Fairmont, Dubai

AM Best's
MENA Insurance Market Briefing

17 November 2023

Fairmont, Dubai

AM Best's MENA Insurance Market Briefing

Nick Charteris-Black
Managing Director, Market Development – EMEA

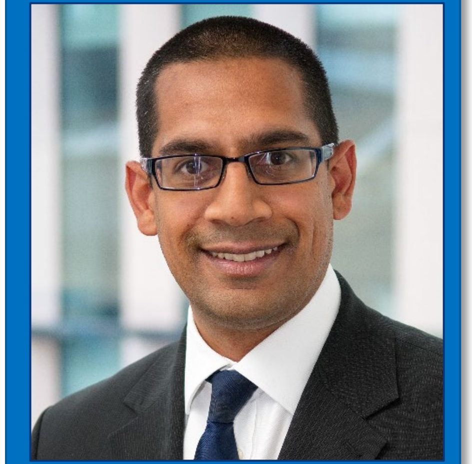
17 November 2023

Presenters

Nick Charteris-Black
Managing Director, Market Development – EMEA

Vasilis Katsipis
General Manager, MENA, South and Central Asia

Greg Carter
Managing Director, Analytics – EMEA & AP



Mahesh Mistry
Senior Director, Head of Analytics – London

Ben Diaz-Clegg
Senior Financial Analyst

Agenda – Insurance Market Briefing

09:15 **Welcome and Introductory Comments**
Nick Charteris-Black, Managing Director, Market Development – EMEA

09:20 **Global Reinsurance Market Update**
Greg Carter, Managing Director, Analytics – EMEA & AP

09:50 **Benchmarking MENA Ratings**
Ben Diaz-Clegg, Senior Financial Analyst, Analytics

10:20

10:50 **Dealing with the Permacrisis/Polycrisis**
Mahesh Mistry, Senior Director, Head of Analytics – London

11:25 **M&A in the GCC insurance Market – A Changing Landscape?**
Vasilis Katsipis, General Manager, MENA, South and Central Asia

12:00 **Q&A**

12:30 **Networking Lunch**

Disclaimer

Regulated by Dubai Financial Services Authority (DFSA) as a Representative Office.

Disclaimer

US Securities Laws explicitly prohibit the issuance or maintenance of a credit rating where a person involved in the sales or marketing of a product or service of the CRA also participates in determining or monitoring the credit rating, or developing or approving procedures or methodologies used for determining the credit rating.

<u>No part of this presentation amounts to sales / marketing activity and AM Best's Rating Division employees are prohibited from participating in commercial discussions.</u>

Any queries of a commercial nature should be directed to AM Best's Market Development function.

Global Reinsurance Market Update

Greg Carter
Managing Director, Analytics
EMEA & Asia Pacific

Global Reinsurance Market – Discussion Outline

- Outlook, Main Drivers, Key Themes
- Is There Actually a “Capacity Shortage”?
- Results Improving, but still Playing Catch-Up / IFRS 17 Transition
- Business Models Evolving – Hybrids, Role of ILS, Distribution
- AM Best’s Expectations – The Next 12 Months

Global Reinsurance Market Outlook – Stable

Headwinds	Tailwinds
"Available" capital ≠ "Deployed" capital Investor caution	Reinsurers remain well capitalized despite buffers having shrunk
More complex and evolving risk environment Volatile investment markets	Demand remains strong, characterized by flight to quality
Inflationary pressures, rising interest rates Higher cost of capital	Technical results continue to improve Underwriting discipline expected to last
Protection gap bound to widen Pressure to innovate to maintain relevance in broader economy	Reinsurers have shown in the past their ability to innovate and re-invent themselves

Is There Actually a "Capacity Shortage"?

Why is this Cycle Different?

Leading indicators to historic reinsurance company formations

Single major event:
Hurricanes
Earthquakes
Terrorism

Material capital erosion

Sharp rates increase in a short period of time

New 2023/24 class?

Rising interest rates only since 2022

Higher cost of opportunity

Gradual rate increases before1/1/23

Alternative Capital

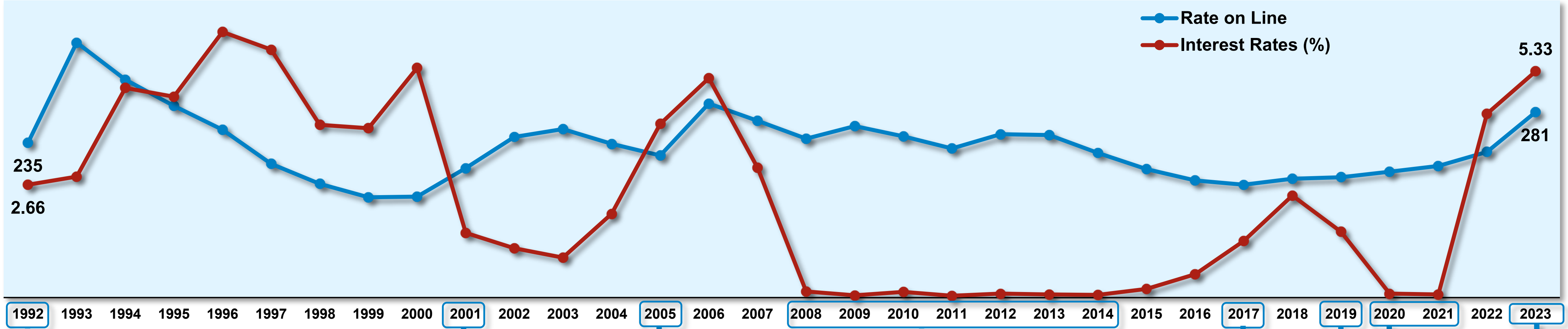
Plateaued since 2018

No single major catastrophe event

Accumulation of more frequent secondary perils

Global reinsurers remain well capitalised

Why is this Cycle Different?



Hurricane Andrew
Increase in interest rates

9/11 terror attack

Hurricanes – Katrina, Rita, Wilma

Sustained lower interest rates for over six years
Japan and NZ Earthquakes
Thailand Floods
Hurricane Sandy

Hurricanes – Harvey, Irma, Maria

COVID-19 Pandemic
Decline in interest rates
Expansionary monetary policies

High inflation
Rising interest rates
Low unemployment
Secondary perils

New reinsurers enter the market in response to these events

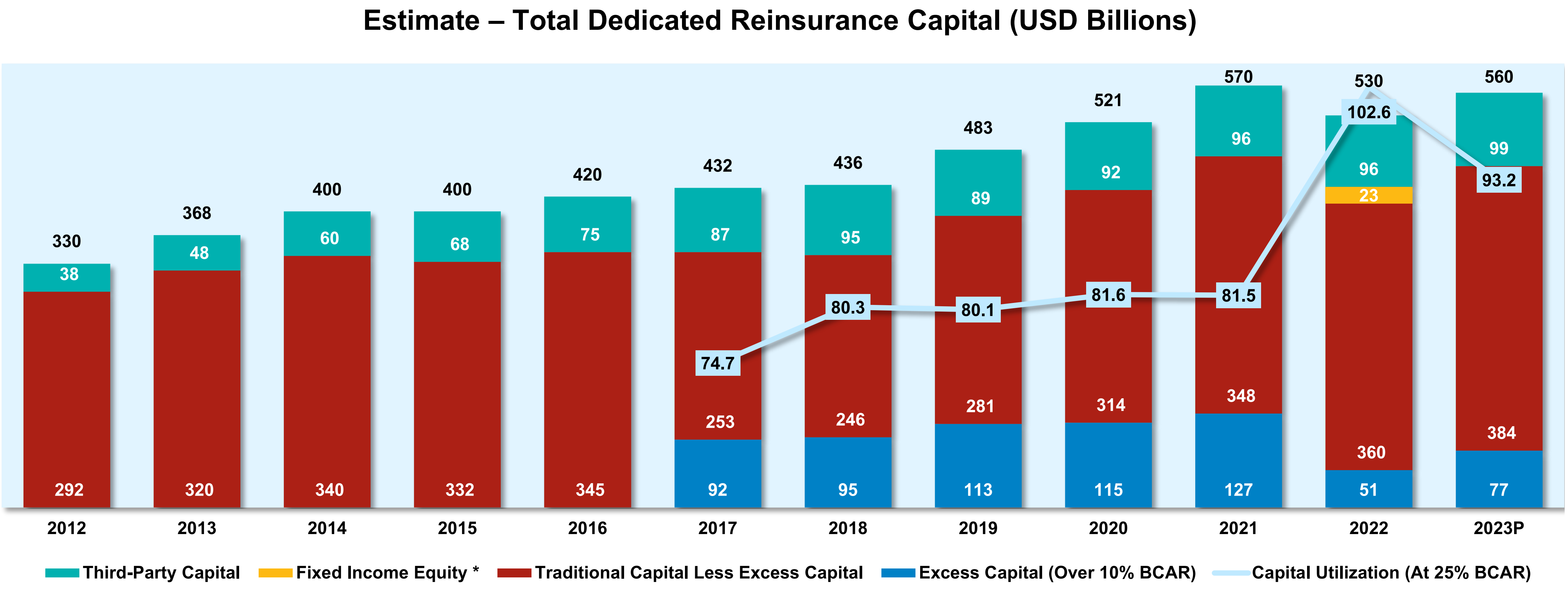
No new entrants

Limited number of new entrants

Our Insight, Your Advantage™

Sources: Estimates by Guy Carpenter and AM Best

Global Reinsurance Market Capital



Notes: *: For reinsurers that have ample cash liquidity to support their potential shock losses, the "fixed-income equity" adjustment captures the amount of capital that AM Best anticipates will be recovered as bonds mature over time

Sources: Estimates by Guy Carpenter and AM Best

Ratings – Reinsurers Retain Financial Strength

Negative Factors

- Fixed-income unrealized investment losses
- Persistent high claims activity
- Weather-related and secondary perils
- Best's Capital Adequacy Ratios declined, but balance sheet strength remains unchanged
- Operating performance impacted

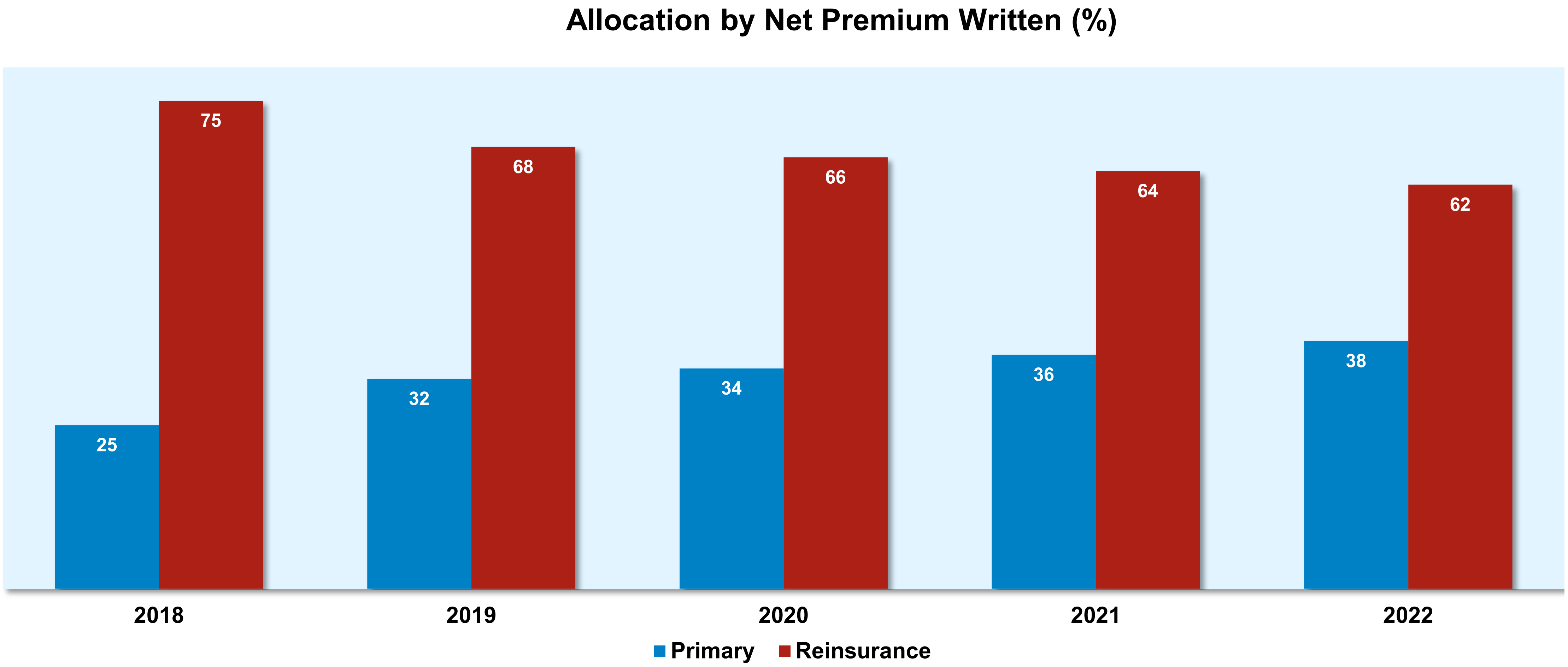
Positive Factors

- Capital buffers protection
- Higher interest rates
- Asset Liability Management
- High credit quality of investment portfolios
- Dividend policy / share buybacks unaffected
- Balance sheet strength assessment remains unchanged
- Underwriting discipline

Results Improving, but Still Playing Catch-Up

IFRS 17 Transition

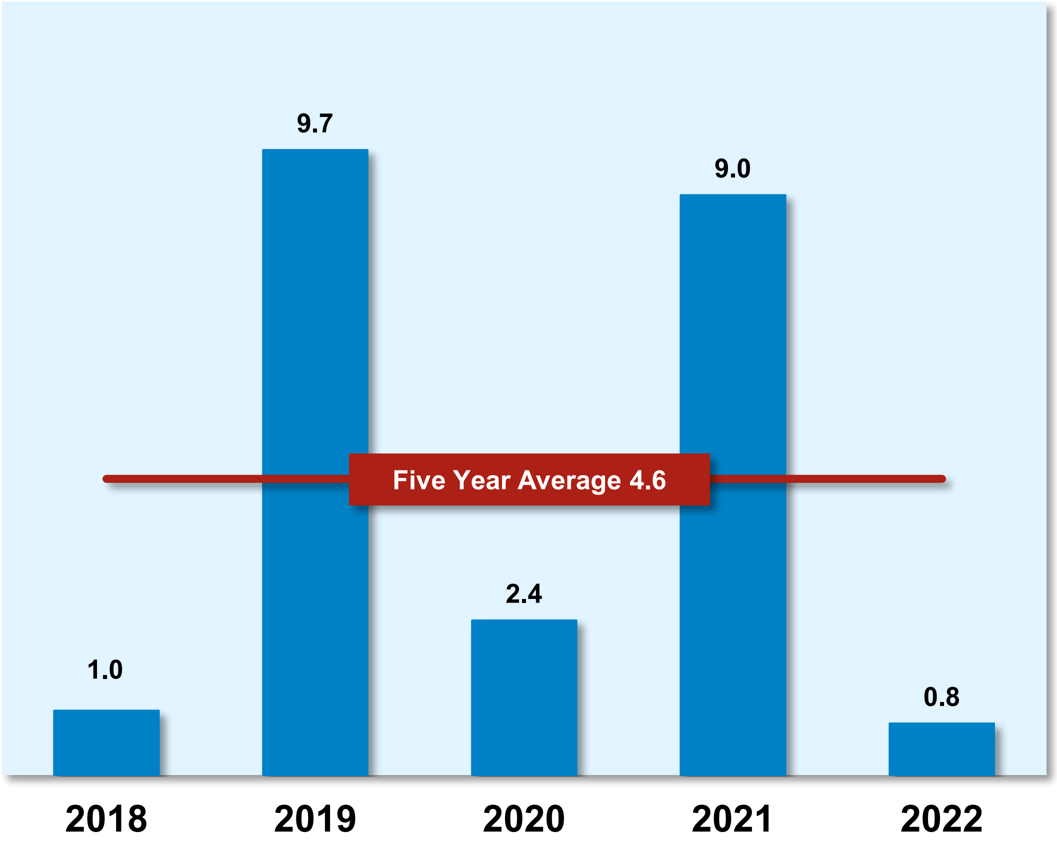
Global Reinsurance – Primary Insurance vs. Reinsurance



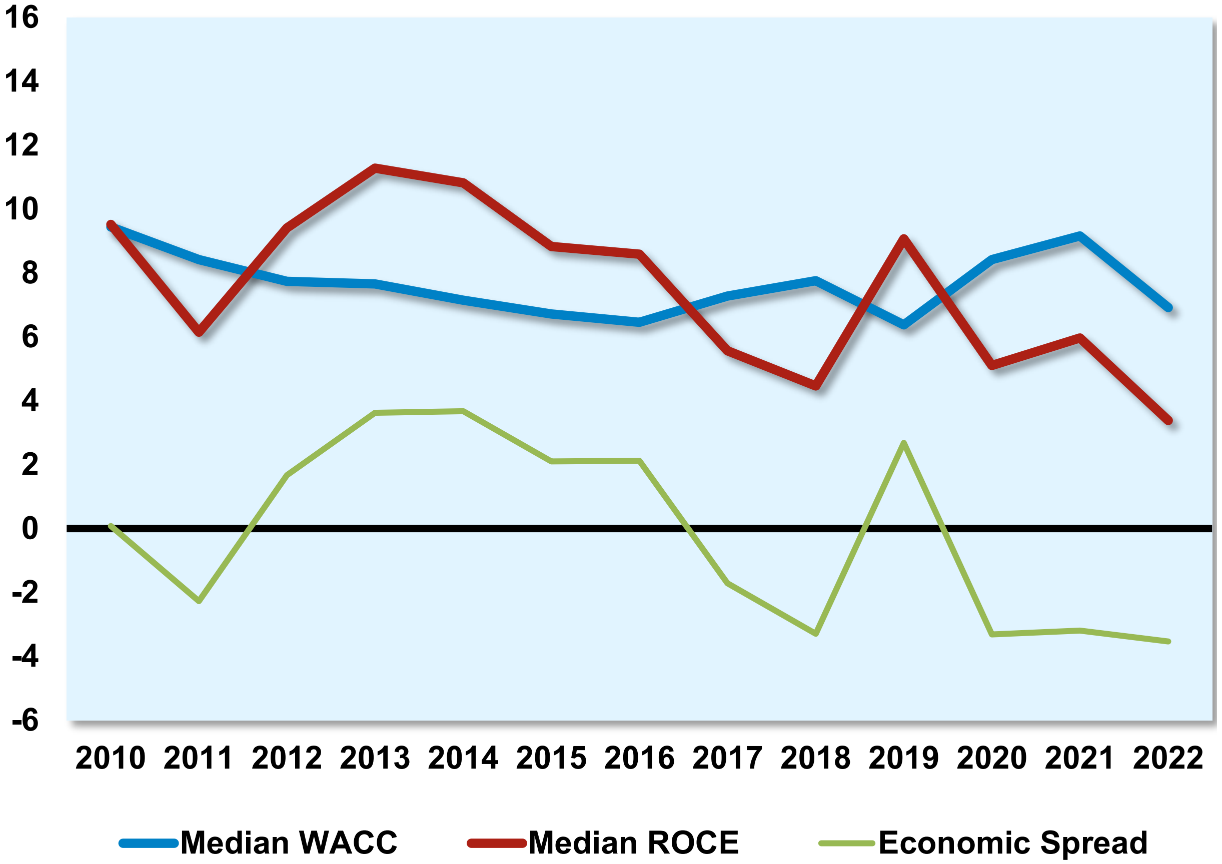
Based on the 25 largest reinsurance groups.
Source: AM Best data and research

Global Reinsurance Market Performance

Return on Equity (%)



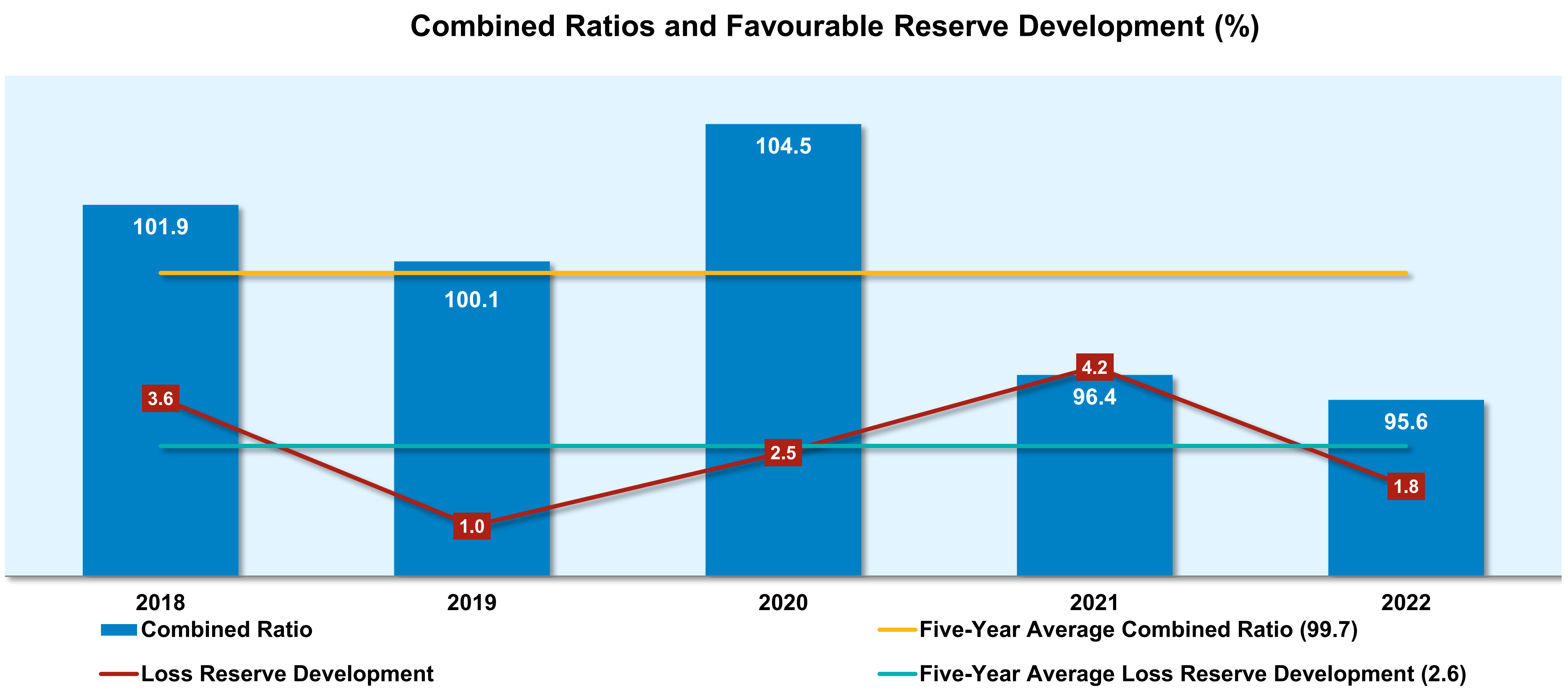
Reinsurers' Median Weighted Average Cost of Capital (WACC) Compared to Median Return on Capital Employed (ROCE) (%)



Our Insight, Your Advantage™

Sources: Return on Equity - AM Best data and research,
WACC and ROCE - Bloomberg

Global Reinsurance Market Performance



Our Insight, Your Advantage™

Source: AM Best data and research

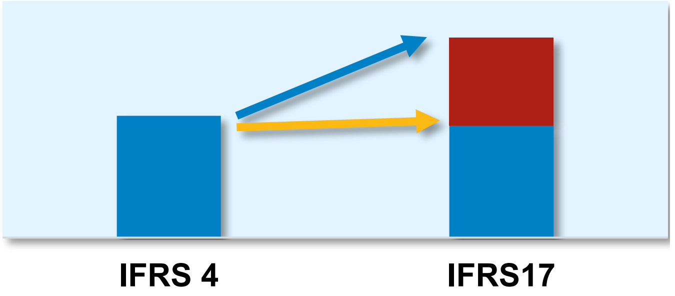
Transition to IFRS 9 and IFRS 17

For consistency, AM Best always takes an economic view of a company or group's balance sheet

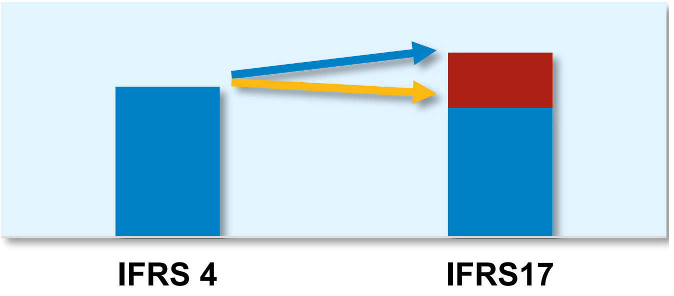
Capital & Surplus **Contractual Service Margin**

(For illustrative purposes only – Not to scale)

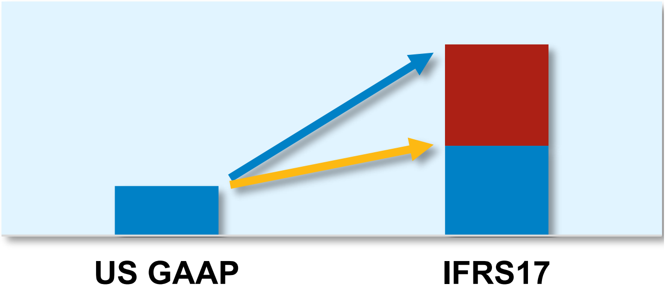
Munich Re



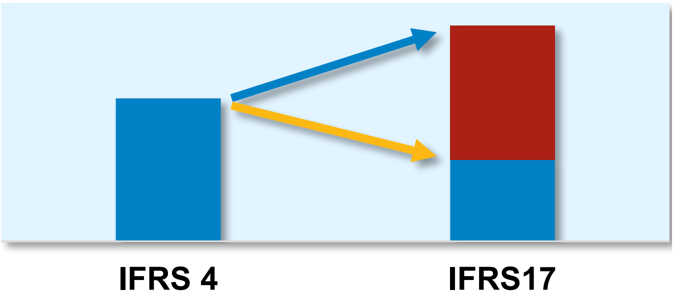
Hannover Re



Swiss Re

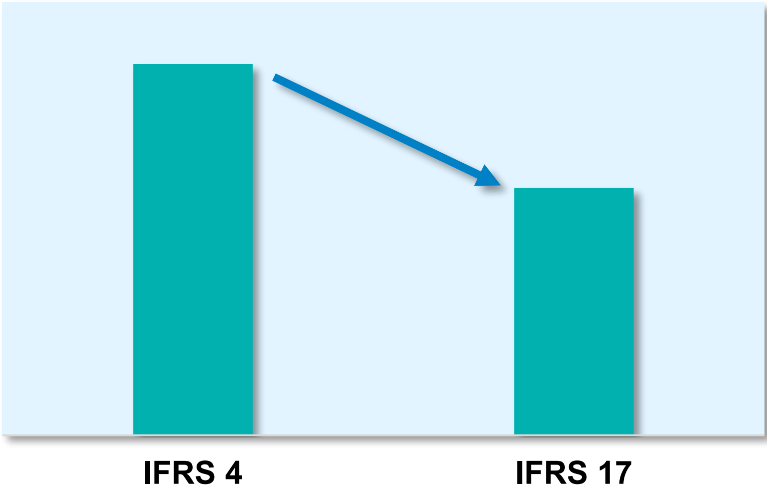


SCOR



Financial Leverage

(Debt/[IFRS Equity+CSM+Debt])

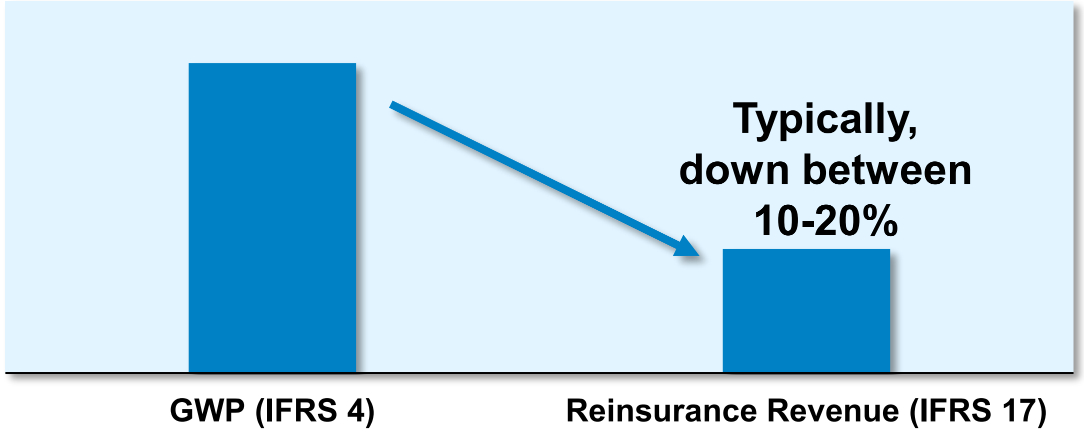


Source: AM Best data and research

Transition to IFRS 9 and IFRS 17

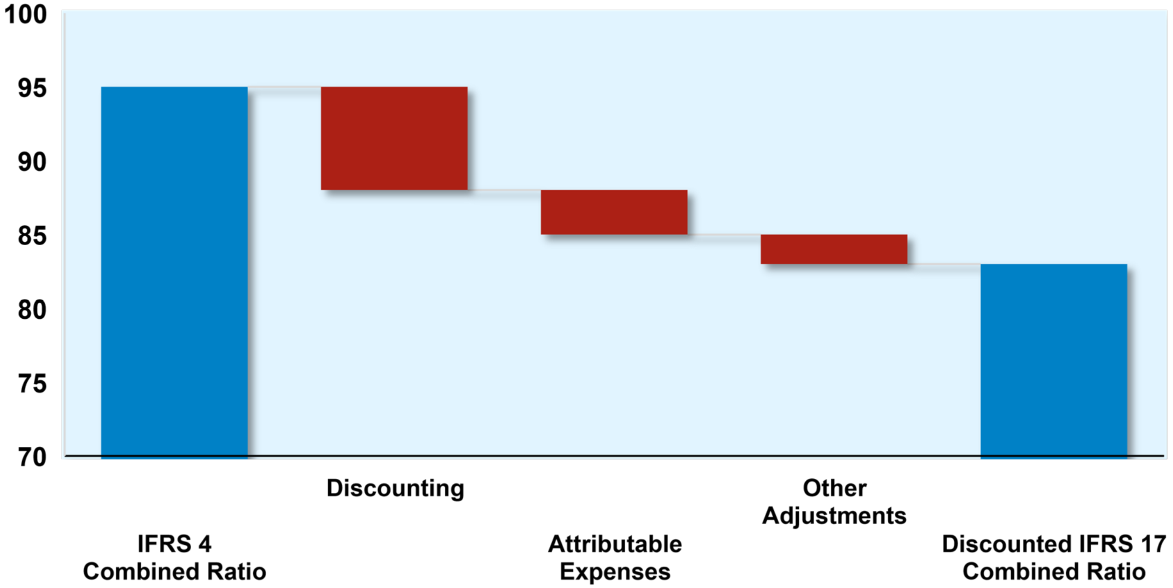
Comparisons against US GAAP writers will become more challenging

Transitioning from Premiums Written to (Re)insurance Revenue



Return on Equity (Income/IFRS Equity)

Favourable Movements in Combined Ratio



Source: AM Best data and research

Business Models Evolving –

Hybrids
Role of ILS
Distribution

Evolution of Business Models

Investors seem to prefer diversified, flexible companies, with a proven track record

High demand for reinsurance, driven by flight to quality. Financial strength is paramount

Well diversified, nimble and established reinsurers in a strong position

Specialised reinsurers have become rare

Expansion of established players more likely than new entrants

Alternative capital has become more of a partner than a competitor

Evolving distribution models critical to expand business

What to Expect for the Next 12 Months?

AM Best's Expectations – The Next 12 Months

Underwriting profits –
to continue

Rate increases –
to continue at a slower pace

Disciplined expansion of the reinsurance segment –
led by major players

Significant new capital / number of new entrants –
unlikely

Inflationary pressures and high interest rates –
to remain

Renewed appetite for volatile lines of business –
but with tighter terms and conditions

Emerging risks –
slow expansion

Higher retentions –
here to stay

Key Themes for the Reinsurance Sector - 2023

There is no capacity shortage
just smarter allocation

Results improving
but reinsurers still catching up

Business models evolving
the death of the specialist?

Global Reinsurance Market Update

Greg Carter
Managing Director, Analytics
EMEA & Asia Pacific

Q&A

Benchmarking MENA Ratings

Ben Diaz Clegg
Senior Financial Analyst, Analytics

Issuer Credit Ratings In MENA

Rating Units
≈ 46

Upgrades	Downgrades
1 (0)	5 (2)

Outlook Distribution
Positive 2%
Stable 76%
Negative 22%

Issuer Credit Rating and Outlook Changes – MENA

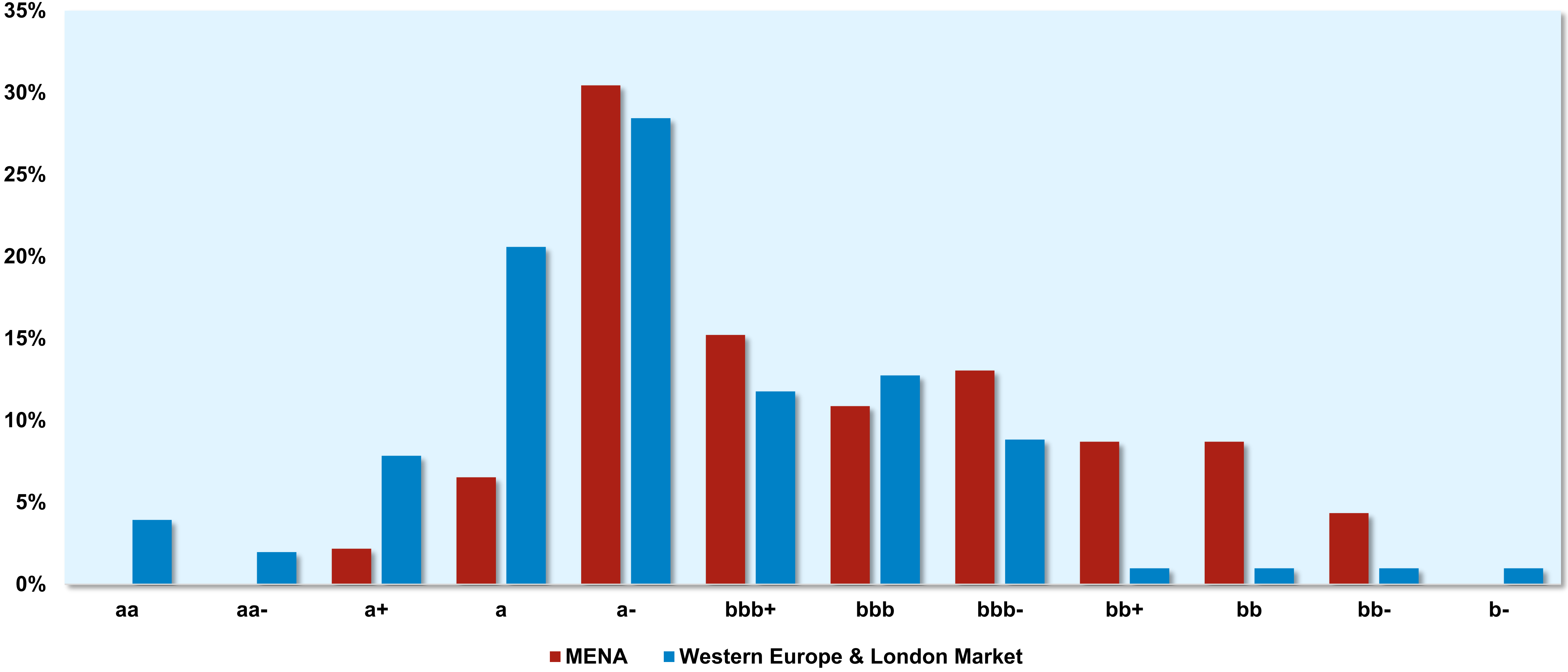
Changes in Balance Sheet Strength
1 Upgrade, 3 Downgrades

Operating Performance
2 Downgrades

Stable Outlook to Positive	0
Negative Outlook to Stable	2
Positive Outlook to Stable	1
Stable Outlook to Negative	4

Source: AM Best data and research
Data as of September 2023

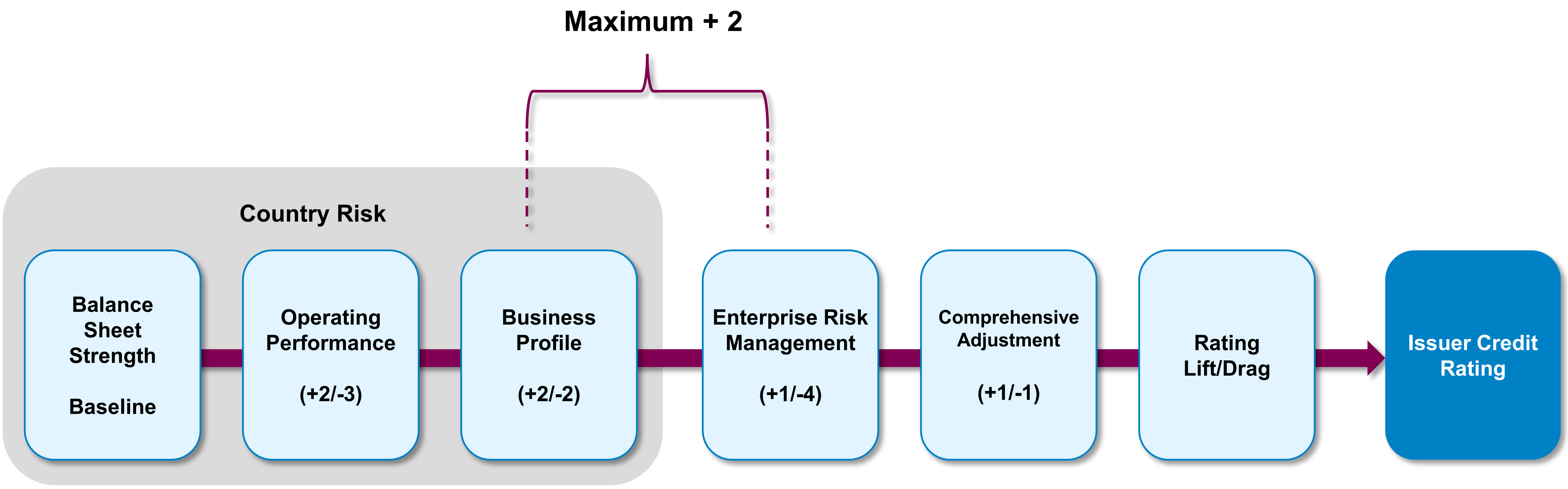
Issuer Credit Ratings EMEA - Distribution



Our Insight, Your Advantage™

Source: AM Best data and research
Data as of September 2023

AM Best's Rating Process - Recap



AM Best's Rating Process – Recap (Cont.)

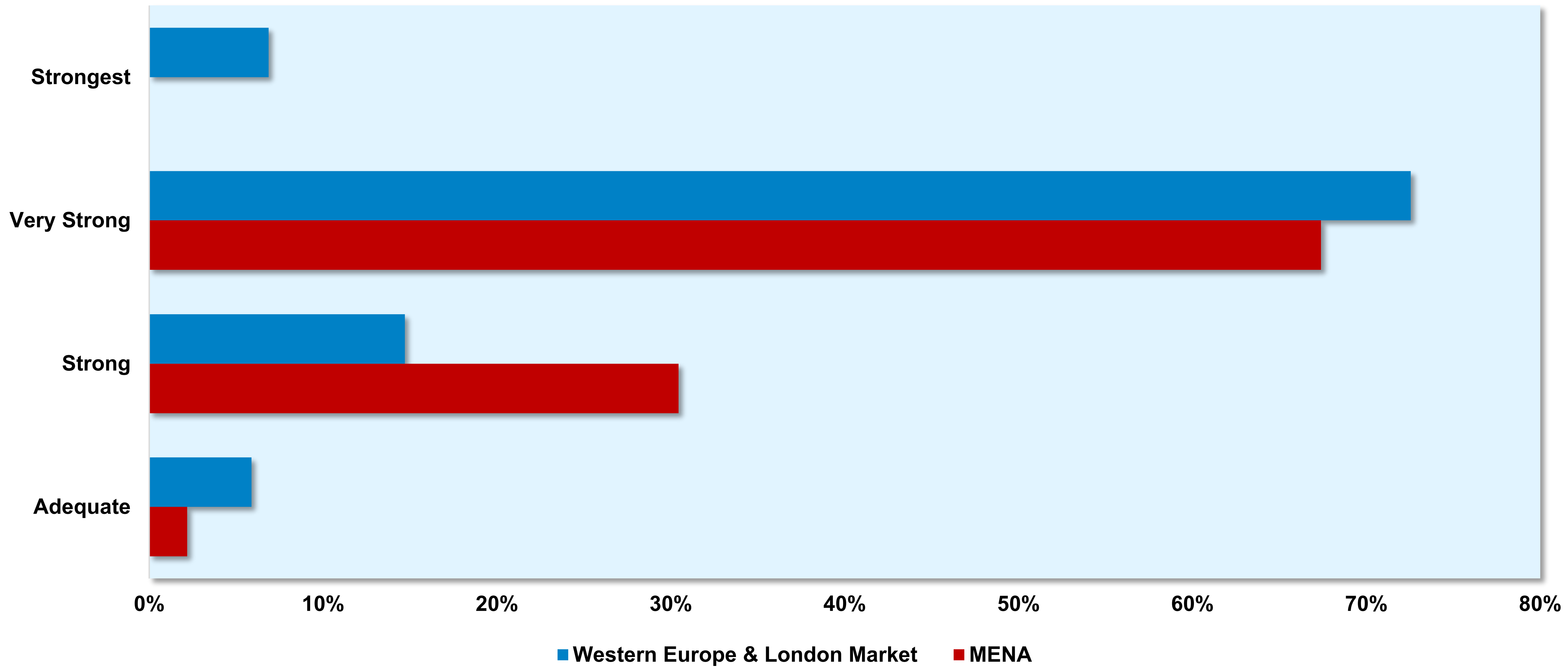
Balance Sheet Strength Baseline	Operating Performance (+2/-3)	Business Profile (+2/-2)	Enterprise Risk Management (+1/-4)
Assessment	**Assessment**	**Assessment**	**Assessment**
Strongest	Very Strong +2	Very Favourable +2	Very Strong +1
Very Strong	Strong +1	Favourable +1	Appropriate 0
Strong	Adequate 0	Neutral 0	Marginal -1
Adequate	Marginal -1	Limited -1	Weak -2
Weak	Weak -2	Very Limited -2	Very Weak -3/4
Very Weak	Very Weak -3		

AM Best's Rating Process – Recap (Cont.)

Overall Balance Sheet Strength Assessment

Combined Balance Sheet Assessment (Rating Unit/Holding Company)	Country Risk Tier				
	CRT-1	CRT-2	CRT-3	CRT-4	CRT-5
Strongest	a+/a	a+/a	a/a-	a-/bbb+	bbb+/bbb
Very Strong	a/a-	a/a-	a-/bbb+	bbb+/bbb	bbb/bbb-
Strong	a-/bbb+	a-/bbb+	bbb+/bbb/bbb-	bbb/bbb-/bb+	bbb-/bb+/bb
Adequate	bbb+/bbb/bbb-	bbb+/bbb/bbb-	bbb-/bb+/bb	bb/bb-	bb/bb-/b+
Weak	bb+/bb/bb-	bb+/bb/bb-	bb-/b+/b	b+/b/b-	b/b-/ccc+
Very Weak	b+ and below	b+ and below	b- and below	ccc+ and below	ccc and below

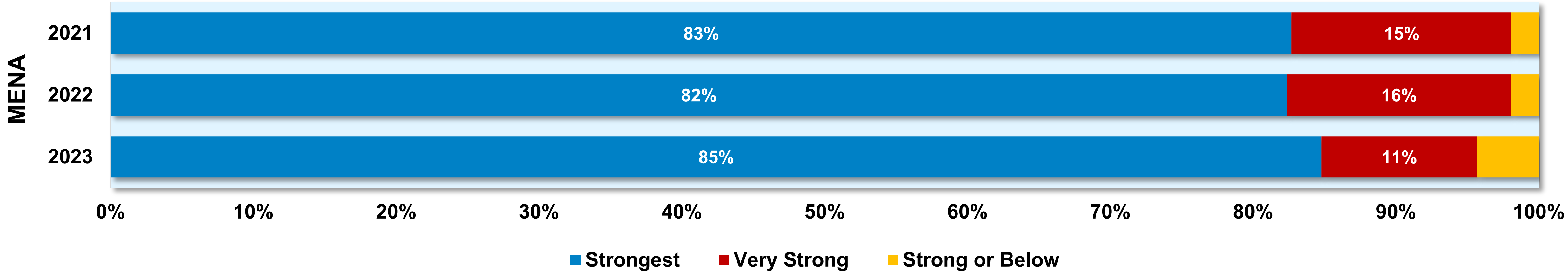
MENA Balance Sheet Strength - Distribution of Assessments (%)

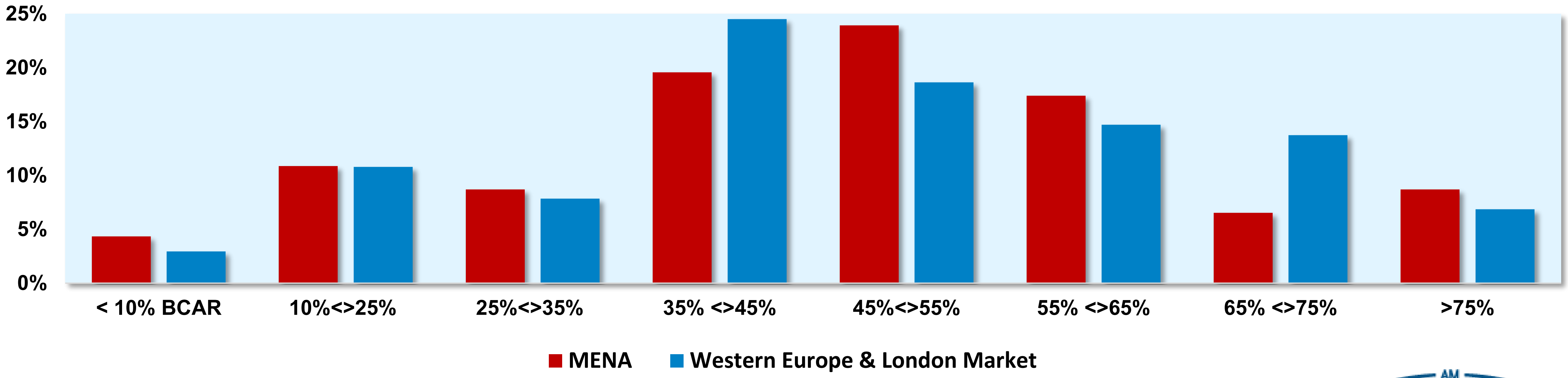


Our Insight, Your Advantage™

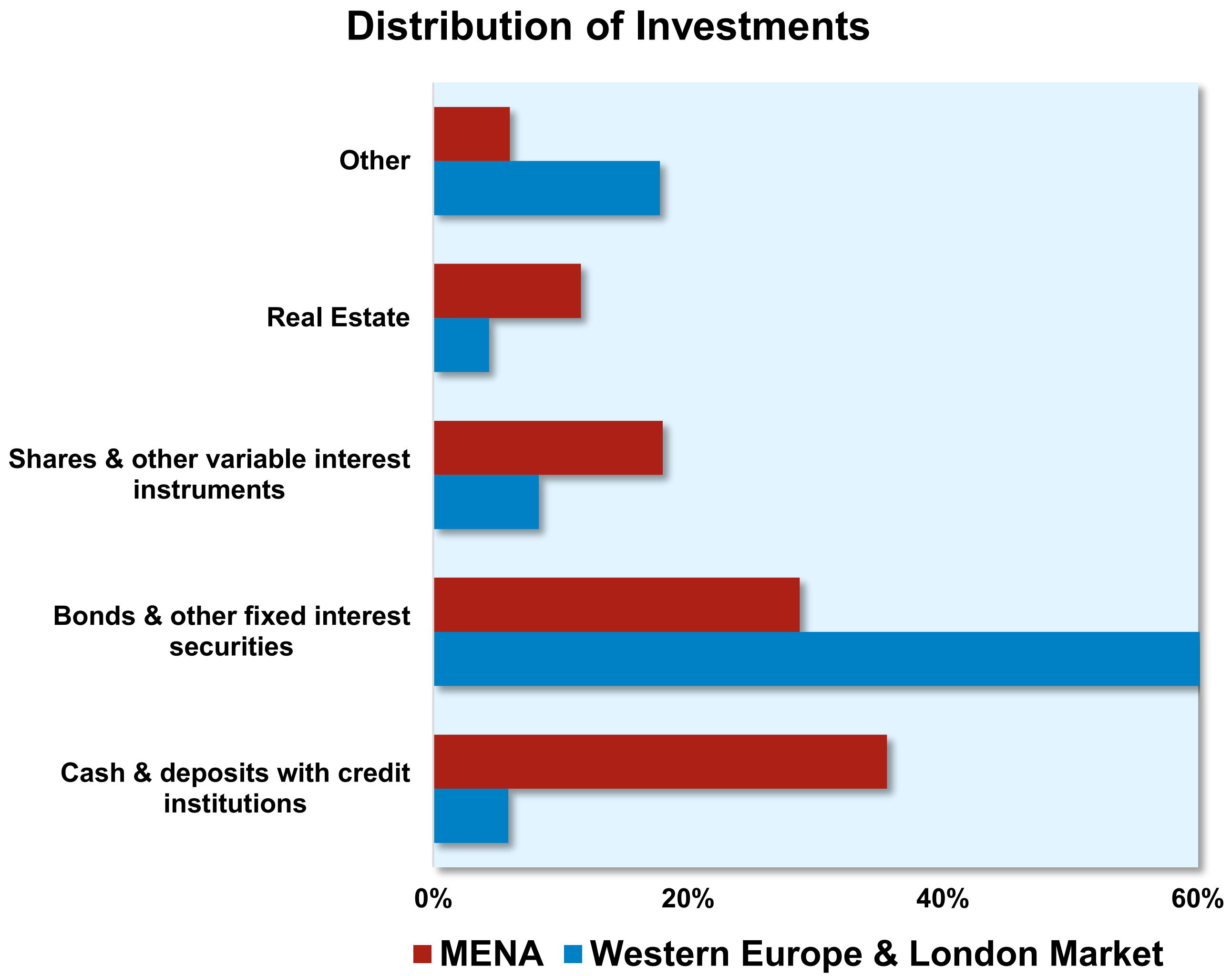
Source: AM Best data and research
Data as of September 2023

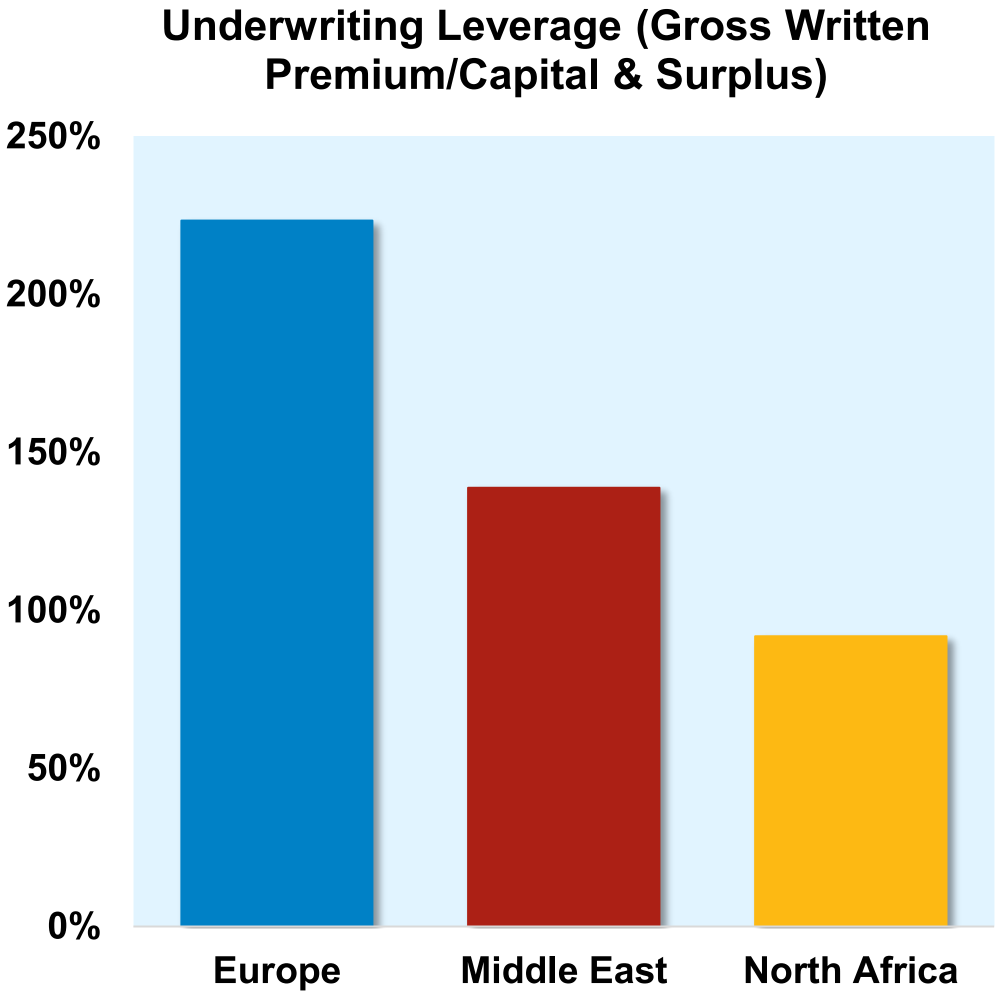
MENA Balance Sheet Strength - Distribution of BCAR Scores (%)





Balance Sheet Strength – Distribution of Capital Requirements





Source: AM Best data and research
Data as of year-end 2022

MENA Balance Sheet Strength vs BCAR Distribution (%)

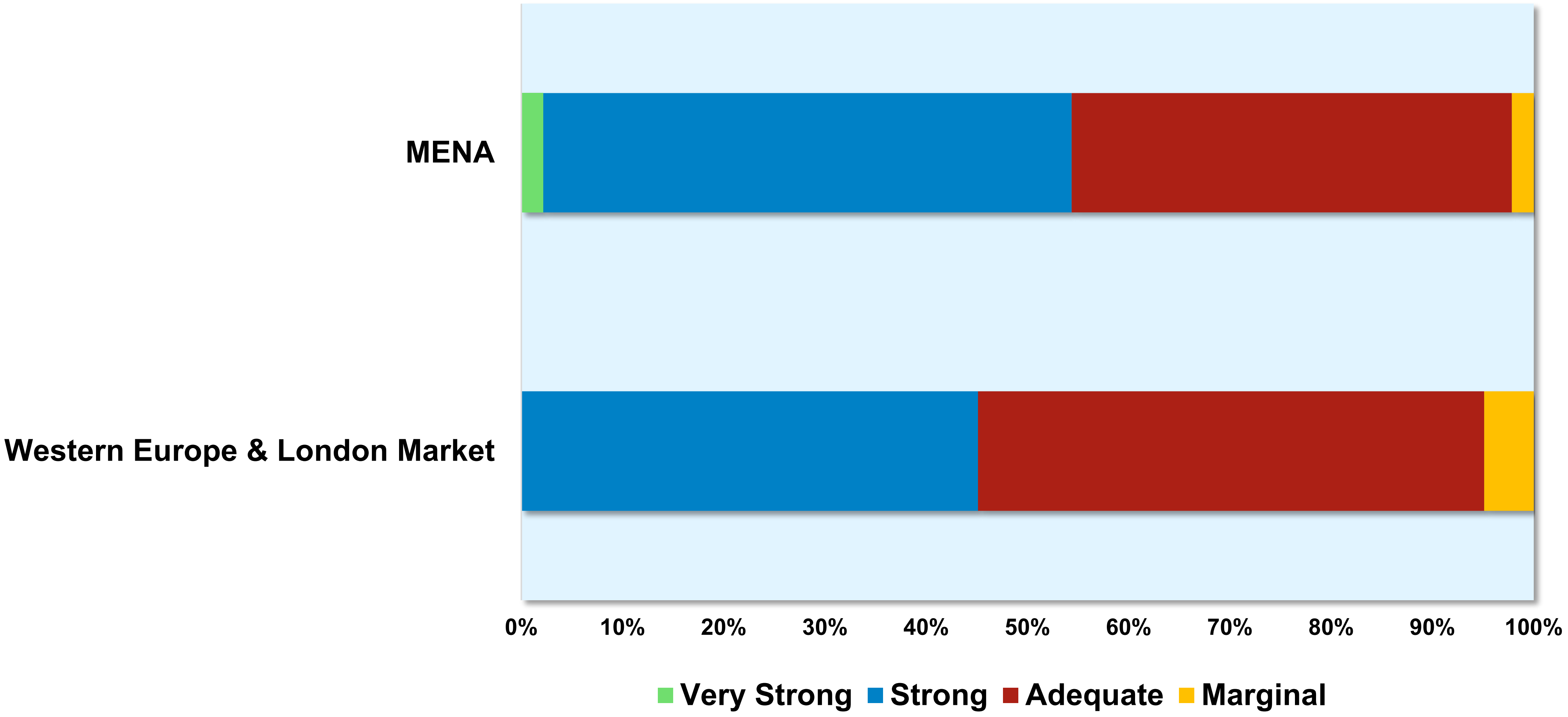
BCAR Assessment \ Balance Sheet Strength	Strongest	Very Strong	Strong	Adequate	Weak	Very Weak
Strongest		65	20			
Very Strong		2	9			
Strong			2			
Adequate				2		
Weak						
Very Weak						

Other Quantitative & Qualitative Considerations

- Asset quality / diversification
- Stress test
- Asset liability matching
- Liquidity
- Reserve adequacy
- Reinsurance quality / appropriateness / dependence
- Fungibility of capital
- Internal capital model

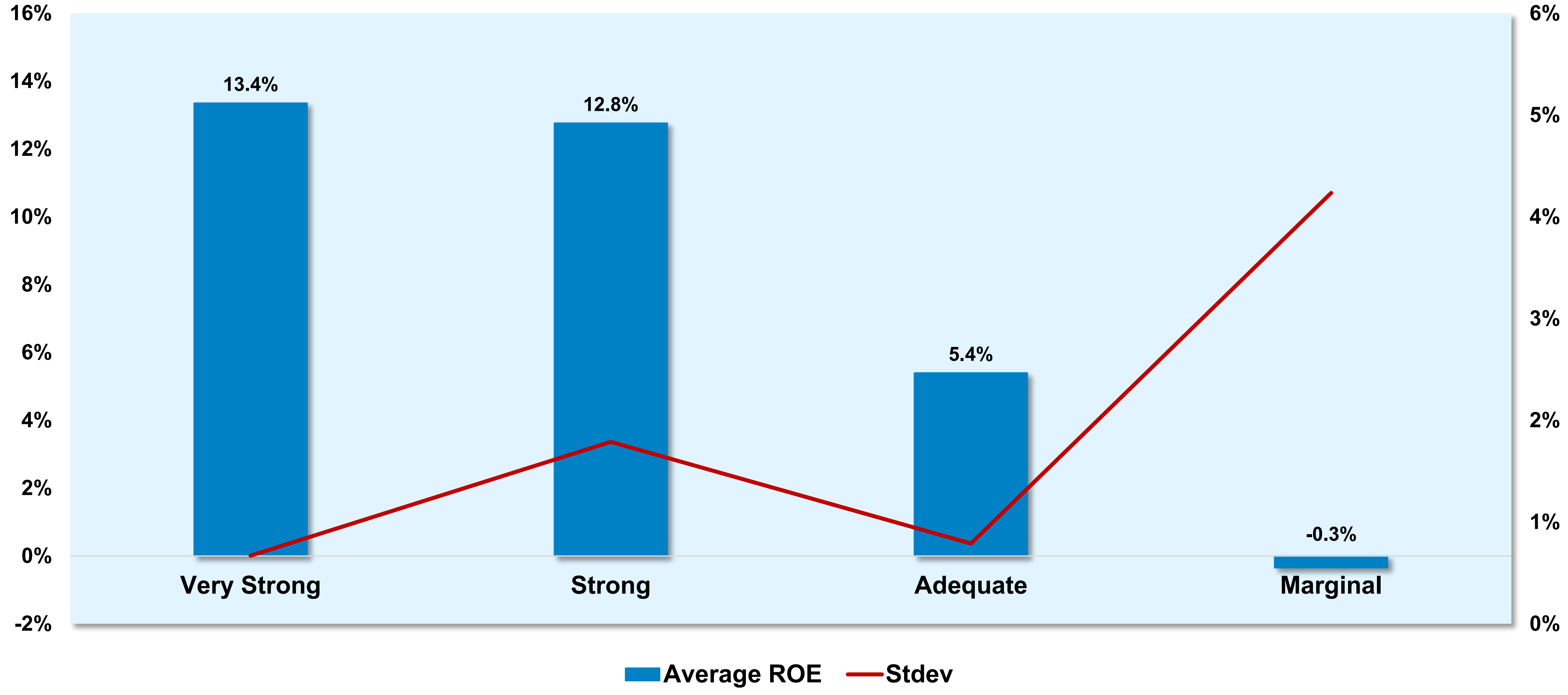
Source: AM Best data and research
Data as of September 2023

Operating Performance - Distribution of Assessments (%)



Source: AM Best data and research
Data as of September 2023

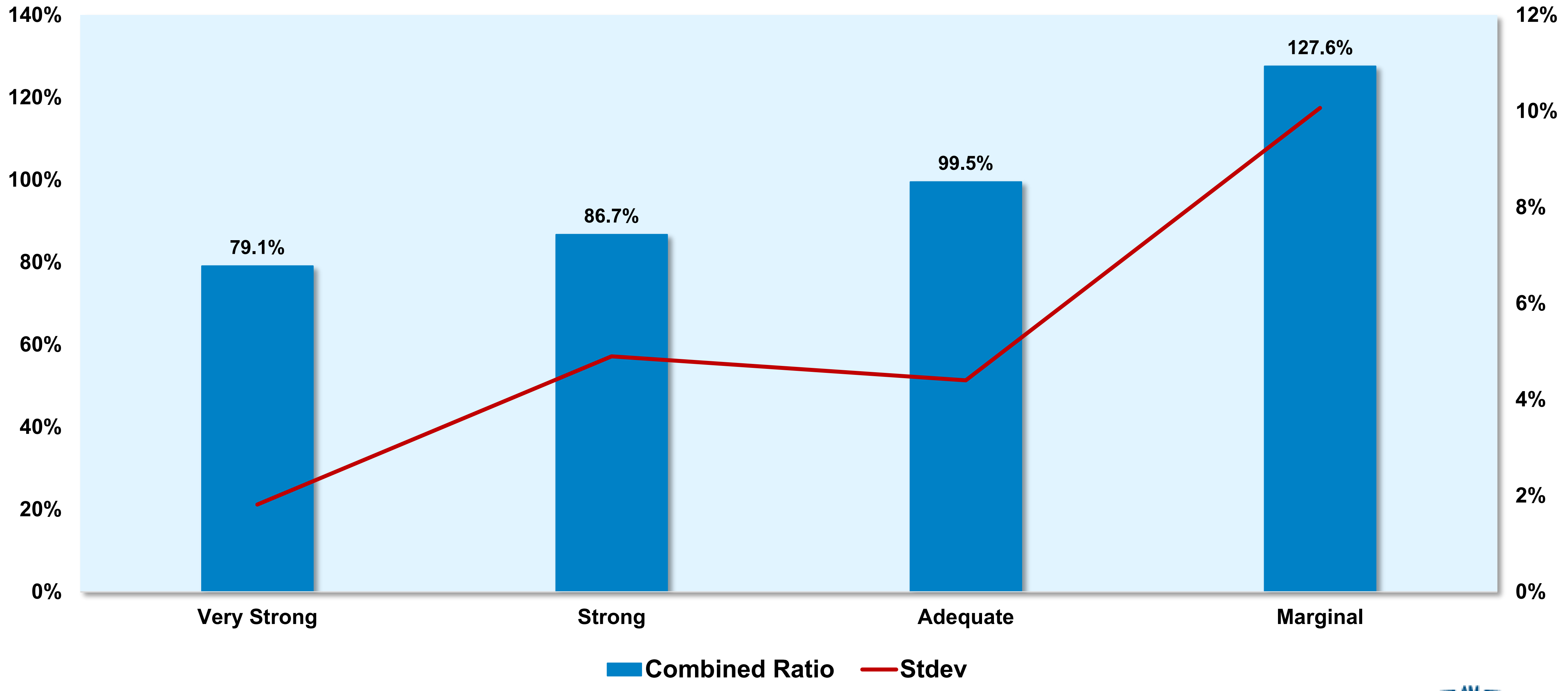
MENA Operating Performance – Five-Year (2018-2022) Average Return on Equity



Our Insight, Your Advantage™

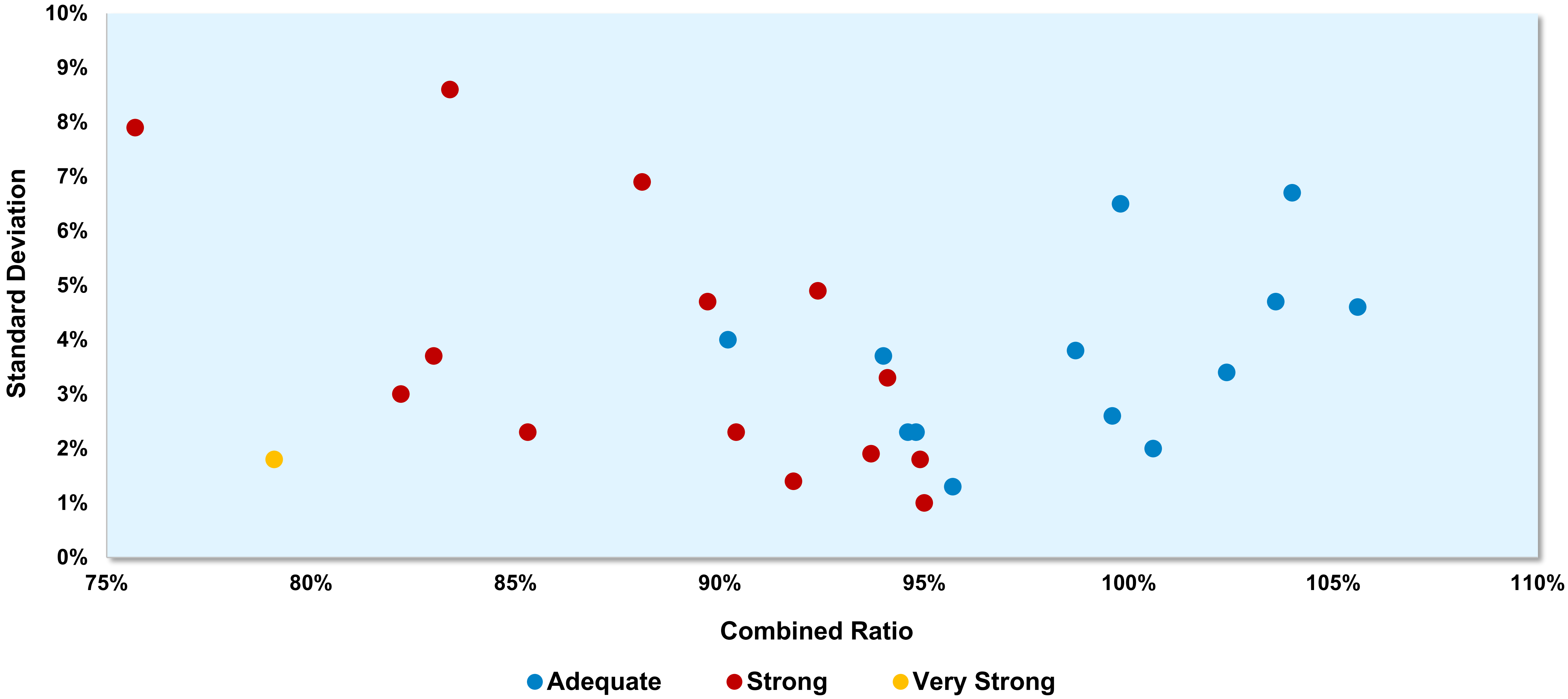
Source: AM Best data and research

MENA Operating Performance – Five-Year (2018-2022) Average Combined Ratio



Source: AM Best data and research

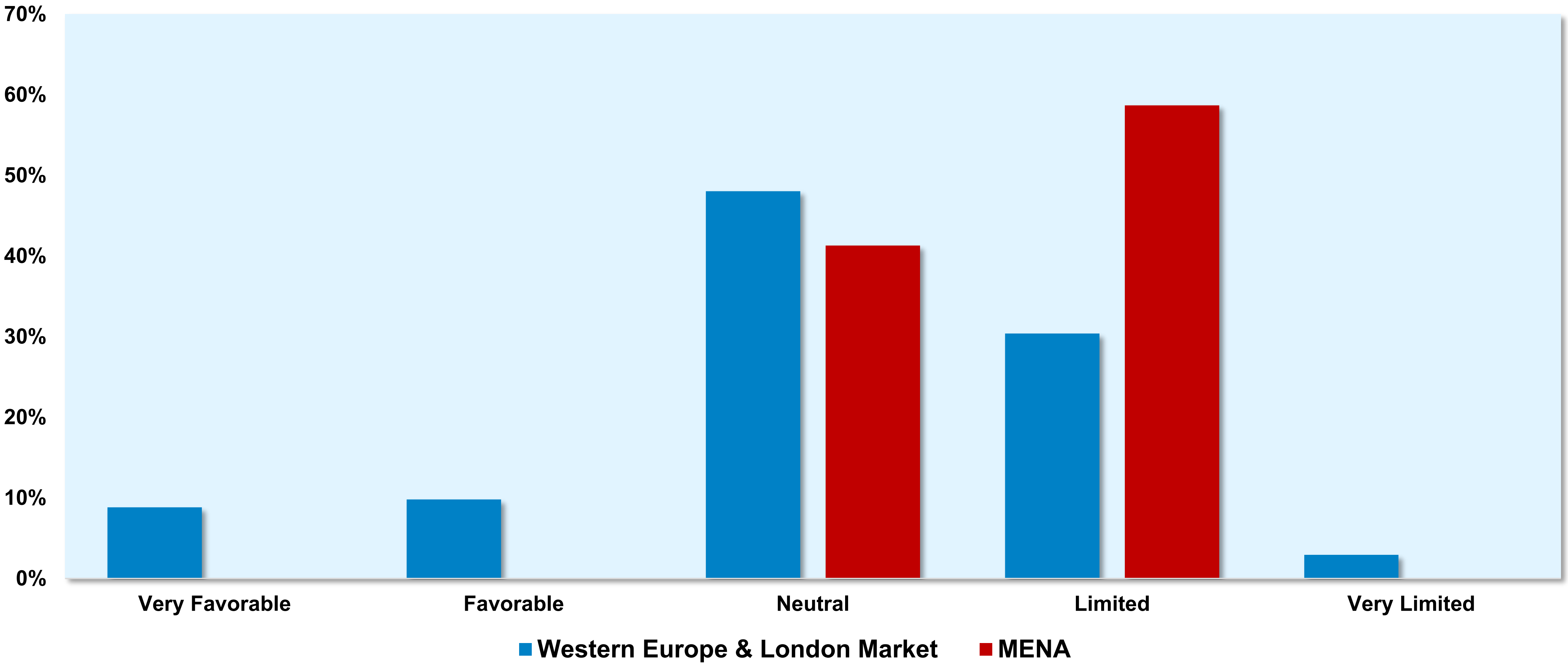
Operating Performance – Five-Year (2018-2022) Combined Ratio vs Standard Deviation



Our Insight, Your Advantage™

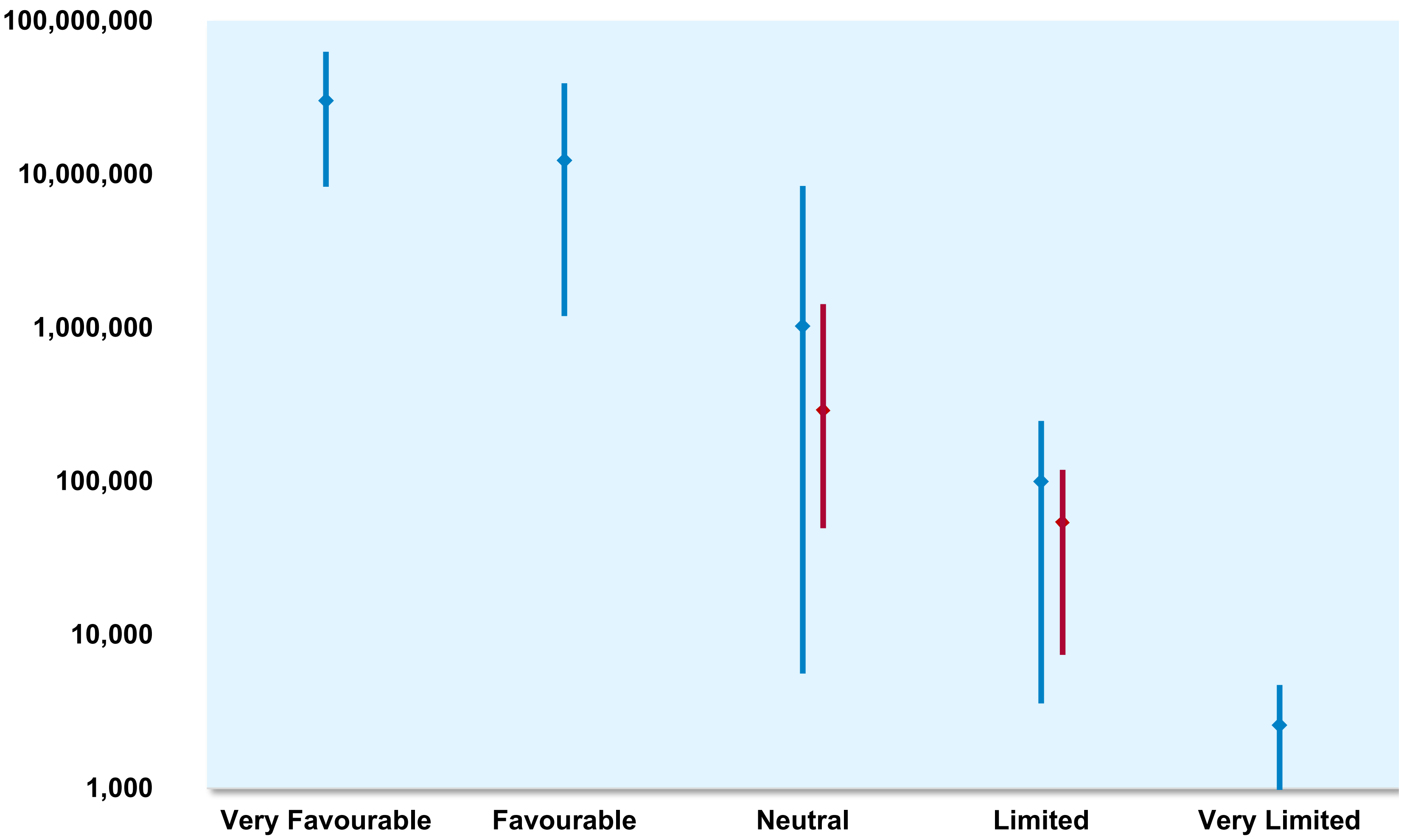
Source: AM Best data and research

Business Profile - Distribution of Assessments (%)



Source: AM Best data and research
Data as of September 2023

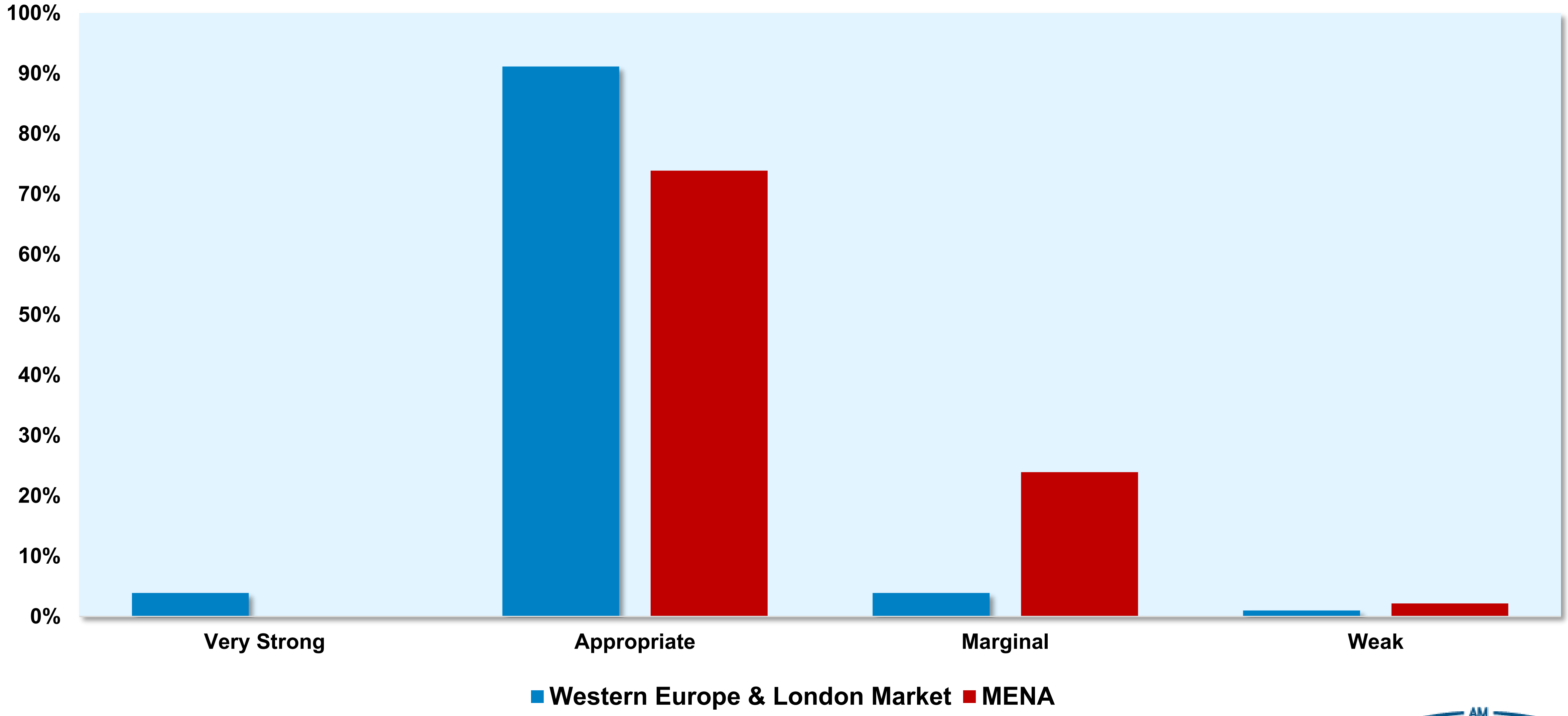
Business Profile - Average Net Earned Premium (USD 000)



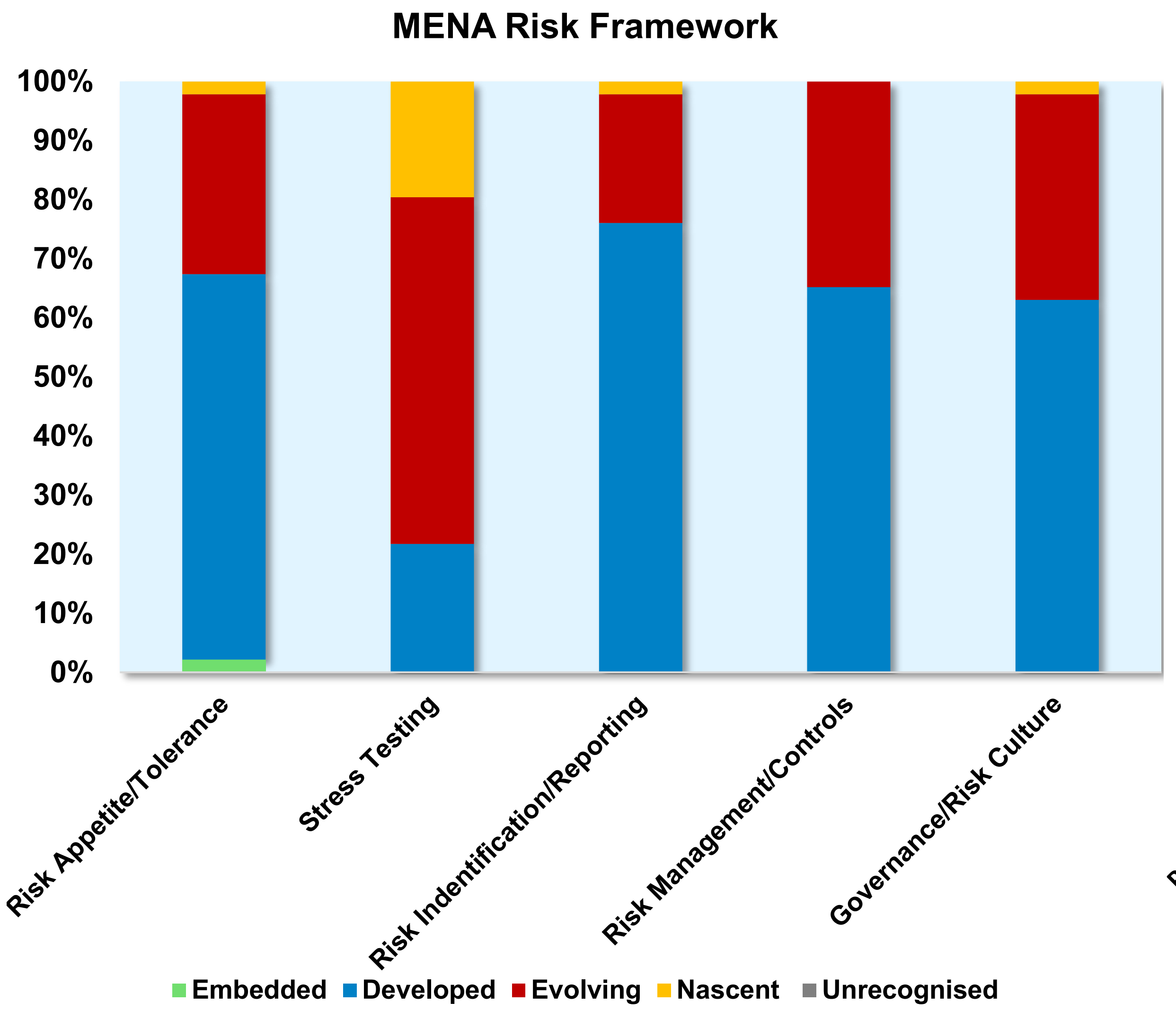
Business Profile Review Components	
Product/Geographic Concentration	Product Risk
Market Position	Degree of Competition
Pricing Sophistication & Data Quality	Management Quality
Regulatory, Event & Market Risks	Distribution Channels
Innovation	

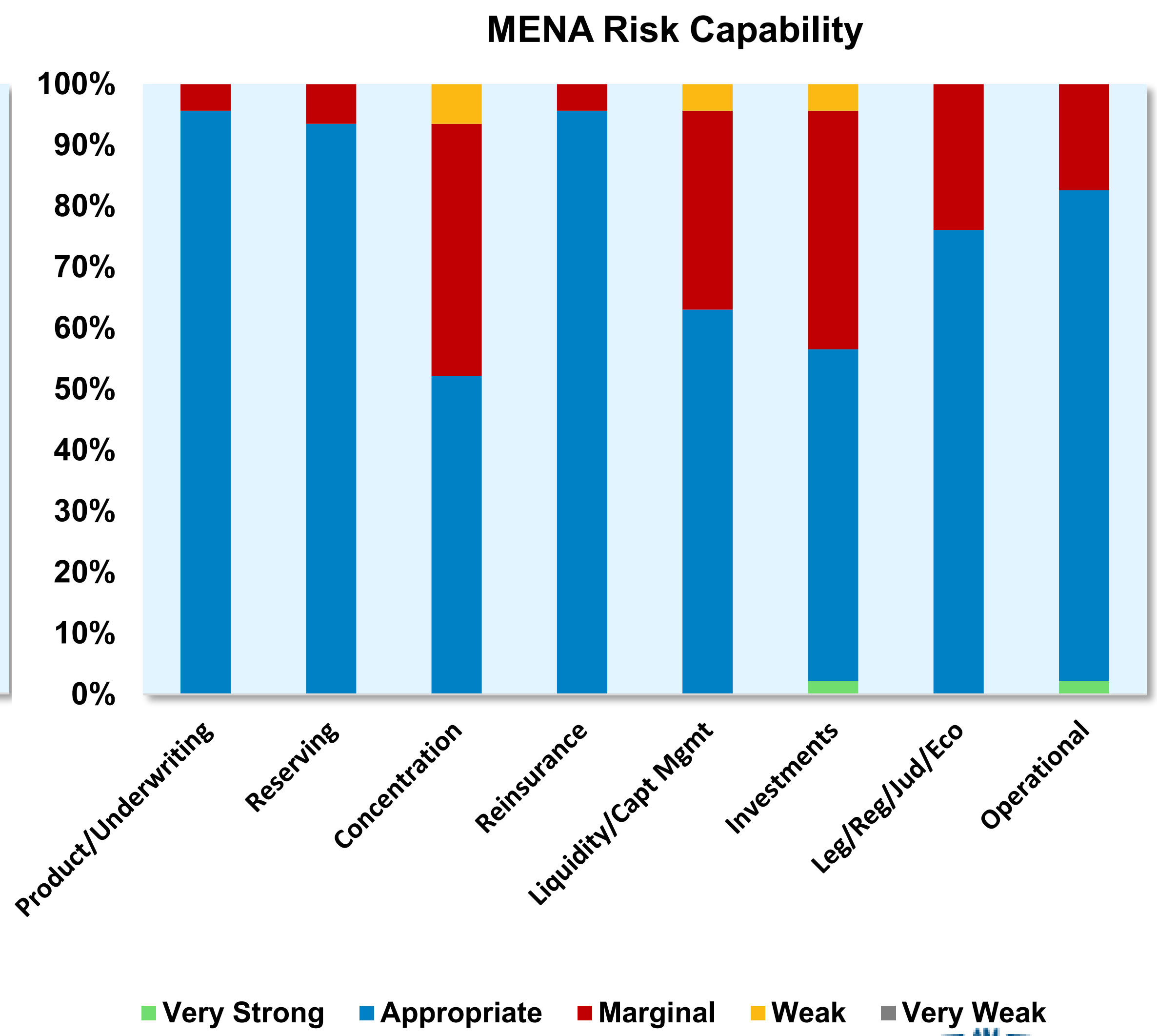
Source: AM Best data and research
Data as of year-end 2022

Enterprise Risk Management - Distribution of Assessments (%)



Enterprise Risk Management - Distribution of Risk Framework and Risk Capability Assessments (%)





Our Insight, Your Advantage™

Source: AM Best data and research
Data as of September 2023

IFRS 17 – Readiness, Impact on Ratings

IFRS 17 – Market Preparedness and Impact on Ratings

- Expect deadlines will be met in larger MENA markets. **What if companies fail to apply the standard?**
  - Potential red flag regarding the governance of the company in question
- Cost and effort remains significant, as expected
- **Large variability between insurers regarding progress and understanding of standards**
  - Limited communication to the market seems to be because work is ongoing, and the subject matter is difficult
- Variations in presentation of accounts **not expected to impact credit fundamentals**
- **Accounts may lead to new insights**, **however**:
  - A new model will help draw out insights from other models
  - There will also be new surprises and sensitivities to learn about

Benchmarking MENA Ratings

Ben Diaz Clegg
Senior Financial Analyst, Analytics

Q&A

Agenda – Insurance Market Briefing

09:15 **Welcome and Introductory Comments**
Nick Charteris-Black, Managing Director, Market Development – EMEA

09:20 **Global Reinsurance Market Update**
Greg Carter, Managing Director, Analytics – EMEA & AP

09:50 **Benchmarking MENA Ratings**
Ben Diaz-Clegg, Senior Financial Analyst, Analytics

10:20

10:50 **Dealing with the Permacrisis/Polycrisis**
Mahesh Mistry, Senior Director, Head of Analytics – London

11:25 **M&A in the GCC insurance Market – A Changing Landscape?**
Vasilis Katsipis, General Manager, MENA, South and Central Asia

12:00 **Q&A**

12:30 **Networking Lunch**

Dealing with the Permacrisis/Polycrisis

Mahesh Mistry, Senior Director,
Head of Analytics - London

Polycrisis and Permacrisis

Polycrisis

The simultaneous occurrence of several catastrophic events

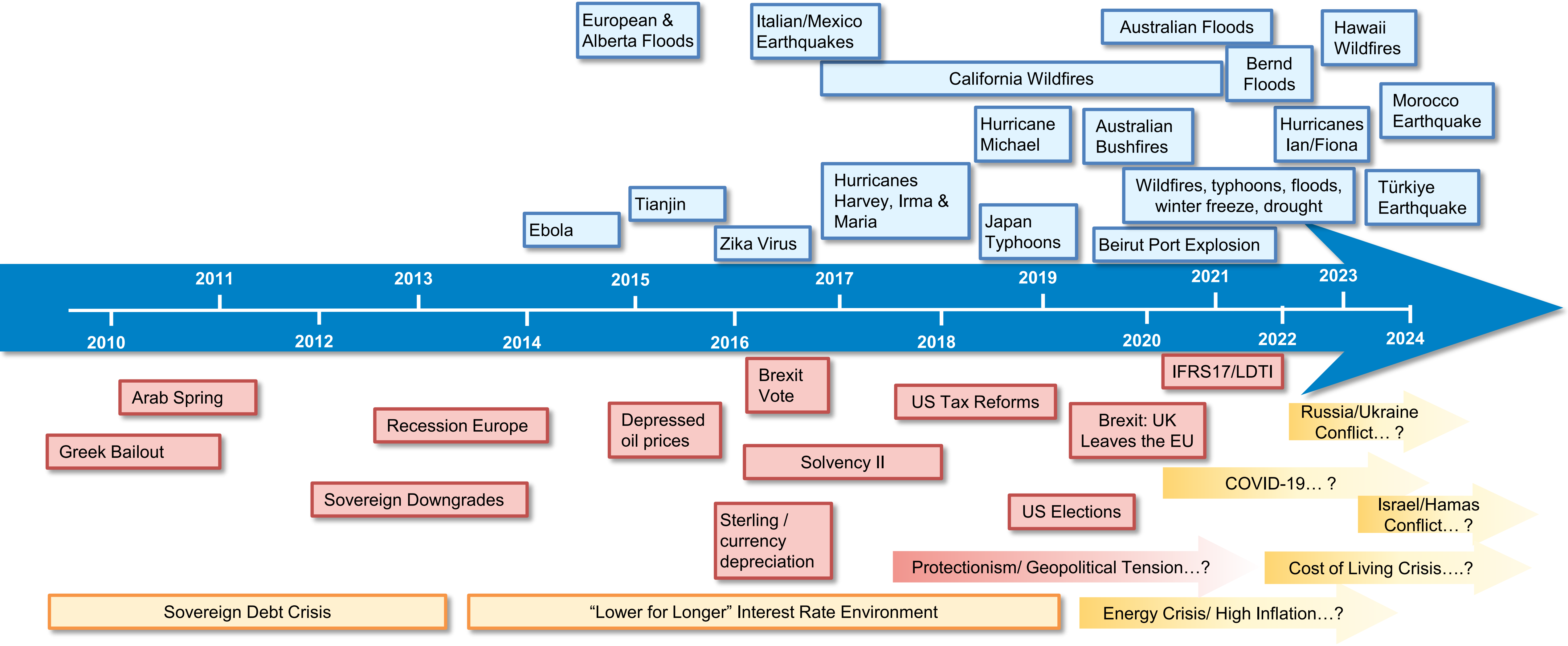
- Stems from climate, political, geopolitical and economic forces
- Where disparate crises interact – such that the overall impact far exceeds the sum of each part

Permacrisis
(Collins Dictionary Word of the Year 2022)

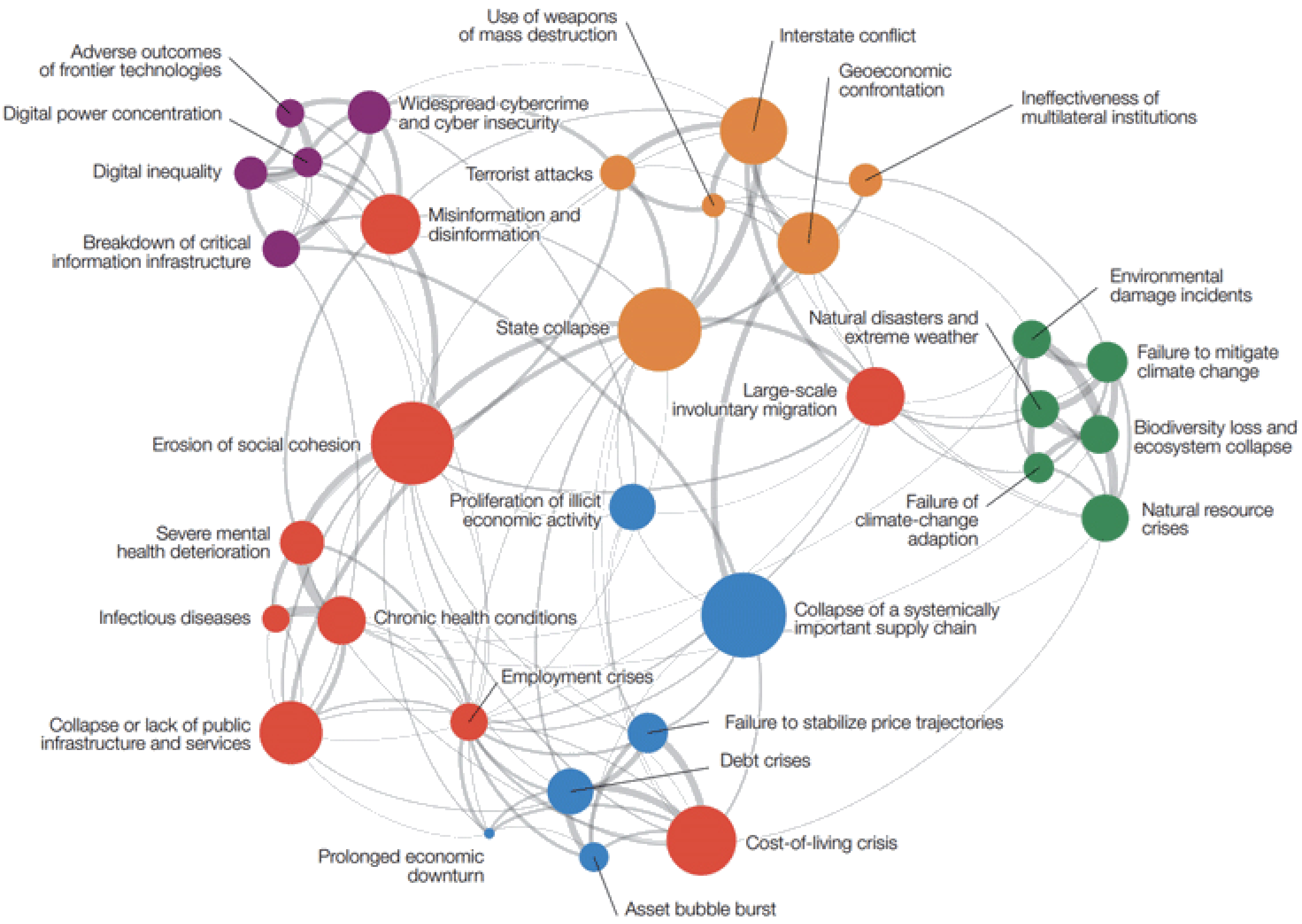
An extended period of instability and insecurity, especially one resulting from a series of catastrophic events

- A static and permanently difficult situation
- Outcome cannot be predicted
- Can only be managed – not resolved

Market Events Help To Shape ERM Developments



Interconnectivity of Risks



Market Environment –

Increasingly interconnected between risk categories, with a higher degree of contagion

- Economic
- Environmental
- Geopolitical
- Societal
- Technological

Source: World Economic Forum - Global Risks Report 2023

Risks Permeate Through Insurance Sector

Pandemic

- Supply Chain Disruption
- Government support packages
- Court Cases – T&Cs
- Economic Slowdown
- Longer term health concerns
- Globalisation – speed of response
- BI Claims
- Loss of Lives – mortality experience

Regional Conflict

- Political risks, aviation, marine
- Added Volatility and Instability
- Clarity in T&Cs
- Inflation
- Geopolitical tensions
- Asset Write-downs
- Economic Slowdown
- Cost of Living Crisis

Change in Risk Priorities

Uncertainties Tied to Climate Risk, Geopolitical Risks, Inflation, Rising Cyber Exposure, Changing Regulation

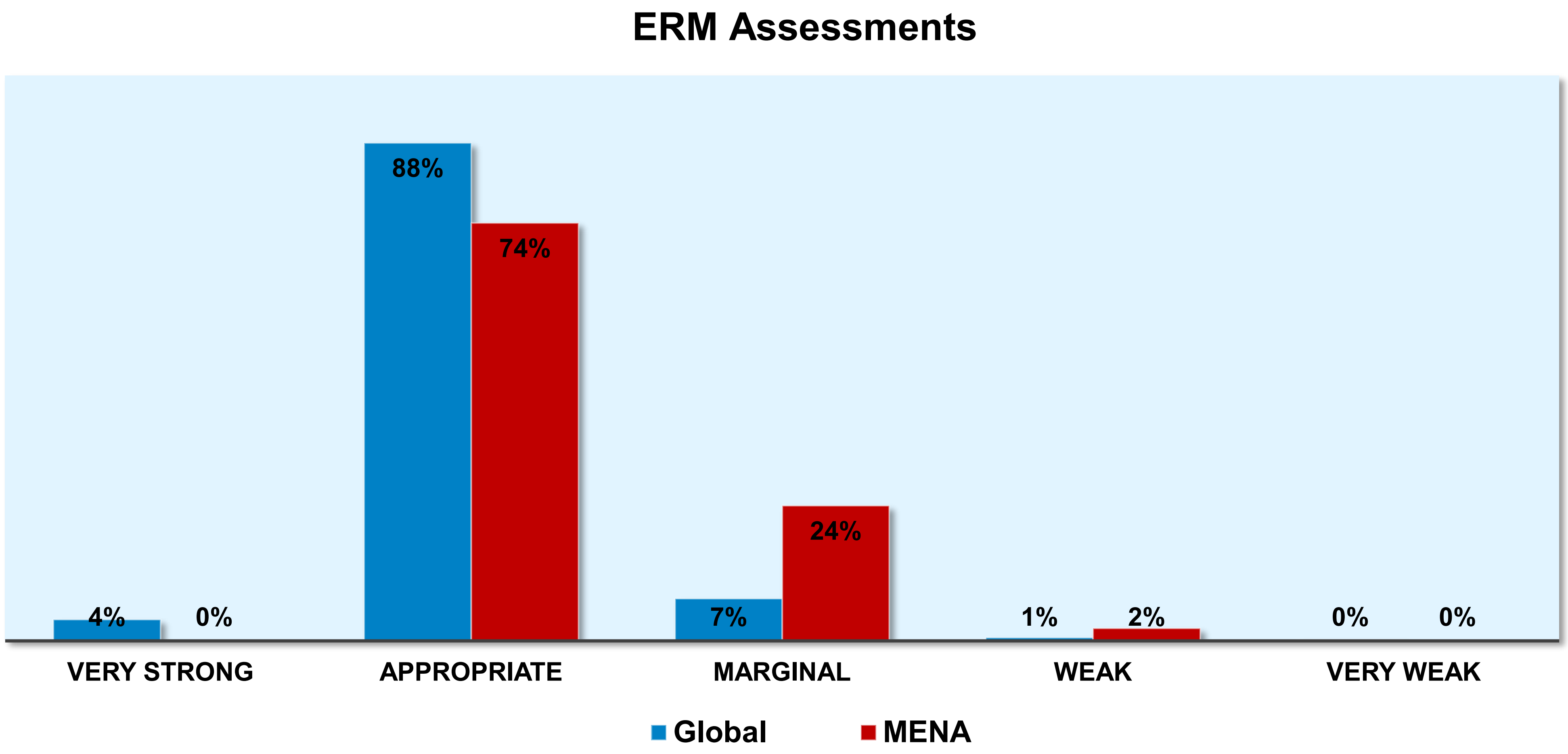
2014	2018	2022	2023
BI - Supply Chain Disruptions	BI - Supply Chain Disruptions	Cyber	Cyber
Natural Catastrophes	Cyber	BI - Supply Chain Disruptions	BI - Supply Chain Disruptions
Fire, Explosion	Natural Catastrophes	Natural Catastrophes	Macroeconomic Developments
Changes in Regulation and Legislation	Market Developments	Pandemic Outbreak	Energy Crisis
Market Stagnation or Decline	Changes in Regulation and Legislation	Changes in Regulation and Legislation	Changes in Regulation and Legislation
Loss of Reputation and Brand Value	Fire, Explosion	Climate Change	Natural Catastrophes
Intensified Competition	New Technologies	Fire, Explosion	Climate Change
Cyber	Loss of Reputation and Brand Value	Market Developments	Shortage of Skilled Workforce
Theft, fraud corruption	Political Risks and Violence	Shortage of Skilled Workforce	Fire, Explosion
Quality deficiencies / defects	Climate Change	Macroeconomic Developments	Political Risk and Violence

Source: Allianz Risk Barometer reports

Dealing with the Polycrisis / Permacrisis – Risk Management is Key

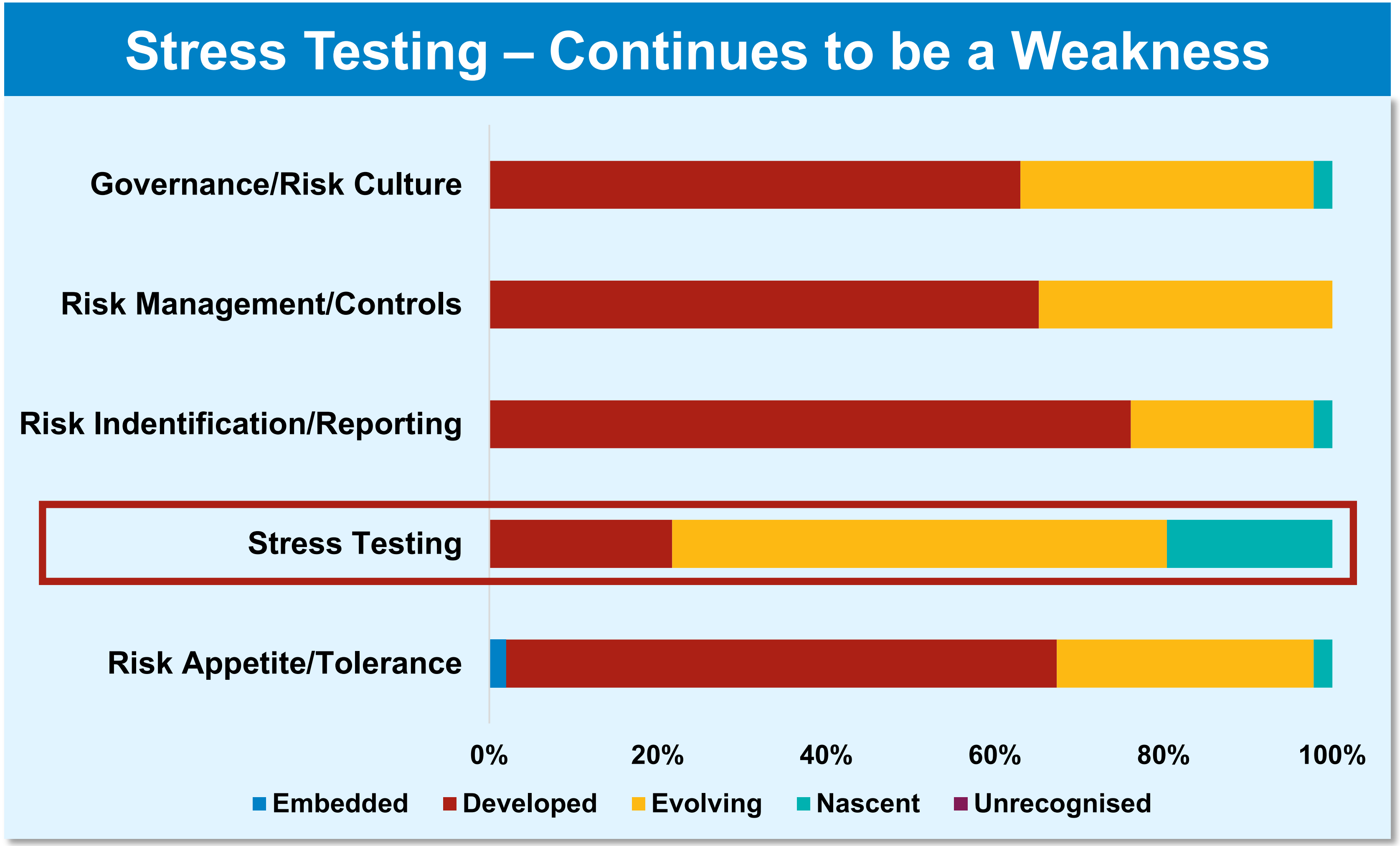
Impact on Ratings	Balance Sheet Strength	Operating Performance	Business Profile	Parent Companies (Lift / Drag)
Ratings generally resilient	Resilient balance sheets	Greater volatility in underwriting and investments performance	Larger, diversified companies have shown more resilience	Impact on parent companies in other sectors can be varied
More downward pressure	Gradual erosion of BCAR, though remaining within 'Strongest' category	Events hampered ROEs – returns below expectation	Concentrated, single market, single product players seen more impact	
Impact more acute for concentrated, single market or single product (re)insurers	Impact more acute for concentrated, single market or product (re)insurers	Focus on improving stability of returns – higher margin business	Focus on reshaping portfolio and exposures	
Larger, diversified companies have fared better	Focus on Capital Management	Inflation - reserving and pricing trends		
	Access to capital markets			

AM Best-Rated Insurers Show Resilience to Events



Source: AM Best data and research

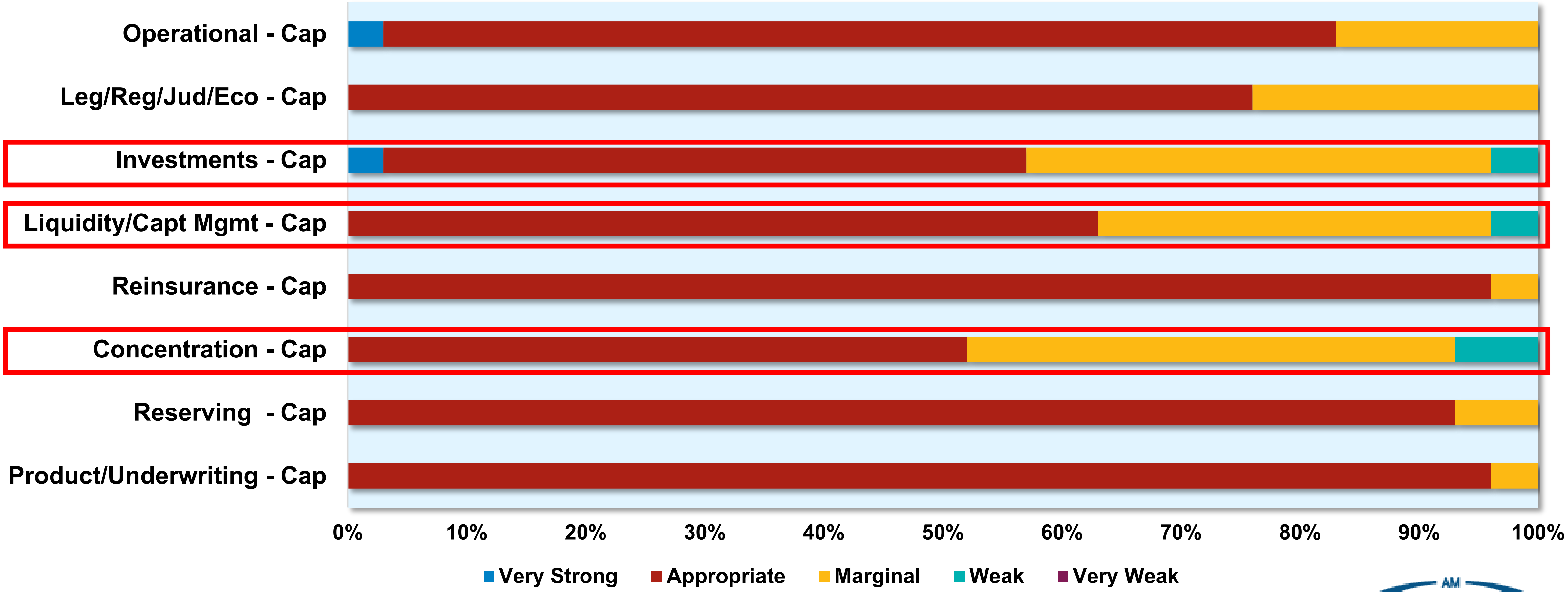
AM Best's ERM Assessment – MENA Risk Framework Evaluation



Source: AM Best data and research

AM Best's ERM Assessment – MENA Risk Profile Evaluation

Liquidity/Capital Management Generally Strong – Concentration is a Key Risk



Source: AM Best data and research

Market Response – Exposure Management & Stress Testing

Risk Appetite / Tolerance

Risk appetite and tolerance generally within expectation. Events absorbed by the market. In some instances, some small, concentrated companies have been over exposed

Exposures

Redefining T&Cs, exclusions, single event and accumulation limits, attachment points

Modelling & Stress Testing

Stress testing different perils (nat cats, climate, cyber, casualty cats, pandemic, SRCC, secondary perils) – models coming under greater scrutiny

Risk Transfer

Review of broader risk transfer mechanisms to manage risk

Correlation & Accumulation

Focus on correlation and accumulation management

Regulation

Mandated regulatory resilience tests (nat cat, cyber, pandemic)

Market Environment

Changes – Insurer vs. Reinsurer market dynamics

Reverse Stress Testing

Considering events/scenarios that could be a detriment to the company and its associated tail risk

Inflation

Constantly reviewed and actively managed – impact on reserving and pricing

Market Response

Risk Sharing

Public Private Partnerships (PPP)

- Not a new concept, but in the limelight again
- Pools acting as direct, co- or re-insurers, with governments as buyers or guarantors
- Often legislation required – mandatory covers, opt-in / opt-out clauses
- NatCat (such as Morrocco, Turkey), Flood, Terrorism
- Cost of insurance v willingness-to-pay

ILS Markets

- Risks are being dissected and shared with different parties

Capital Management & Performance

Balance Sheets Generally Remain Strong – Operating Performance Generally Below Expectations

- Marginal cost of capital rising; ROE expectations rise
- Access to new capital has been difficult for new insurers, but existing players have good financial flexibility
- Rising inflation and interest rates also led to losses on insurers' fixed income holdings
- Inflation has had an impact on reserving and pricing, operating costs
- Larger balance sheets needed to absorb more risk; reinsurance dependence remains high
- Evidence of capital support from shareholders appears muted in the region

Market Response – Macro-economic

Macro-Economic

Companies Generally in a Strong Position Going into the most Recent Financial Crisis

- Lessons learnt from previous financial crises
- Continued regulatory and tax reforms
- Inflation – rising since Spring 2021 for most economies
- Interest rates – steep increase during 2022
- Volatile energy prices
- Labour shortages – qualified professionals

Geopolitical Changes

Cost of Doing Business Continues to Rise

- Tensions elevated in the region
- Political trends navigate towards nationalism, introducing fragmentation and trade barriers
- Local regulators introducing new rules and closer monitoring of (re)insurers
- Market players are thinking carefully how to adjust expansion or development strategies into markets with high growth potential, but also high potential to political or regulatory reforms

Challenges Ahead

- Climate Risk
- Cyber Risk
- SRCC
- Litigation
- Regulatory Risk
- Digitalisation: AI

Frequency and Severity of Events –

Likely to increase

Macro-Economic Environment –

Remains uncertain and volatile

Key Takeaways

Uncertainty Remains –

In regards to the end
of the Poly- and Permacrisis environment

Strong Balance Sheets –

Needed to cope with heightened cost of doing business and absorbing unforeseen events

Insurance Industry has Shown Resilience to Market Events –

Effective and adaptable ERM remains key to manage unknown events

Uncertainty and Volatility Also –

Create opportunities

Dealing with the Permacrisis/Polycrisis

Mahesh Mistry, Senior Director,
Head of Analytics – London

Q&A

M&A in the GCC insurance Market – A Changing Landscape?

Vasilis Katsipis
General Manager, MENA, South and Central Asia

Agenda

The Market

M&A to Date

Forces Impacting M&A in the Future

Conclusion

Agenda

The Market

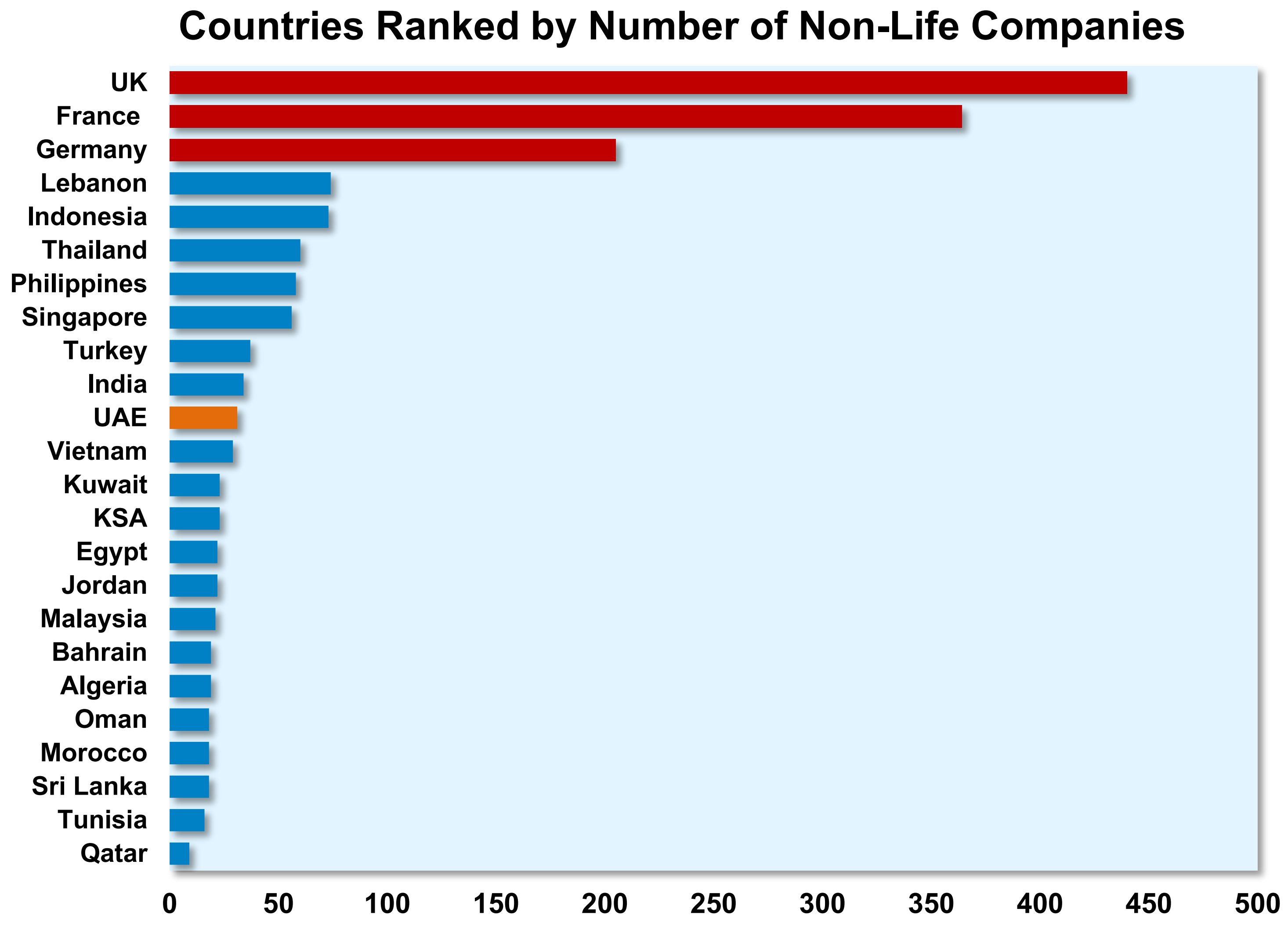
M&A to Date

Forces Impacting M&A in the Future

Conclusion

Our Insight, Your Advantage™

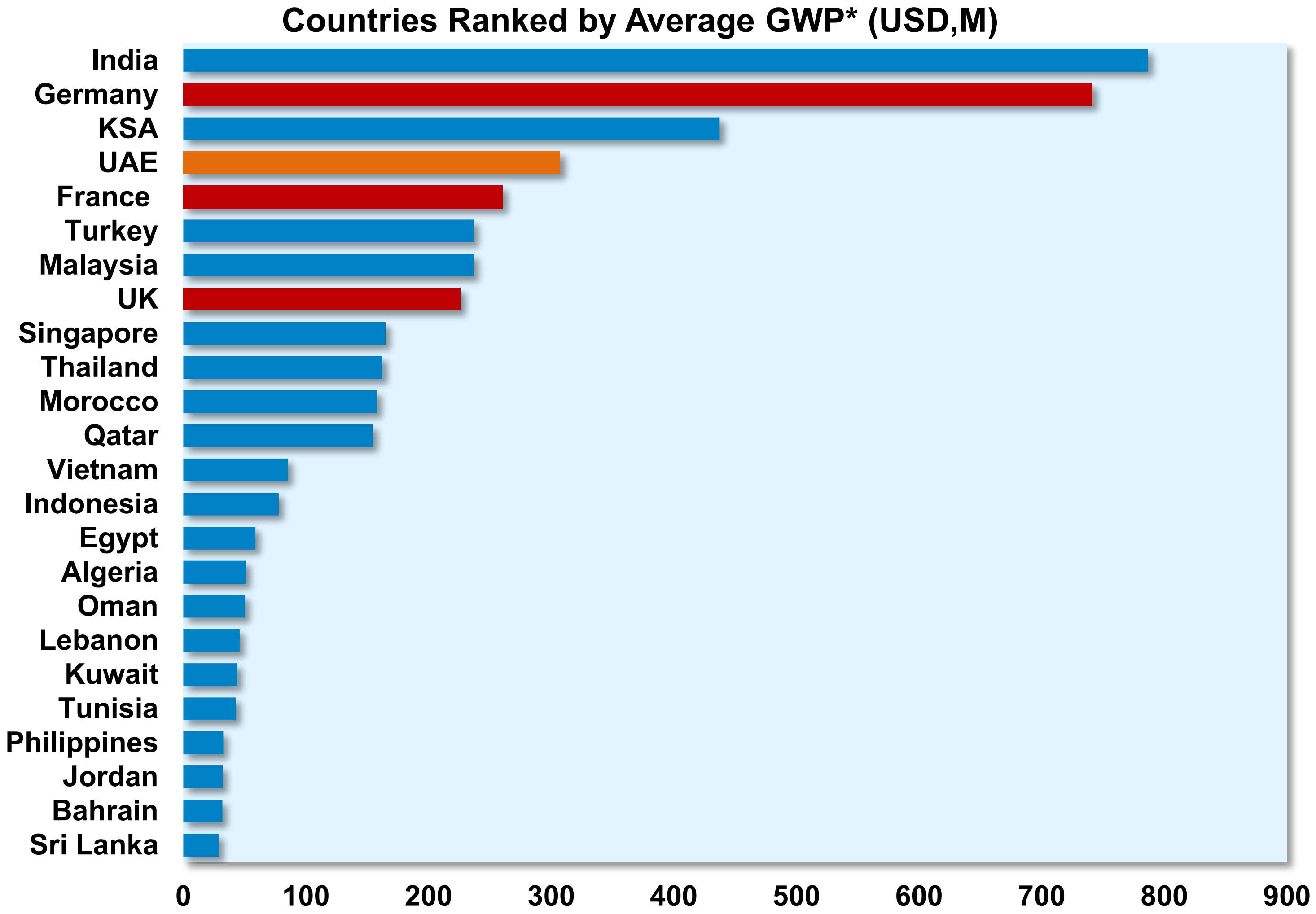
Great Variance Among Insurance Markets



- **Mature markets have far more non-life insurance companies operating**
- **Great variance among emerging markets with regulation, business opportunities, local practices and historical reasons being the main drivers of the number of companies**
- **UAE seems to have relatively high number of non-life insurance companies**
- **Should number of companies be proportional to the size of the insurance market?**

Source: AXCO

Picture is Different When Considering GWP

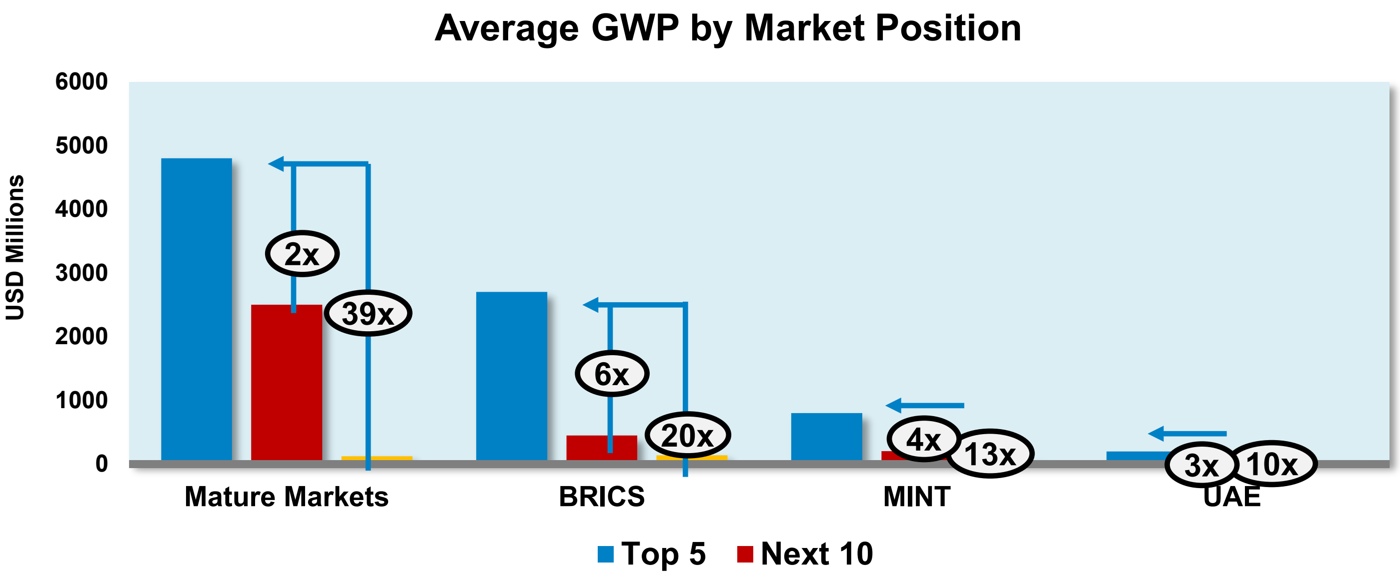


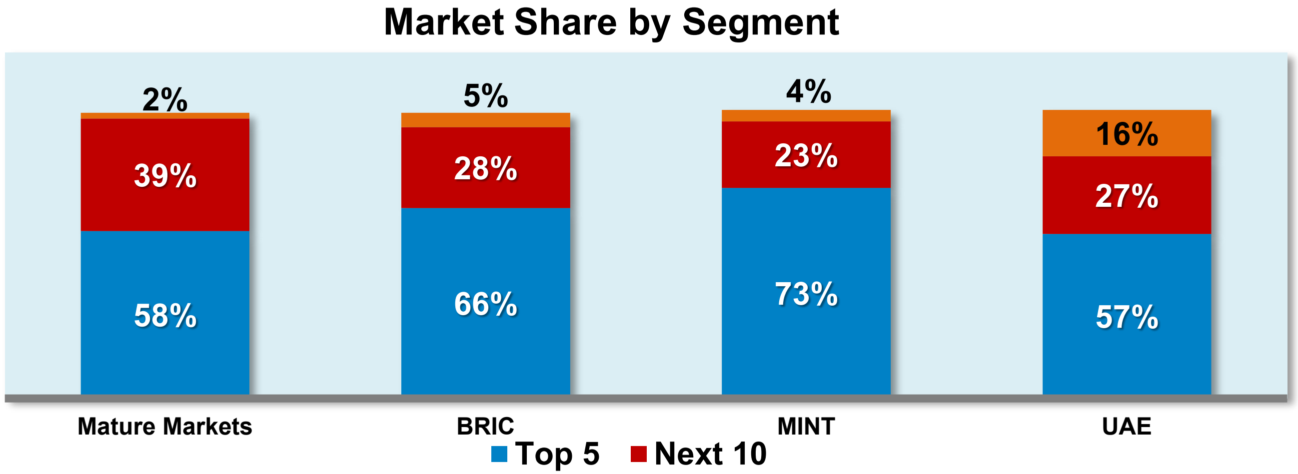
*Average GWP = Total GWP / Number of non-life companies

- Barriers to entry exist in several markets
- Resulting in higher concentration in certain markets
- Mature markets are more competitive than indicated given the existence of a few very large insurers
- On this metric the UAE seems very concentrated – only India and KSA seem to have more barriers to entry

Source: AXCO, Swiss Re Sigma Report

Lack of Specialisation Intensifies Competition in Smaller Markets





- **Relative size of segments varies by market**
- **In emerging markets, the gap between larger and smaller companies is directly related to the size of the market**
- **Competition in smaller emerging markets more intense**
- **UAE has the highest market share among smallest companies**

Source: Best's Financial Suite – Global

Agenda

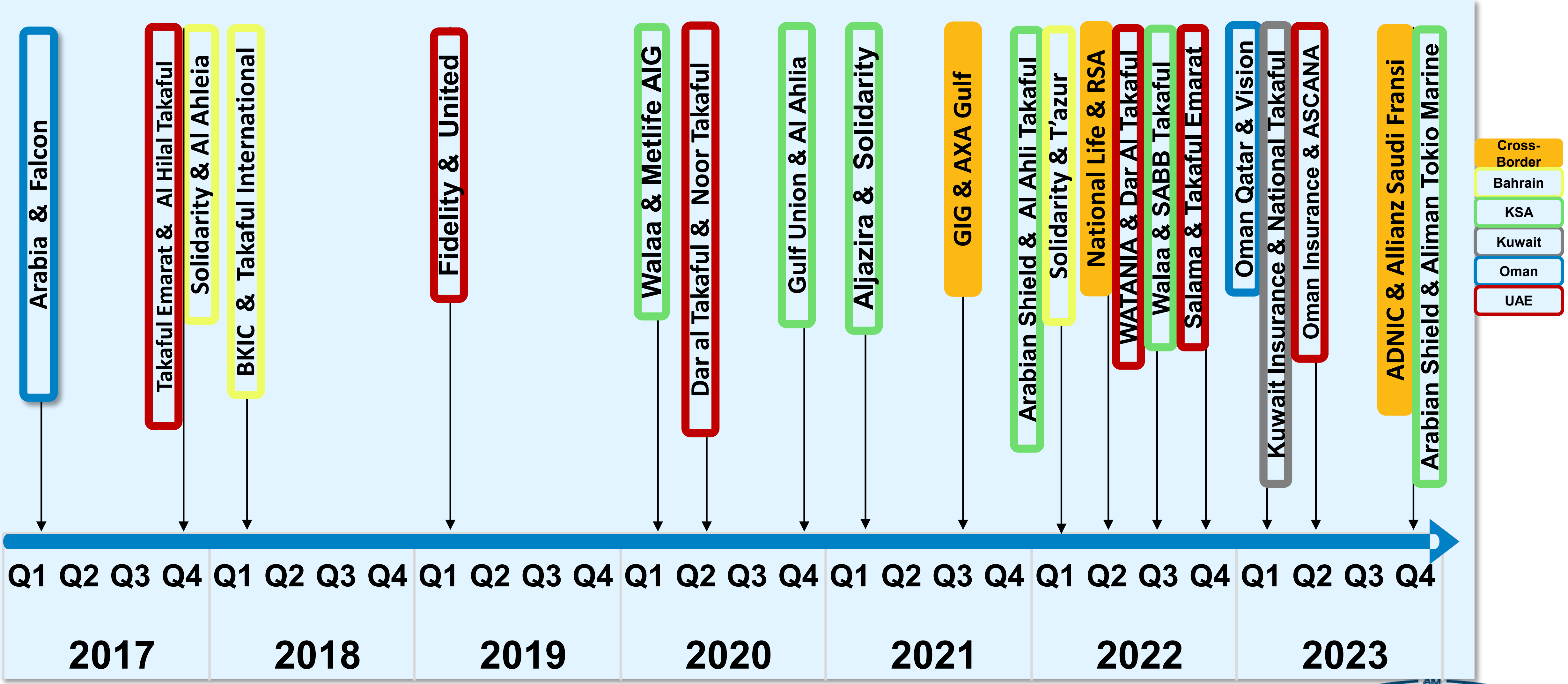
The Market

M&A to Date

Forces Impacting M&A in the Future

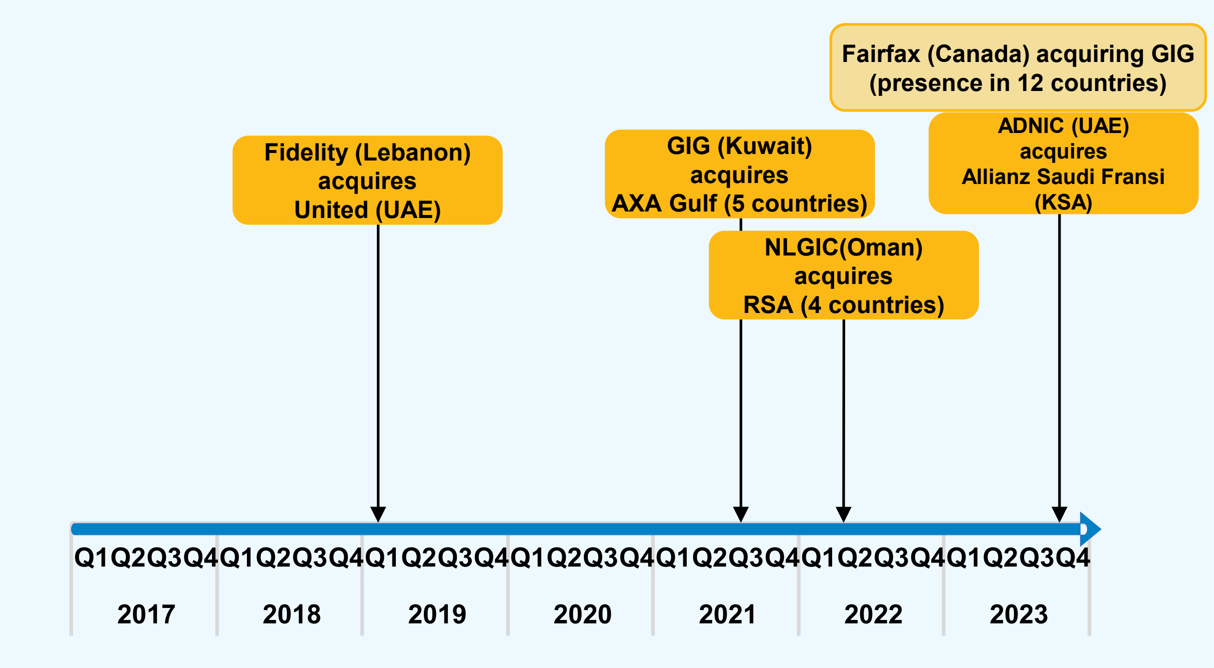
Conclusion

Insurance Company M&A in the GCC (Completed Deals Only)



Sources: Company notifications & Trade Press

Cross-Border Acquisitions



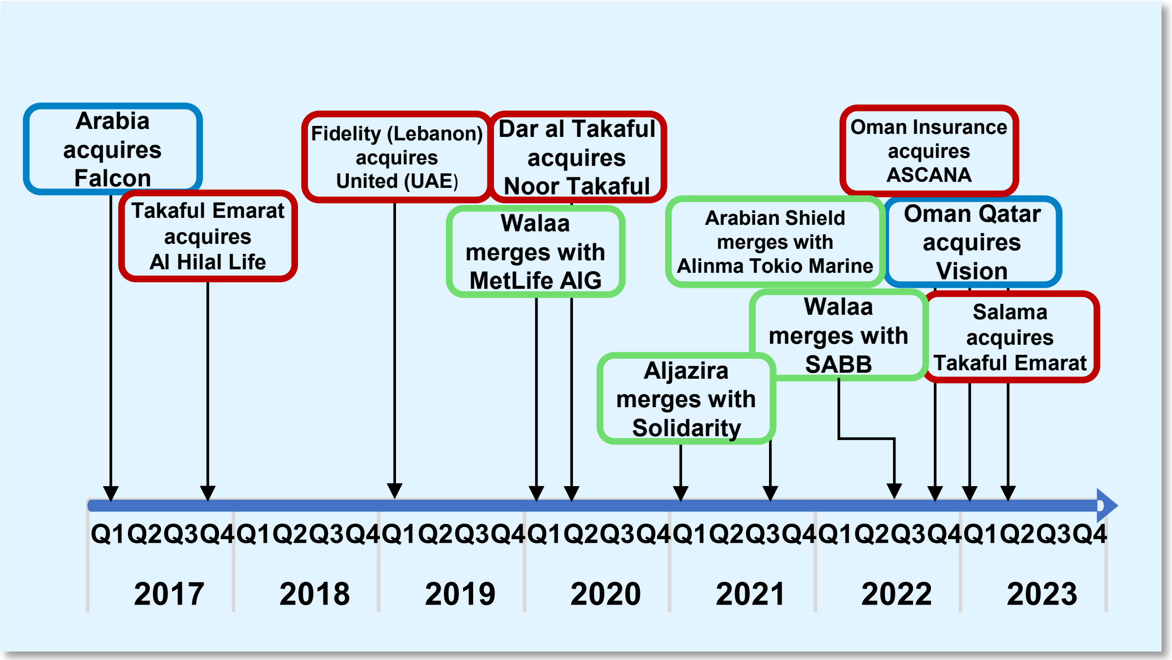
- Not a new phenomenon
- Much of the activity is the result of international insurers selling their local operations
- Acquisition of GIG by Fairfax is the exception

- Most cross-border acquisitions are mainly motivated by access to new markets
- Often not a clear-cut case as acquirer may have a subsidiary with small presence in the target market
- Acquisition prices not always published but recent pricing has been in the range of x9 – x15 of previous year's profits
- Not many buyers but there seems to be significant appetite to pay premium prices for strong operations
- Emergence of first local insurers establishing regional networks

➔ Limited appetite from international players but emergence of new regional insurers

Sources: Company notifications & Trade Press

M&A Driven Mainly by MCR Considerations



- **Only companies failing to meet MCR and moving in “the wrong direction” included in the list**
- **Broader regulatory issues present but meeting the MCR seems to be the headline issue**

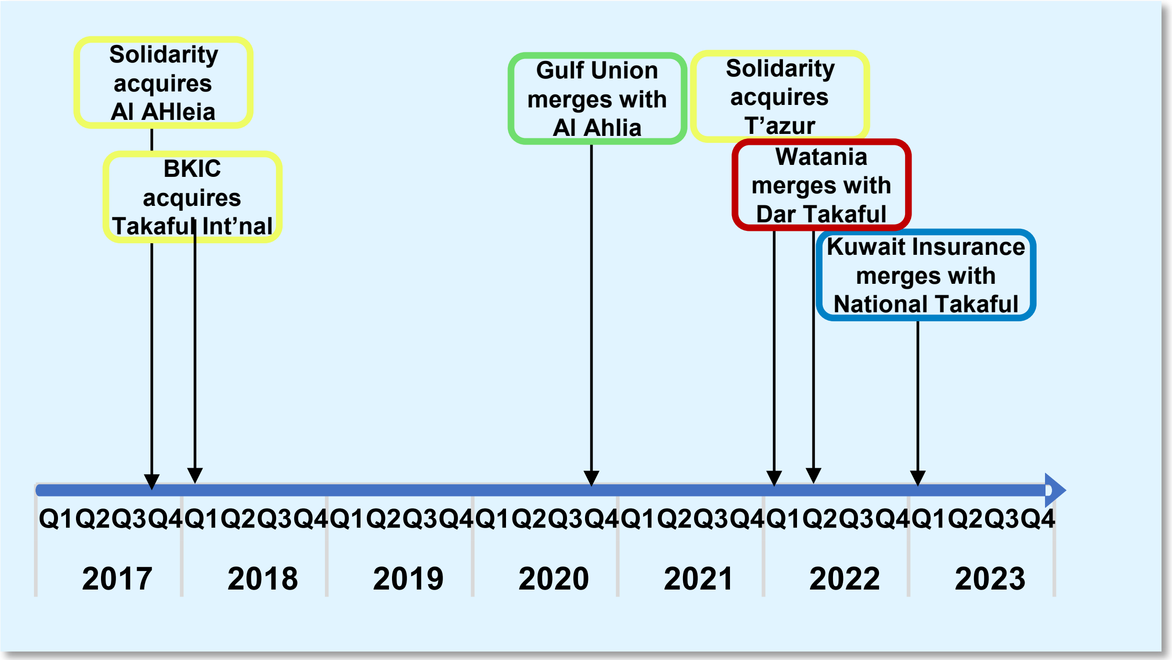
- **Almost half of all M&A activity in the GCC during the last 7 years can be attributed to failing to meet the MCR**
- **More occurrences in the last 4 years**
- **Companies fall below MCR even in markets where the MCR has not been revised**
- **There are still some companies below MCR**
- **In some cases, values paid are high due to the expectation of capital release following the merger**
- **Often these tend to be the cheapest M&A deals in terms of profit multiples**

➔ **There is more M&A activity to come as companies fall below their minimum capital requirements**

➔ **Timing is dependent on pressure applied by the regulators**

Sources: Company notifications & Trade Press

M&A Driven by Other Reasons



- **M&A activity that is not motivated by urgent capital requirements or international expansion**

- **Increased activity in last 3 years**
- **Often driven by expansion of companies within their own market**
- **Certain companies seem to have M&A as part of their expansion plans**
- **Acquired targets tend to be reasonably performing entities before the acquisition**
- **Access to new segments (e.g. Takaful for a traditional insurer) and economies of scale some of the key motivating factors**

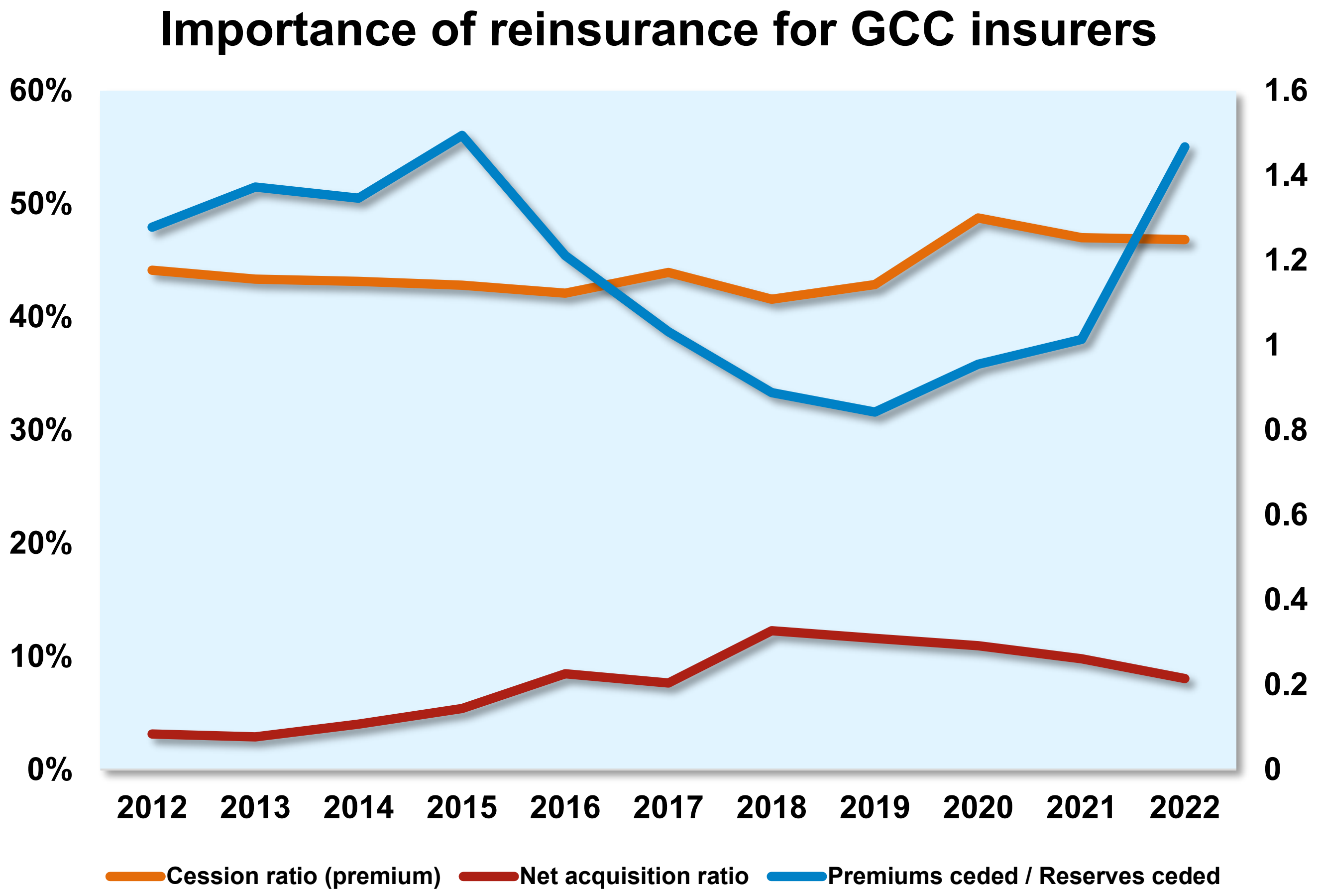
➔ **Possibility for accelerated activity as more companies refine their strategies of market access and seek to obtain greater economies of scale**

Sources: Company notifications & Trade Press

Agenda

- The Market
- M&A to Date
- **Forces Impacting M&A in the Future**
- Conclusion

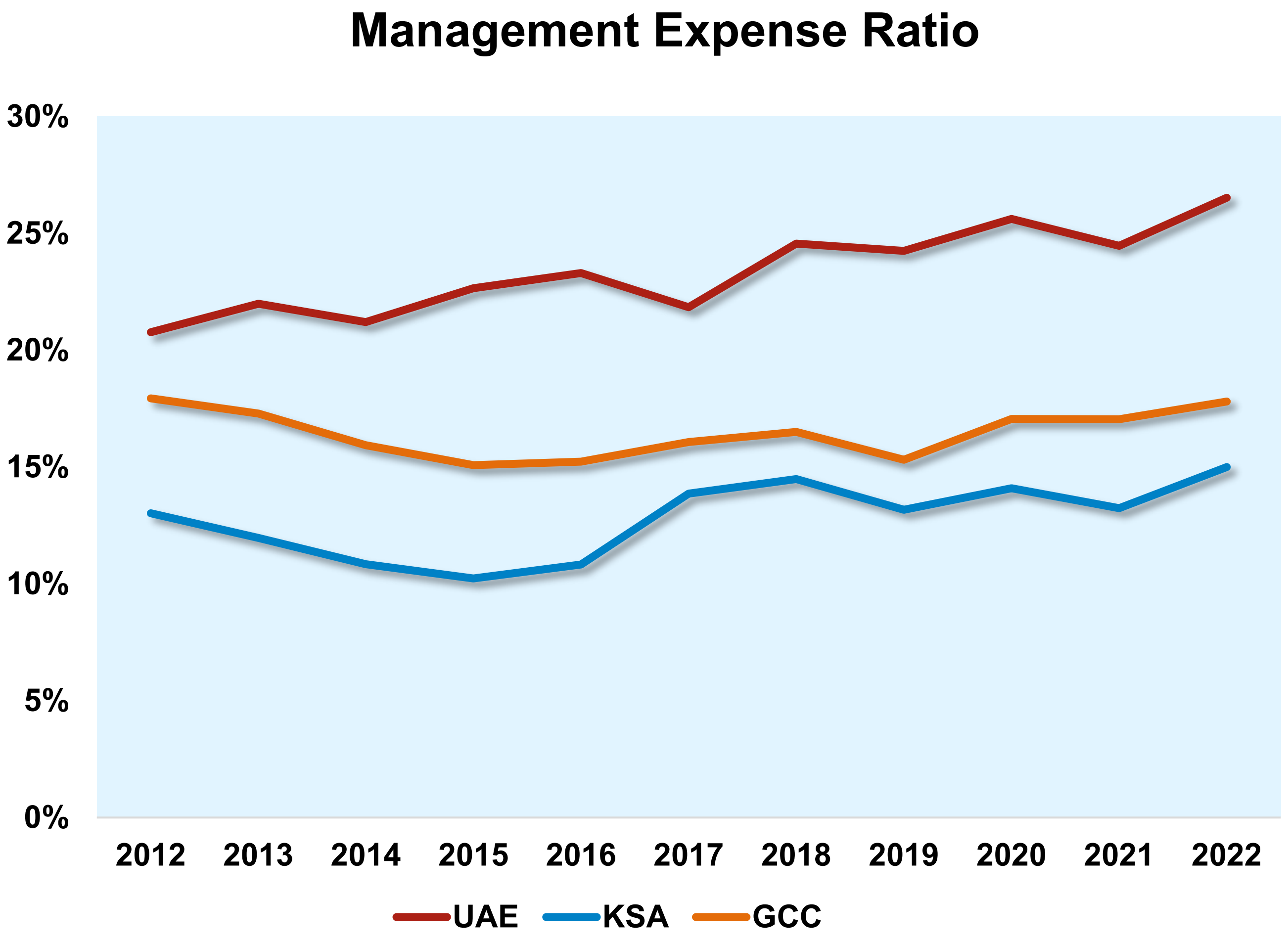
Reinsurance is Critical to GCC Insurers, It Gets More Expensive



- **Cession ratios remain very high, companies cede around 50% of their premiums**
- **High reinsurance commissions help support company profitability**
- **Indications that reinsurance paid by GCC insurers is getting more expensive - this will threaten their profitability**
- **High reinsurance rates drive increasing number of captives being set up - this can drive part of the premiums away from local insurers**

Source: Best's Financial Suite - Global

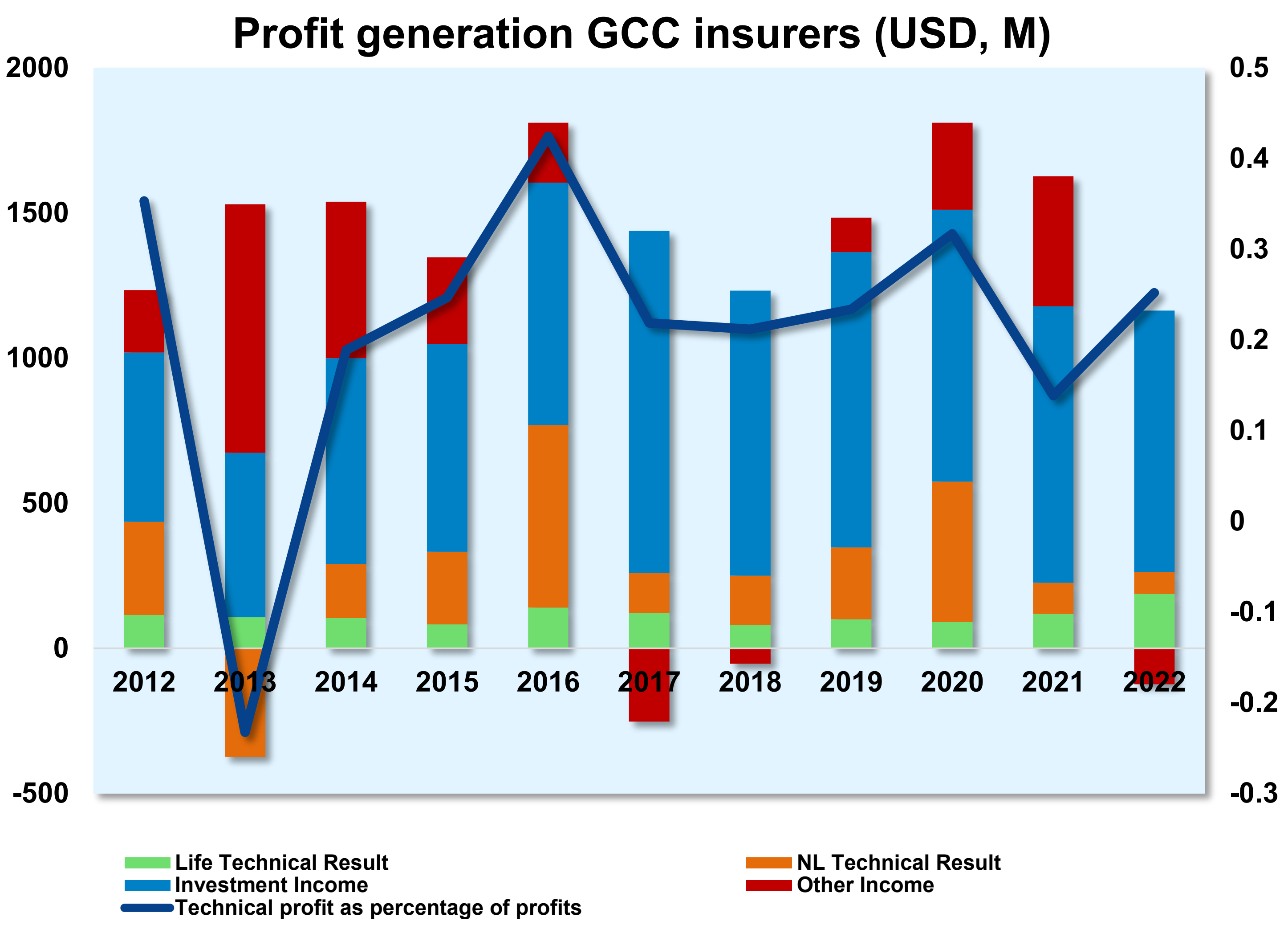
Increasing Cost of Transacting Business



- Management expenses have been increasing in most GCC markets
- This is more profound in the larger markets of UAE and Saudi
- Reducing margins mean that profitability is increasing dependent on
  a. Underwriting
  b. Reinsurance commissions
- With reinsurance rates increasing and many companies following the same underwriting the profitability of the industry is likely to suffer

Source: Best's Financial Suite - Global

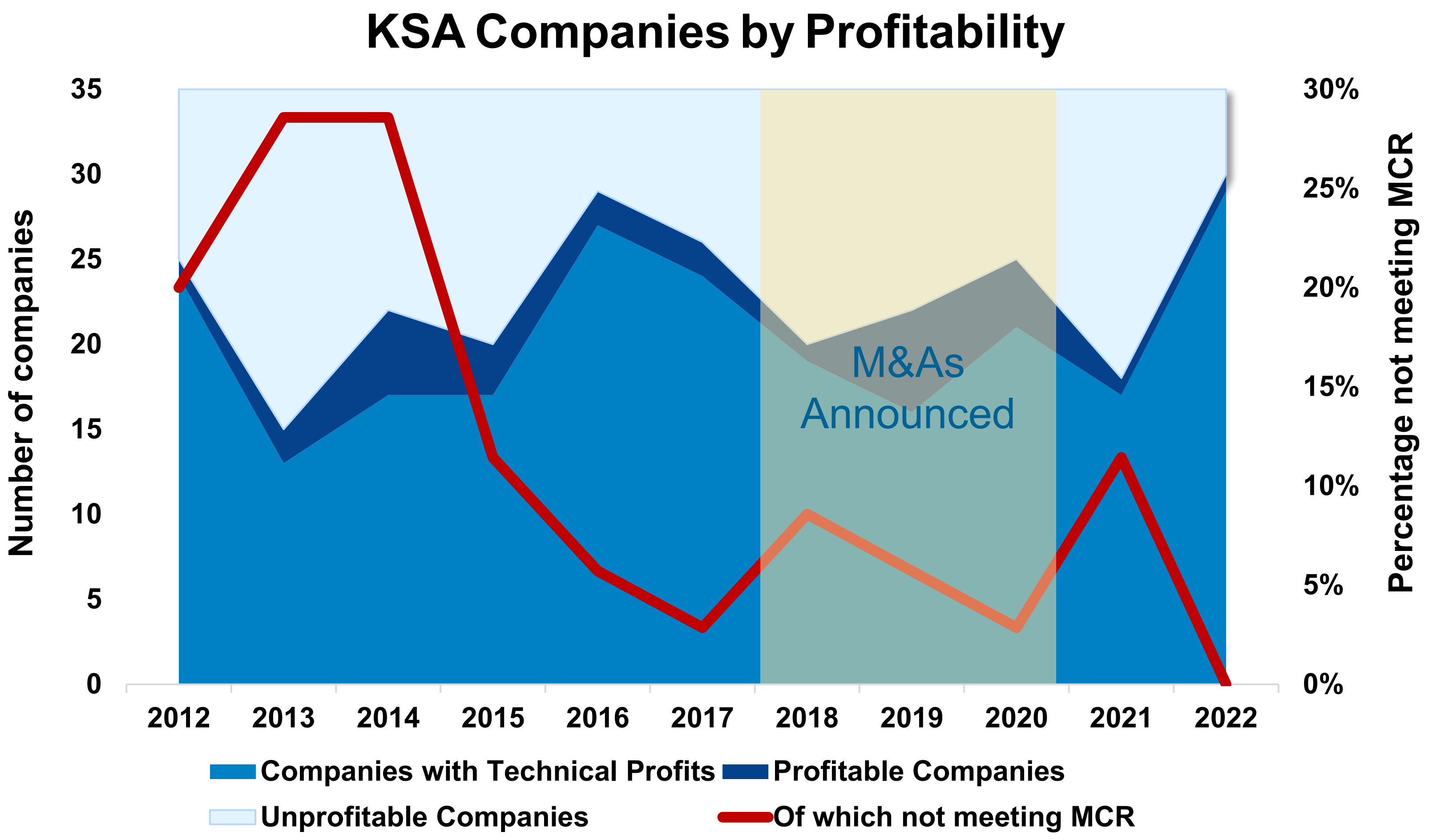
Profitability Declining



- Decline in overall market profitability over the last 3 years
- Technical profitability close to historical lows
- However, strong investment results and income from sale of investments support profitability
- Underwriting elements of profitability account for less than 30%
- Value of insurance companies to their shareholders depends heavily on investments rather than the core business

Source: Best's Financial Suite - Global

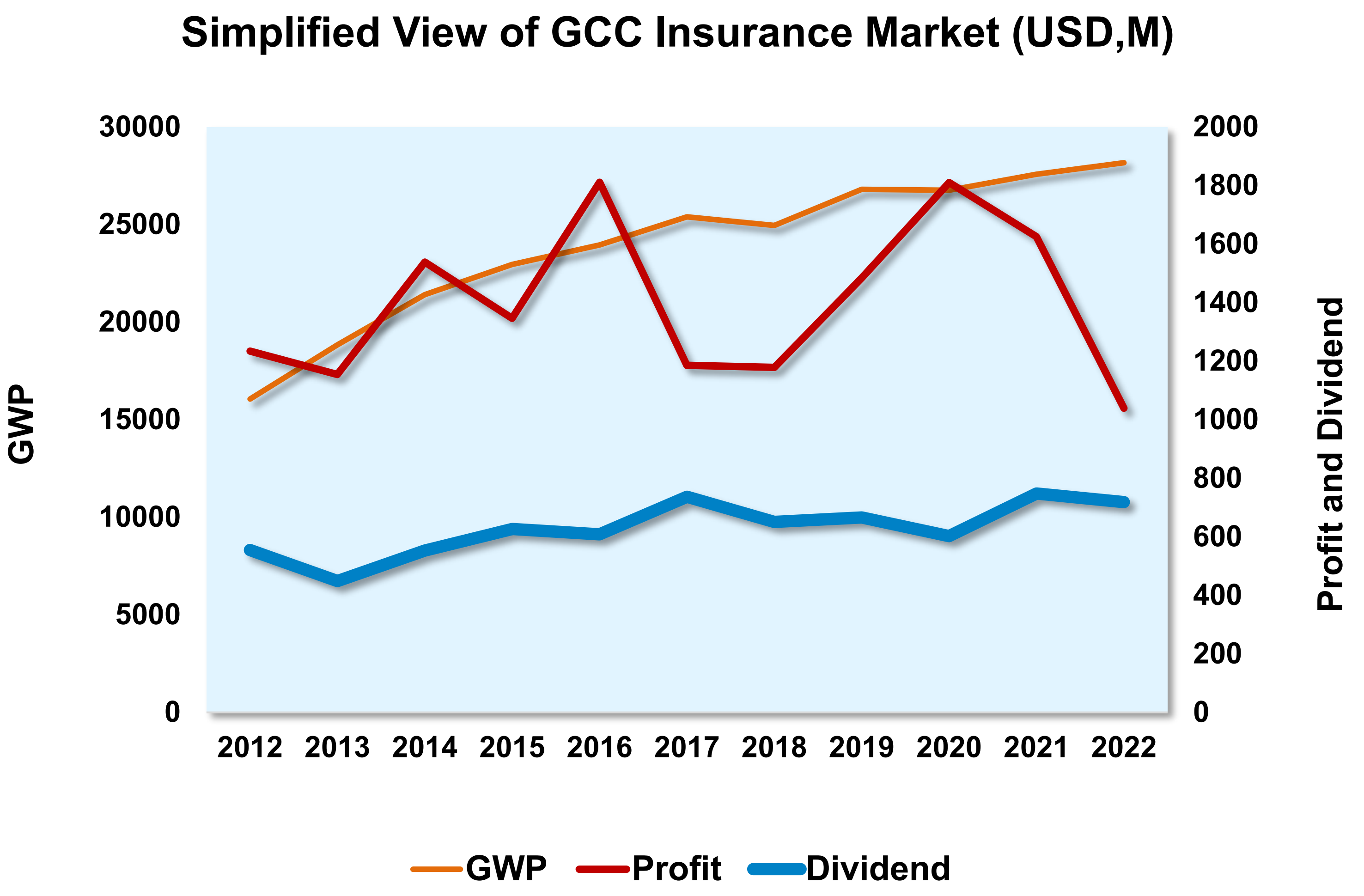
In KSA Most M&A were Initiated While Profitability was Dipping



- Many companies recapitalised in the earlier part of the period
- As profits started declining increasing number of companies were making losses and falling short of MCR
- Deals concluded much later
- Currently there are no companies falling below MCR – This is a picture that is repeated throughout the region
- Difficult to figure out the cause, and the effect between the improved profitability and MCR coverage

Source: Best's Financial Suite - Global

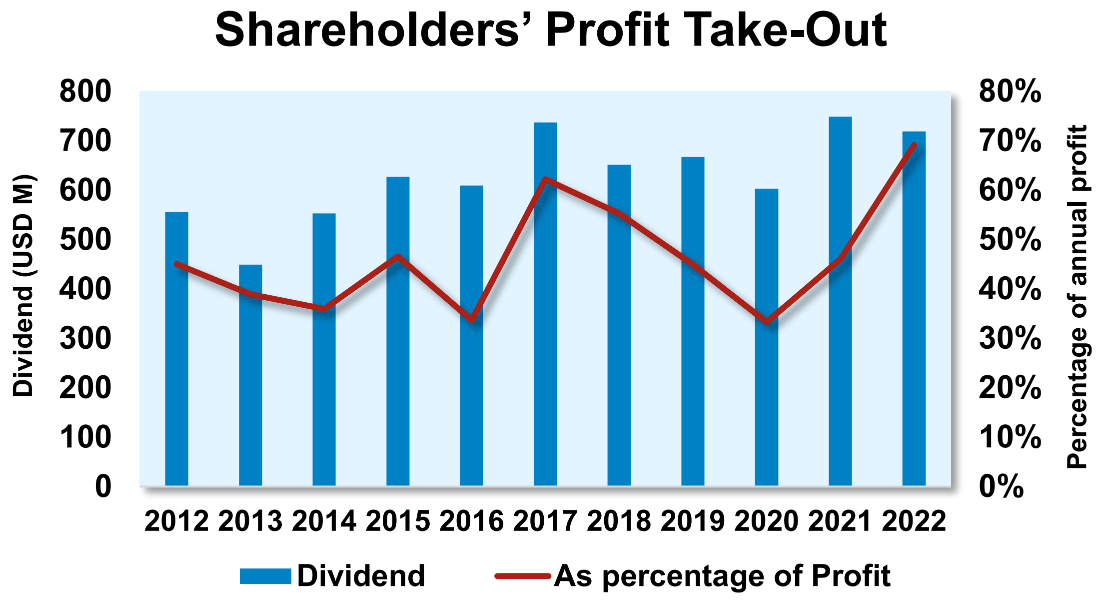
Shareholders’ Emphasis on Dividend Payment

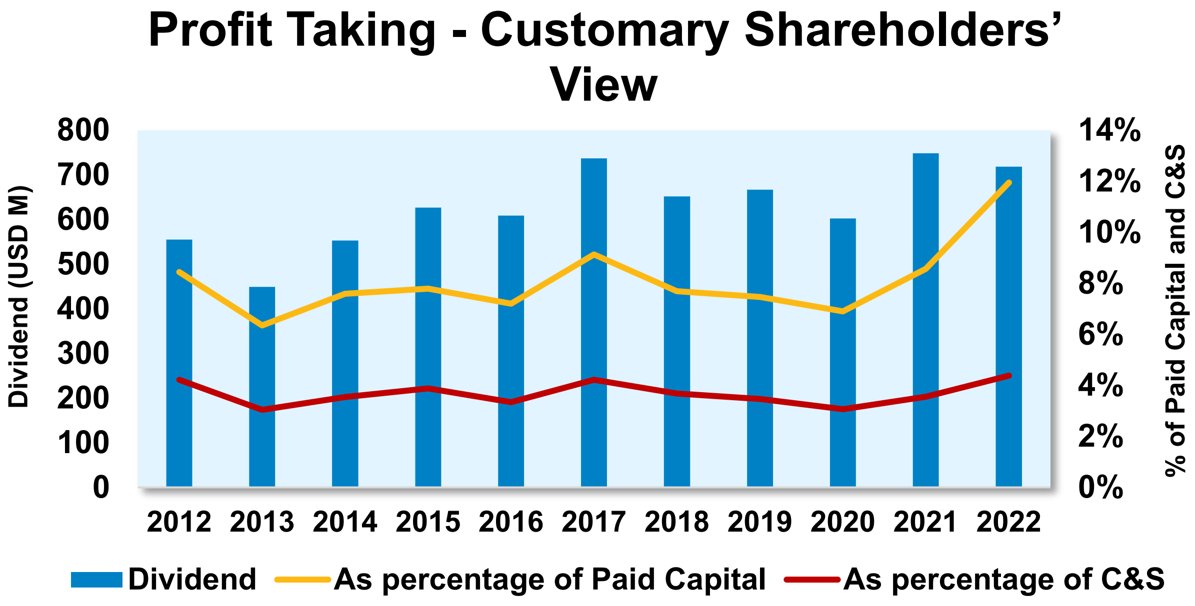


- **Shareholders give heavy emphasis on dividend payment ability of insurance companies**
- **Based on this the market has been doing well and its performance strengthening**
- **However, profit making ability has been more erratic**
- **This despite growing top line**
- **Because of this background some shareholders are willing to consider alternatives to their investments**

Source: Best’s Financial Suite - Global

Disconnect Between Profitability and Dividend Payment





- On average 70% of profits generated are paid out as dividend
- Dividends increasing in a period of declining profits
- Most companies do not follow their pay-out ratios

- Most companies pay dividends based on the par-value of capital
- Shareholders may not feel they are taking excessive dividends
- This can be both positive and negative for M&A activity as it supports uneconomical expectations

Source: Best's Financial Suite - Global

Changing Regulatory Requirements

Stricter implementation of minimum capital requirements	• Pressure on shareholders to either recapitalise or sell • No impact on better capitalised companies but those less capitalised become uneconomical
Introduction of RBC models	• Brings greater sophistication on capital management • Positive and negative pressures on capitalisation depending on the company
Introduction of governance requirements	• Reduced representation of shareholders on Boards
More detailed reporting requirements	• Greater ability for timely regulatory intervention • Increased cost of operation
Introduction of IFRS17	• Long term greater transparency but short-to-medium term confusion • Increased difficulty in communicating results to shareholders • Increased cost of operation

Agenda

- The Market
- M&A to Date
- Forces Impacting M&A in the Future
- **Conclusion**

Conclusion

- **M&A activity has accelerated in the GCC insurance market; More than 10% of the companies in the market have been involved in an M&A deal that has been completed**
- **Regulatory pressures have been the main driver for the M&A activity until now**
- **Few companies have tried to build a regional footprint through M&A**
- **Going forward the increasing cost of operation and reduced technical profitability will fuel more M&A**
- **However, uneconomical dividend practices will continue distorting the market and delaying decisions**

M&A in the GCC insurance Market – A Changing Landscape?

Vasilis Katsipis
General Manager, MENA, South and Central Asia

Q&A

Fairmont, Dubai

AM Best's
MENA Insurance Market Briefing

17 November 2023