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Credit Opinion: Al-Ain Ahlia Insurance Co.

Global Credit Research - 28 May 2015

Abu Dhabi, United Arab Emirates

Ratings

Category	Moody's Rating
Rating Outlook	STA
Insurance Financial Strength	A3

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Key Indicators

Al-Ain Ahlia Insurance Co.[1][2]

	2014	2013	2012	2011	2010
As Reported (UAE Dirham Millions)					
Total Assets	1,885	1,762	1,552	1,630	1,712
Total Shareholder's Equity	1,196	1,140	986	963	1,012
Net income (loss) attributable to common shareholders	65	42	50	53	62
Gross Premiums Written	600	517	462	504	594
Net Premiums Written	208	212	196	202	205
Moody's Adjusted Ratios					
High Risk Assets % Shareholder's Equity	66.4%	75.6%	68.5%	71.4%	69.8%
Reinsurance Recoverable % Shareholder's Equity	42.4%	42.9%	50.0%	54.2%	50.2%
Goodwill & Intangibles % Shareholder's Equity	-	-	-	-	-
Gross Underwriting Leverage	0.8x	0.7x	0.8x	0.9x	1.0x
Return on avg. Capital (1 yr. avg ROC)	5.6%	4.0%	5.2%	5.4%	5.9%
Sharpe Ratio of ROC (5 yr. avg)	712.4%	548.1%	243.5%	164.8%	119.2%
Adv./(Fav.) Loss Dev. % Beg. Reserves (1 yr. avg)	NA	NA	NA	NA	NA
Financial Leverage	0.0%	0.0%	0.0%	0.0%	0.0%
Total Leverage	0.0%	0.0%	0.0%	0.0%	0.0%
Earnings Coverage (1 yr.)	NM	NM	NM	NM	NM
Cash Flow Coverage (1 yr.)	NA	NA	NA	NA	NA

[1] Information based on IFRS financial statements as of Fiscal YE December 31 [2] Certain items may have been relabeled and/or reclassified for global consistency

Opinion

SUMMARY RATING RATIONALE

Al-Ain Ahlia Insurance Co. is an Abu-Dhabi based insurance company which provides all major lines of insurance, but with a focus on large commercial projects, particularly oil & gas related. It was established in 1975 and is currently c.20% owned by the State of Abu Dhabi. The rating reflects Al-Ain Ahlia's strong business position in the Abu Dhabi market as one of the principal state-owned insurance companies for large State commercial projects, its excellent capitalisation levels and robust reinsurance program, somewhat offset by a higher risk investment strategy compared to typical Western insurers.

In accordance with Moody's rating methodology for GRIs, the rating of Al-Ain Ahlia reflects a combination of the following inputs: (i) a baseline credit assessment of 7 (on a scale of 1 to 21, where 1 represents the lowest credit risk); (ii) 90% dependence, reflecting the company's operating and financial proximity to the government of Abu Dhabi; and (iii) 30% support, reflecting the importance of Al-Ain Ahlia in its capacity as an insurer of government projects offset by the limited state ownership of 19.7%.

The rating also reflects Al-Ain Ahlia's (i) strong market position in the UAE insurance market; (ii) good technical experience in the oil and gas business lines combined with a good cooperation with major international reinsurers; (iii) excellent capital position with gross underwriting leverage at 0.8x in 2014; and iv) strong underwriting profitability with a 5 year average combined ratio of 88% in 2014. These strengths are tempered by (i) the high risk investment strategy, with large investment in equities and real estate; and (ii) the focus on Abu Dhabi (Aa2, Stable) which creates geographic concentration risk and reliance on the Abu Dhabi economic performance.

Credit Strengths

Strong business position in Abu Dhabi, as a leading Government-owned insurer

Good technical experience in the oil and gas business lines combined with a good cooperation with major international reinsurers

Excellent capital position with gross underwriting leverage at 0.8x in 2014

Strong underwriting profitability with a 5 year average combined ratio of 88% in 2014

Credit Challenges

High risk investment strategy, with large investments in equities and real estate

Focus on Abu Dhabi, which creates geographic concentration risk and reliance on the Abu Dhabi economic performance

Rating Outlook

The outlook is stable.

What Could Change the Rating - Up

Significant reduction in investment risk, with a greater focus on high quality bond investments and deposits

Improvement in profitability, with return on capital of over 10% and/or combined ratios below 85% consistently

Wider geographic diversity, with a commanding position in the wider Emirates or elsewhere in the GCC

What Could Change the Rating - Down

Weakened capital position with gross underwriting leverage increasing to 2.5x or lower quality reinsurance program

Deterioration in the underwriting performance, with combined ratios above 100% for several years or increased volatility within business lines

Increased exposure to risky asset classes, such as equities or property

What to Watch for:

Potential political instability within the wider region and the impact, if any, of the declining oil prices on the insurance market and the value of their investments

Further pricing pressure and asset valuation volatility

DETAILED RATING CONSIDERATION

Moody's rates Al-Ain-Ahlia A3 for insurance financial strength which is in line with the adjusted rating indicated by the Moody's insurance financial strength rating scorecard.

Market Position, Brand and Distribution: A - LEADING GOVERNMENT-OWNED INSURER WITH A TOP 5 POSITION IN UAE

Al-Ain Ahlia is a primary insurance company based in Abu Dhabi. It was established in 1975 as one of two Government-owned insurers. Al-Ain Ahlia concentrates primarily on construction and energy risks where they have considerable past experience and a very strong market presence. With a market share of about 1.8% in a highly competitive UAE market, Al-Ain-Ahlia is one of the 5 largest national players. Al-Ain Ahlia scores highly on technical quotations because of its technical expertise through its co-operation with recognized leaders in the reinsurance markets, its history of oil and engineering insurance in the region, its strong reinsurance program, and its State ownership.

Al-Ain Ahlia historically targeted 15% premium growth per annum, but growth is somewhat dependent on the timing of major projects that had been delayed by financial crises. We note that some large projects are scheduled to be developed, with ADNOC alone planning to award numerous multi-billion dollar projects in the near future. Al-Ain Ahlia's premiums grew c. 16% in 2014 and is expected to further benefit from successful tenders, albeit existing soft market conditions may hinder premium growth to some extent.

Distribution is primarily through direct relationships, particularly for the government contracts, through the main office and a small network of branches in Abu Dhabi, Dubai, Al Ain and Sharjah for personal lines business. Some major commercial contracts are acquired via brokers. Moody's regards the market position as in line with an `A' range insurer.

Product Risk and Diversification: Baa - FOCUS ON INDUSTRIAL LINES, CONCENTRATION WITHIN UAE

Geographic diversification is considered to be weak, given the focus on Abu Dhabi. Al-Ain Ahlia does write some inwards reinsurance from the rest of the Gulf region, but it is low in comparison to its Abu Dhabi and UAE premium levels. Nevertheless, Abu Dhabi is a strong economy within the Gulf region, with significant hydrocarbon resources and has been relatively immune from the recent financial crisis. Al-Ain Ahlia's main lines of business include Fire and General Accident (27%), motor (25%), life and health (27%), energy (13%) and Marine/Aviation (8%) of 2014 GPW (this includes commissions as well).

Asset Quality : Baa - HIGH CONCENTRATION TO PROPERTY AND EQUITY INVESTMENTS

Al-Ain Ahlia invests largely in cash/time deposits (36% of invested assets as at YE2014), equities (26% as at YE2014) and investment real estate (38% as at YE2014). High risk assets (equities and real estate) to shareholders' funds reduced to 66.4% as at YE2014 (75.6% at YE2013) but is still relatively high. It should further be noted there are concentration risks as the equities are primarily invested in UAE stocks, mostly in Abu Dhabi. With the exception of the real estate, the portfolio is highly liquid, with most equities being listed. The company has no goodwill on its balance sheet. Reinsurance recoverable to shareholders' equity, at 42.4% at YE 2014 was broadly similar to that of 2013 and demonstrate some exposure to reinsurance partners, although the metric is consistent with a Moody's Aa-parameter.

Overall, asset quality is considered to be in line with a Baa rating.

Capital Adequacy: A - HIGH CAPITAL LEVELS COMPARED TO WESTERN PLAYERS, BUT SIMILAR TO LOCAL PEERS

With a Gross Underwriting Leverage of 0.8x at YE 2014, Al-Ain Ahlia enjoys `Aaa' levels of capital on a raw score basis. However, a considerable amount of the assets are deemed to be high risk. The Gross Underwriting Leverage with 100% of high risk assets deducted from Shareholders Funds is 2.2x which is still strong, and in the `Aa' range.

Al-Ain Ahlia places significant emphasis on its outwards reinsurance program and we note that strong retrocession is often an important factor when the Government awards insurance contracts. Al-Ain Ahlia has strong long-term relationships with most key global reinsurers. Net retentions are low in comparison to total equity of AED1,196 million at YE 2014.

We regard capital adequacy to be in line with that of an `A' company.

Profitability: A - CONSISTENT GOOD BOTTOM LINE AND UNDERWRITING PROFITABILITY, ALTHOUGH SLIGHTLY DECLINING IN THE RECENT PAST

With a 5 year return on capital of 5.2% Al-Ain Ahlia is highly profitable, although this indicator is lower than pre-crises levels. Stripping out investment income, return on capital is a more modest 2.2% in 2014 and 1.8% in 2013, and it has been fairly stable. Underwriting results have been good with a combined ratio of 91.4% in 2014 (2013: 93.8%) and 5-year average (2009-2013) combined ratio of 87.7%, which compares favorable against rated GCC peers (both on a Moody's basis). Moody's expects the underwriting results to be reasonably volatile due to the lumpy nature of the portfolio, however this has remained relatively stable during the last few years. Net underwriting profit increased to AED69.7 million in 2014 compared to AED59.7 million in 2013.

Moody's considers the profitability to be in line with an `A' rated company.

Reserve Adequacy: A - SHORT TAIL NATURE OF BUSINESS MAKES THE LESS SOPHISTICATED RESERVE STRATEGY SUFFICIENT

Reserving is regarded as fairly low risk. The average tail is 4 months and Al-Ain Ahlia appoints independent loss adjusters for all claims above AED50,000. There is no discounting in the reserves and triangles are not available, as is common place within the region.

Reserves are typically covered with cash, and coverage level (on a net of reinsurance basis) is very high at 16.7x in 2014 (2013: 12.5x) (0.9x on a gross basis for 2014 and 0.7x for 2013). IBNRs are set in line with Abu Dhabi regulatory requirements, but tend to overstate losses given the nature of the portfolio, significantly above the regional peer group.

Reserve adequacy is viewed to be in line with an `A' rated company.

Financial Flexibility : Baa - CURRENTLY UNLEVERED, BUT POTENTIAL CAPITAL ACCESS LIMITED

Al-Ain Ahlia is currently un-levered, and consequently the EBIT coverage ratios and debt leverage metrics are extremely strong and in line with a `Aaa' rating. Nevertheless, Moody's regards Al-Ain Ahlia's ability to access capital as being more constrained. Al-Ain Ahlia is listed on the Abu Dhabi stock exchange where it would be able to source additional funds, although Moody's regards the depth of this market to be fairly limited.

We consider the financial flexibility to be in line with a `Baa' rating.

Operating Environment : Aaa-A - ECONOMIC STABILITY OF UAE IS OFFSET BY UNDERDEVELOPED INSURANCE MARKET

Al-Ain Ahlia operates almost exclusively in Abu Dhabi which Moody's views as a medium level risk for insurance operating environment. The insurance market is still in a developmental stage, with growth potentially volatile and with some large risk concentrations and overprovision of insurance products leading to significant levels of price competition. Offsetting this is the economic stability of Abu Dhabi, which is rated Aa2 (Sovereign rating) with a stable outlook reflecting its status as the richest of the emirates with high hydrocarbon wealth and the stability of the domestic political environment.

Other Considerations

Management, Governance and Risk Management

Moody's considers Al-Ain Ahlia's risk management to be somewhat more sophisticated than peers in the region. Through its co-operations with its insurance partners Al-Ain Ahlia has, in Moody's opinion, a fairly strong understanding of underwriting and reserving risks in the lines of business it writes. Al-Ain Ahlia's extensive history of oil and gas insurance in the region also supports the selected underwriting. Investment risks are high, but Al Ain Ahlia's local knowledge, expertise and track record of local investments help mitigate these risks.

Accounting and Disclosure

Al-Ain Ahlia reports under IFRS. Although disclosure is limited in comparison to Western peers, it is in line with local insurers. Disclosure by line of business could be improved.

Ownership

Al-Ain Ahlia is 19.7% owned by the State, through the Abu Dhabi Investment Council. Further Royal family ownership exists through the private investments of members of the Royal family.

Rating Factors

Al-Ain Ahlia Insurance Co.[1][2]

Financial Strength Rating Scorecard	Aaa	Aa	A	Baa	Ba	B	Caa	Score	Adjusted Score
Business Profile								**Baa**	**Baa**
Market Position and Brand (25%)								**Baa**	**A**
- Relative Market Share Ratio			**X**						
- Underwriting Expense Ratio % Net Premiums Written						**44.0%**			
Product Focus and Diversification (10%)								**A**	**Baa**
- Product Risk			**X**						
- P&C Insurance Product Diversification		**X**							
- Geographic Diversification						**X**			
Financial Profile								**Aa**	**A**
Asset Quality (10%)								**Aa**	**Baa**
- High Risk Assets % Shareholder's Equity			**66.4%**						
- Reinsurance Recoverable % Shareholder's Equity		**42.4%**							
- Goodwill & Intangibles % Shareholder's Equity	**0.0%**								
Capital Adequacy (15%)								**Aaa**	**A**
- Gross Underwriting Leverage	**0.8x**								
Profitability (15%)								**Aa**	**A**
- Return on Capital (5 yr. avg)			**5.2%**						
- Sharpe Ratio of ROC (5 yr. avg)	**712.4%**								
Reserve Adequacy (10%)								**A**	**A**
- Adv./(Fav.) Loss Dev. % Beg. Reserves (5 yr. wtd avg)			**0.0%**						
Financial Flexibility (15%)								**Aa**	**Baa**
- Financial Leverage	**0.0%**								
- Total Leverage	**0.0%**								
- Earnings Coverage (5 yr. avg)									
- Cash Flow Coverage (5 yr. avg)									
Operating Environment								**Aaa - A**	**Aaa - A**
Aggregate Profile								**A1**	**A3**

[1] Information based on IFRS financial statements as of Fiscal YE December 31 [2] The Scorecard rating is an important component of the company's published rating, reflecting the stand-alone financial strength before other considerations (discussed above) are incorporated into the analysis

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