SHINHAN FINANCIAL GROUP CO LTD
Form 20-F
April 30, 2018
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As filed with the Securities and Exchange Commission on April 30, 2018

UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

Form 20-F

(Mark One)

REGISTRATION STATEMENT PURSUANT TO SECTION 12(b) OR 12(g) OF THE SECURITIES EXCHANGE ACT OF 1934

OR

ANNUAL REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934

For the fiscal year ended December 31, 2017

OR

TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934

For the transition period from __________ to __________

OR

SHELL COMPANY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934

Date of event requiring this shell company report

Commission File Number: 001-31798

Shinhan Financial Group Co., Ltd.

(Exact name of registrant as specified in its charter)

N/A	**The Republic of Korea**
(Translation of registrant s name into English)	**(Jurisdiction of incorporation or organization)**

20, Sejong-daero 9-gil, Jung-gu

Seoul 04513, Korea

(Address of principal executive offices)

Yu Sunghun, +822 6360 3071(T), irshy@shinhan.com, +822 6360 3098 (F), 20, Sejong-daero 9-gil, Jung-gu, Seoul 04513, Korea

(Name, Telephone, E-mail and/or Facsimile number and Address of Company Contact Person)

Securities registered or to be registered pursuant to Section 12(b) of the Act:

Title of Each Class:	Name of Each Exchange on Which Registered:
Common stock, par value Won 5,000 per share	**New York Stock Exchange***
American depositary shares	**New York Stock Exchange**

* Not for trading, but only in connection with the listing of American depositary shares on the New York Stock Exchange, pursuant to the requirements of the Securities and Exchange Commission.

Securities registered or to be registered pursuant to Section 12(g) of the Act:

None

Securities for which there is a reporting obligation pursuant to Section 15(d) of the Act:

None

Indicate the number of outstanding shares of each of Shinhan Financial Group s classes of capital or common stock as of the close of the last full fiscal year covered by this Annual Report: 474,199,587 shares of common stock, par value of Won 5,000 per share.

Indicate by check mark if the registrant is a well-known seasoned issuer, as defined in Rule 405 of the Securities Act: Yes No

If this report is an annual or transition report, indicate by check mark if the registrant is not required to file reports pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934: Yes No

Note Checking the box above will not relieve any registrant required to file reports pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934 from their obligations under those Sections.

Indicate by check mark whether the registrant: (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. Yes No

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (§232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). Yes No

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, or an emerging growth company. See the definitions of large accelerated filer, accelerated filer, and emerging growth company in Rule 12b-2 of the Exchange Act.

Large accelerated filer	Accelerated filer
Non-accelerated filer	Emerging growth company

If an emerging growth company that prepares its financial statements in accordance with U.S. GAAP, indicate by check mark if the registrant has elected not to use the extended transition period for complying with any new or revised financial accounting standards provided pursuant to Section 13(a) of the Exchange Act.

The term new or revised financial accounting standard refers to any update issued by the Financial Accounting Standards Board to its Accounting Standards Codification after April 5, 2012.

Indicate by check mark which basis of accounting the registrant has used to prepare the financial statements included in this filing:

U.S. GAAP	International Financial Reporting Standards as issued by the International Accounting Standards Board	Other

If Other has been checked in response to the previous question, indicate by check mark which financial statement item the registrant has elected to follow: Item 17 Item 18

If this is an annual report, indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act): Yes No

(APPLICABLE ONLY TO ISSUERS INVOLVED IN BANKRUPTCY PROCEEDINGS DURING THE PAST FIVE YEARS)

Indicate by check mark whether the registrant has filed all documents and reports required to be filed by Section 12, 13 or 15(d) of the Securities Exchange Act of 1934 subsequent to the distribution of securities under a plan confirmed by a court: Yes No

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CERTAIN DEFINED TERMS, CONVENTIONS AND CURRENCY OF PRESENTATION

Unless otherwise specified or the context otherwise requires:

- the terms we, us, our, Shinhan Financial Group, SFG and the Group mean Shinhan Financial Group and its consolidated subsidiaries; and

- the terms Shinhan Financial Group Co., Ltd., our company and our holding company mean Shinhan Financial Group Co., Ltd.

All references to Korea or the Republic contained in this annual report are to the Republic of Korea. All references to the Government are to the government of the Republic of Korea. References to the Financial Services Commission are to the Financial Services Commission of Korea, and references to the Financial Supervisory Service are to the Financial Supervisory Service of Korea, the executive body of the Financial Services Commission.

The fiscal year for us and our subsidiaries ends on December 31 of each year. Unless otherwise specified or the context otherwise requires, all references to a particular year are to the year ended December 31 of that year.

The currency of the primary economic environment in which we operate is Korean Won.

In this annual report, unless otherwise indicated, all references to Won ~~or~~ W are to the currency of the Republic of Korea, and all references to U.S. Dollars, Dollars, $ or US$ are to the currency of the United States of America. Unless otherwise indicated, all translations from Won to Dollars were made at ₩1,067.4 to US$1.00, which was the noon buying rate in the City of New York on December 29, 2017 for cable transfers according to the H.10 statistical release of the Federal Reserve Board (the Noon Buying Rate). On April 13, 2018, the Noon Buying Rate was ₩1,070.6 to US$1.00. The Noon Buying Rate has been volatile recently and the U.S. Dollar amounts referred to in this report should not be relied upon as an accurate reflection of our results of operations. We expect this volatility to continue in the near future. No representation is made that the Won or U.S. Dollar amounts referred to in this report could have been or could be converted into Dollars or Won, as the case may be, at any particular rate or at all.

Unless otherwise indicated, the financial information presented in this annual report has been prepared on a consolidated basis in accordance with International Financial Reporting Standards (IFRS) as issued by the International Accounting Standards Board (IASB).

Any discrepancies in the tables included herein between totals and sums of the amounts listed are due to rounding.

FORWARD LOOKING STATEMENTS

This annual report includes forward-looking statements, as defined in Section 27A of the U.S. Securities Act, as amended, and Section 21E of the U.S. Securities Exchange Act of 1934, as amended (the Exchange Act), including statements regarding our expectations and projections for future operating performance and business prospects. The words believe, expect, anticipate, estimate, project and similar words used in connection with any discussion of future operating or financial performance identify forward-looking statements. In addition, all statements other than statements of historical facts included in this annual report are forward-looking statements.

Although we believe that the expectations reflected in the forward-looking statements are reasonable, we can give no assurance that such expectations will prove to be correct. All forward-looking statements are management s present expectations of future events and are subject to a number of factors and uncertainties that

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could cause actual results to differ materially from those described in the forward-looking statements. This annual report discloses, under the caption Item 3.D. Risk Factors and elsewhere, important factors that could cause actual results to differ materially from our expectations (Cautionary Statements). Included among the factors discussed under the caption Item 3.D. Risk Factors are the followings risks related to our business, which could cause actual results to differ materially from those described in the forward-looking statements: the risk of adverse impacts from an economic downturn; increased competition; market volatility in securities and derivatives markets, interest or foreign exchange rates or indices; other factors impacting our operational plans; or legislative and/or regulatory developments. We caution you not to place undue reliance on the forward-looking statements, which speak only as of the date of this annual report. All subsequent written and oral forward-looking statements attributable to us or persons acting on our behalf are expressly qualified in their entirety by the Cautionary Statements.

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ITEM 1. *IDENTITY OF DIRECTORS, SENIOR MANAGEMENT AND ADVISERS*

Not applicable.

ITEM 2. *OFFER STATISTICS AND EXPECTED TIMETABLE*

Not applicable.

ITEM 3. *KEY INFORMATION*

ITEM 3.A. Selected Financial Data

The selected consolidated income statement and balance sheet data set forth below for the years ended December 31, 2013, 2014, 2015, 2016 and 2017 have been derived from our consolidated financial statements which have been prepared in accordance with IFRS as issued by the IASB. Our consolidated financial statements as of and for the years ended December 31, 2013, 2014, 2015, 2016 and 2017 have been audited by independent registered public accounting firm KPMG Samjong Accounting Corp.

You should read the following data with the more detailed information contained in Item 5. Operating and Financial Review and Prospects and our consolidated financial statements included in Item 18. Financial Statements. Historical results are not necessarily indicative of future results.

Consolidated Income Statement Data

	Year Ended December 31,					
	2013	**2014**	**2015**	**2016**	**2017**	**2017[1]**
	(In billions of Won and millions of US$, except per common share data)					
Interest income	₩ 12,591	₩ 12,061	₩ 11,130	₩ 11,236	₩ 11,799	$ 11,054
Interest expense	(5,986)	(5,271)	(4,437)	(4,031)	(3,956)	(3,706)
Net interest income	**6,605**	**6,790**	**6,693**	**7,205**	**7,843**	**7,348**
Fees and commission income	3,490	3,561	3,897	3,804	4,045	3,790
Fees and commission expense	(2,103)	(2,091)	(2,276)	(2,238)	(2,334)	(2,187)
Net fees and commission income	**1,387**	**1,469**	**1,621**	**1,566**	**1,711**	**1,603**
Net insurance loss	(383)	(413)	(432)	(419)	(460)	(431)
Dividend income	156	176	308	282	257	241
Net trading income (loss)	75	262	(344)	370	963	902
Net foreign currency transaction gain	296	224	78	462	364	341
Net gain (loss) on financial instruments designated at fair value through profit or loss	(122)	(361)	460	(502)	(1,060)	(993)
	701	681	772	648	499	468

Net gain on sale of available-for-sale financial assets						
Impairment losses on financial assets	(1,340)	(1,174)	(1,264)	(1,196)	(1,015)	(951)
General and administrative expenses	(4,203)	(4,463)	(4,475)	(4,509)	(4,811)	(4,507)
Net other operating expenses	(540)	(536)	(444)	(798)	(462)	(434)
Operating income	**2,632**	**2,655**	**2,973**	**3,109**	**3,829**	**3,587**
Equity method income	7	31	21	10	20	19
Other non-operating income (loss), net	37	182	147	52	(53)	(49)
Profit before income taxes	**2,676**	**2,868**	**3,141**	**3,171**	**3,796**	**3,557**
Income tax expense	(621)	(668)	(695)	(346)	(848)	(795)
Profit for the year	**₩ 2,055**	**₩ 2,200**	**₩ 2,446**	**₩ 2,825**	**₩ 2,948**	**$ 2,762**

	Year Ended December 31,					
	2013	2014	2015	2016	2017	2017[1]
	(In billions of Won and millions of US$, except per common share data)					
Other comprehensive income (loss) for the year, net of income tax						
Items that are or may be reclassified to profit or loss:						
Foreign currency translation adjustments for foreign operations	₩ (58)	₩ (13)	₩ (6)	₩ 12	₩ (194)	$ (182)
Net change in unrealized fair value of available-for-sale financial assets	(269)	136	(266)	(434)	(323)	(303)
Equity in other comprehensive income (loss) of associates	(5)	6	12	3	(23)	(21)
Net change in unrealized fair value of cash flow hedges	6	(16)	3	(1)	16	15
Other comprehensive income (loss) of separate account	(2)	6	2	(4)	(9)	(9)
	(328)	119	(255)	(424)	(533)	(500)
Items that will never be reclassified to profit or loss:						
Remeasurements of defined benefit liability	19	(154)	(82)	15	103	97
Equity in other comprehensive income (loss) of associates					1	1
	19	(154)	(82)	15	104	98
Total other comprehensive loss, net of income tax	(309)	(36)	(337)	(409)	(429)	(402)
Total comprehensive income for the year	**₩ 1,746**	**₩ 2,164**	**₩ 2,109**	**₩ 2,416**	**₩ 2,519**	**$ 2,360**
Net income attributable to:						
Equity holders of the Group	₩ 1,898	₩ 2,081	₩ 2,367	₩ 2,775	₩ 2,918	$ 2,733
Non-controlling interest	157	119	79	50	30	29
Total comprehensive income attributable to:						
Equity holders of the Group	1,591	2,046	2,034	2,367	2,490	2,333
Non-controlling interest	155	118	75	49	29	27
Earnings per share:						
Basic earnings per share in Won and US$[2]	3,810	4,195	4,789	5,736	6,116	5.73
Dilutive earnings per share in Won and US$[3]	3,810	4,195	4,789	5,736	6,116	5.73

Notes:

(1) Won amounts are expressed in U.S. Dollar at the rate of ₩1,067.4 to US$1.00, the Noon Buying Rate in effect on December 29, 2017 for the convenience of readers. No representation is made that the Won or U.S. Dollar amounts referred to above could have been or could be converted into U.S. Dollars or Won, as the case may be, at any particular rate or at all.

(2) Basic earnings per share are calculated by dividing net income available to holders of our common shares by the weighted average number of common shares issued and outstanding for the relevant period.

(3) Dilutive earnings per share are calculated in a manner consistent with basic earnings per share, while giving effect to the potential dilution that could occur if convertible securities, options or other contracts to issue common shares were converted into or exercised for common shares. Common shares issuable upon conversion of redeemable convertible preferred shares are potentially dilutive.

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Consolidated Balance Sheet Data

	2013	2014	2015	2016	2017	2017[1]
	(In billions of Won and millions of US$, except per common share data)					
Assets						
Cash and due from banks	₩ 16,473	₩ 20,585	₩ 22,024	₩ 19,181	₩ 22,669	$ 21,237
Trading assets	18,033	24,362	22,638	26,696	28,464	26,667
Financial assets designated at fair value through profit or loss	3,361	2,737	3,244	3,416	3,579	3,353
Derivative assets	1,717	1,568	1,995	3,003	3,400	3,185
Loans, net	205,723	221,618	246,441	259,011	275,566	258,165
Available-for-sale financial assets	33,597	31,418	33,966	37,663	42,117	39,458
Held-to-maturity financial assets	11,031	13,373	16,192	19,805	24,991	23,413
Property and equipment, net	3,214	3,147	3,055	3,146	3,022	2,831
Intangible assets, net	4,226	4,153	4,266	4,227	4,272	4,002
Investments in associates	329	342	393	354	631	591
Current tax receivable	6	11	10	13	25	23
Deferred tax assets	196	228	164	641	592	555
Investment properties, net	690	268	209	353	418	392
Other assets, net	12,451	14,203	15,947	18,167	16,552	15,508
Assets held for sale	243	9	4	4	8	7
Total assets	**₩ 311,290**	**₩ 338,022**	**₩ 370,548**	**₩ 395,680**	**₩ 426,306**	**$ 399,387**
Liabilities						
Deposits	₩ 178,810	₩ 193,710	₩ 217,676	₩ 235,138	₩ 249,419	$ 233,670
Trading liabilities	1,258	2,689	2,135	1,977	1,848	1,732
Financial liabilities designated at fair value through profit or loss	5,909	8,996	8,916	9,234	8,298	7,774
Derivative liabilities	2,019	1,718	2,599	3,528	3,488	3,267
Borrowings	20,143	22,974	21,734	25,294	27,587	25,845
Debt securities issued	37,491	37,335	41,221	44,327	51,341	48,099
Liability for defined benefit obligations	118	309	226	131	7	7
Provisions	750	694	699	729	429	402
Current tax payable	239	257	142	273	349	327
Deferred tax liabilities	15	10	16	11	10	9
Liabilities under insurance contracts	15,662	17,776	20,058	22,377	24,515	22,967
Other liabilities	19,021	21,040	23,313	20,916	25,312	23,714
Total liabilities	**₩ 281,435**	**₩ 307,507**	**₩ 338,735**	**₩ 363,935**	**₩ 392,603**	**$ 367,813**

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	2013	2014	2015	2016	2017	2017[1]
	(In billions of Won and millions of US$, except per common share data)					
Equity						
Capital stock	₩ 2,645	₩ 2,645	₩ 2,645	₩ 2,645	₩ 2,645	$ 2,478
Hybrid bond	537	537	737	498	424	397
Capital surplus	9,887	9,887	9,887	9,887	9,887	9,263
Capital adjustments	(393)	(393)	(424)	(458)	(398)	(373)
Accumulated other comprehensive income	673	638	305	(102)	(530)	(496)
Retained earnings	14,189	15,869	17,690	18,640	20,791	19,478
Total equity attributable to equity holders of the Group	27,538	29,184	30,840	31,110	32,819	30,747
Non-controlling interest	2,317	1,331	973	635	884	827
Total equity	**₩ 29,855**	**₩ 30,515**	**₩ 31,813**	**₩ 31,745**	**₩ 33,703**	**$ 31,574**
Total liabilities and equity	**₩ 311,290**	**₩ 338,022**	**₩ 370,548**	**₩ 395,680**	**₩ 426,306**	**$ 399,387**

Note:

(1) Won amounts are expressed in U.S. Dollar at the rate of ₩1,067.4 to US$1.00, the Noon Buying Rate in effect on December 29, 2017 for the convenience of readers. No representation is made that the Won or U.S. Dollar amounts referred to above could have been or could be converted into U.S. Dollars or Won, as the case may be, at any particular rate or at all.

Dividends

	Year Ended December 31,				
	2013	2014	2015	2016	2017
	(In Won and US$)				
Cash dividends per share of common stock:					
In Korean Won	₩ 650	₩ 950	₩ 1,200	₩ 1,450	₩ 1,450
In U.S. Dollars[1]	$ 0.62	$ 0.87	$ 1.03	$ 1.20	$ 1.36
Cash dividends per share of preferred stock:					
In Korean Won	₩ 5,580	₩ 5,580	₩ 5,580	₩ N/A	₩ N/A
In U.S. Dollars[1]	$ 5.29	$ 5.12	$ 4.77	$ N/A	$ N/A

Note:

(1) Won amounts for 2013, 2014, 2015, 2016 and 2017 are expressed in U.S. Dollar at the rate of ₩1,055.3, ₩1,090.9, ₩1,169.3, ₩1,203.7 and ₩1,067.4, respectively, to US$1.00, the Noon Buying Rate in effect on December 31, 2013, 2014, 2015, 2016 and 2017, respectively, for the convenience of readers. No representation is made that the Won or U.S. Dollar amounts referred to above could have been or could be converted into U.S. Dollars or Won, as the case may be, at any particular rate or at all.

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Selected Statistical Information

Profitability Ratios and Other Data

	Year Ended December 31,				
	2013	2014	2015	2016	2017
	(Percentages)				
Net income attributable to the Group as a percentage of:					
Average total assets[1]	0.66%	0.68%	0.69%	0.73%	0.72%
Average total Group stockholders equity[1]	7.03	7.25	7.87	8.97	8.94
Dividend payout ratio[2]	19.47	24.66	27.21	25.62	23.92
Net interest spread[3]	1.95	1.93	1.78	1.83	1.94
Net interest margin[4]	2.36	2.31	2.08	2.06	2.13
Efficiency ratio[5]	88.25	87.31	88.15	88.73	89.04
Cost-to-income ratio[6]	52.41	55.32	52.74	51.34	52.39
Cost-to-average assets ratio[1][7]	6.48	6.09	6.56	6.45	7.48
Equity to average asset ratio[1][8]	9.43	9.36	8.72	8.14	8.00

Notes:

(1) Average total assets (including average interest-earning assets), liabilities (including average interest-bearing liabilities) and stockholder s equity are based on (a) daily balances for Shinhan Bank and (b) quarterly balances for other subsidiaries.

(2) Represents the ratio of total dividends declared on common and preferred stock and hybrid bonds as a percentage of net income attributable to the Group.

(3) Represents the difference between the yield on average interest-earning assets and the cost of average interest-bearing liabilities.

(4) Represents the ratio of net interest income to average interest-earning assets.

(5) Represents the ratio of non-interest expense to the sum of net interest income and non-interest income. Efficiency ratio is used as a measure of efficiency for banks and financial institutions. Efficiency ratio may be reconciled to comparable line items in our income statements for the periods indicated as follows:

	Year Ended December 31,				
	2013	2014	2015	2016	2017
	(In billions of Won, except percentages)				
Non-interest expense (A)	₩ 20,100	₩ 19,733	₩ 23,368	₩ 24,957	₩ 30,831
Divided by					
The sum of net interest income and non-interest income (B)	22,776	22,601	26,509	28,127	34,627
Net interest income	6,605	6,790	6,693	7,205	7,843

Non-interest income	16,171	15,811	19,816	20,922	26,784
Efficiency ratio ((A) as a percentage of (B))	88.25%	87.31%	88.15%	88.73%	89.04%

(6) Represents the ratio of general and administrative expenses to the sum of net interest income, net fee and commission income, net gain on financial assets and liabilities at fair value through profit or loss and net other operating income.

(7) Represents the ratio of non-interest expense to average total assets.

(8) Represents the ratio of average stockholders equity to average total assets.

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Asset Quality Ratios

	As of December 31,				
	2013	2014	2015	2016	2017
	(In billions of Won, except percentages)				
Total gross loans	₩ 207,987	₩ 223,879	₩ 248,429	₩ 261,004	₩ 277,489
Total allowance for loan losses	₩ 2,476	₩ 2,501	₩ 2,318	₩ 2,361	₩ 2,311
Allowance for loan losses as a percentage of total loans	1.19%	1.12%	0.93%	0.90%	0.83%
Impaired loans[(1)]	₩ 2,386	₩ 2,127	₩ 1,902	₩ 1,804	₩ 1,793
Impaired loans as a percentage of total loans	1.15%	0.95%	0.77%	0.69%	0.65%
Allowance as a percentage of impaired loans	103.77%	117.58%	121.87%	130.88%	128.89%
Total non-performing loans[(2)]	₩ 1,197	₩ 1,286	₩ 1,333	₩ 1,174	₩ 1,075
Non-performing loans as a percentage of total loans	0.58%	0.57%	0.54%	0.45%	0.39%
Allowance as a percentage of total assets	0.80%	0.74%	0.63%	0.60%	0.54%

Notes:

(1) Impaired loans include (i) loans for which the borrower has defaulted under Basel standards applicable during the relevant period and (ii) loans that qualify as troubled debt restructurings applicable during the relevant period.

(2) Non-performing loans are defined as loans, whether corporate or retail, that are past due more than 90 days.

Capital Ratios

	As of December 31,				
	2013	2014	2015	2016	2017
	(Percentages)				
Group BIS ratio[(1)]	13.43%	13.05%	13.39%	15.00%	14.78%
Total capital adequacy ratio of Shinhan Bank	16.29	15.43	14.75	15.70	15.59
Adjusted equity capital ratio of Shinhan Card[(2)]	30.41	29.69	28.88	26.23	24.52
Solvency ratio for Shinhan Life Insurance[(3)]	253.06	230.69	204.19	178.28	175.41

Notes:

(1)

Under the guidelines of the Financial Services Commission applicable to financial holding companies, the minimum requisite capital ratio applicable to us is the Bank for International Settlement (BIS) ratio of 8%. This computation is based on our consolidated financial statements in accordance with IFRS. See Item 4.B. Business Overview Supervision and Regulation Principal Regulations Applicable to Financial Holding Companies Capital Adequacy.

(2) Represents the ratio of total adjusted shareholders equity to total adjusted assets and is computed in accordance with the guidelines issued by the Financial Services Commission for credit card companies. Under these guidelines, a credit card company is required to maintain a minimum adjusted equity capital ratio of 8%. This computation is based on the consolidated financial statements of the credit card company prepared in accordance with IFRS. See Item 4.B. Business Overview Supervision and Regulation Principal Regulations Applicable to Credit Card Companies Capital Adequacy.

(3) Solvency ratio is the ratio of the solvency margin to the standard amount of solvency margin as defined and computed in accordance with the guidelines issued by the Financial Services Commission for life insurance companies. Under these guidelines, Shinhan Life Insurance is required to maintain a minimum solvency ratio of 100%. See Item 4.B. Business Overview Supervision and Regulation Principal Regulations Applicable to Insurance Companies Capital Adequacy.

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The Financial Services Commission regulations require that capital ratios be computed based on our consolidated financial statements under IFRS and regulatory guidelines. The following table sets forth our capital ratios computed on the basis of our consolidated financial statements under IFRS and the regulatory guidelines of the Financial Services Commission.

	As of December 31,		
	2015	2016	2017
	(In millions of Won, except percentages)		
Risk-weighted assets	₩ 203,274,542	₩ 198,642,643	₩ 207,768,636
Total risk-adjusted capital	₩ 27,216,448	₩ 29,786,515	₩ 30,713,464
Tier I capital	₩ 23,194,191	₩ 26,210,420	₩ 27,672,892
Tier I common equity capital	₩ 21,882,816	₩ 25,325,054	₩ 26,756,509
Capital adequacy ratio (%)	13.39%	15.00%	14.78%
Tier I capital adequacy ratio (%)	11.41%	13.19%	13.32%
Common equity capital adequacy ratio (%)	10.77%	12.75%	12.88%

Exchange Rates

The following table sets forth, for the periods and dates indicated, certain information concerning the Noon Buying Rate in Won per US$1.00.

Year Ended December 31,	At End of Period	Average[(1)]	High	Low
	(Won per US$1.00)			
2013	1,055.3	1,094.6	1,161.3	1,050.1
2014	1,090.9	1,054.0	1,117.7	1,008.9
2015	1,169.3	1,133.7	1,196.4	1,063.0
2016	1,203.7	1,160.5	1,242.6	1,090.3
2017	1,067.4	1,141.6	1,207.2	1,067.4
October	1,115.7	1,130.9	1,146.5	1,115.7
November	1,084.8	1,099.8	1,120.0	1,079.3
December	1,067.4	1,082.9	1,094.6	1,067.4
2018 (through April 13)	1,070.6	1,070.1	1,093.0	1,054.6
January	1,068.3	1,065.6	1,073.6	1,057.6
February	1,082.1	1,078.5	1,093.0	1,065.3
March	1,061.0	1,069.9	1,081.3	1,060.3
April (through April 13)	1,070.6	1,063.9	1,070.6	1,054.6

Source: Federal Reserve Board

Note:

(1) The average rate for annual and interim periods were calculated by taking the simple average of the Noon Buying Rates on the last day of each month during the relevant period. The average rates for the monthly periods (or portion thereof) were calculated by taking the simple average of the daily Noon Buying Rates during the relevant month (or portion thereof).

We have translated certain amounts in Korean Won, which appear in this annual report, into U.S. Dollars for convenience. This does not mean that the Won amounts referred to could have been, or could be, converted into U.S. Dollars at any particular rate, the rates stated above, or at all. Unless otherwise stated, translations of Won amounts to U.S. Dollars are based on the Noon Buying Rate in effect on December 29, 2017, which was ₩1,067.4 to US$1.00. On April 13, 2018, the Noon Buying Rate in effect was ₩1,070.6 to US$1.00.

ITEM 3.B. Capitalization and Indebtedness

Not applicable.

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ITEM 3.C. Reasons for the Offer and Use of Proceeds
Not applicable.

ITEM 3.D. Risk Factors
An investment in the American depositary shares representing our common shares involves a number of risks. You should carefully consider the following information about the risks we face, together with the other information contained in this annual report, in evaluating us and our business.

Risks Relating to Our Overall Business

Difficult conditions and turbulence in the Korean and global economy and financial markets may adversely affect our business, asset quality, capital adequacy and earnings.

Most of our assets are located in, and we generate most of our income from, Korea. Accordingly, our business and profitability are largely dependent on the general economic and social conditions in Korea, including interest rates, inflation, exports, personal expenditures and consumption, unemployment, demand for business products and services, debt service burden of households and businesses, the general availability of credit, the asset value of real estate and securities and other factors affecting the financial well-being of our corporate and retail customers.

The Korean economy is closely integrated with, and is significantly affected by, developments in the global economy. In light of the ongoing general uncertainty about economic and political conditions in Europe, signs of cooling economy for China and the continuing geopolitical and social instability in various parts of the Middle East, including Iraq, Syria and Yemen, as well as in the former republics of the Soviet Union, including Russia and Ukraine, among others, significant uncertainty remains as to the global economic prospects in general and has adversely affected, and may continue to adversely affect, the Korean economy. In addition, as the Korean economy matures, it is increasingly exposed to the risk of a scissor effect, namely being pursued by competitors in less advanced economies while not having fully caught up with competitors in advanced economies, which risk is amplified by the fact that Korean economy is heavily dependent on exports. The Korean economy also continues to face other difficulties, including sluggishness in domestic consumption and investment, volatility in the real estate market, rising household debt, potential declines in productivity due to aging demographics and low birth rates, and a rise in youth unemployment. Any future deterioration of the global and Korean economies could adversely affect our business, financial condition and results of operations.

In particular, difficulties in financial and economic conditions could result in significant deterioration in the quality of our assets and accumulation of higher provisioning, allowances for loan losses and charge-offs as an increasing number of our corporate and retail customers declare bankruptcy or insolvency or otherwise face increasing difficulties in meeting their debt obligations. For example, in 2011 and 2012, the continuing slump in the real estate market and the shipbuilding industry led to increased delinquency among our corporate borrowers in the construction, real estate leasing, shipbuilding and shipping industries, and in certain cases, even insolvency, workouts, recovery proceedings and/or voluntary arrangements with creditors, as was the case for the current and former member companies of the STX Group, Keangnam Enterprises Co., Ltd., Dongbu Steel Co., Ltd., Sambu Construction Co., Ltd. and Hanjin Heavy Industries & Construction Co., Ltd. During the same period, the sustained slump in the real estate market also led to increased delinquency among our retail borrowers, and in particular, borrowers with collective loans for pre-sale of newly constructed apartment units.

Accordingly, Shinhan Bank s delinquency ratio (based on delinquency of one or more month and net of charge-offs and loan sales) increased from 0.48% as of December 31, 2010 to 0.60% as of December 31, 2011 and 0.61% as of December 31, 2012. However, primarily due to a modest rebound in the housing market and Shinhan Bank s active efforts to reduce its exposure to such troubled industries and other at-risk borrowers through preemptive risk management policies and increased lending to borrowers with high-quality credit profiles as part of Shinhan Bank s strategic initiative to improve its asset quality, Shinhan Bank s delinquency ratio decreased to 0.39% as of December 31, 2013 and 0.31% as of December 31, 2014, remained stable at 0.33% as of December 31, 2015 and further decreased to 0.28% as of December 31, 2016 and 0.23% as of December 31, 2017. There is no assurance, however, that Shinhan Bank will not experience further loan losses from borrowers in the troubled industries since the quality of loans to such borrowers may further deteriorate due to the continued slump in these industries or for other reasons. As for Shinhan Card, its delinquency ratio under the Financial Services Commission guidelines decreased from 2.64% as of December 31, 2012 to 2.15%, 2.18%, 1.69%, 1.68% and 1.49% as of December 31, 2013, 2014, 2015, 2016 and 2017, respectively, largely as a result of its enhanced preemptive risk management and controlled asset growth as well as the sale of large non-performing loans to improve its asset quality.

Moreover, as was the case during the global financial crisis of 2008-2009, depending on the nature of the difficulties in the financial markets and general economy, we may be forced to scale back certain of our core lending activities and other operations and/or borrow money at a higher funding cost or face a tightening in the net interest spread, any of which may have a negative impact on our earnings and profitability. Furthermore, while we and our principal subsidiaries currently maintain a capital adequacy ratio at a level higher than the required regulatory minimum, there is no guarantee that an even higher capital requirement will not be imposed by the Government in case of a renewed economic crisis.

In addition, given the highly integrated nature of financial systems and economic relationships worldwide, there may be other unanticipated systemic or other risks that may not be presently predictable. Any of these risks, if materialized, may have a material adverse effect on our business, liquidity, financial condition and results of operations.

Competition in the Korean financial services industry is intense, and may further intensify.

Competition in the Korean financial services industry is, and is likely to remain, intense, including as a result of the sustained low interest rate environment (which narrows opportunities to make profit based on the spread between lending rates and funding rates), the continuing sluggishness in the general economy, the growing maturation and saturation of the industry as a whole, the entry of new market participants and deregulation, among others.

In the banking sector, Shinhan Bank competes principally with other national commercial banks in Korea, but also faces competition from a number of additional banking institutions, including branches and subsidiaries of foreign banks operating in Korea, regional banks, government-owned development banks and Korea s specialized banks, such as Korea Development Bank, Industrial Bank of Korea and the National Federation of Fisheries Cooperatives, as well as various other types of financial service providers, including savings institutions (such as mutual savings and finance companies, credit unions and credit cooperatives), investment companies (such as securities brokerage firms, merchant banking corporations and asset management companies) and life insurance companies. As of December 31, 2017, Korea had six major nationwide domestic commercial banks (including Citibank Korea Inc. and Standard Chartered Bank Korea Limited, both of which are domestic commercial banks acquired by global financial institutions), six regional commercial banks and branches and subsidiaries of 38 foreign banks. Foreign financial institutions, many of which have greater experiences and resources than we do, may continue to enter the Korean market and compete with us in providing financial products and services either by themselves or in partnership with existing Korean financial institutions.

In the small- and medium-sized enterprise and retail banking segments, which have been Shinhan Bank s traditional core businesses, competition is expected to increase further. In recent years, Korean banks, including Shinhan Bank, have increasingly focused on stable asset growth based on quality credit, such as corporate borrowers with high credit ratings, loans to small office, home office (SOHO) with high levels of collateralization, and mortgage and home equity loans within the limits of the prescribed loan-to-value ratios and debt-to-income ratios. This common shift in focus toward stable growth based on less risky assets has intensified competition as banks compete for the same limited pool of quality credit by engaging in price competition or by other means, although Shinhan Bank has traditionally focused, and will continue to focus, on enhancing profitability rather than increasing asset size or market share, and has avoided, to the extent practicable, engaging in price competition by way of lowering lending rates. In addition, such competition may result in lower net interest margin and reduced overall profitability, especially if the low interest rate environment were to continue for a significant period of time. Although net interest margin may improve if the base interest rate is increased during 2018, the effect on Shinhan Bank s results of operations may be less beneficial due to increased volatility of market interest rates and tighter regulations regarding SOHO loans, including the implementation of additional credit review guidelines for individual businesses. Therefore, if competing financial institutions seek to expand market share by lowering their lending rates, Shinhan Bank may suffer customer loss, especially among customers who select their lenders principally on the basis of lending rates. In response thereto or for other strategic reasons, Shinhan Bank may subsequently lower its lending rates to stay competitive, which could lead to a decrease in its net interest margins and outweigh any potential positive impact on the net interest margin from a general rise in market interest rates. Any future decline in Shinhan Bank s customer base or its net interest margins could have an adverse effect on our results of operations and financial condition.

In the credit card sector, Shinhan Card competes principally with existing monoline credit card companies, credit card divisions of commercial banks, consumer finance companies, other financial institutions and, recently, credit card service providers allied with mobile telecommunications service providers in Korea. Competition has been historically intense in this sector and the market has shown signs of saturation as existing and new credit card service providers make significant investments and engage in aggressive marketing campaigns and promotions to acquire new customers and target customers with high credit quality. While competition has subsided somewhat recently due to stricter government regulations, such as curbs on excessive marketing expenses, competition remains intense and credit card issuers may continue to compete with Shinhan Card for customers by offering lower interest rates and fees, higher credit limits, more attractive promotions and incentives and alternative products such as phone cards, gift cards and low-interest consumer loan products. As a result, Shinhan Card may lose customers or service opportunities to competing credit card issuers and/or incur higher marketing expenses. In addition, the Government regulations adopted in 2012 mandating lower merchant fees chargeable to small- and medium-sized enterprises (which are subject to revision every three years) and the Government guidelines issued in 2013 suggesting lower standard interest rates for cash advances and card loans have reduced, and are likely to continue to limit, the revenues of credit card companies, including Shinhan Card. Beginning January 31, 2016, a further reduction in the merchant fees chargeable to small- and medium-sized enterprises went into effect. In addition, due to the implementation of the Improper Solicitation and Graft Act on September 28, 2016, revenue growth for corporate cards and service related industries such as dining, floral and entertainment have shown signs of decline. In July 2017, the Enforcement Decree of the Specialized Credit Finance Business Act was amended to expand the range of small- and medium-sized enterprises subject to lower merchant fees. Additional regulations on loans reducing maximum interest rates chargeable from 27.9% to 24% came into effect in February 2018, placing further downward pressure on the results of operations for credit card companies for 2018 and beyond, and amendments to regulations requiring further downward adjustments to merchant fees are expected to continue in the near future. Furthermore, the Government s recent guidelines to bolster consumer protection and protect customers personal data in the aftermath of data leaks at certain credit companies (not including Shinhan Card) may result in additional compliance costs for Shinhan Card. Customer attrition, together with any further lowering of fees or reduction in base and market interest rates and/or additional expenses from more extensive marketing and promotional campaigns that Shinhan Card might implement to acquire and retain customers, could reduce its revenues and earnings. Furthermore, the average credit quality of Shinhan Card s customers may deteriorate if customers with higher credit quality borrow from our competitors rather than Shinhan Card and it may become more difficult for Shinhan Card to attract and maintain quality customers. In general, the growth, market share and profitability of Shinhan Card s operations may decline or become negative as a result of market saturation in this sector, interest rate competition, pressure to lower fee rates and incur higher marketing expenses, as well as Government regulation and social and economic developments in Korea that are beyond our control, such as changes in consumer confidence levels, spending patterns or public perception of credit card usage and consumer debt. If Shinhan Card fails to maintain or attract new cardholders or increase the card usage by existing customers or experiences deterioration in its asset quality and a rise in delinquency, our business, financial condition and results of operations may be adversely affected.

In other financial services sectors, our other subsidiaries also compete in a highly fragmented market. Some of our competitors, particularly the major global financial institutions, have greater experience and resources than we do.

Consolidation among our rival institutions and the Government s privatization efforts may also add competition in the markets in which we and our subsidiaries conduct business. A number of significant mergers and acquisitions in the industry have taken place in Korea over the past decade, including the acquisition of Hanmi Bank by an affiliate of Citibank in 2004, Standard Chartered Bank s acquisition of Korea First Bank in 2005, Chohung Bank s merger with Shinhan Bank in 2006 and Hana Financial Group s acquisition of Korea Exchange Bank in 2012 and the resulting merger of Hana Bank and Korea Exchange Bank in September 2015. Moreover, in 2014, pursuant to the implementation of the Government s privatization plan with respect to Woori Finance Holdings (now merged into Woori Bank) and its former subsidiaries, Woori Financial, Woori Asset Management and Woori F&I were acquired by KB Financial Group, Kiwoom Securities and Daishin Securities, respectively, and Woori Investment & Securities, Woori Aviva Life Insurance and Woori FG Savings Bank were acquired by NongHyup Financial Group. In addition, in October 2014, the Government s ownership interest in the holding companies of Kwangju Bank and Kyongnam Bank were acquired by JB Financial Group and BS Financial Group (now BNK Financial Group), respectively. In 2015, the Government decided to sell a 30% to 40% interest in Woori Bank to multiple investors in separate blocks ranging from 4% to 10% each. Since December 2016, Korea Deposit Insurance Corporation has consummated sales transactions with seven institutional investors including Kiwoom Securities, Korea Investment and Securities, Hanwha Life Insurance, Tongyang Life Insurance, Eugene Asset Management, Mirae Asset Global Investments and IMM Private Equity for the sale of an aggregate 29.7% interest in Woori Bank in separate blocks. In the securities brokerage sector, Mirae Asset acquired KDB Daewoo Securities in 2016, creating the largest brokerage company in Korea by assets. On June 1, 2016, KB Financial Group completed its acquisition of Hyundai Securities and merged it with its existing brokerage unit, KB Investment & Securities Co, creating the fifth largest brokerage company in Korea by assets. Any of these developments may place us at a competitive disadvantage and outweigh any potential benefit to us in the form of opportunities to acquire new customers who are displeased with the level of services at the newly reorganized entities or to provide credit facilities to corporate customers who wish to maintain relationships with a wide range of banks in order to diversify their sources of funding. We expect that such consolidation and other structural changes in the financial industry will continue. Other financial institutions may seek to acquire or merge with other entities, and the financial institutions resulting from such consolidation may, by virtue of their increased size and business scope, provide greater competition for us. Increased competition and continuing consolidation may lead to decreased margins, resulting in a material adverse impact on our future profitability.

Regulatory reforms and the general modernization of business practices in Korea have also led to increased competition among financial institutions in Korea. Since July 2015, the Financial Services Commission has provided, through the Korea Financial Telecommunications and Clearings Institute, the integrated automatic payment transfer management service, which allows account holders to search for, terminate or modify automatic payments they have set up with financial institutions participating in such service (currently including banks, securities companies and other financial institutions such as The Post Office, Korean Federation of Community Credit Cooperatives, National Credit Union Federation of Korea, Mutual Savings Bank and National Forestry Cooperative Federation). In addition, the Financial Services Commission began providing the integrated account management service from December 2016, which allows account holders to search for detailed information of their bank accounts opened in banks participating in such service, close small-sum inactive accounts (i.e., accounts with no transaction activity during the previous one year period and with a balance of less than ₩500,000) and transfer the balance in such accounts to other accounts. Moreover, in December 2017, the Financial Services Commission introduced the my account at a glance system, which enables consumers to

view their key financial account information online, including information on banks, insurances, mutual finance, loan and card issuances on one page. The my account at a glance system is expected to become available on mobile channels and expand its scope of services to include savings banks and securities within 2018. Since their introduction, the integrated automatic payment transfer management and integrated account management services have gained widespread acceptance, evidenced by the fact that, as of September 30, 2017, these services have been used by approximately 17.6 million and 8.0 million users, respectively. As the reform of the financial sector continues, competition may become more intense among existing banks, insurance companies, securities companies and other financial organizations and may lead to significant changes in the current Korean financial market. As a result, Shinhan Bank may face difficulties in increasing or retaining its deposits, which in turn may result in an increase in its cost of funding and a decrease in its settlement and remittance service fee revenue.

Furthermore, as the Korean economy further develops and new business opportunities arise, more competitors may enter the financial services industry. For example, as online service providers and technology companies with large-scale user networks, such as Kakao Corp., NAVER and Samsung Electronics, recently make significant inroads in providing virtual payment services through a system based on a growing convergence of financial services and technology commonly referred to as fintech, competition for online customers is growing not just among commercial banks, but also from online and mobile payment service providers. Also, widespread consumer acceptance of mobile phone payment services in lieu of credit card services could add to the competitive threat faced by existing credit card service providers, including our credit card subsidiary. In 2015, the Government announced its plans to allow Internet-only banks to operate in Korea. KT consortium s K-Bank and Kakao consortium s Kakao Bank commenced operations in April 2017 and July 2017, respectively. Internet-only banks may have advantages over traditional banks as the former can pass savings in labor and overhead costs to their customers by offering higher interest rates on deposit accounts, lower loan costs and reduced service fees. Accordingly, commercial banks will likely face increasing pressure to upgrade their service platforms to attract and maintain online users, which represents a growing customer base compared to traditional customers who have primarily conducted banking in-person at physical banking branches.

Recently, following the global financial crisis, the Government has subjected Korean financial institutions to stricter regulatory requirements and guidelines in areas of asset quality, capital adequacy, liquidity and residential and other lending practices (including a requirement to maintain a certain ratio of core capital to total risk exposure, which was introduced in January 2018 in order to control excessive leverage), which has had a dampening effect on competition. The Financial Services Commission implemented the capital requirements of Basel III, whose minimum requirements were phased in sequentially from December 1, 2013 through full implementation by January 1, 2015, based on the guidelines set forth in the amended Regulation on the Supervision of the Banking Business and the Detailed Regulation on the Supervision of the Banking Business. In addition, the Financial Services Commission is currently implementing the Basel III requirements relating to liquidity coverage ratio and capital conservation buffer, each of which will be fully phased in by January 1, 2019. As of January 1, 2016, the Financial Services Commission implemented Basel III requirements relating to accumulation of additional capital for systemically important banks and bank holding companies and countercyclical capital buffer requirements. Each year, the Financial Services Commission may designate banks with significant influence (based on size and connectivity with other financial institutions) on the domestic financial system as a domestic systemically important bank and require the accumulation of additional capital in accordance with the highest of: (i) ratio of common equity capital to risk-weighted assets, ranging from 0.0% to 2.0%, depending on the systematic importance evaluation score, (ii) if the bank s holding company is a domestic systemically important bank holding company, the capital ratio corresponding to the additional capital required for the bank holding company under the Financial Holding Company Supervision Regulations, or (iii) if the bank is also a global systemically important bank, as defined by the Basel Committee on Banking Supervision (the Basel Committee), the capital ratio as required by the Basel Committee. According to the instructions of the Financial Services Commission, domestic systematically important banks including Shinhan Bank are required to maintain an additional capital buffer of 0.25% since January 1, 2016, with such buffer to increase by 0.25% annually to 1.00% by January 1, 2019. The Financial Services Commission may also, upon quarterly review, determine and require banks to accumulate a required level of countercyclical capital buffer within the range of

0% to 2.5% of risk-weighted assets, taking into account factors such as the degree of increase in credit relative to the gross domestic product. However, there is no assurance that these measures will have the effect of curbing competition or that the Government will not reverse or reduce such measures or introduce other deregulatory measures, which may further intensify competition in the Korean financial services industry. For further details on the capital requirements applicable to us, see Item 4.B. Business Overview Supervision and Regulation Principal Regulations Applicable to Financial Holding Companies Capital Adequacy.

If, despite our efforts to adapt to the changing macroeconomic environment and comply with new regulations, we are unable to compete effectively in the changing business and regulatory environment, our profit margin and market share may erode and our future growth opportunities may become limited, which could adversely affect our business, financial condition and results of operations.

We and our subsidiaries need to maintain our capital ratios above minimum required levels, and the failure to so maintain could result in the suspension of some or all of our operations.

We and our subsidiaries in Korea are required to maintain specified capital adequacy ratios. For example, since January 1, 2015, we and our banking subsidiaries in Korea are required to maintain a minimum common equity Tier I capital adequacy ratio of 4.5%, a Tier I capital adequacy ratio of 6.0% and a total capital (BIS) ratio of 8.0%. These ratios measure the respective regulatory capital as a percentage of risk-weighted assets on a consolidated basis and are determined based on guidelines of the Financial Services Commission. In addition, as further described below, Shinhan Bank is also required to maintain a capital conservation buffer and additional capital as a domestic systemically important bank and may be required to maintain a countercyclical capital buffer. Also, our subsidiaries Shinhan Card, Shinhan Life Insurance and Shinhan Investment are each required to maintain a consolidated adjusted equity capital ratio of 8.0%, a solvency ratio of 100% and a net equity ratio of 100%, respectively.

While we and our subsidiaries currently maintain capital adequacy ratios in excess of the respective required regulatory minimum levels, we or our subsidiaries may not be able to continue to satisfy the capital adequacy requirements for a number of reasons, including an increase in risky assets and provisioning expenses, substitution costs related to the disposal of problem loans, declines in the value of securities portfolios, adverse changes in foreign currency exchange rates, changes in the capital ratio requirements, the guidelines regarding the computation of capital ratios, or the framework set by the Basel Committee upon which the guidelines of the Financial Services Commission are based, or other adverse developments affecting our asset quality or equity capital.

In December 2010, the Basel Committee issued final rules in respect of (i) a global regulatory framework for more resilient banks and banking systems and (ii) an international framework for liquidity risk measurement, standards and monitoring, which together are commonly referred to as Basel III. Under Basel III, Tier I capital is defined to include common equity Tier I and additional Tier I capital. Common equity Tier I capital is a new category of capital primarily consisting of common stock, capital surplus, retained earnings and other comprehensive income (progressively phased into the capital ratio calculation over several years). The new minimum capital requirements, including the minimum common equity Tier I requirement of 4.5% and additional mandatory capital conservation buffer requirement of 2.5%, are currently being implemented in phases until January 1, 2019. Additional discretionary countercyclical capital buffer requirements are also expected to be phased in, which will range at the discretion of national regulators between 0% and 2.5% of risk-weighted assets. Basel III also introduces a minimum leverage ratio requirement. On December 7, 2017, the Basel Committee finalized several key methodologies for measuring risk-weighted assets. The revisions include a standardized approach for credit risk, standardized approach for operational risk, revisions to the credit valuation adjustment (CVA) risk framework and constraints on the use of internal models. The Basel Committee had also previously finalized a revised standardized model for counterparty credit risk, revisions to the securitization framework and its fundamental review of the trading book, which updates both modeled and standardized approaches for market risk measurement. The revisions also include a capital floor set at 72.5% of total risk-weighted assets based on the revised standardized approaches to limit the extent to which banks can reduce risk-weighted asset levels through the use of internal models.

In order to implement the capital requirements under Basel III in Korea, the Regulation on the Supervision of the Banking Business was amended, effective December 1, 2013. Under the amended Regulation on the Supervision of the Banking Business, effective from January 1, 2015, commercial banks in Korea are required to maintain a minimum common equity Tier I ratio of 4.5%, a minimum Tier I capital ratio of 6.0% and a minimum total capital (BIS) ratio of 8.0%. The Regulation on the Supervision of the Banking Business was further amended on December 26, 2014, to implement the liquidity coverage ratio requirements under Basel III in increments of 5% annually, from 80% as of January 1, 2015 to 100% as of January 1, 2019. Capital conservation buffer requirements are also being phased in from January 1, 2016 in increments of 0.625% annually, to the effect that commercial banks in Korea will be required to maintain a capital conservation buffer of 2.5% as of January 1, 2019. If a commercial bank fails to maintain such capital conservation buffer requirements, such bank will be subject to certain restrictions relating to its use of income, such as distributing dividends and purchasing treasury stock. As of January 1, 2016, the Financial Services Commission implemented Basel III requirements relating to accumulation of additional capital for systemically important banks and bank holding companies and countercyclical capital buffer requirements. Each year, the Financial Services Commission may designate banks with significant influence (based on size and connectivity with other financial institutions) on the domestic financial system as a domestic systemically important bank and require the accumulation of additional capital in accordance with the highest of: (i) ratio of common equity capital to risk-weighted assets, ranging from 0.0% to 2.0%, depending on the systematic importance evaluation score, (ii) if the bank s holding company is a domestic systemically important bank holding company, the capital ratio corresponding to the additional capital required for the bank holding company under the Financial Holding Company Supervision Regulations, or (iii) if the bank is also a global systemically important bank, as defined by the Basel Committee, the capital ratio as required by the Basel Committee. Shinhan Financial Group, Shinhan Bank and Jeju Bank were selected as a domestic systemically important bank holding company and domestic systemically important bank, respectively, for 2017. According to the instructions of the Financial Services Commission, domestic systematically important banks including the Bank are required to maintain an additional capital buffer of 0.25% since January 1, 2016, with such buffer to increase by 0.25% annually to 1.00% by January 1, 2019. The Financial Services Commission may also, upon quarterly review, determine and require banks to accumulate a required level of countercyclical capital buffer within the range of 0% to 2.5% of risk-weighted assets, taking into account factors such as the degree of increase in credit relative to the gross domestic product. Since March 2016, the Financial Services Commission has maintained countercyclical capital buffer requirements at 0%, and the Financial Supervisory Service is expected to maintain the countercyclical capital buffer requirement at 0% for the first quarter of 2018.

We and our banking subsidiaries are currently, and have been, in full compliance with Basel III requirements as implemented in Korea since its introduction in December 2013. However, there is no assurance that we will continue to be able to be in compliance with Basel III requirements. New requirements under Basel III may require an increase in the credit risk capital requirements in the future, which may require us or our subsidiaries to either improve asset quality or raise additional capital. In addition, if the capital adequacy ratios of us or our subsidiaries were to fall below the required levels, the Financial Services Commission might impose penalties ranging from a warning to suspension or revocation of our or our subsidiaries business licenses. In order to maintain the capital adequacy ratios above the required levels, we or our subsidiaries may be required to raise additional capital through equity financing, but there is no assurance that we or our subsidiaries will be able to do so on commercially favorable terms or at all and, even if successful, any such capital raising may have a dilutive effect on our shareholders with respect to their interest in us or on us with respect to our interest in our subsidiaries.

Liquidity, funding management and credit ratings are critical to our ongoing performance.

Liquidity is essential to our business as a financial intermediary, and we may seek additional funding in the near future to satisfy liquidity needs, meet regulatory requirements, enhance our capital levels or fund the growth of our operations as opportunities arise.

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For example, Basel III includes an international framework for liquidity risk measurement, standards and monitoring, as noted above, including a new minimum liquidity standard, known as the liquidity coverage ratio, which is designed to ensure that banks have an adequate stock of unencumbered high quality liquid assets (HQLA) that can be easily and speedily converted into cash in the private marketplace to survive a significant stress scenario lasting 30 calendar days. The liquidity coverage ratio is computed as (a) the value of a banking organization s HQLA, divided by (b) its total expected net cash outflows over the next 30 calendar days under stress scenarios. The minimum liquidity coverage ratio is 100%. In January 2013, the Basel Committee released a revised formulation of the liquidity coverage ratio, one of two quantitative liquidity measures approved in December 2010 as part of Basel III. The Basel Committee extended the timetable for full phase-in of the liquidity coverage ratio to the effect that the minimum liquidity coverage ratio was set at 60% as of January 1, 2015 and thereafter rises in annual increments of 10% so that the minimum liquidity coverage ratio will be 100% as of January 1, 2019. In December 2014, the Financial Services Commission promulgated regulations to implement the liquidity requirements of Basel III, including raising the minimum liquidity coverage ratio to 80% as of January 1, 2015 and thereafter by annual increments of 5% so that the minimum liquidity coverage ratio for commercial banks in Korea will be 100% as of January 1, 2019.

A substantial part of the liquidity and funding requirements for our banking subsidiaries is met through short-term customer deposits, which typically roll over upon maturity. While the volume of our customer deposits has generally been stable over time, customer deposits have from time to time declined substantially due to the popularity of other, higher-yielding investment opportunities, namely stocks and mutual funds, for example, during times of bullish stock markets. During such times, our banking subsidiaries were required to obtain alternative funding at higher costs. There is no assurance that a similar development will not occur in the future. In addition, in recent years, we have faced increasing pricing competition from our competitors with respect to our deposit products. If we do not continue to offer competitive interest rates to our deposit customers, we may lose their business, which has traditionally provided a stable and low-cost source of funding. In addition, even if we are able to match our competitors pricing, doing so may result in an increase in our funding costs, which may have an adverse impact on our results of operations.

We and our subsidiaries also raise funds in capital markets and borrow from other financial institutions, the cost of which depends on market rates and the general availability of credit and the terms of which may limit our ability to pay dividends, make acquisitions or subject us to other restrictive covenants. While we and our subsidiaries are not currently facing liquidity difficulties in any material respect, if we or our subsidiaries are unable to obtain the funding we need on terms commercially acceptable to us for an extended period of time for whatever reason, we may not be able to ensure our financial viability, meet regulatory requirements, implement our strategies or compete effectively.

Credit ratings affect the cost and other terms upon which we and our subsidiaries are able to obtain funding. Domestic and international rating agencies regularly evaluate us and our subsidiaries, and their ratings of our and our subsidiaries long-term debt are based on a number of factors, including our financial strength as well as conditions affecting the financial services industry and the Korean economy in general. There can be no assurance that the rating agencies will maintain our current ratings or outlooks. There is no assurance that Shinhan Bank, Shinhan Card, any of our other major subsidiaries or our holding company will not experience a downgrade in their respective credit ratings and outlooks for reasons related to the general Korean economy or reasons specific to such entity. Any downgrades in the credit ratings and outlooks of us and our subsidiaries will likely increase our cost of funding, limit our access to capital markets and other borrowings, or require us to provide additional credit enhancement in financial transactions, any of which could adversely affect our liquidity, net interest margins and profitability, and in turn, our business, financial condition and results of operations.

Changes in interest rates, foreign exchange rates, bond and equity prices, and other market factors have affected and will continue to affect our business, results of operations and financial condition.

The most significant market risks we face are interest rate, foreign exchange and bond and equity price risks. Changes in interest rate levels, yield curves and spreads may affect the interest rate margin realized

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between lending and borrowing costs. Changes in foreign currency exchange rates, particularly in the Korean Won to U.S. Dollar exchange rates, affect the value of our assets and liabilities denominated in foreign currencies, the reported earnings of our non-Korean subsidiaries and income from foreign exchange dealings, and substantial and rapid fluctuations in exchange rates may cause difficulty in obtaining foreign currency-denominated financing in the international financial markets on commercial terms acceptable to us or at all. The performance of financial markets may affect bond and equity prices and, therefore, cause changes in the value of our investment and trading portfolios. While we have implemented risk management systems to mitigate and control these and other market risks to which we are exposed, it is difficult to predict with accuracy changes in economic or market conditions and to anticipate the effects that such changes could have on our business, financial condition and results of operations.

Of particular importance is the change in the base and market interest rates. Since 2009, Korea, like many other countries, has experienced a low interest rate environment despite some marginal fluctuations, in part due to the Government s policy to stimulate the economy through active rate-lowering measures. Between 2009 and 2014, the base interest rate set by the Bank of Korea remained within the band between 2.00% and 3.25%. In an effort to support Korea s economy in light of the recent slowdown in Korea s growth and uncertain global economic prospects, the Bank of Korea reduced the base interest rate to 1.75% in March 2015, 1.50% in June 2015, and further reduced such rate to the historic low of 1.25% in June 2016. In November 2017, the Bank of Korea raised the base interest rate to 1.50%, marking the first time it has increased the base interest rate since 2011. Interest rate movements, in terms of magnitude and timing as well as their relative impact on our assets and liabilities, have a significant impact on our net interest margin and profitability, particularly with respect to our financial products that are sensitive to such movements. For example, if the interest rates applicable to our loans (which are recorded as assets) increase at a slower pace or by a thinner margin than the interest rates applicable to our deposits (which are recorded as liabilities), our net interest margin will shrink and our profitability will be negatively affected. In addition, the relative size and composition of our variable rate loans and deposits (as compared to our fixed rate loans and deposits) may also impact our net interest margin. Furthermore, the difference in the average term of our interest-earning assets (primarily loans) compared to our interest-bearing liabilities (primarily deposits) may also impact our net interest margin. For example, since our deposits tend to have longer terms, on average, than those of our loans, our deposits are on average less sensitive to movements in the base interest rates on which our deposits and loans tend to be pegged, and therefore, a decrease in the base interest rates tends to decrease our net interest margin while an increase in the base interest rates tends to have the opposite effect. While we continually manage our assets and liabilities to minimize our exposure to interest rate volatility, such efforts by us may not mitigate the impact of interest rate volatility in a timely or effective manner, and our net interest margin, and in turn our financial condition and results of operations, could suffer significantly.

We cannot assure you when and to what extent the Government will in the future adjust the base interest rate, to which the market interest rate correlates. A decision to adjust the base interest rate is subject to many policy considerations as well as market factors, including the general economic cycle, inflationary levels, interest rates in other economies and foreign currency exchange rates, among others. In general, a decrease in interest rates adversely affects our interest income due to the different maturity structure for our assets and liabilities as discussed above. In contrast, if there were to be a significant or sustained increase in interest rates, all else being equal, such movement would lead to a decline in the value of traded debt securities and could also raise our funding costs, while reducing loan demand, especially among retail customers. Rising interest rates may therefore require us to re-balance our assets and liabilities in order to minimize the risk of potential mismatches in our asset liability management and to maintain our profitability. In addition, rising interest rates may adversely affect the Korean economy and the financial condition of our corporate and retail borrowers, including holders of our credit cards, which in turn may lead to deterioration of asset quality for our credit portfolio. Since most of our retail and corporate loans bear interest at rates that adjust periodically based on prevailing market rates, a sustained increase in interest rates will increase the funding costs of our borrowers and may adversely affect their ability to make payments on their outstanding loans. See Item 5.A.

Operating Results   Interest Rates.

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We may incur losses associated with our counterparty exposures.

We face the risk that counterparties will be unable to honor contractual obligations to us or our subsidiaries. These parties may default on their obligations to us or our subsidiaries due to bankruptcy, lack of liquidity, operational failure or other reasons. This risk may arise, for example, from entering into swaps or other derivative contracts under which counterparties have obligations to make payments to us or our subsidiaries or in executing currency or other trades that fail to settle at the required time due to non-delivery by the counterparty or systems failure by clearing agents, exchanges, clearing houses or other financial intermediaries. Any realization of counterparty risk may adversely affect our business, operations and financial condition.

Risks Relating to Our Banking Business

We have significant exposure to small- and medium-sized enterprises, and financial difficulties experienced by such enterprises may result in a deterioration of our asset quality.

Our banking activities are conducted primarily through our wholly-owned subsidiary, Shinhan Bank. One of our core banking businesses has historically been and continues to be lending to small- and medium-sized enterprises (as defined in Item 4.B. Business Overview Our Principal Activities Corporate Banking Services Small- and Medium-sized Enterprises Banking). Our loans (before allowance for loan losses and deferred loan origination costs and fees) to such enterprises amounted to ₩67,336 billion as of December 31, 2015, ₩71,757 billion as of December 31, 2016 and ₩78,556 billion as of December 31, 2017, representing 27.1%, 27.5% and 28.3%, respectively, of our total loan portfolio as of such dates.

Compared to loans to large corporations, which tend to be better capitalized and better able to weather business downturns, or loans to individuals and households, which tend to be secured with homes and with respect to which the borrowers are therefore less willing to default, loans to small- and medium-sized enterprises have historically had a relatively higher delinquency ratio. Many small- and medium-sized enterprises represent sole proprietorships or small businesses dependent on a relatively limited number of suppliers or customers and tend to be affected to a greater extent than large corporate borrowers by fluctuations in the Korean and global economy. In addition, small- and medium-sized enterprises often maintain less sophisticated financial records than large corporate borrowers. Therefore, it is generally more difficult for banks to judge the level of risk inherent in lending to such enterprises, as compared to large corporations. In addition, many small- and medium-sized enterprises are dependent on business relationships with large corporations in Korea, primarily as suppliers. Any difficulties encountered by those large corporations would likely have not only an adverse effect on the liquidity and financial condition of related small- and medium-sized enterprises, including those to which we have exposure, but also result in an impairment of their ability to repay loans. As large Korean corporations continue to expand into China, Southeast Asia and other countries with lower labor costs and other expenses by relocating their production plants and facilities to such countries, such development may have a material adverse impact on such small- and medium-sized enterprises.

Financial difficulties experienced by small- and medium-sized enterprises as a result of, among other things, recent economic difficulties in Korea and globally and aggressive marketing and intense competition among banks to lend to this segment in recent years, coupled with our efforts to counter asset quality deterioration through conservative lending policy, have led to a fluctuation in the asset quality of our loans to this segment. As of December 31, 2015, 2016 and 2017, Shinhan Bank s delinquent loans to small- and medium-sized enterprises were ₩308 billion, ₩362 billion and ₩303 billion, respectively, representing delinquency ratios (net of charge-offs and loan sales) of 0.46%, 0.51%, 0.39% respectively. If the ongoing difficulties in the Korean or global economy were to continue or aggravate, the delinquency ratio for our loans to small- and medium-sized enterprises may rise.

Of particular concern is our significant exposure to enterprises in the real estate and leasing and construction industries. As of December 31, 2017, Shinhan Bank had outstanding loans (before allowance for loan losses and deferred loan origination costs and fees) to enterprises in the real estate and leasing and construction industries

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(many of which are small- and medium-sized enterprises) of ₩21,490 billion and ₩2,550 billion, respectively, representing 9.2% and 1.1%, respectively, of its total loan portfolio as of such date. We also have other exposure to borrowers in these sectors of the Korean economy, including extending guarantees for the benefit of such companies and holding debt and equity securities issued by such companies. In addition, Shinhan Bank has exposure to borrowers in the shipbuilding and shipping industries, which have yet to stage a meaningful turnaround.

The enterprises in the real estate development and construction industries in Korea, which are heavily concentrated in the housing market, continue to experience difficulties amid slowing real estate demand despite a moderate recovery in recent years, largely due to a combination of factors including the Government s policy measures to stabilize the real estate market, oversupply of residential property, ongoing economic sluggishness in Korea and globally and the demographic changes in the Korean population. We also have limited exposure to real estate project financing, particularly by construction companies that have built residential units in provinces outside the metropolitan Seoul area, which have experienced a relatively low rate of pre-sales, the proceeds from which the construction companies primarily rely on as a key source for liquidity and cash flow.

Any of the foregoing developments may result in deterioration in the asset quality of our banking subsidiaries. See Item 4.B. Business Overview Description of Assets and Liabilities Credit Exposures to Companies in Workout and Recovery Proceedings. We have been taking active steps to curtail delinquency among our small- and medium-sized enterprise customers, including by way of strengthening loan application review processes and closely monitoring borrowers in troubled sectors. Despite such efforts, there is no assurance that the delinquency ratio for our loans to small- and medium-sized enterprises will not rise in the future, especially if the Korean economy were to face renewed difficulties and, as a result, the liquidity and cash flow of these borrowers deteriorate. A significant rise in the delinquency ratios among these borrowers would lead to increased charge-offs and higher provisioning and reduced interest and fee income, which would have a material adverse effect on our business, financial condition and results of operations.

A decline in the value of the collateral securing our loans or our inability to fully realize the collateral value may adversely affect our credit portfolio.

Most of our mortgage and home equity loans are secured by borrowers homes, other real estate, other securities and guarantees (which are principally provided by the Government and other financial institutions), and a substantial portion of our corporate loans are also secured, including by real estate. As of December 31, 2017, the secured portion of Shinhan Bank s loans (before allowance for loan losses and deferred loan origination costs and fees) amounted to ₩106,503 billion, representing 49.8% of its total loans. No assurance can be given that the collateral value will not materially decline in the future. Shinhan Bank s general policy for mortgage and home equity loans is to lend up to 40% to 70% of the appraised value of the collateral and to periodically re-appraise such collateral. However, if the real estate market in Korea experiences a downturn, the value of the collateral may fall below the outstanding principal balance of related mortgage loans. Borrowers of such under-collateralized mortgages or loans may be forced to pay back all or a portion of such mortgage loans or, if unable to meet the collateral requirement through such repayment, sell the underlying collateral, which sales may lead to a further decline in the price of real estate in general and set off a chain reaction for other borrowers due to the further decline in the value of collateral. Declines in real estate prices reduce the collateral values securing our mortgage and home equity loans, and such reductions in collateral values may result in our inability to cover the uncollectible portion of our secured loans. A decline in the value of the real estate or other collateral securing our loans, or our inability to obtain additional collateral in the event of such decline, may result in the deterioration of our asset quality and require us to make additional loan loss provisions. In Korea, foreclosure on collateral generally requires a written petition to a Korean court. Foreclosure procedures in Korea generally take 10 to 14 months from initiation to collection depending on the nature of the collateral, and foreclosure applications may be subject to delays and administrative requirements, which may result in a decrease in the recovery value of such collateral. No assurance can be given that we will be able to realize the full value of collateral as a result of, among others, delays in foreclosure proceedings, defects in the perfection of collateral and general declines in collateral value. Our failure to recover the expected value of collateral could expose us to significant losses.

Guarantees received in connection with our real estate financing may not provide sufficient coverage.

Primarily through Shinhan Bank, we, alone or together with other financial institutions, provide financing to real estate development projects, which are concentrated largely in the construction of residential complexes. Developers in Korea commonly use project financing to acquire land and pay for related project development costs. As a market practice, lenders in project financing, including Shinhan Bank, generally receive from general contractors a performance guarantee for the completion of projects by the developers as well as a payment guarantee for the loans raised by a special purpose financing vehicle established by the developers in order to procure the construction orders, as the developers tend to be small and highly leveraged. As of December 31, 2017, the total outstanding amount of Shinhan Bank s real estate project financing-related exposure was ₩1.7 trillion, which represents a decrease over the years as Shinhan Bank has actively reduced new exposures in this area in light of the sustained downturn in the Korean real estate market. However, if defaults were to significantly increase under our existing loans to real estate development projects and the general contractors fail to pay the guaranteed amount necessary to cover the amount of our financings, this may have an adverse effect on our business, financial condition and results of operations.

A limited portion of our credit exposure is concentrated in a relatively small number of large corporate borrowers, and future financial difficulties experienced by them may have an adverse impact on us.

Of Shinhan Bank s 10 largest corporate exposures as of December 31, 2017, two were companies for which Shinhan Bank was a main creditor bank. All of the 10 companies are or were members of the main debtor groups as identified by the Governor of the Financial Supervisory Service, which are mostly comprised of the largest Korean commercial conglomerates known as *chaebols*. As of such date, the total amount of Shinhan Bank s exposures to the 10 companies was ₩18,053 billion, or 11.5%, of its total exposures. As of that date, Shinhan Bank s single largest outstanding exposure to a main debtor group amounted to ₩4,328 billion, or 2.8%, of its total exposures. Largely due to the continued stagnation in the shipbuilding industry, current and former member companies of the STX Group, one of the leading conglomerates in Korea, entered into voluntary arrangements in 2013 with their creditors (including Shinhan Bank) to improve their credit situation, and STX Offshore & Shipbuilding and STX Heavy Industries, two of the STX Group s member companies, recently filed for court receivership in May 2016 and July 2016, respectively. Due to stagnation in the construction industry, Keangnam Enterprises Co., Ltd., a large construction company in Korea, also entered into workout proceedings in 2013 and subsequently filed for recovery proceedings in March 2015. Dongbu Steel Co., Ltd. and Sambu Construction Co., Ltd. also experienced significant hardship and entered into workout or recovery proceedings in 2015. Additionally, in October 2015, creditors of Daewoo Shipbuilding & Marine Engineering Co., Ltd., led by Korea Development Bank, announced a restructuring plan that included cash injection and additional loans totaling ₩4.2 trillion and extensive streamlining measures, and in November 2016, Korea Development Bank agreed to swap ₩1.8 trillion of debt to equity and the Export-Import Bank of Korea agreed to issue ₩1 trillion of perpetual bonds. Amidst continued deterioration of Daewoo Shipbuilding & Marine Engineering Co., Ltd. s financial conditions, in March 2017, Korea Development Bank and the Export-Import Bank of Korea further agreed to provide an additional ₩2.9 trillion in loans and swap ₩1.6 trillion of debt to equity, provided that other creditors and bondholders agree to certain debt-to-equity swaps and extension of maturities. In January 2016, Hanjin Heavy Industries & Construction Co., Ltd. entered into voluntary restructuring agreements with its creditors due to liquidity shortage in the wake of prolonged industry slowdown. As part of its active past efforts to reduce exposure to the shipbuilding and construction sectors, Shinhan Bank currently has limited exposure to the aforementioned troubled companies. However, if the credit quality of Shinhan Bank s exposure to large corporations, including those in the main debtor groups, declines, Shinhan Bank may be required to record additional loan loss provisions in respect of loans and impairment losses in respect of securities, which would adversely affect its financial condition, results of operations and capital adequacy. No assurance can be given that the allowances it has recognized against these exposures will be sufficient to cover all future losses arising from such exposures, especially in the case of a prolonged or renewed economic downturn.

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A limited number of the main debtor groups to which Shinhan Bank has credit exposure are subject to restructuring programs or are otherwise making significant efforts to improve their financial conditions, such as by obtaining intragroup loans and entering into agreements for further improvement of their capital structures. No assurance can be given that there will not be future restructuring with Shinhan Bank s major corporate customers or that such restructuring will not result in significant losses to Shinhan Bank with less than full recovery. In addition, if the Government decides to pursue an aggressive restructuring policy with respect to distressed companies, Korean commercial banks, including Shinhan Bank, may face a temporary rise in delinquencies and intensified pressure for additional provisioning. Furthermore, bankruptcies or financial difficulties of large corporations, including *chaebol* groups, may have an adverse ripple effect of triggering delinquencies and impairment of Shinhan Bank s loans to small- and medium-sized enterprises that supply parts or labor to such corporations. If Shinhan Bank experiences future losses from its exposure to large corporations, including *chaebol* groups, it may have a material adverse effect on Shinhan Bank s business, financial condition and results of operations. See Item 4.B. Business Overview Description of Assets and Liabilities Loans Loan Portfolio Exposure to Main Debtor Groups.

The asset quality of our retail loan portfolio may deteriorate.

In recent years, consumer debt, including lending to households and small unincorporated businesses, has continued to increase in Korea. Shinhan Bank s portfolio of retail loans is comprised of two principal product types, namely secured retail loans (which are primarily comprised of mortgage and home equity loans secured by real estate) and general purpose loans (which are unsecured loans and tend to carry a higher credit risk). As of December 31, 2017, Shinhan Bank s retail loan portfolio (before allowance for loan losses and deferred loan origination costs and fees) was ₩103,724 billion, representing 44.6% of its total loans outstanding. As of December 31, 2015, 2016 and 2017, Shinhan Bank s non-performing retail loans were ₩148 billion, ₩157 billion and ₩215 billion, respectively, representing non-performing loan ratios (net of charge-offs and loan sales) of 0.16%, 0.16% and 0.21%, respectively.

Our large exposure to consumer debt means that we are exposed to changes in economic conditions affecting Korean consumers. For example, a rise in unemployment, an increase in interest rates or a decline in housing prices in Korea could adversely affect the ability of consumers to make payments and increase the likelihood of potential defaults. Economic difficulties in Korea that may burden consumers could result in increasing delinquencies and a decline in the asset quality of the our household loan portfolio, which may in turn require us to record higher provisions for credit loss and charge-offs and may materially and adversely affect our financial condition and results of operations.

Any deterioration in the asset quality of our guarantees and acceptances will likely have a material adverse effect on our financial condition and results of operations.

In the normal course of banking activities, we make various commitments and incur certain contingent liabilities in the form of guarantees and acceptances. Financial guarantees, which are contracts that require us to make specified payments to reimburse the beneficiary of the guarantee for a loss such beneficiary incurs because the debtor in respect of which the guarantee is given fails to make payments when due in accordance with the terms of the relevant debt instrument, are recognized initially at fair value, and such initial fair value is amortized over the life of the financial guarantee. Other guarantees are recorded as off-balance sheet items in the notes to our financial statements and those guarantees that we have confirmed to make payments are recorded on the statements of financial position. As of December 31, 2017, we had aggregate guarantees and acceptances of ₩12,882 billion, for which we provided allowances for losses of ₩79.8 billion. If there is significant deterioration in the quality of assets underlying our guarantees and acceptances, our allowances may be insufficient to cover actual losses resulting in respect of these liabilities.

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Risks Relating to Our Credit Card Business

Future changes in market conditions as well as other factors, such as stricter regulation, may lead to reduced revenues and deterioration in the asset quality of credit card receivables.

As of December 31, 2015, 2016 and 2017, Shinhan Card s interest-earning credit card assets amounted to ₩21,323 billion, ₩22,765 billion and ₩25,250 billion, respectively. Our large exposure to credit card and other consumer debt means that we are exposed to changes in economic conditions affecting Korean consumers in general. For example, a rise in unemployment, an increase in interest rates, a downturn in the real estate market, or a general contraction or other difficulties affecting the Korean economy may lead Korean consumers to reduce spending (a substantial portion of which is conducted through credit card transactions), which in turn leads to reduced earnings for our credit card business, as well as to higher default rates on credit card loans, deterioration in the quality of our credit card assets and increased difficulties in recovering written-off assets from which a significant portion of Shinhan Card s revenues is derived. Any of these developments could have a material adverse effect on our business, financial condition and results of operations.

Increasing consumer and corporate spending and borrowing on our card products and growth in card lending balances depend in part on Shinhan Card s ability to develop and issue new or enhanced card and prepaid products and increase revenue from such products and services, as well as the level of discretionary income among our cardholders, which is largely affected by macroeconomic factors beyond our control. In addition, credit card companies in Korea, including Shinhan Card, may not be able to enjoy any rapid growth in revenue over the long term due to the maturing nature of the credit card industry, in part due to oversaturation of credit card service providers. Shinhan Card s future earnings and profitability also depend on its ability to attract new cardholders, reduce cardholder attrition, increase merchant coverage and capture a greater share of customers total credit card spending in Korea and overseas. Shinhan Card may not be able to manage and expand cardholder benefits in a cost-effective manner or contain the growth of marketing, promotion and reward expenses to a commercially reasonable level. If Shinhan Card is not successful in increasing customer spending, maintaining or expanding its market position and asset growth, or containing costs or cardholder benefits, its financial condition, results of operations and cash flow could be negatively affected.

KT consortium s K-Bank and Kakao consortium s Kakao Bank commenced operations in April 2017 and July 2017, respectively. Internet-only banks are expected to become major competitors to Shinhan Card in various business areas, particularly in the mid-term interest loan market. In addition, with the rapid growth of online service providers and technology companies providing virtual payment services, more competitors are entering the financial payments industry, creating a new paradigm in the payments market and changing the competitive landscape. New competitors, including Kakao Corp., NAVER and Samsung Electronics, have introduced new payment methods which are now competing with Shinhan Card s payment model AppCard. In 2018, Kakao Bank is expected to compete with credit card service providers by launching its own credit card business and expanding its mid-range interest rate loan offerings. Shinhan Card is currently making efforts to enhance its AppCard payment model and cooperating with other credit card service providers to promote its joint NFC (near field communication) payment network.

In addition, Government regulations aimed at protecting small- and medium-sized enterprises, such as the reduction of fees chargeable to small- and medium-sized merchants, may have a material adverse effect on our revenues from Shinhan Card. In January 2012, the Government expanded the definition of a small- and medium-sized merchant to include those with annual sales of up to ₩200 million and, effective September 2012, lowered fees chargeable to such merchants from 1.8% to 1.5% with respect to credit cards. In January 2015, the Government further expanded the definition of a small- and medium-sized merchant to include those with annual sales of more than ₩200 million and up to ₩300 million, and imposed a cap on fees chargeable to such merchants at 2.0% with respect to credit cards. In November 2015, the Government announced a further reduction in the merchant fees chargeable to small- and medium-sized enterprises with respect to credit cards, effective January 31, 2016, from 2.0% to 1.3% for merchants with annual sales of more than ₩200 million and up to ₩300 million, and from 1.5% to 0.8% for merchants with annual sales of up to ₩200 million. In July

2017, the Enforcement Decree of the Specialized Credit Finance Business Act was amended to expand the range of small- and medium-sized enterprises subject to lower merchant fees. Upon the amendment, merchants with annual sales of more than ₩300 million and up to ₩500 million are subject to merchant fees chargeable with respect to credit cards of 1.3%, and merchants with annual sales of up to ₩300 million are subject to merchant fees chargeable with respect to credit cards of 0.8%. Pursuant to the Specialized Credit Financial Business Act, the rates of fees chargeable to merchants are subject to review and revision every three years, and the rates of fees chargeable may be further adjusted due to changes in relevant regulations or Government policy. Amendments to regulations requiring further downward adjustments to merchant fees are expected to continue in the near future.

In 2013, the Government also implemented measures regulating marketing costs in order to control excessive marketing campaigns and curtail undue marketing expenses, which had the effect of impeding revenue growth for credit card companies, but also reduced or slowed the growth in their marketing expenses. In addition, effective December 2013, the Government introduced guidelines to curb the interest rates that credit card companies, including Shinhan Card, may charge on card loans and cash advances. Furthermore, the Government also provides tax incentives, among others, for the use of check cards (where the amounts paid with check cards are instantly debited from the customer s bank accounts) to encourage the use of check cards in lieu of credit cards in an attempt to preempt a potential rise in delinquency among credit card users, and if check cards are widely used in lieu of credit cards, this would reduce interest income from credit cards, which generally have a longer repayment period than that of check cards, and may have an adverse impact on Shinhan Card s revenues and results of operations.

Risks Relating to Our Other Businesses

We may experience significant losses from our investments and, to a lesser extent, trading activities due to market fluctuations.

We enter into and maintain large investment positions in fixed income products, primarily through our treasury and investment operations. These activities are described in Item 4.B. Business Overview Our Principal Activities Other Banking Services. We also maintain smaller trading positions, including equity and equity-linked securities and derivative financial instruments as part of our operations. Taking these positions entails making assessments about financial market conditions and trends. The revenues and profits we derive from many of these positions and related transactions are dependent on market prices, which are beyond our control. When we own assets such as debt or equity securities, a decline in market prices, for example, as a result of fluctuating market interest rates or stock market indices, can expose us to trading and valuation losses. If market prices move in a way that we have not anticipated, we may experience losses. In addition, when markets are volatile and subject to rapid changes in price directions, actual market prices may be contrary to our assessments and lead to lower than anticipated revenues or profits, or even result in losses, with respect to the related transactions and positions.

We may generate losses from our brokerage and other commission- and fee-based business.

We, through our investment and other subsidiaries, currently provide, and seek to expand the offerings of, brokerage and other commission- and fee-based services. Downturns in stock markets typically lead to a decline in the volume of transactions that we execute for our customers and, therefore, a decline in our non-interest revenues. In addition, because the fees that we charge for managing our clients portfolios are often based on the size of the assets under management, a downturn in the stock market, which has the effect of reducing the value of our clients portfolios or increasing the amount of withdrawals, also generally reduces the fees we receive from our securities brokerage, trust account management and other asset management services. Even in the absence of a market downturn, below-market performance by our securities, trust account or asset management subsidiaries may result in increased withdrawals and reduced cash inflows, which would reduce the revenue we receive from these businesses. In addition, protracted declines in asset prices can reduce liquidity for assets held by us and lead to material losses if we cannot close out or otherwise dispose of deteriorating positions in a timely way or at commercially reasonable prices.

Prolonged periods of declining or low interest rates may reduce or turn negative our investment margin on savings insurance products and result in an increase in the valuation of our liabilities associated with these products.

We, principally through Shinhan Life Insurance, offer fixed rate insurance policies such as savings insurance products that include guaranteed benefits. These products expose us to the risk that changes in interest rates will reduce our investment margin, which is the difference between the amounts that we are required to pay under the contracts and the rate of return we earn on investments intended to support obligations under such contracts. During periods of declining or low interest rates, we may have to invest insurance cash flows and reinvest the cash flows we received as interest or return of principal on our investments in lower yielding instruments. In addition, during periods of declining or low interest rates, fixed rate policies may become relatively more attractive investments to consumers. This could result in an increase in payments we are required to pay on such products and higher percentage of such products remaining in-force from year to year, during a period when our new investments carry lower returns. During periods of sustained lower interest rates, our reserves for policy liabilities may not be sufficient to meet future policy obligations and may need to be strengthened.

Significantly lower or negative investment margins may cause us to accelerate amortization, thereby reducing net income in the affected reporting period and potentially negatively affecting our credit instrument covenants or rating agency assessment of our financial condition. In addition, under IFRS 17, which is expected to become effective beginning 2021, insurance contract liabilities will be calculated in terms of market value (as the present value of future insurance cash flows with a provision for risk) instead of book value. As the discount rate will reflect current interest rates rather than book yields, we may have a significantly higher debt balance under IFRS 17 due to higher insurance liabilities, thereby resulting in a decrease in our risk-based capital.

Other Risks Relating to Us as the Holding Company

Our ability to continue to pay dividends and service debt will depend on the level of profits and cash flows of our subsidiaries.

We are a financial holding company with minimal operating assets other than the shares of our subsidiaries. Our primary source of funding and cash flow is dividends from, or disposition of our interests in, our subsidiaries or our cash resources, most of which are currently the result of borrowings. Since our principal assets are the outstanding capital stock of our subsidiaries, our ability to pay dividends on our common and preferred shares and service debt will mainly depend on the dividend payments from our subsidiaries.

Companies in Korea are subject to certain legal and regulatory restrictions with respect to payment of dividends. For example, under the Korean Commercial Code, dividends may only be paid out of distributable income, which is calculated by subtracting the aggregate amount of a company s paid-in capital and certain mandatory legal reserves from its net assets, in each case as of the end of the prior fiscal year. In addition, financial companies in Korea, including banks, credit card companies, securities companies and life insurers, such as our subsidiaries, must meet minimum capital requirements and capital adequacy ratios applicable to their respective industries before dividends can be paid. For example, under the Banking Act of 1950, as amended (the Banking Act), a bank is required to credit at least 10% of its net profit to a legal reserve each time it pays dividends on distributable income until such time when this reserve equals the amount of its total paid-in capital, and under the Banking Act, the Specialized Credit Financial Business Act and the regulations promulgated by the Financial Services Commission, if a bank or a credit card company fails to meet its required capital adequacy ratio or is otherwise subject to the management improvement measures imposed by the Financial Services Commission, then the Financial Services Commission may restrict the declaration and payment of dividend by such a bank or credit card company. In addition, if our or our subsidiaries capital adequacy ratios fall below the required levels, our ability to pay dividends may be restricted by the Financial Services Commission.

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Damage to our reputation could harm our business.

We are one of the largest and most influential financial institutions in Korea by virtue of our financial track records, market share and the size of our operations and customer base. Our reputation is critical to maintaining our relationships with clients, investors, regulators and the general public. Our reputation can be damaged in numerous ways, including, among others, employee misconduct (including embezzlement), cyber or other security breaches, litigation, compliance failures, corporate governance issues, failure to properly address potential conflicts of interest, the activities of customers and counterparties over which we have limited or no control, prolonged or exacting scrutiny from regulatory authorities and customers regarding our trade practices, or uncertainty about our financial soundness and our reliability. If we are unable to prevent or properly address these concerns, we could lose our existing or prospective customers and investors, which could adversely affect our business, financial condition and results of operations.

Our risk management policies and procedures may not be fully effective at all times.

In the course of our operations, we must manage a number of risks, such as credit risks, market risks and operational risks. We seek to monitor and manage our risk exposures through a comprehensive risk management platform, encompassing centralized risk management organization and credit evaluation systems, reporting and monitoring systems, early warning systems and other risk management infrastructure, using a variety of risk management strategies and techniques. See Item 4.B. Business Overview Risk Management. Although we devote significant resources to developing and improving our risk management policies and procedures and expect to continue to do so in the future, our risk management practices may not be fully effective at all times in eliminating or mitigating risk exposures in all market environments or against all types of risk, including risks that are unidentified or unanticipated. For example, from time to time, a limited number of our and our subsidiaries personnel have engaged in embezzlement of substantial amounts for an extended period of time before such activities were detected by our risk management systems. In response to these incidents, we have strengthened our internal control procedures by, among others, implementing a real-time monitoring system, but there is no assurance that such measures will be sufficient to prevent similar employee misconducts in the future. Management of credit, market and operational risk requires, among others, policies and procedures to record properly and verify a large number of transactions and events, and we cannot assure you that these policies and procedures will prove to be fully effective at all times against all the risks we face.

We may experience disruptions, delays and other difficulties relating to our information technology systems.

We rely on our information technology systems to seamlessly provide our wide-ranging financial services as well as for our daily operations, including billing, online and offline financial transactions settlement and record keeping. We continually upgrade, and make substantial expenditures to upgrade, our group-wide information technology system, including in relation to customer data-sharing and other customer relations management systems, particularly in light of the heightened cyber security risks from advances in technology. Despite our best efforts, however, we may experience disruptions, delays, cyber or other security breaches or other difficulties relating to our information technology systems, and may not timely upgrade our systems as currently planned. Any of these developments may have an adverse effect on our business, particularly if our customers perceive us to not be providing the best-in-class cyber security systems and failing to timely and fully rectify any glitches in our information technology systems.

Our activities are subject to cyber security risk.

Our activities have been, and will continue to be, subject to an increasing risk of cyber-attacks, the nature of which is continually evolving. Cyber security risks include unauthorized access, through system-wide hacking or other means, to privileged and sensitive customer information, including passwords and account information, and illegal use thereof. Cyber security risk is generally on the rise as a growing number of our customers increasingly rely on our Internet- and mobile phone-based banking services for various types of financial transactions. While we vigilantly protect customer data through encryption and other security programs and have made substantial investments to build and upgrade our systems and defenses to address the growing threats from cyber-attacks, there is no assurance that such data will not be subject to future security breaches. In addition, there can be no assurance that we will not experience a leakage of customer information or other security breaches as a result of illegal activities by our employees, outside consultants or hackers, or otherwise.

For example, in March 2013, we experienced a temporary interruption in providing online financial services due to large-scale cyber-attacks by unidentified sources on the security systems of major broadcasting networks and financial institutions in Korea. The interruption of our online financial services lasted approximately 90 minutes, after which our online system resumed without further malfunction. The Financial Supervisory Service conducted an investigation into the incident and found that Shinhan Bank and Jeju Bank had not properly maintained their information technology administrator accounts and vaccine servers. As a result, in December 2013, the Financial Supervisory Service notified Shinhan Bank and Jeju Bank of an institutional caution (which does not give rise to significant sanctions unlike in the case of repeated institutional warnings) and imposed disciplinary actions against five of Shinhan Bank s employees and three of Jeju Bank s employees. We do not believe such incident resulted in any material loss or leakage of customer information or other sensitive data.

Major financial institutions in Korea have also fallen victim to large-scale data leakage in the past. In December 2013, it was reported that there was a leakage of personal information of approximately 130,000 customers of Standard Chartered Bank and Citibank in Korea, which leakage was attributed to a third party sub-contractor in the case of Standard Chartered Bank, and an employee in the case of Citibank. In addition, in January 2014, it was reported that there was a leakage of personal information of approximately 100 million customers of NH Card, Lotte Card and KB Card in Korea due to illegal access to such information by an employee of a third party credit information company in the course of developing information technology programs for these three credit card companies.

Other than the cyber security attack in March 2013 as discussed above, we have not experienced any material security breaches in the past, including any similar large scale leakage of customer information. In order to minimize the risk of security breaches related to customer and our other proprietary information, we have taken a series of group-wide preventive measures, such as the adoption and implementation of a best-in-class information security system and reinforcement of internal control measures. We are fully committed to maintaining the highest standards of cyber security and consumer protection measures and upgrading them continually. We have implemented the ISO 27001-certified security management system for us and all our subsidiaries, and we have obtained the Information Security Management System certification for most of our subsidiaries. Our Joint Security Control Center s McAfee security management system enables us to continuously monitor for signs of potential cyber-attacks and provides us with advance warnings that will allow us to promptly respond to such attacks. We believe such certifications represent third-party validations that we are in compliance with best-in-class international standards on matters of information security. Our security management system continuously monitors for signs of potential cyber-attacks and is designed to provide early warning alerts to enable prompt action by us. In order to prevent intentional and accidental security issues by our employees, we have created a violation monitoring system, reinforcing our security measures by preemptively identifying various scenarios of threats and by collecting and analyzing different types of data that allows us to quickly identify any potential security violations. Moreover, we established a new information security lab to build a continuous security research and development system to respond to hacking and other cyber threats. Through these measures, we are developing technical capabilities necessary to respond to the latest security threats. We also provide intensive employee training to our information technology staff and other employees on cyber security and have adopted advanced security infrastructure (including through hiring a highly competent team of information security experts) for online financial services such as mandatory website certification and keyboard security functions. In addition, reviews of our system are conducted through periodic audits and simulation reviews by external experts. In addition, in compliance with applicable regulations we currently carry insurance to cover cyber security breaches up to ₩10 billion in relation to our banking business and up to ₩3 billion in the aggregate and up to ₩1 billion per incident for our securities investment business and have set

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aside a reserve of ₩1 billion for our credit card business. In addition, in light of the growing use of smart phones and other mobile devices to access financial services, we have implemented security measures (including encryptions and service terminal monitoring) to provide a secure mobile banking service as well as to prevent illegal leakage or sharing of customer data and otherwise enhance customer privacy. We are also keenly aware of the litigation and regulatory sanctions risks that may arise from security breaches and are aggressively reinforcing a group-wide culture that stresses safety and good custodianship as among our highest priorities. Furthermore, we are actively taking steps to implement preventive and other steps recommended or required by the regulatory authorities in relation to actual and potential financial scams. However, given the unpredictable and continually evolving nature of cyber security threats due to advances in technology or other reasons, there is no assurance that, notwithstanding our best efforts at maintaining the best-in-class cyber security systems, we will not be vulnerable to major cyber security attacks in the future.

The public is developing heightened awareness about the importance of keeping their personal data private, and the financial regulators are placing greater emphasis on data protection by financial service providers. For example, under the Personal Information Protection Act, as last amended in October 2017, financial institutions, as personal information manager, may not collect, store, maintain, utilize or provide resident registration numbers of their customers, unless other laws or regulations specifically request or permit the management of resident registration numbers. Further, under the Use and Protection of Credit Information Act, as last amended in November 2017 with effect from May 2018, a financial institution has a higher duty to protect credit information, meaning information necessary to assess the creditworthiness of the counterparty to financial transactions and other commercial transactions. Such regulations have considerably restricted a financial institution s ability to transfer or provide the information to its affiliate or holding company, and treble damages can be imposed on a financial institution for a leakage of such information. In addition, under the Electronic Financial Transaction Act, as last amended in April 2017 with effect from October 2017, a financial institution is primarily responsible for compensating its customers harmed by the financial institution s cyber security breach, even if the breach is not directly attributable to the financial institution. We maintain an integrated system that closely monitors customer information to ensure compliance with data protection laws and regulations.

If a cyber or other security breach were to happen with respect to us or any of our subsidiaries, it may result in litigation by affected customers or other third parties (including class actions), compensation for any losses suffered by victims of cyber security attacks, reputational damage, loss of customers, heightened regulatory scrutiny and related sanctions, more stringent compliance with the present and future regulatory restrictions, and other costs related to damage control, reparation and reinforcement of information security systems, any of which may have a material adverse effect on our business, results of operations and financial condition.

Our customers may become victims to voice phishing or other financial scams, for which we may be required to make monetary compensation and suffer damage to our business and reputation.

In recent years, financial scams known as voice phishing have been on the rise in Korea. While voice phishing takes many forms and has evolved over time in terms of sophistication, it typically involves the scammer making a phone call to a victim under false pretenses (for example, the scammer pretending to be a member of law enforcement, an employee of a financial institution or even an abductor of the victim s child) and luring the victim to transfer money to an untraceable account controlled by the scammer. More recently, voice phishing has increasingly taken the form of the scammer hacking or otherwise wrongfully obtaining personal financial information of the victim (such as credit card numbers or Internet banking login information) over the telephone or other means and illegally using such information to obtain credit card loans or cash advances through automated telephone banking or Internet banking. Reportedly, a substantial number of such scammers belong to international criminal syndicates with bases overseas, such as China, with operatives in Korea.

In response to the growing incidents of voice phishing, regulatory authorities have undertaken a number of steps to protect consumers against voice phishing and other financial scams. There is no assurance, however, that the regulatory activities will have the desired effect of substantially eradicating or even containing the incidents of voice phishing or other financial scams. For example, following an investigation in November and December 2011 of major credit card companies, including Shinhan Card, as to their compliance with regulations on card loan-related voice phishing and the scope of damage suffered by customers as a result of voice phishing, the Financial Supervisory Service issued a number of guidelines for credit companies to comply with in order to minimize damage from voice phishing, including, among others, (i) strengthening identity verification procedures for card loan applications that are made online or through the automated response system, (ii) delaying the timing of loan payout by a few hours following the approval of card loan application, and (iii) giving an option to customers to block card loan applications. In May 2012, Shinhan Card completed all necessary steps to fully comply with these additional guidelines and has been in full compliance since then.

Although the financial institutions are often not legally at fault for the damage suffered by victims of voice phishing, the compensation scheme was adopted largely in consideration of social responsibility among financial institutions and that the financial institutions were not required to, and therefore in many instances did not, confirm the personal identity of the card loan or cash advance applicants prior to the adoption of such scheme. On December 8, 2011, Shinhan Card began implementing a mandatory outcall procedure to verify the personal identity of applicants for card loans and cash advances if not requested in person. In January 2012, financial institutions, the Financial Supervisory Service, the police and other related institutions formed a joint committee to prevent voice phishing incidents and implemented preventive measures such as enforcing a 10 minute delay for withdrawal of credit card loans of ₩3 million or more from an automated teller machine. In addition, Shinhan Card and our other subsidiaries have established a fraud detection system that identifies any questionable transactions based on deviations from a customer s conventional transaction patterns.

Partly as a result of these efforts, Shinhan Card did not receive any claims in 2017 in relation to voice phishing. Accordingly, we do not believe that any currently outstanding claims in relation to voice phishing will have a material adverse impact on our business, financial condition or results of operations. Additionally, other than voice phishing incidents and the recent cyber security attacks as discussed above, we have not experienced any material security breaches in the past. However, given continual advances in technology and the increasing sophistication of the financial scammers, there is no assurance that we will be able to prevent future financial scams or that the frequency and scope of financial scams will not rise. If financial scams involving us and our subsidiaries were to continue or to become more prevalent, it may result in compensation for any losses suffered by victims thereof, reputational damage, loss of customers, heightened regulatory scrutiny and related sanctions, compliance with the present and future regulatory restrictions, and other costs related to damage control, reparation and reinforcement of our preventive measures, any of which may have a material adverse effect on our business, results of operations and financial condition.

Legal claims and regulatory risks arise in the conduct of our business.

In the ordinary course of our business, we are subject to regulatory oversight and potential legal and administrative liability risk. We are also subject to a variety of other claims, disputes, legal proceedings and government investigations in Korea and other jurisdictions where we are active. See Item 8.A. Consolidated Statements and Other Financial Information Legal Proceedings. These types of proceedings may expose us to substantial monetary and/or reputational damages and legal defense costs, injunctive relief, criminal and civil penalties and the potential for regulatory restrictions on our businesses. The outcome of these matters cannot be predicted and they could adversely affect our future business.

While we plan to rigorously defend our positions in the lawsuits or other regulatory proceedings against us, it is difficult to predict the final outcome of such cases. The total amount in dispute may increase during the course of litigation and other lawsuits may be brought against us based on similar allegations. Accordingly, these lawsuits and other proceedings may have a material adverse effect on our business, financial condition and results of operations.

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Risks Relating to Law, Regulation and Government Policy

We are a heavily regulated entity and operate in a legal and regulatory environment that is subject to change, and violations could result in penalties and other regulatory actions.

As a financial services provider, we are subject to a number of regulations that are designed to maintain the safety and soundness of Korea s financial system, to ensure our compliance with economic and other obligations and to limit our risk exposure. These regulations may limit our activities, and changes in these regulations may increase our costs of doing business. Regulatory agencies frequently review regulations relating to our business and implement new regulatory measures, including increasing the minimum required provisioning levels or capital adequacy ratios applicable to us and our subsidiaries from time to time. We expect the regulatory environment in which we operate to continue to change. Changes in regulations applicable to us, our subsidiaries and our or their business or changes in the implementation or interpretation of such regulations could affect us and our subsidiaries in unpredictable ways and could adversely affect our business, results of operations and financial condition.

Upon implementation of the Government-proposed Financial Consumer Protection Act (currently pending at the National Assembly s subcommittee for review of the bill), banks as financial instrument distributors will be subject to heightened investor protection measures, including stricter distribution guidelines, improved financial dispute resolution system, increased liability for damages borne by direct financial instrument distributors and newly imposed penalty surcharges. We may also become subject to other restrictions on our operations as a result of future changes in laws and regulations, including more stringent liquidity and capital requirements under Basel III, which are being adopted in phases in Korea in consideration of, among others, the pace and scope of international adoption of such requirements. Any of these regulatory developments may have a material adverse effect on our ability to expand operations or adequately manage our risks and liabilities. For further details on the principal laws and regulations applicable to us as a holding company and our principal subsidiaries, see Item 4.B. Business Overview Supervision and Regulation.

In addition, violations of law and regulations could expose us to significant liabilities and sanctions. For example, the Financial Supervisory Service conducts periodic audits on us and, from time to time, we have received institutional warnings from the Financial Supervisory Service. If the Financial Supervisory Service determines as part of such audit or otherwise that our financial condition, including the financial conditions of our operating subsidiaries, is unsound or that we have violated applicable law or regulations, including Financial Services Commission orders, or if we or our operating subsidiaries fail to meet the applicable requisite capital ratio or the capital adequacy ratio, as the case may be, set forth under Korean law, the Financial Supervisory Service may ask the Financial Services Commission to order, among other things, cancellations of authorization, permission or registration of the business, suspensions of a part or all of the business, closures of branch offices, recommendations for dismissal of officers or suspensions of officers from performing their duties, or may order, among other things, institutional warnings, institutional cautions, reprimanding warnings on officers, cautionary warnings on officers or cautions on officers. From time to time, our subsidiaries, including Shinhan Bank and Shinhan Card, have been subject to investigations and/or sanctions from the Financial Supervisory Service. See Item 8.A. Consolidated Statements and Other Financial Information Legal Proceedings. If any such measures are imposed on us or our subsidiaries as a result of unsound financial condition or failure to comply with minimum capital adequacy requirements or for other reasons, it will have a material adverse effect on us and our subsidiaries business, financial condition and results of operations.

The Government may encourage targeted lending to certain sectors in furtherance of policy objectives, and we may take this factor into account.

The Government has encouraged and may in the future encourage targeted lending to certain types of enterprises and individuals in furtherance of government initiatives. The Government, through its regulatory bodies such as the Financial Services Commission, from time to time announces lending policies to encourage Korean banks and financial institutions, including us and our subsidiaries, to lend to particular industries, business groups or customer segments, and, in certain cases, has provided lower cost funding through loans made by the Bank of Korea for further lending to specific customer segments.

For example, the Government has taken and is taking various initiatives to support small- and medium-sized enterprises and low-income individuals, who were disproportionately affected by the downturn in the Korean and global economy in the late 2000s and have yet to fully recover. As part of these initiatives, the Financial Supervisory Service has recently encouraged banks in Korea to increase lending to small- and medium-sized enterprises in order to ease the financial burden on such enterprises amid sluggish economic recovery, and in February 2016, the Bank of Korea announced that it would increase support for loans to small- and medium-sized enterprises by ₩9 trillion in anticipation of growing liquidity difficulties among such enterprises in light of the sustained sluggishness of the general economy and to stimulate trade exports, infrastructure investments and entrepreneurial efforts. The financial regulators have also adopted several measures designed to improve certain lending practices of the commercial banks which practices were perceived as having an unduly prohibitive effect on extending loans to small- to medium-sized enterprises.

In addition, as a way of supporting the Government s initiative to assist promising start-ups and venture companies, in February 2015, the financial regulators announced that they would encourage the banks in Korea to increase lending to technology companies in the small- to medium-sized enterprise segment by an annual target of ₩20 trillion and to enhance technology-related credit review capabilities. Pursuant to these initiatives, the total lending to technology companies in the small- to medium-sized enterprise segment, on a cumulative basis, reached ₩32.6 trillion in 2015, ₩58.4 trillion in 2016 and ₩84.0 trillion in 2017. In January 2017, the Financial Services Commission announced that it would further encourage lending to technology companies with a goal of reaching total lending, on a cumulative basis, of ₩80 trillion by the end of 2017. As of December 31, 2017, Shinhan Bank s total lending to technology companies reached, on a cumulative basis, ₩12.3 trillion.

Furthermore, in response to an increasing level of consumer debt and amid concerns over the debt-servicing capacity of retail borrowers if interest rates were to rise, the Financial Services Commission announced in February 2014 plans to increase the proportion of fixed interest rate loans and installment principal repayment-based loans within the total housing loans extended by commercial banks (which loans have historically been, for the most part, variable interest rate loans with the entire principal being repaid at maturity, which is usually rolled over on an annual basis). According to this plan, the target proportion for fixed interest rate loans was set at 20%, 35%, 37.5% and 40% and the target proportion for installment principal repayment-based housing loans was set at 20%, 35%, 40% and 45%, each by the end of 2014, 2015, 2016 and 2017, respectively. Amid concerns about increasing household debt, the target proportion for fixed interest rate loans for 2016, 2017 and 2018 were increased to 40%, 45% and 47.5%, respectively, and the target proportion for installment principal repayment-based housing loans for 2016 and 2017 were increased to 45% and 55%, respectively, and maintained at 55% for 2018. In addition, an expanded tax deduction limit for interest repayment is granted for loans with maturity of 10 years or more (compared to 15 years or more prior to this plan). The Financial Services Commission announced that it would examine whether banks meet their targets on an annual basis.

In furtherance of the policy to expand the proportion of fixed rate housing loans, the Financial Services Commission implemented Relief Debt Conversion program from March 24 to March 27, 2015 and from March 30 to April 3, 2015, respectively, under which borrowers of eligible housing loans (namely, loans that have been in existence for one year or more since the original loan date, with no delinquency in the past six months, with principal amounts of ₩500 million or less and for houses valued at ₩900 million or less that are on a floating rate basis and/or an interest payment only basis) might convert such loans to new fixed rate loans in respect of which the borrowers would be required to repay the principal and interest in installment for a term of 10, 15, 20 or 30 years without a grace period, provided that the new loans pass the maximum loan-to-value ratio of 70% (irrespective of the location of the property) and the maximum debt-to-income ratio of 60% (only in respect of apartment units located in the greater Seoul metropolitan area, subject to certain exceptions). The borrowers were allowed to convert the original loans only at the banks that extended such loans. The banks holding the newly converted fixed rate loans are required to sell such loans to Korea Housing Finance

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Corporation, a government-controlled entity, which will then securitize such loans and issue mortgage-backed securities (backed by such loans) to be purchased by the banks who sold the loans in proportion to the amounts of the loans sold, and the banks will be required to hold such securities for a period of one year, after which the bank can sell or dispose of such securities in the market or otherwise. According to the Financial Services Commission, under this program, approximately 327,000 borrowers converted loans in the aggregate amount of ₩31.7 trillion to fixed rate loans, of which Shinhan Bank accounted for approximately 13.5%. Due in large part to such initiatives, fixed interest rate loans and installment principal repayment-based loans accounted for 44.6% and 49.1%, respectively, of the total housing loans extended by commercial banks in Korea as of September 2017, according to data published by the Government in November 2017. Fixed interest rate and installment principal repayment-based housing loans accounted for 44.9% and 49.1%, respectively, of the housing loans extended by Shinhan Bank as of December 31, 2017.

In the event that market interest rates increase from those applicable during this program s implementation in March and April 2015, we may experience valuation or realization losses on the mortgage-backed securities to be held by Shinhan Bank. Due to the prevailing interest rate environment and other market conditions, we also may not be able to sell or otherwise dispose of the mortgage backed securities in the market or otherwise in amounts or at prices commercially reasonable to us. In addition, as a result of this program we may incur additional costs from recalibrating our asset portfolio and asset-liability management policy. Any of these developments could adversely affect our results of operations and financial condition.

We, on a voluntary basis, may factor the existence of the Government s policies and encouragements into consideration in making loans although the ultimate decision whether to make loans remains with us and is made based on our internal credit approval procedures and risk management systems independently of Government policies. In addition, in tandem with providing additional loans to small- and medium-sized enterprises and low-income individuals, Shinhan Bank takes active steps to mitigate the potential adverse impacts from making bad loans to enterprises or individuals with high risk profiles as a result of such arrangement, such as by strengthening its loan review and post-lending monitoring processes. However, we cannot assure you that such arrangement did not or will not, or similar or other government-led initiatives in the future will not, result in a suboptimal allocation of our loan portfolio from a risk-reward perspective compared to what we would have allocated based on purely commercial decisions in the absence of such initiatives. The Government may implement similar or other initiatives in the future to spur the overall economy or encourage the growth of targeted industries or relief to certain segments of the population. Specifically, the Government may introduce lending-related initiatives or enforce existing ones in a heightened fashion during times when small- and medium-sized enterprises or low-income households on average are facing an increased level of financial distress or vulnerability due to an economic downturn, which makes lending to them in the volume and the manner suggested by the Government even riskier and less commercially desirable. Accordingly, such policy-driven lending may create enhanced difficulties for us in terms of risk management, deterioration of our asset quality and reduced earnings, compared to what would have been in the absence of such initiatives, which may have an adverse effect on our business, financial condition and results of operations.

The Government may also encourage investments in certain institutions in furtherance of policy objectives, and we may not recoup our investments therein in a timely or otherwise commercially reasonable manner.

In addition to targeted lending, the Government may from time to time encourage or request the financial institutions in Korea, including us and our subsidiaries, to make investments in, or provide other forms of financial support to, certain institutions in furtherance of the Government s policy objectives. In response thereto, we have made and will continue to make the ultimate decision on whether, how and to what extent we will comply with such encouragements or requests based on our internal risk assessment and in accordance with our risk management systems and policies. At the same time, as a leading member of the financial service industry in Korea and as a responsible corporate citizen we will also fully give due consideration to such encouragements or requests from the Government, especially in relation to the long-term benefit arising from furthering the policy objective of maintaining a sound financial system, even if complying with such requests may involve additional short-term costs and risks to a limited extent.

For example, to deal with a growing number of non-performing loans in the wake of the global financial crisis of 2008-2009, the Government sponsored the establishment of United Asset Management Company Ltd. (UAMCO) in October 2009 through capital contributions from six major policy and commercial banks, namely Shinhan Bank, Kookmin Bank, KEB Hana Bank, Industrial Bank of Korea, Woori Bank and Nonghyup Bank. The Government originally planned to dispose of UAMCO during 2015 and establish a new company that specializes in corporate restructuring, but the Government scrapped such plans and instead decided to reorganize UAMCO and expand its restructuring business. As part of an effort to strengthen its balance sheet, UAMCO received additional capital contributions in May 2016 from two new shareholders, Korea Development Bank and the Export-Import Bank of Korea, and two of its existing shareholders, Woori Bank and Nonghyup Bank. Shinhan Bank has committed to contribute ₩175 billion of capital to UAMCO, of which ₩85 billion has been contributed to date. As of the date hereof, Shinhan Bank holds a 14% equity interest in UAMCO, while seven other policy and commercial banks each hold interests ranging from 2% to 14%.

UAMCO seeks to achieve financial improvement of struggling companies through a wide range of restructuring programs, including debt restructuring, capital injection, asset sales, corporate reorganization, workouts and liquidation and bankruptcy proceedings and is the largest purchaser in Korea of non-performing financial assets generally. Shinhan Bank sold non-performing assets to UAMCO in the amount of ₩39.1 billion, ₩103.5 billion and ₩118.2 billion in 2015, 2016 and 2017, respectively. With an enlarged capital base following the recent capital contributions mentioned above, it is expected that UAMCO will play a more active role in the restructuring of the Korean corporate sector. The Government is also considering an amendment of the Financial Investment Services and Capital Markets Act of Korea to facilitate the business activities of UAMCO.

If UAMCO is successful in its expanded restructuring activities, it is anticipated that financial institutions including us will be able to further enhance their financial soundness by transferring more non-performing loans to UAMCO rather than directly engaging in the restructuring activities of the troubled borrowers. However, Shinhan Bank or other banks may be requested by the Government to make additional capital contributions or loans to UAMCO, which may entail unanticipated costs. Additionally, given the generally poor quality of our non-performing assets, there is no assurance that we will be able to sell such assets held by us to UAMCO on commercially reasonable terms and on a timely basis. Furthermore, there is no assurance that in furtherance of similar or other policy objectives, the Government may not request or otherwise encourage us or our subsidiaries to provide similar or other investments or provide other financial support for which we are not duly compensated or otherwise take up additional risk that we would not normally have undertaken, which may have an adverse effect on our business, financial condition and results of operations.

The level and scope of government oversight of our retail lending business, particularly regarding mortgage and home equity loans, may change depending on the economic or political climate.

Real estate comprises the most significant asset for a substantial number of households in Korea, and movements of housing prices have generally had a significant impact on the domestic economy. Accordingly, regulating housing prices, either in terms of attempting to stem actual or anticipated excessive speculation during times of a suspected housing price bubble and spur the pricing and/or volume of real estate transactions during times of a depressed real estate market by way of tax subsidy, guidelines to lending institutions or otherwise, has been a key policy initiative for the Government.

For example, during the early to mid-2000s, the Government adopted several regulatory measures, including in relation to retail banking, to stem a rise in speculation in real estate investments generally and in select areas. Some of the measures undertaken in the past include requiring financial institutions to impose stricter debt-to-income ratio and loan-to-value ratio requirements for mortgage loans for real property located in areas deemed to have engaged in a high level of speculation, raising property tax on real estate transactions for owners of multiple residential units, adopting a ceiling on the sale price of newly constructed housing units and recommending that commercial banks restrain from making further mortgage and home equity lending, among others. In addition, amid a prolonged slump in the housing market in Korea, in April 2013, the Government announced a Real Estate Comprehensive Countermeasure, which provides, among other things, for (i) reduced capital gains tax and (ii) exemption of acquisition tax for first-time homebuyers. In addition, in November 2013, the Government announced a permanent reduction in acquisition tax, with retrospective application from August 2013. Prior to such reduction, acquisition tax was assessed on a differentiated scale based on whether the homebuyer was purchasing a primary home or a secondary home, with the former being assessed an acquisition tax of 2% for the purchase of homes under ₩900 million and 4% for homes exceeding ₩900 million, and the latter being assessed an acquisition tax of 4% regardless of the price of the home. Under the new regulatory structure, the differentiated tax scale for primary homes and secondary homes is eliminated, and all homebuyers are assessed an acquisition tax of 1% for the purchase of homes under ₩600 million, 2% for homes exceeding ₩600 million but less than ₩900 million and 3% for homes exceeding ₩900 million. Furthermore, in February 2014, the Financial Services Commission announced plans to increase the proportion of fixed interest rate loans and installment principal repayment-based loans within the total housing loans extended by commercial banks. See The Government may encourage targeted lending to certain sectors in furtherance of policy objectives, and we may take this factor into account. In addition, in order to rationalize the regulations on the housing loans, the Financial Supervisory Service provided administrative instructions in July 2014, which have been extended and amended several times, that all financial institutions including banks under the Banking Act are subject to the maximum loan-to-value ratio of 70% (irrespective of the location of the property, subject to certain exceptions) and the maximum debt-to-income ratio of 60% (only in respect of apartment units located in the greater Seoul metropolitan area, subject to certain exceptions). The above administrative instructions have been replaced by the Regulation on the Supervision of the Banking Business and the Detailed Regulation on the Supervision of the Banking Business reflecting the tightened measures as discussed below. In November 2016, amid concerns about increasing household debt, the Government announced another Real Estate Comprehensive Countermeasure requiring property buyers in Seoul to retain ownership for a longer period of time and increasing down payments to be made on the property. In January 2017, in order to modernize credit review methods and stabilize the management of household debt, the Financial Services Commission announced the planned introduction of a debt service ratio and a new debt-to-income ratio. The new debt-to-income ratio, which has been implemented beginning January 31, 2018 reflects (i) both principal and interest payments on the applicable mortgage and home equity loan and existing mortgage and home equity loans and (ii) interest payments on other loans. Previously, debt-to-income ratio had only reflected (i) both principal and interest payments on the applicable mortgage and home equity loan and (ii) interest payments on existing mortgage and home equity loans. Debt service ratios reflect principal and interest payments on both the applicable loan and other loans and are expected to be introduced on a trial basis as a self-regulatory reference index beginning on March 26, 2018, with full implementation expected to take place in October 2018. The new debt-to-income ratios will be used as the primary reference index in the evaluation and approval process for mortgage and home equity loans, and debt service ratios, once fully implemented, are expected to be used as a supplementary reference index providing additional limits on mortgage and home equity loans.

On August 2, 2017, the Government unveiled a tighter set of real estate market measures aimed at taming speculation and deterring the rise of housing prices. Pursuant to the measures, beginning August 3, 2017, Seoul, Sejong Special Self-Governing City and Gwacheon were named overheated speculative districts, with the loan limits of those buying homes there to be tightened to 40% of their property value from 60%. The maximum debt-to-income ratio will be capped at 40% from 50%. Eleven districts in Seoul and Sejong Special Self-Governing City have also been designated speculative districts subject to higher taxes and tougher regulations. The August 2, 2017 measures come after President Moon Jae-in administration s first countermeasures, unveiled on June 19, 2017, which were designed to prevent the resale of home purchasing rights of real estate assets in Seoul while tightening the bars for maximum loan-to-value ratio for home buyers to 60% from 70% and maximum debt-to-income ratio to 50% from 60% in the regions designated as adjustment targeted areas (comprised of Seoul, Sejong Special Self-Governing City, seven cities in Gyeonggi Province and seven boroughs in Busan Metropolitan City). However, the new lending limits, which became effective on July 3, 2017, failed to halt the surge in housing prices, thus leading to the more stringent measures announced on August 2, 2017. Currently, loan-to-value ratios and new debt-to-income ratios in overheated speculative districts, speculative districts, adjustment targeted areas and other regions are regulated by the Regulation on the Supervision of the

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Banking Business and the Detailed Regulation on the Supervision of the Banking Business. These renewed measures are expected to lead to a decline in the overall volume of home mortgage loans but may result in an increase in long-term deposits loans required for house rentals and lending to borrowers with high credit profiles.

Pursuant to the Regulation on the Supervision of the Banking Business, the Bank must maintain a loan to deposit ratio of no more than 100%. Currently, in calculating the loan to deposit ratio, there is no differentiation between retail loans and corporate loans. However, the Regulation on the Supervision of the Banking Business is expected to be amended during the first quarter of 2018 to provide that, beginning from the second half of 2018, in calculating such loan to deposit ratio, retail loans and corporate loans will be weighed differently, with retail loans subject to a multiple of 115% and corporate loans subject to a multiple of 85%, thereby increasing the impact of retail loans and reducing the impact of corporate loans in calculating such ratio. Additionally, the Detailed Regulation on the Supervision of the Banking Business is also expected to be amended during the first quarter of 2018 to provide for a weighted multiple to be applied to mortgage and home equity loans where the loan-to-value exceeds 60% in determining required minimum total capital (BIS) ratio. Further, the Regulation on the Supervision of the Banking Business is expected to be amended during the second half of 2018 to introduce an additional countercyclical capital buffer requirement that specifically addresses the increase in credit in the retail sector. This is in addition to and separate from the existing general countercyclical capital buffer requirements that take into account the degree of increase in credit generally relative to the gross domestic product. The Detailed Regulation on the Supervision of the Banking Business is also expected to be amended during the second half of 2018 to add concentration of risk in the retail sector as an additional criteria when the FSS evaluates the risk management systems of Korean banks.

There is no assurance that Government measures will achieve their intended results. While any Government measure that is designed to stimulate growth in the real estate sector may result in growth of, and improved profitability for, our retail lending business (particularly with respect to mortgage and home equity loans) at least for the short term, such measure could also result in unintended consequences, including potentially excessive speculation resulting in a bubble for the Korean real estate market and a subsequent market crash. In contrast, any Government measure changing the direction of its stimulative measures (for example, in order to preemptively curtail an actual or anticipated bubble in the real estate market) may result in a contraction of the real estate market, a decline in real estate prices and consequently, a reduction in the growth of, and profitability for, our retail and/or other lending businesses, as well as otherwise have an adverse effect on our business, financial condition and results of operations or profitability. See Risks Relating to Our Banking Business A decline in the value of the collateral securing our loans or our inability to fully realize the collateral value may adversely affect our credit portfolio.

We engage in limited settlement transactions involving Iran which may subject us to legal or reputational risks.

The U.S. Department of the Treasury s Office of Foreign Assets Control (OFAC) administers and enforces certain laws and regulations (OFAC Sanctions) that impose restrictions upon U.S. persons with respect to dealings with or related to certain countries, governments, entities and individuals that are the subject of OFAC Sanctions, including Iran, and maintains a list of specially designated nationals (the SDN List), whose assets are blocked and with whom U.S. persons are generally prohibited from dealing. Non-U.S. persons can be held liable for violations of OFAC Sanctions on various legal grounds, such as causing violations by U.S. persons by engaging in transactions completed in part in the United States. The European Union also enforces certain laws and regulations that impose restrictions upon nationals and entities of, and business conducted in, member states with respect to activities or transactions with certain countries, governments, entities and individuals that are the subject of such laws and regulations. The United Nations Security Council and other governmental entities also impose similar sanctions.

In August 2016, the government of South Korea authorized Shinhan Bank to act as a settlement bank for Euro-denominated transactions between South Korean and Iranian businesses. Prior to the granting of this

permission, payments for business activities were settled only in Korean Won and we did not participate in such settlements. As of December 31, 2017, Shinhan Bank has processed ten such transactions that has resulted in a minimal amount of revenue. We expect that the volume of these transactions and any revenue gained from them, if any, will continue to be minimal for the foreseeable future. Since August 2017, Shinhan Bank has ceased processing any such transactions. We are committed to engaging only in lawful activities and in obeying all relevant OFAC and European Union sanctions but cannot guarantee that actions taken by our employees will not violate such sanctions. Moreover, the relaxation of US and European Union sanctions undertaken pursuant to the Joint Comprehensive Plan of Action (JCPOA) may snap-back into place in the event that Iran fails to comply with its commitments under the JCPOA. As such, we cannot predict with a reasonable degree of certainty whether our Euro-denominated, Iran-related settlement business may become sanctionable. Additionally, changes in U.S. policy regarding Iran may also result in our dealings with Iran becoming sanctionable. Consequently, our activities related to Iran subject us to potential legal or reputational risks.

Risks Relating to Korea

Unfavorable financial and economic conditions in Korea and globally may have a material adverse impact on our asset quality, liquidity and financial performance.

We are incorporated in Korea, where most of our assets are located and most of our income is generated. As a result, we are subject to political, economic, legal and regulatory risks specific to Korea, and our business, results of operations and financial condition are substantially dependent on developments relating to the Korean economy. As Korea s economy is highly dependent on the health and direction of the global economy, and investors reactions to developments in one country can have adverse effects on the securities price of companies in other countries, we are also subject to the fluctuations of the global economy and financial markets. Factors that determine economic and business cycles in the Korean or global economy are for the most part beyond our control and inherently uncertain. In addition to discussions of recent developments regarding the global economic and market uncertainties and the risks relating to us as provided elsewhere in this section, factors that could have an adverse impact on Korea s economy in the future include, among others:

- continued volatility or deterioration in Korea s credit and capital markets;

- difficulties in the financial sectors in Europe, China and elsewhere and increased sovereign default risks in select countries and the resulting adverse effects on the global financial markets;

- declines in consumer confidence and a slowdown in consumer spending and corporate investments;

- adverse changes or volatility in foreign currency reserve levels, commodity prices (including oil prices), exchange rates (including fluctuation of the U.S. Dollar, the Euro or the Japanese Yen exchange rates or revaluation of the Chinese Renminbi and the overall impact of the referendum in the United Kingdom in June 2016, in which the majority of voters voted in favor of an exit from the European Union (Brexit) on the value of the Korean Won), interest rates, inflation rates or stock markets;

increasing levels of household debt;

increasing delinquencies and credit defaults by retail and small- and medium-sized enterprise borrowers;

continuing adverse conditions in the economies of countries and regions that are important export markets for Korea, such as the United States, Europe, Japan and China, or in emerging market economies in Asia or elsewhere, as well as increased uncertainty in the wake of Brexit;

the economic impact of any pending or future free trade agreements;

social and labor unrest;

decreases in the market prices of Korean real estate;

a decrease in tax revenue and a substantial increase in the Government s expenditures for fiscal stimulus measures, unemployment compensation and other economic and social programs that, together, would lead to an increased government budget deficit;

financial problems or lack of progress in the restructuring of Korean business groups, other large troubled companies, their suppliers or the financial sector;

loss of investor confidence arising from corporate accounting irregularities and corporate governance issues concerning certain Korean business groups;

increases in social expenditures to support an aging population in Korea or decreases in economic productivity due to the declining population size in Korea;

geopolitical uncertainty and risk of further attacks by terrorist groups around the world, including the actions of the so-called Islamic State ;

the occurrence of severe health epidemics in Korea and other parts of the world, including the recent Ebola, Middle East Respiratory Syndrome (MERS) and Zika virus outbreaks;

deterioration in economic or diplomatic relations between Korea and its trading partners or allies, including deterioration resulting from territorial or trade disputes or disagreements in foreign policy such as the recent diplomatic tension between Korea and China with respect to the deployment of the Terminal High Altitude Area Defense (THAAD) system in Korea and trade disputes between Korea and the United States with respect to the imposition of anti-dumping duties on Korean steel, washing machines, transformers and solar panels;;

political uncertainty, or increasing strife among or within political parties in Korea, and political gridlock within the government or in the legislature, which prevents or disrupts timely and effective policy making;

hostilities or political or social tensions involving oil-producing countries in the Middle East and North Africa and any material disruption in the global supply of oil or sudden increase in the price of oil;

political or social tensions involving Russia and any resulting adverse effects on the global supply of oil or the global financial markets;

the occurrence of natural or man-made disasters in Korea (such as the sinking of the Sewol ferry in April 2014, which significantly dampened consumer sentiment in Korea for months) and other parts of the world, particularly in trading partners of Korea; and an increase in the level of tensions or an outbreak of hostilities between North Korea and Korea or the United States.

Any future deterioration of the Korean economy could have an adverse effect on our business, financial condition and results of operations.

Tensions with North Korea could have an adverse effect on us, the price of our common shares and our American depositary shares.

Relations between Korea and North Korea have been tense throughout Korea s modern history. The level of tension between the two Koreas has fluctuated and may increase abruptly as a result of current and future events. In particular, since the death of Kim Jong-il in December 2011, there has been increased uncertainty with respect to the future of North Korea s political leadership and concern regarding its implications for political and economic stability in the region. Although Kim Jong-il s third son, Kim Jong-eun has assumed power as his father s designated successor, the long-term outcome of such leadership transition remains uncertain. In February 2017, Kim Jong-eun s half-brother, Kim Jong-nam, was reported to have been assassinated in an international airport in Malaysia.

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In addition, there continues to be heightened security tension in the region stemming from North Korea s hostile military and diplomatic actions, including in respect of its nuclear weapons and long-range missile programs. Some examples from recent years include the following:

North Korea renounced its obligations under the Nuclear Non-Proliferation Treaty in January 2003 and conducted three rounds of nuclear tests between October 2006 to February 2013, which increased tensions in the region and elicited strong objections worldwide. On January 6, 2016, North Korea announced that it had successfully conducted its first hydrogen bomb test, hours after international monitors detected a 5.1 magnitude earthquake near a known nuclear testing site in the country. The alleged test followed a statement made in the previous month by Kim Jong-un, who claimed that North Korea had developed a hydrogen bomb. On February 7, 2016, North Korea launched a rocket, claimed by them to be carrying a satellite intended for scientific observation. The launch was widely suspected by the international community to be a cover for testing a long-range missile capable of carrying a nuclear warhead. On February 18, 2016, U.S. President Barack Obama signed into law mandatory sanctions on North Korea to punish it for its recent nuclear and missile tests, human rights violations and cyber crimes. The bill, which marks the first measure by the United States to exclusively target North Korea, is intended to seize the assets of anyone engaging in business related to North Korea s weapons program, and authorizes US$50 million over five years to transmit radio broadcasts into the country and support humanitarian assistance projects. On March 2, 2016, the United Nations Security Council voted unanimously to adopt a resolution to impose sanctions against North Korea, which include inspection of all cargo going to and from North Korea, a ban on all weapons trade and the expulsion of North Korean diplomats who engage in illicit activities. Also, on March 4, 2016, the European Union announced that it would expand its sanctions on North Korea, adding additional companies and individuals to its list of sanction targets. In September 2016, North Korea announced that it had successfully tested a nuclear warhead that could be mounted on ballistic missiles. In response, the Government condemned the test, and on November 30 2016, the United Nations Security Council unanimously passed a resolution imposing additional sanctions on North Korea including an annual cap on North Korea s exports of coal and a prohibition on exports of non-ferrous metals such as copper, nickel, silver and zinc. In March 2017, North Korea launched four midrange missiles aimed at the U.S. military bases in Japan, which landed off the east coast of the Korean peninsula. The United Nations Security Council condemned the launches and expressed its plan to adopt additional measures against the regime. On April 4, 2017, one day before the first meeting between U.S. President Donald Trump and Chinese President Xi Jinping, North Korea launched a ballistic missile which landed off the east coast of the Korean peninsula. In addition to the United Nations Security Council s condemnation, representatives of the Government and China expressed their plan to impose stronger sanctions on North Korea. On April 15, 2017, North Korea launched another missile which failed when it exploded immediately after liftoff. In response, the Government condemned the launch as a violation of the resolution of the United Nations Security Council and warned that North Korea would have to face punitive consequences if this leads to a future nuclear experiment or launch of an intercontinental ballistic missile. In July 2017, North Korea conducted two intercontinental ballistic missile tests which displayed further development of its long-range ballistic missile capabilities that potentially enable it to target certain areas of the United States as well as other neighboring countries in the Asia-Pacific region. In response, the United Nations Security Council unanimously adopted stronger sanctions against North Korea. In August 2017, North Korea announced its plan to launch four ballistic missiles targeting Guam, resulting in heightened diplomatic tensions between North Korea and the United States. In September 2017, North Korea detonated a sixth nuclear bomb, the most powerful weapon that North Korea has ever tested. Such detonation further heightened diplomatic tensions between North Korea and other nations. Each of the United Nations, the United States and the European Union adopted additional sanctions against North Korea. Spain, Mexico, Peru and Kuwait expelled from their respective territories the ambassadors of North Korea. In November 2017, North Korea conducted a test launch of another intercontinental ballistic missile, which, due to its improved size, power and range of distance, may potentially enable North Korea to target the United States mainland.

In August 2015, two Korean soldiers were injured in a landmine explosion while on routine patrol of the southern side of the demilitarized zone. Claiming the landmines were set by North Koreans, the Korean army re-initiated its propaganda program toward North Korea utilizing loudspeakers near the demilitarized zone. In retaliation, the North Korean army fired artillery rounds on the loudspeakers, resulting in the highest level of military readiness for both sides. High-ranking officials from North Korea and Korea subsequently met for discussions intending to diffuse military tensions and released a joint statement whereby, among other things, North Korea expressed regret over the landmine explosions that wounded the Korean soldiers.

From time to time, North Korea has fired short- to medium-range missiles from the coast of the Korean peninsula into the sea. Recently in March 2015, North Korea fired seven surface-to-air missiles into waters off its east coast in apparent protest of annual joint military exercises being held by Korea and the United States.

In December 2013, Jang Sung-taek, a relative of Kim Jong-un, who was widely speculated to be the second in command after Kim Jong-un, was executed on charges of sedition. There are reports that such development may cause further political and social instability in North Korea and/or adoption of more hostile policies that could engender further friction with North Korea and the rest of the world.

In April 2013, North Korea blocked Koreans from entering the industrial complex in the border city of Kaesong. In the same month, the United States deployed nuclear-capable carriers in the Korean air and sea space. In September 2013, however, Korea and North Korea reached an agreement and resumed operation of the Kaesong Industrial Complex. In February 2014, the U.S. Congressional Research Service reported that Korea s approach toward the expansion and internationalization of the Kaesong Industrial Complex could conflict with U.S. legislative efforts to expand its sanctions on North Korea. On February 10, 2016, in retaliation of North Korea s recent launch of a long-range rocket, Korea announced that it would halt its operations of the Kaesong Industrial Complex to impede North Korea s utilization of funds from the industrial complex to finance its nuclear and missile programs. In response, North Korea announced on February 11, 2016 that it would expel all Korean employees from the industrial complex and freeze all Korean assets in the complex. All 280 Korean workers present at Kaesong left hours after the announcement by North Korea, and the complex remains closed as of the date hereof.

In March 2013, North Korea stated that it had entered a state of war with Korea, declaring the 1953 armistice invalid, and put its artillery at the highest level of combat readiness to protest the Korea-United States allies military drills and additional sanctions imposed on North Korea for its missile and nuclear tests.

North Korea s economy also faces severe challenges, including severe inflation and food shortages, which may further aggravate social and political tensions within North Korea. In addition, reunification of Korea and North Korea could occur in the future, which would entail significant economic commitment and expenditure by Korea that may outweigh any resulting economic benefits of reunification.

There can be no assurance that the level of tension on the Korean peninsula will not escalate in the future or that the political regime in North Korea may not suddenly collapse. Any further increase in tension or uncertainty relating to the military, political or economic stability in the Korean peninsula, including a breakdown of diplomatic negotiations over the North Korean nuclear program, occurrence of military hostilities, heightened concerns about the stability of

North Korea s political leadership or its actual collapse, a leadership crisis, a breakdown of high-level contacts or accelerated reunification could have a material adverse effect on our business, financial condition and results of operations, as well as the price of our common shares and our American depositary shares.

Risks Relating to Our American Depositary Shares

There are restrictions on withdrawal and deposit of common shares under the depositary facility.

Under the deposit agreement, holders of shares of our common stock may deposit those shares with the depositary bank s custodian in Korea and obtain American depositary shares, and holders of American depositary shares may surrender American depositary shares to the depositary bank and receive shares of our common stock. However, under current Korean laws and regulations, the depositary bank is required to obtain our prior consent for the number of shares to be deposited in any given proposed deposit which exceeds the difference between (1) the aggregate number of shares deposited by us for the issuance of American depositary shares (including deposits in connection with the initial and all subsequent offerings of American depositary shares and stock dividends or other distributions related to these American depositary shares) and (2) the number of shares on deposit with the depositary bank at the time of such proposed deposit. We have consented to the deposit of outstanding shares of common stock as long as the number of American depositary shares outstanding at any time does not exceed 40,432,628. As a result, if you surrender American depositary shares and withdraw shares of common stock, you may not be able to deposit the shares again to obtain American depositary shares.

Ownership of our shares is restricted under Korean law.

Under the Financial Holding Companies Act, any single shareholder (together with certain persons in a special relationship with such shareholder) may acquire beneficial ownership of up to 10% of the total issued and outstanding shares with voting rights of a bank holding company controlling national banks such as us. In addition, any person, except for a non-financial business group company (as defined below), may acquire in excess of 10% of the total voting shares issued and outstanding of a financial holding company which controls a national bank, provided that a prior approval from the Financial Services Commission is obtained each time such person s aggregate holdings exceed 10% (or 15% in the case of a financial holding company controlling regional banks only), 25% or 33% of the total voting shares issued and outstanding of such financial holding company. The Government and the Korea Deposit Insurance Corporation are exempt from this limit. Furthermore, certain non-financial business group companies (i.e., (i) any same shareholder group with aggregate net assets of all non-financial business companies belonging to such group of not less than 25% of the aggregate net assets of all members of such group; (ii) any same shareholder group with aggregate assets of all non-financial business companies belonging to such group of not less than ₩2 trillion; or (iii) any mutual fund in which a same shareholder group identified in (i) or (ii) above owns more than 4% of the total shares issued and outstanding of such mutual fund) may not acquire beneficial ownership in us in excess of 4% of our outstanding voting shares, provided that such non-financial business group companies may acquire beneficial ownership of up to 10% of our outstanding voting shares with the approval of the Financial Services Commission under the condition that such non-financial business group companies will not exercise voting rights in respect of such shares in excess of the 4% limit. See Item 4.B. Business Overview Supervision and Regulation Principal Regulations Applicable to Financial Holding Companies Restrictions on Financial Holding Company Ownership. To the extent that the total number of shares of our common stock that you and your affiliates own together exceeds these limits, you will not be entitled to exercise the voting rights for the excess shares, and the Financial Services Commission may order you to dispose of the excess shares within a period of up to six months. Failure to comply with such an order would result in a fine of up to ₩50 million, plus an additional charge of up to 0.03% of the book value of such shares per day until the date of disposal.

Holders of our ADSs will not have preemptive rights in certain circumstances.

The Korean Commercial Code and our articles of incorporation require us, with some exceptions, to offer shareholders the right to subscribe for new shares in proportion to their existing ownership percentage whenever new shares are issued. If we offer any rights to subscribe for additional shares of our common stock or any rights of any other nature, the depositary bank, after consultation with us, may make the rights available to you or use reasonable efforts to dispose of the rights on your behalf and make the net proceeds available to you. The depositary bank, however, is not required to make available to you any rights to purchase any additional shares unless it deems that doing so is lawful and feasible and:

a registration statement filed by us under the U.S. Securities Act of 1933, as amended, is in effect with respect to those shares; or

the offering and sale of those shares is exempt from or is not subject to the registration requirements of the U.S. Securities Act.

We are under no obligation to file any registration statement with the U.S. Securities and Exchange Commission. If a registration statement is required for you to exercise preemptive rights but is not filed by us, you will not be able to exercise your preemptive rights for additional shares and you will suffer dilution of your equity interest in us.

Holders of our ADSs will not be able to exercise dissent and appraisal rights unless they have withdrawn the underlying shares of our common stock and become our direct stockholders.

Under Korean law, in some limited circumstances, including the transfer of the whole or any significant part of our business and the merger or consolidation of us with another company, dissenting stockholders have the right to require us to purchase their shares under Korean law. However, under our deposit agreement, holders of our American depositary shares do not have, and may not instruct the depositary as to the exercise of, any dissenter s rights provided to the holders of our common shares under Korean law. Therefore, if holders of our American depositary shares wish to exercise dissenting rights, they must withdraw the underlying common stock from the American depositary shares facility (and incur charges relating to that withdrawal) and become our direct stockholders prior to the record date of the stockholders meeting at which the relevant transaction is to be approved, in order to exercise dissent and appraisal rights.

The market value of your investment in our ADSs may fluctuate due to the volatility of the Korean securities market.

Our common stock is listed on the KRX KOSPI Division of the Korea Exchange, which has a smaller market capitalization and is more volatile than the securities markets in the United States and many European countries. The market value of ADSs may fluctuate in response to the fluctuation of the trading price of shares of our common stock on the Stock Market Division of the Korea Exchange. The Stock Market Division of the Korea Exchange has experienced substantial fluctuations in the prices and volumes of sales of listed securities and the Stock Market Division of the Korea Exchange has prescribed a fixed range in which share prices are permitted to move on a daily basis. Like other securities markets, including those in developed markets, the Korean securities market has experienced problems including market manipulation, insider trading and settlement failures. The recurrence of these or similar problems could have a material adverse effect on the market price and liquidity of the securities of Korean companies, including our common stock and ADSs, in both the domestic and the international markets.

The Government has the potential ability to exert substantial influence over many aspects of the private sector business community, and in the past has exerted that influence from time to time. For example, the Government has promoted mergers to reduce what it considers excess capacity in a particular industry and has also encouraged private companies to publicly offer their securities. Similar actions in the future could have the effect of depressing or boosting the Korean securities market, whether or not intended to do so. Accordingly, actions by the government, or the perception that such actions are taking place, may take place or has ceased, may cause sudden movements in the market prices of the securities of Korean companies in the future, which may affect the market price and liquidity of our common stock and ADSs.

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Your dividend payments and the amount you may realize upon a sale of your ADSs will be affected by fluctuations in the exchange rate between the U.S. Dollar and the Won.

Investors who purchase the American depositary shares will be required to pay for them in U.S. Dollars. Our outstanding shares are listed on the Korea Exchange and are quoted and traded in Won. Cash dividends, if any, in respect of the shares represented by the American depositary shares will be paid to the depositary bank in Won and then converted by the depositary bank into U.S. Dollars, subject to certain conditions. Accordingly, fluctuations in the exchange rate between the Won and the U.S. Dollar will affect, among other things, the amounts a registered holder or beneficial owner of the American depositary shares will receive from the depositary bank in respect of dividends, the U.S. Dollar value of the proceeds which a holder or owner would receive upon sale in Korea of the shares obtained upon surrender of American depositary shares and the secondary market price of the American depositary shares.

If the Government deems that certain emergency circumstances are likely to occur, it may restrict the depositary bank from converting and remitting dividends in Dollars.

If the Government deems that certain emergency circumstances are likely to occur, it may impose restrictions such as requiring foreign investors to obtain prior Government approval for the acquisition of Korean securities or for the repatriation of interest or dividends arising from Korean securities or sales proceeds from disposition of such securities. These emergency circumstances include any or all of the following:

- sudden fluctuations in interest rates or exchange rates;
- extreme difficulty in stabilizing the balance of payments; and
- a substantial disturbance in the Korean financial and capital markets.

The depositary bank may not be able to secure such prior approval from the government for the payment of dividends to foreign investors when the Government deems that there are emergency circumstances in the Korean financial markets.

Other Risks

We are generally subject to Korean corporate governance and disclosure standards, which differ in significant respects from those in other countries.

Companies in Korea, including us, are subject to corporate governance standards applicable to Korean public companies which differ in many respects from standards applicable in other countries, including the United States. As a reporting company registered with the Securities and Exchange Commission and listed on the New York Stock Exchange, we are, and in the future will be, subject to certain corporate governance standards as mandated by the Sarbanes-Oxley Act of 2002. However, foreign private issuers, including us, are exempt from certain corporate governance requirements under the Sarbanes-Oxley Act or under the rules of the New York Stock Exchange. For significant differences, see Item 16G. Corporate Governance. There may also be less publicly available information about Korean companies, such as us, than is regularly made available by public or non-public companies in other countries. Such differences in corporate governance standards and less public information could result in less than satisfactory corporate governance practices or disclosure to investors in certain countries.

You may not be able to enforce a judgment of a foreign court against us.

We are a corporation with limited liability organized under the laws of Korea. All or substantially all of our directors and officers and other persons named in this annual report reside in Korea, and all or a substantial portion of the assets of our directors and officers and other persons named in this annual report and substantially all of our assets are located in Korea. As a result, it may not be possible for holders of the American depository shares to effect service of process within the United States, or to enforce against them or us in the United States judgments obtained in United States courts based on the civil liability provisions of the federal securities laws of the United States. There is doubt as to the enforceability in Korea, either in original actions or in actions for enforcement of judgments of United States courts, of civil liabilities predicated on the United States federal securities laws.

We may become a passive foreign investment company (PFIC), which could result in adverse U.S. tax consequences to U.S. investors.

Based upon the past and projected composition of our income and valuation of our assets, including goodwill, we do not believe that we were a PFIC for 2017, and we do not expect to be a PFIC in 2018 or to become one in the foreseeable future, although there can be no assurance in this regard. If, however, we become a PFIC, such characterization could result in adverse U.S. tax consequences to you if you are a U.S. investor. For example, if we become a PFIC, our U.S. investors will become subject to increased tax liabilities under U.S. tax laws and regulations and will become subject to burdensome reporting requirements. Our PFIC status is determined on an annual basis and depends on the composition of our income and assets. Specifically, we will be classified as a PFIC for U.S. tax purposes if either: (i) 75% or more of our gross income in a taxable year is passive income, or (ii) the average percentage of our assets by value in a taxable year which produce or are held for the production of passive income (which generally includes cash) is at least 50%. Special rules treat certain income earned by a non-U.S. corporation engaged in the active conduct of a banking business as non-passive income. See Item 10.E. Taxation Certain United States Federal Income Tax Consequences Passive Foreign Investment Company Rules. We cannot assure you that we will not be a PFIC for 2018 or any future taxable year.

ITEM 4. *INFORMATION ON THE COMPANY*

ITEM 4.A. History and Development of the Company

Introduction

We are one of the leading financial institutions in Korea in terms of total assets, revenues, profitability and capital adequacy, among others. Incorporated on September 1, 2001, we are the first privately-held financial holding company to be established in Korea. Since inception, we have developed and introduced a wide range of financial products and services in Korea and aimed to deliver comprehensive financial solutions to clients through a convenient one-portal network. According to reports by the Financial Supervisory Service, we are the second largest financial services provider in Korea (as measured by consolidated total assets as of December 31, 2017) and operate the second largest banking business (as measured by consolidated total bank assets as of December 31, 2017) and the largest credit card business (as measured by the total credit purchase volume in 2017) in Korea.

We have experienced substantial growth through several mergers and acquisitions. Most notably, our acquisition of Chohung Bank in 2003 has enabled us to have the second largest banking operations in Korea. In addition, our acquisition in March 2007 of LG Card, the then largest credit card company in Korea, has enabled us to have the largest credit card operations in Korea and significantly expand our non-banking business capacity so as to achieve a balanced business portfolio.

We currently have 14 direct subsidiaries and 25 indirect subsidiaries offering a wide range of financial products and services, including commercial banking, corporate banking, private banking, credit card, asset management, brokerage and insurance services. We believe that such breadth of services will help us to meet the diversified needs of our present and potential clients. We currently serve approximately 18.6 million active customers, which we believe is the largest customer base in Korea, through approximately 26,443 employees at approximately 1,435 network branches group-wide. While substantially all of our revenues have been historically derived from Korea, we aim to serve the needs of our customers through a global network of 178 offices in the

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United States, Canada, the United Kingdom, Japan, the People s Republic of China, Germany, India, Australia, Hong Kong, Vietnam, Cambodia, Kazakhstan, Singapore, Mexico, Uzbekistan, Myanmar, Poland, Indonesia, the Philippines and the United Arab Emirates.

Our registered office and corporate headquarters are located at 20, Sejong-daero 9-gil, Jung-gu, Seoul, Korea 04513 and our telephone number is +822 6360 3000.

Our Strategy

Since our inception in 2001, we have pursued the following objectives as the core of our long-term strategy: (i) balanced growth in our banking and non-banking businesses, (ii) continued creation of value by identifying new business opportunities and gaining a competitive edge through differentiating our business model from that of our competitors, and (iii) becoming the market leader in Korea and a world-class financial holding company through enhancement of our management systems and core competencies.

Following the global financial crisis that began in the second half of 2008, a new set of challenges for financial service providers such as us and our subsidiaries has emerged in the form of a new normal in the business environment with the following general trends: (i) demographic changes due to declining birth rates and increasingly aging population, (ii) prolonged periods of low growth and low interest rates, (iii) rapid innovation in the financial industry as a result of advancements in information and communication technology (ICT) and digital finance technologies, and (iv) amplifying effects of challenges and opportunities globally. Constant changes in the global markets demand that financial service providers consistently develop new financial trends, ensure customer satisfaction by offering competitive products and services in the continued low-interest rate environment, maintain a sound infrastructure that can withstand external shocks, and enhance social responsibility and accountability.

In recognition of these trends in our business environment and in order to realize our long-term vision of becoming a world-class financial group, we have recently adopted a near term mission, the 2020 SMART Project, of (i) solidifying our position as a leading financial group in Korea and (ii) building the foundation for success in the Asian market. We aim to become Korea s number one financial brand and, at the same time, achieve meaningful growth in overseas markets by expanding into regions with high growth potential.

More specifically, our key strategic priorities currently include the following:

Diversification of future growth strategies. By implementing our organic and inorganic growth strategies together, we will strive to strengthen the competitiveness of our group s strategic businesses including global investment banking, wealth management, investment trusts and real estate, as well as expand our non-banking and global business portfolio.

Lead value creation through creative innovation. By generating new ideas that drive global trends, we will strive for a synergy that increases value for both our customers and the Group. In particular, we plan to implement innovative approaches in emerging business sectors such as digital finance, retirement planning and real estate portfolio management, so that we can increase the value of our customers assets and develop new drivers of growth for the future.

Accelerate our digital transformation. By offering a distinct customer experience through innovative channels and enhancing the competitiveness of our digital products and services, we will strive to further develop our digital competitiveness in all value chain areas. In addition, we will apply our digital technology in increasing the efficiency and automation of our operation processes. We will strategically respond to disruptive digital business models in our markets and cultivate and collaborate with innovative domestic and overseas startups to build cutting edge digital ecosystems and platforms.

Secure new opportunities for growth with global operations. We will continue to expand into global high growth markets to procure a strong source of growth. To pursue meaningful advancement and move beyond a simple survey of opportunities, we plan to explore various new market entry strategies while establishing a firm presence in local markets. We will continue to grow our non-banking business portfolio, increase the profitability of our overseas banking entities and expand our presence in key markets.

Implement integration and build One Shinhan system by reforming the Group s operating system. We will reform our operating system to (i) provide our customers with a single portal that integrates multiple business lines and (ii) continue developing integrated financial products and services. Through such strategies, we intend to enhance the group s operational efficiency and proactively accommodate customers needs regarding total financial service packages.

Optimize risk management preemptively in preparation for low economic growth and external shock. In order to attain sustainable growth in an environment where risk factors are amplified and the threat of financial crises lingers, we plan to take precautionary measures to address negative external factors before they arise. Moreover, we will enhance our risk management system and credit review models through the use of big data and a proactive crisis response system to prepare for potential volatility, uncertainty, complexity and ambiguity.

Establish a strong organizational culture based on the Shinhan Way. We will further upgrade our policies and operating system according to our value of future-oriented compassionate finance. We aim to further invigorate the group s creative and proactive culture while nurturing a new generation of leaders based on the Shinhan Way.

At the subsidiary level, we plan to implement the following strategies with respect to our core business lines:

in commercial banking, our primary objective is to challenge ourselves to reach a new level of excellence and solidifying our position as a leading bank. Commercial banking is our principal business line and has the highest level of profitability in Korea based on its strong risk management capacity. Equipped with an extensive branch network and a broad customer base, our commercial banking business serves as the key sales and distribution channel for the various financial products and services we provide. In 2018, we seek to solidify our brand and market position in a highly competitive commercial banking market by strengthening our competitiveness in areas of core competencies by further investing in Shinhan Bank s digital transformation initiative, creating country-specific models as part of our glocalization efforts, enhancing organizational capacity and strategic partnerships with non-banking companies through our client focused One Shinhan strategy, strategically reducing costs, rationalizing our distribution of resources including channels and personnel and seeking new sources of profit for sustainable growth. Our plan is to further optimize risk management to address the volatility of the business environment and to continue reinforcing our commercial banking operations high profitability and central role in strengthening group-wide synergy.

in the credit card business, our primary objective is to focus on establishing a business model that can respond and adapt to trends and changes in the future. With such goals, we will strive to preemptively address rapid developments in the technology environment such as fintech, mobile payment services and Internet-only banks and overcome the industry s low structural growth and weakened profitability. To this end, we plan to implement changes to our core business operations by strengthening our risk management capabilities and enhancing the capabilities of our personnel and organization in order to achieve a leading position in the credit card industry and accelerate our Digital First initiative. We also plan to boost our competitiveness in the mobile payment service market and increase strategic alliances based on our mobile platform. Additionally, through an overall expansion of our credit card business, we aim to diversify revenue models and become even more active in entering overseas markets. We also seek to bolster our customer service by solidifying our industry leadership in the credit card industry and improve profitability by utilizing our resources strategically.

in the securities business, our primary objective is to provide the best financial solutions, innovative products and services to our customers. We seek to solidify our position as a comprehensive financial investment service provider, providing leading brokerage and financial advisory services in Korea by continuing organic growth and fostering collaboration among group subsidiaries. In addition, we will continue to cultivate a customer-centric corporate culture. We will actively invest in channel innovation by incorporating our group collaboration efforts including the expansion of branches offering multiple services and accelerating our digital transition efforts. We will also enhance our specialized financial market capabilities by increasing our supply of trendsetting market products and strengthening our investment banking capabilities. Furthermore, to ensure reliable asset management for our customers, we plan to steadily update our risk management and customer profit and wealth management capabilities including hedge funds.

in the life insurance business, our primary objective is to attain key competitive capabilities to pioneer the new market order. To establish our life insurance program as the standard for the industry, we aim to broaden the reach of our operations to all business sectors and strengthen our execution capacity. Our strategy is to become a leader in the life insurance industry in terms of products, services and profits by offering a differentiated and unique product portfolio, implementing a digital transformation focused business model, strategically reducing costs and rationalizing our distribution of resources including channels and personnel. In 2018, we will focus on profit-based product offerings, optimizing our wealth management capabilities and implementing changes to our operations system in preparation of the implementation of IFRS 17, which is expected to become effective beginning 2021.

Our History and Development

On September 1, 2001, we were formed as a financial holding company under the Financial Holding Companies Act, as a result of acquiring all of the issued shares of the following four entities from their former shareholders in exchange for shares of our common stock: (i) Shinhan Bank, a nationwide commercial bank listed on the Korea Exchange, (ii) Shinhan Securities Co., Ltd., a securities brokerage company listed on the Korea Exchange, (iii) Shinhan Capital Co., Ltd., a leasing company listed on the Korea Exchange Korean Securities Dealers Automated Quotations (KRX KOSDAQ), and (iv) Shinhan Investment Trust Management Co., Ltd., a privately held investment trust management company. On September 10, 2001, the common stock of our holding company was listed on what is currently the KRX KOSPI Market.

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Since our inception, we have expanded our operations, in large part, through strategic acquisitions or formation of joint ventures. Our key acquisitions and joint venture formations are described as below:

Date of Acquisition	Entity	Principal Activities	Method of Establishment
April 2002	Jeju Bank	Regional banking	Acquisition from Korea Deposit Insurance Corporation
July 2002	Shinhan Investment Corp.[1]	Securities and investment	Acquisition from the SsangYong Group
August 2002	Shinhan BNP Paribas Investment Trust Management Co., Ltd.[2]	Investment advisory	50:50 joint venture with BNP Paribas
August 2003	Chohung Bank	Commercial banking	Acquisition from creditors
December 2005	Shinhan Life Insurance	Life insurance services	Acquisition from shareholders
March 2007	LG Card	Credit card services	Acquisition from creditors
January 2012	Tomato Mutual Savings Bank[3]	Savings bank	Purchase and assumption of assets and liabilities from creditors
January 2013	Yehanbyoul Savings Bank[4]	Savings bank	Acquisition from Korea Deposit Insurance Corporation

Notes:

(1) Renamed as Shinhan Investment Corp. from Goodmorning Shinhan Securities Co., Ltd. effective August 2009.
(2) In January 2009, SH Asset Management Co., Ltd. and Shinhan BNP Paribas Investment Trust Management merged to form Shinhan BNP Paribas Asset Management Co., Ltd.

(3) Shinhan Hope Co., Ltd. was established on December 12, 2011, to purchase and assume certain assets and liabilities of Tomato Mutual Savings Bank. On December 28, 2011, Shinhan Hope Co., Ltd. obtained a savings bank license, changed its name to Shinhan Savings Bank and became our direct subsidiary.

(4) In January 2013, we entered into a share purchase agreement with Korea Deposit Insurance Corporation for the acquisition of Yehanbyoul Savings Bank, a savings bank located in Korea, for ₩45.3 billion, and received regulatory approval to merge Yehanbyoul Savings Bank into our existing subsidiary Shinhan Saving Bank. On April 1, 2013, Shinhan Savings Bank and Yehanbyoul Savings Bank merged into a single entity, with Yehanbyoul Savings Bank being the surviving entity and the newly merged bank being named Shinhan Savings Bank.

ITEM 4.B. Business Overview

Unless otherwise specifically mentioned, the following business overview is presented on a consolidated basis under IFRS.

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Our Principal Activities

We provide comprehensive financial services, principally consisting of the following:

- commercial banking services, consisting of:
  - retail banking, which primarily focuses on making loans to or receiving deposits from individual customers (including high net-worth individuals and families) and, to a lesser extent, not-for-profit institutions such as hospitals, airports and schools;
  - corporate banking, which primarily focuses on making loans to or receiving deposits from for-profit corporations, including small- and medium-sized enterprises, and providing investment banking services to corporate clients;
  - international banking, which primarily focuses on management of overseas subsidiaries and branch operations and other international businesses; and
  - other banking, which consists of treasury business (including internal asset and liability management and other non-deposit funding activities), securities investing and trading and derivatives trading, as well as administration of the overall banking operations.
- credit card services;
- securities brokerage services;
- life insurance services;
- asset management services, including brokerage and trading of various securities, related margin lending and deposit and trust services, and other asset management services; and
- other services, including leasing and equipment financing, savings banking services, loan collection and credit reporting, collective investment administrative services and financial system development services as well as engaging in private equity investments through formation of private equity funds on a private placement basis.

In addition to the above-mentioned business activities, we, at the holding company level, have the wealth management planning office and corporate & investment banking business department, whose primary function is to support cross-divisional management with respect to these specific functional areas.

Our principal business activities are not subject to any material seasonal trends. While we have a number of overseas branches and subsidiaries, substantially all of our assets are located, and substantially all of our revenues are generated, in Korea.

Deposit-Taking Activities

Principally through Shinhan Bank, we offer many deposit products that target different customer segments with features tailored to each segment s financial and other profiles. Our deposit products consist principally of the following:

Demand deposits. Demand deposits do not accrue interest or accrue interest at a lower rate than time or savings deposits and allow the customer to deposit and withdraw funds at any time. If interest-bearing, demand deposits have interest accruing at a fixed or variable rate depending on the period and the amount of deposit. Demand deposits constituted approximately 14.6%, 16.1% and 16.6% of our total deposits as of December 31, 2015, 2016 and 2017, respectively. Demand deposits paid average interest of 0.44%, 0.37% and 0.36% in 2015, 2016 and 2017, respectively.

Savings deposits. Savings deposits allow the customer to deposit and withdraw funds at any time and accrue interest at an adjustable interest rate, which is typically lower than the rate applicable to time or installment deposits. Savings deposits constituted approximately 28.6%, 28.3% and 30.1% of our total deposits as of December 31, 2015, 2016 and 2017, respectively, and paid average interest of 0.70%, 0.59% and 0.51% in 2015, 2016 and 2017, respectively.

Time deposits. Time deposits generally require the customer to maintain a deposit for a fixed term during which the deposit accrues interest at a fixed rate or a variable rate based on certain financial indexes, including the Cost of Funds Index (COFIX) published by the Korean Federation of Banks. If the deposit is withdrawn prior to the end of the fixed term, the customer is paid a lower interest rate than that originally offered. The term typically ranges from one month to five years. Time deposits constituted approximately 54.8%, 52.8% and 50.3% of our total deposits as of December 31, 2015, 2016 and 2017, respectively, and paid average interest of 2.03%, 1.64% and 1.55% in 2015, 2016 and 2017, respectively.

Other deposits. Other deposits consist mainly of certificates of deposit. Certificates of deposit typically have maturities from 30 days to two years. Interest rates on certificates of deposit are determined based on the length of the deposit and prevailing market interest rates. Certificates of deposit are sold at a discount to their face value, reflecting the interest payable on the certificates of deposit. Certificates of deposit constituted approximately 2.1%, 2.8% and 3.0% of our total deposits as of December 31, 2015, 2016 and 2017, respectively and paid average interest of 1.20%, 1.47% and 1.57% in 2015, 2016 and 2017, respectively.

We also offer deposits which provide the customer with preferential rights to housing subscriptions under the Housing Law and Rules on Housing Supply (the Housing Law), and eligibility for mortgage and home equity loans. As a result of an amendment to the Housing Law in June 2015, new subscriptions to housing subscription savings accounts, housing subscription time deposits accounts and housing subscription installment savings accounts became no longer available after September 1, 2015. Instead, general housing subscription savings accounts (which combine all of the functions of the aforementioned three accounts) presently remain available to all. The contribution period is from the subscription date to the date on which the account holder is selected as the purchaser of a house, and the required monthly contribution amount is from a minimum of ₩20,000 to a maximum of ₩500,000. The interests accrued on general housing subscription savings accounts are paid in lump sum upon termination of the account, and such interests shall be calculated at the interest rate determined and announced by the Ministry of Land, Infrastructure and Transport. Those who have a general housing subscription savings account and meet certain other criteria are granted a preferential subscription right for the purchase of a house. In the case of privately funded houses, the aggregate amount of contributions made to the account must be at least the applicable deposit threshold amount for the location and area of the relevant house (from ₩2 million up to ₩15 million). It is impossible to change the account holder name of a general housing subscription savings account except in the case of inheritance by the death of the original account holder. For information on our deposits in Korean Won based on the principal types of deposit products we offer, see Description of Assets and Liabilities Funding Deposits.

The rate of interest payable on our deposit products may vary significantly, depending on average funding costs, the rate of return on our interest-earning assets, prevailing market interest rates among financial institutions and other major financial indicators.

We also offer court deposit services for litigants in Korean courts, which involve providing effectively an escrow service for litigants involved in certain types of legal or other proceedings. Chohung Bank historically was a dominant provider of such services since 1958, and following the acquisition of Chohung Bank, we continue to hold a dominant market share in these services. Such deposits typically carry interest rates lower than the market rates (by approximately 0.5% per annum) and amounted to ₩6,480 billion, ₩5,656 billion and ₩5,639 billion as of December 31, 2015, 2016 and 2017, respectively.

The Monetary Policy Committee of the Bank of Korea imposes a reserve requirement on Won currency deposits at commercial banks at rates ranging from 0% to 7%, based generally on maturity and the type of deposit instrument. See Supervision and Regulation Principal Regulations Applicable to Banks Liquidity.

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The Depositor Protection Act provides for a deposit insurance system under which the Korea Deposit Insurance Corporation guarantees repayment of eligible bank deposits to depositors up to ₩50 million per depositor and ₩50 million per insured under the defined contribution retirement pension per bank. See Supervision and Regulation Principal Regulations Applicable to Banks Deposit Insurance System.

Retail Banking Services

Overview

We provide retail banking services primarily through Shinhan Bank, and, to a significantly lesser extent, through Jeju Bank, a regional commercial bank. Our retail loans, before allowance for loan losses and deferred loan origination costs and fees and excluding credit card receivables, amounted to ₩111,590 billion as of December 31, 2017.

Retail banking services include mortgage and home equity lending and retail lending as well as demand, savings and fixed deposit-taking, checking account services, electronic banking and automatic teller machines (ATM) services, bill paying services, payroll and check-cashing services, currency exchange and wire fund transfer. We believe that providing modern and efficient retail banking services is important to maintaining our public profile and as a source of fee-based income. Accordingly, we believe that our retail banking services and products will become increasingly important in the coming years as the domestic banking sector further develops and becomes more complex.

Retail banking has been and will continue to remain one of our core businesses. Our strategy in retail banking is to provide prompt and comprehensive services to retail customers through increased automation and improved customer service, as well as a streamlined branch network focused on sales. The retail segment places an emphasis on targeting high net worth individuals.

Retail Lending Activities

We offer various retail loan products, consisting principally of loans to individuals and households. Our retail loan products target different segments of the population with features tailored to each segment s financial profile and other characteristics, including customer s occupation, age, loan purpose, collateral requirements and the duration of the customer s relationship with Shinhan Bank. Our retail loans consist principally of the following:

- *Mortgage and home equity loans,* which are mostly comprised of mortgage loans that are used to finance home purchases and are generally secured by the housing unit being purchased; and

- *Other retail loans,* which are loans made to customers for any purpose other than mortgage and home equity loans and the terms of which vary based primarily upon the characteristics of the borrower and which are either unsecured or secured, or guaranteed by deposits or by a third party. Other retail loans also include advance loans extended on an unsecured basis to retail borrowers the use of proceeds for which is restricted to financing of home purchases prior to the completion of the construction.

As of December 31, 2017, our mortgage and home equity loans and other retail loans accounted for 52.9% and 47.1% of our total Won-denominated retail loans (excluding credit card loans), respectively.

For secured loans, our policy is to lend up to 40 to 100% of the appraisal value of the collateral, after taking into account the value of any lien or other security interest that has priority over our security interest (other than petty claims). The loan-to-value ratio of secured loans is updated on a monthly basis using the most recent appraisal value of the collateral. For mortgage and home equity loans, our policy is to lend up to 70% of the appraisal value of the collateral. As of December 31, 2017, the loan-to-value ratio of mortgage and home equity loans of Shinhan Bank was approximately 51.8%. As of December 31, 2017, substantially all of our mortgage and home equity loans were secured by residential property.

Under the administrative instructions of the Financial Supervisory Service effective August 1, 2014 (which have been extended several times and are effective until July 2, 2018), our banking subsidiaries (i) are subject to a limit on loan-to-value ratio of 70% when extending home mortgage loans; (ii) are required to comply with a limit on debt-to-income ratio of 60% in extending home mortgage loans (amounting to more than ₩100 million) for the purchase of apartments that are secured by such apartments if they are located in the Seoul metropolitan area, excluding some areas such as island areas; and (iii) are required to apply greater flexibility in determining the debt-to-income ratio by considering the expected earnings potential. In addition, the supervising authorities in Korea issue administrative instructions to Korean banks, which have the effect of regulating the access of borrowers to housing loans and, as such, demand for real estate properties. For example, the Financial Supervisory Service issued administrative instructions to financial institutions to (except in limited circumstances) verify the borrower s ability to repay based on proof of income prior to making a mortgage and home equity loan regardless of the type or value of the collateral or the location of the property, which has had the effect of practically barring the grant of any new mortgage and home equity loans to borrowers without verifiable income.

Our banking subsidiaries extend mortgage and home equity loans in compliance with the applicable regulations and administrative instructions by the relevant supervising authorities.

The following table sets forth a breakdown of our retail loans.

	As of December 31,		
	2015	2016	2017
	(In billions of Won, except percentages)		
Retail loans(1)			
Mortgage and home-equity loans	₩ 54,983	₩ 56,235	₩ 59,078
Other retail loans	41,035	47,949	52,512
Percentage of retail loans to total gross loans	38.7%	39.9%	40.2%

Note:

(1) Before allowance for loan losses and deferred loan origination costs and fees and excludes credit card receivables.

The total mortgage and home equity loans amounted to ₩59,078 billion as of December 31, 2017, and as of such date, consisted of amortizing loans (whose principal is repaid by part of the installment payments) in the amount of ₩52,871 billion and non-amortizing loans in the amount of ₩6,207 billion. In addition, as of December 31, 2017, we also provided lines of credit in the aggregate outstanding amount of ₩705 billion for non-amortizing loans.

Pricing

The interest rates payable on Shinhan Bank s retail loans are either periodically adjusted floating rates (based on a base rate determined for three-month, six-month or twelve-month periods derived using an internal transfer price system, which reflects the market cost of funding, as adjusted to account for expenses related to lending and the profit margin of the relevant loan products) or fixed rates that reflect the market cost of funding, as adjusted to account for expenses related to lending and the profit margin. Fixed rate loans are offered only on a limited basis and at a premium to floating rate loans. For unsecured loans, which Shinhan Bank provides on a floating or fixed rate basis, interest rates thereon reflect a margin based on, among other things, the borrower s credit score as determined during its loan approval process. For secured loans, the credit limit is based on the type of collateral, priority with respect to the collateral and the loan-to-value ratio. Shinhan Bank may adjust the pricing of these loans to reflect the borrower s current and/or expected future contribution to Shinhan Bank s profitability. The interest rate on Shinhan Bank s loan products may become adjusted at the time the loan is extended. If a loan is terminated within three years following the date of the loan, the borrower is required to pay an early termination fee, which is typically 0.8% to 1.4% of the outstanding principal amount of and accrued and unpaid interest on the loan, multiplied by a fraction the numerator of which is the number of the remaining days on the loan until maturity and the denominator of which is the number of days comprising the term of the loan or three years, whichever is greater.

As of December 31, 2017, Shinhan Bank s three-month, six-month and twelve-month base rates were approximately 1.66%, 1.83% and 1.98%, respectively. As of December 31, 2017, Shinhan Bank s fixed rates for mortgage and home equity loans with a maturity of five years were approximately 4.88%. Shinhan Bank s fixed rates for other retail loans with a maturity of one year ranged from 4.17% to 14.00%, depending on the credit scores of its customers.

As of December 31, 2017, 76.3% of Shinhan Bank s total retail loans were floating rate loans and 23.7% were fixed rate loans. As of the same date, 68.9% of Shinhan Bank s retail loans with maturity of more than one year were floating rate loans and 31.1% were fixed rate loans.

The interest rate charged to customers by our banking subsidiaries is based, in part, on the cost of funds index, or COFIX, which is published by the Korean Federation of Banks. COFIX is computed based on the weighted average interest of select funding products (including time deposits, housing and other installment savings deposits, repos, discounted bills and senior non-convertible financial debentures) of eight major Korean banks (comprised of Shinhan Bank, Kookmin Bank, Woori Bank, KEB Hana Bank, Nonghyup Bank, Industrial Bank of Korea, Citibank Korea Inc. and Standard Chartered Bank Korea Limited). Each bank then independently determines the interest rate applicable to its respective customers by adding a spread to the COFIX based on the difference between the COFIX and such bank s general funding costs, administration fees, the customer s credit score, the maturity of the loan and other customer-specific premiums and discounts based on the customer relationship with such bank. These interest rates are typically adjusted on a monthly basis.

Private Banking

Historically, we have focused on customers with high net worth. Our retail banking services include providing private banking services to high net worth customers who seek personal advice in complex financial matters. Our aim in private banking is to help enhance wealth accumulation by, and increase the financial sophistication of, our high net-worth clients by offering them customized wealth management solutions and comprehensive financial services including asset portfolio and fund management, tax consulting, real estate management and family office services, among others. Since the end of 2011, in order to preemptively respond to evolving customer needs and promote asset growth by inducing greater synergy between commercial banking and investment advisory services offered by Shinhan Investment, Shinhan Bank launched private wealth management centers which combine certain branches of Shinhan Bank with those of Shinhan Investment located in the same area. Shinhan Bank s strength in private banking has been widely recognized by a number of significant industry awards in recent years, including the Best Wealth Manager in Korea (awarded six consecutive years) and Best Private Bank in Korea (awarded three consecutive years) awards by The Asset magazine in 2017 and the Best Private Bank in Korea by The Asian Banker in 2017.

As of December 31, 2017, Shinhan Bank operated 27 private wealth management service centers nationwide, including 18 in Seoul, three in the suburbs of Seoul and six in cities located in other regions in Korea. As of December 31, 2017, Shinhan Bank had approximately 7,574 private banking customers, who typically are required to have a minimum of ₩500 million in assets under management with us to qualify for private banking services.

Corporate Banking Services

Overview

We provide corporate banking services, primarily through Shinhan Bank, to small- and medium-sized enterprises, including enterprises known as SOHO (standing for small office, home office), which are small

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enterprises operated by individuals or households, and, to a lesser extent, to large corporations, including corporations that are affiliated with *chaebols*. We also lend to government-controlled enterprises.

The following table sets forth the balances and percentage of our total loans (before allowance for loan losses and deferred loan origination costs and fees) attributable to each category of our corporate lending business as of the dates indicated.

	As of December 31,					
	2015		2016		2017	
	(In billions of Won, except percentages)					
Small- and medium-sized enterprises loans[(1)]	₩ 67,336	27.1%	₩ 71,757	27.5%	₩ 78,556	28.3%
Large corporate loans	33,742	13.6	34,131	13.1	35,664	12.9
Others[(2)]	32,796	13.2	31,482	12.0	31,038	11.1
Total corporate loans	₩ 133,874	53.9%	₩ 137,370	52.6%	₩ 145,258	52.3%

Notes:

(1) Represents the principal amount of loans extended to corporations meeting the definition of small- and medium-sized enterprises under the Basic Act on Small- and Medium-sized Enterprises and its Presidential Decree.

(2) Includes loans to governmental agencies, loans to banks and other corporate loans, including loans originated by subsidiaries other than Shinhan Bank which are classified as corporate loans for purposes of financial reporting.

Small- and Medium-sized Enterprises Banking

Under the Basic Act on Small- and Medium-sized Enterprises (the SME Basic Act) and the related Presidential Decree, as amended and effective from January 27, 2016, in order to qualify as a small- and medium-sized enterprise, (i) the enterprise s total assets at the end of the immediately preceding fiscal year must be less than ₩500 billion, (ii) the enterprise must meet the standards prescribed by the Presidential Decree in relation to the average and total annual sales revenues applicable to the type of its main business, and (iii) the enterprise must meet the standards of management independence from ownership as prescribed by the Presidential Decree, including non-membership in a conglomerate as defined in the Monopoly Regulations and Fair Trade Act. However, if any entity which was a small- and medium-sized enterprise as defined in the SME Basic Act prior to the latest amendment no longer meets such definition following such amendment, such entity will be deemed a small- and medium-sized enterprise for purposes of the SME Basic Act. Non-profit enterprises that satisfy certain requirements prescribed in the SME Basic Act and its Presidential Decree may qualify as a small- and medium-sized enterprise. Furthermore, cooperatives and federations of cooperatives as prescribed by the Presidential Decree are deemed as small- and medium-sized enterprises, effective from April 15, 2014. As of December 31, 2017, we made loans to 270,660 small- and medium-sized enterprises for an aggregate amount of ₩78,556 billion (before allowance for loan losses and deferred loan origination costs and fees).

We believe that Shinhan Bank, whose traditional focus has been on small- and medium-sized enterprises lending, is well-positioned to succeed in the small- and medium-sized enterprises market in light of its marketing capabilities (which we believe have provided Shinhan Bank with significant customer loyalty) and its prudent risk management practices, including conservative credit rating systems for credit approval. To maintain or increase its market share of small- and medium-sized enterprises lending, Shinhan Bank:

has accumulated a market-leading expertise and familiarity as to customers and products. We believe Shinhan Bank has an in-depth understanding of the credit risks embedded in this market segment, allowing Shinhan Bank to develop loan and other products specifically tailored to the needs of this market segment;

operates a relationship management system to provide customer service that is tailored to small-and medium-sized enterprises. Shinhan Bank currently has relationship management teams in 184 banking branches, of which 49 are corporate banking branches and 135 are hybrid banking branches designed to serve both retail customers and, to a limited extent, corporate customers. These relationship management teams market products, and review and approve smaller loans with less credit risks; and

continues to focus on cross-selling loan products with other products. For example, when Shinhan Bank lends to small- and medium-sized enterprises, it also explores opportunities to cross-sell retail loans or deposit products to the employees of these enterprises or to provide financial advisory services.

Large Corporate Banking

Large corporate customers consist primarily of member companies of *chaebols* and financial institutions. Our large corporate loans amounted to ₩35,664 billion (before allowance for loan losses and deferred loan origination costs and fees) as of December 31, 2017. Large corporate customers tend to have better credit profiles than small- and medium-sized enterprises, and accordingly, Shinhan Bank has expanded its focus on these customers as part of its risk management policy.

Shinhan Bank aims to be a one-stop financial solution provider that also partners with its corporate clients in their corporate expansion and growth endeavors. To that end, Shinhan Bank provides a wide range of corporate banking services, including investment banking, real estate financing, overseas real estate project financing, large development project financing, infrastructure financing, structured financing, equity investments/venture investments, mergers and acquisitions consulting, securitization and derivatives services, including securities and derivative products and foreign exchange trading. Shinhan Bank, through Shinhan Asia Limited, a subsidiary in Hong Kong, also arranges financing for, and offers consulting services to, Korean companies expanding their business overseas, particularly in Asia.

Electronic Corporate Banking

Shinhan Bank offers to corporate customers a web-based total cash management service known as Shinhan Bizbank. Shinhan Bizbank supports substantially all types of banking transactions ranging from basic transaction history inquiries and fund transfers to opening letters of credit, trade finance, payment management, collection management, sales settlement service, acquisition settlement service, business-to-business settlement service, sweeping, pooling, ERP interface service, host-to-host banking solutions, SWIFT SCORE service and global cash and liquidity management service. In addition, Shinhan Bank provides customers with integrated and advanced access to its financial services through its Inside Bank program, which combines Internet banking, capital management services and enterprise resource planning to better serve corporate customers. The Inside Bank program also seeks to provide customized financial services to meet the comprehensive needs of target corporate customers ranging from conglomerates to small enterprises in various industries, with the goal of enhancing convenience to our corporate customers in accessing our financial services as well as assisting them to strategically manage their funds.

Corporate Lending Activities

Our principal loan products for corporate customers are working capital loans and facilities loans. Working capital loans, which include discounted notes and trade financing, are generally loans used for general working capital purposes. Facilities loans are provided to finance the purchase of equipment and construction of manufacturing plants. As of December 31, 2017, working capital loans and facilities loans amounted to ₩59,744 billion and ₩48,998 billion, respectively, representing 54.9% and 45.1% of our total Won-denominated corporate loans. Working capital loans generally have a maturity of one year, but may be extended on an annual basis for an aggregate term of three years in the case of unsecured loans and five years in the case of secured loans. Facilities loans have a maximum maturity of 15 years, are typically repaid in semiannual installments per annum and may be entitled to a grace period not exceeding one-third of the loan term with respect to the first repayment; facilities loans with a term of three years or less may be paid in full at maturity.

Loans to corporations may be unsecured or secured by real estate, deposits or guaranty certificates. As of December 31, 2017, secured loans and guaranteed loans (including loans secured by guaranty certificates issued by credit guarantee insurance funds) accounted for 58.7% and 12.6%, respectively, of our Won-denominated loans to small- and medium-sized enterprises. As of December 31, 2017, 49.5% of the corporate loans were secured by real estate.

When evaluating whether to extend loans to corporate customers, Shinhan Bank reviews their creditworthiness, credit score, value of any collateral and/or third party guarantee. The value of collateral is computed using a formula that takes into account the appraised value of the collateral, any prior liens or other claims against the collateral and an adjustment factor based on a number of considerations including, with respect to property, the average value of any nearby property sold in a court-supervised auction during the previous year. Shinhan Bank revalues collateral when a secured loan is renewed or if a trigger event occurs with respect to the loan in question.

Pricing

Shinhan Bank determines the price for its corporate loan products based principally on their respective cost of funding and the expected loss rate based on the borrower s credit risk. As of December 31, 2017, 45.4% of Shinhan Bank s corporate loans with outstanding maturities of one year or more had variable interest rates as determined by the applicable market rates.

More specifically, interest rates on Shinhan Bank s corporate loans are generally determined as follows:

Interest rate = (Shinhan Bank s periodic market floating rate *or* reference rate) *plus* transaction cost *plus* credit spread *plus* risk premium *plus or minus* discretionary adjustment.

Depending on the market condition and the agreement with the borrower, Shinhan Bank may use either its periodic market floating rate or the reference rate as the base rate in determining the interest rate for the borrower. As of December 31, 2017, Shinhan Bank s periodic market floating rates (which are based on a base rate determined for a three-month, six-month, one-year, two-year, three-year or five-year period, as applicable, as derived using Shinhan Bank s market rate system) were 1.66% for three months, 1.83% for six months, 1.98% for one year, 2.26% for two years, 2.36% for three years and 2.58% for five years. As of the same date, Shinhan Bank s reference rate was 4.75%. The reference rate refers to the base lending rate used by Shinhan Bank and is determined annually by Shinhan Bank s Asset & Liability Management Committee based on, among others, Shinhan Bank s funding costs, cost efficiency ratio and discretionary margin.

Transaction cost reflects the standardized transaction cost assigned to each loan product and other miscellaneous costs, including contributions to the Credit Guarantee Fund, and education taxes. The Credit Guarantee Fund is a statutorily created entity that provides credit guarantees to loans made by commercial banks and is funded by mandatory contributions from commercial banks in the amount of approximately 0.36% of all loans (excluding certain loans such as facility loans) made by them.

The credit spread is added to the periodic floating rate to reflect the expected loss based on the borrower s credit rating and the value of any collateral or payment guarantee. In addition, Shinhan Bank adds a risk premium which takes into account the potential of unexpected loss that may exceed the expected loss from the credit rating assigned to a particular borrower.

A discretionary adjustment rate is added or subtracted to reflect the borrower s current and/or future contribution to Shinhan Bank s profitability. If additional credit is provided by way of a guarantee, the adjustment rate is subtracted to reflect such change in the credit spread. In addition, depending on the price and other terms set by competing banks for similar borrowers, Shinhan Bank may reduce the interest rate to compete more effectively with other banks.

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International Business

Shinhan Bank also engages in treasury and investment activities in international capital markets, principally including foreign currency-denominated securities trading, foreign exchange trading and services, trade-related financial services, international factoring services and foreign banking operations through its overseas branches and subsidiaries. Shinhan Bank aims to become a leading bank in Asia and expand its international business by focusing on further bolstering its overseas network, localizing its overseas operations and diversifying its product offerings, particularly in terms of asset management, in order to meet the various financing needs of its current and potential customers overseas.

Other Banking Services

Other banking businesses carried on by Shinhan Bank include treasury business (including internal asset and liability management and other non-deposit funding activities), trading of, and investment in, debt securities and, to a lesser extent, equity securities for its own accounts, derivative trading activities, as well as managing back-office functions.

Treasury

Shinhan Bank s treasury division provides funds to all of Shinhan Bank s business operations and ensures the liquidity of its operation. To secure stable long-term funds, Shinhan Bank uses fixed and floating rate notes, debentures, structured financing and other advanced funding methods. As for overseas funding, Shinhan Bank closely monitors the feasibility of raising funds in currencies other than the U.S. Dollar, such as the Japanese Yen and the Euro. In addition, Shinhan Bank makes call loans and borrows call money in the short-term money market. Call loans are short-term lending among banks and financial institutions in either Korean Won or foreign currencies with a minimum transaction amount of ₩100 million and maturities of typically one day.

Securities Investment and Trading

Shinhan Bank invests in and trades securities for its own accounts in order to maintain adequate sources of liquidity and to generate interest income, dividend income and capital gains. Shinhan Bank s trading and investment portfolios consist primarily of Korean treasury securities and debt securities issued by Korean government agencies, local governments or certain government-invested enterprises, debt securities issued by financial institutions and equity securities listed on the KRX KOSPI Market and KRX KOSDAQ Market of the Korea Exchange. For a detailed description of our securities investment portfolio, see Description of Assets and Liabilities Investment Portfolio.

Derivatives Trading

Shinhan Bank provides to its customers, and to a limited extent, trades for its proprietary accounts, a broad range of derivatives products, which include:

- interest rate swaps, options, and futures relating to Korean Won interest rate risks and LIBOR risks, respectively;
- cross-currency swaps, largely for Korean Won against U.S. Dollars, Japanese Yen and Euros;

- equity and equity-linked options;
- foreign currency forwards, options and swaps;
- commodity forwards, swaps and options;
- credit derivatives; and
- KOSPI 200 indexed equity options.

Shinhan Bank s outstanding derivatives commitments in terms of notional amount were ₩132,785 billion, ₩174,866 billion and ₩183,457 billion in 2015, 2016 and 2017, respectively. Such derivative operations generally focus on addressing the needs of Shinhan Bank s corporate clients to enter into derivatives contracts to hedge their risk exposure and entering into back-to-back derivatives to hedge Shinhan Bank s risk exposure that results from such client contracts.

Shinhan Bank also enters into derivative contracts to hedge the interest rate and foreign currency risk exposures that arise from its own assets and liabilities. In addition, to a limited extent, Shinhan Bank engages in the proprietary trading of derivatives within its regulated open position limits. See Description of Assets and Liabilities Derivatives.

Trust Account Management Services

Overview

Shinhan Bank s trust account management services involve management of trust accounts, primarily in the form of money trusts. Trust account customers are typically individuals seeking higher rates of return than those offered by bank account deposits. Because deposit reserve requirements do not apply to deposits held in trust accounts as opposed to deposits held in bank accounts, and regulations governing trust accounts tend to be less strict, Shinhan Bank is generally able to offer higher rates of return on trust account products than on bank deposit products. However, in recent years, due to the ongoing low interest environment, Shinhan Bank has not been able to offer attractive rates of return on its trust account products.

Trust account products generally require higher minimum deposit amounts than those required by comparable bank account deposit products. Unlike bank deposit products, deposits in trust accounts are invested primarily in securities (consisting principally of debt securities and beneficiary certificate for real estate financing) and, to a lesser extent, in loans, as the relative shortage of funding sources require that trust accounts be invested in a higher percentage of liquid assets.

Under the Banking Act, the Financial Investment Services and Capital Markets Act and the Trust Act, assets in trust accounts are required to be segregated from other assets of the trustee bank and are unavailable to satisfy the claims of the depositors or other creditors of such bank. Accordingly, trust accounts that are not guaranteed as to principal (or as to both principal and interest) are accounted for and reported separately from the bank accounts. See Supervision and Regulation. Trust accounts are regulated by the Trust Act and the Financial Investment Services and Capital Markets Act, and most national commercial banks offer similar trust account products. Shinhan Bank earns income from trust account management services, which is recorded as net trust management fees.

As of December 31, 2015, 2016 and 2017, Shinhan Bank had total trust assets of ₩37,304, ₩45,058 billion and ₩58,536 billion respectively, comprised principally of securities investments of ₩7,688 billion, ₩10,885 billion and ₩16,870 billion respectively; real property investments of ₩7,576 billion, ₩8,914 billion and ₩12,053 billion, respectively; and loans with an aggregate principal amount of ₩454 billion, ₩472 billion and ₩469 billion, respectively. Securities investments consisted of corporate bonds, government-related bonds and other securities, primarily commercial paper. As of December 31, 2015, 2016 and 2017, debt securities accounted for 19.2%, 22.9% and 27.3%, respectively, and equity securities constituted 1.4%, 1.3% and 1.5%, respectively, of Shinhan Bank s total trust assets. Loans made by trust accounts are similar in type to those made by bank accounts, except that they are made only in Korean Won. As of December 31, 2015, 2016 and 2017, approximately 53.3%, 52.1% and 57.1%, respectively, of the amount of loans from the trust accounts were collateralized or guaranteed. In making investment from funds received for each trust account, each trust product maintains investment guidelines applicable to each such product which set forth, among other things, company-, industry- and security-specific limitations.

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Trust Products

In Korea, trust products typically take the form of money trusts, which are discretionary trusts over which (except in the case of a specified money trust) the trustees have investment discretion subject to applicable law and is commingled and managed jointly for each type of trust account. The specified money trusts are established on behalf of customers who give specific directions as to how their trust assets should be invested.

Money trusts managed by Shinhan Bank s trust account business amounted to ₩24,093 billion, ₩29,476 billion and ₩37,700 billion as of December 31, 2015, 2016 and 2017, respectively.

Shinhan Bank offers variable rate trust products through its retail branch network. As of December 31, 2015, 2016 and 2017, Shinhan Bank s variable rate trust accounts amounted to ₩20,443 billion, ₩25,634 billion and ₩33,720 billion, respectively, of which principal guaranteed variable rate trust accounts amounted to ₩3,649 billion, ₩3,841 billion and ₩3,979 billion, respectively. Variable rate trust accounts offer their holders variable rates of return on the principal amount of the deposits in the trust accounts and do not offer a guaranteed return on the principal of deposits, except in the limited cases of principal guaranteed variable rate trust accounts, for which payment of the principal amount is guaranteed. Shinhan Bank charges a lump sum or a fixed percentage of the assets held in such trusts as a management fee, and, depending on the trust products, is also entitled to additional fees in the event of early termination of the trusts by the customer. Korean banks, including Shinhan Bank, are currently allowed to guarantee the principal of the following types of variable rate trust account products: (i) existing individual pension trusts, (ii) new individual pension trusts, (iii) existing retirement pension trusts, (iv) new retirement pension trusts, (v) pension trusts and (vi) employee retirement benefit trusts. Shinhan Bank also offers an insignificant amount of guaranteed fixed rate trust products (amounting to ₩1.0 billion, ₩1.0 billion and ₩1.0 billion as of December 31, 2015, 2016 and 2017, respectively), which provide to its holders a guaranteed return of the principal as well as a guaranteed fixed rate of return. These products are carry-overs from past offerings, and Shinhan Bank no longer offers guaranteed fixed rate trust products.

Credit Card Services

Products and Services

We currently provide our credit card services principally through our credit card subsidiary, Shinhan Card, and to a limited extent, Jeju Bank.

Shinhan Card offers a wide range of credit card and other services, principally consisting of the following:

- *credit card services*, which involve providing cardholders with credit up to a preset limit to purchase products and services. Repayment for credit card purchases may be made either (i) on a lump-sum basis, namely, in full at the end of a monthly billing cycle or (ii) on a revolving basis subject to a minimum monthly payment. The minimum monthly payment for holders of credit cards issued before December 30, 2014 is the greater of (x) 5% to 20% of the amount outstanding (depending on the cardholder s credit) or (y) ₩30,000. The minimum monthly payment for holders of credit cards issued on or after December 30, 2014 is the greater of (x) 10% to 20% of the amount outstanding (depending on the cardholder s credit) or (y) ₩50,000. Currently, the outstanding credit card balance subject to the revolving basis payments generally accrues interest at the effective annual rates of approximately 5.4% to 24.0%.

cash advances, which enable the cardholders to withdraw cash subject to a preset limit from an ATM machine or a bank branch. Repayments for cash advances may be made either on a lump-sum basis or, in the case of credit cards issued before December 30, 2014, on a revolving basis. Currently, the lump-sum cash advances generally accrue interest at the effective annual rates of approximately 6.1% to 24.0% and the revolving cash advances generally accrue interest at a minimum rate of 5% to 20% of the outstanding balance (depending on the cardholder s credit).

installment purchases, which provide customers with an option to purchase products and services from select merchants on an installment basis for which repayments must be made in equal amounts over a fixed term generally ranging from two to 24 months, and for certain limited types of cards, up to 36 months. Currently, the outstanding installment purchase balances generally accrue interest at the effective annual rates of approximately 9.5% to 20.9%.

card loans, which enable cardholders to receive, up to a preset limit, a loan which is generally unsecured. Repayment of card loans is made generally by (i) repaying principal and interest in equal amounts on an installment basis over a fixed term of two to 36 months, (ii) repaying the principal and interest amounts in full at maturity, or (iii) making interest-only payments during the initial grace period of either three months or six months and repaying the principal and interest amounts on a monthly installment basis over the remaining period of typically two to 36 months. Currently, the outstanding card loan balances generally accrue interest at the effective annual rates of approximately 6.16% to 23.9%. Delinquent credit card receivables can also be restructured into loans, which we classify as card loans, and these loans generally accrue interest at the effective annual rates of approximately 11.9% to 19.5% over a fixed term whose maximum is 72 months.

Shinhan Card derives revenues from annual membership fees paid by credit cardholders, interest charged on credit card balances, fees and interest charged on cash advances and card loans, interest charged on late and deferred payments and merchant fees paid by retail and service establishments. Merchant fees and interest on cash advances constitute the largest source of revenue.

The annual membership fees for credit cards vary depending on the type of credit card and the benefits offered thereunder. For standard credit cards and most of the affinity and co-branded cards, Shinhan Card charges an annual membership fee ranging from ₩2,000 to ₩1,000,000 per credit card, depending on the type of the card and the cardholder profile. Certain government affinity cards have no annual membership fee. If Shinhan Card s customers make cash advances using ATMs of a financial institution other than Shinhan Card, Shinhan Card also charges a usage fee for such cash advances in an amount equivalent to the fees charged by such financial institution for the use of its ATM plus costs to cover Shinhan Card s related administration expenses.

Any accounts that are unpaid when due are deemed to be delinquent accounts, for which Shinhan Card levies a late charge in lieu of the interest rates applicable prior to default. The late charge rate currently ranges from 22.4% to 24.0% per annum. Beginning in the first half of 2018, instead of levying a late charge in lieu of interest rates prior to default, Shinhan Card will maintain the interest rates prior to default but add a late charge rate of 3% in addition to the interest rates prior to default.

Merchant discount fees, which are processing fees Shinhan Card charges to merchants, can be up to the regulatory limit of 2.5% of the purchased amount depending on the merchant used, with the average charge for credit cards being 1.61% in 2017. For small- and medium-sized merchants, the applicable regulations impose reduced fee rates of 0.8% (in the case of merchants with annual sales of ₩300 million or less) and 1.3% (in the case of merchants with annual sales of more than ₩300 million and up to ₩500 million), respectively, of the purchased amount.

Although making payments on a revolving basis is more common in many other countries, this payment method is still in its early stages of development in Korea. Cardholders in Korea are generally required to repay their purchases within approximately 14 to 44 days of purchase depending on their payment cycle, except in the case of installment purchases where the repayment term is typically three to six months. Accounts that remain unpaid after this period are deemed to be delinquent, and Shinhan Card levies late charges on and closely monitors such accounts. For purchases made on an installment basis, Shinhan Card charges interest on unpaid amounts at rates that vary according to the terms of repayment.

Cardholders are required to settle their outstanding balances in accordance with the terms of the credit cards they hold. Cardholders are required to select the monthly settlement date when they open the credit card account and may subsequently change the settlement date but no more than once every 60 days. Settlement dates at or around the end of each month are the most popular since salaries are typically paid at the end of the month.

In addition to credit card services, Shinhan Card also offers check cards, which are similar to debit cards in the United States and many other countries, to retail and corporate customers. A check card can be used at any of the merchants that accept credit cards issued by Shinhan Card and the amount charged to a check card is directly debited from the cardholder s designated bank account. Check cards have a low risk of default and involve minimal funding costs. Although Shinhan Card does not charge annual membership fees on check cards, merchants are charged fees on the amount purchased using check cards at a rate between 0.50% and 2.50%, depending on the type of business, which is lower than the corresponding fee charged for credit card use.

Credit Card Products

Shinhan Card offers a wide range of credit card products tailored for credit cardholders lives and to satisfy their preferences and needs. Credit card products offered by Shinhan Card include:

- cards that provide additional benefits such as frequent flyer miles and reward program points that can be redeemed by the customer for complementary services, prices or cash;

- platinum cards and other preferred membership cards, which have higher credit limits and provide additional services in return for higher annual membership fees;

- cards with additional features to preferred customers, such as revolving credit cards, travel services and insurance;

- cards with fraud detection and security systems to prevent the misuse of credit cards and to encourage the use of credit cards over the Internet;

- corporate and affinity cards that are issued to employees or members of particular companies or organizations; and

- mobile phone cards allowing customers to conduct wireless credit card transactions through their mobile phones.

Customers and Merchants

In addition to internal growth through cross-selling, we seek to enhance our market position by selectively targeting new customers with high net worth and solid credit quality through the use of a sophisticated and market-oriented risk management system. Shinhan Card screens its credit card applicants and sets individualized credit limits for such applicants according to internal guidelines based on a comprehensive credit scoring system. We also seek to provide a wide variety of differentiated products and services tailored to our customers individualized needs through precision analysis and customer segmentation based on the big data we have compiled on our approximately 22 million customers. We have also formed a team dedicated to the fintech business by actively pursuing technology developments and strategic alliances with key partners as well as additional teams focused on innovation and creating new sources of value for our clients through the development of big data and digital platforms. For example, Shinhan Card has an AI Lab team devoted to integrating artificial intelligence technology to its services and channels.

The following table sets forth the number of customers of Shinhan Card and the number of merchants at which Shinhan Card can be used for purchases as of the dates indicated.

	As of December 31,		
	2015	2016	2017
	(In thousands, except percentages)		
Shinhan Card:			
Number of credit card holders[(1)]	12,163	12,216	12.424
Personal accounts	12,052	12,097	12.295
Corporate accounts	111	119	129
Active ratio[(2)]	97.9%	97.3%	96.3%
Number of merchants	2,513	2,626	2.724

Notes:

(1) Represents the number of cardholders whose card use is not subject to suspension or termination as of the relevant date.

(2) Represents the ratio of accounts used at least once within the last six months to the total accounts as of year-end.

Installment Finance

Shinhan Card provides installment finance services to customers to facilitate purchases of durable consumer goods such as new and used cars, appliances, computers and other home electronics products. Revenues from installment finance operations accounted for 2.08% of Shinhan Card s total operating revenue in 2017. Shinhan Card pays the merchants when Shinhan Card s customers purchase such goods, and the customers remit monthly installment payments to Shinhan Card over a number of months, generally up to 36 months (and, in the case of installment financings for automobile purchases, up to 72 months), as agreed with the customers. For installment finance products for new cars, Shinhan Card historically charged, in addition to interest, an initial financing fee of up to 9.9% of the purchase price, depending on the customer s credit score, the installment period and installment amount. Initial financing fees charged in connection with installment finance products for new cars, however, were abolished effective March 2, 2013 pursuant to the Financial Consumer Report (Automobile Financings) issued by the Financial Supervisory Service on January 29, 2013. Shinhan Card has installment financing arrangements with over 10,000 merchants in Korea, including major car dealers, manufacturers and large retailers with nationwide networks, such as electronics goods stores.

Shinhan Card promptly processes installment financing applications and, based on the extensive credit information it possesses or can access, it is able to offer flexible installment payment terms tailored to individual needs of the customers. Shinhan Card also devotes significant efforts to developing and maintaining its relationships with merchants, which are the most important source of referrals for installment finance customers. Shinhan Card makes prompt payments to merchants for goods purchased by the installment finance customers.

Auto Lease

Shinhan Card currently provides auto leasing financing to retail customers and corporations. Revenues from auto lease operations accounted for 1.39% of Shinhan Card s total operating revenue in 2017.

Securities Brokerage Services

Overview

Through Shinhan Investment, we provide a wide range of financial investment services to our diversified customer base including corporations, institutional investors, governments and individuals. Financial investment services offered by Shinhan Investment range from securities brokerage services, investment advice and financial planning services, and investment banking services such as underwriting and M&A advisory services. Subject to market conditions, Shinhan Investment also engages in equity- and stock index-linked derivatives sales and brokerage, proprietary trading and brokerage services for futures involving interest rates, currency and commodities as well as foreign exchange margin trading.

As of December 31, 2017, according to internal data, Shinhan Investment s annual market share of Korean equity brokerage market was 5.07% (consisting of 2.43% in the retail segment, 0.61% in the institutional segment and 2.03% in the international segment) in terms of total brokerage volume, ranking third among securities firms in Korea. As of the same date, according to internal data, Shinhan Investment held the ninth largest annual market share in the options brokerage segment and the seventh largest annual market share in the KOSPI 200 futures segment of 6.91% and 5.92%, respectively, in terms of total brokerage volume with respect to these products.

Products and Services

Shinhan Investment provides principally the following services:

- *retail client services.* These services include equity and bond brokerage, investment advisory and financial planning services to retail customers, with a focus on high net worth individuals. The fees generated include brokerage commissions for the purchase and sale of securities, asset management fees, interest income from credit extensions (including in the form of stock subscription loans), margin transaction loans and loans secured by deposited securities.

- *institutional client services:*

  - *brokerage services.* These services include brokerage of stocks, corporate bonds, futures and options provided to Shinhan Investment s institutional and international customers and sale of institutional financial products. These services are currently supported by a team of approximately 78 research analysts that specialize in equity, bonds and derivatives research.

  - *investment banking services.* These services include a wide array of investment banking services to Shinhan Investment s corporate customers, such as domestic and international initial public offerings, mergers and acquisitions advisory services, bond issuances, underwriting, capital increase, asset-backed securitizations, issuance of convertible bonds and bonds with warrants, structured financing, issuance of asset-backed commercial papers and project financings involving infrastructure, real estate and shipbuilding.

Shinhan Investment also engages, to a limited extent, in proprietary trading in equity and debt securities, derivative products and over-the-counter market products.

With respect to brokerage services, in the face of intense competition in the domestic brokerage industry, Shinhan Investment primarily focuses on strengthening profitability through service differentiation and efficient management of its distribution network rather than enlarging its market share indiscriminately through lowering fees and commissions. Shinhan Investment s service differentiation efforts include offering its customers opportunities to purchase stocks in a wide range of countries (currently more than 28 countries), leveraging synergy opportunities afforded by affiliation with other Shinhan entities such as offering brokerage accounts maintained at Shinhan Bank and Shinhan Capital.

With respect to investment banking services, Shinhan Investment concentrates on equity capital markets, debt capital markets, project finance and mergers and acquisitions. To a limited extent, Shinhan Investment also engages in private equity investments through formation of private equity funds by soliciting investors on a private placement basis. To better serve its international customers, Shinhan Investment has established four overseas service centers in Hong Kong, New York, Vietnam and Indonesia. In July 2015, we acquired a 100% stake in Nam An Securities (subsequently launched as Shinhan Securities Vietnam Co., Ltd.), a Vietnamese

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securities services firm that provides investment banking and asset management services. In addition, in order to seize the rapid growth opportunity and as part of its expansion efforts in Indonesia, Shinhan Investment acquired a 99% stake in PT Makinta Securities, an Indonesian investment banking firm in July 2016 and subsequently launched it as an overseas subsidiary offering investment banking and brokerage services under the name PT Shinhan Sekuritas Indonesia in December 2016. To further expand and stabilize our global businesses, we made further capital investments totalling US$62 million in December 2017 in our subsidiaries located in Hong Kong, New York, Vietnam and Indonesia.

Life Insurance Services

We provide life insurance products and services primarily through Shinhan Life Insurance. Shinhan Life Insurance provides its services through diversified distribution channels consisting of financial planners, telemarketers, agency marketers and bancassurance specialists. As of December 31, 2015, 2016 and 2017, Shinhan Life Insurance had total assets of ₩24,545 billion, ₩27,500 billion and ₩29,719 billion and net profits of ₩100 billion, ₩151 billion and ₩121 billion, respectively.

Other Services

Through our other subsidiaries, we also provide asset management, leasing and equipment financing, savings banking, loan collection and credit reporting, collective investment administration and financial system development services. Through Shinhan Private Equity (in addition to Shinhan Investment), we are also engaged in private equity investments through formation of private equity funds by soliciting investors on a private placement basis.

Asset Management Services

In addition to personalized wealth management services provided as part of our private banking and securities brokerage services, we also provide asset management services through Shinhan BNP Paribas Asset Management, a joint venture with BNP Paribas Asset Management Holding, of which we and BNP Paribas Asset Management Holding hold 65:35 interests, respectively. Shinhan BNP Paribas Asset Management ranked fifth among asset managers in Korea in terms of assets under management as of December 31, 2017, and provides a wide range of investment products, including traditional equity/fixed income funds as well as alternative investment products, to retail and institutional clients. As a joint venture with BNP Paribas Asset Management Holding, we believe Shinhan BNP Paribas Asset Management derives significant benefits from BNP Paribas s global network of investment professionals and expertise in the asset management industry. As of December 31, 2017, Shinhan BNP Paribas Asset Management had assets under management amounting to approximately ₩40,962 billion. To a limited extent, Shinhan Investment also provides asset management services for discretionary accounts, see Securities Brokerage Services.

Leasing and Equipment Financing

We provide leasing and equipment financing services to our corporate customers mainly through Shinhan Capital. Shinhan Capital provides customers with leasing, installment financing and new technology financing, equipment leasing, and corporate credit financing. Shinhan Capital s strength has traditionally been in leasing of ships, printing machines, automobiles and other specialty items, but it also offers other leasing and financing services, such as corporate restructuring services for financially troubled companies, project financing for real estate and infrastructure development, corporate leasing and equipment financing.

Savings Banking

Through Shinhan Savings Bank, we provide savings banking services in accordance with the Mutual Savings Bank Act to customers that generally would not, due to their credit profile, qualify for our commercial banking services or who seek higher returns on their deposits than those offered by our commercial banking subsidiaries. Established in December 2011, Shinhan Savings Bank offers savings and other deposit products with relatively higher interest rates and loans (usually in relatively small amounts and on customer-tailored terms and including loans for which we receive credit support from the Government) primarily to small- to medium-sized enterprises and low income households who would not generally qualify for our commercial banking services. Shinhan Savings Bank has assumed the assets and liabilities of Tomato Savings Bank, which we acquired in January 2012, and has merged into Yehanbyoul Savings Bank, which we acquired in March 2013, with Yehanbyoul Savings Bank as the surviving entity with its name changed to Shinhan Savings Bank. Both Tomato Savings Bank and Yehanbyoul Savings Bank were facing liquidity troubles due to difficulties in the real estate project financing business as a result of the prolonged slump in the Korean real estate market at the time we acquired them. We closely monitor the business activities and product offerings of Shinhan Savings Bank to ensure its financial soundness.

Loan Collection and Credit Reporting

We centralize credit collection and credit reporting operations for our subsidiaries through Shinhan Credit Information Co. Ltd., which also provides similar services to third party customers. Shinhan Credit Information s services include debt collection, credit inquiries, credit reporting, civil application/petition services and process agent services, among others. Shinhan Credit Information also manages participants in credit recovery programs and provides support to the Kookmin Happy Fund, which is a Government-established fund that supports retail borrowers with low credit scores by purchasing defaulted loans from creditors or providing credit guarantees to enable such borrowers to refinance at lower rates.

Collective Investment Administration Services

We provide integrated collective investment administration services through Shinhan AITAS Co., Ltd. Shinhan AITAS provides general management service, asset management systems, accounting systems and trading systems to asset management companies and institutional investors. The target customers for these collective investment administration services are asset managers, investment advisors and institutional investors, and Shinhan AITAS seeks to provide a comprehensive service package including the computation of the reference value for funds, evaluation of fund performance, provision of trading systems and fund-related legal administrative services.

Private Equity

To a limited extent, through Shinhan Alternative Investment, we are also engaged in private equity investments through formation of private equity funds. The private equity funds receive funding from investors on a private placement basis, which funds are then invested in equity securities in companies for a variety of reasons, including management control, business turnaround or corporate governance improvements.

Financial System Development Services

We provide financial system development services through Shinhan Data Systems, which offers system integration, system management, IT outsourcing, business process outsourcing and IT consulting services.

Real Estate Investment Trust (REIT) Asset Management

Through our wholly owned subsidiary, Shinhan REITs Management Co., Ltd., we provide real estate investment and management services to real estate investment trusts.

Our Distribution Network

We offer a wide range of financial services to retail and corporate customers through a variety of distribution networks and channels established by our subsidiaries. The following table presents the geographical distribution of our distribution network based on the branch offices and other distribution channels of our principal subsidiaries, as of December 31, 2017.

Distribution Channels in Korea[1]	Shinhan Bank	Jeju Bank	Shinhan Card	Shinhan Investment	Shinhan Life Insurance	Total
Seoul metropolitan	351	2	7	54	51	465
Gyeonggi province	192		4	19	32	247
Six major cities:	168	1	6	22	48	245
Incheon	59		1	3	13	76
Busan	38	1	1	6	15	61
Gwangju	13		1	3	6	23
Daegu	24		1	4	5	34
Ulsan	14		1	3	2	20
Daejeon	20		1	3	7	31
Sub-total	711	3	17	95	131	957
Others	154	35	6	19	50	264
Total	865	38	23	114	181	1,221

Note:

(1) Includes our main office and those of our subsidiaries.

Banking Service Channels

Our banking services are primarily provided through an extensive branch network, specializing in retail and corporate banking services, as complemented by self-service terminals and electronic banking, as well as an overseas services network.

As of December 31, 2017, Shinhan Bank s branch network in Korea comprised of 865 service centers, consisting of our headquarters, 672 retail banking service centers, nine corporate banking service centers primarily designed to serve large corporate customers and 184 hybrid banking branches designed to serve retail as well as small-business corporate customers. Shinhan Bank s banking branches are designed to provide one-stop banking services tailored to their respective target customers.

Retail Banking Channels

In Korea, many retail transactions are conducted in cash or with credit cards, and conventional checking accounts are generally not offered or used as widely as in other countries such as the United States. An extensive retail branch network has traditionally played an important role as the main platform for a wide range of banking transactions.

However, a growing number of customers are turning to other service channels to meet their banking needs, such as Internet banking, mobile banking and other forms of non-face-to-face platforms. In response to such changes, Shinhan Bank has recently focused on reorganizing its retail branch network, including shifting, merger or closure of certain branches that are considered redundant.

Recently, one of the key initiatives at Shinhan Bank has been to target high net worth individuals through private banking. Our private banking services are provided principally through private banking relationship managers who, within target customer groups, assist clients in developing individual investment strategies. We believe that such relationship managers help us foster enduring relationships with our clients. Private banking customers also have access to Shinhan Bank s retail branch network and other general banking products Shinhan Bank offers through its retail banking operations.

Corporate Banking Channels

Shinhan Bank currently provides corporate banking services through corporate banking service centers primarily designed to serve large corporate customers and hybrid banking branches designed to serve retail as well as small-business corporate customers. Small- and medium-sized enterprises have traditionally been Shinhan Bank s core corporate customers and we plan to continue to maintain Shinhan Bank s strength vis-à-vis these customers.

Self-Service Terminals

In order to complement its banking branch network, Shinhan Bank maintains an extensive network of automated banking machines, which are located in branches and in unmanned outlets. These automated banking machines consist of ATMs, cash dispensers and passbook printers. In December 2015, Shinhan Bank introduced a new generation of automated self-service machines called digital kiosks, which are currently being test-run at 17 branches in the Seoul metropolitan area. These digital kiosks feature biometric authentication technology and can perform a wide range of services that are unavailable through traditional ATMs, such as opening new accounts, issuance of debit and check cards, foreign currency exchange and overseas remittance of foreign currency. As of December 31, 2017, Shinhan Bank had 6,076 ATMs, nine cash dispensers and 35 digital kiosks. Shinhan Bank has actively promoted the use of these distribution outlets in order to provide convenient service to customers, as well as to maximize the marketing and sales functions at the branch level, reduce employee costs and improve profitability. In 2017, automated banking machine transactions accounted for a substantial portion of total deposit and withdrawal transactions of Shinhan Bank in terms of the number of transactions and fee revenue generated, respectively.

Electronic Banking

Shinhan Bank s Internet banking services are more comprehensive than those available at the counter, including such services as 24 hour account balance posting, real-time account transfer, overseas remittance and loan requests. Shinhan Bank also offers mobile banking services in order to enable customers to make speedy, convenient and secure banking transactions using mobile phones. As of December 31, 2017, Shinhan Bank had approximately 17,002,657 subscribers to its Internet banking services and approximately 12,757,346 users of its smart banking applications, representing an increase of 5.1% and 9.6%, respectively, compared to December 31, 2016. Shinhan Bank continues to experience a rise in the number of online and mobile banking users. Shinhan Bank began offering online and mobile banking initially with a view to saving costs rather than increasing revenues, but is currently exploring ways to leverage the possibility of increase revenues through online and mobile banking given that these services offer customers with easier and more convenient access to banking services without limitations of time and space as well as offer tailored and customized service to each customer. In September 2017, Shinhan Bank launched Shinhan Tong, a new mobile and web based platform that is more user friendly and easier to access than previous platforms and does not require additional applications or certifications. Shinhan Tong utilizes mobile identification and non-face-to-face identity authentication technology, which allows users to open new bank accounts, exchange currencies and use other services such as credit card application services without having to visit a physical bank branch.

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Overseas Distribution Network

The table below sets forth Shinhan Bank s overseas banking subsidiaries and branches as of December 31, 2017.

Business Unit	Location	Year Established or Acquired
Subsidiaries		
Shinhan Asia Ltd.	Hong Kong SAR, China	1982
Shinhan Bank Europe GmbH(1)	Frankfurt, Germany	1994
Shinhan Bank America	New York, U.S.A.	2003
Shinhan Bank (China) Limited	Beijing, China	2008
Shinhan Khmer Bank PLC	Phnom Penh, Cambodia	2007
Shinhan Bank Kazakhstan Limited	Almaty, Kazakhstan	2008
Shinhan Bank Canada	Toronto, Canada	2009
Shinhan Bank Japan(2)	Tokyo, Japan	2009
Shinhan Bank Vietnam Ltd.(3)	Ho Chi Minh City, Vietnam	2011
Banco Shinhan de Mexico(4)	Mexico City, Mexico	2015
PT Bank Shinhan Indonesia(5)	Jakarta, Indonesia	2016
Branches		
New York	U.S.A.	1989
Singapore	Singapore	1990
London	United Kingdom	1991
Mumbai	India	1996
Hong Kong	China	2006
New Delhi	India	2006
Kancheepuram	India	2014
Pune	India	2014
Manila	Philippines	2015
Dubai	United Arab Emirates	2015
Sydney	Australia	2016
Yangon	Myanmar	2016
Ahmedabad	India	2016
Ranga Reddy	India	2016
Representative Offices		
Mexico	Mexico City, Mexico	2008
Uzbekistan	Tashkent, Uzbekistan	2009
Myanmar	Yangon, Myanmar	2013
Poland(1)	Wroclaw, Poland	2014

Notes:

(1) Shinhan Bank Europe GmbH established a representative office in Poland in 2014.
(2) While Shinhan Bank established the subsidiary in Japan in 2009, Shinhan Bank has provided banking services in Japan through a branch structure since 1986.
(3) Prior to the establishment of this subsidiary in 2011, Shinhan Bank provided banking services in Vietnam through a branch since 1995.
(4) Banco Shinhan de Mexico obtained a preliminary license in August 2015. In December 2017, Banco Shinhan de Mexico obtained a full business license.

(5) Shinhan Bank acquired a 98.01% stake in Bank Metro Express and a 100% stake in Centratama Nasional Bank, two banks in Indonesia, in November 2015 and December 2016, respectively. On February 17, 2016, Bank Metro Express obtained a license to conduct business activities in the name of PT Bank Shinhan Indonesia. Centratama Nasional Bank was merged with PT Bank Shinhan Indonesia on December 6, 2016.

Currently, our overseas subsidiaries and branches are primarily engaged in trade financing and local currency funding for Korean companies and Korean nationals in the overseas markets, as well as providing foreign exchange services in conjunction with Shinhan Bank s headquarters. On a limited basis, these overseas branches and subsidiaries also engage in investment and trading of securities of foreign issuers. In the future, as part of our globalization efforts, we plan to expand our coverage of local customers in the overseas markets by providing a wider range of services in retail and corporate banking, and to that end, we have increasingly established subsidiaries in lieu of branches in select markets and in 2011 merged two of our Vietnam banking subsidiaries in order to enhance our presence and enable greater flexibility in its service offerings in these markets. We plan to maintain our focus on organic growth, while we may selectively pursue acquisitions in markets where it is difficult to obtain local banking licenses through greenfield entry. In furtherance of this objective, Shinhan Bank acquired a 98.01% stake in Bank Metro Express and a 100% stake in Centratama Nasional Bank, two banks in Indonesia, in November 2015 and December 2016, respectively. The Bank completed the merger of the two banks in December 2016. The Bank also opened additional branches in Australia, Myanmar and India in the second half of 2016. In April 2017, Shinhan Bank Vietnam Co., Ltd. acquired ANZ Bank (Vietnam) Limited s retail division. We plan to continue our efforts to expand our overseas banking service network and global operations.

Credit Card Distribution Channels

Shinhan Card primarily uses three distribution channels to attract new credit card customers: (i) the banking and credit card branch network, (ii) sales agents, and (iii) business partnerships and affiliations with vendors.

The branch network for our credit card operations consisted of 865 branches as of December 31, 2017 of Shinhan Bank and 23 card sales branches of Shinhan Card. The use of the established distribution network of Shinhan Bank is part of the group-wide cross-selling efforts of selling credit card products to existing banking customers. In 2017, the number of new cardholders acquired through our banking distribution network accounted for approximately 23.9% of the total number of new cardholders. We believe that the banking distribution network will continue to provide a stable and low-cost venue for acquiring high-quality credit cardholders.

The sales agents represented the most significant source of Shinhan Card s new cardholders in 2017, and the number of new cardholders acquired through sales agents accounted for approximately 47.3% of the total number of Shinhan Card s new cardholders in 2017. As of December 31, 2017, Shinhan Card had 3,066 sales agents, who were independent contractors. These sales agents assist prospective customers with the application process and customer service. Compensation of these sales agents is generally tied to the transaction volume of the customers introduced by them, and we believe this system helps to enhance profitability.

As a way of acquiring new cardholders, Shinhan Card also has business partnership and affiliation arrangements with a number of vendors, including gas stations, major retailers, airlines and telecommunication and Internet service providers. Shinhan Card plans to continue to leverage its alliances with such vendors to attract new cardholders.

In November 2014, as an initial step to exploring potential opportunities overseas, Shinhan Card established its first overseas subsidiary in Kazakhstan, LLP MFO Shinhan Finance, as Kazakhstan was deemed to have relatively low entry barriers to foreign financial institutions, high growth potential for retail operations and the possibility of leveraging Shinhan Bank s network. LLP MFO Shinhan Finance obtained its business license in the first half of 2015 and commenced operations in July 2015, including installment financing and credit loans. In 2018, LLP MFO Shinhan

Finance is planning to expand its marketing channels and improve profitability by diversifying its loan product offerings.

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In December 2015, Shinhan Card acquired a majority stake in PT Swadharma Indotama Finance, a multi finance company in Indonesia, and changed its legal name to PT Shinhan Indo Finance. PT Shinhan Indo Finance engages in corporate and retail operations, including installment financing and financial leases, and began offering credit card services in January 2017 after obtaining its credit card business license in December 2016. It is currently focusing on expanding its client base by utilizing the Shinhan Bank network as well as employees and clients of its affiliate company, the Salim Group. In order to expand its retail operations, in 2018, PT Shinhan Indo Finance is planning to expand its car sales network through partnerships with local car dealers. In addition, it is planning to improve its profit structure by reducing operating costs and enhancing the quality of its assets.

In March 2016, to accelerate our global business expansion, we established Shinhan Microfinance, a local subsidiary in Myanmar. Shinhan Microfinance obtained its microfinance business license in July 2016 and launched operations in September 2016. In 2017, it expanded its business operations from Yangon to nearby Bago. In 2018, Shinhan Microfinance is planning to increase its assets and profit volume by diversifying the range of microfinance products it offers.

In January 2018, Shinhan Card acquired Prudential Vietnam Finance Company Limited to enter the consumer finance market in Vietnam. The acquisition is expected to be completed during the second half of 2018 and enable a stronger presence and synergy with Shinhan Bank and Shinhan Investment, both of which currently have operations in Vietnam.

Securities Brokerage Distribution Channels

Our securities brokerage services are conducted principally through Shinhan Investment. As of December 31, 2017, Shinhan Investment had 114 service centers nationwide, and four overseas subsidiaries based in Hong Kong, New York, Vietnam and Indonesia to service our corporate customers.

Approximately 50% of our brokerage branches are located in the Seoul metropolitan area with a focus on attracting high net worth individual customers as well as enhancing synergy with our retail and corporate banking branch network. We plan to continue to explore new business opportunities, particularly in the corporate customer segment, through further cooperation between Shinhan Investment and Shinhan Bank.

Insurance Sales and Distribution Channels

We sell and provide our insurance services primarily through Shinhan Life Insurance. Shinhan Life Insurance, in addition to distributing bancassurance products through our bank branches, also distributes a wide range of life insurance products through its own branch network, an agency network of financial planners and telemarketers, as well as through the Internet. As of December 31, 2017, Shinhan Life Insurance had 181 branches and 10 customer support centers. These branches are staffed by financial planners, telemarketers, agent marketers and bancassurance to meet the various needs of our insurance and lending customers. Our group-wide customer support centers arrange for policy loans (namely loans secured by the cash surrender value of the underlying insurance policy) for our insurance customers and, to a limited extent, other loans to other customers, and also handle insurance payments.

Information Technology

We dedicate substantial resources to maintaining a sophisticated information technology system to support our operations management and provide high quality customer service. Our information and technology system is operated at a group-wide level based on comprehensive group-wide information collection and processing. We also operate a single group-wide enterprise information technology system known as enterprise data warehouse for customer relations management capabilities, risk management systems and data processing. We continually upgrade our group-wide information technology system in order to apply the best-in-class technology to our risk management systems to reflect the changes in our business environment as well as enhance differentiation from our competitors.

In 2013, we completed the construction of the Integrated Data Center, which is responsible for comprehensive management of information technology systems for our subsidiaries on a group-wide basis. This center ensures a stable use of a central information processing facilities for at least 15 years and is designed to maximize operational and cost efficiency as well as enhance information security by combining the various data centers previously used by our subsidiaries. All of our subsidiaries have completed relocation of their information management capabilities to this center by the first half of 2014.

In order to enhance security and trustworthiness of the financial services provided by us, we continually seek to enhance a group-wide set of standards for information security and upgrade the related systems. In 2008, we established group-wide information systems and policies, which have since been continually updated and upgraded. In 2014, we further upgraded the group-wide information security control tower to a best-in-class level and replaced most of our internal information security staff with highly qualified outside experts in order to reinforce our security defense capabilities in the event of cyber breaches. In addition, we have a team within our group to provide specialized data protection and related support services to our smaller operating subsidiaries, and we take active measures to preemptively forestall any security breaches through mock trials.

At the subsidiary level, we also continue to upgrade the information technology infrastructure and services for each of our subsidiaries to enhance the quality of our customer service specific to such subsidiary and thereby bolster their respective competitiveness, including with respect to electronic and mobile banking (including by means of smartphones), online consultation, expanded sales services and customized informational services. In addition, we have recently strengthened our indirect service channels through a major upgrade of the corporate online banking services and expansion of mobile phone-based product offerings and sales and service networks, such as the launch of Shinhan Bank s banking application SOL and upgrades to Shinhan Investment s Shinhan iAlpha application system, in light of the growing base of customers who increasingly access financial services through their mobile phones. We also established in April 2015 a new credit evaluation system with enhanced precision in assessing the creditworthiness of our corporate customers, which has enabled us to manage our credit risk more effectively. On a group-wide level, we are enhancing the efficiency of the information technology operations of our subsidiaries through cloud computing and are planning to build a platform based on blockchain, open application programming interface and big data technology. Furthermore, we have expanded, and will continue to expand, our information technology systems to support the sales and operational capabilities of our overseas subsidiaries and branches through a global customer management system as well as provide country-specific financial services.

The information technology system for each of our subsidiaries is currently backed up on a real-time basis. In 2014, we converted the pre-existing data center to a back-up and disaster recovery center for all our subsidiaries operations in order to provide customer services in a continued seamless manner even in the case of an interruption at Shinhan Data Center. We believe that our centralized back-up systems enable more efficient back-up at a higher level of security.

Competition

Competition in the Korean financial services industry is, and is likely to remain, intense, including as a result of the sustained low interest rate environment (which narrows opportunities to make profit based on the spread between lending rates and funding rates), the continuing sluggishness in the general economy, the growing maturation and saturation of the industry as a whole, the entry of new market participants and deregulation, among others.

In the banking sector, Shinhan Bank competes principally with other national commercial banks in Korea, but also faces competition from a number of additional banking institutions, including branches and subsidiaries of foreign banks operating in Korea, regional banks, government-owned development banks and Korea s specialized banks, such as Korea Development Bank, Industrial Bank of Korea and the National Federation of Fisheries Cooperatives, as well as various other types of financial service providers, including savings institutions (such as mutual savings and finance companies, credit unions and credit cooperatives), investment companies (such as securities brokerage firms, merchant banking corporations and asset management companies) and life insurance companies. As of December 31, 2017, Korea had six major nationwide domestic commercial banks (including Citibank Korea Inc. and Standard Chartered Bank Korea Limited, both of which are domestic commercial banks acquired by global financial institutions), six regional commercial banks and branches and subsidiaries of 38 foreign banks. Foreign financial institutions, many of which have greater experiences and resources than we do, may continue to enter the Korean market and compete with us in providing financial products and services either by themselves or in partnership with existing Korean financial institutions.

In the small- and medium-sized enterprise and retail banking segments, which have been Shinhan Bank s traditional core businesses, competition is expected to increase further. In recent years, Korean banks, including Shinhan Bank, have increasingly focused on stable asset growth based on quality credit, such as corporate borrowers with high credit ratings, loans to SOHO with high levels of collateralization, and mortgage and home equity loans within the limits of the prescribed loan-to-value ratios and debt-to-income ratios. This common shift in focus toward stable growth based on less risky assets has intensified competition as banks compete for the same limited pool of quality credit by engaging in price competition or by other means, although Shinhan Bank has traditionally focused, and will continue to focus, on enhancing profitability rather than increasing asset size or market share, and has avoided, to the extent practicable, engaging in price competition by way of lowering lending rates. In addition, such competition may result in lower net interest margin and reduced overall profitability, especially if the low interest rate environment were to continue for a significant period of time. Although net interest margin may improve if the base interest rate is increased during 2018, the effect on Shinhan Bank s results of operations may be less beneficial due to increased volatility of market interest rates and tighter regulations regarding SOHO loans, including the implementation of additional credit review guidelines for individual businesses. Therefore, if competing financial institutions seek to expand market share by lowering their lending rates, Shinhan Bank may suffer customer loss, especially among customers who select their lenders principally on the basis of lending rates. In response thereto or for other strategic reasons, Shinhan Bank may subsequently lower its lending rates to stay competitive, which could lead to a decrease in its net interest margins and outweigh any potential positive impact on the net interest margin from a general rise in market interest rates. Any future decline in Shinhan Bank s customer base or its net interest margins could have an adverse effect on our results of operations and financial condition.

In the credit card sector, Shinhan Card competes principally with existing monoline credit card companies, credit card divisions of commercial banks, consumer finance companies, other financial institutions and, recently, credit card service providers allied with mobile telecommunications service providers in Korea. Competition has been historically intense in this sector and the market has shown signs of saturation as existing and new credit card service providers make significant investments and engage in aggressive marketing campaigns and promotions to acquire new customers and target customers with high credit quality. While competition has subsided somewhat recently due to stricter government regulations, such as curbs on excessive marketing expenses, competition remains intense and credit card issuers may continue to compete with Shinhan Card for customers by offering lower interest rates and fees, higher credit limits, more attractive promotions and incentives and alternative products such as phone cards, gift cards and low-interest consumer loan products. As a result, Shinhan Card may lose customers or service opportunities to competing credit card issuers and/or incur higher marketing expenses. In addition, the Government regulations adopted in 2012 mandating lower merchant fees chargeable to small- and medium-sized enterprises (which are subject to revision every three years) and the Government guidelines issued in 2013 suggesting lower standard interest rates for cash advances and card loans have reduced, and are likely to continue to limit, the revenues of credit card companies, including Shinhan Card. Beginning January 31, 2016, a further reduction in the merchant fees chargeable to small- and medium-sized enterprises went into effect. In addition, due to the implementation of the Improper Solicitation and Graft Act on September 28, 2016, revenue growth for corporate cards and service related industries such as dining, floral and entertainment have shown signs of decline. In July 2017, the Enforcement Decree of the

Specialized Credit Finance Business Act was amended to expand the range of small- and medium-sized enterprises subject to lower merchant fees. Additional regulations on loans reducing maximum interest rates chargeable from 27.9% to 24%

came into effect in February 2018, placing further downward pressure on the results of operations for credit card companies for 2018 and beyond, and amendments to regulations requiring further downward adjustments to merchant fees are expected to continue in the near future. Furthermore, the Government s recent guidelines to bolster consumer protection and protect customers personal data in the aftermath of data leaks at certain credit companies (not including Shinhan Card) may result in additional compliance costs for Shinhan Card. Customer attrition, together with any further lowering of fees or reduction in base and market interest rates and/or additional expenses from more extensive marketing and promotional campaigns that Shinhan Card might implement to acquire and retain customers, could reduce its revenues and earnings. Furthermore, the average credit quality of Shinhan Card s customers may deteriorate if customers with higher credit quality borrow from our competitors rather than Shinhan Card and it may become more difficult for Shinhan Card to attract and maintain quality customers. In general, the growth, market share and profitability of Shinhan Card s operations may decline or become negative as a result of market saturation in this sector, interest rate competition, pressure to lower fee rates and incur higher marketing expenses, as well as Government regulation and social and economic developments in Korea that are beyond our control, such as changes in consumer confidence levels, spending patterns or public perception of credit card usage and consumer debt. If Shinhan Card fails to maintain or attract new cardholders or increase the card usage by existing customers or experiences deterioration in its asset quality and a rise in delinquency, our business, financial condition and results of operations may be adversely affected.

In other financial services sectors, our other subsidiaries also compete in a highly fragmented market. Some of our competitors, particularly the major global financial institutions, have greater experience and resources than we do.

Consolidation among our rival institutions and the Government s privatization efforts may also add competition in the markets in which we and our subsidiaries conduct business. A number of significant mergers and acquisitions in the industry have taken place in Korea over the past decade, including the acquisition of Hanmi Bank by an affiliate of Citibank in 2004, Standard Chartered Bank s acquisition of Korea First Bank in 2005, Chohung Bank s merger with Shinhan Bank in 2006 and Hana Financial Group s acquisition of Korea Exchange Bank in 2012 and the resulting merger of Hana Bank and Korea Exchange Bank in September 2015. Moreover, in 2014, pursuant to the implementation of the Government s privatization plan with respect to Woori Finance Holdings (now merged into Woori Bank) and its former subsidiaries, Woori Financial, Woori Asset Management and Woori F&I were acquired by KB Financial Group, Kiwoom Securities and Daishin Securities, respectively, and Woori Investment & Securities, Woori Aviva Life Insurance and Woori FG Savings Bank were acquired by NongHyup Financial Group. In addition, in October 2014, the Government s ownership interest in the holding companies of Kwangju Bank and Kyongnam Bank were acquired by JB Financial Group and BS Financial Group (now BNK Financial Group), respectively. In 2015, the Government decided to sell a 30% to 40% interest in Woori Bank to multiple investors in separate blocks ranging from 4% to 10% each. Since December 2016, Korea Deposit Insurance Corporation has consummated sales transactions with seven institutional investors including Kiwoom Securities, Korea Investment and Securities, Hanwha Life Insurance, Tongyang Life Insurance, Eugene Asset Management, Mirae Asset Global Investments and IMM Private Equity for the sale of an aggregate 29.7% interest in Woori Bank in separate blocks. In the securities brokerage sector, Mirae Asset acquired KDB Daewoo Securities in 2016, creating the largest brokerage company in Korea by assets. On June 1, 2016, KB Financial Group completed its acquisition of Hyundai Securities and merged it with its existing brokerage unit, KB Investment & Securities Co, creating the fifth largest brokerage company in Korea by assets. Any of these developments may place us at a competitive disadvantage and outweigh any potential benefit to us in the form of opportunities to acquire new customers who are displeased with the level of services at the newly reorganized entities or to provide credit facilities to corporate customers who wish to maintain relationships with a wide range of banks in order to diversify their sources of funding. We expect that such consolidation and other structural changes in the financial industry will continue. Other financial institutions may seek to acquire or merge with other entities, and the financial institutions resulting from such consolidation may, by virtue of their increased size and business scope, provide greater competition for us. Increased

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competition and continuing consolidation may lead to decreased margins, resulting in a material adverse impact on our future profitability.

Regulatory reforms and the general modernization of business practices in Korea have also led to increased competition among financial institutions in Korea. Since July 2015, the Financial Services Commission has provided, through the Korea Financial Telecommunications and Clearings Institute, the integrated automatic payment transfer management service, which allows account holders to search for, terminate or modify automatic payments they have set up with financial institutions participating in such service (currently including banks, securities companies and other financial institutions such as The Post Office, Korean Federation of Community Credit Cooperatives, National Credit Union Federation of Korea, Mutual Savings Bank and National Forestry Cooperative Federation). In addition, the Financial Services Commission began providing the integrated account management service from December 2016, which allows account holders to search for detailed information of their bank accounts opened in banks participating in such service, close small-sum inactive accounts (i.e., accounts with no transaction activity during the previous one year period and with a balance of less than ₩500,000) and transfer the balance in such accounts to other accounts. Moreover, in December 2017, the Financial Services Commission introduced the my account at a glance system, which enables consumers to view their key financial account information online, including information on banks, insurances, mutual finance, loan and card issuances on one page. The my account at a glance system is expected to become available on mobile channels and expand its scope of services to include savings banks and securities within 2018. Since their introduction, the integrated automatic payment transfer management and integrated account management services have gained widespread acceptance, evidenced by the fact that, as of September 30, 2017, these services have been used by approximately 17.6 million and 8.0 million users, respectively. As the reform of the financial sector continues, competition may become more intense among existing banks, insurance companies, securities companies and other financial organizations and may lead to significant changes in the current Korean financial market. As a result, Shinhan Bank may face difficulties in increasing or retaining its deposits, which in turn may result in an increase in its cost of funding and a decrease in its settlement and remittance service fee revenue.

Furthermore, as the Korean economy further develops and new business opportunities arise, more competitors may enter the financial services industry. For example, as online service providers and technology companies with large-scale user networks, such as Kakao Corp., NAVER and Samsung Electronics, recently make significant inroads in providing virtual payment services through a system based on a growing convergence of financial services and technology commonly referred to as fintech, competition for online customers is growing not just among commercial banks, but also from online and mobile payment service providers. Also, widespread consumer acceptance of mobile phone payment services in lieu of credit card services could add to the competitive threat faced by existing credit card service providers, including our credit card subsidiary. In 2015, the Government announced its plans to allow Internet-only banks to operate in Korea. KT consortium s K-Bank and Kakao consortium s Kakao Bank commenced operations in April 2017 and July 2017, respectively. Internet-only banks may have advantages over traditional banks as the former can pass savings in labor and overhead costs to their customers by offering higher interest rates on deposit accounts, lower loan costs and reduced service fees. Accordingly, commercial banks will likely face increasing pressure to upgrade their service platforms to attract and maintain online users, which represents a growing customer base compared to traditional customers who have primarily conducted banking in-person at physical banking branches.

Recently, following the global financial crisis, the Government has subjected Korean financial institutions to stricter regulatory requirements and guidelines in areas of asset quality, capital adequacy, liquidity and residential and other lending practices (including a requirement to maintain a certain ratio of core capital to total risk exposure, which was introduced in January 2018 in order to control excessive leverage), which has had a dampening effect on competition. The Financial Services Commission implemented the capital requirements of Basel III, whose minimum requirements were phased in sequentially from December 1, 2013 through full implementation by January 1, 2015, based on the guidelines set forth in the amended Regulation on the Supervision of the Banking Business and the Detailed Regulation on the Supervision of the Banking Business. In addition, the Financial Services Commission is currently implementing the Basel III requirements relating to

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liquidity coverage ratio and capital conservation buffer, each of which will be fully phased in by January 1, 2019. As of January 1, 2016, the Financial Services Commission implemented Basel III requirements relating to accumulation of additional capital for systemically important banks and bank holding companies and countercyclical capital buffer requirements. Each year, the Financial Services Commission may designate banks with significant influence (based on size and connectivity with other financial institutions) on the domestic financial system as a domestic systemically important bank and require the accumulation of additional capital in accordance with the highest of: (i) ratio of common equity capital to risk-weighted assets, ranging from 0.0% to 2.0%, depending on the systematic importance evaluation score, (ii) if the bank s holding company is a domestic systemically important bank holding company, the capital ratio corresponding to the additional capital required for the bank holding company under the Financial Holding Company Supervision Regulations, or (iii) if the bank is also a global systemically important bank, as defined by the Basel Committee, the capital ratio as required by the Basel Committee. According to the instructions of the Financial Services Commission, domestic systematically important banks including Shinhan Bank are required to maintain an additional capital buffer of 0.25% since January 1, 2016, with such buffer to increase by 0.25% annually to 1.00% by January 1, 2019. The Financial Services Commission may also, upon quarterly review, determine and require banks to accumulate a required level of countercyclical capital buffer within the range of 0% to 2.5% of risk-weighted assets, taking into account factors such as the degree of increase in credit relative to the gross domestic product. However, there is no assurance that these measures will have the effect of curbing competition or that the Government will not reverse or reduce such measures or introduce other deregulatory measures, which may further intensify competition in the Korean financial services industry.

If, despite our efforts to adapt to the changing macroeconomic environment and comply with new regulations, we are unable to compete effectively in the changing business and regulatory environment, our profit margin and market share may erode and our future growth opportunities may become limited, which could adversely affect our business, financial condition and results of operations. See Item 3.D. Risk Factors Risks Relating to Our Overall Business Competition in the Korean financial services industry is intense, and may further intensify and Item 4.B. Business Overview Supervision and Regulation Financial Investment Services and Capital Markets Act.

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Description of Assets and Liabilities

Loans

As of December 31, 2017, our total gross loan portfolio was ₩277,489 billion, which represented an increase of 6.3% from ₩261,004 billion at December 31, 2016. The increase in our portfolio primarily reflects a 5.7% increase in corporate loans and an 7.1% increase in retail loans.

Loan Types

The following table presents our loans by type for the periods indicated. Except where specified otherwise, all loan amounts stated below are before deduction for loan loss allowances. Total loans reflect our loan portfolio, including past due amounts.

	As of December 31,				
	2013	2014	2015	2016	2017
	(In billions of Won)				
Corporate					
Corporate loans[(1)]	₩ 102,823	₩ 112,145	₩ 125,155	₩ 128,672	₩ 138,277
Public and other[(2)]	2,525	2,135	2,191	2,154	2,298
Loans to banks[(3)]	6,103	4,684	4,653	4,730	2,970
Lease financing	1,721	1,844	1,875	1,814	1,713
Total Corporate	113,172	120,808	133,874	137,370	145,258
Retail					
Mortgages and home equity	46,908	50,652	54,983	56,235	59,078
Other retail[(4)]	30,242	34,278	41,035	47,949	52,512
Total Retail	77,150	84,930	96,018	104,184	111,590
Credit cards	17,665	18,141	18,537	19,450	20,641
Total loans[(5)]	₩ 207,987	₩ 223,879	₩ 248,429	₩ 261,004	₩ 277,489

Notes:

(1) Consists primarily of working capital loans, general purpose loans, bills purchased and trade-related notes and excludes loans to public institutions and commercial banks.
(2) Consists of working capital loans and loan facilities to public institutions and non-profit organizations.
(3) Consists of interbank loans and call loans.
(4) Consists of general unsecured loans and loans secured by collateral other than housing to retail customers.

(5) As of December 31, 2013, 2014, 2015, 2016 and 2017, approximately 90.0%, 89.1%, 89.4%, 88.9% and 88.2% of our total gross loans, respectively, were Won-denominated.

Loan Portfolio

The total exposure of us or our banking subsidiaries to any single borrower and exposure to any single group of companies belonging to the same conglomerate is limited by law to 20% and 25%, respectively, of the Net Total Equity Capital (as defined in Supervision and Regulation).

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Twenty Largest Exposures by Individual Borrower

As of December 31, 2017, our 20 largest exposures, consisting of loans, securities and guarantees and acceptances, totaled ₩55,195 billion. The following table sets forth our total exposures to these top 20 borrowers as of December 31, 2017.

	Loans in Won Currency	Loans in Foreign Currency	Securities	Guarantees and Acceptances	Others	Total Exposure	Impaired Loans and Guarantees and Acceptances
	(In billions of Won)						
Ministry of Strategy and Finance	₩ 0	₩	₩ 15,183	₩	₩	₩ 15,183	₩
The Bank of Korea	980		6,524	0		7,504	
Korea Housing Finance Corporation.	0		5,517			5,517	
Korea Development Bank	14	6	4,802			4,821	
Industrial Bank of Korea.	637		2,295			2,932	
Export-Import Bank of Korea			2,170	54		2,224	
Korea Securities Finance Corporation.	756		1,459			2,215	
Korea Deposit Insurance Corporation.			2,198			2,198	
Samsung Electronics Co., Ltd.		1,920	25		0	1,944	
Nonghyup Bank.	543	8	817	2		1,371	
Korea Land & Housing Corporation			1,279			1,279	
Woori Bank.	94	195	978			1,268	
Kookmin Bank.	477		771	0		1,247	
Korea Investment & Securities Co., Ltd.	919		30			949	
Small& Medium Business Corporations	0		893			893	
KEB Hana Bank	127	129	618	3		878	
LG Electronics Inc.	105	73	209	417		805	
Hotel Lotte Co., Ltd.	170	284	30	205		689	
Korea Student Aid Foundation			652			652	
KB Kookmin Card Co., Ltd.	68		559			628	
Total	₩ 4,891	₩ 2,614	₩ 47,008	₩ 681	₩ 0	₩ 55,195	₩

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Exposure to Main Debtor Groups

As of December 31, 2017, our total exposure to the main debtor groups as identified by the Governor of the Financial Supervisory Service amounted to ₩26,568 billion. The main debtor groups are largely comprised of *chaebols*. The following table shows, as of December 31, 2017, our total exposures to the ten main debtor groups to which we have the largest exposure.

Main Debtor Groups	Loans in Won Currency	Loans in Foreign Currency	Securities	Guarantees and Acceptances	Others	Total Exposure	Amounts of Impaired Loans and Guarantees and Acceptances
			(In billions of Won)				
Samsung	₩ 302	₩ 2,491	₩ 844	₩ 849	₩ 0	₩ 4,486	₩
Hyundai Motors	1,112	1,625	921	309	0	3,968	
Lotte	407	712	1,013	461	0	2,592	
LG	521	206	457	641	0	1,825	
SK	542	243	585	373	0	1,743	
Hanwha	549	229	476	299	0	1,552	
Hyundai Heavy Industries	158	107	35	1,085		1,385	
LS	133	377	266	591		1,367	
GS	344	114	334	113	0	906	
Hyosung	161	408	72	129	0	770	
Total	₩ 4,229	₩ 6,512	₩ 5,003	₩ 4,850	₩ 0	₩ 20,594	₩

Loan Concentration by Industry

The following table shows the aggregate balance of our corporate loans by industry concentration as of December 31, 2017.

Industry	Aggregate Loan Balance (In billions of Won)	Percentage of Total Corporate Loan Balance (Percentages)
Manufacturing	₩ 42,241	29.1%
Real estate, leasing and service	25,032	17.2
Retail and wholesale	19,325	13.3
Finance and insurance	11,420	7.9

Transportation, storage and communication		3,837	2.6
Hotel and leisure		3,728	2.6
Construction		3,185	2.2
Other service[(1)]		13,860	9.5
Other[(2)]		22,630	15.6
Total	₩	145,258	100.0%

Notes:

(1) Includes other service industries such as publication, media and education.

(2) Includes other industries such as agriculture, forestry, mining, electricity and gas.

Maturity Analysis

The following table sets out the scheduled maturities (presented in terms of time remaining until maturity) of our loan portfolio as of December 31, 2017. The amounts below are before deduction of attributable loan loss

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reserves. In the case of installment payment loans, maturities have been adjusted to take into account the timing of installment payments.

	As of December 31, 2017			
	1 Year or Less	Over 1 Year but Not More Than 5 Years	Over 5 Years(1)	Total
	(In billions of Won)			
Corporate:				
Corporate loans	₩ 96,642	₩ 36,388	₩ 5,247	₩ 138,277
Public and other	1,419	733	146	2,298
Loans to banks	2,287	556	127	2,970
Lease financing	670	1,037	6	1,713
Total corporate	₩ 101,018	₩ 38,714	₩ 5,526	₩ 145,258
Retail:				
Mortgage and home equity	₩ 9,540	₩ 15,128	₩ 34,410	₩ 59,078
Other retail	34,333	10,919	7,260	52,512
Total retail	₩ 43,873	₩ 26,047	₩ 41,670	₩ 111,590
Credit cards	₩ 18,171	₩ 2,270	₩ 200	₩ 20,641
Total loans	₩ 163,062	₩ 67,031	₩ 47,396	₩ 277,489

Note:

(1) Includes overdue loans.

We may roll over our corporate loans (primarily consisting of working capital loans and facility loans) and retail loans (to the extent not payable in installments) after we conduct our standard loan reviews in accordance with our loan review procedures. Working capital loans may generally be extended on an annual basis for an aggregate term of up to five years. Facilities loans, which are generally secured, may generally be extended on an annual basis for a maximum of 15 years from the origination date. Retail loans may be extended for additional terms of up to 12 months for an aggregate term of ten years from the origination date for both unsecured loans and secured loans.

Interest Rate Sensitivity

The following table presents a breakdown of our loans in terms of interest rate sensitivity as of December 31, 2017.

	As of December 31, 2017		
	Due Within 1 Year[1]	Due After 1 Year	Total
	(In billions of Won)		
Fixed rate loans[1]	₩ 84,785	₩ 46,828	₩ 131,613
Variable rate loans[2]	78,277	67,599	145,876
Total loans	₩ 163,062	₩ 114,427	₩ 277,489

Notes:

(1) Fixed rate loans are loans for which the interest rate is fixed for the entire term of the loan.

(2) Variable or adjustable rate loans are for which the interest rate is not fixed for the entire term of the loan.

For additional information regarding our management of interest rate risk, see Risk Management.

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Nonaccrual Loans and Past Due Accruing Loans

Except in the case of repurchased loans, we generally recognize interest income on nonaccrual loans using the rate of interest used to discount the future cash flows of such loans for the purpose of measuring impairment loss. Generally, we discontinue accruing of interest on loans (other than repurchased loans) when payment of interest and/or principal becomes past due by 90 days. Loans (other than repurchased loans) are not reclassified as accruing until interest and principal payments are brought current.

We generally do not request borrowers to make immediate repayment of the whole outstanding principal balances and related accrued interest on loans whose interest payments are past due for one to 14 days in the case of commercial loans and one to 30 days in the case of retail loans.

Interest foregone is interest due on nonaccrual loans that has not been accrued in our books of account. In 2013, 2014, 2015, 2016 and 2017, we would have recorded gross interest income of ₩119 billion, ₩113 billion, ₩79 billion, ₩91 billion and ₩96 billion, respectively, on loans accounted for on a nonaccrual basis throughout the respective years, or since origination for loans held for part of the year, had the loans been current with respect to their original contractual terms. The amount of interest income on those loans that was included in our net income in 2013, 2014, 2015, 2016 and 2017 were ₩58 billion, ₩53 billion, ₩39 billion, ₩38 billion and ₩42 billion, respectively.

The following table shows, at the dates indicated, the amount of loans that are placed on a nonaccrual basis and accruing loans which are past due one day or more. The term accruing but past due one day includes loans which are still accruing interest but on which principal or interest payments are contractually past due one day or more. We continue to accrue interest on loans where the total amount of loan outstanding, including accrued interest, is fully secured by cash on deposits.

	As of December 31,				
	2013	**2014**	**2015**	**2016**	**2017**
			(In billions of Won)		
Loans accounted for on a nonaccrual basis[1]					
Corporate	₩ 1,660	₩ 1,358	₩ 1,235	₩ 1,102	₩ 1,035
Retail	217	233	228	243	311
Credit cards	108	152	93	86	67
Sub-total	1,985	1,743	1,556	1,431	1,413
Accruing loans which are contractually past due one day or more as to principal or interest					
Corporate	194	183	176	234	199
Retail	436	374	316	313	440
Credit cards	524	466	399	369	509
Sub-total	1,154	1,023	891	916	1,148
Total	₩ 3,139	₩ 2,766	₩ 2,447	₩ 2,347	₩ 2,561

Note:

(1) Represents either loans that are troubled debt restructuring or loans for which payment of interest and/or principal became past due by 90 days or more (adjusting for any overlap due to loans that satisfy both prongs so as to avoid double counting).

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Troubled Debt Restructurings

The following table presents, at the dates indicated, our loans which are troubled debt restructurings. These loans mainly consist of corporate loans that have been restructured through the process of workout and recovery proceedings. See Credit Exposures to Companies in Workout and Recovery Proceedings. These loans accrue interest at rates lower than the original contractual terms, or involve the extension of the original contractual maturity as a result of a variation of terms upon restructuring.

	As of December 31,				
	2013	2014	2015	2016	2017
	(In billions of Won)				
Loans classified as troubled debt restructurings (excluding nonaccrual and past due loans)	₩ 71	₩ 173	₩ 244	₩ 133	₩ 10
Loans classified as troubled debt restructurings (including nonaccrual and past due loans)	₩ 756	₩ 635	₩ 714	₩ 526	₩ 502

The following table presents, for the periods indicated and with respect to the restructured loans, the amounts that would have been recorded as our interest income under the original contract terms of the restructured loans, and the amounts that were actually recorded as our interest income for such loans under the restructured contractual terms of such loans.

	2013	2014	2015	2016	2017
	(In billions of Won)				
Interest income under the original contractual terms of the restructured loans(1)	₩ 68	₩ 21	₩ 22	₩ 17	₩ 15
Interest income under the restructured contractual terms of the restructured loans(1)	₩ 15	₩ 12	₩ 6	₩ 8	₩ 11

Note:

(1) Includes nonaccrual and past due loans.

The following table presents a breakdown of the outstanding balance and specific allowance for loan losses as of December 31, 2013, 2014, 2015, 2016 and 2017 of corporate loans classified as troubled debt restructurings (including nonaccrual and past due loans) by the type of restructuring to which such loans are subject.

	As of December 31,									
	2013		2014		2015		2016		2017	
	Outstanding Balance	Allowance	Outstanding Balance	Allowance	Outstanding Balance	Allowance	Outstanding Balance	Allowance	Outstanding Balance	Allowance
	(In billions of Won)									

Workout	₩571	₩ 266	₩476	₩ 471	₩506	₩ 215	₩410	₩ 214	₩387	₩ 275
Recovery Proceedings	185	75	159	144	208	63	113	32	109	36
Others(1)							3	2	6	5
Total	₩756	₩ 341	₩635	₩ 615	₩714	₩ 278	₩526	₩ 248	₩502	₩ 316

Note:

(1) Principally consists of loans subject to corporate turnaround or corporate reorganization pursuant to the Debtor Rehabilitation and Bankruptcy Act (also known as the Consolidated Insolvency Act).

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The following table presents the outstanding balance and specific allowance for loan losses as of December 31, 2013, 2014, 2015, 2016 and 2017 of retail loans (including nonaccrual and past due loans) subject to credit rehabilitation programs for retail borrowers. All such loans became modified under credit rehabilitation programs and became beneficiaries of maturity extension and interest rate reductions, while a substantially limited portion of such loans also became beneficiaries of debt forgiveness and deferral. For more information on the credit rehabilitation program, see Credit Exposures to Companies in Workout and Recovery Proceedings Credit Rehabilitation Programs for Delinquent Consumer and Small- and Medium-sized Enterprise Borrowers.

	As of December 31,									
	2013		2014		2015		2016		2017	
	Outstanding Balance	Allowance	Outstanding Balance	Allowance	Outstanding Balance	Allowance	Outstanding Balance	Allowance	Outstanding Balance	Allowance
	(In billions of Won)									
Retail loans subject to credit rehabilitation programs (1):	₩ 41	₩ 30	₩ 45	₩ 27	₩ 61	₩ 40	₩ 84	₩ 49	₩ 118	₩ 70

Note:

(1) Includes nonaccrual and past due loans.

The following table presents, as of the dates indicated and with respect to corporate loans, the amounts of restructured loans that were considered impaired and classified as nonaccrual pursuant to our general interest accrual policy as described in Accrual Policy for Restructured Loans. The table also presents, for the periods indicated and with respect to corporate loans, the amounts of total charge-off on restructured loans and the amounts of charge-off as part of debt-to-equity conversions.

	As of and for the year ended December 31,				
	2013	2014	2015	2016	2017
	(In billions of Won)				
Impaired and nonaccrual restructured loans	₩ 685	₩ 462	₩ 470	₩ 393	₩ 492
Total charge-off of restructured loans	₩ 153	₩ 55	₩ 259	₩ 118	₩ 89
Charge-off as part of debt-to-equity conversion	₩ 29	₩ 32	₩ 51	₩ 22	₩ 68

Credit Exposures to Companies in Workout and Recovery Proceedings

Our credit exposures to restructuring are monitored and managed by our Corporate Credit Support Department. As of December 31, 2017, 0.18% of our total loans, or ₩502 billion (of which ₩492 billion was classified as nonaccrual and ₩10 billion was classified as accruing), was under restructuring. Restructuring of our credit exposures generally takes the form of workout and recovery proceedings.

Workout

Under the old Corporate Restructuring Promotion Act, which expired on December 31, 2015, all creditors that are financial institutions were required to participate in a creditors committee. The old Corporate Restructuring Promotion Act was mandatorily applicable to a wide range of financial institutions in Korea, including commercial banks, insurance companies, asset management companies, securities companies, merchant banks, the Korea Deposit Insurance Corporation and the Korea Asset Management Corporation. Under this act, the approval of financial institution creditors holding not less than 75% of the total debt outstanding of a borrower was required for such borrower s restructuring plan, including debt restructuring and provision of additional funds, which plan would be binding on all the financial institution creditors of the borrower, provided that any financial institution creditor that disagrees with the final restructuring plan approved by the creditors committee has the right to request the creditors committee to purchase its claims at a mutually agreed price. In

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the event that the creditors committee and the dissenting financial institution creditor fail to come to an agreement, the act provided that a mediation committee consisting of seven experts be formed to resolve the matter.

The above-mentioned old Corporate Restructuring Promotion Act expired on December 31, 2015, and a new Corporate Restructuring Promotion Act, which modified and expanded the old act in several respects, was passed in the National Assembly of Korea on March 3, 2016. The new Corporate Restructuring Promotion Act expanded the definition of borrower subject to the act from any enterprise whose total amount of credit granted from financial institution creditors is at least ₩50 billion to any enterprise that is a corporation under the Korean Commercial Code or any other entity performing commercial activities. The new Corporate Restructuring Promotion Act also expanded the definition of creditor who may participate in a creditors committee from financial institution creditors to all creditors who have claims to the borrower through granting of credit.

Under the new act, the creditors that constitute the creditors committee shall be determined at the committee s initial assembly based on the approval of creditors that hold 75% or more of the total debt outstanding held by creditors notified of such initial assembly. Although creditors that are not financial institutions or possess less than 1% of the total amount of claims to the borrower are not required to be notified of the assembly of the creditors committee, such creditors shall not be excluded from the committee if they wish to participate. Resolutions of the creditors committee shall be adopted by the approval of creditors holding 75% or more of the total debt outstanding to the creditors of the committee. However, if a single creditor holds 75% or more of the total debt outstanding to the creditors of the committee, resolutions shall be adopted by a vote of 40% or more of the total number of creditors of the committee, including such single creditor. In addition, a resolution of the creditors committee on debt restructuring shall be effective only with the consent of creditors holding at least 75% of the total amount of the secured claims of the creditors of the committee. The new Corporate Restructuring Promotion Act is set to expire on June 30, 2018.

The total loan amount currently undergoing workout as of December 31, 2017 was ₩387 billion.

Recovery Proceedings

Under the Debtor Rehabilitation and Bankruptcy Act, which took effect on April 1, 2006, court receiverships have been replaced with recovery proceedings. In a recovery proceeding, unlike court receivership proceedings where the management of the debtor company was vested in a court appointed receiver, the existing chief executive officer of the debtor company may continue to manage the debtor company, provided, that (i) neither fraudulent conveyance nor concealment of assets existed, (ii) the financial failure of the debtor company was not due to gross negligence of such chief executive officer, and (iii) no creditors meeting was convened to request, based on reasonable cause, a court-appointed receiver to replace such chief executive officer. Recovery proceeding may be commenced by any insolvent debtor. Furthermore, in an effort to meet global standards, international bankruptcy procedures have been introduced in Korea under which a receiver of a foreign bankruptcy proceeding may, upon receiving Korean court approval of the ongoing foreign bankruptcy proceeding, apply for or participate in a Korean bankruptcy proceeding. Similarly, a receiver in a domestic recovery proceeding or a bankruptcy trustee is allowed to perform its duties in a foreign country where an asset of the debtor is located to the extent the applicable foreign law permits.

As of December 31, 2017, the total loan amount subject to recovery proceedings was ₩109 billion. No loan amount was subject to court receivership or composition proceedings.

Loans in the process of workout and recovery proceedings are reported as nonaccrual loans on our statements of financial position as described in Nonaccrual Loans and Past Due Accruing Loans above since generally, they are past due by more than 90 days and interest does not accrue on such loans. Restructured loans that meet the definition of a troubled debt restructuring are reported as troubled debt restructurings as described above in Troubled Debt

Restructurings. Such restructured loans are reported as either loans or

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securities on our statements of financial position depending on the type of instrument we receive as a result of the restructuring.

Credit Rehabilitation Programs for Delinquent Consumer and Small- and Medium-sized Enterprise Borrowers

In light of the gradual increase in delinquencies in credit card and other consumer credit, the Korean government has implemented a number of measures intended to support the rehabilitation of the credit of delinquent consumer borrowers. These measures may affect the amount and timing of our collections and recoveries on our delinquent consumer credits.

The Credit Counseling and Recovery Service offers two programs for individual debtors, the pre-workout program and the individual workout program, both of which are available to individuals with total debt amounts of ₩1.5 billion or less (secured debt amount of ₩1 billion or less and unsecured debt amount of ₩500 million or less). The pre-workout program is offered to individuals whose delinquency period is between 31 days and 89 days (including those whose delinquency period is between one day and 30 days but with annual income of ₩40 million or less and cumulative delinquency period of 30 days or more within the year immediately preceding the application date), and the individual workout program is offered to individuals whose delinquency period is three months or more. When an individual debtor applies for the pre-workout or individual workout program, the Credit Counseling and Recovery Service will deliberate and resolve on a debt restructuring plan, and once the creditor financial institution that is in a credit recovery support agreement with the Credit Counseling and Recovery Service and holding the majority of each of the unsecured claims and secured claims to the relevant individual debtor agrees to such debt restructuring plan, the plan will be finalized and debt restructuring measures, such as extension of maturity, adjustment of interest rates or reduction of debt, will be taken according to the pre-workout program or individual workout program applied for.

Under the Debtor Rehabilitation and Bankruptcy Act, a qualified individual debtor with outstanding debts in an aggregate amount not exceeding threshold amounts of ₩500 million of unsecured debt and/or ₩1 billion of secured debt may restructure his or her debts through a court-supervised debt restructuring that is binding on creditors.

We may provide the pre-workout program by restructuring loans in the following ways to prevent a borrower, whose debt is expected to be long overdue, to become a financial defaulter:

Extension of maturity: Based on considerations of the type of loan, type of collateral, total loan amount, probability of repayment and credit records, the maturity of unsecured loans may be extended up to 10 years and maturity of secured loans may be extended up to 20 years.

Interest rate adjustment: The interest rate of the loan may be adjusted by up to 50% of the original interest rate, within a range of 5% to 10%; provided that if the original interest rate is less than 5% per annum, no adjustment applies. However, for loans to vulnerable social groups as defined by the Credit Counseling and Recovery Service, the interest rate may be adjusted by up to 65% of the original interest rate. The adjusted interest rate applies to the principal amount following any adjustment thereto as part of the pre-workout program.

Debt forgiveness: Debt forgiveness under the pre-workout program is limited to overdue interest and is not applicable to principal, interest or expenses.

Deferral: Based on considerations of the probability of repayment and credit records, loan repayment may be deferred on a semi-annual basis for a maximum of two years. However, a deferral period of more than one year is only available to borrowers whose total number of principal and interest payments are more than 12 times. In the case of deferring repayment of principal, interest accrues at 3% per annum during the deferral period.

In 2017, the aggregate amount of our retail credit (including credit card receivables) provided by Shinhan Bank which became subject to the pre-workout program was ₩118 billion. We believe that our participation in

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such pre-workout program has not had a material impact on the overall asset quality of our retail loans and credit card portfolio or on our results of operations and financial condition to date.

Under the guidelines of the Financial Supervisory Commission, Korean banks, including Shinhan Bank, operated since 2008 a fast track program which was a liquidity support program for small- and medium-sized companies. As the fast track program ended as of December 31, 2016, the Financial Supervisory Service implemented a swift financial assistance program for small- and medium-sized companies for a period of five years beginning on January 1, 2017. Banks and other financial institutions participating in the program will, based on an evaluation of credit risks, provide financial assistance (including extension of maturity on existing obligations and lower interest rates) to small- and medium-sized companies that are experiencing temporary liquidity crises but have a credit rating exceeding a certain threshold. In principle, the application of the swift financial assistance program to companies will be limited to three years, but such application may be extended, in consultation with the creditor financial institutions concerned, one time for an additional period of up to one year.

Loan Modification Programs for Loans under Troubled Debt Restructuring

We generally offer the following types of concessions in relation to restructured loans: reduction of interest rate, forgiveness of overdue interest, extension of the term for repayment of principal, conversion of debt into equity or a combination of the foregoing. The nature and degree of such concessions vary depending on, among other things, the creditworthiness of the borrower, the size of loans being restructured, the existing terms of the loans and other factors deemed relevant by the relevant creditors committee. We generally do not restructure an existing loan into multiple new loans.

The following table presents a breakdown of the gross amount of loans under restructuring as of December 31, 2013, 2014, 2015, 2016 and 2017 by our loan modification programs, as further categorized according to the loan category and performing versus non-performing status at each fiscal year end.

	December 31, 2013		
Modification Programs	**Non-Performing**	**Performing**	**Total**
		(In billions of Won)	
Extension of due date for principal and interest	₩ 2	₩ 81	₩ 83
Reduction of interest rate	54	283	337
Forgiveness of principal			
Equity conversion			
Additional lending[1]	27	169	196
Others[2]	37	103	140
Total	₩ 120	₩ 636	₩ 756

	December 31, 2014		
Modification Programs	**Non-Performing**	**Performing**	**Total**
		(In billions of Won)	
Extension of due date for principal and interest	₩ 4	₩ 3	₩ 7
Reduction of interest rate	52	260	312

Forgiveness of principal	10		10
Equity conversion			
Additional lending[(1)]	1	198	199
Others[(2)]	61	46	107
Total	₩ 128	₩ 507	₩ 635

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	December 31, 2015		
Modification Programs	Non-Performing	Performing	Total
		(In billions of Won)	
Extension of due date for principal and interest	₩	₩ 87	₩ 87
Reduction of interest rate	119	368	487
Forgiveness of principal			
Equity conversion			
Additional lending(1)	4	19	23
Others(2)	87	30	117
Total	₩ 210	₩ 504	₩ 714

	December 31, 2016		
Modification Programs	Non-Performing	Performing	Total
		(In billions of Won)	
Extension of due date for principal and interest	₩	₩ 92	₩ 92
Reduction of interest rate	3	234	237
Forgiveness of principal			
Equity conversion			
Additional lending(1)		37	37
Others(2)	116	44	160
Total	₩ 119	₩ 407	₩ 526

	December 31, 2017		
Modification Programs	Non-Performing	Performing	Total
		(In billions of Won)	
Extension of due date for principal and interest	₩ 3	₩ 82	₩ 85
Reduction of interest rate	9	299	308
Forgiveness of principal			
Equity conversion			
Additional lending(1)			
Others(2)	70	39	109
Total	₩ 82	₩ 420	₩ 502

Notes:

(1) Represents additional loans provided to the borrower at favorable terms as part of the restructuring package, which may include extension of the due date or reduction of interest rate, among others.

(2) Principally consists of restructured loans whose restructuring terms were not determined as of the date indicated. A loan is deemed to be subject to restructuring upon the commencement of the recovery proceedings or when the relevant creditors committee or our credit officer determines that the borrower will be subject to workout, and in many cases the restructuring terms for such loans are not determined at the time such loans are deemed to be subject to restructuring.

Debt-to-equity Conversion

We distinguish between loans that we consider to be collectible under modified terms and loans that we consider to be uncollectible regardless of any modification of terms. With respect to loans in the latter category, we convert a portion of such loans into equity securities following negotiation with the borrowers and charge off the remainder of such loans as further described below. The equity securities so converted are recorded at fair value, based on the market value of such securities if available or the appraisal value of such securities by an outside appraiser if a market value is unavailable. In 2017, our loans restructured into equity securities amounted to ₩68 billion, which was subsequently charged off.

Debt-to-equity conversion generally has two primary benefits. One, the debt-to-equity conversion reduces the amount of loans and related interest expenses of the borrower, resulting in lesser debt burden and greater liquidity for the borrower, a greater likelihood of its exit from restructuring and the repayment of its obligations to us. Two, in the case of a successful turnaround of the borrower, we are entitled to the upside gains from the increase in the value of the equity securities so converted. Notwithstanding these benefits, however, the resulting impact from the debt-to-equity conversion on our interest income is generally not material as the loans being converted as part of restructuring are generally deemed to be uncollectible regardless any modification of terms. As for the impact on our asset classification, we generally apply the same asset classification standards to both non-restructured and restructured loans. As for restructured loans, we also consider additional factors such as the borrower s adherence to its business plans and execution of the self-help measures, among others, to the extent applicable. In consideration of such criteria, we generally classify loans subject to workout as precautionary. For a general discussion of our loan classifications, see Supervision and Regulation Principal Regulations Applicable to Financial Holding Companies Capital Adequacy.

Evaluation of Loan Modification Programs

We currently do not conduct a systematic or quantitative evaluation of the success of any particular concession by type, whether historically, relative to each other or relative to other financial institutions in Korea, although we do monitor on an individual basis the compliance by the borrower with the modified terms of the restructured loans. This is principally due to the following reasons.

One, in the case of large corporations subject to or about to be subject to restructuring, which represents the most significant restructuring cases in Korea, the restructuring process is generally not driven by us, but by a creditors committee involving several large creditor financial institutions, and in the case of very large corporations or corporations that are members of large business conglomerates, the process frequently involves the guidance of the Government in light of the potential ripple effects of the restructuring on the general economy. Hence, it is difficult for us to collect data that would help us to evaluate the success of a particular concession based on the credit profile of the borrower and the type of concessions offered.

Two, the unavailability of systematic analysis notwithstanding, our general sense is that the restructuring cases in Korea have, to a large part, been successful as measured in terms of the ability of the borrowers to exit restructuring programs relatively quickly and further that the failed cases have not been particularly material. As a result, to date, we have not found it particularly necessary or helpful to expend the time and resources required to conduct a systematic analysis for purposes of evaluating the success of concessions by the type of a particular concession offered.

We do, however, measure the success of concessions in limited ways, that is, principally in terms of how well the borrower complies with the terms and conditions of the restructuring plan as agreed between the borrower and its creditor institutions. A restructuring plan typically includes a business plan and self-help measures to be undertaken by the borrower. We monitor the borrower s compliance with the restructuring plan on a periodic basis (namely, annual, semiannual or quarterly in accordance with the terms of the restructuring plan) and evaluate the success thereof principally in terms of three attributes: (i) the progress in the execution of the business plan, (ii) the progress in the execution of the self-help measures and (iii) other qualitative factors such as major developments in the general economy, the regulatory environment, the competitive landscape, the quality of senior management and personnel, and transparency in management. We also closely monitor the cash inflows and outflows of the borrower, and the creditors committee typically has the right to participate in decision-making related to major spending and borrowings by the borrower.

Accrual Policy for Restructured Loans

For purposes of our accrual policy, we classify restructured loans principally into (i) loans subject to workout pursuant to the Corporate Restructuring Promotion Act and (ii) loans subject to recovery proceedings pursuant to the Debtor Rehabilitation and Bankruptcy Act, which is the comprehensive bankruptcy-related law in Korea. See Credit Exposures to Companies in Workout and Recovery Proceedings. As for loans subject to workout, our general policy is to discontinue accruing interest on a loan when payment of principal and/or interest thereon becomes past due by 90 days or more, as described above in Nonaccrual Loans and Past Due Accruing Loans . Interest is recognized on these loans on a cash basis (i.e., when collected) from the date such loan is reclassified as non-accruing, and such loans are not reclassified as accruing until the overdue principal and/or interest amounts are paid in full. This general policy also applies to loans subject to workout even if such loans are restructured loans. In the case of loans subject to recovery proceedings, we discontinue accruing interest immediately upon the borrowers becoming subject to recovery proceedings (even if such loans are not yet delinquent) in light of the heightened uncertainty regarding the borrower s ability to repay. Interest on such loans are recognized on a cash basis and such loans are not reclassified as accruing until the borrower exits recovery proceedings. Accordingly, under our accrual policy, the number of payments made on a nonaccrual restructured loan is not a relevant factor in determining whether to reinstate such loan to the accrual status.

Determination of Performance of Restructured Loans

In determining whether a borrower has satisfactorily performed its obligations under the existing loan terms, we principally review the payment history of the borrower, namely whether the borrower has been delinquent by one day or more pursuant to our general interest accrual policy. In determining whether a borrower has shown the capacity to continue to perform under the restructured terms, we primarily rely upon the assessment of our credit officers (or the creditors committee in the case of large corporate borrowers with significant outstanding loans) of the likelihood of the borrower s ability to repay under the restructured terms, which assessment takes into account the size of the loans in question, the credit profile of the borrower, the original terms of the loans and other factors deemed relevant by the relevant credit officers. Depending on various factors such as the size of the loans in question and the credit profile of the borrower, we or the relevant creditors committee, as the case may be, sometimes engage an outside advisory firm to perform further due diligence in order to supplement the aforementioned assessment. In certain cases, the borrowers also submit self-help proposals to facilitate obtaining the approval for restructuring, which measures are then also taken into consideration by our credit officers or the relevant creditors committees, as the case may be, in determining their future capacity to continue to perform under the restructured terms.

Charge-off of Restructured Loans

As for loans that we consider to be collectible under modified terms (for example, by extending the due date for the payment of principal and/or interest or reducing the interest rate below the applicable interest rate to a rate below the prevailing market rate, or a combination of the foregoing), we generally restructure such loans under the modified terms and do not charge off any portion of such loans.

As for loans that we consider to be uncollectible regardless of any modification of terms, we negotiate with the borrower to have a portion of such loans converted into equity securities (usually common stock) of the borrower in consideration, among others, of (i) the degree to which such conversion will alleviate the debt burdens and liquidity concerns of the borrower, (ii) our potential upside from the gain in the value of the equity securities compared to the likelihood of collection if the loans were not converted into equity securities, and (iii) the borrower s concerns regarding its shareholding structure subsequent to such conversion. We then charge off the remainder of the loans not converted into equity securities. The value of the equity securities so converted is recorded at fair value, based on the market value of such securities if available or the appraisal value of such securities by an outside appraiser if a market value is unavailable.

Since we generally do not accrue interest on loans subject to recovery proceedings while we generally accrue interest on loans subject to workout unless past due by 90 days or more, charge-off is not a relevant factor we consider when determining the accrual status of a particular restructured loan.

We continue to accrue interest on restructured loans if we conclude that repayment of interest and principal contractually due on the entire debt is reasonably assured. Such conclusion is reached only after we have carefully reviewed the borrower s ability to repay based on an assessment, among others, of various factors such as the size of the loans in question and the credit quality of the borrower by our credit officer or the relevant creditors committee as supplemented by the due diligence by outside advisory firms, as the case may be.

Potential Problem Loans

We operate an early warning system in order to enable a more systematic and real-time monitoring of loans with significant potential of default. This system assists our management in making decisions by identifying loans which have serious doubt as to the ability of the borrowers to comply with their respective loan repayment terms as well as loans with significant potential of non-repayment.

We classify potential problem loans as loans that are designated as early warning loans and reported to the Financial Supervisory Service. The early warning loans designation applies to borrowers that have been (i) identified by our early warning system as exhibiting signs of credit risk based on the relevant borrower s financial data, credit information and/or transactions with banks and, following such identification and (ii) designated by our loan officers as potential problem loans on their evaluation of known information about such borrowers possible credit problems. Such loans are required to be reported on a quarterly basis to the Financial Supervisory Service. If a borrower s loans are designated as early warning loans pursuant to the process described above and included in our quarterly report to the Financial Supervisory Service, we consider this to be an indication of serious doubt as to such borrower s ability to comply with repayment terms in the near future. As of December 31, 2017, we had ₩979 billion of potential problem loans.

Provisioning Policy

We conduct periodic and systematic detailed reviews of our loan portfolios to identify credit risks and to establish the overall allowance for loan losses. Our management believes the allowance for loan losses reflects the best estimate of the probable loan losses incurred as of the date of each statement of financial position.

We first assess whether objective evidence of impairment exists individually for loans and receivables that are individually significant, and individually or collectively for financial assets that are not individually significant. If we determine that no objective evidence of impairment exists for an individually assessed financial asset, whether significant or not, we include the asset in a group of financial assets with similar credit risk characteristics and collectively assess them for impairment. Assets that are individually assessed for impairment and for which an impairment loss is or continues to be recognized are not included in a collective assessment of impairment.

If there is objective evidence that a financial asset, such as a loan or receivable, has suffered impairment loss, the amount of the impairment loss is measured as the difference between the asset s carrying amount and the present value of estimated future cash flow (excluding anticipated future credit losses) discounted at the financial asset s original effective interest rate (i.e., the effective interest rate computed at initial recognition).

If the financial asset in question is a loan or receivable with a floating rate, the discount rate used to evaluate impairment loss is the current effective interest rate defined in the relevant transaction agreement. The present value of estimated future cash flows of secured financial assets is calculated by including cash flows from collateral after deducting costs to acquire and sell the collateral, regardless of the probability of realization of such collateral.

In assessing collective impairment, we rate and classify financial assets based on credit risk assessment or credit rating assessment process that takes into account asset type, industry, regional location, collateral type, delinquency and other relevant factors.

Future cash flow of financial assets applicable to collective impairment assessment is estimated by using statistical modeling of historical trends of the probability of default, timing of recoveries and the amount of loss incurred, as adjusted for management s judgment as to whether current economic and credit conditions are such that the impairment losses are likely to be greater or less than suggested by historical modeling. When adjusting future cash flow based on historical modeling, we ensure that such adjustments are in line with changes and trends of observable data. Methodologies and assumptions used to estimate future cash flow are evaluated on a regular basis in order to reduce any discrepancy between impairment loss estimation and actual loss. See Item 5.A. Operating Results Critical Accounting Policies Impairment of Financial Assets Allowance for Loan Losses.

Corporate Loans

We review corporate loans annually for potential impairment through a formal credit review. In addition, our loan officers consider the credits for impairment throughout the year if there is an indication that an impairment event has occurred.

Under IFRS, a loan is impaired if objective evidence indicates that a loss event has occurred after the initial recognition of the asset, and if the loss event had a negative effect on the estimated future cash flows of that asset and can be estimated reliably. We consider, among others, the following loans to be impaired:

- loans whose principal or interest amount is more than 90 days past due;
- loans that by reason of non-performance becomes subject to write-off, charge-off, debt restructuring (including recovery proceedings and workout) or bankruptcy;
- loans to customers whose credit record shows past instances of delinquency, enforcement of guarantee or subrogation; and
- loans to customers who become finally insolvent by an order to suspend settlement of personal checks, corporate checks or promissory note.

Loan loss allowances for corporate loans are established based on whether a particular loan is impaired. Corporate loans with relatively small balances are evaluated collectively for impairment as they are managed collectively.

Loans individually identified for review and considered impaired

Consistent with the internal credit risk monitoring policies, we evaluate impaired loans with relatively large balances (typically more than ₩3 billion) individually for impairment. Loan loss allowances for these loans are generally established by discounting the estimated future cash flows (both principal and interest) we expect to receive using the loan s effective interest rate. We consider the likelihood of all possible outcomes in determining our best estimate of expected future cash flows. Management consults closely with individual loan officers and reviews the cash flow assumptions used to ensure these estimates are valid.

We establish allowances for impaired corporate loans when the discounted cash flow of the loan is lower than its carrying amount. The allowance is equal to the difference between the discounted cash flow amount of the loan and its carrying amount.

We may also measure impairment by reference to the loan s observable market price; however this information is not commonly available in Korea.

Loans collectively evaluated for impairment

We also establish allowances for impaired corporate loans with relatively small balances (typically ₩3 billion or less). We manage these loans on a portfolio basis and therefore collectively evaluate them for

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impairment since it is impractical to analyze each such loan on an individual basis. The allowance for such loans is determined based on loss factors taking into consideration past performance of the portfolio, previous loan loss history and charge-off information.

We identify loss factors based on the discounted cash flow (DCF) model using a statistical tool with look-back periods longer than a year. For impaired corporate loans whose amounts are relatively small, we use the collective DCF model, under which cash flow projections for the relevant loans are not individually computed for each borrower, but are collectively computed for a group of loans sharing similar characteristics (for example, retail versus corporate, secured versus unsecured, and so forth), except that, when we discount the projected cash flow at the present value, we apply the interest rate effective prior to impairment specific to each borrower.

Loans not specifically identified as impaired

We establish allowances collectively for non-impaired corporate loans to reflect losses incurred within the portfolio which have not yet been specifically identified as impaired. We use the probability of default / loss given default method, also known as the Advanced Internal Rating-Based (AIRB) approach under Basel II, to calculate the historical loss rate on migration analysis based on measurable long-term risk factors such as probability of default from risk grading and loss given default based on the Basel II framework.

As for the probability of default-based loan grouping, corporate loans are grouped into different risk classes based on the credit rating assigned by the relevant credit evaluation model, and retail loans are grouped into different risk classes based on the type of the loan, maturity structure and the duration of delinquency.

As for the loss given default-based loan grouping, secured loans are grouped into different risk classes based on the type of collateral, the location of the collateral and the loan-to-value ratio to which they are subject, and unsecured loans are grouped into different risk classes based on the type of the loan.

Retail Loans

We consider the following retail loans to be impaired for an individual assessment of impairment:

- loans whose principal or interest amount is more than 90 days past due;
- loans that by reason of non-performance becomes subject to write-off, charge-off, debt restructuring (including recovery proceedings and workout) or bankruptcy;
- loans to customers whose credit record shows past instances of delinquency, enforcement of guarantee or subrogation; and
- loans to customers who become finally insolvent by an order to suspend settlement of personal checks, corporate checks or promissory note.

The provisioning policy for retail loans is similar to that for corporate loans, except that different groupings are used for retail loans for purposes of determining probability of default and loss given default in that all retail loans, regardless of their size, are collectively (rather than individually) assessed due to difficulties in obtaining personal information, such as personal income and assets.

For loan losses for retail loans, we also establish allowances based on loss factors taking into consideration the historical performance of the portfolio, previous loan loss history and charge-off information over a nine-year look-back period for loans secured by real estate and a four-year look-back period for unsecured loans and other secured loans.

We further adjust the loss factors based on factors that may impact loss recognition which have not been adequately captured by our historical analysis. These factors include:

- changes in economic and business conditions such as levels of unemployment and housing price;

- changes in the nature and volume of the portfolio, including any concentration of credits; and

- external factors such as regulatory or government requirements.

Credit Cards

Prior to 2017, we established an allowance for the credit card portfolio using a roll-rate model. A roll-rate model is a statistical tool used to monitor the progression of loans based on aging of the balance and established loss rates. The actual loss rates derived from this model are used to project the percentage of losses within each aging category based on performance over a five-year look-back period. BASEL II requires a minimum of nine years of data collection (consisting of a minimum five-year observation period for defaults and a minimum four-year observation period for post-default recoveries) as a necessary condition to using the internal model approach. After its merger with LG Card in 2007, Shinhan Card has worked to establish a risk management system and met the BASEL II nine-year data collection requirement in October 2016. Through the operation of a credit review system and risk management system based on Basel II requirements, we have gained the necessary data to create internal models that can calculate PD/LGD and credit conversion factors for different groups of borrowers of financial assets.

At the end of December 2016, the Financial Supervisory Service granted Shinhan Card final approval to use the internal model approach. During the first quarter of 2017, Shinhan Card completed the establishment of the IFRS loan loss calculation system, for example, by replacing BASEL II risk components with risk components for financial reporting in accordance with IAS 39, and Shinhan Card revised the calculation methodology of loan losses from a roll-rate model to an internal model approach.

The internal model approach calculates separate default rates and loss given default for different groups of customers, differentiated based on the characteristics of both the customers and the products that they use. The internal model approach disaggregates customers into more than twice the number of groups than does the roll-rate model. Whereas the roll-rate model does not distinguish between customers with high and low risks of default when calculating roll rates, the internal model approach allows for a more sophisticated calculation of loan loss that reflects the customers credit ratings.

Our general policy is to be proactive in our collection procedures, and we therefore emphasize collections at an early stage of delinquency, although we increase the level of collection efforts as the delinquency period increases with respect to the relevant account. Efforts to collect from cardholders whose account balances are up to 30 days past due are generally made by our credit support centers at Shinhan Card.

For card accounts with balances that are more than 30 days past due, we generally assign collection to our collection branches. During the first two months of their appointment, these collection branches rely on postal or telephone notice and take measures to locate and provisionally attach accounts receivables or other properties of the delinquent cardholders. For card accounts that are charged off, we outsource collection to external collection centers such as Shinhan Credit Information, which is our subsidiary, Mirae Credit Information Services Corp. and Koryo Credit Information.

Loan Aging Schedule

The following table shows our loan aging schedule (excluding accrued interest) for all loans as of the dates indicated.

As of December 31,	Current Amount	%	Past Due Up to 3 Months Amount	%	Past Due 3-6 Months Amount	%	Past Due More Than 6 Months Amount	%	Total Amount
	(In billions of Won, except percentages)								
2013	₩ 205,282	98.70	₩ 1,508	0.73	₩ 420	0.20	₩ 777	0.37	₩ 207,987
2014	221,273	98.84	1,320	0.59	706	0.32	580	0.26	223,879
2015	245,997	99.02	1,098	0.44	781	0.31	553	0.22	248,429
2016	258,650	99.10	1,180	0.45	643	0.25	531	0.20	261,004
2017	274,935	99.08	1,479	0.53	616	0.22	459	0.17	277,489

Non-Performing Loans

Non-performing loans are defined as loans past due by more than 90 days. The following table shows, as of the dates indicated, the amount of the total non-performing loan portfolio and as a percentage of our total loans.

	As of December 31, 2013	2014	2015	2016	2017
	(In billions of Won, except percentages)				
Total non-performing loans	₩ 1,197	₩ 1,286	₩ 1,333	₩ 1,174	₩ 1,075
As a percentage of total loans	0.58%	0.57%	0.54%	0.45%	0.39%

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Analysis of Non-Performing Loans

The following table sets forth, for the periods indicated, the total non-performing loans by the borrower type.

As of December 31,												
2013			2014			2015			2016			20
tal Loans	Non-Performing Loans (1)	Ratio of Non-Performing Loans	Total Loans	Non-Performing Loans (1)	Ratio of Non-Performing Loans	Total Loans	Non-Performing Loans (1)	Ratio of Non-Performing Loans	Total Loans	Non-Performing Loans (1)	Ratio of Non-Performing Loans	Total Loans
(In billions of Won, except percentages)												
2,823	₩ 529	0.51%	₩ 112,145	₩ 551	0.49%	₩ 125,155	₩ 664	0.53%	₩ 128,672	₩ 480	0.37%	₩ 138,277
2,525			2,135			2,191	1	0.05	2,154			2,298
5,103			4,684			4,653			4,730			2,970
1,721	11	0.64	1,844	15	0.81	1,875	16	0.85	1,814	20	1.10	1,713
3,172	540	0.48	120,808	566	0.47	133,874	680	0.51	137,370	500	0.36	145,258
5,908	41	0.09	50,652	56	0.11	54,983	45	0.08	56,235	33	0.06	59,078
0,242	174	0.58	34,278	173	0.50	41,035	193	0.47	47,949	222	0.46	52,512
7,150	215	0.28	84,930	229	0.27	96,018	238	0.25	104,184	255	0.24	111,590
7,665	442	2.50	18,141	491	2.71	18,537	415	2.24	19,450	419	2.15	20,641
7,987	₩ 1,197	0.58%	₩ 223,879	₩ 1,286	0.57%	₩ 248,429	₩ 1,333	0.54%	₩ 261,004	₩ 1,174	0.45%	₩ 277,489

Note:

(1)

The number of days past due of restructured credit card loans is calculated from the first date of non-payment regardless of subsequent modification of terms.

(2) Includes debtors such as local and regional authorities, state-owned enterprises and non-profit organizations.

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Non-Performing Loans by Industry

The following table sets forth a breakdown of our non-performing corporate loans by industry as of December 31, 2017.

Industry	Aggregate Non-Performing Corporate Loan Balance	Percentage of Total Non-Performing Corporate Loan Balance
	(In billions of Won)	(Percentages)
Construction	₩ 22	6.5%
Manufacturing	145	42.5
Real estate, leasing and service	33	9.7
Retail and wholesale	49	14.4
Finance and insurance	1	0.3
Hotel and leisure	15	4.4
Transportation, storage and communication	12	3.5
Other service[(1)]	23	6.7
Other[(2)]	41	12.0
Total	₩ 341	100.0%

Notes:

(1) Includes other service industries such as publication, media and education.
(2) Includes other industries such as agriculture, forestry, mining, electricity and gas.

Top 20 Non-Performing Loans

As of December 31, 2017, our 20 largest non-performing loans accounted 11.6% of our total non-performing loan portfolio. The following table shows, at the date indicated, certain information regarding our 20 largest non-performing loans.

	As of December 31, 2017		
	Industry	Gross Principal Outstanding	Allowance for Loan

						Losses
			(In billions of Won)			
1	Borrower A	Construction	₩	18	₩	2
2	Borrower B	Other service		15		6
3	Borrower C	Retail and wholesale		12		12
4	Borrower D	Manufacturing		11		6
5	Borrower E	Manufacturing		9		9
6	Borrower F	Real estate, leasing and service		8		
7	Borrower G	Manufacturing		5		2
8	Borrower H	Other service		4		
9	Borrower I	Real estate, leasing and service		4		
10	Borrower J	Manufacturing		4		1
11	Borrower K	Manufacturing		4		4
12	Borrower L	Manufacturing		4		2
13	Borrower M	Manufacturing		4		4
14	Borrower N	Real estate, leasing and service		4		1
15	Borrower O	Other service		4		2
16	Borrower P	Manufacturing		3		1
17	Borrower Q	Manufacturing		3		3
18	Borrower R	Manufacturing		3		
19	Borrower S	Transportation, storage, and communication		3		1
20	Borrower T	Real estate, leasing and service		3		
			₩	125	₩	56

Non-Performing Loan Strategy

One of our primary objectives is to prevent our loans from becoming non-performing. Through our corporate credit rating system, which is designed to prevent our loan officers from extending new loans to borrowers with high credit risks based on the borrower s credit rating, we seek to reduce credit risk related to future non-performing loans. Our early warning system is designed to bring any sudden increase in a borrower s credit risk to the attention of our loan officers, who then closely monitor such loans.

If a loan becomes non-performing notwithstanding such preventive mechanism, an officer at the branch level responsible for monitoring non-performing loans will commence due diligence on the borrower s assets, send a notice demanding payment or a notice that we will take or prepare for legal action.

At the same time, we also initiate our non-performing loan management process, which includes:

- identifying loans subject to a proposed sale by assessing the estimated losses from such sale based on the estimated recovery value of collateral, if any, for such non-performing loans;
- identifying loans subject to charge-off based on the estimated recovery value of collateral, if any, for such non-performing loans and the estimated rate of recovery of unsecured loans; and
- to a limited extent, identifying commercial loans subject to normalization efforts based on the cash-flow situation of the borrower.

Once the details of a non-performing loan are identified, we pursue early solutions for recovery. Actual recovery efforts for non-performing loans are handled by the relevant department, depending on the nature of such loans and the borrower, among others. The officers or agents of the responsible departments and units use a variety of methods to resolve non-performing loans, including:

- making phone calls and paying visits to the borrower to request payment;
- continuing to assess and evaluate assets of our borrowers; and
- if necessary, initiating legal action such as foreclosures, attachment and litigation.

In order to promote speedy recovery on loans subject to foreclosures and litigation, the branch responsible for handling these loans may transfer them to the relevant unit at headquarters.

Our policy is to commence legal action within one month after default on promissory notes and four months after delinquency of payment on other types of loans. For loans to insolvent or bankrupt borrowers or when we conclude that it is not possible to recover through normal procedures, we take prompt legal actions regardless of the grace period.

In addition to making efforts to collect on these non-performing loans, we take other measures to reduce the level of our non-performing loans, including:

- selling non-performing loans to third parties including the Korea Asset Management Corporation;
- entering into asset-backed securitization transactions with respect to non-performing loans;
- managing retail loans that are three months or more past due through Shinhan Credit Information under an agency agreement; and
- using third-party collection agencies including credit information companies.

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In 2017, we sold non-performing loans in the amount of ₩146 billion to third parties, including ₩31 billion transferred to Meritz Securities Co., Ltd., a merchant banking corporation. Loans transferred to third parties meet the criteria of true sale and are derecognized accordingly.

The following table presents a roll-forward of our non-performing loans in 2017.

		(In billions of Won)
Non-performing loans as of December 31, 2016	₩	1,174
Additional non-performing loans due to delinquency		545
Loans sold		(146)
Loans charged off		(378)
Loans modified and returned to performing		(42)
Other adjustments(1)		(78)
Non-performing loans as of December 31, 2017	₩	1,075

Note:

(1) Represents loans paid down or paid off and loans returned to performing other than as a result of modification. We do not separately collect and analyze data relating to non-performing loans other than those that were sold, charged off, modified and returned to performing, or transferred to held-for-sale investment portfolio.

Allocation of Allowance for Loan Losses

The following table presents, as of the dates indicated, the allocation of our loan loss allowance by loan type.

	As of December 31,									
	2013		2014		2015		2016		2017	
	(In billions of Won, except percentages)									
	Amount	Loans % of Total Loans	Amount	Loans % of Total Loans	Amount	Loans % of Total Loans	Amount	Loans % of Total Loans	Amount	Loans % of Total Loans
Corporate										
Corporate loans	₩ 1,576	63.7%	₩ 1,502	60.1%	₩ 1,357	58.5%	₩ 1,312	55.6%	₩ 1,285	55.6%
Public and other	10	0.4	11	0.4	8	0.4	8	0.3	5	0.2
	5	0.2	12	0.5	10	0.4	8	0.3	9	0.4

Loan to banks										
Lease financing	21	0.9	26	1.0	29	1.3	34	1.4	50	2.2
Total corporate	1,612	65.1	1,551	62.0	1,404	60.6	1,362	57.7	1,349	58.4
Retail										
Mortgages and home equity	26	1.1	31	1.2	33	1.4	29	1.2	27	1.2
Other retail	190	7.7	198	7.9	206	8.9	267	11.3	331	14.3
Total retail	216	8.7	229	9.2	239	10.3	296	12.5	358	15.5
Credit cards	648	26.2	721	28.8	675	29.1	703	29.8	604	26.1
Total allowance for loan losses	₩ 2,476	100.0%	₩ 2,501	100.0%	₩ 2,318	100.0%	₩ 2,361	100.0%	₩ 2,311	100.0%

Our total allowance for loan losses decreased by ₩50 billion, or 2.1%, to ₩2,311 billion as of December 31, 2017 from ₩2,361 billion as of December 31, 2016, primarily due to an increase in reversal of allowances for credit card loan losses as a result of changing the allowance model of Shinhan Card from a roll-rate model in 2016 to an internal model approach in 2017, which was partially offset by an increase in allowance for retail loan losses due to an increase in exposure to retail customers during 2017.

Our total allowance for loan losses increased by ₩43 billion, or 1.9%, to ₩2,361 billion as of December 31, 2016 from ₩2,318 billion as of December 31, 2015, primarily due to an increase in exposure to retail customers during 2016 as well as a decrease in charge-off for non-performing loans compared to 2015.

Analysis of Allowance for Loan Losses

The following table presents an analysis of our loan loss experience for each of the years indicated.

	2013	2014	2015	2016	2017
			(In billions of Won, except percentages)		
Balance at the beginning of the period	₩ 2,800	₩ 2,476	₩ 2,501	₩ 2,318	₩ 2,361
Amounts charged against income	1,082	895	1,022	1,103	801
Gross charge-offs:					
Corporate:					
Corporate loans	(799)	(515)	(731)	(758)	(376)
Public and other			(2)	(1)	(1)
Loan to banks					
Lease financing	(33)	(16)	(60)	(42)	(4)
Retail:					
Mortgage and home equity	(4)	(3)			(2)
Other retail	(242)	(153)	(128)	(130)	(137)
Credit cards	(657)	(500)	(520)	(462)	(540)
Total gross charge-offs	(1,735)	(1,187)	(1,441)	(1,393)	(1,060)
Recoveries:					
Corporate:					
Corporate loans	150	177	88	125	81
Public and other		11			
Loan to banks					
Lease financing	1	2	1	1	1
Retail:					
Mortgage and home equity			3		1
Other retail	28	19	24	35	43
Credit cards	217	182	171	176	185
Total recoveries	396	391	287	337	311
Other	(67)	(74)	(51)	(4)	(102)
Net charge-offs	(1,406)	(870)	(1,205)	(1,060)	(851)
Balance at the end of the period	₩ 2,476	₩ 2,501	₩ 2,318	₩ 2,361	₩ 2,311
	0.68%	0.41%	0.51%	0.42%	0.32%

Ratio of net charge-offs during the period to average loans outstanding during the period

Loan Charge-offs

Our gross charge-offs decreased by 23.9% from ₩1,393 billion in 2016 to ₩1,060 billion in 2017, primarily due to a decrease in the amount of charge-offs for corporate loans in 2017 compared to 2016. Our gross charge-offs decreased by 3.3% from ₩1,441 billion in 2015 to ₩1,393 billion in 2016, primarily due to a decrease in the amount of charge-offs for credit card loans compared to 2015. Our gross charge-offs increased from ₩1,187 billion in 2014 to ₩1,441 billion in 2015, primarily due to our ongoing efforts to improve asset quality.

In 2017, the charge-off on restructured loans amounted to ₩89 billion, of which ₩68 billion was related to loans converted into equity securities as part of restructuring. With respect to a loan that we consider to be

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uncollectible regardless of any modification of terms, we convert a portion of such loan into equity securities following negotiation with the borrower and charge off the remainder of such loan as previously discussed in Troubled Debt Restructurings Charge-off of Loans Subject to Restructuring. The equity securities so converted are recorded at fair value, based on the market value of such securities if available or the appraisal value of such securities by an outside appraiser if a market value is unavailable.

We attempt to minimize loans to be charged off by practicing a sound credit approval process based on credit risk analysis prior to extending loans and a systematic management of outstanding loans. For charge-off of restructured loans, see Loan Modification Programs for Loans under Restructuring Charge-off of Restructured Loans above.

Loans to be Charged-off

Loans are charged off if they are deemed to be uncollectible by falling under any of the following categories:

- loans for which collection is not foreseeable due to insolvency or bankruptcy, dissolution or the termination of the debtor s business;
- loans for which collection is not foreseeable due to the death or disappearance of debtors;
- loans for which collection expenses exceed the collectable amount;
- loans for which collection is not possible through legal or any other means;
- payments in arrears in respect of credit cards that are overdue for more than six months;
- payments outstanding on unsecured retail loans that are overdue for more than nine months;
- payments in arrears in respect of leases that are overdue for more than 12 months;
- the portion of loans classified as estimated loss, net of any recovery from collateral, which is deemed to be uncollectible; or
- domestic loans that are required by the Financial Supervisory Service to be charged-off, or loans held by our foreign subsidiaries or branches for which a charge-off or special provisioning is required by the relevant regulatory authority.

Timeline for Charge-off

Shinhan Bank s loans to be charged-off must be charged-off within one year of the month they are deemed to be uncollectible. If such loans are not charged-off within one year, the reason for the delay must be reported to Shinhan Bank s Audit Department.

Procedure for Charge-off Approval

An application for Shinhan Bank s loans to be charged-off is submitted by the relevant branch or department to the Credit Collection Department. The Credit Collection Department refers the application to the Audit Department for their review to ensure compliance with the Bank s internal procedures for charge-offs. The Credit Collection Department, after reviewing the application to confirm that it meets relevant requirements, seeks approval from the Financial Supervisory Service for the charge-offs, which is typically granted. Once the Financial Supervisory Service approves (except for household loans with estimated losses of ₩10 million or less, whose charge-off is considered automatically approved by the Financial Supervisory Service), loans are charged-off upon approval by the President of Shinhan Bank. As for Shinhan Card, it generally charges off receivables that are 180 days past due following internal review.

Treatment of Loans Charged-off

Once loans are charged off, they are derecognized from our statements of financial position and are classified as charged-off loans. We continue collection efforts in respect of these loans through third-party collection agencies, including the Korea Asset Management Corporation, and Shinhan Credit Information, which is our subsidiary. The General Manager of the Credit Collection Department must report to the Financial Supervisory Service the amounts of loans permanently written off or recovered during each reporting period.

Treatment of Collateral

When we determine that a loan collateralized by real estate cannot be recovered through normal collection channels, we generally petition a court to foreclose and sell the collateral through a court-supervised auction within one month after default and insolvency and within four months after delinquency. However, this procedure does not apply to companies under restructuring, recovery proceedings, workout or other court proceedings where there are restrictions on such auction procedures. Filing of such petition with the court generally encourages the debtor to repay the overdue loan. If a debtor ultimately fails to repay and the court grants its approval for foreclosure, we sell the collateral and recover the principal amount and interest accrued up to the sales price, net of expenses incurred from the auction. Foreclosure proceedings under the laws and regulations of Korea typically take nine months to one year from initiation to collection depending on the nature of the collateral.

Financial Statement Presentation

Our financial statements generally report as charges-offs unsecured retail loans that are overdue for more than 12 months. Leases are charged off when past due for more than twelve months. For collateral dependent loans, we charge off the excess of the book value of the subject loan over the amount received or to be received from the sale of the underlying collateral when the collateral is sold as part of a foreclosure proceeding and its sale price becomes known through court publication as part of such proceeding.

Investment Portfolio

Investment Policy

We invest in and trade Won-denominated and, to a lesser extent, foreign currency-denominated securities for our own account in order to:

- maintain the stability and diversification of our assets;
- maintain adequate sources of back-up liquidity to match our funding requirements; and
- supplement income from our core lending activities.

When making an investment decision with respect to particular securities, we consider macroeconomic trends, industry analysis and credit evaluation, among others.

Our securities investment activities are subject to a number of regulatory guidelines, including limitations prescribed under the Financial Holding Companies Act and the Banking Act. Generally, a financial holding company is prohibited from acquiring more than 5% of the total issued and outstanding shares of another finance-related company (other than its direct and indirect subsidiaries). Furthermore, under these regulations, Shinhan Bank must limit its investments in shares and securities with a maturity in excess of three years (other than monetary stabilization bonds issued by the Bank of Korea and national government bonds) to 100.0% of the sum of Tier I and Tier II capital (less any deductions) of Shinhan Bank. Generally, Shinhan Bank is also prohibited from acquiring more than 15.0% of the shares with voting rights issued by any other corporation (other than for the purpose of establishing or acquiring a subsidiary). Further information on the regulatory

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environment governing our investment activities is set out in Supervision and Regulation Principal Regulations Applicable to Banks Restrictions on Investments in Property, Principal Regulations Applicable to Banks Restrictions on Shareholdings in Other Companies, Principal Regulations Applicable to Financial Holding Companies Liquidity and Principal Regulations Applicable to Financial Holding Companies Restrictions on Shareholdings in Other Companies.

Book Value and Fair Value

The following table sets out the book value and fair value of investments in our investment portfolio as of the dates indicated.

	As of December 31, 2015		As of December 31, 2016		As of December 31, 2017	
	Book Value	Fair Value	Book Value	Fair Value	Book Value	Fair Value
			(In billions of Won)			
Financial assets designated at fair value						
Marketable equity securities	₩ 1,364	₩ 1,364	₩ 1,508	₩ 1,508	₩ 1,468	₩ 1,468
Debt securities:						
Korean treasury and governmental agencies	104	104	334	334	530	530
Debt securities issued by financial institutions	837	837	794	794	716	716
Corporate debt securities	937	937	780	780	856	856
Debt securities issued by foreign government					9	9
Mortgage-backed and asset-backed securities	2	2				
Others						
Total Fair Value Through Profit and Loss	₩ 3,244	₩ 3,244	₩ 3,416	₩ 3,416	₩ 3,579	₩ 3,579
Available-for-sale securities						
Marketable equity securities	₩ 4,929	₩ 4,929	₩ 4,841	₩ 4,841	₩ 4,930	₩ 4,930
Debt securities:						
Korean treasury and governmental agencies	3,606	3,606	4,198	4,198	6,497	6,497
Debt securities issued by financial institutions	15,594	15,594	17,225	17,225	17,650	17,650
Corporate debt securities	6,723	6,723	7,937	7,937	9,602	9,602
Debt securities issued by foreign government	676	676	1,110	1,110	1,073	1,073
Mortgage-backed and asset-backed securities	2,438	2,438	2,352	2,352	2,365	2,365
Total Available-for-sale	₩ 33,966	₩ 33,966	₩ 37,663	₩ 37,663	₩ 42,117	₩ 42,117
Held-to-maturity securities						
Debt securities:						
Korean treasury and governmental agencies	₩ 9,432	₩ 10,413	₩ 10,894	₩ 11,742	₩ 14,495	₩ 14,913
Debt securities issued by financial institutions	1,264	1,315	2,092	2,073	2,708	2,694

Corporate debt securities	2,902	3,136	3,505	3,661	3,859	3,897
Debt securities issued by foreign government	97	97	621	565	669	643
Mortgage-backed and asset-backed securities	2,497	2,528	2,693	2,691	3,260	3,243
Total Held-to-maturity	₩ 16,192	₩ 17,489	₩ 19,805	₩ 20,732	₩ 24,991	₩ 25,390
Trading Securities						
Marketable equity securities	₩ 3,043	₩ 3,043	₩ 4,058	₩ 4,058	₩ 4,634	₩ 4,634
Debt securities:						
Korean treasury and governmental agencies	3,255	3,255	4,236	4,236	3,178	3,178
Financial institutions	6,776	6,776	7,461	7,461	8,014	8,014
Corporations	9,304	9,304	10,244	10,244	11,863	11,863
Mortgage-backed and asset-backed securities	106	106	348	348	509	509
Debt securities issued by foreign governments	5	5	101	101	77	77
Other trading assets	149	149	248	248	189	189
Total Trading	₩ 22,638	₩ 22,638	₩ 26,696	₩ 26,696	₩ 28,464	₩ 28,464
Total securities	₩ 76,040	₩ 77,337	₩ 87,580	₩ 88,507	₩ 99,151	₩ 99,550

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Maturity Analysis

The following table categorizes our securities by maturity and weighted average yield as of December 31, 2017.

	As of December 31, 2017														
	1 Year or Less			Over 1 but within 5 Years			Over 5 but within 10 Years			Over 10 Years			Total		
	Carrying Amount		Weighted Average Yield(1)	Carrying Amount		Weighted Average Yield(1)	Carrying Amount		Weighted Average Yield(1)	Carrying Amount		Weighted Average Yield(1)	Carrying Amount		Weighted Average Yield(1)
	(In billions of Won, except percentages)														
Financial assets designated at fair value:															
Korean treasury securities and government agencies	₩		%	₩	219	2.26%	₩	147	2.47%	₩	164	2.46%	₩	530	2.38%
Debt securities issued by financial institutions		66	2.14%		495	2.83%		155	3.59%			%		716	2.93%
Corporate debt securities		206	1.85%		443	2.49%		127	2.98%		80	5.13%		856	2.66%
Debt securities issued by foreign governments		9	%			%			%			%		9	%
Mortgage-backed securities and asset-backed securities			%			%			%			%			%
Total	₩	281	1.86%	₩	1,157	2.59%	₩	429	3.03%	₩	244	3.34%	₩	2,111	2.67%
Available-for-sale securities:															
Korean treasury securities and government agencies	₩	581	1.47%	₩	4,298	1.70%	₩	209	2.12%	₩	1,409	1.95%	₩	6,497	1.75%
Debt securities issued by financial institutions		9,418	1.55%		6,788	1.97%		183	3.79%		1,261	0.45%		17,650	1.66%
Corporate debt securities		2,750	1.64%		4,479	2.08%		103	0.70%		2,270	0.70%		9,602	1.62%
		534	3.35%		302	4.55%		157	6.31%		80	5.80%		1,073	4.31%

Debt securities issued by foreign governments										
Mortgage-backed securities and asset-backed securities	372	1.83%	1,036	1.94%		%	957	0.94%	2,365	1.51%
Total	₩ 13,655	1.64%	₩ 16,903	1.98%	₩ 652	3.37%	₩ 5,977	1.05%	₩ 37,187	1.73%
Held-to-maturity securities:										
Korean treasury securities and government agencies	₩ 846	4.65%	₩ 8,439	2.31%	₩ 127	3.03%	₩ 5,083	2.69%	₩ 14,495	2.59%
Debt securities issued by financial institutions	489	1.75%	625	1.88%	74	4.79%	1,520	5.01%	2,708	3.69%
Corporate debt securities	217	2.53%	925	2.15%	146	3.60%	2,571	2.57%	3,859	2.51%
Debt securities issued by foreign governments	26	6.10%	113	5.01%	121	6.80%	409	3.89%	669	4.69%
Mortgage-backed securities and asset-backed securities		%	2,279	2.33%	186	2.52%	795	0.64%	3,260	1.93%
Total	₩ 1,578	3.48%	₩ 12,381	2.30%	₩ 654	3.91%	₩ 10,378	2.89%	₩ 24,991	2.66%
Trading securities:										
Korean treasury securities and government agencies	₩ 348	1.78%	₩ 1,723	2.09%	₩ 1,085	2.36%	₩ 22	2.46%	₩ 3,178	2.15%
Debt securities issued by financial institutions	4,620	1.65%	3,314	2.07%	8	2.88%	72	2.68%	8,014	1.83%
Corporate debt securities	9,779	1.90%	1,992	2.94%	53	2.73%	39	1.05%	11,863	2.08%
Debt securities issued by foreign governments		%	58	0.54%	19	1.05%		%	77	0.67%
Mortgage-backed securities and asset-backed securities	212	2.14%	275	2.15%	19	1.61%	3	%	509	2.11%
Total	₩ 14,959	1.82%	₩ 7,362	2.30%	₩ 1,184	2.35%	₩ 136	2.12%	₩ 23,641	2.00%

Total	₩ 30,473	₩ 37,803	₩ 2,919	₩ 16,735	₩ 87,930

Note:

(1) The weighted-average yield for the portfolio represents the yield to maturity for each individual security, weighted using its amortized cost.

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Concentrations of Risk

The following table presents securities held by us whose aggregate book value exceeded 10% of our stockholders equity as of December 31, 2017. As of December 31, 2017, 10% of our stockholders equity was W3,370 billion.

	As of December 31, 2017	
	Book Value	Fair Value
	(In billions of Won)	
Name of issuer:		
Ministry of Strategy and Finance	₩ 23,287	₩ 23,945
The Korea Development Bank	₩ 4,857	₩ 4,867
The Bank of Korea	₩ 9,663	₩ 9,979
The Korea Housing Finance Corp	₩ 5,360	₩ 5,337

All of the above entities are either an agency of the Korean government or an entity controlled by the Korean government.

Credit-Related Commitments and Guarantees

In the normal course of our operations, we make various commitments and guarantees to meet the financing and other business needs of our customers. Commitments and guarantees are usually in the form of, among others, commitments to extend credit, commercial letters of credit, standby letters of credit and performance guarantees. The contractual amount of these financial instruments represents the maximum possible loss amount if the account party draws down the commitment or we should fulfill our obligation under the guarantee and the account party fails to perform under the contract.

The following table sets forth our credit-related commitments and guarantees as of the dates indicated.

	As of December 31,		
	2015	2016	2017
	(In billions of Won)		
Commitments to extend credit	₩ 75,443	₩ 74,541	₩ 73,373
Commercial letters of credit	2,377	2,777	2,744
Other[1]	22,327	21,826	21,530
Total	₩ 100,147	₩ 99,144	₩ 97,647

Note:

(1)

Consists of financial guarantees, performance guarantees, liquidity facilities to special purpose entities, acceptances, guarantee on trust accounts and endorsed bills.

We have credit-related commitments that are not reflected on our statements of financial position, which primarily consist of commitments to extend credit and commercial letters of credit. Commitments to extend credit, including credit lines, represent unfunded portions of authorizations to extend credit in the form of loans. These commitments expire on fixed dates and a customer is required to comply with predetermined conditions to draw funds under the commitments. Commercial letters of credit are undertakings on behalf of customers authorizing third parties to make drawdowns up to a stipulated amount under specific terms and conditions. They are generally short-term and collateralized by the underlying shipments of goods to which they relate.

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We also have guarantees that are recorded on our statements of financial position at their fair value at inception which are amortized over the life of the guarantees. Such guarantees generally include standby letters of credit, other financial and performance guarantees and liquidity facilities to special purpose entities. Standby letters of credit are irrevocable obligations to pay third-party beneficiaries when our customers fail to repay loans or debt instruments, which are generally in foreign currencies. A substantial portion of these standby letters of credit are secured by collateral, including trade-related documents. Other financial and performance guarantees are irrevocable assurances that we will pay beneficiaries if our customers fail to perform their obligations under certain contracts. Liquidity facilities to special purpose entities are irrevocable commitments to provide contingent liquidity credit lines to special purpose entities established by our customers in the event that a triggering event such as shortage of cash occurs.

The commitments and guarantees do not necessarily represent our exposure since they often expire unused.

Derivatives

As discussed under Business Overview Our Principal Activities Other Banking Services Derivatives Trading above we engage in derivatives trading activities primarily on behalf of our customers so that they may hedge their risks and also enter into back-to-back derivatives with other financial institutions to cover exposures arising from such transactions. In addition, we enter into derivatives transactions to hedge against risk exposures arising from our own assets and liabilities, some of which are non-trading derivatives that do not qualify for hedge accounting treatment.

The following shows, as of December 31, 2017, the gross notional or contractual amounts of derivatives held or issued for (i) trading and (ii) non-trading that qualify for hedge accounting.

	As of December 31, 2017		
	Underlying Notional Amount(1)	Estimated Fair Value Assets	Estimated Fair Value Liabilities
	(In billions of Won)		
Trading:			
Foreign exchange derivatives:			
Future and forward contracts	₩ 101,987	₩ 1,896	₩ 1,638
Swaps	30,270	855	865
Options	1,178	12	12
Sub-total	133,435	2,763	2,515
Interest rate derivatives:			
Future and forward contracts	1,546	2	
Swaps	83,895	204	209
Options	310		2
Sub-total	85,751	206	211
Credit derivatives:			
Swaps	2,443	63	11

Sub-total	2,443	63	11
Equity derivatives:			
Swaps and forward contracts	4,223	112	14
Options	4,469	115	30
Future contracts	527		1
Sub-total	9,219	227	45

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	As of December 31, 2017		
	Underlying Notional Amount[1]	Estimated Fair Value Assets	Estimated Fair Value Liabilities
	(In billions of Won)		
Commodity derivatives:			
Swaps and forward contracts	932	16	23
Options	5		
Future contracts	122	6	
Sub-total	1,059	22	23
Total	₩ 231,907	₩ 3,281	₩ 2,805
Non-trading:			
Hedge accounting:			
Foreign exchange derivatives:			
Swaps	₩ 3,866	₩ 59	₩ 162
Future and forward contracts	1,227	50	2
Interest rate derivatives:			
Swaps	8,088	10	519
Total	₩ 13,181	₩ 119	₩ 683

Note:

(1) Notional amounts in foreign currencies were converted into Won at prevailing exchange rates as of December 29, 2017.

Funding

We obtain funding from a variety of sources, both domestic and foreign. Our principal source of funding is customer deposits obtained from our banking operations, and we from time to time issue equity and debt securities, including preferred shares. In addition, our subsidiaries acquire funding through call money, borrowings from the Bank of Korea, other short-term borrowings, corporate debentures and other long-term debt, including debt and equity securities issuances, asset-backed securitizations and repurchase transactions, to complement, or if necessary, replace funding through customer deposits. For further details relating to funding by us and our subsidiaries, see Item 5.B. Liquidity and Capital Resources.

Deposits

Although the majority of our bank deposits are short-term, the majority of our depositors have historically rolled over their deposits at maturity, providing our banking operation with a stable source of funding.

The following table shows the average balances of our deposits and the average rates paid on our deposits for the periods indicated.

	2015		2016		2017	
	Average Balance[1]	Average Rate Paid	Average Balance[1]	Average Rate Paid	Average Balance[1]	Average Rate Paid
	(In billions of Won, except percentages)					
Interest-bearing deposits:						
Demand deposits	₩ 26,365	0.44%	₩ 30,865	0.37%	₩ 35,978	0.36%
Savings deposits	56,083	0.70	63,061	0.59	69,671	0.51
Time deposits	113,932	2.03	123,716	1.64	121,050	1.55
Other deposits	3,555	1.20	4,744	1.47	8,164	1.57
Total interest-bearing deposits	₩ 199,935	1.43%	₩ 222,386	1.16%	₩ 234,863	1.06%

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Note:

(1) Average balances are based on (a) daily balances of Shinhan Bank and (b) quarterly balances for other subsidiaries.

For a breakdown of deposit products, see Our Principal Activities Deposit-taking Activities, except that cover bills sold are recorded on short-term borrowings and securities sold under repurchase agreements are recorded as secured borrowings.

Certificates of Deposit and Other Time Deposits

The following table presents the certificates of deposit and other time deposits in excess of ₩100 million by remaining maturities as of December 31, 2017.

	As of December 31, 2017		
	Certificates of Deposit	Other Time Deposits	Total
	(In billions of Won)		
Maturing within three months	₩ 2,853	₩ 26,239	₩ 29,092
After three but within six months	2,045	21,102	23,147
After six but within 12 months	1,876	34,129	36,005
After 12 months	330	5,868	6,198
Total	₩ 7,104	₩ 87,338	₩ 94,442

A majority of our certificates of deposit accounts and other time deposits issued by our foreign offices is in the amount of US$100,000 or more.

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Short-term Borrowings

The following table presents information regarding our short-term borrowings (borrowings with an original maturity of one year or less) for the periods indicated.

2015				2016					201		
verage Balance standing(1)	Highest Balances at Any Month-end	Weighted Average Interest Rate(2)	Year-end Interest Rate	Balance Outstanding	Average Balance Outstanding(1)	Highest Balances at Any Month-end	Weighted Average Interest Rate(2)	Year-end Interest Rate	Balance Outstanding	Average Balance Outstanding(1)	Highe Balanc at An Month-
(In billions of Won, except for percentages)											
1,712	₩ 2,107	0.67%	0.10 - 0.75%	₩ 2,669	₩ 2,451	₩ 2,689	0.65%	0.50 - 0.75%	₩ 2,913	₩ 2,903	₩ 2,9
2,368	5,736	1.58	0.32 - 7.00	1,130	1,582	2,699	1.35	0.10 - 10.00	857	1,892	4,0
8,010	13,149	0.96	0.00 - 7.95	11,146	11,180	13,084	0.75	0.00 - 4.60	14,375	13,047	14,4
12,090	₩ 20,992	1.04%		₩ 14,945	₩ 15,213	₩ 18,472	0.80%		₩ 18,145	₩ 17,842	₩ 21,4

Notes:

(1) Average balances are based on (a) daily balances of Shinhan Bank and (b) quarterly balances for other subsidiaries.

(2) Weighted-average interest rates are calculated by dividing the total interest expenses by the average amount borrowed.

(3) Borrowings from the Bank of Korea generally mature within one month for borrowings in Won and six months for borrowings in foreign currencies.

(4) Other short-term borrowings included borrowings from trust accounts, bills sold, and borrowings in domestic and foreign currencies.

Our short-term borrowings have maturities of less than one year which are generally unsecured with the exception of borrowings from the Bank of Korea, which are generally secured with available-for-sale or held-to-maturity securities held by us.

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Risk Management

Overview

As a financial services provider, we are exposed to various risks relating to our lending, credit card, insurance, securities investment, trading and leasing businesses, our deposit taking and borrowing activities and our operating environment. The principal risks to which we are exposed are credit risk, market risk, interest rate risk, liquidity risk and operational risk. These risks are recognized, measured and reported in accordance with risk management guidelines established at our holding company level and implemented at the subsidiary level through a carefully stratified checks-and-balances system.

We believe that our risk management system has been instrumental to building our reputation as a well-managed and prudent financial service provider and withstanding various external shocks. In particular, during the global financial crisis of 2008 and 2009, we believe our risk management provided effective early warning signals which helped us to proactively reconfigure our asset portfolio and substantially reduce our exposure to troubled debtors and thereby avoid what could have been a substantially greater credit loss during such crisis, and we are carefully upgrading and refining our risk management system in the face of current and potential economic difficulties at global, regional and domestic levels.

Our group-wide risk management philosophy is to instill a culture of effective risk management and awareness at all levels of our organization and pursue a proper balance between risk and return in our business activities in order to achieve a sustainable growth. In particular, our group-wide risk management is guided by the following core principles:

- carrying out all business activities within prescribed risk tolerance levels and prudently balancing profitability and risk management;
- standardizing the risk management process and monitoring compliance at a group-wide level;
- operating a prudent risk management decision making system backed by active participation by management;
- creating and operating a risk management organization independent of business activities;
- operating a performance management system that enhances clear and prompt identification of risks when making business decisions;
- aiming to achieve preemptive and practical risk management; and
- prudent preparation for known and unknown contingencies.

We take the following steps to implement the foregoing risk management principles:

risk capital management Risk capital refers to capital necessary to compensate for losses in case of a potential risk being realized, and risk capital management refers to the process of asset management based on considerations of risk exposure and risk appetite for our total assets so that we can maintain an appropriate level of risk capital. As part of our risk capital management, we and our subsidiaries have adopted and maintain various risk planning processes and reflect such risk planning in our business and financial planning. We also maintain a risk limit management system to ensure that risks in our business do not exceed prescribed limits.

risk monitoring We proactively, preemptively and periodically review risks that may impact our overall operations, including through a multidimensional risk monitoring system. Currently, each of our subsidiaries is required to report to the holding company any factors that could have a material impact on group-wide risk management, and the holding company reports to our chief risk officer and other members of our senior management the results of risk monitoring weekly, monthly and on an *ad hoc* basis as needed. In addition, we perform preemptive risk management through a risk dashboard system under which we closely monitor any increase in asset size, risk levels and sensitivity to external factors with respect to the major asset portfolios of each of our subsidiaries, and to the extent such monitoring yields any warning signals, we promptly analyze the causes and, if necessary, formulate and implement actions in response thereto.

risk review Prior to entering any new business, offering any new products or changing any major policies, we review any relevant risk factors based on a prescribed risk management checklist and, in the case of changes for which assessment of risk factors is difficult, perform reasonable decision-making in order to avoid taking any unduly risky action. The risk management departments of all our subsidiaries are required to review all new businesses, products and services prior to their launch and closely monitor the development of any related risks following their launch, and in the case of any action that involves more than one subsidiary, the relevant risk management departments are required to consult with the risk management team at the holding company level prior to making any independent risk reviews.

crisis management We maintain a group-wide risk management system to detect the early warnings signals of any crisis and, in the event of a crisis actually happening, to respond on a timely, efficient and flexible basis so as to ensure our survival as a going concern. Each of our subsidiaries maintains crisis planning for three levels of contingencies, namely, alert, imminent crisis and crisis, determination of which is made based on quantitative and qualitative monitoring and consequence analysis, and upon the occurrence of any such contingency, is required to respond according to a prescribed contingency plan. At the holding company level, we maintain and install a crisis detection and response system which is applied consistently group-wide, and upon the occurrence of an imminent crisis or crisis event at a subsidiary level, we directly take charge of the situation at the holding company level so that we manage it on a concerted group-wide basis.

Organization

Our risk management system is organized along the following hierarchy (from top to bottom): at the holding company level, the Group Risk Management Committee, the Group Risk Management Council, the Group Chief Risk Officer and the Group Risk Management Team, and at the subsidiary level, the Risk Management Committee, the Chief Risk Officer and the Risk Management Team of the relevant subsidiary. The Group Risk Management Committee, which is under the supervision of our holding company s board of directors, sets the basic group-wide risk management policies and strategies. Our Group Chief Risk Officer reports to the Group Risk Management Committee, and the Group Risk Management Council coordinates the risk management policies and strategies at the group level as well as at the subsidiary level among each of our subsidiaries. Each of our subsidiaries also has a separate Risk Management Committee, Risk Management Working Committee and Risk Management Team, whose tasks are to implement the group-wide risk management policies and strategies at the subsidiary level as well as to set risk management policies and strategies specific to such subsidiary in line with the group-wide guidelines. We also have the Group Risk Management Team, which supports our Chief Risk Officer in his or her risk management and supervisory role.

In order to maintain the group-wide risk at an appropriate level, we use a hierarchical risk limit system under which the Group Risk Management Committee assigns reasonable risk limits for the entire group and each of our subsidiaries, and the Risk Management Committee and the Risk Management Working Committee of each of our subsidiaries manage the subsidiary-specific risks by establishing and managing risk limits in more detail by type of risk and type of product for each department and division within such subsidiary. Further details follow.

At the holding company level:

Group Risk Management Committee The Group Risk Management Committee consists of four outside directors of our holding company. The Group Risk Management Committee convenes at least quarterly and on an *ad hoc* basis as needed. Specifically, the Group Risk Management Committee does the following: (i) establish the overall risk management policies consistent with management strategies, (ii) set reasonable risk limits for the entire group and each of our subsidiaries, (iii) approve appropriate investment limits or permissible loss limits, (iv) enact and amend risk management regulations, and (v) decide other risk management-related issues the board of directors or the Group Risk Management Committee sees fit to discuss. The results of the Group Risk Management Committee meetings are reported to the board of directors of our holding company. The Group Risk Management Committee makes decisions through affirmative votes by a majority of the committee members.

Group Risk Management Council Comprised of the Group Chief Risk Officer and Chief Risk Officers of each of our subsidiaries, the Group Risk Management Council provides a forum for risk management executives from each subsidiary to discuss our group-wide risk management guidelines and strategy in order to maintain consistency in the group-wide risk policies and strategies.

Group Chief Risk Officer The Group Chief Risk Officer assists the Group Risk Management Committee by implementing the risk policies and strategies as well as ensuring consistency in the risk management systems of our subsidiaries. Furthermore, the Group Chief Risk Officer evaluates the Chief Risk Officer of each subsidiary in addition to monitoring the risk management practices of each subsidiary.

Group Risk Management Team This team provides support and assistance to the Group Chief Risk Officer in carrying out his or her responsibilities.

At the subsidiary level:

Risk Management Committee In order to maintain group-wide risk at an appropriate level, we have established a hierarchical risk limit system where the Group Risk Management Committee establishes risk limits for us and our subsidiaries, and each of our subsidiaries establishes and manages risk limits in more detail by type of risk and type of product for each department and division within such subsidiary. In accordance with the group risk management policies and strategies, the Risk Management Committee at the subsidiary level establishes its own risk management policies and strategies in more detail and the respective risk management department implements those policies and strategies.

Risk Management Team The Risk Management Team, operating independently from the business units of each of our subsidiaries, monitors, assesses, manages and controls the overall risk of its operations and reports all major risk-related issues to the Group Risk Management Team at the holding company level, which then reports to the Group Chief Risk Officer.

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The following is a flowchart of our risk management system at the holding company level and the subsidiary level.

Credit Risk Management

Credit risk, which is the risk of loss from default by borrowers, other obligors or other counterparties to the transactions that we have entered into, is the greatest risk we face. Our credit risk management encompasses all areas of credit that may result in potential economic loss, including not just transactions that are recorded on our balance sheets, but also off-balance-sheet transactions such as guarantees, loan commitments and derivatives transactions. A substantial majority of our credit risk relates to the operations of Shinhan Bank and Shinhan Card.

Credit Risk Management of Shinhan Bank

Shinhan Bank s credit risk management is guided by the following principles:

- achieve a profit level corresponding to the level of risks involved;
- improve asset quality and achieve an optimal mix of asset portfolios;
- avoid excessive loan concentration in a particular borrower or sector;
- closely monitor the borrower s ability to repay the debt; and
- provide financial support to advance the growth of select customers.

Major policies for Shinhan Bank s credit risk management, including Shinhan Bank s overall credit risk management plan and credit policy guidelines, are determined by the Risk Policy Committee of Shinhan Bank, the executive decision-making body for management of credit risk. The Risk Policy Committee is headed by the Chief Risk Officer, and also comprises of the Chief Credit Officer and the heads of each business unit. In order to separate the loan approval functions from credit policy decision-making, Shinhan Bank has a Credit Review Committee that performs credit review evaluations with a focus on improving the asset quality of and profitability from the loans being made, and operates separately from the Risk Policy Committee. Both the Risk Policy Committee and the Credit Review Committee make decisions by a vote of two-thirds or more of the attending members of the respective committees, which must constitute at least two-thirds of the respective committee members to satisfy the respective quorum.

Shinhan Bank complies with credit risk management procedures pursuant to internal guidelines and regulations and continually monitors and improves these guidelines and regulations. Its credit risk management procedures include:

- credit evaluation and approval;
- credit review and monitoring; and
- credit risk assessment and control.

Credit Evaluation and Approval

All loan applicants and guarantors are subject to credit evaluation before approval of any loans. Credit evaluation of loan applicants are carried out by senior officers of Shinhan Bank specifically charged with granting loan approvals. Loan evaluation is carried out by a group rather than by an individual reviewer through an objective and deliberative process. Credit ratings of loan applicants and guarantors influence loan interest rates, the level of internal approval required, credit exposure limits, calculation of potential losses and estimated cost of capital, and therefore are determined objectively and independently by the relevant business unit. Shinhan Bank uses a credit scoring system for retail loans and a credit-risk rating system for corporate loans.

Each of Shinhan Bank s borrowers is assigned a credit rating, which is based on a comprehensive internal credit evaluation system that considers a variety of criteria. For retail borrowers, the credit rating takes into account the borrower s biographic details, past dealings with Shinhan Bank and external credit rating information, among other things. For corporate borrowers, the credit rating takes into account financial indicators as well as non-financial indicators such as industry risk, operational risk and management risk, among other things. The credit rating, once assigned, serves as the fundamental instrument for Shinhan Bank s credit risk management, and is applied to a wide range of credit risk management processes, including credit approval, credit limit management, loan pricing and computation of allowance for loan losses. Shinhan Bank has separate credit evaluation systems for retail customers, SOHO customers and corporate customers, which are further segmented and refined to meet Basel II requirements, which requirements have not changed under Basel III. See Item 5.A. Operating Results Critical Accounting Policies Impairment of Financial Assets Allowance for Loan Losses.

Retail Loans

Loan applications for retail loans are reviewed in accordance with Shinhan Bank s credit scoring system and the objective statistics models for secured and unsecured loans maintained and operated by Shinhan Bank s Retail Banking Division. Shinhan Bank s credit scoring system is an automated credit approval system used to evaluate loan applications and determine the appropriate pricing for the loan, and takes into account factors such as a borrower s personal information, transaction history with Shinhan Bank and other financial institutions and other relevant credit information. The applicant is assigned a score, which is used to determine (i) whether to approve the applicant s loan, (ii) the amount of loan to be granted, and (iii) the interest rates thereon. The applicant s score also determines whether the applicant is approved for credit, conditionally approved, subject to further assessment, or denied. If the applicant becomes subject to further assessment, the appropriate discretionary body, either at the branch level or at the headquarter level, makes a reassessment based on qualitative as well as quantitative factors, such as credit history, occupation and past relationship with Shinhan Bank.

For mortgage and home equity loans and loans secured by real estate, Shinhan Bank evaluates the value of the real estate offered as collateral using a proprietary database, which contains information about real estate values throughout Korea. In addition, Shinhan Bank uses up-to-date information provided by third parties regarding the real estate market and property values in Korea. While Shinhan Bank uses internal staff from the processing centers to appraise the value of the real estate collateral, Shinhan Bank also hires certified appraisers to review and co-sign the appraisal value of real estate collateral that have an appraisal value exceeding ₩3 billion, as initially determined by the processing centers. Shinhan Bank also reevaluates internally, on a summary basis, the appraisal value of collateral at least every year.

For loans secured by securities, deposits or other assets other than real estate, Shinhan Bank requires borrowers to observe specified collateral ratios in respect of secured obligations.

Corporate Loans

Shinhan Bank rates all of its corporate borrowers using internally developed credit evaluation systems. These systems consider a variety of criteria (quantitative, qualitative, financial and non-financial) in order to standardize credit decisions and focus on the quality of borrowers rather than the size of loans. The quantitative considerations include the borrower s financial and other data, while the qualitative considerations are based on the judgment of Shinhan Bank s credit officers as to the borrower s ability to repay. Financial considerations include financial variables and ratios based on customer s financial statements, such as return on assets and cash flow to total debt ratios, and non-financial considerations include, among other things, the industry to which the borrower s businesses belong, the borrower s competitive position in its industry, its operating and funding capabilities, the quality of its management and controlling stockholders (based in part on interviews with its officers and employees), technological capabilities and labor relations.

In addition, in order to enhance the accuracy of its internal credit reviews, Shinhan Bank also considers reports prepared by external credit rating services, such as Nice Information Service and Korea Enterprise Data, and monitors and improves the effectiveness of the credit risk-rating systems using a database that it updates continually with actual default records.

Based on the scores calculated under the credit rating system, which takes into account the evaluation criteria described above and the probability of default, Shinhan Bank assigns the borrower one of 23 grades (from the highest of AAA to the lowest of D3). Grades AA through B are further broken down into +, 0 or -. Grades AAA through B- are classified as normal, grade CCC precautionary, and grades CC through D3 non-performing. The credit risk-rating model is further differentiated by the size of the corporate borrower and the type of credit facilities.

Loan Approval Process

Loans are generally approved after evaluations and approvals by the relationship manager at the branch level as well as the committee of the applicable business unit at Shinhan Bank. The approval limit for retail loans is made based on Shinhan Bank s automated credit scoring system. In the case of large corporate loans, approval limits are also reviewed and approved by a Credit Officer at the headquarter level. Depending on the size and the importance of the loan, the approval process is further reviewed by the Credit Officer Committee or the Master Credit Officer Committee. If the loan is considered significant or the amount exceeds the discretion limit of the Master Credit Officer Committee, further evaluation is made by the Credit Review Committee, which is Shinhan Bank s highest decision-making body in relation to credit approval. The Credit Review Committee s evaluation and approval of loan limits vary depending on the credit ratings of the borrowers as determined by Shinhan Bank s internal credit rating system. For example, for borrowers with a credit rating of B-, the Credit Review Committee evaluates and approves unsecured loans in excess of ₩10 billion and secured loans in excess of ₩15 billion, whereas for borrowers with a credit rating of AAA, the Credit Review Committee evaluates and approves unsecured loans in excess of ₩40 billion and secured loans in excess of ₩90 billion. The Credit Review Committee holds at least two meetings a week to approve applications for large-sized loans whose principal amounts exceed prescribed levels set by it.

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The chart below summarizes the credit approval process of our banking operation. The Master Credit Officer and the Head of Business Division do not make individual decisions on loan approval, but are part of the decision-making process at the group level.

The reviewer at each level of the review process may in its discretion approve loans up to a maximum amount per loan assigned to such level. The discretionary loan approval limit for each level of the loan approval process takes into account the total amount of loans extended to the borrower, the credit level of the applicant based on credit review, the existence and value of collateral and the level of credit risk established by the credit rating system. The discretionary loan amount approval limit ranges from ₩15 million for unsecured retail loans with a credit rating of B-, which are subject to approvals by the retail branch manager, to ₩90 billion for secured loans with a credit rating of AAA, which are subject to approvals by the Master Credit Officer Committee. Any loans exceeding the maximum discretionary loan amount approval limit must be approved by the Credit Review Committee.

Credit Review and Monitoring

Shinhan Bank continually reviews and monitors existing credit risks primarily with respect to borrowers. In particular, Shinhan Bank s automated early warning system conducts daily examination for borrowers using over 206 financial and non-financial factors, and the branch manager and the credit officer must conduct periodic loan review and report to an independent Credit Review Department which analyzes in detail the results and adjusts credit ratings accordingly. Based on these reviews, Shinhan Bank adjusts a borrower s credit rating, credit limit and credit policies. In addition, the group credit rating of the borrower s group, if applicable, may be adjusted following a periodic review of the main debtor groups, mostly comprised of *chaebols*, as identified by the Governor of the Financial Supervisory Service based on their outstanding credit exposures, of which 63 were identified as such as of December 31, 2017. Shinhan Bank also continually reviews other factors, such as industry-specific conditions for the borrower s business and its domestic and overseas asset base and operations, in order to ensure that the assigned ratings are appropriate. The Credit Review Department provides credit review reports, independent of underwriting, to the Chief Risk Officer on a monthly basis.

The early warning system performs automatic daily checks for borrowers to whom Shinhan Bank has more than ₩1 billion of total exposure (which represents the total outstanding amount due from a borrower, net of collateral for deposit, installment savings, guarantees and import guarantee money) or ₩500 million of net credit exposure (which represents total exposure net of effective collateral). When the early warning systems detects a warning signal, such signal and other findings from the monitoring are reviewed by the Credit Review Department in the case of a borrower to whom Shinhan Bank has more than ₩2 billion of exposure, and by the relationship manager and the Credit Officer in the case of a borrower to whom Shinhan Bank has ₩2 billion or less of exposure. In addition, Shinhan Bank carries out a preemptive review of each borrower in accordance with changes in credit risk factors based on changes in the economic environment. The results of such preemptive review are continually reported to the Chief Risk Officer of Shinhan Bank.

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Depending on the nature of the signals detected by the early warning system, a borrower may be classified as deteriorating credit and become subject to evaluation for a possible downgrade in rating, or may be initially classified as showing early warning signs or become reinstated to the normal borrower status. For borrowers classified as showing early warning signs, the relevant relationship manager gathers information and conducts a review of the borrower to determine whether the borrower should be classified as a deteriorating credit or whether to impose management improvement warnings or implement joint creditors management. If the borrower becomes non-performing, Shinhan Bank s collection department directly manages such borrower s account in order to maximize recovery rate, and conducts auctions, court proceedings, sale of assets or corporate restructuring as needed.

Pursuant to the foregoing credit review and monitoring procedures and in order to promptly prevent deterioration of loan qualities, Shinhan Bank classifies potentially problematic borrowers into (i) borrowers that show early warning signals, (ii) borrowers that require precaution, (iii) borrowers that require observation and (iv) normal borrowers, and treats them differentially accordingly.

In order to curtail delinquency among its corporate customers, Shinhan Bank takes primarily the following measures: (i) systematic monitoring of borrowers with sizable outstanding loans and (ii) heightened monitoring of borrowers with bad credit history and/or belonging to troubled industries.

Systematic monitoring of borrowers with sizable outstanding loans. Shinhan Bank currently applies a heightened monitoring system to corporate borrowers with outstanding loans (other than guaranteed loans and loans secured by specified types of collaterals such as deposits with us or letters of credit) in the aggregate amount of ₩1 billion or more and borrowers with net outstanding loans (i.e., the outstanding loan amount minus the fair value of collaterals (other than as aforesaid) securing such loans) in the aggregate amount of ₩500 million or more. Under this monitoring system, each such borrower is assigned one of the following ratings:

Normal borrower a borrower with a credit rating of B- or above that are deemed to carry a low risk of default;

Borrower that requires observation a borrower that carries some risk of potential default and therefore requires periodic monitoring to detect any elevation of such risk;

Borrower that requires precaution a borrower with an elevated risk of default and therefore requires detailed reassessment of the credit quality of such borrower and precaution in extending any further loans;

Borrower with early warning signs a borrower with a high level of default risk; and

Problematic or reorganized borrower a borrower currently in default and either subject to workout or restructuring or showing no signs of recovery.

Shinhan Bank conducts systematic monitoring of the foregoing borrowers at intervals depending on the borrower s credit rating (for example, every 12 months for normal borrowers with a credit rating of AAA to A, every nine months for normal borrowers with a credit rating of A- to BBB+, every six months for a credit rating of BBB to B- and every three months for borrowers with a credit rating of CCC or below and borrowers not deemed to be normal). In addition, the loan reviewer may request more frequent monitoring if the borrower is showing signs of deteriorating credit quality. For borrowers with outstanding loan amounts of ₩2 billion or more, Shinhan Bank also monitors the revenues and earnings of such borrower on a quarterly basis within 10 weeks following the end of each quarter.

Heightened monitoring of borrowers with bad credit history and/or belonging to troubled industries. In addition to the systematic monitoring discussed above, Shinhan Bank also carries out additional monitoring for borrowers that, among others, (i) are rated as requiring observation, requiring precaution or with early

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warning signs as noted above, (ii) have prior history of delinquency or restructuring or (iii) have borrowings that are classified as substandard or below. Based on the heightened monitoring of these borrowers, Shinhan Bank adjusts contingency planning as to how the overall asset quality of a specific industry should change for each phase of the business cycle, how Shinhan Bank should limit or reduce its exposure to such borrowers, and how our group-wide delinquency and non-performing ratio would change, among other things.

Credit Risk Assessment and Control

In order to assess credit risk in a systematic manner, Shinhan Bank has developed and upgraded systems designed to quantify credit risk based on selection and monitoring of various statistics, including delinquency rate, non-performing loan ratio, expected loan loss and weighted average risk rating.

Shinhan Bank controls loan concentration by monitoring and managing loans at two levels: portfolio level and individual loan account level. In order to maintain portfolio-level credit risk at an appropriate level, Shinhan Bank manages its loans using value-at-risk (VaR) limits for the entire bank as well as for each of its business units. In order to prevent concentration of risk in a particular borrower or borrower class, Shinhan Bank also manages credit risk by borrower, industry, country and other detailed categories.

Shinhan Bank measures credit risk using internally accumulated data. Shinhan Bank measures expected and unexpected losses with respect to total assets monthly, which Shinhan Bank refers to when setting risk limits for, and allocating capital to, its business groups. Expected loss is calculated based on the probability of default, the loss given default, the exposure at default and the past bankruptcy rate and recovery rate, and Shinhan Bank provides allowance for loan losses accordingly. Shinhan Bank makes provisioning at a level which is the higher of the Financial Supervisory Service requirement or Shinhan Bank s internal calculation. Unexpected loss is predicted based on VaR, which is used to determine compliance with the aggregate credit risk limit for Shinhan Bank as well as the credit risk limit for the relevant department within Shinhan Bank. Shinhan Bank uses the AIRB method as proposed by the Basel Committee to compute VaR at the account-specific level as well as to measure risk adjusted performance.

Credit Risk Management of Shinhan Card

Major policies for Shinhan Card s credit risk management are determined by Shinhan Card s Risk Management Council, and Shinhan Card s Risk Management Committee is responsible for approving them. Shinhan Card s Risk Management Council is headed by the Chief Risk Officer, and also comprises of the heads of each business unit, supporting unit and relevant department at Shinhan Card. Shinhan Card s Risk Management Council convenes at least once every month and may also convene on an *ad hoc* basis as needed. Shinhan Card s Risk Management Committee is comprised of three Non-Standing Directors. Shinhan Card s Risk Management Committee convenes at least once every quarter and may also convene on an *ad hoc* basis as needed.

The risk of loss from default by the cardholders or credit card loan borrowers is Shinhan Card s greatest credit risk. Shinhan Card manages its credit risk based on the following principles:

- achieve profit at a level corresponding to the level of risks involved;

- improve asset quality and achieve an optimal mix of asset portfolios; and closely monitor borrower s ability to repay the debt.

Credit Card Approval Process

Shinhan Card uses an automated credit scoring system to approve credit card applications or credit card authorizations. The credit scoring system is divided into two sub-systems: the behavior scoring system and the

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application scoring system. The behavior scoring system is based largely on the credit history of the cardholder or borrower, and the application scoring system is based largely on personal information of the applicant. For credit card applicants with whom we have an existing relationship, Shinhan Card s credit scoring system considers internally gathered information such as the ability to repay, total assets, the length of the existing relationship and the applicant s contribution to Shinhan Card s profitability. The credit scoring system also automatically conducts credit checks on all credit card applicants. Shinhan Card gathers information about the applicant s transaction history with financial institutions, including banks and credit card companies, from a number of third party credit reporting agencies including, among others, National Information & Credit Evaluation Inc. and Korea Credit Bureau. These credit checks reveal a list of the delinquent customers of all credit card issuers in Korea.

If a credit score assigned to an applicant is above the minimum threshold, the application is approved unless overridden based on other considerations such as delinquencies with other credit card companies. For a credit card application by a long-standing customer with a good credit history, Shinhan Card may, on a discretionary basis, approve the application notwithstanding the assigned credit score unless overridden by other considerations. All of these factors also serve as the basis for setting a credit limit for approved applications.

The following describes the process of how Shinhan Card sets credit limits for credit cards, cash advances and card loans:

*Credit purchase and cash advance limit*s These limits are set based on the applicant s limit request and Shinhan Card s credit screening criteria. Unless a cardholder requests a reduction in the credit purchase and/or cash advance limit, Shinhan Card is required to provide prior notice to the cardholder for any reduction in such cardholder s limit. However, if the accountholder defaults or the cardholder s credit limit is reduced according to the terms of the card agreement, Shinhan Card may lower the credit limit before notifying the accountholder.

Card loan limit This limit is set monthly by Shinhan Card based on the cardholder s credit rating and transaction history. The card loan limit can be adjusted monthly based on the cardholder s credit standing without prior notification.

Monitoring

Shinhan Card continually monitors all cardholders and accounts using a behavior scoring system. The behavior scoring system predicts a cardholder s payment pattern by evaluating the cardholder s credit history, card usage and amounts, payment status and other relevant data. The behavior score is recalculated each month and is used to manage the accounts and approval of additional loans and other products to the cardholder. Shinhan Card also uses the scoring system to monitor its overall risk exposure and to modify its credit risk management strategy.

Loan Application Review and On-going Credit Review

When reviewing new applications and conducting an ongoing credit review for retail loans, installment purchase loans and personal leases, Shinhan Card uses criteria substantially similar to those used in the credit underwriting system and the credit review system for cardholders. For retail loans, installment purchase loans and personal leases to existing cardholders, Shinhan Card reviews their card usage history in addition to other factors such as their income, occupation and assets.

Fraud Loss Prevention

Shinhan Card seeks to minimize losses from the fraudulent use of credit cards issued by it. Shinhan Card focuses on preventing fraudulent uses and, following the occurrence of a fraudulent use, makes investigations in order to make the responsible party bear the losses. Misuses of lost credit cards account for a substantial majority of Shinhan Card s fraud-related losses. Through its fraud loss prevention system, Shinhan Card seeks to detect, on a real-time basis, transactions that are unusual or inconsistent with prior usage history and calls are made to the relevant cardholders to confirm their purchases. A team at Shinhan Card dedicated to investigating fraud losses also examines whether the cardholder was at fault by, for example, not reporting a lost card or failing to endorse the card, or whether the relevant merchant was negligent in checking the identity of the user. Fault may also lie with delivery companies that fail to deliver credit cards to the relevant applicant. In such instances, Shinhan Card attempts to recover fraud losses from the responsible party. To prevent misuse of a card as well as to manage credit risk, Shinhan Card s information technology system will automatically suspend the use of a card (i) when, as a result of ongoing monitoring, fraudulent use or loss of the card is suspected based on the accountholder s credit score, or (ii) at the request of the accountholder.

Approximately 94% of Shinhan Card s cardholders consent to Shinhan Card s accessing their travel records to detect any misuse of credit cards while they are traveling abroad. Shinhan Card also offers cardholders additional fraud protection through a fee-based texting service. At the cardholder s option, Shinhan Card notifies the cardholder of any credit card activity in his or her account by sending a text message to his or her mobile phone. This notification service allows customers to quickly and easily identify any fraudulent use of their credit cards.

Credit Risk Management of Shinhan Investment

In accordance with the guidelines of the Financial Supervisory Service, Shinhan Investment assesses its credit risks (including through VaR analyses) and allocates the maximum limit for the credit amount at risk by department. Shinhan Investment also assesses the counterparty risks in all credit-related transactions, such as loans, acquisition financings and derivative transactions and takes corresponding risk management measures. In assessing the credit risk of a corporate counterparty, Shinhan Investment considers such counterparty s corporate credit rating obtained from Shinhan Group Corporate Credit Rating System. Through its risk management system, Shinhan Investment also closely monitors credit risk exposures by counterparty, industry, conglomerates, credit ratings and country. Shinhan Investment conducts credit risk stress tests on a daily basis based on probability of default and also conducts more advanced stress tests from time to time, the results of which are then reported to its management as well as the Group Chief Risk Officer to support group-wide credit risk management.

Market Risk Management

Market risk is the risk of loss generated by fluctuations in market prices such as interest rates, foreign exchange rates and equity prices. The principal market risks to which we are exposed are interest rate risk and, to a lesser extent, foreign exchange and equity price risk. These risks stem from our trading and non-trading activities relating to financial instruments such as loans, deposits, securities and financial derivatives. We divide market risk into risks arising from trading activities and risks arising from non-trading activities.

Our market risks arise primarily from Shinhan Bank, and to a lesser extent, Shinhan Investment, our securities trading and brokerage subsidiary, which faces market risk relating to its trading activities.

Shinhan Bank s Risk Management Committee establishes overall market risk management principles for both the trading and non-trading activities of Shinhan Bank. Based on these principles, the Risk Policy Committee acts as the executive decision-making body in relation to Shinhan Bank s market risks in terms of setting its risk management policies and risk limits in relation to market risks and assets and controlling market risks arising from trading and non-trading activities of Shinhan Bank. The Risk Policy Committee consists of deputy presidents in charge of Shinhan Bank s seven business groups and Shinhan Bank s Chief Risk Officer and the Chief Financial Officer. At least on a monthly basis, the Risk Policy Committee reviews and approves reports relating to, among others, the position and

VaR with respect to Shinhan Bank s trading activities and the position, VaR, duration gap and market value analysis and net interest income simulation with respect to its non-trading activities. In addition, Shinhan Bank s Risk Engineering Department comprehensively manages market risks on an independent basis from Shinhan Bank s operating departments, and functions as the middle office of Shinhan Bank. Shinhan Bank measures market risk with respect to all assets and liabilities in bank accounts and trust accounts in accordance with the regulations promulgated by the Financial Services Commission.

Shinhan Investment manages its market risk based on its overall risk limit established by its risk management committee as well as the risk limits and detailed risk management guidelines for each product and department established by its Risk Management Working Committee. Shinhan Investment s Risk Management Working Committee is the executive decision-making body for managing market risks related to Shinhan Investment, and determines, among other things, Shinhan Investment s overall market risk management policies and strategies, and assesses and approves trading activities and limits. In addition, Shinhan Investment s Risk Management Department manages various market risk limits and monitors operating conditions on an independent basis from Shinhan Investment s operating departments. Shinhan Investment assesses the adequacy of these limits at least annually. In addition, Shinhan Investment assesses the market risks of its trading assets. The assessment procedure is based on the standard procedures set by the Financial Supervisory Service as well as an internally developed model. Shinhan Investment assesses the risk amount and VaR, and manages the risk by setting a risk limit per sector as well as a VaR limit.

Shinhan Life Insurance manages its market risk based on its overall risk limit established by its risk management committee. Shinhan Life Insurance manages market risk in regard to assets that are subject to trading activities and foreign exchange positions. Shinhan Life Insurance assesses the market risk amount and the ten-day VaR, a procedure based on the delta-normal method, and manages market risk by setting a ten-day VaR limit. Shinhan Life Insurance assessed the adequacy of these limits at least annually and implements back tests on market risk determinations by comparing daily profit and loss against one-day VaR in 2017.

Shinhan Card does not have any assets with significant exposure to market risks and therefore does not maintain a risk management policy with respect to market risks.

We use financial information prepared on a separate basis according to IFRS for the market risk management of our subsidiaries and, unless otherwise specified herein, financial information in this annual report presented for quantitative market risk disclosure relating to our subsidiaries have been prepared in accordance with IFRS on a separate basis.

Market Risk Exposure from Trading Activities

Shinhan Bank s trading activities principally consist of:

- trading activities to realize short-term profits from trading in the equity and debt securities markets and the foreign currency markets based on Shinhan Bank s short-term forecast of changes in market situation and customer demand, for its own account as well as for the trust accounts of Shinhan Bank s customers; and

- trading activities primarily to realize profits from arbitrage transactions involving derivatives such as swaps, forwards, futures and options, and, to a lesser extent, to sell derivative products to Shinhan Bank s customers and to cover market risk associated with those trading activities.

Shinhan Investment s trading activities principally consist of trading for customers and for proprietary accounts equity and debt securities and derivatives based on stock prices, stock indexes, interest rates, foreign currency exchange rates and commodity prices.

As a result of these trading activities, Shinhan Bank is exposed principally to interest rate risk, foreign currency exchange rate risk and equity risk, and Shinhan Investment is exposed principally to equity risk and interest rate risk.

Interest Rate Risk

Shinhan Bank s exposure to interest rate risk arises primarily from Won-denominated debt securities, directly held or indirectly held through beneficiary certificates, and, to a lesser extent, from interest rate derivatives. Shinhan Bank s exposure to interest rate risk arising from foreign currency-denominated trading debt securities is minimal since its net position in those securities is not significant. As Shinhan Bank s trading accounts are marked-to-market daily, it manages the interest rate risk related to its trading accounts using VaR, a market value-based tool.

Shinhan Investment s interest rate risk arises primarily from management of its interest rate-sensitive asset portfolio, which mainly consists of debt securities, interest rate swaps and government bond futures, and the level of such risk exposure depends largely on the variance between the interest rate movement assumptions built into the asset portfolio and the actual interest rate movements and the spread between a derivative product and its underlying assets. Shinhan Investment quantifies and manages the interest rate-related exposure by daily conducting VaR and stress tests on a marked-to-market basis.

Foreign Currency Exchange Rate Risk

Shinhan Bank s exposure to foreign currency exchange rate risk mainly relates to its assets and liabilities, including derivatives such as foreign currency forwards and futures and currency swaps, which are denominated in currencies other than the Won. Shinhan Bank manages foreign currency exchange rate risk, including the corresponding risks faced by its overseas branches, on a consolidated basis by covering all of its foreign exchange spot and forward positions in both trading and non-trading accounts.

Shinhan Bank s net foreign currency open position represents the difference between its foreign currency assets and liabilities as offset against forward foreign currency positions, and is Shinhan Bank s principal exposure to foreign currency exchange rate risk. The Risk Policy Committee oversees Shinhan Bank s foreign currency exposure for both trading and non-trading activities by establishing limits for the net foreign currency open position, loss limits and VaR limits. Shinhan Bank centrally monitors and manages its foreign exchange positions through its Financial Engineering Center. Dealers in the Financial Engineering Center manage Shinhan Bank s consolidated position within preset limits through spot trading, forward contracts, currency options, futures and swaps and foreign currency swaps. Shinhan Bank sets a limit for net open positions by currency. The limits for currencies other than the U.S. Dollar, Japanese Yen, Euro and Chinese Yuan are set in a conservative manner in order to minimize trading in such currencies.

Shinhan Investment faces foreign currency exchange rate risk in relation to the following product offerings: currency forwards, currency swaps and currency futures. Shinhan Investment centrally monitors and manages transactions involving such products through its Fixed Income, Currency & Commodities Departments. Shinhan Investment s Risk Management Working Committee, which is delegated with the authority to approve foreign currency-related transactions and limits on the related open positions, manages the related foreign exchange risk by setting nominal limits on the amounts of foreign exchange-related products and monitoring compliance with such limits on a daily basis. As of December 31, 2017, Shinhan Investment s net open position related to foreign currency-related products was US$759.6 million, and its open positions related to the sale of Won-U.S. Dollar forwards and Won-U.S. Dollar futures were US$(1,509.6) million and US$1,096.6 million, respectively.

Shinhan Capital faces considerable foreign currency exchange rate exposure in respect of its leasing business, but maintains its net exposure below US$24.5 million by hedging its foreign exchange positions using forwards and currency swaps.

The net open foreign currency positions held by our other subsidiaries are insignificant.

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The following table shows Shinhan Bank s net foreign currency open positions as of December 31, 2015, 2016 and 2017. Positive amounts represent long exposures and negative amounts represent short exposures.

Currency	As of December 31, 2015	2016	2017
	(In millions of US$)		
U.S. Dollars	$ (24.2)	$ (125.0)	$ 47.3
Japanese Yen	9.6	(9.2)	(3.9)
Euro	(1.2)	(4.6)	3.4
Others	784.2	886.4	1,113.9
Total	$ 768.5	$ 747.6	$ 1,160.8

Equity Risk

Shinhan Bank s equity risk related to trading activities mainly involves trading equity portfolios of Korean companies and Korea Stock Price Index futures and options. The trading equity portfolio consists of stocks listed on the KRX KOSPI Market or the KRX KOSDAQ Market of the Korea Exchange and nearest-month or second nearest-month futures contracts under strict limits on diversification as well as limits on positions. Shinhan Bank maintains strict scrutiny of these activities in light of the volatility in the Korean stock market and closely monitors the loss limits and the observance thereof. Although Shinhan Bank holds a substantially smaller amount of equity securities than debt securities in its trading accounts, the VaR of trading account equity risk is generally higher than that of trading account interest rate risk due to high volatility in the value of equity securities. As of December 31, 2015, 2016 and 2017, Shinhan Bank held ₩76.8 billion, ₩192.9 billion and ₩219.0 billion, respectively, of equity securities in its trading accounts (including the trust accounts).

Shinhan Investment s equity risk related to trading activities also mainly involves the trading of equity portfolio of Korean companies and Korea Stock Price Index futures and options. As of December 31, 2015, 2016 and 2017, the total amount of equity securities at risk held by Shinhan Investment was ₩30.1 billion, ₩36.7 billion and ₩22.8 billion, respectively.

Equity positions held by our other subsidiaries are insignificant.

Management of Market Risk from Trading Activities

The following table presents an overview of market risk, measured by VaR, from trading activities of Shinhan Bank and Shinhan Investment, respectively, as of and for the year ended December 31, 2017. For market risk management purposes, Shinhan Bank includes in the computation of total VaR its trading portfolio in bank accounts and assets in trust accounts, in each case, for which it guarantees principal or fixed return in accordance with the Financial Services Commission regulations.

	Trading Portfolio VaR for the Year 2017 Average	Minimum	Maximum	As of December 31, 2017

	(In billions of Won)			
Shinhan Bank:(1)				
Interest rate	₩ 38.4	₩ 22.2	₩ 50.2	₩ 25.1
Foreign exchange(2)	43.8	41.6	46.2	41.9
Equities	4.1	3.0	5.6	4.7
Option volatility(3)	0.1	0.0	0.1	0.1
Commodity	0.0	0.0	0.0	0.0
Less: portfolio diversification(4)	(36.5)	(24.8)	(46.0)	(26.4)