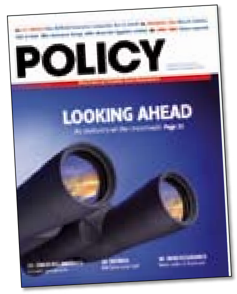


LOOKING AHEAD

an industry at the crossroads

WITH THE DAWN OF A NEW DECADE, POLICY ASKED FIVE INDUSTRY LEADERS TO REFLECT ON THE LESSONS OF 2009 AND TO CONSIDER WHAT THE FUTURE HOLDS FOR MIDDLE EAST INSURANCE COMPANIES. THEY ALSO REFLECT ON WHETHER THE QUEST FOR A HARD MARKET REMAINS AN IMPOSSIBLE DREAM AND EXPRESS THEIR WISH LISTS FOR THE LONG-TERM HEALTH AND DEVELOPMENT OF THE INDUSTRY

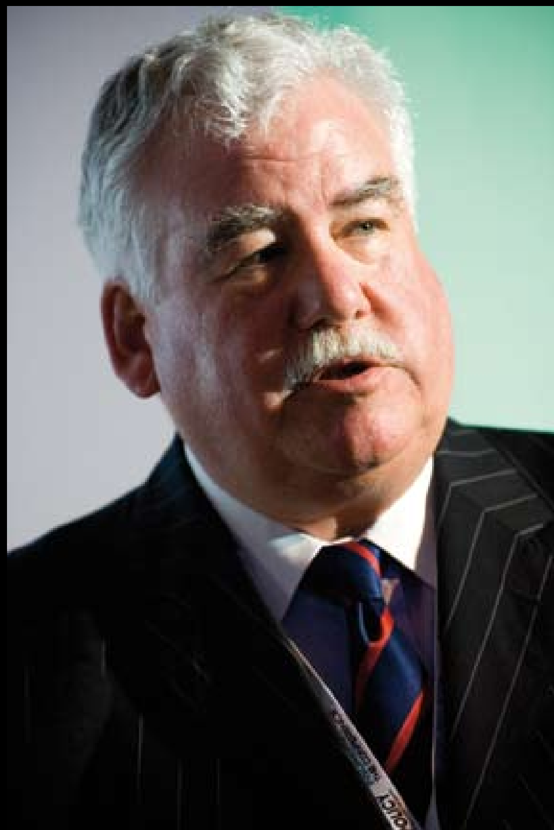
WHAT LESSONS HAVE BEEN LEARNED FROM 2009 AND WHAT DO YOU EXPECT TO BE (OR SHOULD BE) KEY AREAS OF FOCUS FOR MIDDLE EAST INSURERS IN 2010?

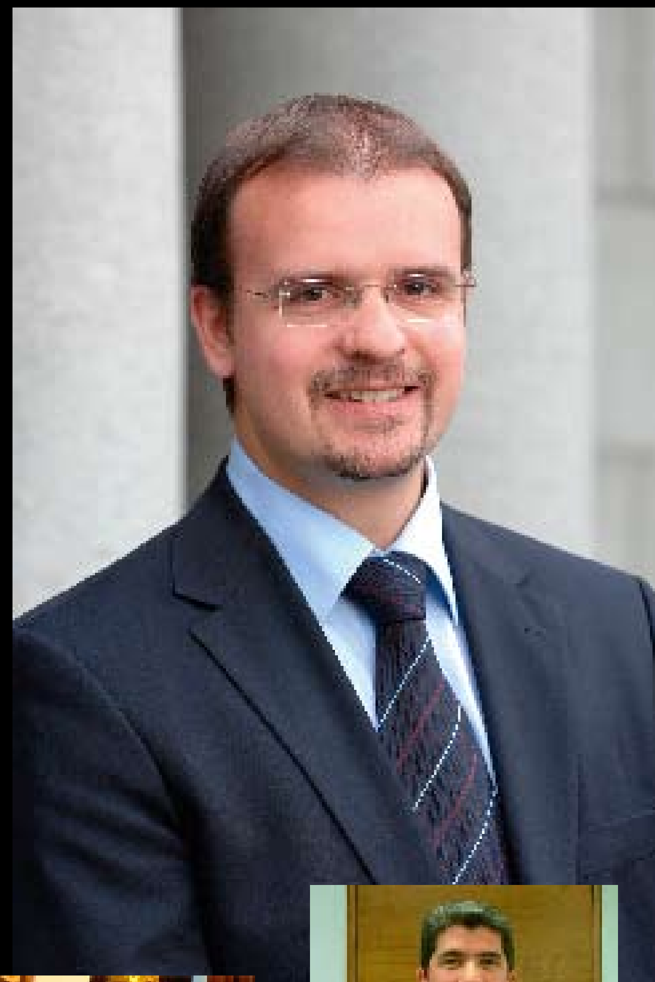
Yassir Albaharna The recent financial crisis offered hard evidence that Enterprise Risk Management (ERM) is critical for the success of insurance companies or other financial institutions. However, just adopting ERM will not be able to prevent an insurance company from either insolvency or suffering large losses of their market value. The crisis demonstrated that adopting ERM programmes for the only purpose of fulfilling rating agency requirements may not be the best practice. The effectiveness of ERM strategies should be the main area of focus of all companies including Middle East insurers. Insurance companies also learned that the ERM process should pay more attention to systemic risk, ie that there is a risk of collapse of an entire financial system or capital market that needs to be planned for.

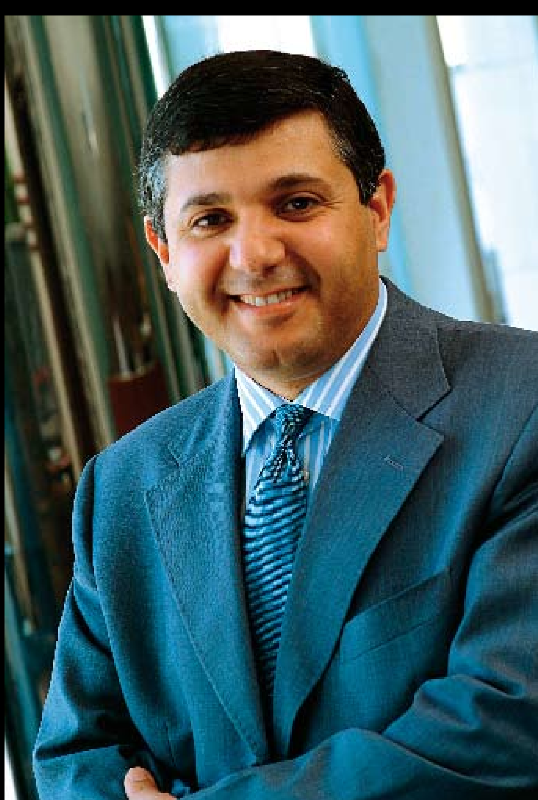
I believe insurance companies will continue to shift to "back-to-basics" models, focusing on their core underwriting business, rather than relying on investments as the main source of earnings.

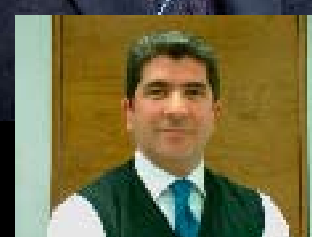
Lukas Mueller The situation in the GCC markets continues to be too competitive and current prices are not sustainable, particularly in times of financial markets turbulence

- The opportunistic reinsurance buying behaviour of cedents will not succeed in the long term
- The risk for financial lines of business such as BBB and FG will continue to increase, further underlining the necessity for annual aggregate limits per person and company
- Exposures for D&O covers are expected to go up significantly
- Moral hazard increases significantly in times of financial turbulence, especially for property and hull
- Sharing of risks by the way of facultative inward and/or co-insurance increases counter party risk
- Underwriting discipline is to be maintained or even tightened
- Alignment of interest between insurer









CLOCKWISE FROM LEFT
Yassir Albaharna, chief executive officer, Arab Insurance Group (Arig)
Gail P Norstrom, chief executive officer, Gulf Reinsurance (Gulf Re)
Lukas Mueller, head of client management for Middle East & Turkey at Swiss Re
Elias R Chedid, director, Chedid Corporate Solutions LLP
Jamil R Bahou, group managing director, Crescent Global Group

and reinsurer is key in order to maintain long-standing partnerships

Elias Chedid Once again, the practice of market forces proves to be stronger than practical logic. While insurers and reinsurers realise the importance of having to go back to basics by tilting the profitability scale in favor of underwriting profits versus investment profits… yet we have seen competition forcing soft rates in various classes of business. Rates have not properly adjusted to required levels and reinsurers have shown slightly moderate resilient positions in that regard, although they were highly affected by the financial crises.

The fact that 2009 initial estimates has not witnessed insured catastrophes and man-made disasters at the scale of 2008 (US$24bn in 2009 v US$50 in 2008 according to Swiss Re sigma), has probably led to reducing the grip on available market capacity and thus softened market rates. The only regional impact would be the final results of Jeddah, Saudi Arabia floods, as its impact on insurers and reinsurers is not yet concluded, but may affect Saudi 2010 renewals.

2010 should be the year of total risk management and continuous realignment of resources. The impact of the financial crises would carry its weight to 2010 and may be felt in talent transfer, possible premium collection delays, account cancellations, volume reduction in certain countries. Accordingly key areas to focus on by insurers would be managing risk exposure. This can be by client selection, field underwriting, contracting external consultants for the purpose of internal re-alignment of resources and processes to reduce future operating expense ratios and increase performance.

Gail Norstrom Investment risk management must be more conservative… asset diversification, liquidity management, and more rational dividend policies come quickly to mind. A sharper focus on technical underwriting is needed … profits must be made from underwriting as well as investments in order to build balance sheets.

“THE IMPACT OF THE FINANCIAL CRISES WOULD CARRY ITS WEIGHT TO 2010 AND MAY BE FELT IN TALENT TRANSFER, POSSIBLE PREMIUM COLLECTION DELAYS, ACCOUNT CANCELLATIONS AND VOLUME REDUCTION IN CERTAIN COUNTRIES”

Elias R Chedid, director, Chedid Corporate Solutions LLP

Jamil Bahou I believe the lessons learned in 2009 following the global economic crisis are numerous. The main lesson for insurers should definitely be don’t take anything for granted especially returns on investments made. Focus on your underwriting, developing and deploying better risk modelling, as well as focus on better risk management practice. Focus areas for 2010 we believe should be on differentiation, product development, and portfolio rationalisation.

WHAT DO YOU THINK WILL FUEL GROWTH IN 2010? WHAT NEW/UNTAPPED OPPORTUNITIES ARE THERE?

Yassir Albaharna The Middle East insurance market is growing and changing rapidly. Although in global terms this market is relatively small, the scope for further expansion is huge. The region offers vast opportunities for existing as well as new players and is generally expected to grow annually at more that 20 per cent in coming years. This is as a result of its low market penetration, rising awareness level, health consciousness and initiatives taken by governments of various countries in the region. Regional markets have been affected by the financial situation. However, although there has been a slow down in the markets, the region did not actually go into recession during 2009. The opportunity for 2010, therefore, remains strong. The main drivers for the Middle East insurance industry 2010 are:

- Bancassurance
- Takaful insurance whose global market is expected to grow five-fold by 2015
- The region is generally viewed as having the strongest growth dynamics over the near term. Despite economic conditions, there are still projects valued in excess of US$1.5trn in the pipeline in this region. A number of markets are supported by governments that share the determination and have the funds to aggressively develop infrastructure and industry. That creates a demand for insurance and reinsurance.

Lukas Mueller The high oil prices over the past few years have allowed most GCC countries to accumulate large capital funds

- The GCC enjoys a solid economic outlook despite the current turmoil and the slowdown of growth
- There is considerable opportunity for reinsurers across the GCC, including in the UAE, KSA and Qatar – high cession rates
- Life insurance in general has great growth potential (due to its low insurance penetration in the GCC)
- Other key growth areas include compulsory insurance, motor, medical and professional indemnity lines
- Equally, Takaful products play an important role. They still represent a small part of the market with a share of

less than 10 per cent, but are expected to expand quickly. Retakaful should benefit likewise.
• A proper asset/liability mix is crucial
• New mandatory LoB's

Elias Chedid Opportunities are always there for those who see them. Growth needs leaders who grab opportunities and transform them into profitable business. Untapped opportunities are mostly in regulatory requirements and governmental spending, matched by the market gaps in new product manufacturing and distribution methods.

Gail Norstrom I don't think there will be much insurance premium growth in 2010… certainly no more than overall GDP growth. Medical insurance may be the exception. With all the contract disputes (and fallout from these disputes) I think there will be a long- term growing awareness in the desirability of purchasing Directors and Officers (D&O) Liability insurance as well as Employment Practices Liability (EPL) insurance – although probably not in 2010.

Jamil Bahou In 2010, I believe growth will come from several areas. The first is in the employee benefits area as more and more gulf countries make health insurance compulsory.

The other hugely untapped area is individual lines, or the man on the street. We have been very active in this area, and I believe this is an area where there is growth to be made.

WITH SO MANY LINES OF BUSINESS HIT IN 2009, IS THE WORST OVER OR DO YOU FORESEE MORE BUSINESS DRYING UP?

Yassir Albaharna We would expect the markets to improve during 2010, although it will still be worse than before the current financial crisis started. In particular, marine cargo was impacted more than some other regional markets since it is a global trade. Construction and property remain more affected in the private sectors, but government plans remain broadly on track. Life and health markets were less severely hit and we would expect to see growth continue in these markets. Over all, I would expect a better 2010.

Lukas Mueller Engineering and marine were affected most by the economic crisis – these major premium contributors are no longer fuelling the market. As a consequence, competition in the remaining LoB's has substantially increased and will continue to go up and loss ratios will rise.

Elias Chedid It all depends on how you look at problems to define what is the worst. Looking at the Middle East market in general, marine insurance was surly hit in 2009. The 2010 planned projects especially, Abu Dhabi and Saudi, coupled with expected increased compulsory insurance requirements in certain GCC countries may overshadow what you described as drying up business. Compulsory insurance laws under way and those already enacted form a main mechanism for maintaining industry resonance.

Gail Norstrom Written premiums will move, at best, with the overall economy. The shortfall in projected 2009 premium writings is negatively affecting treaty reinsurance results which may put more pressure on 2010 treaty renewals.

Jamil Bahou It remains to be seen. I think all would agree that there is a lot of economic uncertainty out there. Most of the GCC seems to be in better shape with the exception of Dubai.

DOES THE QUEST FOR A HARD MARKET IN THE REGION REMAIN AN IMPOSSIBLE DREAM? WHAT CAN INSURERS DO IN THE FACE OF CUTTHROAT PRICE COMPETITION?

Yassir Albaharna Based on current trends we would expect a hardening of the market in 2010. January renewal negotiations suggest this is indeed occurring. The "dream" would remain a shallowing of or end to the cyclical nature of markets beyond 2010, especially on non life. This would require strong regulation and the implementation of disciplined underwriting and ERM practices by all in order to be achieved. The role of reinsurers is vital in this.

Lukas Mueller The Middle East has not yet experienced a hard market (not even after 9/11). As long as there is ample reinsurance capacity available and reinsurers do not put more pressure on local players to achieve a better alignment of risk, insurance companies are unlikely to change their business model – and a market hardening will not take place in the near future

Insurance companies need to stop with the current cut throat competition and differentiate themselves by the services and product offerings they provide

"THE RISK FOR FINANCIAL LINES OF BUSINESS SUCH AS BBB AND FG WILL CONTINUE TO INCREASE, FURTHER UNDERLINING THE NECESSITY FOR ANNUAL AGGREGATE LIMITS PER PERSON AND COMPANY"

Lukas Mueller, head of client management for Middle East & Turkey at Swiss Re

Elias Chedid If the market rates softening could not be controlled during a financial crisis period as the one we have witnessed, then definitely reversing the equation is not easy but not impossible. Rates are defined by risk, costs and capacity. Hardening rates depends on controlling these three. No simple answer to face cut-throat price competition. But the right direction towards harder rates would be when the major market players focus on investing in people and technology, improving risk retention and market information, diversifying portfolios between commercial and retail, focusing on service and product packaging, applying sound risk management practice.

Gail Norstrom To quote Jason Light of Emirates Insurance there will have to be "blood on the carpet" before we'll see a hard market in the GCC. This most likely would be a great cat event (>US$100bn) elsewhere in the world on top of already significant losses. Insurers in the region will keep irrationally competing until the supporting reinsurance dries up or gets smarter.

Jamil Bahou I think the quest for a hard market is indeed a dream in the absence of a catastrophic anomaly affecting global capacity.

There is no underwriting discipline in the market, too much coinsurance, and no control. The only thing insurers can do in the face of such competition is innovate.

"INSURERS IN THE REGION WILL KEEP IRRATIONALLY COMPETING UNTIL THE SUPPORTING REINSURANCE DRIES UP OR GETS SMARTER"

Gail P Norstrom, chief executive officer, Gulf Reinsurance (Gulf Re)

WHAT IS YOUR WISH LIST FOR THE LONG-TERM HEALTH AND DEVELOPMENT OF THE MIDDLE EAST INSURANCE MARKETS?

Yassir Albaharna There are many changes and developments needed in this market. However, I will limit myself to three key items on my wish list. These are:

Regulation There is substantial effort being put into insurance regulation all over the MENA region, resulting in more order and much-needed professionalism coming into an industry that appears all set to record good growth over the medium term. The regulatory authorities in the GCC are taking serious steps to regulate the insurance market. They have also demonstrated commitment to adopting international best practices. In Bahrain for instance, the CBB is boasted as setting a first-class regulatory framework uniquely in the region, and has also established a legal framework for captive insurance as well as takaful operators. The CBB is a strong and proactive regulator that frequently consults with the local industry.

Education Education applies at two levels: firstly with the population in general so they gain awareness of insurance and its purposes. This will require Government efforts as well as from the industry. Second is with the level of expertise in the insurance industry itself. Here the reinsurer and the regulator play the key role to ensure that minimum standards exist. This will increase the respect and credibility of the industry with its customers. This will be measured by the quality of selling and the retention of those risks by insurers and reinsurers alike.

Underwriting discipline Underwriting discipline comes hand in hand with the education of the insurance professionals themselves. As I have mentioned previously, the insurance industry needs to return to basic principles of insurance and not rely on investment returns. .

Lukas Mueller Although insurance regulation in the GCC has improved, it still varies widely across the region. The relative lack of regulation and supervision (compared with highly developed global markets has led to a situation where local insurance companies have taken on large investment exposures – which has boosted profits but also accounted for large losses.

- It is crucial to improve the overall transparency of the insurance sector
- Convergence between financial centres and their respective local markets and between individual GCC countries is desirable – a regulatory framework would greatly help these markets to develop
- Again, a stronger alignment of interest between insurers and reinsurers remains high on the wish list for 2010

Elias Chedid I have a simple wish for the Middle East insurance markets to operate liberally within regulatory frameworks in every single country that are set to encourage competition, moral practice and focus on setting minimum customer service standards.

Gail Norstrom A focus on underwriting including promoting the use of higher deductibles and robust risk management/loss control on the part of insurers. Less support of poorly performing treaties by reinsurers.

Jamil Bahou This one is interesting. My wish I would say for the long term health and development of the MENA market would be more regulation and supervision over insurers, brokers, and other players in addition to an accountability system that actually works.