>Provisional Period</th>
<th>Limited Coverage (JPY 10 mil)</th>
</tr>
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<td>Deposits Payable on Demand</td>
<td>Ordinary Deposits, etc.</td>
<td>1971 (Jul)</td>
<td>1996 (Jun)</td>
<td>2001 (Apr)</td>
<td>2002 (Apr)</td>
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(Note) Permanent full coverage is applied for deposits of bearing no interest/payable on demand/providing settlement services since April 2005.
**JAPAN’S EXPERIENCE: TRANSITIONING FROM BLANKET GUARANTEE**

**“Blanket Guarantee and Transition (1996-2005)”**

- **Original period**
  - 5 years
  - (from June 1996 to April 2001)

- **First (full) extension**
  - 1 year
  - (to April 2002)

- **Second (partial) extension**
  - 1 year
  - (for deposits payable on demand)
  - (to April 2003)

- **Third (partial) extension**
  - 2 years
  - (for deposits payable on demand)
  - (to April 2005)

- **Complete resumption of limited coverage**
  - April 2005

With the introduction of permanent full coverage for “deposit for payment and settlement” and “specified settlement obligations”
“Before 1996 : Background”

- The Japanese economy and financial sector began to suffer from critical downturns.
**Japan’s Experience: Transitioning from Blanket Guarantee**

1996: Introduction of Blanket Guarantee
(Major Amendment of Deposit Insurance Law)

- Blanket Guarantee was introduced as a five-year temporary measure to expire in March 2001

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<td>Current Deposits</td>
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<td>Full Coverage</td>
<td>Limited Coverage (anticipated)</td>
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<td>Time Deposits</td>
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- Impact by Asian Financial Crisis etc.
- Failures of Three Major Banks

Diagram showing GDP trends with a significant dip in 1997-98.
"2000: Extension of Measures"  
(Amendment of DI Law)

- One-year Blanket Guarantee extension to March 2002
- Further one year extension (to March 2003) for deposits payable on demand such as ordinary and current deposits
“2000-02: Slump of Economy/ Negative Sentiment”

- Corporate bankruptcy debt ran at historical highs as JPY 24 trillion (2000)
- Nikkei Index dipped below JPY 9,000 for the first time in 19 years (Oct. 2002)
“2002(April): Partial Resumption to Limited Coverage”

- Full Coverage for time deposits was lifted.
- Additional two-year extension of full coverage for deposits payable on demand (2003 to 2005).
- It was determined that payment and settlement deposits would be under full coverage as a permanent measure.

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**JAPAN’S EXPERIENCE: TRANSITIONING FROM BLANKET GUARANTEE**
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Changes in Amounts Outstanding of Deposits (Domestically Licensed Banks)

(¥ trillion)

- Time and Saving Deposits
- Demand Deposits

FY00 2H FY01 1H FY01 2H FY02 1H FY02 2H FY03 1H FY03 2H FY04 1H FY04 2H FY05 1H FY05 2H
JAPAN’S EXPERIENCE: TRANSITIONING FROM BLANKET GUARANTEE

Changes in Amounts Outstanding of Deposits (Domestically Licensed Banks) (¥ trillion)

- Time and Saving Deposits ¥10M～
- Time and Saving Deposits ~¥10M
- Demand Deposits ¥10M～
- Demand Deposits ~¥10M

Years:
- FY00
- FY01
- FY02
- FY03
- FY04
- FY05

Splits:
- 1H
- 2H
“2002(April): Partial Resumption to Limited Coverage”

- Full Coverage for time deposits was lifted
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- It was determined that payment and settlement deposits would be under full coverage as a permanent measure
Japan’s Experience: Transitioning from Blanket Guarantee

“2005 (April): Complete Resumption to Limited Coverage”

- Deposits payable on demand moved back to Limited Coverage
- Permanent measure; Full coverage for payment and settlement


(Note) Permanent full coverage is applied for deposits of bearing no interest/payable on demand/providing settlement services since April 2005
“Wrap Up”

Total Blanket Guarantee of 6 years with Gradual Transitioning Approach

While the original length of the measure was set at 5 years, the situation did not improve enough for the resumption to limited coverage on schedule.

Consequently, the authority decided to extend some provisions, one year extension of Blanket Guarantee and gradual resumption to limited coverage in order to avoid confusion and adverse effects.
Japan’s Experience: Transitioning From Blanket Guarantee

“Wrap Up (contd.)”

- “Early Exit” from Blanket Guarantee is desirable
- However, economic and financial conditions should improve before transition.
- Public confidence and depositors’ sentiment should be restored.
- Otherwise, flexible measures such as the extending the period of transition to limited coverage are worth considering.
Also, it is important to examine the effectiveness of an original deposit insurance system when returning to limited coverage.

In the case of Japan, the provisions of permanent full coverage for payment and settlement deposits and specified settlement obligations reinforced the original system; and eventually it enhanced public confidence during transition.
JAPAN’S EXPERIENCE: TRANSITIONING FROM BLANKET GUARANTEE

Poster

Brochure
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