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Seoul Guarantee Insurance Co.

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Seoul Guarantee Insurance Co.

| | | | | | | | | |
|-----------------------|---------------------|---|-----------------------------|----------|---|--------------------|----------|---|
| Anchor | a- | + | Modifiers | 0 | = | SACP | a- | A+/Stable/-- Financial strength rating |
| ▲ | | | ▲ | | | + | | |
| Business Risk | Strong | | Governance | Neutral | | Support | 2 | |
| Competitive position | Strong | | | | | Group support | 0 | |
| IICRA | Intermediate | | Liquidity | Adequate | | Government support | 2 | |
| Financial Risk | Satisfactory | | Comparable ratings analysis | 0 | | | | |
| Capital and earnings | Strong | | | | | | | |
| Risk exposure | Moderately high | | | | | | | |
| Funding structure | Neutral | | | | | | | |

IICRA--Insurance Industry And Country Risk Assessment.
SACP--Stand-alone credit profile.

Credit Highlights

| Overview | |
|--|--|
| Key strengths | Key risks |
| Strong market presence as the only comprehensive guarantee insurer in Korea. | High sensitivity to a downturn in the economy. |
| Good operating performance backed by controlled distribution channels. | Low geographic diversification benefits relative with global peers'. |

Seoul Guarantee Insurance Co.'s (SGIC) focus on strengthening risk controls will likely gradually enhance its underwriting performance. The insurer's efforts to adjust premium rates and strengthen risk controls on underperforming policy-related products, such as guarantees on deposits for jeonse (lump-sum refundable deposits for rental) or retail loans to mid-to-low credit profile borrowers, in recent years will underpin its underwriting performance in the next two years. These measures amid moderate premium growth will support SGIC's strong capital buffers, in our view. Korea's gradual economic recovery from the COVID-19 pandemic will provide more stable operating conditions for the insurer.

SGIC is likely to maintain its strong presence in Korea's guarantee insurance market. The company's pricing power--stemming from its unique market position as the only comprehensive guarantee insurer in Korea and its controlled distribution channels--underpins its good operating performance. SGIC had a market share of about 26% in terms of the amount of guarantees provided in the financial system as of end-2020.

The likelihood of extraordinary government support to remain high. We expect SGIC to continue to play a very important policy role of supporting business operations of small and midsize enterprises (SME), as well as the stability of the housing market by providing guarantee insurance in Korea. The insurer will maintain a strong link with the government through Korea Deposit Insurance Corp. (KDIC), which owns a 93.85% stakes in SGIC.

Outlook: Stable

The stable outlook on SGIC reflects our view that the insurer will benefit from a high likelihood of extraordinary support from the government over the next two years. SGIC's strong business presence in Korea should help the insurer to maintain its good operating performance. We also believe SGIC will maintain its current capitalization amid moderate premium growth.

Downside scenario

We may lower the ratings if:

- SGIC's operating performance deteriorates significantly, possibly due to weak underwriting standards or aggressive overseas expansion;
- The insurer's capital weakens substantially due to unexpected losses in insurance operations amid a significant economic downturn in Korea; or
- The government opens the guarantee market to other larger domestic property/ casualty (P/C) insurers or privatizes SGIC rapidly. This could undermine the insurer's public role and link with the government.

Upside scenario

We view this to be a remote scenario over the next one to two years. We could raise the rating on SGIC if:

- We revise upward our assessment of SGIC's stand-alone credit profile, possibly due to the insurer's enhanced competitive position while it sustains good operating performance; and
- SGIC strengthens its link with the government such that we see a very high likelihood of extraordinary government support to the insurer.

Key Assumptions

- Korea's real GDP to grow by 4.0% in 2021 as the economy recovers from the COVID-19 pandemic, compared with a 0.9% contraction in 2020.
- The policy rate in Korea to increase to 0.75% by end-2021 and to 1.25% by end-2022, from the current 0.5%.
- Unemployment rate to gradually improve to 3.8% in 2021 and 3.4% in 2022, from 4.0% in 2020.

Seoul Guarantee Insurance Co.--Key Metrics

| (Bil. KRW) | 2018a | 2019a | 2020a | 2021f | 2022f |
|----------------------------------|--------------|--------------|--------------|--------------|--------------|
| Gross premiums written | 1,984 | 1,888 | 1,953 | 1950-2150 | 2000-2200 |
| Net income | 444 | 432 | 329 | 300-400 | 350-450 |
| EBITDA fixed-charge coverage (x) | 101 | 104 | 66 | 80-100 | 80-100 |
| Financial leverage (%) | 1.1 | 1.0 | 0.9 | 1-3 | 1-3 |
| Return on equity (%) | 10.9 | 10.0 | 7.1 | 6-9 | 6-9 |

Seoul Guarantee Insurance Co.--Key Metrics (cont.)

| (Bil. KRW) | 2018a | 2019a | 2020a | 2021f | 2022f |
|--------------------------|--------------|--------------|--------------|--------------|--------------|
| S&P capital adequacy | Strong | Strong | Strong | Strong | Strong |
| Net investment yield (%) | 2.6 | 2.5 | 2.2 | 2-2.5 | 2-2.5 |
| Net combined ratio (%) | 73.5 | 79.3 | 85.8 | 78-83 | 75-80 |
| Return on revenue (%) | 32.4 | 28.5 | 21.3 | 23-28 | 23-28 |

KRW--Korean won. a--Actual. f--Forecast.

Business Risk Profile: Strong

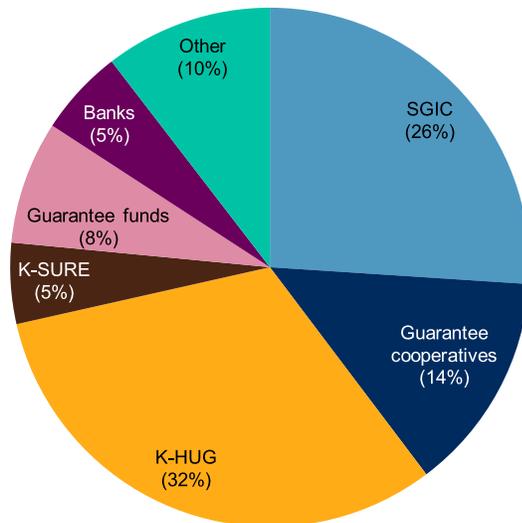
SGIC's strong competitive presence in Korea's guarantee insurance market will remain underpinned by its position as the only comprehensive provider of guarantee insurance in the country. Korea's guarantee industry has a wide range of providers--ranging from cooperatives, banks, and guarantee funds operated by the government. Unlike its peers, SGIC does not face regulations on reach to customers (specific customer groups) or market segments. The insurer has about 26% market share in terms of the amount of outstanding guarantee provided in Korea as of end-2020. SGIC derives its premiums predominantly from Korea, a market that we assess as having intermediate P/C insurance industry and country risk.

SGIC is likely to leverage its leading position in the domestic guarantee insurance market and gradually expand its overseas portfolio. It has operations in the U.S., United Arab Emirates, Vietnam, and China through its branches or representative offices. SGIC has been working to establish a joint venture in China with several Chinese insurers. That said, we expect the pace of overseas expansion to be gradual. This is because of SGIC's record of prudent strategic planning and execution, and potential volatility in the broader global market.

Chart 1

SGIC Has A Strong Presence In The Domestic Guarantee Market

Korea domestic guarantee market share 2020 (based on outstanding guarantees)



KHUG--Korea Housing & Urban Guarantee Corp. K-SURE--Korea Trade Insurance Corp. Source: S&P Global Ratings.

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SGIC's pricing power--stemming from its strong market position and controlled distribution channels--will likely underpin its underwriting performance over the next two years. The insurer's combined ratio increased to about 86% in 2020 from about 69% in 2017 mainly due to deterioration of loss ratios on some credit insurance products such as guarantees on jeonse deposits or retail loans. Credit insurance products comprise about 39% of SGIC's business portfolio in terms of guarantee exposure as of end 2020.

We expect SGIC's efforts to adjust premium rates on some underperforming policy-related credit insurance products in recent years to improve underwriting performance. The company has also been strengthening underwriting standards for these products. SGIC's combined ratio improved to about 66% during the first three months of 2021, down than 85% during the same period a year ago. We note that SGIC's average combined ratio has been about 74% over the past five years, lower than those of its global peers such as CESCE (Compania Espanola de Seguros de Credito a la Exportacion S.A.). A combined ratio below 100% indicates underwriting profit.

Financial Risk Profile: Satisfactory

SGIC is likely to maintain strong capital adequacy, as measured by our capital model, given the insurer's moderate

business growth, improvements in profitability, and prudent investment allocation. However, the sensitivity of guarantee insurance to economic and market downturns dilutes this capital strength. In particular, SGIC's policy role in supporting SMEs and in underwriting guarantee insurance of individuals with mid to low credit profiles could heighten the volatility, in our view.

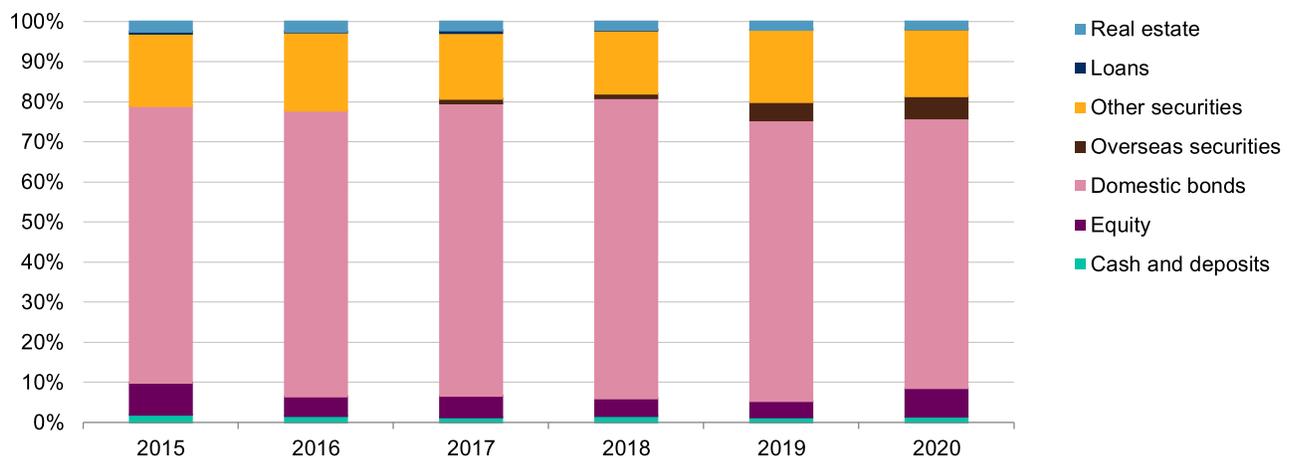
We project SGIC's average net earned premium will increase by 3%-5% annually amid moderate growth prospects over the next few years. The insurer's improving loss ratios on the back of efforts to tighten risk controls will support its underwriting performance.

We anticipate SGIC will maintain a high dividend payout of 30%-40% to repay the government's capital injection received over 2000-2001. The company's payout ratio was about 32% in 2020. SGIC's regulatory solvency ratio was about 415% as of March 31, 2021, higher than that of most of domestic P/C insurers and the regulatory minimum requirement of 100%.

Chart 2

SGIC Has A Stable Investment Portfolio

Break-down of investment assets



Source: S&P Global Ratings.

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We expect SGIC to maintain a prudent investment strategy over the next few years. The insurer's solid underwriting profitability enables it to maintain a largely stable investment portfolio that mostly consists of high-quality fixed income securities diversified across sectors and obligors. As of Dec. 31, 2020, SGIC's relatively high-risk assets, including alternative investments, loans, properties, and equities, accounted for about 25% of the total invested assets.

SGIC will likely continue to increase its overseas investments, although at a very gradual pace, in our view. These overseas investments comprise mainly investment grade bonds of financial institutions or companies in developed markets. We consider the insurer's sensitivity to foreign exchange movements as limited given its hedging strategy using foreign exchange swaps. However, the increase in foreign exchange risk hedging costs could lower investment

yields, especially amid heightened financial market volatility.

In our view, SGIC will adequately manage risks and proactively formulate its business strategy, in coordination with the government via KDIC. The insurer focuses on developing its risk models to reflect the guarantee insurance sector's sensitivity to economic cycles. SGIC sets its risk appetite by incorporating its risk-adjusted return, business growth plans, and capital solvency.

SGIC's financial leverage is likely to remain low, reflecting its proactive capital management strategies. The insurer had a fairly small amount of outstanding commercial paper, at about Korean won (KRW) 45 billion as of Dec. 31, 2020.

Other Key Credit Considerations

Governance

SGIC's ability to adjust and control the execution of its strategies is in line with peers', despite the insurer's policy roles. In general, SGIC's strategic plans are consistent with its capabilities, taking into account market conditions. As a government-owned and highly regulated entity, SGIC maintains a stable governance structure.

Liquidity

SGIC has good access to liquidity sources and holds sufficient liquid assets, in our view. We estimate its liquidity ratio as 1.6x as of end-2020. We do not expect the insurer to face liquidity constraints in meeting its obligations over the next two years, backed by the good quality of its fixed income securities-based asset portfolio and improving operating performance.

Government support

With SGIC undertaking a policy role through the provision of low-margin guarantee insurance to SMEs and the lower-income population, we see a high likelihood of timely and sufficient extraordinary support from the Korean government in the event of financial distress. Our ratings approach is based on SGIC's very important role for, and strong link with, the Korean government.

SGIC carries out policy roles by providing guarantees through memoranda of understanding with the Ministry of SMEs and Startups as well as other government agencies, and by providing guarantees on loans and deposits for jeonse. SGIC also provides guarantees on Saitdol loans, which were launched through a joint effort between SGIC, regulators, and lenders. SGIC provides guarantees for the loans so that retail borrowers with low to midrange credit scores can access credit at lower interest rates.

We believe that, as a majority owner of SGIC, KDIC can influence SGIC's business strategy through participation in shareholder and board of director meetings, as well as through contracts for its business operations. KDIC owns a 93.85% stake in SGIC.

Appendix

| Seoul Guarantee Insurance Co.--Credit Metric History | | | | | |
|--|-------------|-------------|-------------|-------------|-------------|
| | 2020 | 2019 | 2018 | 2017 | 2016 |
| Total invested assets (Bil. KRW) | 7,365 | 6,852 | 6,721 | 6,267 | 5,999 |
| Total shareholder equity (Bil. KRW) | 4,840 | 4,472 | 4,180 | 3,951 | 3,901 |
| Gross premium written (Bil. KRW) | 1,953 | 1,888 | 1,984 | 1,767 | 1,524 |
| Net premium written (Bil. KRW) | 1,664 | 1,623 | 1,771 | 1,609 | 1,387 |
| Net premium earned (Bil. KRW) | 1,643 | 1,645 | 1,602 | 1,468 | 1,376 |
| Reinsurance utilization (%) | 14.8 | 14.0 | 10.7 | 9.0 | 9.0 |
| EBIT (Bil. KRW) | 434 | 564 | 600 | 625 | 820 |
| Net income (attributable to all shareholders) (Bil. KRW) | 329 | 432 | 444 | 460 | 614 |
| Return on revenue (%) | 21.3 | 28.5 | 32.4 | 36.7 | 42.1 |
| Return on shareholders' equity (%) | 7.1 | 10.0 | 10.9 | 11.7 | 16.3 |
| Property/casualty: Net combined ratio (%) | 85.8 | 79.3 | 73.5 | 68.7 | 63.9 |
| Property/casualty: Net expense ratio (%) | 16.9 | 16.2 | 20.2 | 18.5 | 17.0 |
| Net investment yield (%) | 2.2 | 2.5 | 2.6 | 2.4 | 2.5 |
| Net investment yield including investment gains/(losses) (%) | 2.9 | 3.1 | 2.9 | 2.8 | 5.4 |

KRW--Korean won.

Related Criteria

- Criteria | Insurance | General: Insurers Rating Methodology, July 1, 2019
- General Criteria: Group Rating Methodology, July 1, 2019
- General Criteria: Rating Government-Related Entities: Methodology And Assumptions, March 25, 2015
- Criteria | Insurance | Specialty: Trade Credit Insurance Capital Requirements Under S&P Global Ratings' Capital Adequacy Model, Dec. 6, 2013
- Criteria | Insurance | General: Refined Methodology And Assumptions For Analyzing Insurer Capital Adequacy Using The Risk-Based Insurance Capital Model, June 7, 2010
- General Criteria: Use Of CreditWatch And Outlooks, Sept. 14, 2009

Related Research

- Research Update: Korea 'AA/A-1+' Ratings Affirmed; Outlook Stable, April 28, 2021
- Insurance Industry And Country Risk Assessment: Korea Property/Casualty, June 30, 2020

Business And Financial Risk Matrix

| Business risk profile | Financial risk profile | | | | | | | |
|-----------------------|------------------------|-------------|----------|----------------|----------|----------|--------|------------|
| | Excellent | Very Strong | Strong | Satisfactory | Fair | Marginal | Weak | Vulnerable |
| Excellent | aa+ | aa | aa- | a+ | a- | bbb | bb+ | b+ |
| Very Strong | aa | aa/aa- | aa-/a+ | a+/a | a-/bbb+ | bbb/bbb- | bb+/bb | b+ |
| Strong | aa-/a+ | a+/a | a/a- | a-/bbb+ | bbb+/bbb | bbb-/bb+ | bb/bb- | b+/b |
| Satisfactory | a | a/a- | a-/bbb+ | bbb+/bbb | bbb/bbb- | bb+/bb | bb-/b+ | b/b- |
| Fair | a- | a-/bbb+ | bbb+/bbb | bbb/bbb- | bbb-/bb+ | bb/bb- | b+/b | b- |
| Weak | bbb+/bbb | bbb/bbb- | bbb-/bb+ | bb+/bb | bb/bb- | bb-/b+ | b/b- | b- |
| Vulnerable | bbb-/bb+ | bb+/bb | bb/bb- | bb-/b+ | b+/b | b/b- | b- | b- |

Note: Where table indicates two possible outcomes, we determine the anchor as follows: For financial risk profiles that we assess as satisfactory or stronger, we consider the relative strength of both the business risk and financial risk profiles within the cell. This is based on a holistic assessment of the relative strengths of the rating factors of the business risk profile and financial risk profile. For financial risk profiles that we assess as fair or weaker, we typically place more weight on the relative strength of the rating factors of the financial risk profile.

Ratings Detail (As Of August 26, 2021)***Seoul Guarantee Insurance Co.**

Financial Strength Rating

Local Currency

A+/Stable/--

Issuer Credit Rating

Local Currency

A+/Stable/--

Holding Company

None

Domicile

Korea, Republic of

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