



RATING ACTION COMMENTARY

Fitch Affirms Construction Guarantee's IFS at 'A'; Outlook Stable

Thu 09 Dec, 2021 - 9:08 PM ET

Fitch Ratings - Singapore/Hong Kong - 09 Dec 2021: Fitch Ratings has affirmed South Korea-based Construction Guarantee's (CG) Insurer Financial Strength (IFS) Rating at 'A' (Strong). The Outlook is Stable.

KEY RATING DRIVERS

The rating takes into consideration the company's 'Very Strong' capitalisation with a 'Moderate' company profile. It also incorporates the strong state support that CG continues to enjoy. CG, which is supervised by the Ministry of Land, Infrastructure and Transport, was set up to promote the development of the local construction industry by providing insurance coverage for construction firms. The rating also factors in CG's 'Moderate' financial performance and high business concentration risk in the niche domestic construction sector.

CG operates under a regulatory capital regime modelled on the Basel III capital framework. It had a regulatory capital ratio of 301% at end-June 2021, staying above 250% for the past three years, well in excess of the 100% regulatory minimum. This provides a deep cushion for its potentially volatile business portfolio. Net premiums written to total capital was below 0.5x at end-2020 and end-June 2021. Its capitalisation, measured by Fitch's Prism Model Score, was well into 'Very Strong' in 2020 and is likely to remain so for 2021.

The company's return on equity (ROE) amounted to 2.5% in 2020, with a three-year average of 2.6%. It fell to 2.2% in 1H21 on an annualised basis. Its combined ratio was below 85% for the past three years. Nonetheless, Fitch believes CG faces potential volatility in its underwriting performance given its focus on the niche guarantee insurance segment, leaving it vulnerable to cycles in the Korean economy and construction sector.

Fitch ranks CG's company profile as 'Moderate' as a result of a 'Moderate' business profile and 'Moderate/Favourable' corporate governance compared with that of all other Korean non-life insurance companies, given its modest operating scale with limited geographical and business diversity. Fitch therefore scores CG's company profile at 'bbb+' under our credit-factor scoring guidelines. CG sources more than 90% of its business premiums from a niche segment in Korea, resulting in a market share that is less than 1% of aggregate non-life industry premiums.

RATING SENSITIVITIES

Factors that could, individually or collectively, lead to negative rating action/downgrade:

- Perceived weakening of state support for CG.
- Persistent weakening in the company profile in terms of business franchise and operating scale.
- Consistently lower capitalisation, such as the Fitch Prism Model score below 'Strong' and regulatory capital ratio below 200% on a prolonged basis.
- Further material deterioration in financial performance, including its ROE

Factors that could, individually or collectively, lead to positive rating action/upgrade:

- Sustained improvement in the company profile; for instance, better operating scale as well as successful and profitable business diversification in terms of business class and geographical spread.
- Improvement in financial performance, for instance, its ROE improving to above 7% on a sustained basis.
- Maintenance of capitalisation, such as the Fitch Prism Model score at well into 'Strong' and the regulatory capital ratio above 280% on a sustained basis.

BEST/WORST CASE RATING SCENARIO

International scale credit ratings of Financial Institutions and Covered Bond issuers have a best-case rating upgrade scenario (defined as the 99th percentile of rating transitions, measured in a positive direction) of three notches over a three-year rating horizon; and a worst-case rating downgrade scenario (defined as the 99th percentile of rating transitions, measured in a negative direction) of four notches over three years. The complete span of best- and worst-case scenario credit ratings for all rating categories ranges from 'AAA' to 'D'. Best- and worst-case scenario credit ratings are based on historical performance. For more information about the methodology used to determine sector-specific best- and worst-case scenario credit ratings, visit <https://www.fitchratings.com/site/re/10111579>

REFERENCES FOR SUBSTANTIALLY MATERIAL SOURCE CITED AS KEY DRIVER OF RATING

The principal sources of information used in the analysis are described in the Applicable Criteria.

ESG CONSIDERATIONS

Unless otherwise disclosed in this section, the highest level of ESG credit relevance is a score of '3'. This means ESG issues are credit-neutral or have only a minimal credit impact on the entity, either due to their nature or the way in which they are being managed by the entity. For more information on Fitch's ESG Relevance Scores, visit www.fitchratings.com/esg

RATING ACTIONS

ENTITY / DEBT ↕	RATING ↕		PRIOR ↕
Construction Guarantee	Ins Fin Str	A Rating Outlook Stable	A Rating Outlook Stable
	Affirmed		

[VIEW ADDITIONAL RATING DETAILS](#)

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APPLICABLE CRITERIA

[Insurance Rating Criteria \(pub. 26 Nov 2021\) \(including rating assumption sensitivity\)](#)

APPLICABLE MODELS

Numbers in parentheses accompanying applicable model(s) contain hyperlinks to criteria providing description of model(s).

Prism Factor-Based Capital Model, v1.7.2 ([1](#))

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Construction Guarantee

EU Endorsed, UK Endorsed

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Insurance	Asia-Pacific	South Korea
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