INVESTORS SERVICE

Credit Opinion: Al-Ain Ahlia Insurance Co.

Global Credit Research - 06 Feb 2014

Abu Dhabi, United Arab Emirates

Ratings

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

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Key Indicators

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

	2012	2011	2010	2009	2008
As Reported (UAE Dirham Millions)					
Total Assets	**1,552**	**1,630**	**1,712**	**1,876**	**2,179**
Shareholders' Equity	**986**	**963**	**1,012**	**1,096**	**1,154**
Net Income (Loss) Attributable to Common Shareholders	**50**	**53**	**62**	**75**	**144**
Gross Premiums Written	**462**	**504**	**594**	**605**	**696**
Net Premiums Written	**196**	**202**	**205**	**229**	**286**
Moody's Adjusted Ratios					
High Risk Assets % Shareholders' Equity	**68.5%**	**71.4%**	**69.8%**	**65.8%**	**56.1%**
Reinsurance Recoverable % Shareholders' Equity	**50.0%**	**54.2%**	**50.2%**	**46.8%**	**63.0%**
Goodwill & Intangibles % Shareholders' Equity	**-**	**-**	**-**	**-**	**-**
Gross Underwriting Leverage	**0.8x**	**0.9x**	**1.0x**	**0.9x**	**1.2x**
Return on Capital (1 yr)	**5.2%**	**5.4%**	**5.9%**	**6.7%**	**12.1%**
Sharpe Ratio of ROC (5 yr avg)	**243.5%**	**164.8%**	**NA**	**NA**	**NA**
Adv (Fav) Loss Dev % Beginning Reserves (1 yr)	**NA**	**NA**	**NA**	**NA**	**NA**
Financial Leverage	**-**	**-**	**-**	**-**	**-**
Total Leverage	**-**	**-**	**-**	**-**	**-**
Earnings Coverage (1 yr)	**NM**	**NM**	**NM**	**NM**	**NM**
Cash Flow Coverage (1 yr)	**NM**	**NM**	**NM**	**NM**	**NM**

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

Opinion

SUMMARY RATING RATIONALE

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

In accordance with Moody's rating methodology for GRIs, the rating of Al-Ain Ahlia reflects a combination of the following inputs: (i) a baseline credit assessment of a3; (ii) Very High (90%) dependence, reflecting the company's operating and financial proximity to the government of Abu Dhabi; and (iii) Low (0-30%) support, reflecting the importance of Al-Ain Ahlia in its capacity as an insurer of government projects offset by the limited state ownership of 19.7%.

Credit Strengths

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

Good technical proficiency, with long history of oil & gas underwriting and co-operation with major international reinsurers

Excellent capital position, with gross underwriting leverage at 0.8x in 2012

Strong underwriting profitability

Credit Challenges

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

Focus on Abu Dhabi, does create geographic concentration risk and reliance on the Abu Dhabi economic performance

Rating Outlook

The outlook is stable.

What Could Change the Rating - Up

Improvement in the asset quality, with a greater focus on high quality bond investments and deposits.

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

What Could Change the Rating - Down

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

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

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

What to Watch for:

Political instability in the region

Further pricing pressure and asset valuation volatility

Increasing capital requirements for all UAE insurers may improve market-wide pricing discipline

DETAILED RATING CONSIDERATION

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

Market Position, Brand and Distribution: A - LEADING GOVERNMENT-OWNED INSURER WITH A TOP 10

POSITION IN UAE

Al-Ain Ahlia is a primary insurance company based in Abu Dhabi. It was established in 1975 as one of two Government-owned insurers. Al-Ain Ahlia concentrates primarily on construction and energy risks where they have considerable past experience and a very strong market presence. With a market share of about 2% in a highly competitive UAE market, Al-Ain-Ahlia is one of the 10 largest national players.

Al-Ain Ahlia scores highly on technical quotations because of its technical expertise through its co-operation with recognized leaders in the reinsurance markets, its history of oil and engineering insurance in the region, its strong reinsurance program, and its State ownership.

Al-Ain Ahlia historically targeted 15% premium growth per annum, but growth is somewhat dependent on the timing of major projects. However, the award of government project has been affected by financial crises, but some large projects are scheduled to be developed in the next 2-5 years, with ADNOC alone planning to award numerous multi-billion dollar projects. The reduced premium volume during recent years is not attributable to the loss of any key clients, but due to selective reduction of motor portfolio in order to achieve better technical results. At the same time, gross premium are being further reduced by soft market conditions.

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

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

Geographic diversification is considered to be weak, given the focus on Abu Dhabi. Al-Ain Ahlia does write some inwards reinsurance from the rest of the Gulf region, but it is low in comparison to its Abu Dhabi and UAE premium levels. Nevertheless, Abu Dhabi is a strong economy within the Gulf region, with significant hydrocarbon resources and has been relatively immune from the recent financial crisis. Al-Ain Ahlia's main lines of business include Fire and General Accident (92% of 2012 GPW) and Marine/Aviation (8%).

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

Al-Ain Ahlia invests largely in cash/time deposits (31% of invested assets in 2012), equities (24%) and investment real estate (45%). 2012 high risk assets (equities and real estate) of 69% of shareholders funds represent a high level of investment leverage. It should further be noted there are concentration risks as the equities are primarily invested in UAE stocks, mostly in Abu Dhabi. We further note that, as at Q3 2013, quoted and unquoted equities increased to AED 349m (YE 2012: AED 238m), albeit this partly reflects the strong equity market performance in the UAE in 2013.

With the exception of the real estate, the portfolio is highly liquid, with most equities being listed. The company has no goodwill on its balance sheet. Reinsurance recoverables, at 50% of equity at YE 2012 demonstrate some exposure to reinsurance partners, although the metric is consistent with a Moody's Aa-parameter in this regard.

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

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

With a Gross Underwriting Leverage of 0.8x at YE 2012, Al-Ain Ahlia enjoys `Aaa' levels of capital on a raw score basis. However, a considerable amount of the assets are deemed to be high risk. The Gross Underwriting Leverage with 100% of high risk assets deducted from Shareholders Funds is 2.3x which is still strong in the `Aa' range.

Al-Ain Ahlia places significant emphasis on its outwards reinsurance program. Indeed strong retrocession is often an important factor when the Government awards insurance contracts. Al-Ain Ahlia has strong long-term relationships with most key global reinsurers. Net retentions on any single loss are limited to a maximum of US$ 250,000 for Aviation liability, with retentions significantly lower on all other lines of business, which is small in comparison to total equity of AED 986m at YE 2012.

As at Q3 2013, Shareholders' equity increased by 10% to AED 1,081m (YE 2012: AED 986m).

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

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

With a 5 year return on capital of 7.0% Al-Ain Ahlia is highly profitable under the base metrics, although these indicators are lower than pre crises levels. Stripping out investment income, return on capital is a more modest 2.9% over the past 5 years, but fairly stable. Historically, underwriting results have been satisfactory. Following a motor portfolio restructuring, Al-Ain Ahlia recorded a strong combined ratio of 90% in 2012, with the 5 year average also a strong 90% (both on a Moody's basis).

Moody's notes that underwriting results will be reasonably volatile due to the lumpy nature of the portfolio, as shown by the 17% deterioration in 2012 net underwriting profit to AED 58mn compared to AED 71mn in 2011, following a significant improvement during 2010 when net underwriting profit more than doubled. Investment income has stabilized with a 2012 and 2011 net result of AED 22mn, but these are considerable lower figures than the AED 163mn in 2007.

As at Q3 2013, Al-Ain Ahlia reported a net profit of AED 41.4m (Q3 2012: AED 36.8m), with gross premiums written increasing by 11% to AED 404m (Q3 2012: 363m).

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

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

Reserving is regarded as fairly low risk. The average tail is 4 months and Al-Ain Ahlia appoints independent loss adjusters for all claims above AED 50,000. There is no discounting in the reserves and triangles are not available, as is common place within the region.

Reserves are typically covered with cash, and coverage level (on a net of reinsurance basis) is very high at 14.4x (0.7x on a gross basis). IBNRs are set in line with Abu Dhabi regulatory requirements, but tend to overstate losses given the nature of the portfolio, significantly above the regional peer group.

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

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

Al-Ain Ahlia is currently un-levered, and consequently the EBIT coverage ratios and debt leverage metrics are extremely strong and in line with a `Aaa' rating. Nevertheless, Moody's regards Al-Ain Ahlia's ability to access capital as being more constrained.

Al-Ain Ahlia is listed on the Abu Dhabi stock exchange, and would be able to source additional funds through this, although Moody's regards the depth of the market to be fairly limited. We consider the financial flexibility based on limited needs to be in line with a `Baa' rating.

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

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

Other Considerations

Management, Governance and Risk management

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

Accounting and Disclosure

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

Ownership

Al-Ain Ahlia is 19.7% owned by the State, through the Abu Dhabi Investment Council. The Abu Dhabi Sovereign Wealth funds are approximately US$875bn in value. Further Royal family ownership is through the private investments of members of the Royal family.

Rating Factors

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

Financial Strength Rating Scorecard	Aaa	Aa	A	Baa	Ba	B	Caa	Score	Adjusted Score
Business Profile								**A**	**Baa**
Market Position and Brand (25%)								**A**	**A**
- Relative Market Share Ratio			**X**						
- Underwriting Expense Ratio % Net Premiums Written			**X**						
Product Focus and Diversification (10%)								**A**	**Baa**
- Product Risk			**X**						
- P&C Insurance Product Diversification		**X**							
- Geographic Diversification						**X**			
Financial Profile								**Aa**	**A**
Asset Quality (10%)								**Aa**	**Baa**
- High Risk Assets % Shareholders' Equity			**68.5%**						
- Reinsurance Recoverable % Shareholders' Equity		**50.0%**							
- Goodwill & Intangibles % Shareholders' Equity	**0.0%**								
Capital Adequacy (15%)								**Aaa**	**A**
- Gross Underwriting Leverage	**0.8x**								
Profitability (15%)								**A**	**A**
- Return on Capital (5 yr avg)			**7.0%**						
- Sharpe Ratio of ROC (5 yr avg)			**243.5%**						
Reserve Adequacy (10%)									**A**
- Adv (Fav) Loss Dev % Beginning Reserves (5 yr. wtd avg)									
Financial Flexibility (15%)								**Aa**	**Baa**
- Financial Leverage	**0.0%**								
- Total Leverage	**0.0%**								
- Earnings Coverage (5 yr avg)									
- Cash Flow Coverage (5 yr avg)									
Operating Environment								**Aaa - A**	**Aaa - A**
Aggregate Profile								**Aa3**	**A3**

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

considerations (discussed above) are incorporated into the analysis