

RatingsDirect®

Seoul Guarantee Insurance Co.

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Seoul Guarantee Insurance Co.

| SACP* Assessments | | | | SACP* | | Support | | Ratings | | |
|-------------------|----|---|--------------------|-------|---|----------------|---|---------------|---|---------------------------|
| Anchor | a- | + | Modifiers | 0 | = | a- | + | 2 | = | Financial Strength Rating |
| Business Risk | | | ERM and Management | 0 | | Liquidity | 0 | Group Support | 0 | A+/Stable/-- |
| Strong | | | Holistic Analysis | 0 | | Sovereign Risk | 0 | Gov't Support | 2 | |
| Financial Risk | | | | | | | | | | |
| Upper Adequate | | | | | | | | | | |

*Stand-alone credit profile.
See Ratings Detail for a complete list of rated entities and ratings covered by this report.

Major Rating Factors

| Strengths | Weaknesses |
|---|--|
| <ul style="list-style-type: none"> High likelihood of extraordinary government support. Solid market presence as the only comprehensive guarantee insurer in Korea. Good operating performance backed by controlled distribution channels. | <ul style="list-style-type: none"> Concentrated business portfolio in the guarantee insurance market. High sensitivity to a downturn in the economy. |

Rationale

The rating on Seoul Guarantee Insurance Co. (SGIC) reflects our view of a high likelihood that the Korean government would provide timely and sufficient extraordinary support to the insurer in the event of financial distress. SGIC is the only comprehensive provider of guarantee insurance in the domestic market. We believe the insurer will sustain its fairly good operating performance, backed by its strong pricing power stemming from its leading domestic market position and well controlled distribution channels. However, SGIC is exposed to volatility in its capital and earnings, given the guarantee insurance business is vulnerable to an economic downturn.

Outlook: Stable

The stable outlook on SGIC reflects our view of the high likelihood that the Korean government would provide extraordinary support to the insurer in the event of financial distress over the next two years. We expect SGIC's strong business presence in Korea to help the insurer to maintain its good operating performance. We also believe SGIC will maintain its capital position at current levels despite sluggish growth in the domestic market.

Downside scenario

We may lower the ratings if:

- SGIC's operating performance deteriorates significantly from our base-case assumptions, possibly due to loosening underwriting standards or aggressive overseas expansion;
- SGIC's capital weakens substantially, possibly because of unexpected losses in insurance operations due to a significant economic downturn in Korea; or
- The government opens the guarantee market to other larger domestic property and casualty insurers, or the privatization of SGIC takes place and proceeds rapidly, which could undermine the insurer's public role and link with the government. However, we view this as unlikely at least over the next one to two years.

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 (SACP), possibly due to its enhanced competitive position; and
- SGIC's link with the government strengthens such that we see a very high likelihood of extraordinary government support.

Macroeconomic Assumptions

- Policy rates in Korea will increase to 2.0% by 2019 from the current 1.5%.
- Korea's annual real GDP growth will be 2.7% in 2018 and 2.6% in 2019.

Key Metrics

| (KRW in billions) | 2015A | 2016A | 2017A | 2018F | 2019F | 2020F |
|----------------------------------|--------------|--------------|--------------|--------------|--------------|--------------|
| Gross premiums written | 1,443.0 | 1,524.2 | 1,767.1 | 1,825-1,900 | 1,900-2,000 | 1,975-2,100 |
| Net income | 511.3 | 614.3 | 460.0 | 400-450 | 410-460 | 420-470 |
| EBITDA fixed-charge coverage (x) | 54.7 | 67.8 | 79.8 | 80-90 | over 100 | over 100 |
| Financial leverage (%) | 3.6 | 2.8 | 2.0 | 1.0-3.0 | 1.0-3.0 | 1.0-3.0 |
| Return on equity (%) | 14.0 | 16.3 | 11.7 | 10.0-12.0 | 10.0-12.0 | 10.0-12.0 |
| S&P capital adequacy | Very strong | Strong |
| Net investment yield (%) | 2.9 | 2.5 | 2.4 | 2.2-2.6 | 2.2-2.6 | 2.2-2.6 |

| Key Metrics (cont.) | | | | | | |
|----------------------------|--------------|--------------|--------------|--------------|--------------|--------------|
| (KRW in billions) | 2015A | 2016A | 2017A | 2018F | 2019F | 2020F |
| Net combined ratio (%) | 79.4 | 63.9 | 68.7 | 70-75 | 70-75 | 70-75 |
| Return on revenue (%) | 38.3 | 42.1 | 36.7 | 30-35 | 30-35 | 30-35 |

KRW--Korean won. A--Actual. F--Forecast. Forecast data represent S&P Global Ratings' base-case assumptions.

Business Risk Profile: Strong

We expect SGIC to maintain its strong competitive position with good operating performance and stable revenue from mostly controlled distribution channels. The insurer's pricing power stemming from its leading domestic market position and diversified products within the credit and guarantee business supports our view. SGIC's loss ratio has been stable at 50%-55% over the past several years.

We expect SGIC to maintain its solid presence in Korea's guarantee insurance market. The insurer is the only comprehensive provider of guarantee insurance in Korea, with an approximately 23% market share in terms of the amounts of guarantee provided in 2017. SGIC benefits from limited competition due to regulatory controls on the guarantee insurance market. Other guarantee companies (such as cooperatives, banks, and guarantee funds operated by the government) offer slightly different guarantee products in terms of customers or market segment. However, SGIC's concentrated business portfolio in the guarantee insurance market offsets the positive factors to some extent.

Financial Risk Profile : Upper Adequate

In our view, SGIC will remain well capitalized amid stable growth prospects. We expect the insurer to maintain its combined ratio at 70%-75% (indicating solid underwriting profits) over the next one to two years. Our expectation of steady growth in the Korean economy and stable credit quality of the private and public sectors, including households, supports our view.

We expect SGIC to maintain a high dividend payout over the next two years. In our view, these dividends to Korea Deposit Insurance Corp (KDIC), the largest shareholder with 94% stake, serve as a means for SGIC to pay back the government's capital injection received over 2000-2001. SGIC's dividend payout ratio is likely to remain at 50%-80%. The insurer's regulatory risk-based capital ratio was 403% on March 31, 2018, higher than that of most of domestic property and casualty insurers, and the regulatory minimum requirement of 100%.

SGIC is likely to remain exposed to volatility in capital and earnings, given the susceptibility of the guarantee insurance business to economic and market downturns. The insurer's increasing role in supporting small and midsize enterprises (SMEs) and underwriting guarantee insurance of mid-to-low credit profile individuals could heighten the volatility.

These sensitivities are mitigated by SGIC's prudent investment philosophy and limited exposure to risky assets. About 80% of the insurer's investment portfolio consists of good-quality fixed-income securities, and we expect the investment strategy to remain unchanged in the next few years. We also believe SGIC has adequate diversification across sectors and obligors in its investment portfolio.

We believe that SGIC will maintain adequate financial flexibility, supported by its fairly low financial leverage, high fixed-charge coverage, and limited debt. We expect the leverage to gradually reduce on the back of the insurer's continuing earnings accumulation. We also believe SGIC generates sufficient EBITDA to cover fixed charges as well as interest payments. The coverage ratio was about 80x in 2017.

Other Assessments

In our view, SGIC has a fully functioning risk control system to deal with major risk factors. The company has developed its risk models to reflect the guarantee insurance sector's sensitivity to economic cycles. SGIC's risk governance structure also supports its risk management. We believe the company's process for identifying and mitigating emerging risk is still developing. We expect the insurer's enterprise risk management (ERM) to continue to evolve, given its plan to develop a more integrated and strategic risk management system, and in light of Korea's tightening regulatory framework. We assess the insurer's ERM as adequate based on these factors.

We consider SGIC's strategic planning to be in line with market practices. In general, the strategic plans are consistent with the insurer's capabilities, taking into account market conditions. SGIC has occasionally set somewhat aggressive financial and operational goals, but its focus on risk controls remains unchanged, in our view. As a government-owned and highly regulated entity, we do not see any deficiencies in the insurer's governance structure.

SGIC has strong access to liquidity sources. It benefits from the good quality of its fixed income securities-based asset portfolio and stable operating performance. The insurer had outstanding commercial paper (CP) of approximately Korean won (KRW) 75 billion as of Dec. 31, 2017, but we do not believe this will constrain its liquidity profile. The CP redemption schedule is gradual, with maturities ranging to 2051. We see no major refinancing risks and believe SGIC is capable of managing unexpectedly large claims.

Other Considerations

We see a high likelihood of the Korean government providing timely and sufficient extraordinary support to SGIC in the event of financial distress.

As the only comprehensive guarantee insurer in Korea, SGIC plays a very important role in the economy through its support of SME business operations and contribution to the stability of the housing market. SGIC's public role is further illustrated by its "Saitdol" loans, which are jointly offered by SGIC, the regulators, and lenders. SGIC provides guarantees to the loans so that retail borrowers can access credit at lower interest rates.

We expect KDIC to remain a strong and stable shareholder with a 94% stake in SGIC in the next few years. As a majority owner, we believe 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.

Rating Score Snapshot

| Financial Strength Rating | A+ / Stable / -- |
|---------------------------|------------------|
| BRP/FRP Anchor | a- |

Rating Score Snapshot (cont.)

| Financial Strength Rating | A+ / Stable / -- |
|----------------------------------|-------------------------|
| Business Risk Profile | Strong |
| IICRA* | Intermediate Risk |
| Competitive Position | Strong |
| Financial Risk Profile | Upper Adequate |
| Capital & Earnings | Moderately Strong |
| Risk Position | Moderate Risk |
| Financial Flexibility | Adequate |
| Modifiers | 0 |
| ERM and Management | 0 |
| Enterprise Risk Management | Adequate |
| Management & Governance | Satisfactory |
| Holistic Analysis | 0 |
| Liquidity | Strong |
| Support | +2 |
| Group Support | 0 |
| Government Support | +2 |

*Insurance Industry And Country Risk Assessment.

Related Criteria

- General Criteria: Rating Government-Related Entities: Methodology And Assumptions, March 25, 2015
- Criteria - Insurance - Specialty: Trade Credit Insurance Capital Requirements Under Standard & Poor's Capital Adequacy Model, Dec. 6, 2013
- General Criteria: Group Rating Methodology, Nov. 19, 2013
- Criteria - Insurance - General: Enterprise Risk Management, May 7, 2013
- Criteria - Insurance - General: Insurers: Rating Methodology, May 7, 2013
- General Criteria: Methodology: Management And Governance Credit Factors For Corporate Entities And Insurers, Nov. 13, 2012
- 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

- Credit FAQ: How Will IFRS 17 Affect The Credit Quality Of Insurers?, Jun. 5, 2018
- Insurance Industry And Country Risk Assessment: Korea Life, Oct. 11, 2017
- Insurance Industry And Country Risk Assessment: Korea Property/Casualty, Aug. 1, 2017

- Seoul Guarantee Insurance Co. Upgraded To 'A+' On Strengthening Public Roles; Outlook Stable, Jun. 30, 2017

Ratings Detail (As Of July 26, 2018)

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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