The Services of Korea Credit Guarantee Fund
I. SMEs in the Korean Economy

- Importance of SMEs
- Challenges in SME financing
- Credit guarantee system in Korea
Importance of SMEs

Number of Companies
- SMEs 99.8%
- LEs 0.2%

Number of Employees
- SMEs 87%
- LEs 13%

Total Exports
- SMEs 42%
- LEs 58%

Total Production
- SMEs 51%
- LEs 49%
Challenges in SME Financing

- Credit quality gap
- Insufficient collateral to get formal financing
- Higher cost of transaction and information collection
- Low credit assessment ability of financial institutions
- Limited access to formal financing
Credit Guarantee System in Korea

Debtor
SME

Guarantor
KCGF
KOTEC
Local CGFs

Credit
Guarantee

Creditor
Financial Institutions

Credit Guarantee

Contribution

Supervision

Government

Contribution

Application

Credit Investigation

Contribution

Loan

Reguarantee

KFCGF

Municipality

Financial Institutions

Contribution

Contribution
II. Overview of KCGF

- KCGF in brief
- Source of funding
- Leverage ratio
- Organization
- Supervising authorities
- Services
KCGF in brief

- Public institution providing comprehensive support to SMEs
- Established in 1976 by the KCGF Act
- Capital fund of USD 3 billion
- Outstanding credit guarantee over USD 32.1 billion (2004)
- 84 branch offices and 2,200 employees
Source of funding

- Contribution from Government
  : Subject to yearly budget
- Contribution from Financial Institutions
  : 0.2% of designated type of loans
- Guarantee fee, Interest, etc.

- Contribution from Government
- Contribution from financial institutions
- Guarantee fee, etc.
Leverage Ratio

- The total amount of credit guarantees that KCGF can provide as stipulated by the KCGF Act: 20 times the total amount of the capital funds.
- The leverage ratio as of the end of 2004: 10.5

Leverage ratio = \frac{\text{Outstanding credit guarantee}}{\text{Capital fund}}
Supervising Authorities

The National Assembly

KCGF

Ministry of Planning and Budget

Small and Medium Business Administration

The Board of Audit and Inspection

Ministry of Finance and Economy

Budget Allocation

Budget request

Inspection

Contribution

Supervision

Audit
Services

- Credit Guarantee Services
- Credit Insurance Services
- Infrastructure Credit Guarantee Services
- Management Consulting Service
- Comprehensive Support System for SMEs
### III. Credit Guarantee Services

#### Framework
- Types of credit guarantee
- Operating procedures
- Eligibility
- Consultation & Application
- Credit investigation
- Credit evaluation

#### Issuing letter of credit guarantee
- Coverage ratio
- Credit Guarantee Fee
- Guarantee ceiling
- Collateral & guarantor
- Performance
Framework

Credit guarantee for the repayment of loans extended to the enterprise or transaction liabilities assumed by the enterprise
# Types of Credit Guarantee Services

<table>
<thead>
<tr>
<th>Type</th>
<th>Related Liabilities</th>
</tr>
</thead>
<tbody>
<tr>
<td>Indirect Financing</td>
<td></td>
</tr>
<tr>
<td>Bank loans</td>
<td>Loans, overdraft, etc.</td>
</tr>
<tr>
<td>Payment guarantee of banks</td>
<td>Payment guarantees</td>
</tr>
<tr>
<td>Loans from non-banking</td>
<td>Loans, commercial bill discounts, etc.</td>
</tr>
<tr>
<td>financial institutions</td>
<td></td>
</tr>
<tr>
<td>Leases</td>
<td>Leases</td>
</tr>
<tr>
<td>Acceptance of trade bills</td>
<td>Bills of exchange</td>
</tr>
<tr>
<td>Secured loans</td>
<td>Secured loans</td>
</tr>
<tr>
<td>Direct Financing</td>
<td></td>
</tr>
<tr>
<td>Corporate bonds</td>
<td>Corporate bonds</td>
</tr>
<tr>
<td>Credit Transactions</td>
<td></td>
</tr>
<tr>
<td>Commercial bills</td>
<td>Notes payables, etc.</td>
</tr>
<tr>
<td>Performance</td>
<td>Deposit for bids</td>
</tr>
<tr>
<td>Transaction liabilities</td>
<td>Transaction liabilities</td>
</tr>
<tr>
<td>Tax pay</td>
<td>National tax</td>
</tr>
</tbody>
</table>
Types of Credit Guarantee Services

Special Credit Guarantee : P-CBO / CLO Guarantee
- Guarantees for a pool of corporate bonds / loans
- Combining mechanisms of ABS and credit guarantee
- Facilitated corporate financing in a short period of time

KCGF

Credit guarantee

Bank

Credit line

Enterprise

Originator

SPC

Investor

Bonds

Proceeds

Subordinated CBOs

Senior CBOs

Proceeds

Proceeds

Proceeds
Operating Procedure

1st Step: Preview
2nd Step: Application
3rd Step: Credit Investigation
4th Step: Credit Evaluation
5th Step: Approval & Issuance of Letter of Credit Guarantee
Eligibility

General Principle

- Any individual or legal persons who operate business for profit are eligible for credit guarantee services.

- Though large enterprises (LEs) may apply for credit guarantee services, SMEs receive more favorable treatment.
Eligibility

 Eligible Industry Sector

Positive List System

Negative List System

No Restriction

Consultation & Application

Direct Application

Financial Institution  Loan Application  Enterprise  Guarantee Application  KCGF

Indirect Application

Enterprise  Loan Application  KCGF  Guarantee Agreement  Financial Institution
Application

Required Documents

- Enterprise-related documents
  - Business registration certificate
  - Corporation registration certificate
  - Business plan
  - Financial statements, etc.

- Financial transaction-related documents
  - Transaction statements from banks
  - Tax payment certificate, etc.

- Representative-related documents
  - Resident registration certificate
  - Real estate registration certificate, etc.
Credit Investigation

**Preliminary Document Review**
- Analyze submitted documents
- Understand company’s status and operation
- Check forged documents

**On-site Investigation**
- Product demand
- Technology
- Financial Status
- Internal factors
- Facility
- Personnel
- External factors
- Raw-material supply
- Prospects of Industry

Korea Credit Guarantee Fund
## Credit Evaluation

### Guarantee Amount and Evaluation Item

<table>
<thead>
<tr>
<th>Guarantee Amount</th>
<th>Evaluation Item</th>
</tr>
</thead>
<tbody>
<tr>
<td>Simplified Method</td>
<td>Small sum check list</td>
</tr>
<tr>
<td>KRW 50 mil. or less</td>
<td></td>
</tr>
<tr>
<td>Standard Method</td>
<td>Simplified Criteria</td>
</tr>
<tr>
<td>KRW 50 mil. ~ 300 mil.</td>
<td></td>
</tr>
<tr>
<td>Comprehensive Method</td>
<td>Standard Criteria</td>
</tr>
<tr>
<td>Over KRW 300 mil.</td>
<td></td>
</tr>
</tbody>
</table>

### Guarantee Amount

- **KRW 50 Million**
  - Speedy Method
  - Simplified Method
- **KRW 300 Million**
  - Standard Method

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Korea Credit Guarantee Fund
Issuing Letter of Credit Guarantee

KCGF → Enterprise → Financial Institution

Letter of credit guarantee
Issue
Submit

Electronic credit guarantee certificate
Encrypt
Transmit

KCGF → Financial Institution

Korea Credit Guarantee Fund
Coverage Ratio

- 70% ~ 85% depending on the type of guaranteed liability, financial institution (creditor institution) and credit rating of the borrower.
- For reference, 70% is the most widely used coverage ratio around the world. Below 50% was adopted in a few countries but failed.

<table>
<thead>
<tr>
<th>Types of Guaranteed Liabilities</th>
<th>Contributing Banks</th>
<th>Other Lending Institutions</th>
</tr>
</thead>
<tbody>
<tr>
<td>Newly Issued</td>
<td>Discount of Commercial Bills 80%</td>
<td>70~85%</td>
</tr>
<tr>
<td></td>
<td>Trade Financing 80%</td>
<td></td>
</tr>
<tr>
<td></td>
<td>All other liabilities 85%</td>
<td></td>
</tr>
<tr>
<td>Roll-Over</td>
<td>90%</td>
<td>90%</td>
</tr>
</tbody>
</table>
Credit Guarantee Fee

- 0.5 ~2.0% per annum depending on the credit rating of the enterprise
- Additional 0.5% for large enterprises
- Fixed fee applies to certain types of guarantees

<table>
<thead>
<tr>
<th>Credit rating</th>
<th>AAA</th>
<th>AA~A-</th>
<th>BBB+ ~BBB-</th>
<th>BB+ ~BB</th>
<th>BB- ~B+</th>
<th>B</th>
</tr>
</thead>
<tbody>
<tr>
<td>Fee rate</td>
<td>0.5</td>
<td>0.6</td>
<td>0.8</td>
<td>0.9</td>
<td>1.0</td>
<td>1.1</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>Credit rating</th>
<th>B-</th>
<th>CCC+ ~CCC</th>
<th>CCC-</th>
<th>CC</th>
<th>C</th>
<th>D</th>
</tr>
</thead>
<tbody>
<tr>
<td>Fee rate</td>
<td>1.2</td>
<td>1.3</td>
<td>1.4</td>
<td>1.5</td>
<td>2.0</td>
<td>2.0</td>
</tr>
</tbody>
</table>
Guarantee Ceiling

- Normal ceiling on aggregated credit guarantee amount for a single company:
  - KRW 3 billion (USD3 mil.)

- Maximum aggregated credit guarantee amount for a single company, when designated credit guarantees are extended, which are deemed essential for the national economy:
  - KRW 10 billion (USD10 mil.)
Collateral & Guarantor

Collateral: KCGF does not acquire any collateral when extending credit guarantee. The cases when KCGF take collateral are extremely limited.

Guarantor: KCGF limits personal guarantors to those closely related to the company and have a keen interest in it. KCGF tries to minimize the number of guarantors.
### Performance

The chart shows the performance of the Korea Credit Guarantee Fund over the years 1999 to 2004. The data is represented in million USD.

- **Outstanding guarantee**
- **Guarantee provided**

The graph indicates a steady increase in both outstanding guarantees and guarantees provided from 1999 to 2004.
V. Effects of Credit Guarantee on the National Economy

- Production inducement & added value inducement effect
- Tax revenue inducement & job creation effect
- GDP & credit guarantee growth rate
- The most effective government policy tool for SMEs
- Improving SMEs attitude toward credit
Production Inducement & Added Value Inducement Effect

in million USD

- Production Inducement
- Added Value Inducement

Year | Production Inducement | Added Value Inducement
--- | --- | ---
2001 | 1,478 | 765
2002 | 1,430 | 704
2003 | 1,630 | 832
2004 | 1,924 | 963
Tax Revenue Inducement & Job Creation Effect

- **Tax Revenue Inducement (in million USD):**
  - 2001: 83,005
  - 2002: 80,824
  - 2003: 89,936
  - 2004: 95,392

- **Job Creation (in persons):**
  - 2001: 170
  - 2002: 160
  - 2003: 202
  - 2004: 215
The Most Effective Government Policy Tool for SMEs

- Survey conducted by KIET and KCGF
- Evaluated on a 5 point scale

<table>
<thead>
<tr>
<th></th>
<th></th>
<th></th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td>Credit Guarantee</td>
<td>3.33</td>
<td>4.49</td>
<td>4.08</td>
</tr>
<tr>
<td>Government’s Loan</td>
<td>3.04</td>
<td>4.11</td>
<td>3.74</td>
</tr>
<tr>
<td>Tax Reduction &amp; Exemption</td>
<td>2.93</td>
<td>2.90</td>
<td>3.22</td>
</tr>
<tr>
<td>Consulting</td>
<td>2.82</td>
<td>1.80</td>
<td>2.96</td>
</tr>
<tr>
<td>Information Assistance</td>
<td>2.83</td>
<td>1.77</td>
<td>3.18</td>
</tr>
</tbody>
</table>
Improving SME’s Attitude toward Credit

- Enhancing transparency in management
- Recognizing the importance of credit

Agree 90%
Positive effect on management

Agree 95%
Improved understanding on credit

Agree 86%
Cut illegal tax reports
VI. Plans for Further Development of the System

- A Different View on Guarantee
- Adverse Effects of Credit Guarantee
- Action Plans for Renovation of the Credit Guarantee System
A Different View on Credit Guarantee

“The evolution of the government's ratings will be determined by developments in the DPRK and by the success of the government in reducing distortions in its own economy arising from labor inflexibility as well as government activity in allocating credit and guarantees.”

Takahira Ogawa, Director, Standard & Poors
Adverse Effects of Credit Guarantee

- Excessive Guarantee Provision
- Guarantee for Marginal Companies
- Increase in Losses on Guarantee Operations
- Impeding Development of Financial Industry
- Impeding Restructuring of SMEs
- Increasing Burdens on Government Budget
Action Plans for Renovation of Credit Guarantee

- Adoption of Market-friendly Credit Guarantee
  1. Promote effectiveness of guarantee
  2. Enhancing the roles of Private Financial Institutions
  3. Proper Allocation of burdens of Credit Guarantee
Reduction in Credit Guarantee Provision

- Target Annual Reduction of Guarantee
  - 1,000 billions KRW (U$ 1 billion)

Guarantee outstanding
(in billion U$)

Values: 31, 30, 29, 28, 27, 26
Selective and Focused Support

Efficient Utilization of Guarantee Resources

- Large-amount Users
- Long-term Users
- Discourage from using Guarantees
- Penalty

* Plans for Increasing Portion of Innovative SMEs

<table>
<thead>
<tr>
<th>Year</th>
<th>2005</th>
<th>2006</th>
<th>2007</th>
<th>2008</th>
<th>2009</th>
</tr>
</thead>
<tbody>
<tr>
<td>Innovative SMEs</td>
<td>34.0%</td>
<td>38.0%</td>
<td>42.0%</td>
<td>46.0%</td>
<td>50.0%</td>
</tr>
<tr>
<td>Innovative Start-ups</td>
<td>1.3%</td>
<td>3.5%</td>
<td>5.8%</td>
<td>7.2%</td>
<td>10.0%</td>
</tr>
</tbody>
</table>
### Enhancing the Roles of Private Financial Institutions

- **Decrease Average Coverage Ratio**
  - 2005: 85%
  - 2007: 80%

- **Expand Coverage Ratio Differentiation**
  - 2005: 70%-100%
  - 2007: 50%-100%
## Allocating the Burdens of Guarantee Operations among Beneficiaries

<table>
<thead>
<tr>
<th></th>
<th>SMEs</th>
<th>Financial Institutions</th>
<th>Government</th>
</tr>
</thead>
<tbody>
<tr>
<td>Present</td>
<td>20%</td>
<td>30%</td>
<td>50%</td>
</tr>
<tr>
<td>After Renovation</td>
<td>30%</td>
<td>40%</td>
<td>30%</td>
</tr>
</tbody>
</table>
## Allocating the Burdens of Guarantee Operations among Beneficiaries

### Plans for Increasing Average Guarantee Fees

<table>
<thead>
<tr>
<th>Year</th>
<th>2004</th>
<th>2005</th>
<th>2006</th>
<th>2007</th>
</tr>
</thead>
<tbody>
<tr>
<td>Guarantee Fee Ratio (Average)</td>
<td>1.07%</td>
<td>1.12%</td>
<td>1.23%</td>
<td>1.51%</td>
</tr>
</tbody>
</table>
Allocating the Burdens of Guarantee Operations among Beneficiaries

Raising Financial Institutions’ Contribution

2005: 0.3%
2006: 0.4%
VII. Conclusion

A Lesson from A Golf Teacher

“When I ask you to take an aspirin, Please don’t take the whole bottle.”

Havey Penick
Little Red Book, 1992
Thank you

Korea Credit Guarantee Fund

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