

KB Financial Group

FSS discloses dispute resolution guidelines on ELS

Reiterate Rating: BUY | PO: 90,000 KRW | Price: 70,700 KRW

The FSS discloses criteria for compensation

On 11 March 2024, the FSS disclosed a dispute resolution guideline for sellers of ELS linked to the Hang Seng China Enterprises Index (HSCEI), with client losses reaching 54%. The FSS mentioned that the sellers of the ELS products did not fully adhere to the Financial Consumer Protection Act enacted in March 2021, and sees that the sellers should be liable for part of the client losses. It also commented that the dispute resolution guideline considers the responsibilities of both the seller and the individual investor and hopes the guideline provides a quick, rational resolution.

Higher compensation for more boxes ticked

The compensation guideline can be voluntarily applied by each financial company in determining the compensation for customer losses. The compensation rate comprises two main factors – the responsibilities of the seller and the individual investor. For banks, the base compensation rate for losses was set at 20-30%, with an additional 5-10% based on the channels used for selling the product. For individual investors, the rate could go up additionally by a maximum of 45% if elderly or first-time buyers, and it could decline by a maximum of 45%, as well, if the investor is an experienced, large-sized investor in ELS and has made significant profits on the product in the past.

W700bn loss potential for KB

Since the FSS announcement today was a dispute resolution guideline, it could take months for agreements to be made between KB and the individual investors. However, given that this issue has been dragging on since October 2023, we believe KB would want to seal the deal swiftly. We expect KB to recognize the impact of compensations on its P&L in 1Q24 after coming up with a conservative loss estimate. The *Korea Economic Daily* has reported that KB could recognize a W700bn loss in 1H24, which would be 10% of Bloomberg consensus pre-tax earnings for 2024. This is at the upper end of the range we had provided in our previous [report](#). Since the issue has been widely reported for months, we believe consensus should reflect some of the loss potential from ELS – we already consider the losses in our estimates for 2024.

Time to move on; reiterate our Buy rating

We do not like such big costs, but at the same time, these costs had been widely expected, and we believe this is largely in the price, as the FSS announcement was made during market hours and KB's share price ended down only 0.28% on the day. There are some outstanding issues, such as potential fines and additional operational risks on risk-weighted assets. Still, we believe these would be minor compared with the possible compensation for customer losses. We believe ELS was a large negative issue for KB in 2024, and we believe we are passing through the peak of negative news. We reiterate our Buy rating on KB.

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Refer to important disclosures on page 4 to 7. Analyst Certification on page 2. Price Objective Basis/Risk on page 2.

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Equity

Jeehoon Park >>
Research Analyst
Merrill Lynch (Seoul)
+82 2 3707 0532
jeehoon.park@bofa.com

Jisun Lee >>
Research Analyst
Merrill Lynch (Seoul)
+82 2 3707 0418
jisun.lee@bofa.com

Stock Data

Price (Common / ADR)	70,700 KRW / 53.08 USD
Price Objective	90,000 KRW / 69.23 USD
Date Established	8-Mar-2024 / 8-Mar-2024
Investment Opinion	B-1-7 / B-1-7
52-Week Range	46,150 KRW-72,900 KRW
Market Value (mn)	21,615 USD
Market Value (mn)	28,528,233 KRW
Shares Outstanding (mn)	403.5 / 403.5
Average Daily Value (mn)	141.54 USD
Free Float	75.4%
BofA Ticker / Exchange	XKBGF / KSC
BofA Ticker / Exchange	KB / NYS
Bloomberg / Reuters	105560 KS / 105560.KS
ROE (2024E)	8.6%

BofA Global Research Reports

Title: Subtitle	Primary Author	Date Published
Banks - Korea: Raise POs further; see banks as the key beneficiary of the Value-up program	Jeehoon Park	08 March 2024
Banks - Korea: Export recovery a positive signal for banks; upgrade Shinhan, Hana, Woori to Buy	Jeehoon Park	17 January 2024
KB Financial Group: Not too alarmed about potential customer losses on ELS	Jeehoon Park	28 November 2023

Acronyms

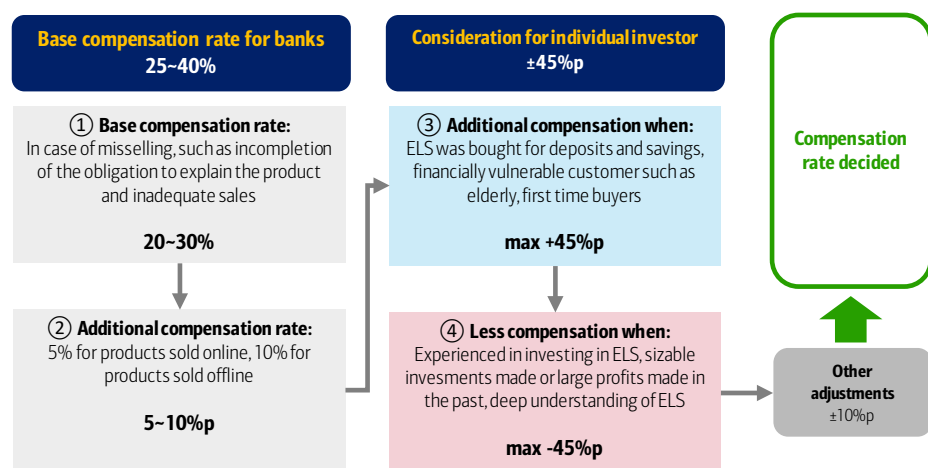
ELS: Equity Linked Security

FSS: Financial Supervisory Service

Passing through the peak of negatives

Exhibit 1: The compensation guideline announced by the FSS

The compensation rate comprises two factors - responsibilities of the seller and individual investors



Source: BofA Global Research, FSS

BofA GLOBAL RESEARCH

Price objective basis & risk

KB Financial Group (XKBGF / KB)

We derive our price objective of W90,000 (\$69.23) using a target P/B multiple of 0.58x derived by the Gordon Growth Model. Our assumptions are 9.3% sustainable RoE (from 24-month average return on equity-RoE), 10% cost of equity, and 2% terminal growth. We then apply a ca. 28% discount to the sustainable RoE assumption, derived by regression analysis of historical RoE discount assuming the same cost of equity and terminal growth, combined with our view of the economic cycle.

Upside risks to our price objective are (1) higher interest rates leading to further expansion of NIM, (2) stronger revenues from non-bank affiliates and (3) regulators becoming supportive of bigger shareholder returns.

Downside risks are (1) economic slowdown leading to higher credit cost (2) lower revenues from non-bank affiliates due to increased market risk, (3) economic slowdown resulting in lower rates and lower NIM, and (4) stronger demands for social contribution due to pressure on economic entities from high inflation.

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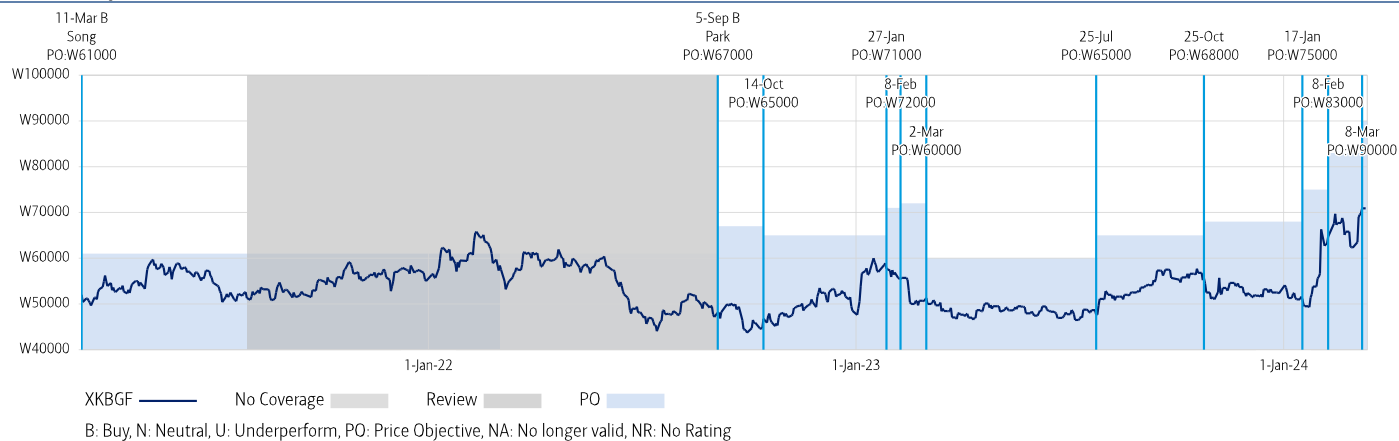
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that exempts the investor's capital gains from Korean tax or (2) the shares sold are sold through the Korea Stock exchange or KOSDAQ exchange and the seller (including related parties) has not owned 25% or more of the shares of the issuer at any time during the year of sale plus the 5 calendar years preceding the year of sale. Investors should seek their own tax advice.

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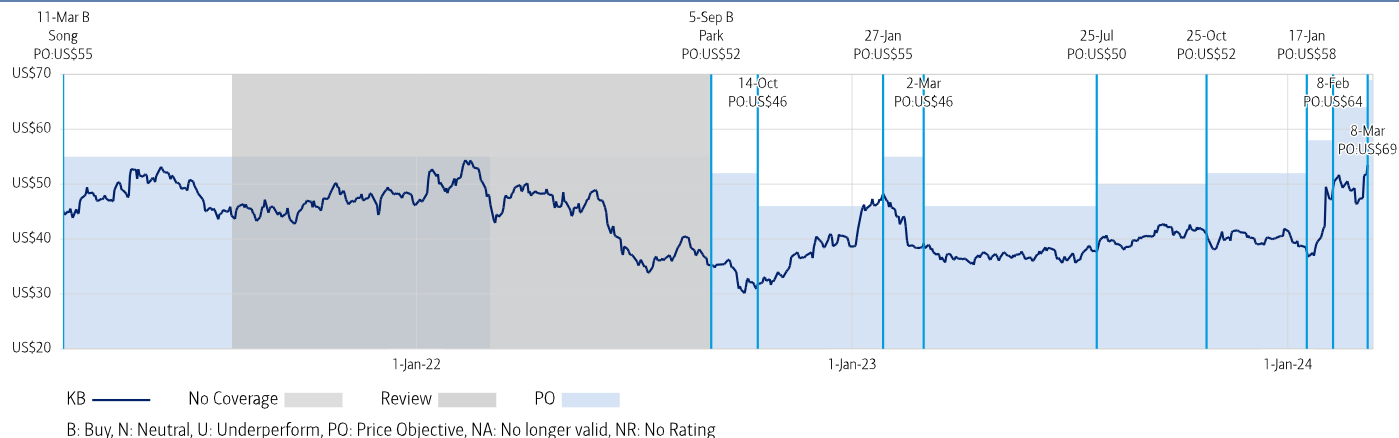
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KB Financial Group (XKBGF) Price Chart



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KB Financial Group (KB) Price Chart



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Equity Investment Rating Distribution: Financial Services Group (as of 31 Dec 2023)

Coverage Universe	Count	Percent	Inv. Banking Relationships ^{R1}	Count	Percent
Buy	156	53.79%	Buy	94	60.26%
Hold	72	24.83%	Hold	48	66.67%
Sell	62	21.38%	Sell	35	56.45%

Equity Investment Rating Distribution: Global Group (as of 31 Dec 2023)

Coverage Universe	Count	Percent	Inv. Banking Relationships ^{R1}	Count	Percent
Buy	1895	53.62%	Buy	1083	57.15%
Hold	832	23.54%	Hold	454	54.57%
Sell	807	22.84%	Sell	383	47.46%

^{R1} Issuers that were investment banking clients of BofA Securities or one of its affiliates within the past 12 months. For purposes of this Investment Rating Distribution, the coverage universe includes only stocks. A stock rated Neutral is included as a Hold, and a stock rated Underperform is included as a Sell.

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