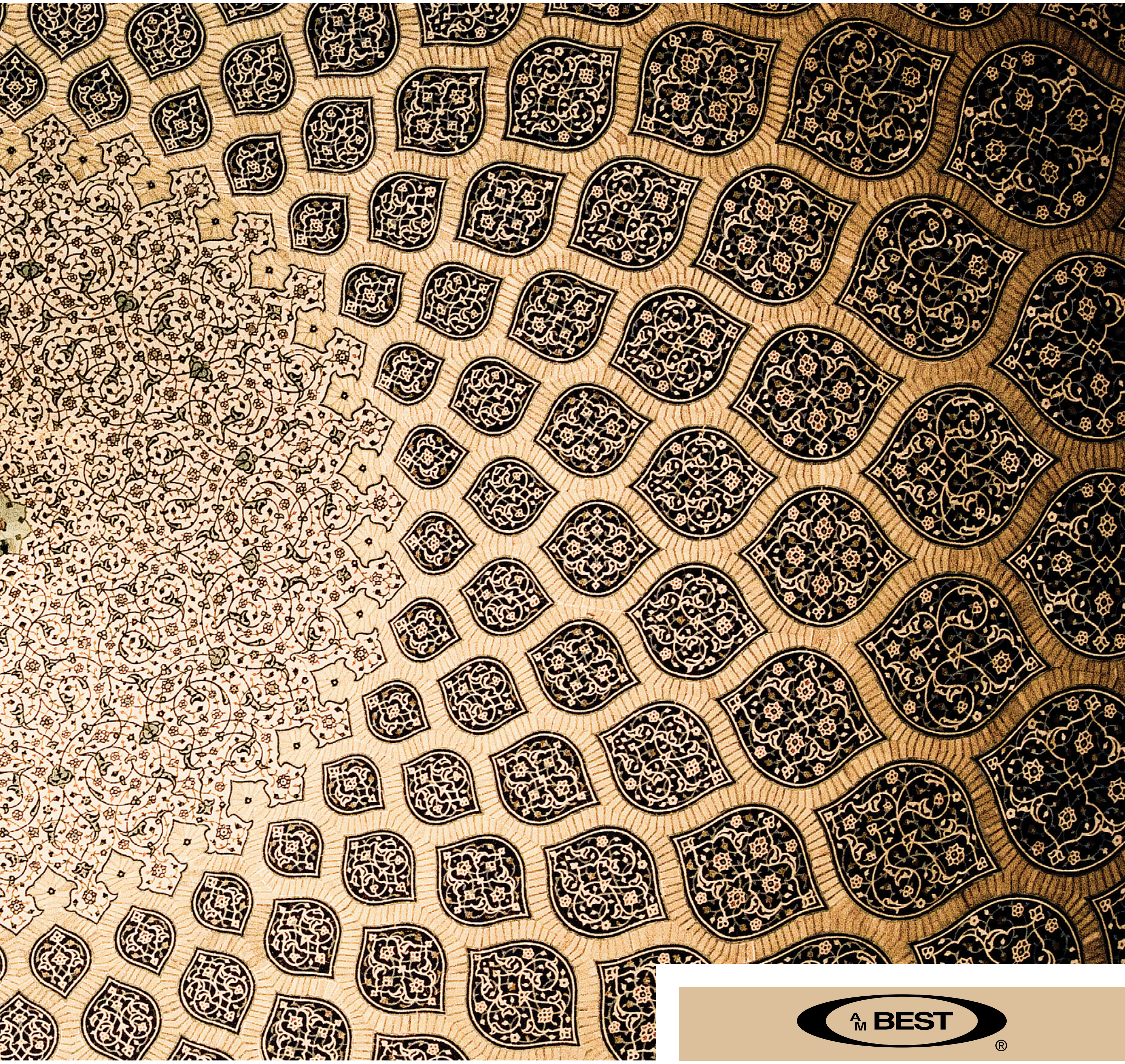
A.M. Best's

TAKAFUL REVIEW

2013 EDITION



A.M. BEST

Contents

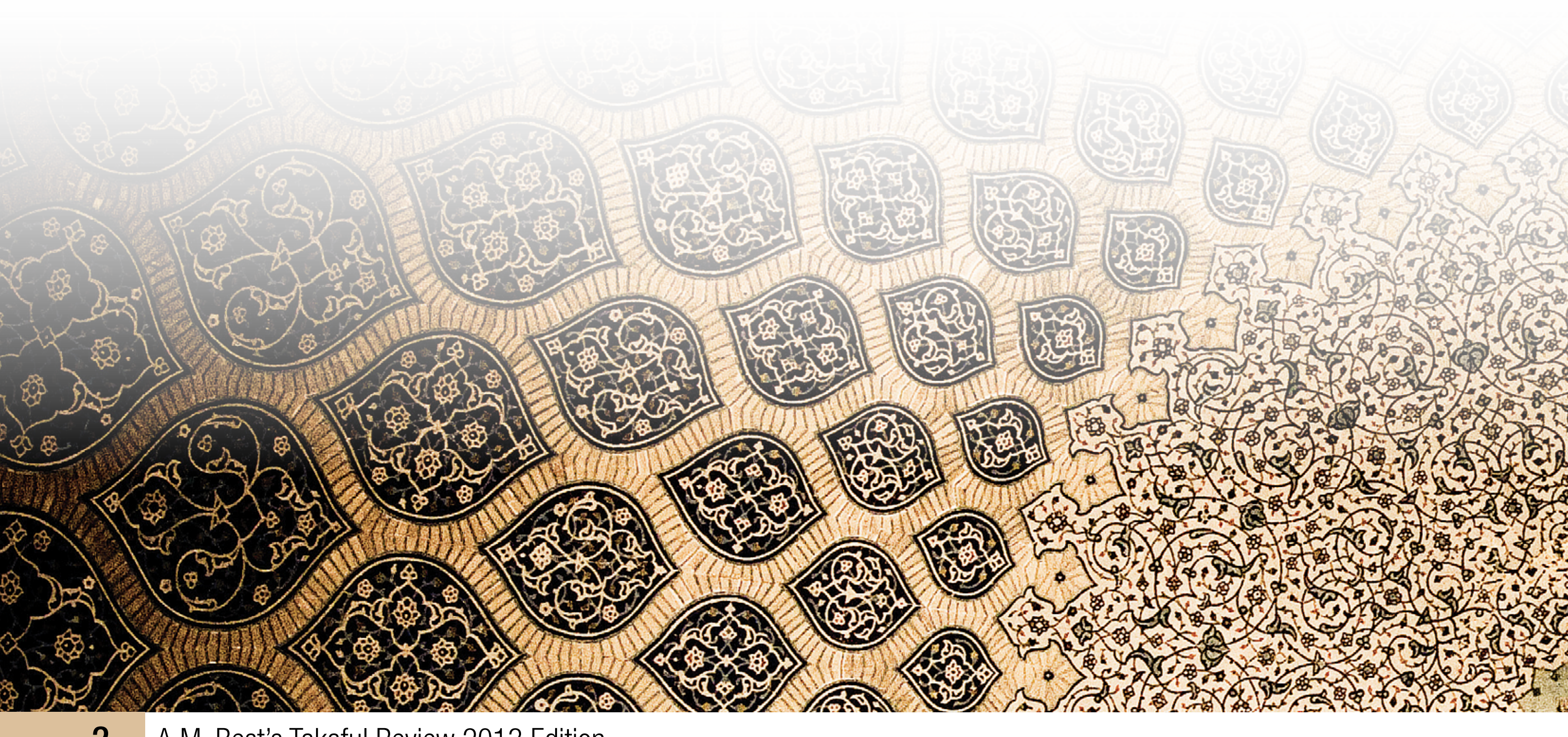
Foreword

The last 12 months have represented an important period for Takaful developments as demand for insurance compliant with Islamic beliefs clearly remains on the rise. The growth of Takaful continues, particularly in the Middle East and Malaysia, despite a prolonged period of global economic uncertainty.

While Takaful operators have enjoyed strong growth to date, the size of the sector, in many markets, is still small compared with the traditional insurance market. In the absence of a significant increase in insurance penetration, companies aim to generate material volumes and capture market share by competing on commoditised product lines. In many cases, Takaful operators are competing directly with their conventional counterparts, with pricing pressure often resulting in lower technical profitability than conventional insurers. In addition, Takaful companies continue to face more limited investment opportunities and are struggling to build up sufficient surpluses in the policyholders' fund which will negate the need for providing Qard Hassan.

Ratings are becoming increasingly important for Takaful companies in recent years in their effort to compete with more established insurers. An increasing number of Takaful companies are focusing on commercial risks and seek expansion overseas. In both cases a rating is seen as a necessary prerequisite in order to be able to compete successfully. Furthermore, 2012 was the year that some regulators in the Middle East started encouraging companies to obtain a financial strength rating, which acts as an additional safety guard in the regulatory regime.

Takaful companies share many similarities with conventional mutual operating structures, although there are also distinctive differences. In 2008, A.M. Best released its specific Takaful rating methodology. This was revised in 2012 and has been well received by practitioners as a useful framework for assessing the performance and prospects of Takaful operations. A copy of the methodology "Rating Takaful (Shari'a Compliant) Insurance Companies" can be found on page 13.



A.M. Best appreciates that the focus of rating analysis for Takaful companies is the degree of security of both participants' and operators' funds and the way they interact. While the Takaful industry has evolved rapidly in recent years, the development of Takaful regulation varies considerably by jurisdiction with the levels of policyholder protection differing from one country to another. In many instances, insurance regulators in the Gulf Cooperation Council (GCC) have been challenged by the emergence and growth of Takaful in their countries.

A.M. Best believes that a robust regulatory regime can provide sufficient policyholder protection and can be crucial in the development of a sound risk management culture. It is increasingly important for Takaful companies to develop and demonstrate that the application of a sound risk framework which will assist them in managing their business. A.M. Best's opinions on Takaful regulation within the GCC have been outlined in the special report "GCC Takaful Regulation Lags Market Growth, Creating Uneven Playing Field" (see page 4).

For A.M. Best, 2012 also represented a milestone following the opening of a new office within the Dubai International Financial Centre. A.M. Best has ratings analysts in its regional centres in London (Europe, Middle East and Africa) and Hong Kong (Asia Pacific), specialising in Takaful operations. By being physically present in the United Arab Emirates, this further demonstrates A.M. Best's commitment to insurers, reinsurers and Takaful operators in the Middle East and North Africa, South and Central Asia regions.

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GCC Takaful Regulation Lags Market Growth, Creating Uneven Playing Field

While the Takaful industry has been developing rapidly in the countries of the Gulf Cooperation Council (GCC), the development of Takaful regulation varies significantly country by country. As a result, the levels of policyholder protection differ from one state to another, which has created opportunities for Takaful operators to pursue regulatory arbitrage.

Indeed, there is significant debate as to the right level of regulation. Market participants in some of the more demanding regimes consider the regulations to be stifling their companies. A.M. Best believes the solution is not less regulation but more consistent application of regulation throughout the region, which has the potential to provide sufficient policyholder protection, and thus safeguard the long-term viability of the Takaful industry.

There are three key issues that need to be examined to establish an adequate level of policyholder protection provided by the regulatory system:

1. *Takaful-specific regulation:* Regulation tailored to the demands of the Takaful model is important, especially in recognizing the existence in Takaful of separate funds for policyholders and shareholders. This is a major difference between Takaful and traditional insurers. Regulation needs to provide the rules under which these funds interact, both during insolvency and when the company is viewed as a going concern.

2. *Obligation to provide Qard Hassan at all times:* Based on key principles of the Takaful model, operators are obliged to provide a Qard Hassan (an interest-free loan) to cover arising deficits. However, the principle leaves unclear the permanence of Qard Hassan because, as a loan, it may need to be repaid to the shareholders when it becomes evident that the Takaful fund is not viable over the long term. Regulators therefore are called to establish the rules of permanence for Qard.

3. *Policyholder priority:* This is important particularly in cases of insolvency, and in most cases, it is provided by the general law rather than the provisions established by insurance regulators.

This special report maps the provisions for Takaful regulation in the GCC and identifies the implications for policyholder protection and its impact on A.M. Best ratings.

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GCC Regulatory Landscape

Each GCC country has its own regulatory system for financial services and insurance. Furthermore, the Dubai International Financial Centre (DIFC), in Dubai, United Arab Emirates (UAE), and the Qatar Financial Centre (QFC), in Doha, Qatar, are subject to their own civil and commercial laws and are exempt from the relevant laws of the countries in which they reside. GCC regulatory regimes can be divided into three categories depending on their regulation of Takaful:

1. Jurisdictions with Takaful-specific regulation, including the UAE, the DIFC, Bahrain and the QFC.

2. The Kingdom of Saudi Arabia, where insurance legislation is applicable to both Takaful and conventional insurance companies.

3. Jurisdictions that currently make little provision for, or recognise, Takaful as a separate type of insurance in their regulatory regimes (Kuwait, Oman and Qatar, excluding QFC.

However, the regulatory landscape for the insurance sector is evolving in the GCC. Oman is expected to issue a new insurance law and Takaful regulations shortly.

Jurisdictions With Takaful-Specific Regulation

United Arab Emirates

The UAE insurance market, broadly speaking, is divided into two sectors:

1. The wider UAE market in which insurers and intermediaries are required to register with the UAE Insurance Authority; and

2. The DIFC (see below), which is regulated by the DIFC Authority (DIFCA) and the Dubai Financial Services Authority (DFSA).

The two sectors are distinct, with the UAE sector primarily concerned with direct insurance of retail customers and risks located in the UAE, and the DIFC being largely a wholesale reinsurance/Retakaful market.

UAE Federal Law 6 of 2007 (2007 UAE insurance law) established the Federal Insurance Authority to govern and issue regulations for the UAE insurance market. The 2007 UAE insurance law repealed the previous insurance legislation, *UAE Federal Law 9 of 1984* (1984 UAE insurance law). However, the 2007 legislation did not address some topics, and as a consequence, some of the regulations published under the 1984 UAE insurance law (as amended by various ministerial decisions) remain in force until they are repealed and replaced.

In 2010, the UAE Insurance Authority issued its first regulations specific to the Takaful industry (the UAE Takaful regulations), pursuant to which Takaful operations may only be undertaken by licensed Takaful companies. Article 24 (1) of the UAE insurance law requires that such entities be public joint stock companies, branches of foreign insurance companies or insurance agents. Each of these entities must be registered and licensed by the UAE Insurance Authority. Additional licensing requirements apply for health insurance in the Emirate of Abu Dhabi. Health insurance-specific legislation is expected shortly in the Emirates of Dubai and Sharjah.

Takaful operators also are required to comply with the provisions of the UAE insurance law. As such, the UAE Takaful regulations must be read in conjunction with the UAE insurance law and the implementing regulations issued from time to time by the UAE Insurance Authority.

Dubai International Financial Centre

The DIFC was established in 2004 as a financial free zone within the UAE and is subject to its own bespoke set of laws and regulations based on those of a number of different jurisdictions (including the United Kingdom and Bermuda). These include contract, employment and data protection laws, among others. The financial free zone concept allows 100% foreign ownership; exemption from the majority of the UAE's commercial laws; and independent regulation of the financial services sector by the DFSA in accordance with the DFSA Rulebook.

In general, the DIFC is a "wholesale" financial centre, from which the conduct of "retail" insurance business is prohibited. In relation to the UAE, a DIFC entity may not enter into a direct insurance contract or act as an intermediary to a direct contract for a risk based in the UAE. It is therefore intended that only reinsurance or Retakaful business in relation to UAE-based risks be conducted from the DIFC.

Establishment in the DIFC can be by way of a branch of a foreign company or a corporate entity. In each case, the establishment and authorisation process requires dual approval, from both the DIFCA and the

DFSA. The Prudential Insurance Business (PIN) Module of the DFSA Rulebook provides that the minimum capital requirement for reinsurers is USD 10 million. The DFSA has waived the requirement to maintain capital locally for branches of multinational reinsurers.

Reinsurance activities are governed principally by the PIN. However, the DFSA has a specific module relating to all types of Islamic financial business, including Retakaful business, set out in the Islamic Financial Rules (IFR) module. Any person wishing to undertake Retakaful business must have an endorsement to undertake Islamic financial business, in addition to being authorised to effect and carry out contracts of insurance.

The Kingdom of Bahrain

All financial institutions, including Takaful and Retakaful operators, are subject to the supervision of the Central Bank of Bahrain (CBB). The CBB publishes a rulebook, Volume 3 of which deals with insurance and includes a specific Takaful module. The CBB Rulebook supersedes *Legislative Decree 17 of 1987* and *Ministerial Order 6 of 1990*, which set out regulations to implement Bahrain's insurance law. *The Central Bank of Bahrain and Financial Institutions Law 2006* (Central Bank law) provides that the rules and regulations of the prior laws remain in force as long as they do not contradict the Central Bank Law (Article 4).

Takaful and Retakaful operators can be established as a branch of a foreign entity or a Bahrain joint stock company. The CBB Rulebook's capital adequacy module (CA) provides that an insurance company whose business is limited to reinsurance must maintain Tier 1 capital of BD 10 million (USD 26 million). For a branch, no minimum capital requirements apply, but solvency margin requirements are based on the Takaful operator's parent company. For a branch office, the CBB requires written confirmation from the head office to provide financial support to meet its obligations. Retakaful operators are required to maintain BD 150,000 (USD 400,000) as a cash deposit with a commercial bank licensed to do business in Bahrain. The CBB Rulebook (GR 7.2) further states that a subsidiary (but not a branch) has to maintain a compulsory reserve of a proportion of its annual profits, being no less than 10% of annual profits until the balance of such compulsory reserve equals 50% of the paid-up capital.

Qatar Financial Centre

The Qatar Financial Centre Regulatory Authority (QFCRA) is the body specifically set up in order to regulate entities within the QFC and is charged with implementing the QFC regulatory framework, pursuant to *Qatar Law No. 7 of 2005* (QFC law). The QFCRA has issued a rulebook that governs the authorisation and continuing supervision of all entities established in the QFC, including those operating as authorised firms and carrying out regulated activities, and the authorisation of approved individuals. The Prudential Insurance Rulebook (PINS) governs the operations of insurers established in the QFC and includes specific provisions relating to Takaful operators in Chapter 6. In addition, the QFCRA has laid down provisions and rules for Takaful operators in the Islamic Finance Rulebook (ISFI) module applicable to entities located in the QFC. However, PINS also contains a separate section titled "Additional Requirements for Takaful Entities" that applies to Islamic financial institutions and Islamic windows.

A Takaful or Retakaful operation may be established by way of the registration of a foreign branch, as well as the incorporation of a limited liability company (LLC) or limited liability partnership (LLP). A protected cell company structure is also available, although this normally would be used for captive insurers. With regard to an LLC or LLP, PINS Rule 3.4 provides that base capital requirements are USD 10 million for establishing a Takaful operation and USD 20 million for establishing a Retakaful operation.

Jurisdiction Where Legislation Applies to Takaful and Conventional Insurance

The Kingdom of Saudi Arabia

The Saudi Arabian Monetary Agency (SAMA) is the regulator of the Saudi Arabian insurance market. SAMA has mandated that all insurance companies be established in a "cooperative" manner. SAMA also directs cooperative insurance companies to distribute 10% of net insurance surplus to policyholders directly or in the form of a reduction in premiums for the following year. The remaining 90% of the net surplus is transferred to the shareholders. SAMA also mandated all insurance companies (existing and new) obtain a license by March 2008 to underwrite business or exit the market. Notably, to obtain a license, an insurer must be established as a joint stock company and invest at least 20% of policyholder funds in government bonds and 20% in bonds issued by Saudi-authorized banks.

The cooperative insurance model in the Kingdom of Saudi Arabia is conceptually distinct from Takaful. Although it involves the concept of distribution of surplus and is therefore deemed to be Shari'a compliant, it does not include provisions relating to the segregation of Takaful funds from shareholder funds; a requirement to invest in a Shari'a compliant manner; or the appointment of Shari'a boards. This does not prevent several Saudi companies from having segregated fund information and appointed Shari'a boards, etc. Even for companies with segregated fund information, any deficit in the policyholders' fund is recompensed from the shareholders' fund without the mechanism of Qard Hassan. Most, if not all, licensed Saudi insurers offer Takaful products, especially in the context of life insurance (family Takaful) and there are reported to be five entities operating purely on a Takaful model.

SAMA has discouraged Takaful operators from using specialist nomenclature in their accounts so as to ensure comparability with other local insurers' published accounts. As a consequence the wakala, mudarabah and Qard Hassan arrangements are "hidden" in accounts. Nevertheless, commentators have suggested that such Takaful operators continue to have competitive advantages over their counterparts in the kingdom.

Jurisdictions Without Specific Takaful Regulation: Kuwait, Oman and Qatar (Excluding QFC)

The jurisdictions in which there is no explicit regulation of Takaful are Kuwait, Oman and "onshore" Qatar (i.e., outside the QFC). The insurance legislation in each of these jurisdictions is relatively old and therefore predates the development of the commercial Takaful market. Thus:

1. The Ministry of Commerce and Industry regulates the Kuwaiti insurance market in accordance with *Law No. 24 of 1961* (Kuwait insurance law).

2. The Capital Market Authority (CMA) regulates the Omani insurance market in accordance with the Insurance Companies Law (Royal Decree 12/79) (Oman insurance law).

3. *Decree Law No. 1 of 1966* (Qatar insurance law), which establishes the legislation that governs insurance activities in Qatar, has not evolved significantly since its promulgation. Qatar differs from Kuwait and Oman insofar as the development of the QFC as a hub for the insurance sector has, to some degree, rendered the "onshore" regulations obsolete. Although theoretically the Minister of Business and Trade supervises the "onshore" market, in practice the sector has seen limited regulatory supervision. Newspaper articles have reported that the Qatar Central Bank (QCB) will act as the insurance regulator once forthcoming draft insurance legislation is enacted. However, there are also reports of a merger of the supervisory bodies of the State of Qatar and the QFC, with the result that the insurance business in the State of Qatar may be submitted to the regulatory supervision of the QFCRA and to the QFC rules and regulations that apply in this respect. It is therefore not clear how any upcoming changes will affect the local insurance market.

Oman is in the process of updating the laws and regulations applicable to the insurance sector, and a new insurance law and specific Takaful regulation are being finalised.

Similar developments are expected in Kuwait, where a new insurance law is reported to have been prepared but is yet to be tabled in Parliament. The new insurance law is expected to increase the minimum capital requirement for insurers to USD 55 million from the current USD 525,000 for local insurers. The new law also is expected to carry a separate code for Takaful companies, focusing on areas such as policyholders' funds, Qard Hassan and the Shari'a supervisory board, among others.

Policyholder Protection

For the purposes of an A.M. Best rating, the protection available to a Takaful company's policyholders is a material consideration. The following section considers some of the legal and regulatory aspects of such protection:

Availability of Qard Hassan

If a Takaful fund runs a deficit, the Takaful operator may be required to provide an interest-free loan (Qard Hassan) from its shareholder funds to make good the shortfall. This is described by the Auditing and Accounting Organisation for Islamic Financial Institutions (AAOIFI) in Shari'a Standard No. 26 (Islamic Insurance) paragraph 10/8 as follows:

> *Where the insurance assets along with indemnities received from re-insurance companies fall short of covering indemnity commitments, the Company may cover the deficit from project financing or Qard Hassan (interest free or benevolent loan) debited to the account of the insurance fund. In this regard, the deficits resulting from commitments of the current year may be covered from the surpluses of the succeeding years. The company may also claim settlement of the deficit from the policyholders if they undertake to do so in the insurance policy.*

An operator's fund with much higher financial strength than its corresponding Takaful fund normally will enhance the capitalisation assessment in respect of the whole insurance operation, reflecting the increased financial strength provided to the Takaful fund's participants. This enhanced financial strength stems from the operator's obligation to provide the Qard Hassan to the Takaful fund in situations of financial distress. From a ratings perspective, whether the provision of Qard Hassan is mandatory under the applicable Takaful regulations is a material consideration when rating a Takaful company.

The provision of Qard Hassan is mandatory in the UAE. Article 9 of the UAE Takaful Regulations explicitly provides that the subscription document issued by the Takaful company to its participants must include the company's commitment to provide such a loan. This is reinforced by Article 28 (1), which provides that such loan must be provided and is limited only by the amount of the shareholders' equity in the Takaful company. A failure to provide Qard Hassan may result in the suspension of the Takaful company's activities by the insurance authority (Article 28 (4)).

An equivalent provision is contained in the CBB Rulebook's CA Section 8.4.5, which provides that where a Takaful fund is failing to meet the requisite solvency requirements, the Takaful company must increase the capital of the fund by way of Qard Hassan. Such Qard Hassan may only be provided with the prior consent of the CBB (CA Section 8.4.9). In addition, CA Section 8.5.1 provides that:

> *Every takaful firm must develop a policy for determining the surplus or deficit arising from takaful operations, the basis of distributing that surplus or deficit between the participants and the shareholders, and the method of transferring any surplus or deficit to the participants. The policy developed must consider all relevant AAOIFI standards including Financial Accounting Standard No. 13 'Disclosure of Bases for Determining and Allocating Surplus or Deficit in Islamic Insurance Companies'.*

In contrast, in the QFC, the details of how a deficit is to be treated are required to be set out in a written policy, and the actual treatment disclosed by an operator in its financial statements in accordance with the AAOIFI FAS 13 (QFCRA Insurance Business Rules 2006 [PINS] Section 6.6.1). Such policy must be provided to the QFCRA, may not be amended without the QFCRA's approval and must be included with the insurance policies sold by the Takaful operator.

Insolvency Protection

There remains an inherent lack of transparency in certain jurisdictions concerning liabilities upon the winding up of a Takaful company. The relative youth of the Takaful industry exacerbates this issue, as there are no recent examples of how Takaful companies have been wound up.

The UAE insurance law (Article 95) provides that the debts and liabilities of an insurance company (including Takaful companies) will be settled in a specified order, whereby the rights of insurance beneficiaries under insurance policies are to receive priority over the ordinary creditors and shareholders of the Takaful company. The technical provisions established by the Takaful operator are to be allocated for this purpose.

Similarly in the DIFC, the DIFC Insolvency (Insurers) Regulations (Article 2.2) provide that "Insurance Debts," to which "an insurer is or may become liable pursuant to a contract of insurance, other than a contract of reinsurance, to a policyholder or other person who has a direct right of action against that insurer…" will rank above the ordinary creditors of the Takaful company.

There are no equivalent provisions in the QFC insolvency regulations, CBB Rulebook and Financial Institutions Law 2006 or under Saudi insurance law.

In Kuwait, the position is unclear as there are no provisions of the Kuwait Civil Code concerning priority of policyholders' claims, other than in respect of the return of premium.

In Oman the issue is under consideration. The current insurance law issued by Royal Decree No. 12/79 does not address policyholder protection in the provisions relating to insolvency of insurance companies. However, A.M. Best understands that the forthcoming insurance law will provide for policyholders to have priority over the ordinary creditors of such entities.

Permanence of Qard Hassan

Qard Hassan, by its nature, is a loan and therefore is expected to be repaid by future profits of the Takaful fund. Absent a binding legal commitment, either in the Takaful legislation of a jurisdiction or in the Takaful policy with regard to the repayment, there is potential risk that the additional funding provided by Qard Hassan could be withdrawn when it is most needed.

Best practice, as reflected in the AAOIFI standards, provides that "the deficits resulting from commitments of the current year may be covered from the surpluses of the succeeding years." It follows, therefore, that the Qard Hassan should be recouped only if the Takaful fund generates a surplus; it should not be repayable in the event of a continuing deficit.

This principle is reflected in the UAE Takaful regulations, which provide at Article 28 (3):

> *The company may recover such loan from the surplus achieved in the next periods whether in one or more payments as decided by the company in general assembly.*

In the QFC, the above principle must be reflected in the policy or policies to be established pursuant to QFCRA Rulebook PINS Module Section 6.6.1. As these policies must be consistent with AAOIFI standards, this would include an obligation only to recoup Qard Hassan when the Takaful fund is in surplus.

The CBB in Bahrain takes a similar approach; the policies governing Qard Hassan must take into account the AAOIFI standards. In addition, the CBB's approval for the issuance of Qard Hassan and the requirement to include a note in the financial statements of the Takaful operator will compel public disclosure that the Qard Hassan will be recouped only from future surplus.

There is no direct equivalent to the above provisions in the DFSA Rulebook. However, in practice, the DFSA will require the policies and procedures of the Takaful operator to address this issue, and variations from the AAOIFI standards will need to be justified.

In jurisdictions that do not have specific Takaful legislation, an issue may arise as to the permanence of the Qard Hassan. A.M. Best is aware of no cases in which a Takaful operator has been subject to an insolvent winding up. A.M. Best would, however, expect the insolvency laws to be applied (as opposed to the priority of debtors being determined by Shari'a scholars). Typically, shareholders' rights will be subordinate to the Takaful operator's ordinary creditors.

Subordination Between Takaful Funds

Where a Takaful operator manages multiple Takaful funds, an additional issue arises as to whether a surplus in one fund can be utilised to subsidise a deficit in another fund. With the notable exception of the QFCRA Rulebook, this issue is not addressed directly in the region's Takaful regulations. It is submitted that such subsidisation is inconsistent with the mutual nature of a Takaful fund whereby the participants share the risk. The QFCRA Rulebook PINS Module, Section 6.5.1, therefore expressly prohibits loans from one Takaful fund to another.

Analysing a Takaful Company – Two-Stage, Risk-Based Capital Approach

Given that one of the key characteristics of a Takaful operation is the existence of two separate funds (the Takaful fund and the operator's fund), the starting point for assessing a particular insurance company's financial strength is to apply Best's Capital Adequacy Ratio (BCAR) proprietary model to the Takaful fund in a way very similar to a mutual company.

This first-tier analysis compares the Takaful fund's surplus to the capital required to support the fund's obligations to participants, per the BCAR model. The BCAR ratio for the Takaful fund, as well as an analysis of trends in the ratio and other key metrics, are the primary drivers of A.M. Best's assessment of the Takaful company's balance sheet strength.

A second-tier capital assessment also is performed on the operator's fund. This second-tier analysis compares the surplus position of the operator's fund to the capital required to support the fund's obligations, per the BCAR model. An operator's fund with much higher financial strength than its corresponding Takaful fund normally will enhance the capitalisation assessment of the whole insurance operation, reflecting the increased financial strength provided to the Takaful fund's participants. This enhanced financial strength stems from the operator's obligation to provide an interest-free loan (Qard Hassan) to the Takaful or policyholders' fund in situations of financial distress. In cases where such a loan has been made to the Takaful fund, the loan will be considered part of the fund's capital base. Additionally, in circumstances where the potential Qard' Hassan (dependent on strength of regulation) is not sufficient to bring the Takaful fund to a suitable capital adequacy level, consideration will be given for shareholders' commitment to the Takaful fund, such as ring-fencing assets in favour of policyholders.

This consolidated view of capital, in effect combining the Takaful and operator's fund for analytical purposes, is particularly important in the assessment of Takaful insurers in the early years of operation. Currently, it is not uncommon for the operator's fund to be in a stronger relative position, given the relatively short track record of most companies, with the resulting low level of surpluses, if any, accumulated at a Takaful fund level. An operator's fund with a weaker financial position may not detract from the overall analysis significantly, since the operator's fund cannot access the Takaful fund surplus. However, in all cases, regardless of which fund is in a stronger relative position, it also is important to compare the capital accumulation trends in each of the separate funds to ensure an appropriate balance in the surplus distribution and fee structure.

Regulation is extremely important in A.M. Best's assessment of Takaful companies. Where regulation is deemed to be weak or unclear, benefit can be given for additional commitments to the Takaful fund from shareholders in favour of policyholders, such as ring-fenced assets, which will be made explicit in A.M. Best's analysis of a company. Additionally, A.M. Best considers the role of the Shari'a board within the organization and any potential differences with regulators on winding up a company. Moreover, A.M. Best believes some of the regulatory safeguards (e.g., ring-fencing of assets within the Takaful fund) are yet to be tested.

The development of the Islamic insurance industry, including the regulatory environment, needs to keep pace with the rest of the financial industry in the GCC region (especially banking).

A.M. Best believes a robust regulatory regime can provide crucial assistance in the development of a sound risk management culture. A.M. Best also believes that given their constraints, Takaful companies need to develop and demonstrate that they can apply an adequate risk–based approach to investment management (because of the reduced investment opportunities); capital adequacy and reserving (given the need for building up surpluses in the long term, especially for family/life business); and control over pricing and adverse selection (given the restrictions on charging extra risk premiums for policyholders representing a greater risk of loss than the aggregate participant pool).

Regulatory Impact in Ratings of Takaful Companies

The regulatory frameworks of the GCC countries clearly provide different levels of policyholder protection for Takaful companies.

The two offshore centres of DIFC and QFC, as well as Bahrain and the UAE, seem to provide the clearest definitions and a more comprehensive set of provisions for the protection of policyholders. In these cases, there is a specific Takaful regulation in place, taking into account the particulars of the Takaful model. The provision of Qard Hassan as a method of support from the policyholders' fund to the Takaful fund is either part of the regulation or included in the contractual agreement between the insured and the insurance company, as the shareholders' fund is obligated to make this loan permanent, if need be. In DIFC and UAE there is the added benefit of clarity in that policyholder liabilities rank senior to any other obligation of the insurance company. The shareholders' fund therefore is obliged to provide up to 100% of its funds for the protection of policyholders. In this case, the shareholders' fund supports, in its totality, policyholder liabilities.

By contrast policyholder protection is unclear in the countries where there is no specific regulation for Takaful companies. Here, the provision of support from the shareholders' fund to the Takaful fund can depend only on the contractual agreement between the company and the policyholders. Similarly, it is

Exhibit 1
Takaful Life & Non-Life – Jurisdictions With/Without Takaful-Specific Regulation

Countries	Takaful-Specific Regulation in Place	Obligation To Provide Qard Hasan	Permanence of Qard Hasan	Policyholder Priority
Bahrain	Yes	Yes	Yes	No Provision
Kingdom of Saudi Arabia	No[1]	No[2]	No	No Provision
Kuwait	No	No[2]	No	Unclear
Oman	No	No[2]	No	Unclear
Qatar	No	No[2]	No	Unclear
United Arab Emirates	Yes	No[2]	No	Most Senior
Free Zones				
Dubai International Financial Centre	Yes	No[2]	No	Most Senior
Qatar Financial Centre	Yes	Yes	Yes	No Provision

[1] In the Kingdom of Saudi Arabia the same regulation applies to traditional and Takaful companies
[2] No regulatory obligation to provide Qard Hasan but Qard Hasan is always part of the contractual agreement
Source: A.M. Best/Clyde & Co. research

unclear as to how permanent such support can be, or indeed the priority of policyholder liabilities in case of insolvency. It is therefore important, in these regimes, to focus on the specifics of the company when evaluating the strength of a Takaful company in such regimes. This takes the form of:

a. The two-level analysis mentioned above and

b. Any additional support the shareholders' fund provides to the Takaful fund. Forms of such support can be segregation of assets for the benefit of shareholders; contractual recognition of the seniority of policyholder liabilities; and the obligation to provide permanent Qard Hassan, etc.

Conclusion

In many instances, GCC insurance regulators have failed to keep up with the emergence and growth of Takaful in their countries. The specificities of the Takaful model mean that the general insurance regulation fails to provide sufficient protection to policyholders of insurance companies. This obviously creates risks not only for specific companies but for the prospects of the Takaful industry, which despite its strong growth to date, is still small compared with the traditional insurance market.

Takaful operators that need to provide sufficient support to their policyholders are required to establish complex and expensive safeguards, e.g., ring-fencing of assets to mitigate the weaknesses of some regulatory regimes.

It is therefore important for both the success of the nascent Takaful operators and for the broader viability of Takaful that regulators develop coherent provisions for the industry. These should be tailored to the specifics of the Takaful model and provide strong policyholder protection.

PUBLISHED: JANUARY 10, 2012

Rating Takaful (Shari'a Compliant) Insurance Companies

This report highlights the main issues arising when applying A.M. Best's rating methodology to takaful insurance companies. Takaful insurance (or insurance compliant with Islamic beliefs) is clearly on the rise, particularly in the Middle East and Malaysia, and despite their many similarities with conventional mutual operating structures, A.M. Best believes there are distinctive issues with these companies that need to be highlighted. However, it is important to mention that the main principles on which A.M. Best's financial strength methodology are based remain unchanged, regardless of the type of company being analysed.

As is discussed later, each takaful company must establish a Shari'a board that sets the basic rules and principles governing the takaful company's activities, and ensuring that it operates within Islamic Shari'a principles. A.M. Best will not specifically comment on takaful companies' degree of compliance with Shari'a. However, as part of the interactive rating evaluation, A.M. Best will discuss items such as: the organization's corporate and management structure; the type of takaful business model employed; corporate governance and the role of the Shari'a board; and the insurer's performance versus key strategic and financial objectives. For further information on the breadth and depth of the rating evaluation, please refer to Appendix 1 – Sample Takaful Meeting Agenda.

The discussion that follows includes: a review of some of the key principles of takaful; how these principles are incorporated into a takaful company's business model; and how A.M. Best's rating methodologies are applied in the assessment of these organizations.

Principles of Takaful

The first takaful insurer was established in Sudan in 1979, and the market now has grown to comprise roughly 200 companies, including "windows" (operations affiliated with conventional insurers). Takaful includes both general (non-life) and family (life) products. The family product line includes life and health insurance plans, as well as education, accident and travel medical plans. The surge of takaful companies in recent times is a response to the commonly accepted incompatibility between Islamic beliefs and the conventional insurance model.

Takaful insurance is essentially a cooperative risk-sharing program established for the well-being of the community. The purpose of this system is not to generate profit, but to uphold the Islamic principle of Al-Takaful – "bear ye one another's burden." As a result, takaful insurance is based on the concept of mutual cooperation, solidarity and brotherhood. Takaful participants contribute (donate) to help protect one another against the impact of unpredicted risk and catastrophe, whereas in the conventional insurance model, policyholders pay premiums to protect themselves, or their interests, from some form of risk.

Other Islamic beliefs or principles that takaful operations intend to address are the avoidance of both uncertainty, particularly in terms of the amount and timing of claim payments to be made; and excessive profit (seen as usury), be it in the form of payments received in the event of death, or any form of financial interest (e.g., bond coupon payments).

Underwriting and actuarial techniques apply in a similar manner as under conventional insurance, in that the takaful insurer evaluates the risk of potential

ADDITIONAL INFORMATION

CRITERIA:

Rating European Mutual Insurers

Understanding Universal BCAR

A.M. Best's Perspective on Operating Leverage

Risk Management and the Rating Process for Insurance Companies

Assessing Country Risk

Rating Members of Insurance Groups

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loss and establishes a contribution (premium) base appropriate for that aggregate risk to protect the pool from undue losses. However, unlike the risk-based premium paid by a policyholder in a conventional insurance model (where each insured pays a rate commensurate with the assumed level of risk), each takaful participant shares equally in supporting the pool in recognition of the underlying principle of mutual cooperation.

As to reinsurance, it also should be based on the takaful pooling concept. The reinsurer should act primarily as a risk manager (retakaful operator) and should not profit excessively from the underwriting results. However, because of the relative lack of capacity and quality of true retakaful carriers, reinsurance with conventional reinsurers may be permitted under certain specified conditions and limitations.

Takaful Models & Structures

For takaful programs to be financially sound over the long term, as well as to provide incentive to takaful insurers to develop and promulgate these programs to provide Muslims with alternatives to conventional insurance, these operators to some degree must be rewarded through profits in a more traditional sense. However, profits are not the end goal of the operation.

Muslims believe there is unity in diversity, so there is not one preferred operating model for takaful insurers. Shari'a scholars generally agree on certain fundamental components that are required to be an accepted takaful company; however, operational differences are tolerated as long as there is no contradiction to any essential religious tenets. There are now three primary operating models.

Ta'awuni Model

The Ta'awuni model (cooperative insurance) practices the concept of pure Mudharabah in daily transactions, where it encourages the Islamic values of brotherhood, unity, solidarity and mutual cooperation. In the pure Mudharabah concept, the takaful company and the participant share the direct investment income, while the participant is entitled to 100% of the surplus, with no deduction made prior to the distribution.

From the Ta'awuni concept, there are two basic models, Al Mudharabah and Al Wakalah. In reality, there are many variations of these basic models, but these variations fundamentally follow one of these two conceptual frameworks.

Retakaful Capacity and Financial Security Issues

Reinsurance following the same applicable Islamic principles as takaful insurance is known as retakaful. Reinsurance of takaful business through retakaful companies has been somewhat controversial within the Islamic insurance marketplace, as the growth of direct takaful writers has far outpaced the available capacity of retakaful. In addition, from a financial strength perspective, there have been ongoing concerns over the placement of reinsurance with lower or non-rated retakaful companies, as opposed to higher rated conventional reinsurers. As a result, takaful insurers in effect face issues with both retakaful capacity and financial security.

This has caused takaful companies to develop alternate strategies, including reinsuring on a conventional basis, contrary to the preference of seeking retakaful support. In recognition of this market reality, the Shari'a scholars have allowed takaful companies to seek support from conventional reinsurers under confined conditions. However, the preference still is to utilize retakaful companies whenever possible. Another manner in which takaful insurers have addressed the issue of retakaful capacity is to co-insure (a form of reinsurance) each other's direct takaful writings to reduce the heavy reliance on conventional reinsurance support.

The shortage of retakaful capacity may inhibit the growth of the takaful industry; however, A.M. Best has observed that the issue of retakaful capacity has begun to ease recently as an increasing number of new retakaful companies are being established in response to the market demands. As part of the rating evaluation, as with any insurer, A.M. Best will review the takaful insurer's reinsurance program and the quality and diversity of its reinsurance providers, including the exposure to counterparty credit risk.

Al Mudharabah. This is a modified profit- and loss-sharing model. The participant and the takaful insurer share the surplus. The sharing of such profit (surplus) differs based on a ratio mutually agreed between the contracting parties. Generally, these risk-sharing arrangements allow the takaful insurer to share in the underwriting results from operations, as well as the favourable performance returns on invested premiums.

Al Wakalah. This is a fee-based model. Cooperative risk-sharing occurs among participants where a takaful insurer simply earns a fee for services (as a Wakeel, or "Agent") and does not participate or share in any underwriting results. The insurer's fee may include a fund management fee and a performance incentive fee.

Waqf Model

Unlike the Al Mudharabah and Al Wakalah models, Waqf operates as a social/governmental enterprise, and programs are operated on a nonprofit basis. Under the Waqf model, the surplus or profit is not owned directly by either the insurer or the participants, and there is no mechanism to distribute the surplus funds. In effect, the insurer retains the surplus funds to support the participant community.

This model, with a single surplus fund, is most like a conventional mutual insurance model. As such, it is rated in a very similar manner to conventional mutuals. For further information on the rating dynamics of mutual insurance companies, please see A.M. Best's "Rating European Mutual Insurance Companies."

The remainder of the report will highlight the unique elements of takaful companies following the Ta'awuni model, and how these factors are incorporated in the rating analysis.

Main Characteristics of Takaful Companies

Takaful insurers have certain unique characteristics that recognize the key principles of Al-Takaful and fundamental Islamic beliefs.

The establishment of two separate funds: A takaful (or policyholders') fund and an operator's (or shareholders') fund. The takaful fund operates under pure cooperative principles, in a very similar way to conventional mutual insurance entities. Underwriting deficits and surpluses are accrued over time within this fund, to which the operator has no direct recourse. As a result, the takaful fund effectively is ring-fenced and protected from default of the operator's fund. Management expenses and seed capital are borne by the operator's fund, where the main income takes the form of either a predefined management fee (to cover costs) or a share of investment returns and underwriting results (or a combination of both).

Solidarity principle and equal surplus distribution: Given the fact that the takaful fund is seen as a pool of risks managed under solidarity principles, it is not meant to accumulate surpluses at levels excessively higher than those strictly needed to protect the fund from volatile results and to support further growth. Likewise, any fees or profit shares received by the operator should be just sufficient to cover management and capital costs while keeping the company running as an ongoing concern.

In case of financial distress for the takaful fund, the operator is committed to provide it with an interest-free loan, Qard' Hasan, for however long it is deemed necessary – providing an additional layer of financial security to the participants. The Qard' Hasan is likely to be limited to the available capital in the operator's fund or a prescribed limit.

The surplus distribution structure is expected to be managed carefully and in a balanced way, so that neither policyholders nor operator make excessive profits at the expense of the other party.

Restricted investments: Shari'a compliance refers not only to the operational structure of the company, but also to its investment policy. Takaful companies must avoid investing in traditional fixed-income securities (due to the coupon interest payment attached). Instead, they are allowed to invest in sukuk (or Islamic bonds, where coupon payments take the form of a profit share on a particular enterprise). Moreover, investments in stocks (in principle allowed) should avoid the financing of non-Islamic activities (such as alcohol or gambling).

In practice, these restrictions often translate into an excessive concentration in stocks (due to the relative scarcity of sukuk), lower than average credit ratings (increased counterparty exposure) and high geographical concentration.

Establishment of a Shari'a board: An essential component in a takaful company's corporate governance is the establishment of a Shari'a board, in addition to the conventional board of directors. The Shari'a board is made up of recognised Islamic scholars, who ensure the company's operational model, profit distribution policies, product design and investment guidelines comply with Islamic principles.

The global shortage of recognised Islamic scholars in the insurance arena and lack of consensus in terms of what constitutes Shari'a compliance is, in A.M. Best's view, a challenge for more rapid development of the industry. Having said this, the emergence of some inter-regional and government-supported initiatives in this respect, as well as the participation of individual scholars in more than one Shari'a board, are positive signs of a gradual but slow trend toward convergence.

Analysing a Takaful Company

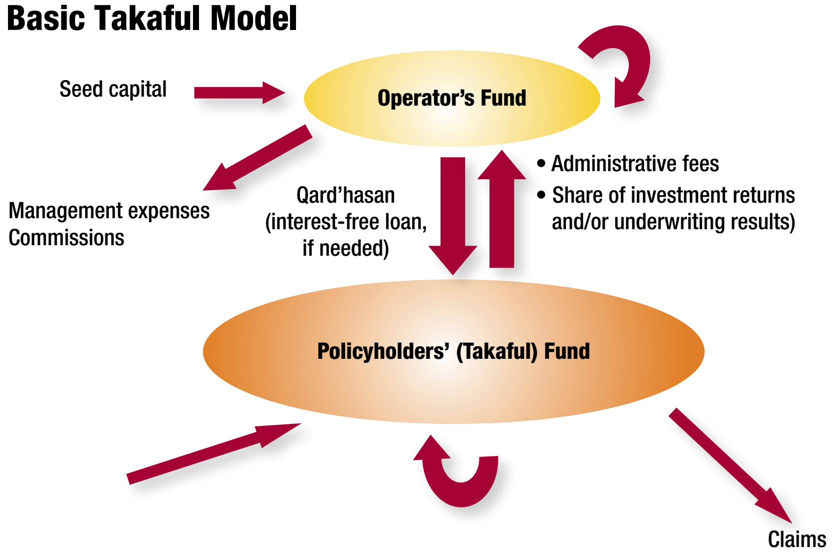
As with conventional mutual insurance companies, takaful insurers have certain limiting features inherent to their business model, such as a relative lack of financial flexibility compared with stock companies, or increased concentration risk compared with broadly diversified insurers. This section discusses some unique elements of takaful insurers and how these are assessed in the rating process.

Two Separate Funds – a Two-Stage Risk-Based Capital Approach

Given that one of the key characteristics of a takaful operation is the existence of two separate funds (the takaful fund and the operator's fund), the starting point for assessing the financial strength of a particular insurance company is to apply Best's Capital Adequacy Ratio (BCAR) proprietary model to the takaful fund in a way very similar to a mutual company.

This first-tier analysis compares the takaful fund's surplus to the capital required to support the fund's obligations to participants, per the BCAR model. The BCAR ratio for the takaful fund, as well as an analysis of the trends in the ratio and other key metrics, is the primary driver of A.M. Best's assessment of the takaful company's balance sheet strength.

Exhibit 1
Basic Takaful Model



A second-tier capital assessment also is performed on the operator's fund. The second-tier analysis compares the surplus position of the operator's fund to the capital required to support the fund's obligations, per the BCAR model.

An operator's fund with much higher financial strength than its corresponding takaful fund normally will enhance the capitalisation assessment in respect of the whole insurance operation, reflecting the increased financial strength provided to the takaful fund's participants. This enhanced financial strength stems from the operator's obligation to provide an interest-free loan (Qard' Hasan) to the takaful or policyholders' fund in situations of financial distress. In cases where such a loan has been made to the takaful fund, the loan will be considered part of the takaful fund's capital base. Additionally, in circumstances where the potential Qard' Hasan (dependent on strength of regulation) is not sufficient to bring the takaful fund to a suitable capital adequacy level, consideration will be given for shareholders' commitment to the takaful fund, such as ring fencing assets in favor of policyholders.

This consolidated view of capital, in effect combining the takaful and operator's fund for analytical purposes, is particularly important in the assessment of takaful insurers in the early years of operation. Currently, it is not uncommon for the operator's fund to be in a stronger relative position, given the relatively short track record of most companies with the resulting low level of surpluses, if any, accumulated at a takaful fund level.

An operator's fund with a weaker financial strength position may not detract from the overall analysis significantly, since the operator's fund cannot access the takaful fund surplus. However, in all cases, regardless of which fund is in a stronger relative position, it also is important to note that this two-tier analysis is supplemented further by a comparison of the capital accumulation trends in each of the separate funds to ensure an appropriate balance in the surplus distribution and fee structure.

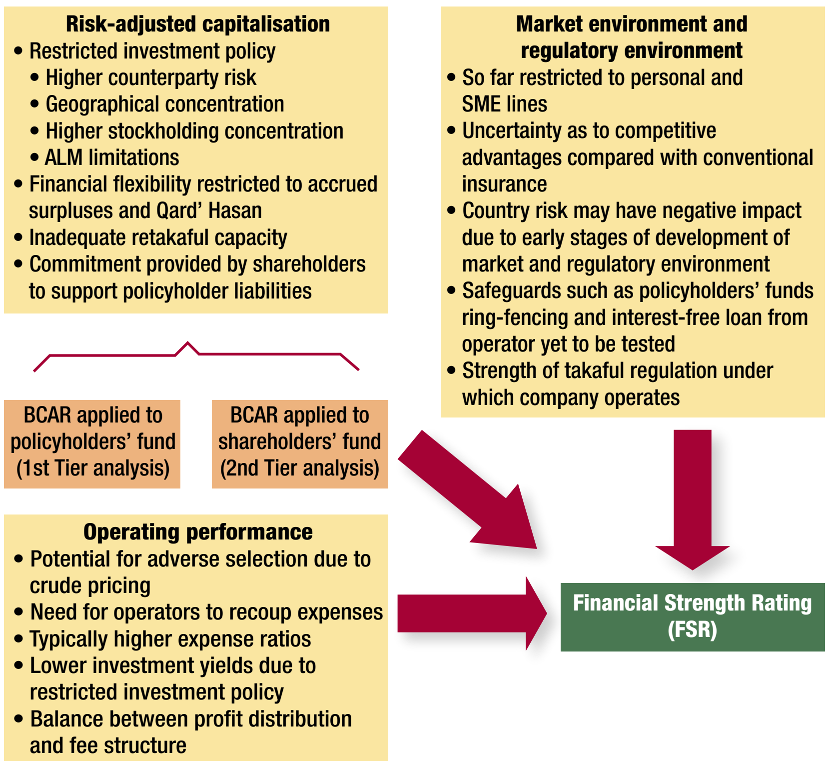
Main Drivers of Balance Sheet Strength in a Takaful Company

Given the comparatively restricted investment policy of a typical takaful company; its consequent higher levels of counterparty risk; geographical concentration; and higher than average proportion of stock holdings, capital requirements in many cases are significantly larger than for a conventional company of a similar size.

The limited classes of invested assets long have been a barrier to the growth of the takaful industry, as well as a limitation on the development of more long-term products, due to the difficulty in addressing asset-liability management issues. The current situation has improved as the capital markets in Islamic countries have begun to mature and more Shari'a-compliant investment products are available in the market. However, demand is still higher than supply, resulting in increased expense for such investment products.

In terms of insurance risk borne by takaful companies, the currently moderate exposures and relative specialisation on domestic and small to medium-sized corporate lines should be expected

Exhibit 2
Analysing a Takaful Company



to keep the capital requirements (as per the BCAR model) modest. These factors, nonetheless, easily can be more than offset by rapid growth of business and excessive concentration in a few product lines, with resulting pressures on capital needs.

An essential feature of all takaful models is participants' sharing of the underwriting surpluses/deficits. Accurately determining the surplus/deficit is, therefore, fundamental to the accounting process. Setting aside a reserve for contingencies always raises the question as to which policyholders own it, i.e. the participants that helped set it up or later generations. This is relevant because the significance of the reserve in the initial years of takaful operations is likely to be substantially greater than in subsequent years. This effectively will result in earlier participants paying to stabilize underwriting results for later participants.

Despite the possible inequity in a pure sense, the building up of a contingency reserve is desirable to enable stability in underwriting results and make it practical to expand the size of the risk pool (as there will be limits to what amounts the takaful operator will be able to provide as Qard' Hasan in case of deficits). A.M. Best considers contingency reserves as part of the capital and surplus of a company when assessing balance sheet strength.

As with conventional insurance operations, an important driving factor in the rating decision for a takaful company is its degree of financial flexibility (i.e. the company's ability to raise equity capital). As with mutual companies, the capital available normally would be expected to reflect significant surpluses accrued over the years within the takaful fund. This component of the analysis is focused mainly on the operator because of the mutual nature of the takaful fund and its inherent lack of financial flexibility. The assessment normally involves a detailed analysis of the ownership structure (and shareholders' solvency) and the record of equity or debt issues. Furthermore, consideration needs to be given for shareholders' capital commitment to the takaful fund.

A.M. Best monitors carefully the quality of the reinsurance program to assess a takaful company's balance sheet protection through reinsurance. This is particularly relevant given the previously mentioned restricted retakaful capacity (and virtual nonexistence of retro-takaful), which may force direct insurers to compromise the security of their insureds.

Operating Performance Issues In a Takaful Company

In principle, any fees paid to the operator on average should be lower than the difference between premiums and claims. In other words, as long as the takaful fund continues to generate surpluses in the long term, there should be no major reason for concern. Having satisfied this condition, at a second level of analysis, A.M. Best believes that to ensure the ongoing existence of the whole insurance operation, it is important as well that the operator at least can cover its expenses from the fees received from the policyholders' fund. For companies to achieve more secure ratings, it is important that the takaful fund generates profits and that there is a suitable balance of profit distribution between shareholders and policyholders, in addition to appropriate management fees to generate surpluses.

During the past few years, takaful companies (particularly in the Middle East) have shown higher expense ratios than their conventional counterparts. The main driver is relatively high management charges and fees to the takaful fund, resulting in low surplus accumulation. However, some companies are adopting prudent fee structures and surplus accumulation to assure a suitable balance of profit distribution and charges is maintained. A.M. Best would expect the current gap to narrow in coming years as takaful business volumes continue to expand rapidly. In addition, A.M. Best expects that over time, the issue of higher expense ratios will be somewhat mitigated by higher customer loyalty and policy persistency driven by the participants' belief in the principles of takaful.

As for investment returns, given takaful companies' constraints in asset management, higher concentration in shares and in a particular geographical region, and increased counterparty credit risk, A.M. Best expects, takaful funds on average to yield lower risk-adjusted returns, experiencing higher volatility and credit defaults. Despite the continuous growth in the supply of Islamic securities, A.M. Best believes the investment opportunities are bound to remain limited for years to come.

Market Environment and Country Risk

Despite the continued impressive growth of the takaful sector overall, rapid growth has not been experienced in all product lines, as the expansion of general or non-life business has outpaced that of the family or life product line. In addition, the typical size of a takaful company remains smaller than that of a conventional insurer. Takaful insurers tend to be smaller, in part due to their relative lack of operating experience (takaful insurers have only been in existence since 1979), and the more limited operating profile of takaful insurers when compared with conventional insurers that have diverse operating platforms and more than a century of operating history.

Going forward, A.M. Best believes the main opportunities and challenges for the sector overall are the development of more robust life insurance platforms, and compulsory lines such as motor third-party liability and health within the non-life business (in particular countries). A growth area within the corporate product line is medium-sized business risk products within the energy and construction sectors, which continue to expand. In general, retention levels for corporate product lines have been improving gradually, providing a more stable base for growth, although the largest risks still are expected to be ceded to the international markets.

A.M. Best believes it is not yet clear whether takaful companies offer any competitive advantage within this market environment. It is debatable whether there is actually an untapped demand (especially in family/life insurance business) due strictly to religious beliefs – and whether this can be unlocked easily through the offer of takaful products.

A material component of the rating process focuses on the market position of the company – its diversification in terms of client base, business lines and distribution network. In particular for takaful companies based in the Middle East, all these factors are related closely to A.M. Best's country risk assessment. The early stage of development of complementary sectors or activities (e.g. Islamic bonds, bancassurance or Internet distribution and retakaful capacity) often may have a negative impact on the final rating assigned.

Regulatory Environment and Risk Management

Regulation is extremely important in A.M. Best's assessment of takaful companies. The strength of regulation varies significantly among jurisdictions, and the protection to policyholders is somewhat unclear. While regulation of takaful companies has developed and improved in recent years, there remains an inherent lack of transparency in certain jurisdictions, particularly concerning the liabilities on winding up a takaful company. Where regulation is deemed to be weak or unclear, benefit can be given for additional commitments to the takaful fund from shareholders in favor of policyholders, such as ring-fenced assets which will be made explicit in A.M. Best's analysis of a company. Additionally, A.M. Best will consider the role of the Shari'a board within the organization and any potential differences with regulators on winding up a company.

Moreover, in A.M. Best's opinion, some of the regulatory safeguards (e.g., ring-fencing of assets within the takaful fund, interest-free loans from operators in case of solvency difficulties, etc.) are yet to be tested. The development of the Islamic insurance industry, including the regulatory environment, needs to keep pace with the rest of the financial industry in the region (especially banking).

In A.M. Best's view, a robust regulatory regime is crucial for the development of a risk management culture. A.M. Best believes that given their constraints, takaful companies need to develop and demonstrate that they can apply an adequate risk-based approach to investment management (because of the reduced investment opportunities); capital adequacy and reserving (given the need for building up surpluses in the long term, especially for family/life business); and pricing/adverse selection control (given the restrictions on charging extra risk premiums for policyholders representing a greater risk of loss than the aggregate participant pool).

Overall, one of the unique challenges facing takaful companies – and A.M. Best as it endeavours to assess their financial strength – is the need to ensure that the objectives set by their Shari'a boards are consistent with key performance indicators based on conventional sound financial and risk management. That includes establishing processes to address all material risks, despite the challenges presented by the limited capacity of retakaful, and concentration risks presented by restrictive investment guidelines and the limited geographic diversity of the current takaful marketplace.

Rating Takaful Windows and Takaful Subsidiaries

There has been an increasing use of takaful windows and takaful subsidiaries as companies seek to widen their offering and service clients. While contributions from the takaful operations are currently small, volumes are increasing and becoming more prominent within conventional insurers' profiles. In addition to the takaful methodology herein, A.M. Best will also use Rating Members of Insurance Groups when rating takaful windows and subsidiaries.

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Evaluating Country Risk

A.M. Best defines country risk as the risk that country-specific factors could adversely affect an insurer's ability to meet its financial obligations. Country risk is evaluated and factored into all A.M. Best ratings. As part of evaluating country risk, A.M. Best identifies the various factors within a country that may directly or indirectly affect an insurance company. In doing so, A.M. Best separates the risks into three main categories: economic risk, political risk and financial system risk. Given A.M. Best's particular focus on the insurance industry, financial system risk is further divided into two sections: insurance risk and non-insurance financial system risk.

A.M. Best's evaluation of country risk is not directly comparable to a sovereign debt rating, which evaluates the ability and willingness of a government to service its debt obligations. Though country risk analysis does consider the finances and policies of a sovereign government, the final determination is not guided by this sole purpose. Additionally, A.M. Best's country risk evaluation does not impose a ceiling on ratings in a given domicile.

Exhibit 1
Relationship Between Ratings and CRTs

Above Average Rating
Average Rating
Below Average Rating

CRT-1	aaa	aa+	aa	aa-	a+	a	a-	bbb+	bbb	bbb-	bb+	bb	bb-	b+	b	b-
CRT-2	aaa	aa+	aa	aa-	a+	a	a-	bbb+	bbb	bbb-	bb+	bb	bb-	b+	b	b-
CRT-3	aaa	aa+	aa	aa-	a+	a	a-	bbb+	bbb	bbb-	bb+	bb	bb-	b+	b	b-
CRT-4	aaa	aa+	aa	aa-	a+	a	a-	bbb+	bbb	bbb-	bb+	bb	bb-	b+	b	b-
CRT-5	aaa	aa+	aa	aa-	a+	a	a-	bbb+	bbb	bbb-	bb+	bb	bb-	b+	b	b-

A.M. Best's approach to country risk analysis employs a data-driven model that scores the level of risk present in a given country, plus a qualitative determination of country-specific conditions that affect the operating environment for an insurer. Countries are placed into one of five tiers, ranging from "CRT-1" (Country Risk Tier 1), denoting a stable environment with the least amount of risk, to "CRT-5" (Country Risk Tier 5) for countries that pose the most risk and, therefore, the greatest challenge to an insurer's financial stability, strength and performance. The conceptual relationship between the relative level of country risk and the rating of an insurer is depicted in **Exhibit 1** above.

In short, as country risk increases (measured by a higher assigned tier), the distribution of ratings migrates down the rating scale. This same relationship effectively applies to any significant category of risk an insurer faces, i.e. higher risk exposure pressures financial stability.

Key elements of country risk can be managed or mitigated, effectively reducing the impact on an insurer's rating. As a result, it is possible for an insurer in any country to achieve A.M. Best's highest Financial Strength Rating (FSR). Country risk is not a ceiling or cap on insurer ratings; it is one of many rating factors.

Country Risk Tier (CRT) assignments are reviewed annually, though significant events and developments are tracked continuously and may cause an interim change to a country's tier assignment. CRTs are evaluations of the current conditions in a country, but they are designed to remain stable through the business cycle. Therefore, political and industry outlooks as well as economic forecasts are integrated into the analysis.

RELATED REPORTS

CRITERIA:

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Rating Members of Insurance Groups

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Elements of Country Risk

The three risk categories in A.M. Best's country risk analysis – economic risk, political risk and financial system risk – will be defined below, and some of the key variables used will be discussed (see **Exhibit 2**).

Exhibit 2

Components of Country Risk Analysis

Economic Risk	Macroeconomy
	Prospects
	International Transactions
	Government Finance
Political Risk	Economic Policy
	Business Environment
	Government Stability
	Social Stability
	International Diplomacy
	Legal System
Financial System Risk	**Non-Insurance Financial System Risk:**
	Banking System
	Vulnerability
	Reporting Standards & Regulations
	Sovereign Debt
	Insurance Financial System Risk:
	Government & Legislation
	Supervisory Authority
	Insurer Accountability

Economic risk is the likelihood that fundamental weaknesses in a country's economy will cause adverse developments for an insurer. A.M. Best's determination of economic risk evaluates the state of the domestic economy, government finances and international transactions, as well as prospects for growth and stability.

Political risk is the likelihood that governmental or bureaucratic inefficiencies, societal tensions, an inadequate legal system or international tensions will cause adverse developments for an insurer. Political risk comprises the stability of a government and society; the effectiveness of international diplomatic relationships; the reliability and integrity of the legal system and business infrastructure; the efficiency of the government bureaucracy; and the appropriateness and effectiveness of the government's economic policies.

Financial system risk (non-insurance) is the risk that financial volatility may erupt due to inadequate reporting standards, weak banking systems or asset markets or poor regulatory structure. Non-insurance financial system risk considers a country's banking system, accounting standards and government finances, and it assesses how vulnerable the financial system is to external or internal volatility. Basel II, World Bank Insolvency Principles and International Accounting Standards all are referenced in the analysis, as are the performances of banks, equity indices and fixed-income securities.

Insurance risk is the risk that the insurance industry's levels of development and public awareness; transparency and effectiveness of regulation; reporting standards; and regulatory sophistication will contribute to a volatile financial system and compromise an insurer's ability to pay claims. Insurance risk, which A.M. Best considers as a distinct subsection of financial system risk, is addressed separately because of the importance of and A.M. Best's specific focus on the industry. The determination is based heavily on the Insurance Core Principles (ICP) of the International Association of Insurance Supervisors (IAIS). A.M. Best employs a sizable subset of the 28 ICPs by organizing them into three categories: 1) government commitment to an open and well-regulated insurance industry; 2) adequacy of supervisory authority and its supporting infrastructure; and 3) insurer accountability.

Calculating Country Risk

The country risk determination begins with the running of the Country Risk Model to generate a "score." The score is a weighted average of the three risk categories. The score then is squared, representing the nonlinear relationship between the score and the actual country risk present in the country. The main equation for calculating the Country Risk Score is as follows:

$$\text{CR Score} = [\omega_E I_E + \omega_P I_P + \omega_{FS}(I_{FSi} + I_{FSni)}]2$$

Where I_E = Economic Risk

I_P = Political Risk

I_{FSi} = Financial System Risk (insurance component)

IF_{Sni} = Financial System Risk (non-insurance component)

ω = weight applied to each category of risk

In special circumstances, such as where a given domicile has a particularly strong relationship with another – such as Guernsey with the United Kingdom – an additional calculation is added that integrates the larger domicile's influence on the stability of the smaller.

The country risk score provides a baseline of evaluation for each country. A country with a higher country risk score indicates a more risky environment as compared with a country that has a lower country risk score. After the model is run, the Country Risk Group evaluates additional qualitative factors that would influence the overall score, or one particular category of risk.

Country Risk Tiers

The assignment of CRTs to score ranges is based on A.M. Best's assertion that the risk in countries can be categorized loosely to provide a basis of comparison, provided that country-by-country differences are acknowledged. Therefore, CRTs can be classified, in a typical scenario, by the following:

CRT-1: Predictable and transparent political environment, legal system and business infrastructure; sophisticated financial system regulation with deep capital markets; mature insurance industry framework.

CRT-2: Predictable and transparent political environment, legal system and business infrastructure; sufficient financial system regulation; mature insurance industry framework.

CRT-3: Developing political environment, legal system and business infrastructure with developing capital markets; developing insurance regulatory structure.

CRT-4: Relatively unpredictable and non-transparent political, legal and business environment with underdeveloped capital markets; partially to fully inadequate regulatory structure.

CRT-5: Unpredictable and opaque political, legal and business environment with limited or nonexistent capital markets; low human development and social instability; nascent insurance industry.

Countries with characteristics of a stable insurance industry environment are highly correlated with those countries that are economically large, stable, diverse and efficiently regulated, with stable political regimes supported by a strong and credible legal system.

Annual and Event-Driven Reviews

Each country that is assigned a Country Risk Tier is reviewed annually. This review includes the model-driven score, the qualitative analysis, a rating impact study and the committee process each

Exhibit 3
Country Risk Evaluation Process

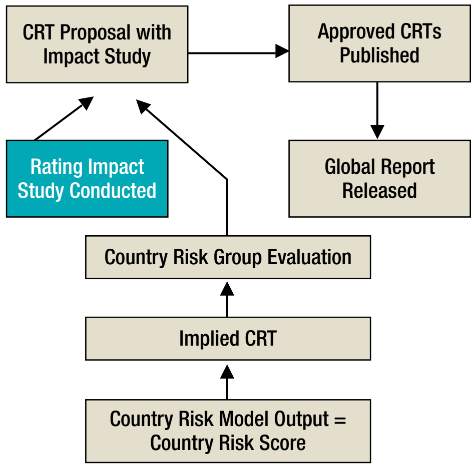

Exhibit 4
Incorporating Country Risk

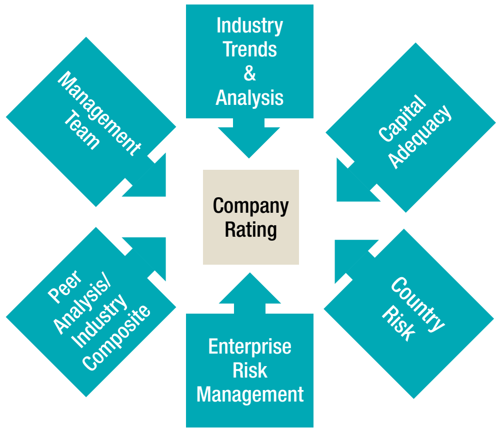

Exhibit 5
Rating Translation

Financial Strength Ratings (FSR) and Issuer Credit Ratings (ICR)

	FSR	ICR			FSR	ICR	
Secure	A++	aaa aa+	Investment Grade	Vulnerable	B	bb+ bb	Non-Investment Grade
	A+	aa aa-			B-	bb-	
	A	a+ a			C++	b+ b	
	A-	a-			C+	b-	
	B++	bbb+ bbb			C	ccc+ ccc	
	B+	bbb-			C-	ccc- cc	

year. During the interim period, the Country Risk Group continually monitors world events and developments and assesses their potential impact on tier assignments. This process is facilitated through the maintenance of a watch list that identifies countries that are experiencing a significantly increased level of volatility that has the potential to impact the CRT.

It is unusual for a country to be moved up or down the scale outside of the annual review cycle, as the CRTs are designed to remain stable through the business cycle and are not subject to frequent upgrades or downgrades. Therefore, while recent developments are factored into the analysis of country risk, they often are not significant enough to warrant an off-cycle change in the tier assignment. In the event of a change in CRT, the ratings of the companies domiciled in that country will be subject to review.

Applying Country Risk to Ratings

A.M. Best's ratings are independent opinions based on a comprehensive quantitative and qualitative evaluation of a company's balance sheet strength, operating performance and business profile. Country risk is one of many factors considered in evaluating a company according to these three characteristics. The level of consideration given to country risk (i.e. the potential impact on the determination of a rating for a company) is determined on a case-by-case basis for each insurer, based on its financial strength, position in the market and ability to mitigate or manage its exposure to country risk.

A.M. Best's Country Risk analysis seeks to identify those aspects of a country that may create a difficult or unpredictable environment for an insurer. For example, a poorly regulated banking system, poorly executed monetary policy or illiquid equity market could leave a financial system more prone to collapse. On average, most companies in CRT-1 or CRT-2 countries would not be impacted adversely by their operating environments (i.e. country risk). In CRT-3, CRT-4 and CRT-5, there is an increasing probability that environmental factors will affect a company's ability to fulfill policyholder obligations.

A.M. Best employs neither a notching process nor a ceiling in applying country risk to ratings. Country risk is one of many factors that are integrated into a Best's Rating. The integration of country risk into a rating outcome is comparable to the integration of other components of the rating analysis such as enterprise risk management (ERM); senior management discipline and track record; capital management; and competitive market position, among others (see Exhibit 4). Analysts are able to ascertain during the rating process whether an insurer is subject to country risk issues. To aid analysts in this process, the Country Risk Group offers internal briefings and mapping guides that serve as benchmarks when comparing insurers across countries and regions.

PUBLISHED: AUGUST 23, 2012

Understanding Universal BCAR

The purpose of this report is to document the existing criteria and methodology related to A.M. Best Co.'s Universal BCAR model, which is used in the evaluation of balance sheet strength for those companies that do not file U.S. or Canadian statutory statements. The Universal BCAR model can also be used in the evaluation of balance sheet strength at the insurance holding company level, regardless of domicile or accounting standard. In addition, the model can also be used to evaluate the prospective balance sheet strength of start-up insurers based on their proposed business plans.

Introduction

The objective of A.M. Best Co.'s financial strength ratings is to provide an opinion of an insurer's financial strength and ability to meet ongoing obligataions to policyholders. The assignment of an interactive rating is derived from an in-depth evaluation of a company's balance sheet strength, operating performance and business profile as compared with A.M. Best's quantitative and qualitative standards.

ADDITIONAL INFORMATION

CRITERIA:

Understanding BCAR for Property/Casualty Insurers

Understanding BCAR for Life/Health Insurers

A.M. Best's Perspective on Operating Leverage

Analyzing Contingent Capital Facilities

The Treatment of Terrorism Risk in the Rating Evaluation

Risk Management and the Rating Process for Insurance Companies

Assessing the Tail Risk of Sidecars

Catastrophe Analysis in A.M. Best Ratings

Equity Credit for Hybrid Securities

Insurance Holding Company and Debt Ratings

Rating Members of Insurance Groups

2011 Best's Briefing: Catastrophe Models and the Rating Process FAQ

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Balance Sheet Strength

In determining a company's ability to meet its current and ongoing obligations to policyholders, the most important area to evaluate is its balance sheet strength, since it is the foundation for policyholder security. Performance then determines how that balance sheet strength will be enhanced, maintained or eroded over time. Balance sheet strength measures the exposure of a company's capital to its operating and financial practices. An analysis of a company's underwriting, financial and asset leverage is very important in assessing its overall balance sheet strength.

Underwriting leverage is generated from current premium writings, reinsurance recoverables and loss reserves. In order to assess whether a company's underwriting leverage is prudent, a number of factors unique to the company are taken into account, including type of business written, quality and appropriateness of its reinsurance program, and adequacy of loss reserves.

Financial leverage is created through debt or debt-like instruments (including financial reinsurance) and is reviewed in conjunction with a company's underwriting leverage. An analysis of financial leverage is conducted at both the operating company and holding company levels, since debt at either level could place a call on the insurer's earnings and strain its cash flow, leading to financial instability.

Asset leverage measures the exposure of a company's capital to investment, interest rate and credit risks. The volatility and credit quality of the investment portfolio, recoverables and agents balances determine the potential impact of asset leverage on the company's balance sheet strength.

A company's underwriting, financial and asset leverage also are subjected to an evaluation by Best's Capital Adequacy Ratio (BCAR), which allows for an integrated review of these leverage areas. The universal BCAR model calculates the Net Required Capital to support the financial risks of the company associated with the exposure of assets and underwriting to adverse economic and market conditions, and compares this required capital to economic capital. Some of the stress tests within BCAR include above-normal catastrophes, a decline in equity markets and a rise in interest rates. This integrated stress evaluation permits a more discerning view of a company's balance sheet strength relative to its operating risks.

A company's BCAR result is extremely useful in evaluating its balance sheet strength, but BCAR is only one component of that analysis. In addition, balance sheet strength is only one component of the overall financial strength rating, which also includes operating performance and business profile. BCAR establishes a guideline for risk-adjusted capital to support a rating, but other factors driving expectations of future balance sheet strength drive the rating as well. All of these factors are important to the overall rating process.

Overview of BCAR

A.M. Best's capital formula uses a risk-based capital approach whereby net required capital is calculated to support three broad risk categories: investment risk, credit risk and underwriting risk. A.M. Best's capital adequacy formula also contains an adjustment for covariance, reflecting the assumed statistical independence of the individual components. A company's adjusted capital is divided by its net required capital, after the covariance adjustment, to determine its BCAR.

Investment Risk

Investment risk includes three main risk components: fixed-income securities, equities and interest rate. Capital charges are applied to different asset classes based on the risk of default, illiquidity and market-value declines in both equity and fixed-income securities. Additionally, higher capital charges are ascribed to affiliated investment holdings, real estate, below-investment-grade bonds and nonaffiliated, privately traded common and preferred shares because of the illiquid nature of the asset and/or the potential volatility of the reported value.

In some instances, some or all of the risk associated with a particular asset may be borne by the policyholder. In those situations, the investment risk to the insurance company may be reduced.

A.M. Best's capital model incorporates an interest-rate risk component that considers the decline in market value of a company's fixed-income portfolio as a result of rising interest rates. The interest rate risk calculation will reflect the fact that companies writing life and annuity products will have an exposure to disintermediation and cash-flow mismatch risks, whereas a company writing property/casualty products will have an interest-rate risk exposure when a shock event occurs. Interest rate risk for annuity writers will vary based on the type of products offered and the source of that business.

Investment risks are typically the main drivers of a life and annuity insurer's capital requirements.

Credit Risk

Capital charges are applied to different receivable balances to reflect third-party default risk. Credit risk factors are ascribed to recoverables from all reinsurers, including affiliates. Required capital for credit risk may be modified after taking into account acceptable collateral offsets for reinsurance balances; the quality of the reinsurers that participate in the company's reinsurance program; and the company's dependence on its reinsurance program. Also included in the credit risk component are charges for premium balances receivable; accrued retrospective premiums; deposits in pools and associations; funds held by ceding insurers; and other, miscellaneous receivables.

Underwriting Risk

This category encompasses the risks associated with net loss and loss-adjustment expense reserves, net premiums written and net unearned premiums. The reserve component requires capital based on the risk inherent in a company's loss and loss-adjustment expense reserves, adjusted for A.M. Best's assessment of its reserve equity. The net premiums written component is a forward-looking component and requires capital based on the pricing risk inherent in a company's expected book of business for the upcoming year. The unearned premium component reflects the exposure to pricing risk on premium that was written in the past but is still unearned as of the current evaluation date.

Required capital for the underwriting risk components may be increased to reflect an additional surcharge for "excessive" exposure growth. In addition, there is credit for a well-diversified book of business, but this credit is minimized for those companies that maintain small books of many lines of business and may not necessarily have expertise in each of them. For those composite companies that write both property/casualty and life insurance, the amount of diversification credit may be increased to reflect the additional benefits from diversifying across insurance sectors.

For life and health insurers, underwriting risks are divided into mortality risks, longevity risks and morbidity risks. Mortality risks are based on volume of life insurance in force, net of reserves and reinsurance, with risk charges grading lower for higher amounts at risk. Longevity risks are present in annuities and certain types of pension plans, as plan participants are living longer than expected when payment amounts originally were determined. Morbidity risks vary by line of business and therefore warrant different charges. Generally, health care lines of business with long-tail risks (disability, long-term care) will have higher premium risk charges than shorter tail risks (medical, critical illness).

For property/casualty insurers, underwriting risk is typically the largest risk category and usually accounts for two-thirds of a company's gross required capital.

Required Capital

Collectively, the investment, credit and underwriting risk components generate more than 99% of a company's gross required capital, with the business risk component generating minimal capital requirements for off-balance sheet items. A company's gross required capital, which is the sum of the capital required to support all of its risk components, reflects the amount of capital needed to support all of those risks if they were to develop simultaneously. However, these individual components then are subjected to a covariance calculation within the BCAR formula to account for the assumed statistical independence of these components. This covariance adjustment essentially says that it is unlikely that all of the individual risk components will develop simultaneously, and this adjustment generally reduces a company's overall required capital.

A.M. Best recognizes the distortions caused by the "square root rule" covariance adjustment, whereby the more capital-intensive risk components are disproportionately accentuated while the less capital-intensive risk components are diminished in their relative contribution to net required capital. Nevertheless, by using other distinct capital measures, A.M. Best can counterbalance this apparent shortcoming.

Determination of Available Capital

A.M. Best makes a number of adjustments to a company's reported capital within its universal capital model to provide a more economic and comparable basis for evaluating capital adequacy. Different accounting methods and regulatory requirements across the world require numerous adjustments to a company's reported capital. Goodwill and other intangible assets are eliminated. Pre-event catastrophe reserves are removed from the loss reserves and moved into available capital on a tax-effected basis. Adjustments for any embedded value in unearned premium reserves, loss reserves and fixed-income securities are made if the company has not already reflected these in its reported capital. Further adjustments are made to capital to reflect other non-balance sheet risks, including catastrophe exposures and debt-service requirements.

A.M. Best's capital model emphasizes permanent capital and consequently will reduce a company's reported surplus for encumbered capital, which includes surplus notes and future debt-service requirements of an affiliated holding company. This reduction, in whole or in part, depends on the magnitude of, and dependence an insurance group has on, debt-like instruments and their associated repayment features.

Both quantitative and qualitative factors are considered in the evaluation of debt. As part of the quantitative analysis, A.M. Best uses a separate model to assist in determining the amount of surpus credit given to surplus notes and debt instruments. The primary issue, which determines the level of credit given, is the term of the debt compared with the length of time needed to pay the bulk of the policy liabilities. Usually, more credit is given to longer term than to short-term debt. Another key determinant is the company's rate of return compared with the interest rate charged on the debt. A company should be earning more than its cost of capital to receive credit for the debt.

On a qualitative basis, issues such as where the debt is held vs. where the cash is used; the existence of other sources of income to offset the cost of debt; fixed-charge coverage; and the overall level of debt relative to the organization's total capital all are considered. For example, when debt is issued at the holding company but the cash is held at the operating insurance company, even though the cash is given full credit in the BCAR analysis of the operating company, the actual rating of the operating company could be limited by the evaluation of the financial leverage and earnings coverage at the holding company.

Exhibit 1
Available Capital Components:

Reported Capital

Equity Adjustments:
- Unearned Premiums
- Assets
- Loss Reserves
- Reinsurance

Debt Adjustments:
- Debt/Hybrid Securities
- Debt-Service Requirements

Other Adjustments:
- Potential Catastrophe Losses (Net of Reins.)
- Future Operating Losses
- Future Dividends
- Contingent Capital
- Contingent Reserves
- Value in Force (Life Business)
- Deferred Acquisition Costs
- Goodwill
- Other Intangible Assets

Formula Drivers

A company's gross capital requirement within A.M. Best's capital model is generated primarily from its investment, credit and underwriting risks. A company that maintains a more aggressive investment portfolio, is heavily concentrated in one asset or sector, or is heavily dependent on pyramided capital likely will generate a lower BCAR value. Companies that have excessive exposure to third-party credit risk or are heavily dependent on reinsurance likely will generate lower BCAR scores. The amount of required capital generated from the underwriting risk components is largely a function of the company's mix of business, amount of available capital, growth in exposure, stability of loss development, profitability, loss-reserve adequacy and length of claims payout. All other things being equal, the absolute BCAR score of a company will be lower because of higher capital requirements associated with greater indicated reserve deficiencies, as well as unstable or unprofitable business.

Exhibit 2
BCAR Guidelines

BCAR	Implied Balance Sheet Strength
Secure:	
175	A++
160	A+
145	A
130	A-
115	B++
100	B+
Vulnerable:	
90	B
80	B-
70	C++
60	C+
50	C
40	C-
<40	D

In addition, the model can be adjusted in response to various market issues. Some examples of the issues that can impact capitalization include rate changes, the stage of the underwriting cycle, changing reinsurance products and reinsurance dependence. The ability of the model to respond to these market issues makes it a robust tool that assists in the evaluation of the company's balance sheet strength.

The basis of risk measurement for some of the key drivers of required capital in the universal BCAR model is expected policyholder deficit. A.M. Best adopted the concept of expected policyholder deficit to better calibrate the model's loss-reserve and premium-risk factors, as well as other risk factors in the model. The concept of expected policyholder deficit allows risk charges to be calibrated to a specific level of insolvency risk and also takes into consideration the expected cost, or severity, of insolvency.

BCAR Is an Absolute Measure

The universal BCAR model produces an absolute score, which is the ratio of the company's adjusted capital to its own net required capital. This company-specific capital ratio indicates whether its capital strength aligns with A.M. Best's "Secure" or "Vulnerable" rating categories and is based on the specific risk profile of a company's operations. A BCAR score below 100% would be considered vulnerable. Given strong, stable operating performance, sound risk management, high quality capital and strong financial flexibility, **Exhibit 2** provides a reasonable guide for the BCAR levels needed to support A.M. Best's Financial Strength Ratings.

Additional Stress Testing

A.M. Best also will stress a company's BCAR score for a second catastrophic event according to the procedures outlined in its criteria report titled *Catastrophe Analysis in A.M. Best Ratings* and its criteria report titled *The Treatment of Terrorism Risk in the Rating Evaluation*. The testing will incorporate natural catastrophes and/or man-made events such as terrorism to monitor how sensitive a company's balance sheet strength is to a second catastrophic event. For casualty writers, an estimate of a casualty shock loss may be used in the analysis of balance sheet strength. Additional stresses may be employed when insurers accumulate large amounts of higher risk investments.

Conclusion

The tools to allocate capital and understand capital strength continue to evolve. These tools often vary in theory, purpose and outcome. It is important to remember that, while they can add significant value, they are only tools. A.M. Best's proprietary universal BCAR is one of those tools that look at capital needs well above financial solvency. A.M. Best will continue to enhance BCAR going forward to improve its accuracy in measuring balance sheet and operating risk.

BCAR is important to A.M. Best's evaluation of both absolute and relative capital strength. Consistent with standards embedded within the universal BCAR model, A.M. Best would expect that well-managed and highly rated companies will maintain capitalization levels in excess of the risk-adjusted amounts indicated by the published guidelines to support their current ratings.

A.M. Best is quick to caution, however, that although BCAR is an important tool in the rating process, it isn't sufficient to serve as the sole basis of a rating assignment. BCAR, like other quantitative measures, has some limitations and doesn't necessarily work for all companies. Consequently, capital adequacy should be viewed within the overall context of the operating and strategic issues surrounding a company. Business profile and operating performance are important rating considerations in evaluating a company's long-term financial strength and viability as well as the quality of the capital that supports the BCAR result. In addition, any holding company considerations also will play a key role in evaluating the financial strength of an insurance company.

In closing, A.M. Best believes that well-managed and highly rated insurers will continue to focus on the fundamentals of building future economic value and financial stability, rather than on managing one, albeit important, component of A.M. Best's rating evaluation.

A.M. Best's Country Risk Tiers

A.M. Best defines country risk as the risk that country-specific factors could adversely affect the claims paying ability of an insurer. Country risk is factored into all A.M. Best ratings.

A.M. Best's country risk methodology, Evaluating Country Risk (see page 21), presents the country risk evaluation process and describes how country risk is integrated into Best's Credit Ratings.

The 97 countries evaluated by A.M. Best are listed according to their Country Risk Tier in the table below.

CRT-1		
Australia	Germany	Netherlands
Austria	Gibraltar	Norway
Belgium	Guernsey	Singapore
Canada	Isle of Man	Sweden
Denmark	Japan	Switzerland
Finland	Jersey	United Kingdom
France	Luxembourg	United States

CRT-2		
Barbados	Hong Kong	New Zealand
Bermuda	Ireland	Slovenia
British Virgin Islands	Italy	South Korea
Cayman Islands	Liechtenstein	Spain
Chile	Macau	Taiwan

CRT-3		
Anguilla	Kuwait	Saint Martin
Bahamas	Malaysia	Saudi Arabia
Bahrain	Malta	Sint Maarten
Brazil	Mexico	South Africa
China	Oman	Thailand
Curacao	Poland	Trinidad & Tobago
Cyprus	Qatar	United Arab Emirates
Israel	Saint Kitts & Nevis	

CRT-4		
Antigua & Barbuda	Indonesia	Peru
Brunei Darussalam	Jordan	Philippines
Colombia	Kazakhstan	Russia
Costa Rica	Mauritius	Tunisia
El Salvador	Morocco	Turkey
India	Panama	

CRT-5		
Algeria	Egypt	Libya
Argentina	Ghana	Nicaragua
Belarus	Guatemala	Nigeria
Bolivia	Honduras	Pakistan
Bosnia and Herzegovina	Jamaica	Ukraine
Dominican Republic	Kenya	Venezuela
Ecuador	Lebanon	Vietnam

A.M. Best's Country Risk Tier listings as of March 2013.

AMB CREDIT REPORT - INSURANCE PROFESSIONAL FOR

ACR RETAKAFUL MEA B.S.C. (C)

Operating Company Non-Life
Ultimate Parent: ACR ReTakaful Holdings Limited

Gajria Tower, 8th Floor, Seef District, PO Box 1591, Manama, Bahrain
Web: www.acrretakaful.com | Tel: 973-1738-8350 | Fax: 973-1738-8351
AMB#: 090059
Ultimate Parent#: 052141

Report Revision Date: 02/20/2013

BEST'S CREDIT RATINGS

Best's Financial Strength Rating: A- Outlook: Stable
Best's Issuer Credit Rating: a- Outlook: Stable

Best's Financial Size Category: VIII

RATING RATIONALE

Rating Rationale: The ratings reflect the adequate capitalization and enhanced enterprise risk management of Asia Capital Reinsurance Group Pte. Ltd. (ACR), Asia Capital Reinsurance Malaysia Sdn Bhd (ACRM), ACR ReTakaful Berhad and ACR ReTakaful MEA. A.M. Best also acknowledges the companies' disciplined and prudent investment strategies.

During the early part of 2012, the capitalization of ACR, ACRM, ACR ReTakaful Berhad and ACR ReTakaful MEA was weakened, largely due to unfavorable underwriting performance as a result of the catastrophe losses that occurred in the Asia-Pacific region in 2011. For the fiscal year ending March 31, 2012, ACR had a net incurred loss ratio of 107%. The net incurred loss ratios for ACRM, ACR ReTakaful Berhad and ACR ReTakaful MEA for the fiscal year ending December 31, 2011, were 123%, 142% and 152%, respectively. Nonetheless, the companies took measures to restore their capital strength, including a capital injection, reducing the net retention of underwriting risks and reducing catastrophe exposures. The risk-adjusted capitalization of ACR, ACRM, ACR ReTakaful SEA and ACR ReTakaful MEA has been restored to an adequate level and is supportive of their current ratings.

The enhanced enterprise risk management framework also safeguards the companies' capitalization going forward.

Offsetting these positive rating factors are the companies' volatile historical underwriting results and the competitive reinsurance market in the Asia-Pacific region.

Future positive rating actions could occur if the companies further improve their risk-based capitalization and demonstrate the ability to achieve consistently favorable operating performance. Conversely, negative rating actions could occur if the companies' operating performance materially deviates from their projections, or their risk-adjusted capitalization declines to a level below A.M. Best's expectations.

FIVE YEAR RATING HISTORY

	BEST'S	
Date	FSR	ICR
12/20/12	A-	a-
01/04/12	A-	a-
12/14/10	A-	a-
11/09/09	A-	a-
07/29/08	A-	a-

BUSINESS PROFILE

ACR Retakaful Holdings, a holding entity incorporated in Dubai in 2008, underwrites business in the retakaful segment through two Sharia' compliant retakaful operating entities: ACR ReTakaful SEA Berhad and ACR ReTakaful MEA B.S.C. (c). The holding company has been capitalized at USD 300 million by three shareholders: Khazanah Nasional, Dubai Islamic Investment Group (DIIG) and ACR Capital Holdings. ACR ReTakaful MEA, which was incorporated in Bahrain in July 16, 2008, explores business opportunities in the Middle East.

ACR ReTakaful MEA focuses on large risk businesses in the retakaful markets, writing a broad range of risk products from property, engineering, marine, aviation, energy and motor to casualty business on both a treaty and facultative basis. In addition to the dedicated focus on retakaful business, the company also capitalizes on quality opportunities arising from the conventional markets.

ACR ReTakaful MEA and ACR ReTakaful SEA have an internal proportional retrocession arrangement with associated companies within the ACR Group. The companies source business in their market and share the business among all the associated companies based on the respective underwriting capacity of each company. The companies, in return, receive inward business from the ACR Group. ACR ReTakaful MEA and ACR ReTakaful SEA have diversified geographically their underwriting risk through this retrocession arrangement.

As at the end of June 2011, ACR ReTakaful MEA generated gross contributions (GC) (excluding an intercompany retrocession arrangement) of almost USD 46 million. Property was the largest line of business accounting for 34% of the GC. Other key portfolios are engineering and motor, which contributed to 23% and 21% of total GC, respectively. For the year to June 2010, 44% of ACR ReTakaful MEA's GC was derived from inward premium received from the ACR Group.

ACR ReTakaful MEA also benefits from the underwriting, claims and risk management expertise of Asia Capital Reinsurance Group Pte. Ltd. (ACR). To mitigate against any potential operational risk, the company adopts similar underwriting guidelines and pricing models to ACR and controls its risk exposures by using ACR's risk management platform.

In view of the current operating landscape in both the retakaful and conventional sectors, with increasing numbers of market participants, A.M. Best remains cautious about the capability of ACR Retakaful Holdings to achieve its planned business growth combined with sound underwriting profitability.

OPERATING PERFORMANCE

Operating Results: As ACR ReTakaful MEA is a newly formed reinsurer and so lacks an operating history, A.M. Best's analysis and expectations are based on actual financials of fiscal years 2009 and 2010 and financial projections provided by the company for the next three years. A.M. Best will closely monitor premium growth and operating results to ensure that they are in line with expectations.

ACR ReTakaful MEA intends to retain planned earnings within the retakaful fund to support ongoing business growth, regardless of wakala fee expenses and the sharing of investment profits from the retakaful funds on a Mudaraba basis. A.M. Best will monitor closely the financial performance of the operation against its stated business plan.

ACR ReTakaful MEA recorded net income after tax for its first two operating years. The underwriting results of the retakaful fund also reported a surplus (after deduction of the wakala fee and sharing of investment profits) as demonstrated by the combined ratio, which remained below 100%.

BALANCE SHEET STRENGTH

Capitalization: To support ACR Retakaful Holdings' accelerated business growth in its early stages of operation, the company infused USD 100 million into ACR ReTakaful SEA and USD 200 million into ACR ReTakaful MEA.

The capital and surplus of ACR ReTakaful MEA has increased in fiscal year 2010 compared to 2009, a result that is attributable to positive net income and retained earnings. Despite the loss from the Thai flooding, the risk-based capitalization as measured by Best's Capital Adequacy Ratio (BCAR) will remain strong for fiscal year 2011. The capitalization of ACR ReTakaful MEA is expected to be adequate to support the planned business growth.

Underwriting leverage (which is defined as the ratio of net written contributions to the sum of both shareholders' and retakaful funds) is expected to remain well below 1 time. As a start-up entity, the BCAR of ACR ReTakaful MEA is subject to more stringent requirements based upon the company's operating profile. In view of the Qard al Hassan (interest-free loan) available to the retakaful policyholders' fund from the shareholders' fund through a trust deed arrangement, A.M. Best believes that the risk-based capital position for the policyholders will be adequate to support planned business growth over the next three years.

Summarized Accounts as of December 31, 2011

Data reflected within all tables of this report has been compiled from the financial statements of this company (Source: Company Financial Statement).

STATEMENT OF INCOME

Technical account:	12/31/2011 USD (000)	12/31/2010 USD (000)
Reinsurance premiums assumed	103,660	118,173
Gross premiums written	103,660	118,173
Reinsurance ceded	19,359	27,956
Net premiums written	84,301	90,217
Increase/(decrease) in gross unearned premiums	-515	26,530
Increase/(decrease) in reinsurers share unearned premiums	-2,369	5,246
Net premiums earned	82,447	68,933
Other technical income	164	122
Total underwriting income	82,611	69,055
Net claims paid	37,616	13,825
Net increase/(decrease) in claims provision	86,008	26,280
Net claims incurred	123,624	40,105
Management expenses	9,602	5,519
Acquisition expenses	24,976	20,533
Net operating expenses	34,578	26,052
Total underwriting expenses	158,202	66,157
Balance on technical account	-75,591	2,898
Combined technical account:		
Reinsurance premiums assumed	103,660	118,173
Gross premiums written	103,660	118,173
Reinsurance ceded	19,359	27,956
Net premiums written	84,301	90,217
Increase/(decrease) in gross unearned premiums	-515	26,530
Increase/(decrease) in reinsurers share unearned premiums	-2,369	5,246
Net premiums earned	82,447	68,933
Other technical income	164	122
Total revenue	82,611	69,055
Net claims paid	37,616	13,825
Net increase/(decrease) in claims provision	86,008	26,280
Net claims incurred	123,624	40,105
Management expenses	9,602	5,519
Acquisition expenses	24,976	20,533

Net operating expenses	34,578	26,052
Total underwriting expenses	158,202	66,157
Balance on combined technical account	-75,591	2,898

Non-technical account:		
Net investment income	4,113	6,603
Exchange gains/(losses)	-2,381	-11
Other income/(expense)	76,284	-5,724
Profit/(loss) before tax	2,425	3,766
Profit/(loss) after tax	2,425	3,766
Transfer to reserves	243	701
Other adjustments	...	-1,923
Retained Profit/(loss) for the financial year	2,182	1,142
Retained Profit/(loss) brought forward	6,189	5,047
Retained Profit/(loss) carried forward	8,371	6,189

MOVEMENT IN CAPITAL & SURPLUS

	12/31/2011 USD(000)	12/31/2010 USD(000)
Capital & surplus brought forward	207,450	205,607
Change in non-distributable reserves	243	701
Change in other reserves	-243	-701
Profit or loss for the year	2,425	3,766
Other changes	...	-1,923
Total change in capital & surplus	2,425	1,843
Capital & surplus carried forward	209,875	207,450

ASSETS

	12/31/2011 USD (000)	12/31/2011 % of total	12/31/2010 USD (000)
Cash & deposits with credit institutions	218,367	47.7	230,996
Bonds & other fixed interest securities	12,988	2.8	9,983
Liquid assets	231,355	50.6	240,979
Total investments	231,355	50.6	240,979
Reinsurers' share of technical reserves - unearned premiums	15,217	3.3	17,609
Reinsurers' share of technical reserves - claims	47,223	10.3	19,630
Total reinsurers share of technical reserves	62,440	13.6	37,239
Insurance/reinsurance debtors	48,939	10.7	30,839
Inter-company debtors	15,572	3.4	936
Other debtors	57,452	12.6	63,886
Total debtors	121,963	26.7	95,661
Fixed assets	56	0.0	126
Prepayments & accrued income	25,875	5.7	24,360
Other assets	15,750	3.4	...
Total assets	457,439	100.0	398,365

LIABILITIES

	12/31/2011 USD (000)	12/31/2011 % of total	12/31/2010 USD (000)
Capital	200,000	43.7	200,000
Paid-up capital	200,000	43.7	200,000
Non-distributable reserves	1,504	0.3	1,261
Retained earnings	8,371	1.8	6,189
Capital & surplus	209,875	45.9	207,450
Minority interests	-50,558	-11.1	8,966
Gross provision for unearned premiums	70,318	15.4	70,898
Gross provision for outstanding claims	174,760	38.2	65,221
Gross provision for other technical reserves	4,000	0.9	...
Total gross technical reserves	249,078	54.5	136,119
Insurance/reinsurance creditors	13,620	3.0	24,681

Inter-company creditors	887	0.2	…
Other creditors	20,906	4.6	9,533
Total creditors	35,413	7.7	34,214
Accruals & deferred income	13,230	2.9	11,196
Other liabilities	401	0.1	420
Total liabilities & surplus	457,439	100.0	398,365

MANAGEMENT

OFFICERS

CEO: Prem Sagar

Department Manager: Maha Fikree
(Head, Human Resources & Administration)

Department Manager: Manoj Lalwani
(Head, Finance & Technical Accounts)

Underwriter: Chris Javitte (Head of Treaty)

DIRECTORS

Datuk Mohd Najib bin Hj. Abdullah
Ercument Cetin Alanya
Marwan Hassan Ali ElKhatib (Deputy Chairman)
Datuk Syed Muhamad bin Syed Abdul Kadir
Ahmad Farouk bin Mohamed
Keith Scott
Kwang Kherng John Tan
Raja Tan Sri Dato Seri Arshad bin Raja Tun Uda (Chairman)

ANALYSIS OF GROSS PREMIUMS WRITTEN

	USD (000) 2011	USD (000) 2010	USD (000) 2009	USD (000) 2008	2007
Reinsurance	103,660	118,173	77,655	2,539	…
Total non-life	103,660	118,173	77,655	2,539	…

REINSURANCE

In addition to the proportional treaties with ACR Group, ACR ReTakaful MEA also has an excess of loss protection program with a limit of USD 2.5 million in excess of USD 7.5 million and USD 10 million in excess of USD 10 million for its own business.

BALANCE SHEET ITEMS

	USD (000) 2011	USD (000) 2010	USD (000) 2009	USD (000) 2008	2007
Liquid assets	231,355	240,979	213,601	200,398	…
Total investments	231,355	240,979	213,601	200,398	…
Total assets	457,439	398,365	298,906	206,394	…
Total gross technical reserves	249,078	136,119	69,100	2,439	…
Net technical reserves	186,638	98,880	51,316	1,516	…
Total liabilities	247,564	190,915	93,299	4,991	…
Capital & surplus	209,875	207,450	205,607	201,403	…

INCOME STATEMENT ITEMS

	USD (000) 2011	USD (000) 2010	USD (000) 2009	USD (000) 2008	2007
Gross premiums written	103,660	118,173	77,655	2,539	…
Net premiums written	84,301	90,217	60,075	1,573	…
Balance on technical account(s)	-75,591	2,898	3,753	-54	…
Profit/(loss) before tax	2,425	3,766	4,204	1,403	…
Profit/(loss) after tax	2,425	3,766	4,204	1,403	…

LIQUIDITY RATIOS (%)

	2011	2010	2009	2008	2007
Total debtors to total assets	26.7	24.0	19.7	1.0	...
Liquid assets to net technical reserves	124.0	243.7	416.2	999.9	...
Liquid assets to total liabilities	93.5	126.2	228.9	999.9	...
Total investments to total liabilities	93.5	126.2	228.9	999.9	...

LEVERAGE RATIOS (%)

	2011	2010	2009	2008	2007
Net premiums written to capital & surplus	40.2	43.5	29.2	0.8	...
Net technical reserves to capital & surplus	88.9	47.7	25.0	0.8	...
Gross premiums written to capital & surplus	49.4	57.0	37.8	1.3	...
Gross technical reserves to capital & surplus	118.7	65.6	33.6	1.2	...
Total debtors to capital & surplus	58.1	46.1	28.7	1.0	...
Total liabilities to capital & surplus	118.0	92.0	45.4	2.5	...

PROFITABILITY RATIOS (%)

	2011	2010	2009	2008	2007
Loss ratio	149.9	58.2	64.8	59.6	...
Operating expense ratio	41.0	28.9	11.1	7.1	...
Combined ratio	191.0	87.1	76.0	66.6	...
Other technical expense or (income) ratio	-0.2	-0.1	-0.1	...	...
Net investment income ratio	5.0	9.6	20.4	999.9	...
Operating ratio	185.8	77.3	55.4	-99.9	...
Return on net premiums written	2.9	4.2	7.0	89.2	...
Return on total assets	0.6	1.1	1.7	...	...
Return on capital & surplus	1.2	1.8	2.1	...	...

AMB CREDIT REPORT - INSURANCE PROFESSIONAL FOR

NATIONAL TAKAFUL COMPANY (WATANIA) PJSC

Operating Company Non-Life

P.O. Box No. 6457, Abu Dhabi, United Arab Emirates
Tel: 971-2-613-8888
AMB#: 092651

Report Revision Date: 03/18/2013

BEST'S CREDIT RATINGS

Best's Financial Strength Rating: B+ Outlook: Stable
Best's Issuer Credit Rating: bbb- Outlook: Stable

Best's Financial Size Category: VI

RATING RATIONALE

Rating Rationale: The ratings for National Takaful Company (Watania) PJSC reflect its strong prospective risk-adjusted capitalisation, supported by strong reinsurance protection and a conservative investment strategy, and sound business plan. Offsetting rating factors are below-target results in 2012 and the execution risk Watania faces in the competitive UAE insurance market.

Profile: UAE-based multiline Takaful -- Watania was established in July 2011 as a non-life Takaful provider initially operating in Abu Dhabi, with plans to increase distribution across the UAE over five years. The company has already opened an office in Dubai, with plans to open offices in other Emirates during 2013. The company provides all non-life lines of Takaful insurance with a profile biased towards group medical business in 2012.

Strong Risk-adjusted Capitalisation -- Watania benefits from strong risk-adjusted capitalisation with sufficient capital to support current and prospective levels of underwriting. Risk-adjusted capitalisation benefits from a low level of retained insurance risk supported by a well-rated reinsurance programme. Financial flexibility is viewed as strong, given supportive shareholders and an oversubscribed IPO in 2011. Capitalisation benefits from a conservative, fixed-income focused investment strategy and low retention with a well-rated reinsurance programme.

Takaful -- A.M. Best views Watania's implementation of a hybrid Wakala model and the regulatory oversight in the UAE to be sufficient to view the company's entire capital as available to policyholders. The ratings of the company in the future may depend on A.M. Best's continued assessment of Takaful regulation and Watania's treatment of Takaful principles.

Technical Performance -- Watania achieved below-plan gross written premiums and profitability in 2012. Watania's GWP portfolio was more biased towards medical business than expected. Due to lower volumes overall, the company was less able to cover its high initial expenses. The loss for 2012 was AED 10.5 million.

Enterprise Risk Management -- Watania's ERM is viewed as developing with a strong structure being implemented over the course of 2013. The company has a financial analysis tool which will be used to monitor capital adequacy and shape business plans as well as reinsurance optimisation and pricing strategy.

Watania has entered the UAE insurance market with a strong business plan; however, it will face fierce competition both from Takaful and conventional insurance providers. The company benefits from experienced management and a good understanding of risk control. In the future, positive or negative rating pressure is likely to result from Watania's ability to successfully execute its business plan.

FIVE YEAR RATING HISTORY

	BEST'S	
Date	FSR	ICR
03/18/13	B+	bbb-

Summarized Accounts as of December 31, 2012

Data reflected within all tables of this report has been compiled from the financial statements of this company (Source: Company Financial Statement).

US $ per Local Currency Unit .2723 = 1 United Arab Emirates Dirham (AED)

STATEMENT OF INCOME

Technical account:	12/31/2012 AED(000)	12/31/2012 USD(000)
Gross premiums written	44,077	12,002
Reinsurance ceded	23,695	6,452
Net premiums written	20,382	5,550
Increase/(decrease) in gross unearned premiums	19,405	5,284
Increase/(decrease) in reinsurers share unearned premiums	10,692	2,911
Net premiums earned	11,669	3,177
Total underwriting income	11,669	3,177
Net claims paid	4,312	1,174
Net increase/(decrease) in claims provision	4,757	1,295
Net claims incurred	9,069	2,469
Management expenses	18,350	4,997
Acquisition expenses	63	17
Net operating expenses	18,413	5,014
Other technical expenses	1,727	470
Total underwriting expenses	29,209	7,954
Balance on technical account	-17,540	-4,776
Combined technical account:		
Gross premiums written	44,077	12,002
Reinsurance ceded	23,695	6,452
Net premiums written	20,382	5,550
Increase/(decrease) in gross unearned premiums	19,405	5,284
Increase/(decrease) in reinsurers share unearned premiums	10,692	2,911
Net premiums earned	11,669	3,177
Total revenue	11,669	3,177
Net claims paid	4,312	1,174
Net increase/(decrease) in claims provision	4,757	1,295
Net claims incurred	9,069	2,469
Management expenses	18,350	4,997
Acquisition expenses	63	17
Net operating expenses	18,413	5,014
Other technical expenses	1,727	470
Total underwriting expenses	29,209	7,954
Balance on combined technical account	-17,540	-4,776
Non-technical account:		
Net investment income	4,233	1,153
Realised capital gains/(losses)	198	54
Unrealised capital gains/(losses)	904	246
Other income/(expense)	-5,420	-1,476
Profit/(loss) before tax	-17,625	-4,799
Profit/(loss) after tax	-17,625	-4,799
Retained Profit/(loss) for the financial year	-17,625	-4,799
Retained Profit/(loss) carried forward	-17,625	-4,799

MOVEMENT IN CAPITAL & SURPLUS

	12/31/2012 AED(000)	12/31/2012 USD(000)
Change in share capital	150,000	40,845
Profit or loss for the year	-17,625	-4,799
Total change in capital & surplus	132,375	36,046
Capital & surplus carried forward	132,375	36,046

ASSETS

	12/31/2012 AED(000)	12/31/2012 % of total	12/31/2012 USD(000)
Cash & deposits with credit institutions	39,703	22.0	10,811
Bonds & other fixed interest securities	89,660	49.6	24,414
Shares & other variable interest instruments	10,246	5.7	2,790
Liquid assets	139,609	77.3	38,016
Total investments	139,609	77.3	38,016
Reinsurers' share of technical reserves - unearned premiums	10,691	5.9	2,911
Reinsurers' share of technical reserves - claims	6,331	3.5	1,724
Total reinsurers share of technical reserves	17,022	9.4	4,635
Insurance/reinsurance debtors	13,483	7.5	3,671
Total debtors	13,483	7.5	3,671
Fixed assets	3,684	2.0	1,003
Prepayments & accrued income	5,144	2.8	1,401
Other assets	1,669	0.9	454
Total assets	180,611	100.0	49,180

LIABILITIES

	12/31/2012 AED(000)	12/31/2012 % of total	12/31/2012 USD(000)
Capital	150,000	83.1	40,845
Paid-up capital	150,000	83.1	40,845
Retained earnings	-17,625	-9.8	-4,799
Capital & surplus	132,375	73.3	36,046
Gross provision for unearned premiums	19,405	10.7	5,284
Gross provision for outstanding claims	11,087	6.1	3,019
Total gross technical reserves	30,492	16.9	8,303
Insurance/reinsurance creditors	9,409	5.2	2,562
Other creditors	2,697	1.5	734
Total creditors	12,106	6.7	3,296
Accruals & deferred income	1,104	0.6	301
Other liabilities	4,534	2.5	1,235
Total liabilities & surplus	180,611	100.0	49,180

ANALYSIS OF GROSS PREMIUMS WRITTEN

	AED (000) 2012	2011	2010	2009	2008
Accident & health	31,329	...	...	...	...
Other classes	12,748	...	...	...	...
Total non-life	44,077	...	...	...	...

BALANCE SHEET ITEMS

	AED (000) 2012	2011	2010	2009	2008
Liquid assets	139,609	...	...	...	...
Total investments	139,609	...	...	...	...
Total assets	180,611	...	...	...	...
Total gross technical reserves	30,492	...	...	...	...
Net technical reserves	13,470	...	...	...	...
Total liabilities	48,236	...	...	...	...
Capital & surplus	132,375	...	...	...	...

INCOME STATEMENT ITEMS

AED (000)	2012	2011	2010	2009	2008
Gross premiums written	44,077	...	...	...	...
Net premiums written	20,382	...	...	...	...
Balance on technical account(s)	-17,540	...	...	...	...
Profit/(loss) before tax	-17,625	...	...	...	...
Profit/(loss) after tax	-17,625	...	...	...	...

LIQUIDITY RATIOS (%)

	2012	2011	2010	2009	2008
Total debtors to total assets	7.5	...	...	...	...
Liquid assets to net technical reserves	999.9	...	...	...	...
Liquid assets to total liabilities	289.4	...	...	...	...
Total investments to total liabilities	289.4	...	...	...	...

LEVERAGE RATIOS (%)

	2012	2011	2010	2009	2008
Net premiums written to capital & surplus	15.4	...	...	...	...
Net technical reserves to capital & surplus	10.2	...	...	...	...
Gross premiums written to capital & surplus	33.3	...	...	...	...
Gross technical reserves to capital & surplus	23.0	...	...	...	...
Total debtors to capital & surplus	10.2	...	...	...	...
Total liabilities to capital & surplus	36.4	...	...	...	...

PROFITABILITY RATIOS (%)

	2012	2011	2010	2009	2008
Loss ratio	77.7	...	...	...	...
Operating expense ratio	90.3	...	...	...	...
Combined ratio	168.1	...	...	...	...
Other technical expense or (income) ratio	8.5	...	...	...	...
Net investment income ratio	36.3	...	...	...	...
Operating ratio	140.3	...	...	...	...
Return on net premiums written	-86.5	...	...	...	...

AMB CREDIT REPORT - INSURANCE PROFESSIONAL FOR

SAUDI UNITED COOPERATIVE INSURANCE COMPANY (WALA'A)

Operating Company Non-Life

Rabiah & Nasser Building, Dhahran Street, Al-Khobar 31952, Saudi Arabia
PO Box 31616, Al-Khobar 31952, Saudi Arabia
Web: www.walaa.com | Tel: 966-3-865-2200 | Fax: 966-3-865-2255
AMB#: 090704

Report Revision Date: 10/29/2012

BEST'S CREDIT RATINGS

Best's Financial Strength Rating: B++ Outlook: Stable
Best's Issuer Credit Rating: bbb Outlook: Stable

Best's Financial Size Category: VI

RATING RATIONALE

Rating Rationale: The ratings reflect Saudi United Cooperative Insurance Company's (Wala'a) good level of risk-adjusted capitalisation, developing local business profile and improving operating performance.

Good level of risk-adjusted capitalisation - - In A.M. Best's opinion, the level of risk-adjusted capitalisation of Wala'a is currently good. A.M. Best notes that although the level of risk-adjusted capitalisation is likely to reduce as the company grows, it is expected to remain at a good level over the medium term. Risk-adjusted capitalisation is supported by a relatively conservative allocation of investments and a reinsurance programme of good credit quality. The company's investments are inclined towards cash and term deposits, which account for over 70% of invested assets. The reinsurance programme includes both proportional and non-proportional cover with international and regional reinsurers that all maintain a Best's Financial Strength Rating (FSR) equivalent to or higher than "B++". Furthermore, Wala'a has been developing an enterprise risk management (ERM) framework, which at first instance is likely to encompass a review of internal processes and the creation of a risk matrix for all of the different departments; however, A.M. Best considers that it will take some time for the ERM framework to become fully embedded into the company's decision-making processes.

Developing local business profile - - Despite its start-up nature, Wala'a has been rapidly enhancing its position within the local Saudi Arabian insurance market. Currently, Wala'a ranks as the nineteenth-largest insurance company by gross written premiums (GWP) and ninth by net profit. In spite of being a relatively new operation, the company's management team and part of the founding shareholders were part of Amity Insurance Company, a company that operated in Saudi Arabia, from Bahrain, during the pre-regulatory era. As the company has been developing its identity, A.M. Best notes that there have been some considerable changes regarding its business mix; however, it is expected to remain more stable going forward with motor and medical business representing approximately 60% of GWP. The company is consolidating itself as a prominent player in the market; however, growth over the coming years is likely to be challenged by smaller players that compete on price and large players with good technical expertise and a favorable position in the market. The growth rate in 2010, the company's second year of operation, was over 50%; in 2011, it is likely to slow down to around 25%, and in 2012, it is likely to remain below 15%.

Improving operating performance - - The company's operating performance has improved in 2011, a year in which Wala'a had its first operational profit. In 2011, net profit before tax reached almost SAR 4.6 million

(USD 1.2 million), which represented a return on adjusted capital and surplus (ROACS) of 1.77%. The company's operating performance in 2011 was underpinned by an improved underwriting performance, with a combined ratio of 97%. Furthermore, given the company's conservative investment portfolio and, so far, decent level of returns from its equity investments, the company's investment performance is sound, supporting its overall profitability. In 2011, the investment yield was 0.46%; however, this figure does not reflect significant unrealised gains through the shareholders' fund. Nevertheless, A.M. Best notes that although the investment portfolio has remained stable, Wala'a has some exposure to equity investments that could give rise to future volatility. Moreover, according to the company's second-quarter 2012 results, the performance of Wala'a has further improved. The profit before tax stood at SAR 6.6 million (USD 1.8 million), 70% higher than the same period last year.

Over the medium term, an improvement in the company's risk-adjusted capitalisation while maintaining a good operating performance could place upward pressure on the ratings. A deterioration in financial performance or risk-adjusted capitalisation could add negative pressure to the ratings.

FIVE YEAR RATING HISTORY

	BEST'S	
Date	FSR	ICR
10/01/12	B++	bbb
09/21/09	NR	NR

BUSINESS PROFILE

Saudi United Cooperative Insurance Company (Wala'a) is a Saudi Joint Stock Company established in 2007. Although relatively new operation, most of its management team and a portion of their founding shareholders were part of Amity Insurance Company (Amity), a company that operated in Saudi Arabia, from Bahrain, during the pre-regulatory era. Saudi United operates through the brand name "Wala'a". The name was adopted in an attempt to differentiate the company from its competitors in an expectation that the Saudi insurance market would be flooded with a large number of new companies after new insurance regulations in the country. Wala'a transacts only non-life business and operates solely in the United Kingdom of Saudi Arabia through its branches and regional officers. The main shareholder of Wala'a is the International General Insurance Co. Ltd with 10.5% ownership share, the remaining shares are distributed through private individuals not owning more than 5% share each. In addition, 40% of the company's shares are publicly traded.

Although Wala'a is seen as a natural transition from Amity's operation, the company has opted to give the option to Amity clients to join the new recently formed company, instead of performing a portfolio transfer. Approximately 70% of Amity clients decided to join Wala'a and premium in 2009, the company's first full year of operation, reached just over USD 38 million. Since then, the company has been growing its premium base quickly. In 2010 premium's growth reached 54% and in 2011 around 27%. However, as the company grows, it is likely that challenges to grow its premium base will also increase as a result of fierce competition emanating from its competitors and the company's priority over profitable accounts rather than premium volume. Premium growth in 2011 is likely to remain below 15%.

The premium distribution of Wala'a has been taking form as the company grows. Although business mix is well distributed, it remains slightly concentrated over motor and medical where both lines have been representing approximately 60%. Nevertheless, A.M. Best notes a shift of distribution between these two business lines between 2011 and 2009. In 2009 motor accounted for approximately 40% of the gross written premium (GWP) and medical for the other 20%; however, in 2011 motor contribution decreased to 23% while medical increase to 35%. Motor business remains a source of loss for almost every company in Saudi Arabia and a shift towards more profitable lines is a natural process; However, although, motor business remains well demanded in the country, it is unlikely that Wala'a will increase its representativeness in relation to its entire portfolio as the company is tightening its underwriting guidelines and claims process. Furthermore, miscellaneous business represented the other 40% of total GWP in 2011. This is mostly represented by engineering, property business and casualty.

The company's net written premium (NWP) have been a little volatile in recent years reflecting the company's change in business mix and different levels of retention and reinsurance programmes for each business line. Given a lower retention levels in motor than in medical, and some concentration of motor business in 2009 retention levels were at 53% in that year, in 2010 retention levels increased to 67% mainly associated with the shift in the company's portfolio towards the medical business; however, as a result of two large engineering contracts in 2011 and the small retention associated with this and other general business lines, retention level has decreased to 52%. A.M best perceives a consolidation in the company's business mix going forward and a retention level between 50% to 55% is expected to be maintained over the coming years.

Motor business relates mainly to individual and small to medium size companies' fleet. The majority of the business is motor comprehensive with only a small share of compulsory third-party liabilities (TPL). TPL business is currently priced by SAMA and given the high level of indemnities the product is generally loss making. The medical business is mostly individuals and relates to the compulsory cover provided to expatriates and their families. This is the most competitive line within the local market and has been driving market overall premium growth in recent years, following the enforcement of the compulsory line.

Although the market is highly broken driven, Wala'a relies on its own sales team to distribute insurance across the Kingdom. Business distributed directly through the company's own commercial team and branches represented 40% of the business, agents accounted for approximately 35% and business emanating from brokers represented the remaining 15%. Going forward the company is looking into strengthening its broker relationship and business emanating from this channel is likely to increase.

RISK MANAGEMENT

The enterprise risk management framework is been developed as the company grows. The company has a risk manager which is in charge of developing the company's ERM framework in addition to provide actuarial services and other related functions. At the moment, the company has been investing time and resources in reviewing policies and procedures, updating its risk register and risk scores and identifying improvements that can be made in regards to its internal controls. In addition, Wala'a has recently set its risk tolerance and is using the risk-adjusted capitalisation model provided by the regulator to manage its capital exposures.

A.M Best considers Wala'a to have a sound reinsurance programme with good credit quality providing the company with a good level of capacity. The probable maximum loss (PML) is calculated based on average net retention, exposure of existing portfolio and previous loss experience. The company actively monitors its accumulation risk, based on its insurance exposure by Cresta Zones.

OPERATING PERFORMANCE

Operating Results: The performance of Wala'a has improved in 2011 after incurring consecutive operating losses in 2009 and 2010. This losses totalled USD 8.5 million. Additionally, although the company was not fully operative in 2008, Wala'a has also experienced losses related to general and administrative expenses that totalled USD 4 million. However, profit before tax reached USD 1.2 million in 2011 underpinned by an improved level of underwriting performance which returned over USD 1 million. Combined ratio (CoR), however, remained high at 97%. Investment income yielded 0.46% in the same period, influenced by low interest rates as most of the company's assets were placed within cash and deposits.

Furthermore, the financial performance in the first six months of 2012 improved compared to a similar period in 2011. Net profits in Q2 2012 reached USD 1.86 million, out of which, USD 1.26 million related to realized gains from its investment portfolio. Technical performance represented USD 602,000, 128% increase compared to Q2 2011.

Underwriting Results: Underwriting performance has been improving over the years and technical profitability has been achieved in the company's third year of operation. In 2011 underwriting profits reached USD 1 million after yielding losses of USD 7.4 million in 2009 and USD 2.1 million in 2010. As per A.M. Best calculation, CoR increased from 94% in 2010 to 97% in 2011. This is explained by the fact that reinsurance share of unearned premium reserves (UPR) is not factored into the expense ratio formula and in 2011 the company was benefited by a large reinsurance portion of unearned premium given a higher premium ceded. If reinsurance share of unearned premium was to be accounted for in the expense ratio, CoR would have been 95% in 2011 against a 101% in 2010.

The main source of profitability is the company's medical business which in 2011 had a CoR of 75% and reported a net profit of over USD 1.6 million. This line is expected to remain benefiting from a good level of expenses and loss ratio going forward. The casualty business has also had a good performance, mainly driven by the employer's liability business. Combined ratio stood at 34% and returned almost USD 1.6 million.

Motor business; however, remains offsetting part of the company's technical profitability. In 2011 the motor business returned losses of USD 2.3 million. A.M. Best notes that motor business represents the biggest challenge of Wala'a going forward and that the management is taking positive steps in regards to its motor book of business. The company has been reducing motor third-party liability (TPL) which has a higher combined ratio than the comprehensive business, closely reviewing the claims processing and carefully monitoring accounts with higher loss ratio. In addition, motor business has not been sold separately and a poor performance on the motor portfolio has been offset by a profitability in other business lines, on a client by client view.

Profitability for other lines of business is driven by marine business with CoR of 78.2% and offset by engineering with a combined ratio of 123.5% and property, 104.4%.

As per Q2 2012 results, underwriting profitability totalled USD 867,483 a significant improvement if compared to a loss of USD 2.4 million from the same period last year. Although top line remained at the same level, the company was able to achieve a better technical return by a lesser concentration on motor TPL business, tightening its claims management and reviewing its claims provisioning. AM. Best expects Wala'a to continue improving its underwriting profitability over the coming years as it builds its loss history, increases its premium volume and reduces the level of losses originated from its motor business.

Investment Results: The investment's portfolio of Wala'a is inclined towards cash and deposits which represented 80% of total invested in 2011. Equities investment totalled USD 12 million and represented another 16% of investments. The other 4% of total invested is placed with fixed income investments. Given the company's concentration of investment is cash and deposits which are placed with local banks in Saudi Arabia, investment yield is underlined by local interest rates which has been yielding approximately 1% in recent years.

Furthermore, A.M Best notes that the company has started to actively trade in equity investments in 2012. In the first quarter of 2012 investment on this class increased to 27% of total invested from 16% in December 2011. However, a portion of this investment was already sold on Q2 2012. The sale of equities on the second quarter of 2012 resulted in a realized gain of USD 1.26 million. A.M. Best does not expect investment on this class to surpass 30% of total invested.

BALANCE SHEET STRENGTH

Capitalization: In A.M. Best's opinion, the level of risk-adjusted capitalisation of Wala'a is currently good. Significant growth over the coming years is likely to have a negative impact on the company's level of risk-adjusted capitalisation. However, A.M. Best anticipates that it will be maintained at a good level. Furthermore, the capital base of Wala'a is protected by a reinsurance programme of good credit quality and a conservative investment profile.

The company started its operation in 2009 with losses brought forward of SAR 19 million (USD 5 million) as a result of initial operation costs and also incurred losses of SAR 36 million (USD 9.5 million) in the first two years of operation. As a result the company's capital base is currently under the minimum capital requirement by the regulator. The company has been already notified by SAMA which in reply has drawn a plan to restore its capital base. However this is under approval by the regulator.

In the meantime, the company has been focusing in restoring its capital from its own operational cash flow and it will not be distributing dividends until capital of SAR 200 million (USD 53.4 million) is reinstated. Capital appears to be improving at a large pace as a result of profits in 2011 and 2012 (until Q2). As per Q2 2012 capital increased 8% to SAR 162.2 million (USD 43.3 million) from SAR 150 million (USD 40 million) in 2010.

Loss Reserves: UPR and IBNR are reserved as per external actuarial study and updated quarterly by the company's in-house risk officer. Outstanding claims are set on a case by case basis and reviewed periodically until the claims are settled. According to the actuarial and in-house risk officer review, reserves are found to be sufficient.

Liquidity: A.M. Best considers Wala'a to have a good level of liquidity. At its 2011 year end, cash and term deposits were greater than net insurance liabilities by almost 200%. The picture is likely to be similar at the 2012 year end.

An independent audit of the company's affairs through December 31, 2011, was conducted by Deloitte & Touche Bakr Abulkhair & Co. and Ernst & Young.

Summarized Accounts as of December 31, 2011 (Unaudited)

Data reflected within all tables of this report has been compiled from the financial statements of this company (Source: Company Financial Statement).

US $ per Local Currency Unit .2667 = 1 Saudi Riyal (SAR)

STATEMENT OF INCOME

Technical account:	12/31/2011 SAR (000)	12/31/2011 USD (000)
Gross premiums written	278,560	74,292
Reinsurance ceded	135,076	36,025
Net premiums written	143,484	38,267
Increase/(decrease) in gross unearned premiums	33,348	8,894
Increase/(decrease) in reinsurers share unearned premiums	43,969	11,727
Net premiums earned	154,105	41,100
Other technical income	310	83
Total underwriting income	154,415	41,182
Net claims paid	91,201	24,323
Net increase/(decrease) in claims provision	10,074	2,687
Net claims incurred	101,275	27,010
Management expenses	33,549	8,948
Acquisition expenses	11,846	3,159
Net operating expenses	45,395	12,107
Other technical expenses	3,768	1,005
Total underwriting expenses	150,438	40,122
Balance on technical account	3,977	1,061

Non-technical account:		
Net investment income	1,201	320
Other income/(expense)	-601	-160
Profit/(loss) before tax	4,577	1,221
Taxation	1,875	500
Profit/(loss) after tax	2,702	721
Retained Profit/(loss) for the financial year	2,702	721
Retained Profit/(loss) brought forward	-54,840	-14,626
Retained Profit/(loss) carried forward	-52,138	-13,905

MOVEMENT IN CAPITAL & SURPLUS

	12/31/2011 SAR (000)	12/31/2011 USD (000)
Capital & surplus brought forward	150,128	40,039
Profit or loss for the year	2,702	721
Capital gains or (losses)	1,655	441
Total change in capital & surplus	4,357	1,162
Capital & surplus carried forward	154,485	41,201

ASSETS

	12/31/2011 SAR (000)	12/31/2011 % of total	12/31/2011 USD (000)
Cash & deposits with credit institutions	223,989	49.7	59,738
Bonds & other fixed interest securities	6,500	1.4	1,734
Shares & other variable interest instruments	41,624	9.2	11,101
Liquid assets	272,113	60.3	72,573
Unquoted investments	800	0.2	213
Mortgages & loans	2,473	0.5	660
Total investments	275,386	61.0	73,445
Reinsurers’ share of technical reserves - unearned premiums	74,893	16.6	19,974
Reinsurers’ share of technical reserves - claims	21,728	4.8	5,795
Total reinsurers share of technical reserves	96,621	21.4	25,769
Insurance/reinsurance debtors	57,260	12.7	15,271
Total debtors	57,260	12.7	15,271
Fixed assets	2,315	0.5	617
Prepayments & accrued income	19,509	4.3	5,203
Total assets	451,091	100.0	120,306

LIABILITIES

	12/31/2011 SAR (000)	12/31/2011 % of total	12/31/2011 USD (000)
Capital	200,000	44.3	53,340
Paid-up capital	200,000	44.3	53,340
Non-distributable reserves	6,624	1.5	1,767
Retained earnings	-52,138	-11.6	-13,905
Capital & surplus	154,486	34.2	41,201
Minority interests	601	0.1	160
Gross provision for unearned premiums	137,803	30.5	36,752
Gross provision for outstanding claims	71,458	15.8	19,058
Total gross technical reserves	209,261	46.4	55,810
Insurance/reinsurance creditors	67,465	15.0	17,993
Total creditors	67,465	15.0	17,993
Accruals & deferred income	17,787	3.9	4,744
Other liabilities	1,491	0.3	398
Total liabilities & surplus	451,091	100.0	120,306

MANAGEMENT

The management team of Wala'a have good experience of both the local and regional markets, enabling the company to achieve a good market position in just few years of operation while improving profitability. However, as the KSA insurance market matures, conditions are becoming increasingly competitive and profit margins are likely to reduce. A.M. Best considers that challenges for management over the coming years will include growing the business in accordance with business plans. While the management team of Wala'a has been developing new partnerships and adding new products to its portfolio, it will need good strategic plans to further enhance the company's position

OFFICERS

CEO: Johnson Varughese
Vice President: Salah Mohammed Al Jaber (Sales & Marketing)
Vice President: Wasif F. Minhas (Technical)

DIRECTORS

Walid Al Jaaferi
Wasef Salim Al Jabsheh
Wasif Al Jabsheh
Sulaiman Abdullah Al Kadi (Chairman)
Abdullah Mohammed Al Othman (Vice Chairman)
Khalid Abdulrahman Al Rajhi
Abdulaziz Saleh Al Rebdi
Walid Suhayl Al Shoaibi
Dr. Sulaiman A. Al Twaijri

ANALYSIS OF GROSS PREMIUMS WRITTEN

	SAR (000) 2011	SAR (000) 2010	SAR (000) 2009	2008	2007
Accident & health	98,541	36,493	28,014	...	...
Automobile	63,415	113,818	56,700	...	...
Other classes	88,152	48,102	40,777	...	...
Property	28,452	21,584	17,429	...	...
Total non-life	278,560	219,997	142,920	...	...

REINSURANCE

A.M. Best believes that Wala'a has a comprehensive reinsurance programme placed with reinsurances of good credit quality. The company's reinsurance protection is formed of quota share, surplus and excess of loss covers, with Wala'a having sufficient retention and capacity within each business line. Medical, motor and marine risks are reinsured on an excess of loss basis. Property and Engineering are protected with proportional reinsurance treaties that provide quota-share and surplus protection in addition to an excess of loss cover. General accidents business is protected under the property and engineering excess of loss cover.

All reinsurers maintain an international credit rating equal to or higher than A.M. Best Financial Strength Rating (FSR) "B++". Furthermore, the leaders of the company's reinsurance programmes are strongly rated international reinsurers with good technical expertise.

GEOGRAPHICAL DISTRIBUTION OF PREMIUMS WRITTEN

	SAR (000) 12/31/2011 Gross	12/31/2011 % of total	SAR (000) 12/31/2010 Gross
Middle East	278,560	100.0	219,997
Total Asia	278,560	100.0	219,997
Total	278,560	100.0	219,997

BALANCE SHEET ITEMS

	SAR (000) 2011	SAR (000) 2010	SAR (000) 2009	SAR (000) 2008	SAR (000) 2007
Liquid assets	272,113	238,796	213,457	181,513	...
Total investments	275,386	242,019	216,180	182,313	185,898
Total assets	451,091	369,095	359,524	186,870	187,517
Total gross technical reserves	209,261	162,504	123,341	...	...
Net technical reserves	112,640	113,187	67,817	...	...
Total liabilities	296,605	218,965	205,325	5,840	359
Capital & surplus	154,486	150,130	154,199	181,030	187,158

INCOME STATEMENT ITEMS

	SAR (000) 2011	SAR (000) 2010	SAR (000) 2009	SAR (000) 2008	SAR (000) 2007
Gross premiums written	278,560	219,997	142,920	...	...
Net premiums written	143,484	147,523	75,686	...	...
Balance on technical account(s)	3,977	-7,910	-27,863	...	...
Profit/(loss) before tax	4,577	-6,984	-25,087	-14,787	...
Profit/(loss) after tax	2,702	-8,909	-26,961	-18,970	...

LIQUIDITY RATIOS (%)

	2011	2010	2009	2008	2007
Total debtors to total assets	12.7	15.7	21.1	...	...
Liquid assets to net technical reserves	241.6	211.0	314.8	...	...
Liquid assets to total liabilities	91.7	109.1	104.0	999.9	...
Total investments to total liabilities	92.8	110.5	105.3	999.9	999.9

LEVERAGE RATIOS (%)

	2011	2010	2009	2008	2007
Net premiums written to capital & surplus	92.9	98.3	49.1	...	...
Net technical reserves to capital & surplus	72.9	75.4	44.0	...	...
Gross premiums written to capital & surplus	180.3	146.5	92.7	...	...
Gross technical reserves to capital & surplus	135.5	108.2	80.0	...	...
Total debtors to capital & surplus	37.1	38.7	49.3	...	...
Total liabilities to capital & surplus	192.0	145.9	133.2	3.2	0.2

PROFITABILITY RATIOS (%)

	2011	2010	2009	2008	2007
Loss ratio	65.7	67.0	112.7	...	...
Operating expense ratio	31.6	26.5	25.5	...	...
Combined ratio	97.4	93.5	138.3	...	...
Other technical expense or (income) ratio	2.4	4.4	5.3	...	...
Net investment income ratio	0.8	0.8	7.8	...	...
Operating ratio	99.0	97.1	135.8	...	...
Return on net premiums written	1.9	-6.0	-35.6	...	...
Return on total assets	0.7	-2.4	-9.9	-10.1	...
Return on capital & surplus	1.8	-5.9	-16.1	-10.3	...

A Best's Financial Strength Rating opinion addresses the relative ability of an insurer to meet its ongoing insurance obligations. The ratings are not assigned to specific insurance policies or contracts and do not address any other risk, including, but not limited to, an insurer's claims-payment policies or procedures; the ability of the insurer to dispute or deny claims payment on grounds of misrepresentation or fraud; or any specific liability contractually borne by the policy or contract holder. A Best's Financial Strength Rating is not a recommendation to purchase, hold or terminate any insurance policy, contract or any other financial obligation issued by an insurer, nor does it address the suitability of any particular policy or contract for a specific purpose or purchaser.

A Best's Debt/Issuer Credit Rating is an opinion regarding the relative future credit risk of an entity, a credit commitment or a debt or debt-like security.

Credit risk is the risk that an entity may not meet its contractual, financial obligations as they come due. These credit ratings do not address any other risk, including but not limited to liquidity risk, market value risk or price volatility of rated securities. The rating is not a recommendation to buy, sell or hold any securities, insurance policies, contracts or any other financial obligations, nor does it address the suitability of any particular financial obligation for a specific purpose or purchaser.

In arriving at a rating decision, A.M. Best relies on third-party audited financial data and/or other information provided to it. While this information is

GUIDE TO BEST'S FINANCIAL STRENGTH RATINGS

A Best's Financial Strength Rating is an independent opinion of an insurer's financial strength and ability to meet its ongoing insurance policy and contract obligations. The rating is based on a comprehensive quantitative and qualitative evaluation of a company's balance sheet strength, operating performance and business profile.

Financial Strength Ratings

	Rating	Descriptor	Definition
Secure	A++, A+	Superior	Assigned to companies that have, in our opinion, a superior ability to meet their ongoing insurance obligations.
	A, A-	Excellent	Assigned to companies that have, in our opinion, an excellent ability to meet their ongoing insurance obligations.
	B++, B+	Good	Assigned to companies that have, in our opinion, a good ability to meet their ongoing insurance obligations.
Vulnerable	B, B-	Fair	Assigned to companies that have, in our opinion, a fair ability to meet their ongoing insurance obligations. Financial strength is vulnerable to adverse changes in underwriting and economic conditions.
	C++, C+	Marginal	Assigned to companies that have, in our opinion, a marginal ability to meet their ongoing insurance obligations. Financial strength is vulnerable to adverse changes in underwriting and economic conditions.
	C, C-	Weak	Assigned to companies that have, in our opinion, a weak ability to meet their ongoing insurance obligations. Financial strength is very vulnerable to adverse changes in underwriting and economic conditions.
	D	Poor	Assigned to companies that have, in our opinion, a poor ability to meet their ongoing insurance obligations. Financial strength is extremely vulnerable to adverse changes in underwriting and economic conditions.
	E	Under Regulatory Supervision	Assigned to companies (and possibly their subsidiaries/affiliates) placed under a significant form of regulatory supervision, control or restraint - including cease and desist orders, conservatorship or rehabilitation, but not liquidation - that prevents conduct of normal, ongoing insurance operations.
	F	In Liquidation	Assigned to companies placed in liquidation by a court of law or by a forced liquidation.
	S	Suspended	Assigned to rated companies when sudden and significant events affect their balance sheet strength or operating performance and rating implications cannot be evaluated due to a lack of timely or adequate information.

Rating Modifiers

Modifier	Descriptor	Definition
u	Under Review	Indicates the rating may change in the near term, typically within six months. Generally is event driven, with positive, negative or developing implications.
pd	Public Data	Indicates rating assigned to insurer that chose not to participate in A.M. Best's interactive rating process. (Discontinued in 2010)
s	Syndicate	Indicates rating assigned to a Lloyd's syndicate.

Outlooks

Indicates potential direction of a Financial Strength Rating over an intermediate term, generally defined as 12 to 36 months.

Positive	Indicates possible rating upgrade due to favorable financial/market trends relative to the current rating level.
Negative	Indicates possible rating downgrade due to unfavorable financial/market trends relative to the current rating level.
Stable	Indicates low likelihood of a rating change due to stable financial/market trends.

Not Rated Designation

NR: Assigned to companies that are not rated by A.M. Best.

Rating Disclosure

A Best's Financial Strength Rating opinion addresses the relative ability of an insurer to meet its ongoing insurance obligations. The ratings are not assigned to specific insurance policies or contracts and do not address any other risk, including, but not limited to, an insurer's claims-payment policies or procedures; the ability of the insurer to dispute or deny claims payment on grounds of misrepresentation or fraud; or any specific liability contractually borne by the policy or contract holder. A Best's Financial Strength Rating is not a recommendation to purchase, hold or terminate any insurance policy, contract or any other financial obligation issued by an insurer, nor does it address the suitability of any particular policy or contract for a specific purpose or purchaser. In arriving at a rating decision, A.M. Best relies on third-party audited financial data and/or other information provided to it. While this information is believed to be reliable, A.M. Best does not independently verify the accuracy or reliability of the information. For additional details, see A.M. Best's *Terms of Use* at *www.ambest.com*.

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GUIDE TO BEST'S DEBT AND ISSUER CREDIT RATINGS

A Best's Debt/Issuer Credit Rating is based on a comprehensive quantitative and qualitative evaluation of a company's balance sheet strength, operating performance and business profile and, where appropriate, the specific nature and details of a rated debt security.

Long-Term Credit Ratings

A Best's Long-Term Debt Rating, assigned to specific issues such as debt and preferred stock, is an independent opinion of an issuer/entity's ability to meet its ongoing financial obligations to security holders when due.

	Rating	Descriptor	Definition
Investment Grade	aaa	Exceptional	Assigned to issues where, in our opinion, the issuer has an exceptional ability to meet the terms of the obligation.
	aa	Very Strong	Assigned to issues where, in our opinion, the issuer has a very strong ability to meet the terms of the obligation.
	a	Strong	Assigned to issues where, in our opinion, the issuer has a strong ability to meet the terms of the obligation.
	bbb	Adequate	Assigned to issues where, in our opinion, the issuer has an adequate ability to meet the terms of the obligation; however, the issue is more susceptible to changes in economic or other conditions.
Non-Investment Grade	bb	Speculative	Assigned to issues where, in our opinion, the issuer has speculative credit characteristics, generally due to a moderate margin of principal and interest payment protection and vulnerability to economic changes.
	b	Very Speculative	Assigned to issues where, in our opinion, the issuer has very speculative credit characteristics, generally due to a modest margin of principal and interest payment protection and extreme vulnerability to economic changes.
	ccc, cc, c	Extremely Speculative	Assigned to issues where, in our opinion, the issuer has extremely speculative credit characteristics, generally due to a minimal margin of principal and interest payment protection and/or limited ability to withstand adverse changes in economic or other conditions.
	d	In Default	Assigned to issues in default on payment of principal, interest or other terms and conditions, or when a bankruptcy petition or similar action has been filed.

A Best's Long-Term Issuer Credit Rating is an opinion of an issuer/entity's ability to meet its ongoing senior financial obligations.

Ratings from "aa" to "ccc" may be enhanced with a "+" (plus) or "-" (minus) to indicate whether credit quality is near the top or bottom of a category.

Short-Term Credit Ratings

A Best's Short-Term Debt Rating is an opinion of an issuer/entity's ability to meet its financial obligations having original maturities of generally less than one year, such as commercial paper.

	Rating	Descriptor	Definition
Investment Grade	AMB-1+	Strongest	Assigned to issues where, in our opinion, the issuer has the strongest ability to repay short-term debt obligations.
	AMB-1	Outstanding	Assigned to issues where, in our opinion, the issuer has an outstanding ability to repay short-term debt obligations.
	AMB-2	Satisfactory	Assigned to issues where, in our opinion, the issuer has a satisfactory ability to repay short-term debt obligations.
	AMB-3	Adequate	Assigned to issues where, in our opinion, the issuer has an adequate ability to repay short-term debt obligations; however, adverse economic conditions likely will reduce the issuer's capacity to meet its financial commitments.
Non-Investment Grade	AMB-4	Speculative	Assigned to issues where, in our opinion, the issuer has speculative credit characteristics and is vulnerable to adverse economic or other external changes, which could have a marked impact on the company's ability to meet its financial commitments.
	d	In Default	Assigned to issues in default on payment of principal, interest or other terms and conditions, or when a bankruptcy petition or similar action has been filed.

A Best's Short-Term Issuer Credit Rating is an opinion of an issuer/entity's ability to meet its senior financial obligations having original maturities of generally less than one year.

Rating Modifiers

Both Long- and Short-Term Credit Ratings can be assigned a modifier. Note: The public data modifier did not apply to Short-Term Credit Ratings, which are only assigned on an interactive basis.

Modifier	Descriptor	Definition
u	Under Review	Indicates the rating may change in the near term, typically within six months. Generally is event driven, with positive, negative or developing implications.
pd	Public Data	Indicates rating assigned to a company that chose not to participate in A.M. Best's interactive rating process. (Discontinued in 2010)
i	Indicative	Indicates rating assigned is indicative.

Outlooks

Indicates the potential direction of a Credit Rating over an intermediate term, generally defined as 12 to 36 months.

Positive	Indicates possible rating upgrade due to favorable financial/market trends relative to the current rating level.
Negative	Indicates possible rating downgrade due to unfavorable financial/market trends relative to the current rating level.
Stable	Indicates low likelihood of a rating change due to stable financial/market trends.

Not Rated Designation

The Not Rated (NR) designation may be assigned to issuers or issues that are not rated.

Rating Disclosure

A Best's Debt/Issuer Credit Rating is an opinion regarding the relative future credit risk of an entity, a credit commitment or a debt or debt-like security. Credit risk is the risk that an entity may not meet its contractual, financial obligations as they come due. These credit ratings do not address any other risk, including but not limited to liquidity risk, market value risk or price volatility of rated securities. The rating is not a recommendation to buy, sell or hold any securities, insurance policies, contracts or any other financial obligations, nor does it address the suitability of any particular financial obligation for a specific purpose or purchaser. In arriving at a rating decision, A.M. Best relies on third-party audited financial data and/or other information provided to it. While this information is believed to be reliable, A.M. Best does not independently verify the accuracy or reliability of the information. For additional details, see A.M. Best's *Terms of Use* at *www.ambest.com*.

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A.M. BEST AT A GLANCE

A.M. Best is a leading provider of ratings, news and financial data with a specialist focus on the worldwide insurance industry. Best's Credit Ratings are recognised as the benchmark for assessing the financial strength of insurance-related organisations and the credit quality of their obligations.

- Established in the U.S. in 1899 and pioneered the concept of financial strength ratings in 1906
- Worldwide headquarters in New Jersey, U.S.; regional centres in London (serving Europe, Middle East and Africa) and Hong Kong (serving Asia and Oceania). Representative offices located in Dubai (serving MENA, South & Central Asia) and Miami (serving Latin America)
- Full-service global ratings capabilities
- Over 3,300 ratings in approximately 75 countries worldwide
- Extensive marketing and publishing capability to promote corporate ratings in local and international markets

Market Coverage

Insurance-related companies operating in various markets, including:

- Property/casualty (non-life) insurers
- Life insurers and annuity writers
- Health insurers
- Reinsurers
- Mutual insurers and Protection & Indemnity (P&I) clubs
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- Lloyd's and its syndicates
- New company formations ("start-ups")
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Competitive Strengths

- Only international rating agency dedicated to the insurance industry
- World's leading provider of insurer Financial Strength Ratings (FSRs) by company coverage
- Foremost rating coverage of the global reinsurance segment
- Leading position in international (re)insurance hubs—including comprehensive coverage of Lloyd's/London market, Bermuda, Zurich
- Leading rating agency for ART and captives coverage
- Key rating agency used by global broker security teams
- Data and research covering 15,000 (re)insurance companies worldwide
- Largest and most comprehensive insurance database providing unique insights by segment and line of business
- Published rating methodology on all key insurance industry segments

Research & News

- Publishers of frequent specialised reports on global insurance industry issues, including sector, company and geographic regional analysis. Extensive global insurance news delivery and resources

Best's Credit Ratings:
The Global Symbol of Financial Strength

RATING DEFINITIONS

Best's Financial Strength Ratings (FSRs) provide an opinion of an insurer's financial strength and ability to meet its ongoing insurance policy and contract obligations.

Best's Issuer Credit Ratings (ICRs) provide an opinion of an entity's ability to meet its ongoing senior financial obligations.

Best's Debt Ratings (DRs) provide an opinion as to the issuer's ability to meet its ongoing financial obligations to security holders when due.

A rating by A.M. Best is based on a comprehensive evaluation of an insurance company's financial strength, operating performance and business profile. A.M. Best also regularly publishes Impairment Studies, which evaluate rating performance over time.

BEST'S CREDIT RATING SCALES

Comparison of Financial Strength Rating (FSR) to Credit Market Scale

	FSR	ICR/DR	
Secure	A++	aaa aa+	Investment Grade
	A+	aa aa-	
	A	a+ a	
	A-	a-	
	B++	bbb+ bbb	
	B+	bbb-	
Vulnerable	B	bb+ bb	Non-Investment Grade
	B-	bb-	
	C++	b+ b	
	C+	b-	
	C	ccc+ ccc	
	C-	ccc- cc	
	D	c	
	E, F	d	

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for Secure-Rated Insurers

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- Thousands of financial professionals worldwide via news vendors such as Reuters, Dow Jones and NewsEdge
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For more information about A.M. Best's ratings of Takaful insurers, please contact:

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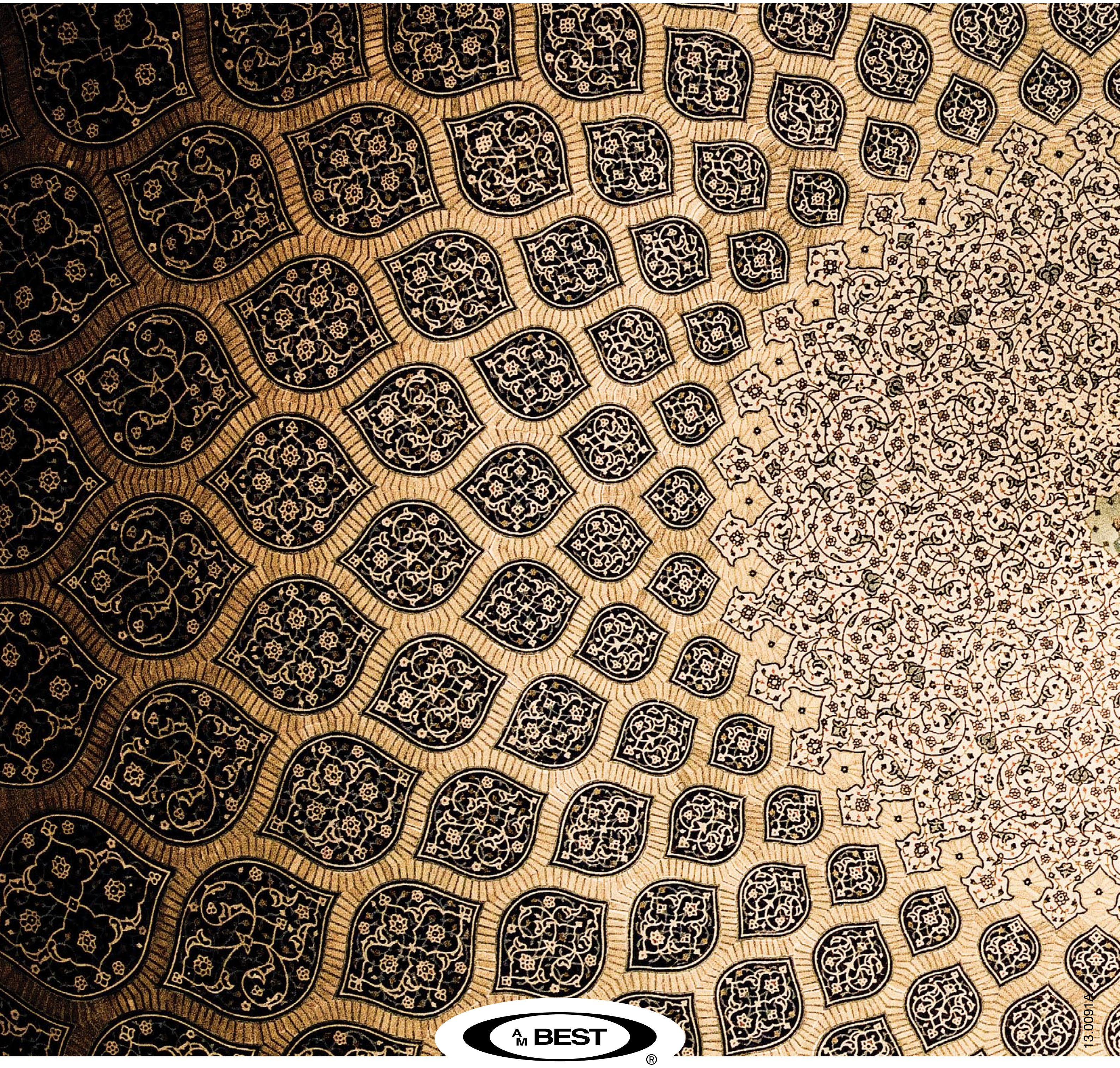

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