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Research Update:

Seoul Guarantee Insurance Co. Upgraded To 'A+' On Strengthening Public Roles; Outlook Stable

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Overview

- We expect SGIC's essential guarantee services for the economy, especially in the SME sector and housing market, to strengthen in the coming years.
- In our view, revitalization of SMEs and stability of the housing market are one of the key policy objectives of the new government to support the economy.
- We believe that the likelihood of the government providing extraordinary support for SGIC is high.
- We are therefore upgrading SGIC to 'A+', from 'A', to reflect the additional government support. At the same time, we are maintaining the stand-alone credit profile on SGIC.
- The stable outlook on SGIC reflects our view that SGIC will likely maintain its fairly good operating performance, backed by its strong market position in Korea, while sustaining its financial risk profile over the next 18-24 months.

Rating Action

On June 30, 2017, S&P Global Ratings raised the long-term financial strength and issuer credit ratings on Korea-based credit and guarantee insurer, Seoul Guarantee Insurance Co. (SGIC), to 'A+' from 'A'. The outlook is stable. At the same time, the stand-alone credit profile (SACP) on SGIC remains 'a-'.

Rationale

We believe SGIC, being the only comprehensive guarantee insurer in Korea, has very important roles in the economy in supporting small and mid-sized enterprises' (SMEs) business operations and contributing to the stability of the housing market. We expect SGIC's roles to further strengthen under the new government in the coming years. We now assess the likelihood of the government providing extraordinary support to SGIC has increased to high. At the same time, we expect the government to continue to maintain its strong link through Korea Deposit Insurance Corp.'s (KDIC; not rated) ownership in SGIC over the next one to two years.

We anticipate stronger cooperation between SGIC and the government to support SMEs through provision of guarantees in business transactions. We believe the government's plan to raise the status of Small and Medium Business Administration (SMBA) as one of the government department led by a minister is an indication of its commitment to support SMEs. SGIC's guarantees provided

through memoranda of understanding (MOUs) with SMBA and other government agencies, such as Korean Intellectual Property Office and National Tax Office, have been growing. We expect the trend to continue in the coming years. The guarantees provided through the MOUs increased to about 9% (Korean won [KRW] 14.5 trillion) of its total in 2016 from about 3% five years ago.

We expect SGIC to continue to provide important guarantee products in Korea's housing market. We believe SGIC's guarantee products, such as guarantee for return of "jeonse" deposits (lump-sum refundable deposits for rental) and jeonse loans, and mortgage credit insurance, are crucial for financing transactions in the housing market. Considering that one of the government's key policy agenda is to maintain the stability of the housing market amid high household leverage, we believe SGIC's roles are getting more important. Moreover, we expect SGIC to provide more guarantees in the rental housing market along with the government's plans to supply more rental houses to support low- to middle-income households.

We believe SGIC's policy role to support individual borrowers with low to midrange credit scores will also likely strengthen. "Saitdol" loans were launched for individual borrowers through a joint effort between SGIC, regulators, and lenders. SGIC provides guarantees for the product so that the borrowers can access the loans at lower rates than previously. This indicates SGIC's growing policy roles, in our view. Saitdol loans had been initially launched with a total capacity of KRW1 trillion in July 2016, but that expanded to KRW2 trillion in April 2017.

We continue to assess SGIC's link with the government as strong. We expect KDIC to remain a strong and stable shareholder with a 94% stake in SGIC in the next few years. We believe KDIC could influence SGIC's business strategy through participation of shareholder and board of director meetings, as well as through the MOU contracts for its business operations. In our view, the privatization of SGIC is unlikely in the next one to two years, because its growing public roles are aligned with the government's policy objectives. We believe that even if a privatization process begins, it could take some time for SGIC's current roles to be fully replaced. However, we cannot completely rule out the possibility that the government may unexpectedly shift its policy directive over SGIC and proceed with privatization in the medium to long term; that constrains our assessment for a stronger link between SGIC and the government.

We expect SGIC to maintain its strong business position in Korea's property and casualty insurance industry, which we assess to have an intermediate industry risk. In our view, SGIC is likely to sustain its fairly good operating performance, backed by its strong pricing power stemming from its leading domestic market position and well-controlled distribution channels. Nevertheless, SGIC's business concentration in guarantee insurance offsets the positive factors, to some extent, in our opinion.

We believe SGIC will likely maintain the current financial risk profile. In our view, SGIC has good capital and earnings, and implements a prudent

investment strategy focusing on high-quality fixed-income investment securities. However, potential volatility in its capital and earnings, given the guarantee insurance business is vulnerable to an economic downturn, constrains its overall risk profile.

Outlook

The stable outlook on SGIC reflects our view that the insurer's strong business position in Korea will help it to maintain its operating performance over the next 18-24 months. We believe SGIC will maintain its capital and earnings at the current level despite sluggish growth in the domestic market and low interest rates. We also expect SGIC's risk profile to remain largely unchanged in the coming two years.

Downside scenario

We may lower the ratings if:

- SGIC's earnings consistently fall below our base-case assumptions (e.g., loss ratios consistently stay above 80%);
- Its capital weakens substantially from the current level, 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 on SGIC proceeds very rapidly, which could undermine SGIC's public roles and its link with the government.

Upside scenario

Although we view this as a remote scenario, we could raise the rating on SGIC if:

- We revise upward our assessment of SGIC's SACP due to its further enhanced competitive position; and
- SGIC's link with the government strengthens so that we assess a very high likelihood of extraordinary government support.

Ratings Score Snapshot

Anchor	a-
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

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
- 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

Ratings List

Upgraded	To	From
Seoul Guarantee Insurance Co.		
Counterparty Credit Rating		
Local Currency	A+/Stable/--	A/Stable/--
Financial Strength Rating		
Local Currency	A+/Stable/--	A/Stable/--

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