August 14, 2022

# Opportunities Arise for MENA Reinsurers, Amid Divergent Economic Conditions

**Longer-term prospects for the reinsurance market may transpire from growing product offerings in primary markets**

## Principal Takeaways

- Hardening reinsurance market conditions in the region, as well as changes in reinsurers' appetites as to where they deploy their capital, have sustained the positive price momentum over recent renewal seasons
- Reinsurance capacity in the region continues to be highly changeable and dynamic, sourced through global reinsurance players, regionally domiciled reinsurers, and reinsurance groups from Africa and Asia
- Divergent economic conditions are expected to continue across the region for oil-exporting and oil-importing countries
- Operational challenges and deteriorating country risk landscapes in several countries have weighed negatively on AM Best's view of the financial strength of the reinsurers domiciled and operating there

Hardening markets conditions over 2021 continued to benefit regional reinsurers domiciled in the Middle East and North Africa (MENA). Positive pricing momentum has been maintained over recent renewal seasons, driven by changes in the region's reinsurance capacity providers, rising claims inflation, elevated frequency of large loss events and improved market discipline. Current market conditions contrast to the persisting soft market experienced in the region prior to 2020, themselves a by-product of plentiful capacity and high levels of price competition.

The reinsurance pricing environment in the MENA region reflects both regional drivers, such as recent underwriting performance strains, as well as global reinsurance trends, and are a clear tailwind for reinsurance providers in the region. In general, AM Best views the region as having good reinsurance growth potential, supported by rebounding economic activity, the extraction of natural resources, and intentions to increase insurance penetration across the region.

However, MENA reinsurers are facing fresh and varying challenges, from supply chain disruptions and inflationary pressures, to elevated economic, financial and political instability in certain markets. AM Best notes that the region is not homogenous, and that what is a positive driver for one market, such as buoyant oil prices, can be a negative contributor for others, and consequently for the regional reinsurers operating there. In this context, AM Best views deteriorating country risk factors in several of the region's markets as a negative credit trend.

## Diverging Economic Conditions to Impact Reinsurance Markets

Over 2021, the MENA region experienced a general improvement in economic conditions as countries rebounded following the COVID-19 pandemic. In AM Best's view, this provided a solid platform for (re)insurance market opportunities. In March 2022, AM Best revised

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its market segment outlook on the Gulf Cooperation Council (GCC)—a significant, and largely oil-reliant, sub-section of the MENA region—to Stable from Negative owing to rallying oil prices driving economic recovery, increased opportunities for insurance sector growth and recovering financial markets.

Several of the economies in the region are heavily reliant on hydrocarbon industries. The current buoyant oil price environment, attributable to supply concerns amid excess demand for oil and energy linked to post-pandemic activity and disruption caused by Russia's invasion of Ukraine, is expected to have a substantial impact on the region's economies. Insurance markets in the region are reliant on government spending—notably from infrastructure projects—for a sizeable share of premium growth. These risks are typically heavily ceded by primary insurers to reinsurance partners, and have provided profitable underwriting opportunities for the region's reinsurers. AM Best expects strengthening economic fundamentals for the region's oil-exporting economies to directly contribute to insurable risk opportunities and in turn premium volumes ceded to the region's reinsurance markets.

Conversely, AM Best notes that certain markets in the region are experiencing a significant economic deterioration. For those countries that are net importers of energy, the current oil price environment is challenging fiscal manoeuvrability, while inflationary pressures and supply side constraints on the importation of foodstuffs and other commodities are compounding economic challenges. In AM Best's view, current geopolitical volatility has served to exacerbate the country risk vulnerabilities exposed during the COVID-19 pandemic, which may constrain opportunities and the financial strength of (re)insurers in those markets.

Deterioration in the country risk environments of several countries has been cited as a driver of negative rating actions taken over the past year on several regional reinsurers with a material concentration of operations, underwriting exposures or asset portfolios to these operating environments. Examples of such jurisdictions that are experiencing heightened country risk challenges include Turkey, Tunisia and Lebanon.

### Economic Transition to Support Longer-Term Opportunities

Longer-term prospects for the reinsurance market may transpire from growing product offerings in primary markets, namely in cyber and liability lines of business along with opportunities created by the commitments of the region's oil-exporting countries to reduce dependence on petrochemicals and create economic diversification. To reach these targets, higher levels of fiscal expenditure are expected to be channelled into 'green' and other infrastructure projects, including green buildings and solar parks. In AM Best's view, the region's reinsurers that can embrace the economic shift, develop the required capabilities and tailor their products accordingly should be well placed to benefit from this expected increase in insurable risk opportunities.

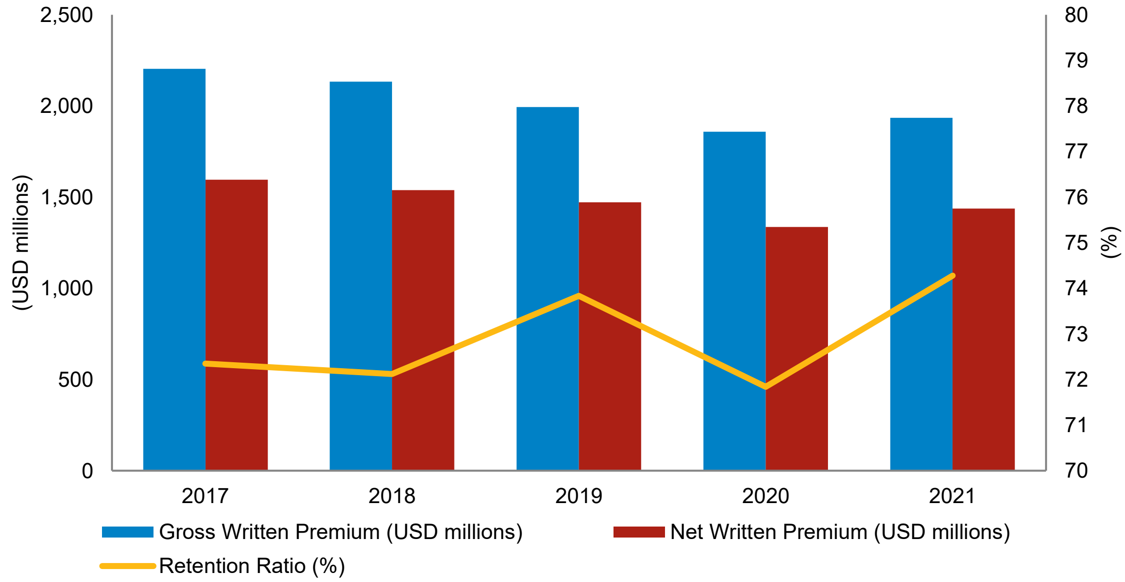
### Reinsurance Capacity in the MENA Region

In general, the region's reinsurance markets remain open and liberal, with few regulatory restrictions concerning the provision of reinsurance capacity. Accordingly, the region's capacity comes from many sources, including global reinsurance players, regionally domiciled reinsurers, and reinsurance groups from Africa and Asia. Furthermore, primary insurance companies in the region are once again increasing their appetite to participate in the reinsurance segment. For international participants, the region has long been seen as an opportunity to diversify their exposures into historically low natural catastrophe risk environments. For others, and reinsurers domiciled in the region, it has provided growth opportunities, often through taking following participations on programmes led by international markets.

Exhibit 1

**MENA Reinsurance – Gross/Net Written Premiums and Retention Ratio, 2017-2021**

(USD millions (Premiums) and % (Retention Ratio))




Sources: BESTLINK

*Best's Financial Suite - Global*, AM Best data and research

Reinsurance capacity in the region continues to be highly changeable and dynamic. In recent periods, several regional and international players, including certain Lloyd's syndicates, have withdrawn from the market, revising their appetite for the region often following weaker than expected performance and an inability to generate sufficient returns. At the same time, appetite clearly remains to participate in the region's reinsurance market, with a steady flow of international reinsurers, as well as African and Asian regional players, establishing a presence to enhance proximity to clients and execute growth and diversification strategies.

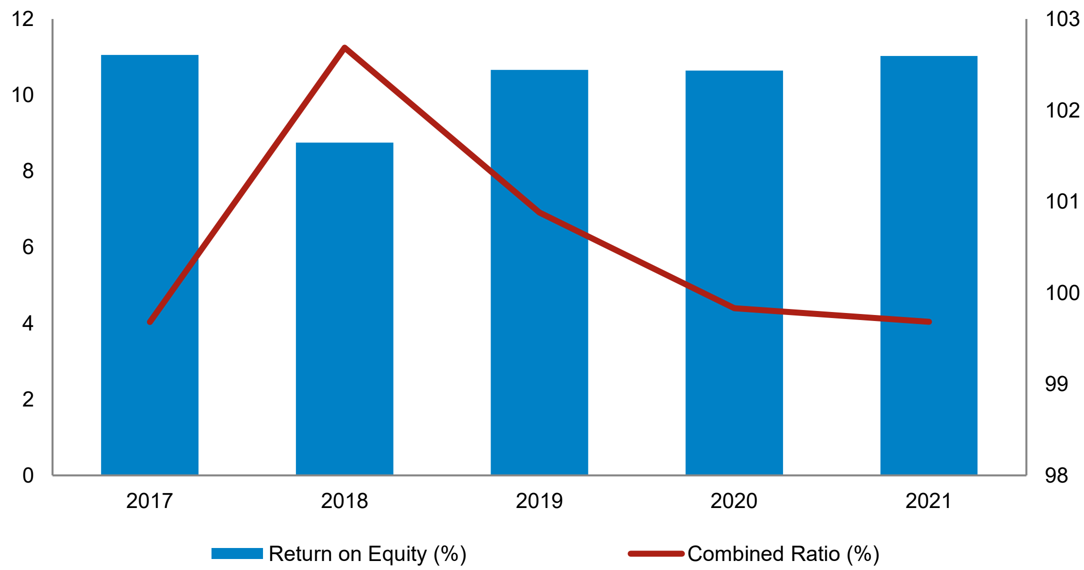
Despite changes in the region's capacity providers, AM Best has yet to note material growth in market premiums written by the remaining regionally domiciled reinsurers (see **Exhibit 1**). This suggests that these companies have not been able to fully capture the premium income left by those exiting the market and that sufficient capacity remains in the market overall. Whilst a marginal increase in premiums has been observed in 2021, this can be largely attributed to rate rises and supportive economic conditions following the lifting of virus containment measures in place during 2020. The premium growth rate observed over 2021 is also partially distorted by currency volatility to the US dollar. While several countries in the region maintain pegs (or similar) to the US dollar, those with free-floating currencies experienced devaluation over the year, and in some cases, positive underlying premium growth rates in local currencies were negative in US dollar terms.

A growing number of the region's primary insurers have shown a renewed interest in participating in the regional reinsurance market on an inward facultative basis. Inward facultative interest has accelerated since 2020 as primary insurers have looked to bolster their toplines and access insurable risk opportunities. AM Best notes that the inward facultative segment has been a source of underwriting losses and volatility for several insurance companies in the market historically, demonstrating the risks presented by this diversification strategy for the region's insurers.

Exhibit 2

**MENA Reinsurance – Market Average Return on Equity and Combined Ratio, 2017-2021**

(%)




Dataset based on a selection of regionally domiciled reinsurers.

Sources: BESTLINK

*Best's Financial Suite - Global*, AM Best data and research

AM Best expects primary insurers' interest in writing inward facultative reinsurance business to remain a competitive dynamic in the coming years, and indicative of reinsurance capacity remaining plentiful in the region. In this context, regional reinsurers will need to demonstrate strong underwriting discipline to ensure that recent positive pricing momentum is not reversed.

## Underwriting Returns – Changing Focus for Regional Reinsurers

Through a period of generally soft market conditions, achieving consistent strong underwriting returns has been a challenge for MENA reinsurers. However, recent market conditions have become more favourable, which, in AM Best's view, is also a signal of an enhanced focus on underwriting profitability.

Aside from strong competition, the performance hurdles faced by the region's reinsurers include a lack of both scale and diversification when compared with their international counterparts, and their participation often as followers on reinsurance programmes, which restricts their ability to influence pricing and terms. Additionally, market-wide performance has been adversely impacted in recent years by an increasing volume of natural catastrophe losses and several single large loss events. Reinsurers in the region are having to adapt pricing and modelling capabilities following greater incidences of weather-related losses, such as flood events (particularly in the GCC), to ensure these exposures are appropriately factored into underwriting decisions and risk appetites. Single large event losses, such as the Beirut blast in August 2020 and several high profile fire events, have weighed particularly on property, engineering and energy lines that in general are heavily ceded by the direct market.

**Exhibit 2** shows the aggregate underwriting performance of reinsurers domiciled in the region, and highlights how overall, the cohort of companies has struggled to achieve consistently profitable underwriting returns in recent years.

Exhibit 3
**MENA Reinsurance – Technical Performance, 2019-2021**
(%)

| | | | Loss Ratio - Non-Life | | | | Combined Ratio - Non-Life | | | |
|---|---|---|---|---|---|---|---|---|---|---|
| **AMB #** | **Company Name** | **Country** | **2019** | **2020** | **2021** | **3yr Avg** | **2019** | **2020** | **2021** | **3yr Avg** |
| 89190 | Arab Reinsurance Co. SAL | Lebanon | 71.1 | 72.6 | 66.6 | 70.1 | 105.7 | 104.0 | 108.0 | 105.9 |
| 85013 | Arab Insurance Group (B.S.C.)[1] | Bahrain | 59.5 | 43.0 | -103.8 | -0.4 | 100.4 | 90.5 | -10.7 | 60.1 |
| 90777 | Compagnie Centrale de Réassurance | Algeria | 59.4 | 52.7 | 51.4 | 54.5 | 84.3 | 82.2 | 77.8 | 81.4 |
| 78849 | Hannover Re Takaful B.S.C. (c) | Bahrain | 63.8 | 63.2 | 43.4 | 56.8 | 102.8 | 100.4 | 85.5 | 96.2 |
| 85585 | Kuwait Reinsurance Co. K.S.C.P. | Kuwait | 65.9 | 68.8 | 65.5 | 66.7 | 96.5 | 97.3 | 92.2 | 95.3 |
| 85454 | Milli Reasurans Turk Anonim Sirketi | Turkey | 89.2 | 88.8 | 113.9 | 97.3 | 122.4 | 123.9 | 150.6 | 132.3 |
| 93609 | Oman Reinsurance Co. SAOC | Oman | 66.5 | 62.1 | 63.1 | 63.9 | 106.6 | 102.8 | 103.0 | 104.1 |
| 90005 | Saudi Reinsurance Company | Saudi Arabia | 63.6 | 58.2 | 61.3 | 61.0 | 95.4 | 94.7 | 96.2 | 95.4 |
| 84052 | Société Centrale de Réassurance | Morocco | 35.1 | 45.1 | 46.3 | 42.2 | 81.8 | 92.5 | 88.4 | 87.6 |
| 83349 | Société Tunisienne de Réassurance | Tunisia | 62.3 | 60.3 | 57.2 | 59.9 | 99.2 | 96.2 | 98.0 | 97.8 |
| 86326 | Trust International Insurance & Reinsurance Co. BSC[2] | Bahrain | 88.9 | - | - | 88.9 | 150.0 | - | - | 150.0 |

1: Aug. 13, 2020: Arab Insurance Group (B.S.C.) announced that it would cease writing further reinsurance business and seek to carry out an orderly run-off of its existing portfolio.
2: At the time of writing audited year-end 2020 and 2021 financial statements were not available

Sources: BESTLINK

*Best's Financial Suite - Global* , AM Best data and research

Strategies adopted by the region's reinsurers vary considerably. They tend to benefit from long-standing, strong positions in their domestic markets, and several are executing strategies to attain regional and international diversification. Strategic shifts are ongoing, with some looking to increase non-proportional and facultative business and reduce reliance on providing proportional capacity.

In this market dynamic, it is not uncommon for the region's reinsurers to report comparatively strong performance in their local markets, where they benefit from local expertise and long-standing relationships with market participants. In contrast, geographical diversification is often accompanied by thinner margins and increased volatility, a function of smaller, "follower" participations, increased cost of market access through intermediaries and varied risk exposures, which differ from those in domestic markets.

**Exhibit 3** highlights the wide range in underwriting returns achieved by MENA domiciled reinsurers, with over half reporting underwriting losses and non-life combined ratios in excess of 100% at least once in the past three years. Given recent improved market conditions, most MENA domiciled reinsurers recorded strengthened combined ratios in 2021. While there were some modest improvements on loss ratios, rate driven premium growth in local currencies provided strong scale benefits and pushed down expense ratios in many cases.

Notwithstanding recent pressures on underwriting margins, overall returns have generally remained robust for the region's reinsurers, with the weighted average return on equity (ROE) for the cohort of companies standing at 10% over the five years to 2021. Thinner underwriting margins have been more than compensated by generally robust investment returns over the period. On a company-by-company basis, the comparability of ROE is somewhat skewed by the prevailing inflationary and interest rate environment in their respective countries of operation.

## Positive Pricing Momentum

Hardening reinsurance market conditions in the region since 2020, as well as changes in reinsurers' appetites as to where they deploy their capital, reflect the lower than anticipated profitability of regional business and the need for reinsurers to strengthen their returns on capital. Additional factors including global reinsurance trends, a tightening focus on underwriting discipline, increased inflationary pressures and in some countries, economic challenges, are contributing positively to the rate environment.

As with global reinsurance markets, the MENA region is not immune from the spectre of inflation, even with the resilience to oil price increases for the net oil-exporting economies. Supply-side inflation may weigh on loss cost trends for the region's reinsurers over the near term. As the inflationary environment develops, the region's reinsurers will need to remain nimble and disciplined to adjust premium rates to ensure loss cost inflation is adequately covered and does not erode already thin underwriting margins.

While recent market hardening is a positive for the region's reinsurers, there remain questions over the sustainability of rate increases, particularly in the context of reinsurance capacity remaining readily available. The extent to which regional reinsurers will be able to benefit from current favourable conditions will depend on a number of factors, including their ability to dictate lead terms and drive extensive rate changes, especially if larger, more diversified competitors are willing and able to accept lower price increases.

AM Best has observed an increased focus in the region on underwriting control, selection and profitability, with some strategic changes emerging as a result. Regional reinsurers are looking to capitalise on the current pricing environment, reduced international capacity and increased loss events to increase their exposure to facultative business. They believe that this is where they will be able to exert greater control over rates, terms and underlying exposures rather than on treaty business.

## MENA Reinsurers – Rating Considerations

AM Best's credit ratings of reinsurers domiciled in the region encompass Financial Strength Ratings (FSR) of "B-" through to "A-". The wide range in FSRs partly reflects divergent country risk conditions across the region. AM Best defines country risk as the risk that country-specific factors could adversely affect an insurer's ability to meet its financial obligations. Countries are placed into

Exhibit 4

**MENA Reinsurers – AM Best-Rated Companies**

Ratings as of August 1, 2022

| AMB # | Company Name | Country (optional) | Best's Long-Term Issuer Credit Rating (ICR) | Best's Financial Strength Rating (FSR) | Best's ICR & FSR Action | Best's ICR & FSR Outlook | Rating Effective Date |
|---|---|---|---|---|---|---|---|
| 89190 | Arab Reinsurance Co. SAL | Lebanon | bb- | B- | Downgraded | Negative | 13-Aug-21 |
| 90777 | Compagnie Centrale de Réassurance | Algeria | bbb- | B+ | Affirmed | Stable | 21-Oct-21 |
| 85585 | Kuwait Reinsurance Co.K.S.C.P. | Kuwait | a- | A- | Affirmed | Stable | 2-Jun-22 |
| 85454 | Milli Reasurans Turk Anonim Sirketi | Turkey | bb- | B- | Downgraded | Negative | 9-Jun-22 |
| 84052 | Société Centrale de Réassurance | Morocco | bbb | B++ | Affirmed | Stable | 10-Dec-21 |
| 83349 | Société Tunisienne de Réassurance | Tunisia | bb+ | B | Downgraded | Negative[1] | 8-Apr-22 |

1: FSR Outlook: Stable

Sources: BESTLINK

*Best's Financial Suite - Global*, AM Best data and research

Exhibit 5

**MENA Reinsurers – AM Best-Rated Companies – Assessment Descriptors**

As of August 1, 2022

| AMB # | Company Name | Balance Sheet Strength Assessment | BCAR @ VaR 99.6 | BCAR Assessment Keyword | Operating Performance Assessment | Business Profile Assessment | Enterprise Risk Managment Assessment |
|---|---|---|---|---|---|---|---|
| 89190 | Arab Reinsurance Co. SAL | Strong | 24% | Very Strong | Marginal | Neutral | Marginal |
| 90777 | Compagnie Centrale de Réassurance | Very Strong | 39% | Strongest | Strong | Neutral | Marginal |
| 85585 | Kuwait Reinsurance Co.K.S.C.P. | Very Strong | 44% | Strongest | Adequate | Neutral | Appropriate |
| 85454 | Milli Reasurans Turk Anonim Sirketi | Adequate | -35% | Very Weak | Adequate | Neutral | Appropriate |
| 84052 | Société Centrale de Réassurance | Strong | 39% | Strongest | Strong | Neutral | Appropriate |
| 83349 | Société Tunisienne de Réassurance | Very Strong | 57% | Strongest | Adequate | Limited | Marginal |

Sources: BESTLINK

*Best's Financial Suite - Global*, AM Best data and research

one of five tiers, ranging from Country Risk Tier 1 (CRT-1), denoting a stable environment with the least amount of risk, to Country Risk Tier 5 (CRT-5) for countries that pose the most risk and, therefore, the greatest challenge to an insurer's financial stability, strength and performance. The MENA region encompasses countries assessed between CRT-3 and CRT-5.

Over the past 12 months, operational challenges and deteriorating country risk landscapes in several countries have weighed negatively on AM Best's view of the financial strength of the reinsurers domiciled and operating there. Increasing economic, fiscal and political risk is prevalent in several of the region's countries, typically the non-oil exporting nations. Increased public debt burdens taken on during the pandemic, coupled with increasing oil and other commodity prices and currency devaluations against the US dollar, have contributed to, among other things, weakening current account balances, sovereign debt downgrades, high inflation and ultimately the need to secure external funding to counteract economic woes.

In this context, several companies have experienced downgrades over the past year to their Long-Term Issuer Credit Ratings (see **Exhibit 4**). Negative rating actions and outlook revisions reflect the impact that elevated country risk can have on a company's balance sheet fundamentals as well as on the risk profile a company must face and manage.

On the whole, AM Best-rated MENA reinsurers tend to demonstrate "strongest levels" of risk-adjusted capitalisation, as measured by Best's Capital Adequacy Ratio, reflective of significant capital buffers relative to their operational exposures **(Exhibit 5)**. Most rated MENA reinsurers typically enjoy preferred or dominant positions in their operating markets resulting in neutral business profile assessments. On the other hand, as highlighted in this report (see **Exhibits 2 and 3**) persistent performance challenges have resulted in a wider range of operating performance assessments, with AM Best-rated MENA reinsurers carrying operating performance assessments that range from "Marginal" to "Strong".

## Retakaful – Yet to Capitalise on a Growing Takaful Market

Retakaful (Islamic reinsurance) operators have yet to achieve traction in the MENA region, despite the expected market opportunities. Initial strong momentum in the retakaful segment has stalled, with several early entrants to the sector withdrawing from the market following inconsistent and underperforming technical returns and an inability to gain necessary scale. Retakaful capacity in the region is currently primarily provided through branches, takaful windows or subsidiaries of conventional reinsurers, rather than "dedicated" retakaful operators.

In AM Best's opinion, several factors have constrained the success of retakaful in the region. These include the underachievement and small size of the region's direct takaful markets and, most notably, competitive pressure from the conventional reinsurance market amidst the ongoing acceptance by Shari'a boards of conventional reinsurance capacity on retakaful panels (often on the basis of their comparative financial strength). Until sufficient insurable risks can be ceded consistently to the retakaful market, the opportunity for dedicated retakaful operators in the region remains limited.

AM Best views the potential of the retakaful market to be highly dependent on the successful development and performance of the region's primary takaful market. Establishing Islamic compliant (re)insurance solutions remains a hot topic in many of the region's markets. The recent establishment of primary takaful regulation and operators in several North African territories is indicative of general support for the segment. If successful, such recent initiatives should ultimately generate more contributions that would increase the demand for retakaful capacity. However, AM Best expects that, at least initially, the retakaful needs of these start-up takaful operators will be met by the opening of takaful windows in already established conventional reinsurers. Given the challenges faced in establishing sustainable, standalone retakaful operators, it is uncertain whether a dedicated retakaful segment will be able to capitalise on these developments in the near term.

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