

Media Release:

Ratings Affirmed On Shin Kong FHC And Key Group Units; Outlook Negative On Earning Volatilities

May 27, 2021

Overview

- Taiwan-based Shin Kong Life's earnings volatility remains high and continues to weigh on its overall financial risk profile.
- We view Shin Kong Life as the flagship company of the Shin Kong FHC group, and any changes in the insurer's credit profile will affect the overall group credit profile.
- We affirmed our issuer credit ratings on Shin Kong Life, Taiwan Shin Kong Commercial Bank (SKB), and Shin Kong FHC. At the same time, we affirmed our issue credit ratings on the companies' outstanding rated debts.
- The outlook on the long-term ratings remains negative to reflect the difficulties Shin Kong Life faces to maintain its financial strength over the next one to two years, given the insurer's earnings volatility and thin buffer in its funding structure and capitalization.

Rating Action

Taiwan Ratings Corp. today affirmed its ratings on Taiwan-domiciled **Shin Kong Life Insurance Co. Ltd.**, **Shin Kong Financial Holding Co. Ltd.** (Shin Kong FHC), and **Taiwan Shin Kong Commercial Bank Co. Ltd.** (SKB). The outlook on the long-term ratings remains negative. At the same time, we affirmed our issue credit ratings on their respective debt issues (see ratings list).

Rationale

Shin Kong Life's financial buffer narrowed in 2020 due to above-average volatility of the insurer's accounting earnings, despite improvement in its technical business value. The insurer's pretax profits dropped in 2020 to its lowest level since 2017 due to a rise in foreign exchange (forex) costs, lower investment yield, as well as less favorable investment performance. This declining performance was partly the result of the insurer's lower capacity to make overseas investments following a local regulatory order in September 2020. On the one hand, we believe that Shin Kong Life's earnings volatility has reduced its financial buffer, of which we view EBIDTA is an important reference point. On the other hand, we recognize the insurer has steadily improved its contract service margin to sustain the long-term value of its

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business. Shin Kong Life has achieved this through consistent product strategies despite a decline in total premiums as the result of the local regulator's product reforms.

Forex risk exposure contributes to potential volatility in Shin Kong Life's capital and earnings.

Continuous forex volatility creates the additional capital volatility for the insurer that could weigh on its overall financial risk profile. While Shin Kong Life has taken on a proactive hedging strategy, we believe it will take time for the insurer to reduce its forex risk to a sustainable level by achieving stable investment performance for its overseas investments.

We see the insurer's proactive capital management and slower growth plans as key factors underpinning its capital and earnings. Shin Kong Life's capital adequacy improved slightly in 2020 on the success of several capital plans. These included capital injections totaling new Taiwan dollar (NT\$) 13.3 billion and the adoption of fair value accounting on the insurer's real estate investments, which helped to boost reported shareholders' equity. Nonetheless, we estimate Shin Kong Life will have only a thin capital buffer for the next one to two years. This reflects likely balance sheet volatility amid potential market volatility and slow capital generation over the period.

Nonetheless, we anticipate Shin Kong Life will sustain its strong competitive position through its well-established brand and satisfactory market share in major products in the domestic market. The good sales contribution from Shin Kong Life's agent force supports this view.

We view Shin Kong Life as the flagship company of the Shin Kong FHC group. Therefore, the risks for the insurer to maintain its financial strength will also affect the overall group credit profile. This will also ultimately affect our ratings on Taiwan Shin Kong Commercial Bank, which we assess as a core group member.

Outlook

Shin Kong Financial Holding Co. Ltd., Shin Kong Life Insurance Co. Ltd., and Taiwan Shin Kong Commercial Bank Co. Ltd.

The negative outlook reflects the potential earnings volatility associated with Shin Kong Life's investments that could negatively affect the insurer's overall financial strength. That's given our view of the thin buffer in Shin Kong Life's funding structure, above-average forex volatility, and thin capital buffer over the next one to two years.

The outlook also reflects the increasing challenges for Shin Kong Life to maintain a stable credit profile over the next one to two years. Nonetheless, we expect Shin Kong FHC group to maintain its competitive position in Taiwan's financial services industry, particularly the life insurance sector. The ratings on Shin Kong Life will move in tandem with the group's consolidated credit profile, as will the ratings on the key group units.

Downward scenario

We may lower the long-term ratings on Shin Kong FHC, Shin Kong Life, and Taiwan Shin Kong Commercial Bank if the group credit profile deteriorates significantly from our base-case assumptions over the next one to two years. This could result from: (1) significant weakening in risk management at the group level and at Shin Kong Life than we previously expected, particularly in terms of forex risk exposure or investment-risk concentration; or (2) Shin Kong Life's funding structure or risk-adjusted capitalization weakens due to poor earnings, slower value of in-force growth, or unexpected market volatility. Either of the above factors could

negatively affect our assessment of Shin Kong Life's financial risk profile or lead us toward the selection of a lower anchor.

Upward scenario

We may revise the rating outlook on Shin Kong FHC, Shin Kong Life, and Taiwan Shin Kong Commercial Bank back to be stable if Shin Kong Life demonstrates persistent control over its forex risk while maintaining stable capitalization. This would have to be accompanied by the insurer's stable investment allocation, strong competitive position compared with its domestic peers, and stable credit profiles for the other core entity.

Rating Score Snapshot

For Shin Kong Life Insurance Co. Ltd.

Business Risk Profile	Satisfactory
Competitive position	Strong
IICRA	Moderately high
Financial Risk Profile	Fair
Capital and earnings	Fair
Risk exposure	Moderately low
Funding structure	Neutral
Modifiers	
Governance	Neutral
Liquidity	Adequate
Financial Strength Rating	twAA-

Related Criteria & Research

Related Criteria

- Criteria | Financial Institutions | Banks: Banking Industry Country Risk Assessment Methodology And Assumptions, Nov 09 2011
- Criteria | Financial Institutions | Banks: Banks: Rating Methodology And Assumptions, Nov 09 2011
- Criteria | Financial Institutions | Banks: Quantitative Metrics For Rating Banks Globally: Methodology And Assumptions, Jul 17 2013
- Criteria | Financial Institutions | General: Risk-Adjusted Capital Framework Methodology, Jul 20 2017
- Criteria | Insurance | General: Insurers Rating Methodology - July 01, 2019
- Criteria | Insurance | General: Refined Methodology And Assumptions For Analyzing Insurer Capital Adequacy Using The Risk-Based Insurance Capital Model - June 07, 2010
- General Criteria: Group Rating Methodology - July 01, 2019
- General Criteria: Hybrid Capital: Methodology And Assumptions, Jul 01 2019
- General Criteria: Methodology For Linking Long-Term And Short-Term Ratings - April 07, 2017
- General Criteria: Methodology For National And Regional Scale Credit Ratings - June 25, 2018
- General Criteria: Principles Of Credit Ratings - February 16, 2011
- TRC Financial Services Issue Credit Rating Criteria, July 31, 2019

Related Research

- Taiwan Ratings' Ratings Definitions – August 10, 2020

(Unless otherwise stated, these articles are published on www.taiwanratings.com)

Ratings List

Ratings Affirmed; Outlook

Shin Kong Life Insurance Co. Ltd.

Issuer Credit Rating	twAA-/Negative/--
Financial Strength Rating	twAA-/Negative/--
Perpetual Accumulative Subordinated Corporate Bond	twA+

Shin Kong Financial Holding Co. Ltd.

Issuer Credit Rating	twA+/Negative/twA-1
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Taiwan Shin Kong Commercial Bank Co. Ltd.

Issuer Credit Rating	twAA-/Negative/twA-1+
Unsecured Subordinated Debenture	twA+
Unsecured Subordinated Debenture	twA

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