

Credit Supplementation Institutions : Going beyond Guarantee for SMEs

Various Business Sectors of KODIT

I . Overview of KODIT

1. Profile of KODIT

On June 1, 1976 KODIT started its operations as a non-profit special legal entity backed by the government under a special law, the Credit Guarantee Fund Act. Its capital is raised largely with contributions from government and financial companies and reached to USD 4.2 billion.

Its outstanding guarantee as of 2016 is USD 41.1 billion and number of guaranteed companies reached to about 202 thousand. About 2000 people work for KODIT to support SMEs. Our business units is composed of 6 categories which are 1 head office, 9 regional headquarters, 107 branches, 15 rechallenge support units, 11 debt collection units and 9 insurance centers.

2. Main Businesses

KODIT provides various services for SMEs as well as credit guarantee. As you are well aware of, our business is to provide credit guarantees. Other than that, we also provide services such as credit insurance, infrastructure credit guarantee, guarantee-aligned equity investment, credit information management, corporate management consulting. The object of these services is to enhance SME's survivability and competitiveness.

3. Business Units

KODIT has business units all around the nation, Which gives KODIT a capability to cover whole nation.

4. Guarantee Services and Products

General credit guarantee services can be classified into four categories according to the types of financing: indirect financing, direct financing, credit transactions between enterprises, and others. Mainly KODIT offers guarantee for bank loans. It is a guarantee for monetary obligations arising from loans extended by bank.

In 2016, KODIT has set a basic objective of "enhancing the growth potential of the economy and acting as an economic safety net by improving the efficiency of credit guarantee operation "by expanding support to startups and innovative sectors, it focuses on the following four core areas (1) Expanding support for the growth engine sectors, (2) Strengthening the role as an economic safety net, (3) Improving the efficiency of guarantee operations, and (4) Minimizing the financial burden on SMEs.

The amount of general credit guarantee was USD 39,482 million, increased by 873 million from the year before. The amount of special guarantee for market stabilization decreased by USD 1,183 million while the issued amount of P-CBO increased by USD 574 million. The

total guarantee supplied in 2016 was USD 41,083 million whereas the newly supplied general guarantee amount was USD 9,772 million, increased by USD 807 million from the previous year.

KODIT offers 11 types of general guarantees. In effect, 7 types of general guarantees are in operation. Outstanding guarantee for bank loans at the end of 2016 was USD 29,910 million or 85.5% of the total outstanding guarantee. Guarantee for loans from non-banking financial institution increased, whereas the others decreased.

5. Capital Fund and operation multiple

KODIT's capital fund is composed of contributions from government, banks and other enterprises, as stipulated in the Credit Guarantee Fund Act. The government contribution varies every year as it is determined after comprehensive evaluation of the guarantee operation and economic outlook. Contributions from banks are determined within the annual rate of 0.3% of their corporate loans and are the most stable sources of fund for KODIT. Other sources of fund are special contributions provided under special agreement with financial institutions, large enterprises and regional governments.

With contributions of USD 1,810 million from government and USD 776 million from financial institutions and corporations in 2016, the underlying asset of KODIT at the end of 2016 reached USD 4.1 billion.

The operation multiple, calculated by dividing the credit guarantee amount by the underlying assets, is a important measure that indicates the capability to supply guarantee in accordance with economic conditions and the capacity for subrogation payment to financial institutions including banks. Article 25 of the Korea Credit Guarantee Fund Act prohibits the operation multiple higher than 20 times. The ration stands at 9.9 as of the end of 2016.

II. Credit Insurance Business

1. Introduction to Credit Insurance

Credit Insurance is a kind of insurance based on account receivable. When you consider business process, there should be 4 steps in the whole process. Firstly you have to put your capital for production and then sell it to customer and collect the payment. For Capital turnover, it takes about 96days in average among every industry. And Account receivable turnover, it takes about 51 days among every industry. It means, account receivable turnover takes more than half of total risk of turnover, because almost every industry's payment methods are based on credit.

Especially, SMEs, they are more exposed to the risk. They tend to have longer period in credit payment transaction due to lack of bargaining power when they make a contract with

powerful customer. And, if one SME is going to bankruptcy, there could be an effect like chain reaction. To reduce this kind of risk credit insurance is really necessary.

Credit insurance can prevent of chain reaction bankruptcies and contribute to creation of stable management environment.

2. Rationale of Credit Insurance

SMEs are exposed a lot different causes of default. Among the every cause, chain reaction bankruptcy caused by customers' insolvency. It takes about 43% of whole causes in bankruptcy. That's why credit insurance service is required.

3. Credit Insurance Service of KODIT

KODIT Started credit insurance business from September 1997 with bill insurance business. April 2008, KODIT expanded the restriction on the range of contractor with expanding of turnover restriction. July 2011, KODIT abolished the restriction on the rage of contractor with removing the restriction on turnover. March 2013, KODIT expanded rage of contractor with adding construction business in eligible industry. As you can see all these dates are related economic crisis. Following foreign exchange crisis in 1999, global financial crisis in 2009, government policy changing from 2013. They have formed developing opportunity of credit insurance business

KODIT has two main products in credit insurance business broadly. One is aggregate insurance which is insuring receivables from numerous buyers. And the other one is individual insurance. To make aggregate insurance contract, we need at least 5 buyers for on contract which take more than 2% of insurant's recent 1-year receivable at lease. For individual insurance, there is no restriction to be a buyer in a contract, basically.

General requirement of insurant(seller) is minimum business age. For aggregate insurance, the enterprise should have at least 2 year experience. And to be a seller in our insurance contract, they should have at least 1 year experience. And they have to have minimum credit rating and construction and retail business can't be a seller in insurance contract. Basically, there is no restriction on qualification to be a buyer, but they should have 2-year business age.

There are general restrictions on types of buyers. Government and public institution and financial institutions can't be a buyer in our insurance contract, because they don't have that much possibility in bankruptcy. And it should not have fraud possibility and it has to satisfy minimum credibility.

In case of non-payment, KODIT pays contract amount of money to insurants. There are 4 types of non-payment. First comes when a buyer doesn't pay receivables within 60 days after predetermined settlement period. Second comes when the bill issued by a buyer is dishonored. Third comes when a buyer files for court receivership. And Fourth comes when a buyer is out of business.

Credit insurance business has been expanding its volume in terms of amount of insured receivables and remains. However, it still takes small portion of whole receivable of SMEs in Korea, we are planning to expand its size and the number of customers in near future.

Nowadays, government policy has been changed. In the past, policy is only focusing on direct financing. Credit guarantee is one of the tool for supporting SMEs directly. However, it's getting more important to provide indirect support. Credit insurance is one of typical tool for support by providing safety net to SMEs business environment.

As a future strategic service of KODIT, we are planning various ways to boost the business. Firstly, we will steadily grow the business size. And we will expand its business area to factoring and credit collection businesses.

Now we are in phase of establishing basis. In a decade we will grow its size and invest in education to make experts in insurance field. Now it's in deficit, so we cannot survive without government aid. However we will set its basis and improve profitability of the business, we will make robust basis of continuing business. At that time we will make self-sustainability and try to make profit.

III. Infrastructure Guarantee Business

1. Introduction to KICGF

KICGF is abbreviation of Korea Infrastructure Credit Guarantee Fund. KICGF is an independent Fund under the management of KODIT. And it takes one of the really important business sectors in KODIT.

KICGF was established to contribute to the timely expansion of infrastructure facilities and to enhance the convenience of public life by supporting the PPP financing. Legal basis for the establishment is stipulated on Article 30 of 'Act on PPP in Infrastructure'. PPP Policy Division of Fiscal Management Bureau in Ministry of Strategy and Finance is the supervising currently.

2. Guarantee Procedure of KICGF

At the first step, a concessionaire who is designated and confirmed by the Ministry of Strategy and Finance, applies for the infrastructure credit guarantee and KICGF interviews the concessionaire. KICGF checks up the eligibility of the project and examines whether the amount of guarantee required for the project exceeds the guarantee limit(ceiling).

At the second step, the concessionaire undergoes credit analysis by KICGF. Factors such as status of business, business prospects, status of investors, total investment cost of the project, financing plan, financial transaction records, expected demand of the facilities, all kinds of

risks, expected financial statements, and etc. shall be checked by KICGF during the credit analysis.

3. Eligibility

53 eligible infrastructure facilities which are mentioned in the presentation can be guaranteed by KICGF. No other facilities that are not listed can be guaranteed by KICGF. Most of our guarantees are concentrated in the roads, railways and harbors. They constitute more than 70% of guarantees in terms of accumulated provision since the establishment of KICGF. Percentage of the roads is 48.7%, railways 14.6% and harbors 8.3% respectively.

4. Performance of KICGF

Regard to the performance of KICGF, KODIT has provided KRW 21.8 tril(USD 17.9 bil) sum of guarantees into PPP market for 233 PPP projects since its operation in 1995. In terms of guarantee approval per year, KODIT has provided KRW 2.5 tril(USD 2.2 bil) guarantees for 10 projects into PPP market in 2016.

5. Flowchart of Guarantee Issuance in PPP

The slide shows the flowchart of guarantee issuance in PPP

1) Sponsors : FI, CI, OIs make investments to Special Purpose Company

2) Loans are extended by lenders to SPC with the credit guarantee of KICGF

3+4) The ownership of the infrastructures shall be transferred to the State or a local government upon the completion of construction, and the concessionaire shall have the rights to manage and operate the infrastructure facilities for a specified period. (BTO:Build-transfer-operate)

Some of the details can be changed depending on the types of mode applied to PPP. e.g. BTL, BOT, BOO

5~7) With the cash flow it makes from the revenues of infrastructure facility, SPC pays the principal and interest of the debt as well as the dividend to FI, CI, OI.

6. Procedure of PPP in Korea in case of Solicited projects

The slide shows the procedure of PPP in Korea for solicited projects. At the first step, public notification of RFP is made by the government.

At the second step, submission of project proposal and evaluation is made.

At the next step, preferred bidder is designated by the government and concession agreement is made between the government and concessionaire.

Next, implementation plan is made and lastly, construction begins.

KICGF is involved at the syndication & financial documentation stage. But in these days, KICGF is also engaged in the financial consulting stage.

7. Role of KICGF

The slide shows what KICGF is doing in PPP. Total investment cost is made up of two different financial sources. They are subsidies from the government and private sector investment. And KICGF provides guarantee for debt only.

8. Funding Structure

As you can see, the total cost at the left side equals the total funding at the right side. Total investment cost is KRW 255 billion and DSRA is KRW 10.8 billion. Meanwhile, the equity invested by CI is KRW 32.5 bil, OI is 2.6 bil. Debt is KRW 161 bil and guaranteed loan is KRW145 bil. Govt subsidy is 69.7 bil which is about 26% of the total cost of project.

IV. Business Supporting Service

1. Consulting Service

In fact, compared to large company, many SMEs can't be equipped professional management infrastructure. Therefore, it is important to offer management supporting for growth of SMEs.

To help SMEs, we provide consulting services for credit risks and management methods. Generally, in consulting field, there are business strategies, HR management, marketing, etc.

We are gathering a lot of information, such as financial statement, qualification of clients, while handling credit guarantee. This information plays a key role in identifying the credit status of SMEs and the problems in business management.

In KODIT, we have been already providing management consulting, special consulting and relationship consulting to our customers.

In the case of CRC consulting which is one of our consulting programs, we can give advice to our customers about credit risk issues.

The main target of this consulting is SMEs with low corporate credit is SMEs with low corporate credit. Even though our general management consulting and special consulting are services connected with experts outside, Credit Risk Consulting is conducted by our own consultants.

This consulting is usually going with five steps. At first, we analyze the macro environment, and then analyze the management environment of the industry in which the company belongs.

And third, we analyze the business status and credit status of the company. And then we look at the strengths and weaknesses of the competition, and look for strength and weakness through comparison with competing groups. Finally, we project and analyze future scenarios for future enterprise developments.

This service provides advice on the credibility of the current credit-rating system and the credibility of the companies, advising us how to deal with the current situation and how to deal it. It is not just a temporary helping of corporate financial difficulties, but also an important role in helping companies keep their operations going.

2. Job Matching Service

One of the services that we offer to SMEs is called job matching service. This service was initiated by trying to reduce difficulties between job seekers and SMEs. Job seekers are finding it difficult to gain accurate information or status regarding the working environment of SMEs. It is also very difficult for SMEs to find suitable talent for their business.

In regarding of this, we are operating a JOB-CLOUD that allows job seekers and SMEs to share job information each other. From this web-site, they can get the most suitable job opening or employees. Although, most of the people who use it are our guarantee customers, we expect to expand its users to potential customers who are not using our guarantee right now.

3. Management Support System

Finally, we are going to talk about the management support system. SMEs have big burden of time and cost when they are faced with legal issues and get a financial counseling. Particularly, it is necessary a management counseling to try M&A and solve financial problem more easily. KODIT offers matching service to our homepage member with experts outside when they would like to get a professional advice. This service is provided free of charge to all SMEs on our web-site.

Until now, I briefly introduced KODIT's service to support stable management environment of SMEs. These methods can be a new role for SMEs that will be placed in more complex market and management environment.