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Insurance Markets In Saudi Arabia In The Wake Of Regulatory Restructuring And The Global Economic Downturn

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In the spring of 2009, uncertainty remains the dominant theme for insurance companies and banks across the Gulf Cooperation Council (GCC) region, as it does internationally. However, even within the GCC, Standard & Poor's Ratings Services detects a widespread belief that the Kingdom of Saudi Arabia (KSA) and its financial institutions have been less affected by the downturn than most of its neighbors, and that recovery will likely come more quickly there than elsewhere. Meanwhile, the ongoing flow of Initial Public Offerings (IPOs) on the Tadawul Stock Exchange in Riyadh in 2009--including the April IPOs of insurers Al Rajhi, Weqaya, ACE Arabia, and AXA Cooperative to raise a cumulative Saudi Arabian riyal (SAR) 260 million (approximately \$69 million) of new capital--indicate that Saudi investors still have considerable liquid assets with which to support attractive business propositions.

In our opinion, it is testament to the underlying strength of the national economy and to the quality of both management and regulation that no Saudi-based insurers or banks have succumbed to serious financial difficulties during the current economic turmoil, though some of the nonbank investment houses have experienced some pressures. Meanwhile, deposit rates at local banks have remained low, indicating that liquidity has been satisfactory and confidence maintained. This is despite a collapse in the oil price from its 2008 peak of around \$150 per barrel down to current levels just below \$50, and the astonishing 56.5% fall in the Tadawul All Share Index (TASI) during the 2008 calendar year or, more starkly, a fall of 63.5% from the TASI's Jan. 12, 2008, high of 11,697.01 and fourth quarter low of 4,264.52. Nevertheless, the fundamental strength of KSA's economic base throughout this period of boom and bust is indicated by Standard & Poor's consistent, very strong 'AA-/Stable/A-1+' sovereign credit ratings on the country.

That the broader economic climate remains in our view at least tolerable is perhaps fortunate for KSA's 20 locally incorporated and licensed insurers and reinsurers, given the fundamental restructuring that the Kingdom's insurance sector is currently undergoing. In essence, this restructuring is the result of the ongoing implementation of the radically new regulations laid down in the Cooperative Insurance Companies Law of July 2003 by the insurance (and banking) supervisor, the Saudi Arabian Monetary Agency (SAMA). The law stipulates, we gather, that to be able to operate directly in the domestic market, insurers and reinsurers must obtain a license from SAMA, and to achieve this they must bring their operations onshore by means of a local listing on the Riyadh Tadawul stock exchange with majority ownership by Saudi nationals. An additional aspect of the regulations has been to force insurers to structure their newly incorporated domestic operations to implicitly comply with Sharia law by operating along cooperative insurance lines, with separate shareholder and policyholder accounts. Insurers have also had to adopt the authorities' newly defined regulations on minimum capitalization, corporate governance, market conduct, and the employment of Saudi citizens.

To date, over 40 companies are said to have approached SAMA for a license, and the 25 of these which have either completed or are completing the licensing process are listed in Table 1. With only a few exceptions, such as Malath Co-Operative Ins. & Reins. Co., SABB Takaful, and Saudi Re for Cooperative Reinsurance Co. (BBB+/Stable/--), most of these "new" companies are far from being true start-ups, except in a purely legal sense. In practice, they are the direct successors of previously offshore operations, and most have inherited management, staff, premises,

branding, and customers similar to those that they previously enjoyed when operating as offshore companies. Indeed, insurers such as Mediterranean & Gulf Coop. Ins. & Reins. Co. (MedGulf), Salama/Saudi IAIC for Co-Operative Ins. Co., Saudi Arabian Co-Operative Ins. Co. (SAICO), and others have antecedents in the Saudi market that go back decades, as has the market leader, Tawuniya/The Company for Cooperative Insurance (A/Negative/--).

In other words, despite the legal, accounting, capital, and ownership upheaval caused by the need to conform to the new regulations, Standard & Poor's expects to see many former offshore companies display substantial continuity as regards management, strategy, staffing, and operations, with little visible interruption at the client-facing end of their activities. As such, we will normally analyze them as established companies and not as genuine start-ups, except where a start-up analysis is appropriate, for example, in the absence of even a pro forma historical track record for the Saudi book of business.

Table 1

Insurers And Reinsurers In The Kingdom of Saudi Arabia As Of May 2009	
1	Tawuniya/The Co. for Cooperative Insurance (A/Negative/-)
2	Mediterranean & Gulf Coop. Ins. & Reins. Co. (MedGulf)
3	Malath Cooperative Ins. & Reins. Co.
4	Saudi Arabian Cooperative Ins. Co. (SAICO)
5	Al Ahli Takaful Co. (ATC)
6	SABB Takaful Co.
7	Arabian Shield Cooperative Ins. Co.
8	Salama/ Saudi IAIC for Cooperative Ins. Co.
9	Gulf Union Cooperative Ins. Co.
10	Saudi Fransi Cooperative Assurance (Allianz SF)
11	Sanad for Cooperative Ins. & Reins. Co.
12	Trade Union Cooperative Insurance Co.
13	Al Sagr Co. for Cooperative Ins.
14	Saudi Indian Co. for Cooperative Ins.
15	Arabia Ins. Cooperative Co.
16	Saudi United Cooperative Ins. Co. (Wala'a)
17	BUPA Arabia for Cooperative Insurance Co.
18	Saudi Re for Coop. Reinsurance Co. (BBB+/Stable/-)
19	United Cooperative Ass. Co. (UCA)
20	Al Ahlia Cooperative Ins. Co. (Al-Ahlia)
21	Allied Cooperative Ins. Group (ACIG)
22	Wiqaya Takaful Ins. & Reins. Co.
23	Al Rajhi Co. for Cooperative Insurance
24	AXA Cooperative Insurance Co.
25	Ace Arabia Cooperative Insurance Co.
26	Buruj Cooperative Insurance Co.
27	Al Alamiya for Cooperative Insurance
28	Gulf General Insurance Co.
29	Solidarity Saudi Takaful Co.

Table 1

Insurers And Reinsurers In The Kingdom of Saudi Arabia As Of May 2009 (cont.)

As of May 2009, companies 1-20 are fully licensed, companies 21-25 are listed on the Tadawul, but are not yet licensed, and companies 26-29 are not yet either listed or licensed.

Strong Economic Factors Underpin The KSA Insurance Market

Publicly available market data for the new insurers and reinsurers in the Kingdom is still somewhat scarce, particularly for 2008. However, a cursory overview of the macroeconomic and demographic factors relating to the country suggests that the insurance and reinsurance sectors have considerable potential for growth in the medium and long term. For example, according to figures monitored by MEED magazine (see table 2), the KSA expects to spend some \$608 billion on planned major projects. At the very least, this spending implies an expansion in insurable activity and thus the probability of growth in premium volumes in the years ahead. Such statistics in our view lend credibility to the optimistic claims of certain Saudi insurers, who forecast total market premiums reaching SAR30 billion (\$8 billion) by the middle of the next decade.

Table 2

Forecast Gulf Spending On Projects

(Mil. \$)	Jan. 2009	Sept. 2008	Jan. 2008	Sept. 2007
Kingdom of Bahrain	64,127	43,599	27,821	31,435
State of Kuwait	306,660	296,319	274,597	252,662
Sultanate of Oman	95,921	92,401	51,023	46,016
State of Qatar	220,671	205,479	156,192	142,466
Kingdom of Saudi Arabia	608,083	564,872	400,882	363,278
United Arab Emirates	1,214,308	967,947	717,223	662,984
Gulf Cooperation Council total	2,509,770	2,170,617	1,627,738	1,498,841

Source: Middle East Economic Digest (MEED).

The KSA dominates the GCC in terms both of GDP and population, with some 20 million nationals supplemented by a large force of six million or more foreign workers and their dependents (see table 3). As for the levels of insurance premium available within the Kingdom, SAMA published statistics in 2008 indicating that the entire sector generated some SAR8.6 billion (\$2.3 billion) of gross premiums in 2007, of which by far the largest lines were health and motor at SAR3.1 billion and SAR2.4 billion, respectively, or 64% of the total (see table 4).

Intuitively, many foreign observers expect energy-related lines to dominate the commercial insurance sector in Saudi Arabia. Yet in our view these expectations may be misplaced given that much of the Kingdom's energy and energy infrastructure is controlled by Saudi Aramco, which channels virtually all of its insurance requirements through its captive insurer, Stellar Insurance Ltd. (AA-/Stable/--), which is currently based in Bermuda. Stellar, in turn, directly accesses the global reinsurance markets for its protection needs.

Table 3

Comparative Demographic And Gross Domestic Product Data For Gulf Cooperation Council And Other World Regions

	Population (mil.)	Population growth (%)	2007 GDP (bil. \$)	GDP growth (%)	GDP per capita (\$000s)	Agriculture (%)	Industry (%)	Services (%)
Kingdom of Bahrain	0.8	1.3	24.6	6.6	34.7	0.3	43.6	56.0

Table 3

Comparative Demographic And Gross Domestic Product Data For Gulf Cooperation Council And Other World Regions (cont.)								
State of Kuwait	2.6	3.6	138.6	5.6	55.3	0.4	54.7	44.9
Sultanate of Oman	3.3	3.2	61.2	5.3	19.1	2.2	38.3	59.5
State of Qatar	0.9	2.3	57.7	7.8	75.9	0.1	73.5	26.4
Kingdom of Saudi Arabia	28.2	1.9	572.2	4.7	20.7	3.0	61.8	35.2
United Arab Emirates	4.6	3.8	145.8	8.5	55.2	1.8	59.3	38.9
Gulf Cooperation Council total	40.4	--	1,000.1	--	30.0	1.3	55.2	43.5
The Russian Federation	141.0	(0.5)	2,076.0	8.1	14.6	4.6	39.1	56.3
U.S.	304.0	0.9	13,860.0	2.2	46.0	0.9	20.6	78.5
EU	491.0	0.1	14,450.0	3.0	32.9	2.0	27.1	70.7
World	6,700.0	1.2	65,820.0	5.2	10.0	4.0	32.0	64.0

Source: United States Central Intelligence Agency.

Table 4

Line of business	2007		2006		Growth 2006-07 (%)
	(Mil. SAR)	Total (%)	(Mil. SAR)	Total (%)	
Health	3,065	36	2,222	32	38
Motor	2,440	28	1,920	28	27
Property	742	9	769	11	(4)
Accident and liability (and other)	577	7	580	8	0
Marine	532	6	431	6	23
Engineering	480	6	544	8	(12)
Protection and savings	327	4	218	3	50
Energy	305	4	127	2	141
Aviation	115	1	126	2	(9)
Total	8,583	100	6,937	100	24

Source: Saudi Arabian Monetary Agency (Insurance Supervision Dept.) Market Survey Report, 2007. SAR--Saudi Arabian riyal.

However, even with the "leakage" of insurance premium through this and other offshore captives (which we believe have so far been unaffected by the new insurance regulations), large premium volumes are still available domestically and, equally importantly, they continue to grow rapidly, thereby creating business opportunities for those newly incorporated insurers and reinsurers still endeavoring to enter the market. Table 4 shows that total available premium in Saudi Arabia grew by 24% between 2006 and 2007. We note that these high rates of premium growth have been inflated by the introduction of compulsory motor and, more gradually, compulsory health insurance for foreign residents in recent years but, even prospectively, most observers expect to see year-on-year growth in total gross premium income approaching 20%, even if an element of this growth is fueled by inflation.

We see insurance penetration and density calculations as giving final indicators of the market's potential. Insurance penetration, notably gross written premiums as a percentage of GDP, reached 0.61% in 2007, up 14.4% on the previous year. Similarly, insurance density (that is, per capita spending on insurance/population) grew by 20.9% in

2007 to reach \$95. Nevertheless, although the rates of growth appear strong, the absolute levels still remain far below those regularly seen in Western and some Asian markets where penetration ratios range from 5% to 9% and density levels can reach as high as \$3,287 (source: SIGMA).

New Minimum Capital Regulations Will Lead To Increased Capacity

With a minimum capital requirement of SAR100 million for insurers and SAR200 million for reinsurers, together with the generally increased levels of capitalization that the compulsory IPO process is bringing, underwriting capacity appears to be increasing across the sector, as is the need to build up business volumes to generate satisfactory profits to remunerate the expanded shareholder base. It therefore seems reasonable to expect these insurers to seek to protect and develop their market presence, although they are not expected to overtake the market's dominant leader, Tawuniya. The latter will undoubtedly face further loss of market share and staff in favor of its newly incorporated rivals. Nevertheless, the growing level of good-quality insurable and reinsurable activity available in the Kingdom suggests that business volumes and technical operating performance at the leading companies will remain at least satisfactory. Standard & Poor's believes that strong technical and overall earnings are a better indicator of underlying performance and success at an insurer than market share percentages alone.

Despite the impressive growth potential and the current surge of newly-incorporated companies seeking to participate in the KSA insurance market, we view the sector as essentially skewed toward a limited number of activities. Table 4 shows that 60.0% of 2007 gross premiums related to general insurance, 35.7% to health, and just 3.8% to life assurance-type protection and savings. Net of the SAR3.0 billion of premium ceded to reinsurers, the bias is even more apparent; a full 84% of the whole market's net retained premiums of SAR5.5 billion related almost equally to the two compulsory lines of health and motor (see table 5).

Table 5

Net Written Premiums By Line Of Business In The Kingdom of Saudi Arabia, 2006-2007					
Line of business	2007		2006		Growth 2006-07 (%)
	(Mil. SAR)	Total (%)	(Mil. SAR)	Total (%)	
Health	2,403	43	1,843	42	30
Motor	2,297	41	1,814	42	27
Protection and savings	267	5	153	4	74
Accident and liability (and other)	219	4	243	6	(10)
Marine	170	3	124	3	37
Engineering	98	2	84	2	16
Property	84	2	81	2	4
Aviation	4	0	4	0	(17)
Energy	2	0	0	0	--
Total	5,544	100	4,347	100	37

Source: Saudi Arabian Monetary Agency (Insurance Supervision Dept.) Market Survey Report, 2007. SAR--Saudi Arabian riyal.

Narrow Focus Of The Market Limits Strategic Choice

We are of the view that local insurers have a limited number of strategic choices, none of them easy. They can aim for volume in the highly competitive, administratively demanding areas of health and motor, or use their niche

technical skills to pursue higher margins on much lower volumes in fire, engineering, marine, accident, and liability. The other alternatives are to take on the banks, fund managers, the local stock exchange, and other investment outlets such as property to attract savings money into the insurance sector by offering the prospect of attractive capital gains potential. Alternatively, they can attempt to join the cut-and-thrust of the international reinsurance markets by accessing a sliver of the 35.4% of national gross premium income that the statistics show as being ceded to reinsurers.

No single approach guarantees success, particularly as the regulatory minimum capital requirements now applicable and the ongoing enthusiasm of local IPO investors means that many of the newly listed insurers now commencing operations are extremely well capitalized relative to likely retained business volumes. In other words, many of the new providers will have too much capital to be able to afford to pursue a small niche strategy while still adequately rewarding their shareholders, unless a significant part of earnings comes from investment income, with all the attendant risks that an aggressive investment strategy inevitably brings.

Health insurance has enormous growth potential

Looking at the marketplace line by line, health insurance (the largest sector by premium volume) may well be the most interesting option for many, if not most insurers at present. Growth has been rapid since 2006 as the authorities introduced compulsory health cover gradually, starting with large employers of expatriate workers and their dependents, and working down to smaller employers. The Ministry of Health, working through the Cooperative Health Insurance Council (CCHI), has robustly promoted compulsory health insurance. Its dual objectives were to reduce spiraling national healthcare costs and to improve the quality of service in healthcare provision through competition. Interestingly, corporations that are now obliged to provide health cover to their foreign workers and their families have often found it equitable to extend similar coverage to their Saudi national employees.

In the light of this experience, there is currently much debate in Saudi Arabia concerning the extension of compulsory health cover to the whole of the Saudi population. Compulsory cover for local nationals could be gradually introduced if, for example, the requirement was extended to encompass all employees, foreign and local, working in the private sector or, ultimately, if public sector employers were also required to provide their staff with health insurance. Were such requirements to be introduced, as many confidently expect, the health insurance sector would continue to see steady long-term growth, with a possible doubling or even tripling of the 2007 gross health premium volume of SAR3.1 billion over the next decade.

For its part, Standard & Poor's acknowledges the commercial potential for insurers in the health care sector in Saudi Arabia, although the sector appears to be already well-served on a direct basis by the existing leading insurers, and by specialist health providers such as BUPA Arabia. Yet even those existing insurers that lack sufficient infrastructure to administer a large health book on their own often feel it necessary to offer the line as an accommodation to their larger corporate clients. They have almost invariably achieved this through the extensive use of third-party administrators (TPAs), of which about half a dozen already operate in the Kingdom.

Standard & Poor's believes that no insurer active in Saudi Arabia in 2008 can afford to ignore the health sector when the related premiums are rising toward half the total net premium in the whole market. Competition is likely to become intense, particularly for major and prestige group health accounts. For the moment, at least, the larger medical insurers are all still managing to achieve sound, but reducing, underwriting profits on the line. That said, we have observed that in other parts of the world health insurance is often problematic because insureds can have a

seemingly insatiable appetite for treatment and also because, when things go wrong, the intensely personal nature of health care can lead to dissatisfaction by influential individuals. These people then "punish" their insurer by withdrawing other business that they control. In other words, the successful health insurer needs to be able to walk a constant tightrope between being too generous and too tough in the use of exclusions and the settlement of claims.

Table 6

Gross Claims Paid By Line Of Business In The Kingdom of Saudi Arabia, 2005-2007						
Line of business	2007		2006		2005	
	(Mil. SAR)	Total (%)	(Mil. SAR)	Total (%)	(Mil. SAR)	Total (%)
Health	1,898	47	1,240	41	963	38
Motor	1,218	30	1,010	33	882	35
Protection and savings	38	1	35	1	45	2
Accident and liability (and other)	170	4	170	6	112	4
Marine	166	4	155	5	240	9
Engineering	219	5	102	3	78	3
Property	283	7	300	10	218	9
Aviation	63	2	18	1	13	1
Energy	6	0	9	0	1	0
Total	4,061	100	3,040	100	2,552	100

Source: Saudi Arabian Monetary Agency (Insurance Supervision Dept.) Market Survey Report, 2007. SAR--Saudi Arabian riyal.

Motor must repair the reputational damage caused by unregulated insurers

After decades of dominating the KSA insurance market in local premium volume terms, motor insurance has now slipped into second place behind health. Motor is also arguably the most competitive sector of the market. The main impetus to volume is the now-compulsory requirement for third-party liability cover, although comprehensive cover is also becoming more common. Before the explosive growth of the health insurance sector, compulsory motor had traditionally been at the core of the retail market and still represents the primary point of contact between the retail individual and the insurance industry.

The nature of motor cover in the previously unregulated market has, in our view, contributed to a jaundiced view of insurance. Too often, the previously unregulated insurers offered poor service and a cavalier approach to the payment of claims. Indeed, many of the smaller motor insurers, that have now been appropriately eliminated by the advent of regulation, used to do little more than sell the physical insurance documentation that the police would ask for in the event of an accident or when renewing a driving license.

In our view, this cheap "protection" served to undermine the economic base of the motor insurance sector, with the realistic premiums charged by professional providers appearing prohibitively expensive. The removal of the unprofessional element suggests that the current generation of providers can now attempt to charge economic rates that vary according to the type of risk.

Standard & Poor's nevertheless notes that the motor account is also the area where the new, explicitly Sharia-compliant takaful insurance companies may enjoy a real competitive advantage. Because motor cover reaches so deeply into the population, it will not only encounter a mass clientele with an innate dislike of insurance based on experiences under the old, unregulated regime but also one that is confused by what does and what does not comply with Sharia law. Assuming that actual pricing is more or less equal, we believe that it is these buyers of motor cover

that will most likely opt for the comfort and ethical security of a takaful product.

As a footnote, a seeming echo of the old, unregulated regime reverberated in February 2009 when the CCHI banned a number of leading insurers from selling health cover for several weeks. We understand this ban was something of a reprimand for these insurers, having sold health insurance certificates to certain small employers without providing any actual cover. It has been subsequently explained that this practice was effected by junior members of staff for personal gain, and that the senior management of the affected insurers had not intended to subvert the spirit of the regulations. Nevertheless, this incident does, in our view, underline the need for close operational risk management inside insurers.

Life protection and savings products remain marginal

As in many countries of the world, it is the banks, rather than insurers, that are most readily associated with savings products. Similarly, such are the opportunities for direct investments in local property and stocks and shares, that there is only negligible demand for insurance-wrapped savings products, particularly as there is little need to shelter income from capital gains taxes. Nevertheless, some insurers are keen to explore and develop opportunities for protection products, in particular the term-life cover required of borrowers lest they die before a loan has been repaid. The recent difficulties affecting certain major foreign providers of sophisticated protection covers and asset management services may, in our opinion, create limited opportunities for Saudi insurers to expand in the life protection and savings space. However, as tables 4, 5, and 6 show, savings and protection still represents a minor part of the overall insurance sector, at just 3.8% of gross and 4.8% of net premiums.

Reinsurance Comes Onshore

Licensed to operate in July 2008, Saudi Re (BBB+/Stable/-) missed the July 1 reinsurance renewal season for many insurers, but nonetheless became the first dedicated, local reinsurer to commence underwriting in the KSA. Until this time, all pure reinsurance capacity in the Kingdom had been provided by offshore regional and, more particularly, international and global reinsurers. Meanwhile, those other KSA-based insurers that also have a license to write reinsurance (hence the reference to "reinsurance" in their company names) are expected to use the license only to write co-insurance which, in Saudi Arabia, is technically handled as if it were reinsurance. Given that no other applications for pure reinsurance licenses are currently before SAMA, it appears likely that Saudi Re will enjoy both a "first mover" advantage and, with over SAR1 billion of capital, will also benefit over the next couple of years from an undisputed local market position. Nevertheless, we expect that in due course at least one or two additional reinsurers will also likely seek to set up in the Kingdom.

We are of the view that given the current hardening of rates in global reinsurance markets as capacity is withdrawn in the wake of investment losses, the creation of an indigenous reinsurer within the Kingdom appears timely. Moreover, the authorities are known to be keen to develop a fully-fledged reinsurance as well as insurance infrastructure within the country. They aim to improve the sophistication of the local market, create skilled employment opportunities for nationals, and to help keep at least a part of the enormous sums currently leaving the country in the form of ceded reinsurance premiums within the Kingdom. As tables 7 and 8 show, as a whole, the GCC region exports over half its markets' gross premium income to reinsurers, with Saudi Arabia transferring SAR3.0 billion in 2007 (35.4% of its gross premiums), excluding the additional, very substantial cessions made by certain captive insurers. It seems natural and, indeed, inevitable that efforts will be made in due course to keep a part of this ceded premium within the KSA, probably by a variety of means including fronting by local insurers and

reinsurers, or even by the creation of pools or other retention devices.

Table 7

Gulf Cooperation Council Reinsurance Markets (2006 Data)			
Country	Insurance premium (mil. \$)	Ceded to reinsurers (%)	Reinsurance premium (mil. \$)
United Arab Emirates	2,726	55	1,499
Kingdom of Saudi Arabia	1,850	37	690
State of Kuwait	628	60	377
State of Qatar	573	58	332
Sultanate of Oman	349	64	223
Kingdom of Bahrain	308	56	173
Total	6,434	51	3,288

Source: Logic Management Consulting Research.

Table 8

Kingdom of Saudi Arabia Insurer Retention Ratios By Line Of Business, 2005-2007			
(%)	2007	2006	2005
Health	78.4	82.9	80.8
Motor	94.1	94.5	93.7
Marine	31.9	28.8	29.5
Engineering	20.3	15.5	19.2
Property/fire	11.3	10.5	10.8
Aviation	3.1	3.4	2.9
Energy	0.8	0.0	0.1
Accident and liability (and other)	38.0	42.0	43.1
Total	64.6	62.4	60.9

Source: Saudi Arabian Monetary Agency (Insurance Supervision Dept.) Market Survey Report, 2007.

Incentives exist for potential entrants to the reinsurance market

We understand that reinsurers considering incorporation within the Kingdom are attracted by the potential to tap at least a part of the ceded premium flow and by the significant regulatory incentives. Such incentives already include local regulations imposing a 5% withholding tax on premiums ceded to foreign reinsurers, and there is also a slightly ambiguous and currently unenforced regulatory requirement that KSA-based insurers should seek to place at least 30% of their reinsurance locally, unless they receive a written waiver from the authorities.

Although Standard & Poor's would not expect SAMA to oblige local companies to place a full 30% of their cessions with just one local reinsurer, Saudi Re is nonetheless expected to benefit from these fiscal and regulatory incentives. Moreover, as additional reinsurers set up in the Kingdom and cedants gain a choice of local reinsurance providers, we believe it becomes easier to believe that the 30% local reinsurance requirement will be much more actively enforced.

Strong Regulation Brings Strong Prospects

The KSA's December 2005 membership of the World Trade Organization may have provided the necessary catalyst for the regulatory changes now being seen in the insurance sector. However, we believe that the real reason behind

the current restructuring of the market is the authorities' genuine desire to provide the country with the modern financial infrastructure it needs to service the increasingly diverse and complex needs of its steadily diversifying economy of \$572.2 billion of GDP as of 2007, as well as the requirements of a young and rapidly growing population.

Given the limited number of Saudi insurance ratings currently in the public domain, it is difficult to discuss an outlook for the Kingdom's insurance and reinsurance sectors in ratings terms. Nevertheless, we revised the outlook on what we consider to be the otherwise strong 'A' rating on Tawuniya to negative on March 31, 2009, given a balance sheet that had been somewhat weakened by generous dividend payments to shareholders, as well as depreciated investment values under the SOCPA (Saudi generally accepted accounting principles) accounting conventions used for the last time in the 2008 accounts ahead of the now compulsory move for all KSA insurers to International Financial Reporting Standards. In general, however, Standard & Poor's is optimistic concerning the very good and even strong prospects of those companies that it has so far had an opportunity to consider in detail. Insurers, like banks, tend to prosper when the economy in which they principally operate is strong, so the medium-term future is at least stable and may become positive.

Nevertheless, in the short term, market conditions are likely to remain very competitive, particularly in the main lines of health and motor, and this inevitably encourages caution. Indeed, after the euphoria among Saudi investors regarding the insurance sector IPOs of 2007 and early 2008, it is salutary to observe that for 2008 the lists of both top gainers and top losers on the Tadawul are dominated by newly incorporated insurers. It is therefore a comfort to see rather more stability in share prices in 2009, even though the TASI did touch a 12-month low of 4,130.01 on March 9, 2009, before recovering to 5,216.84 by April 22, up 3.18% on the start of the year. Meanwhile, the Tadawul Insurance Index of insurer share prices ended 2008 at 609.62 (down from 2,232.30 at the start of that year), and as of April 22, 2009, was up 47.6% at 899.97 relative to the start of the current year.

Table 9

Tadawul Stock Exchange Data On Listed KSA Insurance And Reinsurance Companies (In Order Of Listing Date)							
Company	Total shares issued (mil.)	Free float on Tadawul (mil.)	Free float (%)	Market capitalization as of March 31, 2009 (Mil. SAR)	Share price as of April 22, 2009 (SAR)	Share price as of Dec. 31, 2008 (SAR)	
Tawuniya/The Co. for Cooperative Ins.	50	26.9	53.7	1,400	36.8	34	
Malath Co-Op. Ins. & Reins. Co.	30	14.2	47.5	738	27.5	32.6	
Mediterranean & Gulf Co-Op. Ins. & Reins.	80	54.4	68.0	1,348	19.7	17	
Saudi Fransi Co-Op. Assurance	10	3.5	35.1	628	68.5	41.9	
Salama Co-Op. Ins. Co.	10	8.5	85.0	0	55.3	33.2	
Saudi United Co-Op. Ins. Co. (Wala'a Ins.)	20	19	95.0	414	26.6	14.3	
Arabian Shield Co-Op. Ins. Co.	20	16	80.0	398	25.6	13.8	
SABB Takaful Co.	10	3.5	35.0	615	97	33.3	
Sanad for Co-Op. Ins. & Reins. Co.	20	8	40.0	379	38.1	12.1	
Saudi Arabian Co-Op. Ins. Co. (SAICO)	10	9	90.0	332	45.9	22.4	

Table 9

Tadawul Stock Exchange Data On Listed KSA Insurance And Reinsurance Companies (In Order Of Listing Date) (cont.)						
Saudi Indian Co. for Co-Op. Ins.	10	4	40.0	342	45.9	42.3
Gulf Union Co-Op. Ins. Co.	22	8.8	40.0	537	28.3	12.7
Al Ahli Takaful Co. (ATC)	10	2.6	26.0	648	81.5	43.1
Al Ahlia Co-Op. Ins. Co. (Al-Ahlia)	10	4	40.0	334	47	23.9
Allied Co-Op. Ins. Group (ACIG)	10	4	40.0	520	81.8	22.9
Arabia Ins. Co-Op. Co.	20	8	40.0	410	27.9	13.2
Trade Union Co-Op. Ins. Co.	25	10.5	42.0	430	25.4	12.8
Al Sagr Co. for Co-Op. Ins.	20	18	90.0	558	32	12.1
United Co-Op. Ass. Co. (UCA)	20	8	40.0	408	25.3	35.2
Saudi Re for Cooperative Reins. Co.	100	90	90.0	950	10.7	8.8
BUPA Arabia for Co-Op. Ins. Co.	40	16	40.0	600	17.4	12

Source: Data extracted from Saudi stock exchange (Tadawul) Web site and Bloomberg. N/A--Not applicable.

Concerning operating performance, we believe that SAMA will not long tolerate the behavior of any insurance management team that seeks growth in market share through persistent, excessively low tariffs. That said, we are nonetheless finding that the very strong capitalization that KSA-based insurers often enjoy is being somewhat offset in our analysis by cumulative concerns over the increasingly competitive nature of the marketplace, by the difficulties most companies face in recruiting and retaining skilled senior and operational staff, and also by some insurers' controlled but still significant investment exposure to volatile equity and property markets.

Meanwhile, as a country, Saudi Arabia itself will, we believe, also face challenges as it seeks to further diversify its economy away from a dependence on energy-related activities. In particular, the creation of appropriate and sustainable employment for an already large, young and still rapidly growing population remains a major social and political imperative. Today, over half the population of Saudi Arabia is estimated to be below the age of 21 and many thousands of young men attempt to join the workforce every year.

As long as social, political, or geopolitical issues do not intrude to destabilize the likely evolution, Standard & Poor's believes that there are excellent prospects for the successful development of a well-regulated, thriving domestic and regional insurance and reinsurance infrastructure. This infrastructure, we believe, will help service the needs of the economy while at the same time creating valuable career opportunities for Saudi nationals. That said, we note that insurers are not always held in high esteem either as employers or as service providers, and the industry must organize itself to improve its image in the retail sector by better explaining the value and, to some extent, the ethical acceptability of their products and services. In the interim, the suspicion remains that unless a given type of insurance cover is made compulsory, too many Saudi citizens will simply not want to buy it.

Prospectively, the search for market share and a critical mass of revenue by the Kingdom's many new-entrant insurance providers will, we believe, lead to yet more competitive pressures and to some soft pricing, particularly for prestigious corporate accounts. Consequently, during the newly reformed sector's current development phase, Standard & Poor's expects to see some volatility in major client relationships, staff, and bottom-line earnings before

a clearer landscape starts to emerge in which it will be possible to better identify the likely winners and losers in the new marketplace.

However, even some of the weaker players will, we believe, still be able to buy time, despite consistent underperformance, because of their relatively easy access to additional capital or, in some instances, by privileged access to the corporate business of their major shareholders. At some point soon, and with the likely encouragement of the authorities, Standard & Poor's expects to see some significant moves toward consolidation of the marketplace, with stronger players growing more rapidly than their less successful and smaller peers, and periodically merging with or acquiring them. This being the case, we anticipate a significant concentration of market share in the accounts of the top half dozen or so insurers, even though the total number of licensed companies is likely to remain between 20 and 25 into the long term.

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