

Rating Action: Moody's affirms Construction Guarantee Cooperative's A2 IFSR; outlook stable

8 November 2022

Hong Kong, November 8, 2022 -- Moody's Investors Service has affirmed the A2 insurance financial strength rating (IFSR) of Construction Guarantee Cooperative (CG).

The outlook on CG remains stable.

RATINGS RATIONALE

The affirmation of CG's A2 IFSR reflects the company's leading position in Korea's construction guarantee market, strong capitalization, gradually rising but still low high-risk asset exposure, and moderate but stable profitability.

These strengths are offset by CG's high gross guarantee exposure to its shareholders' equity, exposure to the cyclical guarantee business in the construction industry, and high susceptibility to member-specific shocks .

As the largest player in construction guarantee market, CG extended 63.5% of the industry's construction guarantee balance at the end of June 2022. Moody's views CG's market position will remain strong in the next 12-18 months, despite the ongoing loosening of the regulatory partition between the general construction and specialty construction guarantee markets.

CG's capitalization is strong, given its consistently increasing equity base supported by stable retained earnings and new member contributions. Its gross underwriting leverage remained very low at 0.07x as of 31 December 2021.

Moody's expects CG to maintain good asset quality over the next 12-18 months because of its conservative investment strategy. The cooperative's high-risk assets as a percentage of shareholders' equity rose to 11.8% at the end of June 2022 from 2.5% in 2020, due to its increased alternative investments and equity-type securities in response to the regulatory guideline for government-affiliated financial guarantors to allocate their funds more efficiently. Nevertheless, its high-risk assets remain very low. CG's bond portfolio consists mostly of treasury and bonds from high-quality financial institutions. It also holds a large portion of its investments in bank deposits and money market funds.

Moody's expects CG's profitability to remain moderate over the next 12-18 months, given its policy function to support its member companies with preferential pricing. The cooperative's five-year average return on capital has been stable at 2.7% from 2017 to 2021.

Moody's has also considered the cooperative's close relationship with the Ministry of Land, Infrastructure and Transport (MOLIT) and its important policy function of supporting the domestic construction industry. CG's operations and mandate are governed by the Framework Act on the Construction Industry. Consequently, while CG is not owned by the Government of Korea (Aa2 stable), Moody's assumes that the government will be willing to provide financial and operational support to the cooperative when needed.

The stable outlook reflects Moody's expectation that CG will maintain its leading position in the construction guarantee market, solid capitalization and stable profitability over the next 12-18 months.

FACTORS THAT COULD LEAD TO AN UPGRADE OR DOWNGRADE OF THE RATINGS

WHAT COULD CHANGE THE RATING UP

Moody's could upgrade CG's rating if there is sustained and significant improvement in its profitability; greater business diversification in terms of business lines, industry sectors or geographies, while the cooperative maintains its capitalization and profitability; or stronger operational and financial support from the MOLIT and therefore the government.

WHAT COULD CHANGE THE RATING DOWN

On the other hand, Moody's could downgrade CG's rating if its market position decreases significantly or it loses its status as a leading franchise in the designated guarantee market; its capital strength deteriorates, such that its exposure to guarantee risks as a proportion of equity increases significantly; there is volatility and a substantial weakening in its profitability, such that it consistently records net losses; or its close relationship with the MOLIT weakens, leading to lower willingness by the government to provide support when needed.

The principal methodology used in these ratings was Property and Casualty Insurers Methodology published in August 2022 and available at <https://ratings.moodys.com/api/rmc-documents/391814>. Alternatively, please see the Rating Methodologies page on <https://ratings.moodys.com> for a copy of this methodology.

Construction Guarantee Cooperative mainly provides guarantees, loans and liability insurance services to its members in Korea. As of 30 June 2022, the cooperative's total assets and shareholders' equity were KRW7.6 trillion and KRW6.5 trillion, respectively.

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For further specification of Moody's key rating assumptions and sensitivity analysis, see the sections Methodology Assumptions and Sensitivity to Assumptions in the disclosure form. Moody's Rating Symbols and Definitions can be found on <https://ratings.moodys.com/rating-definitions>.

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