

Qatar Insurance Co. S.A.Q.

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RATING A- (STRONG)

An insurer rated 'A' has strong financial security characteristics, but is somewhat more likely to be affected by adverse business conditions than are insurers with higher ratings.

HOLDING COMPANY

None

GROUP MEMBERS

None

DOMICILE

Qatar

LICENSED

Qatar, Saudi Arabia, UAE, Kuwait

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Issuer trailer

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Rating description

STRONG



RatingsDirect
Publication Date

Aug. 25, 2005

Rating explanation

An insurer rated 'A' has strong financial security characteristics, but is somewhat more likely to be affected by adverse business conditions than are insurers with higher ratings.

Major Rating Factors

Strengths:

- Strong competitive position;
- Very strong capitalization;
- Very strong historical operating performance; and
- Proven management team.

Weaknesses:

- Potential for adverse operational volatility;
- Lack of geographical diversity;
- Very high reliance on reinsurance protection; and
- Locally concentrated investment portfolio.

Rationale

The ratings on Qatar-domiciled underwriter Qatar Insurance Co. S.A.Q. (QIC) reflect the company's strong and established competitive position, very strong capitalization, very strong operating performance, and proven management team and control structure. These factors are partially offset by the potential for adverse operational volatility and lack of geographical diversity in the classes of business upon which QIC focuses, its very high reliance on reinsurance protection, and the heavy local concentration of its investment portfolio.

QIC is a quoted company on the Doha Securities Market (DSM), and the Qatari government has retained a 12% stake in the company since its establishment in 1964.

QIC has a strong competitive position in the State of Qatar (A+/Positive/A-1), where it is the leading "national" insurance company, a status that gives it the right to quote to lead underwrite for all government-sponsored project risks. The Qatari economy is expanding significantly as the government develops liquid natural gas resources and invests in the supporting infrastructure—developments that will require substantial insurance protection. It is expected that QIC's "national" insurer status will be maintained for the foreseeable future.

QIC's capitalization, quality of capital, and capital adequacy are very strong, and therefore a rating strength. QIC's capital adequacy is expected to remain very strong, being supported in 2005 by a rights issue, the proceeds of which will be in part used to finance its operations across the Gulf Cooperation Council (GCC) region. Key risks to capital arise through the very locally focused investment portfolio and QIC's very high dependence upon reinsurance. Nevertheless, capital adequacy is considered able to absorb the potential economic investment risk. The strength of the reinsurance relationships and security of the leading reinsurers used by QIC alleviate this risk. Financial flexibility is considered strong, as demonstrated by the rights issue in the first quarter of 2005. Capital growth from the establishment of the company in 1964 has been solely internally financed through profit retention.

QIC's management is a positive factor for the ratings, having been with the company since the early 1990s and proven itself through its track record of sound earnings and capital growth.

In view of the track record of the risk portfolio and the strengths of management, Standard & Poor's Ratings Services expects QIC to continue to post strong results. Nevertheless, the energy/petrochemical focus of the risk book may lead to increased volatility in operating performance.

Outlook

The stable outlook on QIC reflects Standard & Poor's expectation that the overall financial and risk profiles will remain materially unchanged, and also incorporates the following expectations:

- QIC will maintain its strong competitive position in Qatar through controlled growth as the country's risk base develops further.
- QIC will continue to expand its underwriting presence across the GCC region through closely managed strategic investments.
- QIC's capitalization will remain very strong and not be eroded materially through growth.
- QIC will maintain profitable gross and net operating performances and be in a position to deliver increasing returns to shareholders.
- QIC will continue to maintain very high reinsurance leverage, reflecting the very significant gross value at risk from the core commercial/industrial risks, but deliver good profits thereto.
- QIC's investment portfolio will continue to carry a heavy local focus, with high exposure to equities.

Table 1

Qatar Insurance Co. S.A.Q./Selected Statistics					
	—Year ended Dec. 31—				
(000s QAR)	2004	2003	2002	2001	2000
Total net premiums written	125,129.0	96,973.0	95,839.0	92,489.0	82,318.0
Total revenue*	225,873.0	186,171.0	167,877.0	141,432.0	128,049.0
Non-life (%)	51.5	52.3	56.5	62.5	60.5
Other (%)	48.5	47.7	43.5	37.5	39.5
Core operating result	130,630.0	98,874.0	88,768.0	71,263.6	66,643.0
Non-life (%)	18.7	13.1	20.8	28.7	27.4
Other (%)	81.3	86.9	79.2	71.3	72.6
Net income (before bonus allocation)	128,402.0	96,080.0	86,390.0	69,227.6	64,442.0
Net income	128,402.0	96,080.0	86,390.0	69,227.6	64,442.0
Total assets	1,754,928.0	1,313,078.0	973,362.0	850,069.0	673,613.0
Total equity	1,439,269.0	1,064,054.0	746,174.0	633,877.0	486,564.0

*Based on allocated investment income. QAR—Qatari riyal.

Competitive Position

Table 2

Qatar Insurance Co. S.A.Q./Business Statistics					
—Year ended Dec. 31—					
(000s QAR)	2004	2003	2002	2001	2000
Total gross premiums written	548,560.0	406,666.0	343,944.0	262,632.0	230,676.0
Annual change (%)	34.9	18.2	31.0	13.9	(8.2)
Total net premiums written	125,129.0	96,973.0	95,839.0	92,489.0	82,318.0
Annual change (%)	29.0	1.2	3.6	12.4	17.8
Total assets under management	1,640,740.0	1,228,744.0	901,642.0	742,927.0	579,475.0

QAR—Qatari riyal.

QIC has a strong and market-leading domestic competitive position, and this is expected to continue. The strength of this position reflects the technical capabilities and performance of the company over the long term, as well as its essentially protected status in Qatar as a “national” insurer. QIC is the largest of these, which status offers first refusal to underwrite all government-sponsored project risks; Standard & Poor’s expects this status to be maintained for the foreseeable future. Note that the public sector in Qatar represents some 70% of GDP.

In terms of premium volume, QIC has long been the largest Qatari insurer; summary 2003 data from the Qatari Ministry of Economy & Commerce shows that QIC had a 46% market share, and this grew further in 2004. QIC underwrites primarily in Qatar, where it is the leading company, but also via branches in Abu Dhabi and Dubai (an open insurance market) of the UAE, and Saudi Arabia (as a following underwriter only). QIC established branch operations in Kuwait in May 2005 and a subsidiary in Oman in October 2004, working with local partners.

The State of Qatar is undergoing very significant economic development as it seeks to exploit its gas/energy reserves, thus creating opportunities for the local insurance markets—and for QIC—to participate in the underwriting of these major projects and the related infrastructure development.

QIC demonstrates a stable business relationship with key Qatari businesses in marine, aviation, and energy project development. QIC participates in the risk-pricing decisions and acts as partner in project risk management alongside intermediaries and the banks that introduce finance capital to the projects. Certain of these projects are of very significant economic size, thereby necessitating extensive participation by the international insurance market, to which QIC acts as primary feed through its risk cession, retaining only a small share of these project risks.

QIC is able to demonstrate leading shares of Qatari marine, fire, and workers’ accident risks. Standard & Poor’s expects QIC to maintain its overall leading position in Qatar and to further grow its business both domestically—in response to the expanding Qatari economy—and in other GCC countries.

Management And Corporate Strategy

QIC management is viewed as strong. QIC’s goal is to develop its position in the GCC to become one of the leading regional insurers, with operations in all GCC countries focusing on commercial/industrial risks. The company’s longer term target market is the whole Arabic-speaking marketplace. QIC has established operations in Abu Dhabi and Dubai of the UAE, Saudi Arabia, Kuwait, and Oman.

QIC’s management and underwriting teams have the necessary skills to develop and supervise the risk management process of the GCC commercial/industrial risk markets, which is the key

business focus. QIC's long-term historical profitability—at gross and net underwriting levels—indicates the success of the team, although to some extent this should be viewed in the context of the generally strong underwriting profitability trends demonstrated by local GCC region insurers. QIC targets new business sectors to be profitable within three years; the overall financial objectives are to increase profits annually and to deliver an enhanced annual return.

QIC has shifted its participation in the very competitive local motor market to comprehensive motor cover for cars less than three years old, from the tariff-controlled and unprofitable third-party motor liability business, which action has delivered better earnings.

QIC management intends to take full advantage of the economic growth of the region, but has in place control procedures to ensure that it does not overextend itself and expose its capital base to excessive risk. QIC aims to underwrite only business that is individually profitable; there is no client cross-subsidy philosophy. The management team is stable and has a long track record in the insurance industry, both locally and in the U.K. The management structure reflects the traditional approach of separating financial and underwriting management. There is also a separate investment committee, supported by external consultants that advise, recommend, and review the company's investment program. QIC's internal audit function is subcontracted to Ernst & Young, which reviews both financial and operational performance, controls, and procedures, reporting independently and directly to the QIC board.

Operating Performance

Table 3

Qatar Insurance Co. S.A.Q./Operating Statistics					
	—Year ended Dec. 31—				
(000s QAR)	2004	2003	2002	2001	2000
Total revenue*	225,873.0	186,171.0	167,877.0	141,432.0	128,049.0
Core operating profit	130,630.0	98,874.0	88,768.0	71,263.6	66,643.0
Realized gains/core operating profit (%)	53.8	50.2	45.9	3.6	(0.0)
Net income	128,402.0	96,080.0	86,390.0	69,227.6	64,442.0
Post-tax ROE (%)	10.3	10.6	12.5	12.4	13.5
Total profitability ratio (%)	10.3	10.6	12.5	12.4	13.5
Total gross expense ratio (%)	8.7	8.9	9.4	10.5	10.6
Administrative expense ratio (%)	38.1	37.4	33.6	29.9	29.7
Acquisition expense ratio (%)	(12.0)	(14.7)	(17.5)	(12.0)	(10.8)
Nontechnical expenses/total revenue (%)	2.5	3.0	3.0	3.0	3.4
Nontechnical expenses/total assets (bps)	32.4	43.1	52.3	50.1	64.7
<i>Nonlinked portfolio composition (%)</i>					
Bonds and other fixed-interest securities	9.7	14.2	19.4	15.7	11.3
Equities and other variable-interest securities	61.3	57.7	50.8	47.0	32.1
Property	2.8	2.6	3.9	5.1	5.7
Cash and bank deposits	19.0	17.9	17.7	19.8	24.7
Other investments	7.3	7.6	8.2	12.4	26.2
Total nonlinked investments	100.0	100.0	100.0	100.0	100.0

*Based on allocated investment income. QAR—Qatari riyal. Bps—Basis points.

QIC's earnings profile is very strong, and Standard & Poor's expects the company to continue to be strongly profitable at both the gross and net underwriting levels. The annual performance

profile at both the gross and net underwriting levels continues to be materially better than European or global insurers' norms, and compares well within the GCC region. The 2004 combined ratio of 79% and the return on average shareholder funds of 10.3% compare well with QIC's respective five-year averages of 80% and 11.9%. Standard & Poor's expects that QIC's performance will not demonstrate any material deviation from these averages in 2005.

QIC's gross underwriting earnings expectations are sensitive to the very significant event risks and probable maximum losses of the major energy sector risks it underwrites. However, the reinsurance protection program reduces the net sensitivity. The GCC region is not susceptible to natural catastrophes.

Investments

Standard & Poor's considers QIC's investment portfolio to be appropriate for the company. Although somewhat aggressive, with more than 60% of the portfolio in equities, it offers very generous liquidity cover to the loss reserves. QIC's investment quality is constrained by the Qatari market asset concentration risk, particularly since the bulk of the gross risks are largely denominated in U.S. dollars. Nevertheless, the ongoing peg between the Qatari riyal (QAR) and the U.S. dollar limits the foreign exchange risk.

The DSM index increased by 66% in 2004 (71% in 2003) and a further 55% at midyear 2005, and this very high level of growth is prompted by Qatar's dramatic economic growth prospects and the burgeoning local demand for investment opportunities. Such a sharp rate of increase raises a serious risk of a sharp corrective drop, but the 'A+' local currency sovereign credit rating on the State of Qatar eases Standard & Poor's concerns, as Standard & Poor's believes the government will support the local economy. The DSM presents little opportunity for investment diversity, having only 31 tradable stocks. Although QIC has a readily liquid portfolio, such a narrow investment market creates increased risk of a very material local loss, whereupon the ability to liquidate equity holdings and other investments at market value—if at all possible—may be compromised, creating adverse pricing and some liquidity strains. The DSM index has performed very strongly over the past three years, having significantly outgrown the European and GCC markets.

Qatari government bonds are almost entirely locally held and generate favorable yields. QIC has a small, controlled exposure through sales of puts to derivative contracts relating to Qatari government bonds. There are no naked calls, only covered calls/puts, and the maximum downside risk created is considered easily containable within the company's liquid resources. All options have maturities within six months and are managed daily to ensure minimal adverse loss. QIC's investment committee, which comprises QIC board members, sanctions all derivative-type transactions, and receives regular performance reports.

QIC is planning to invest in the development of new residential real estate in Qatar, which will shift the investment portfolio balance toward less liquid real estate. But the level of capital supporting the company can absorb a strained level of investment risk, which is unlikely to be materially reduced in the coming year.

Liquidity

Liquidity is considered strong. QIC has a very liquid balance sheet, with 84% of total assets at Dec. 31, 2004, in readily liquid form as cash deposits, marketable bonds, and equities. On average from 1998, readily liquid assets have covered technical reserve provisions by more than 8x. Insurance and reinsurance receivables indicate good credit control and pose a manageable bad debt

risk. QIC has maintained positive underwriting and operating cash flow and has suffered no liquidity problems in prior years. All incurred losses have been settled out of current cash flow. QIC benefits from unused letters of credit issued by Standard Chartered Bank (A/Stable/A-1) and HSBC Bank PLC (AA-/Stable/A-1+) for \$25 million and QAR15 million (\$4.1 million, at \$0.27 to 1QAR), respectively. These are fully committed, but non-fee-bearing facilities.

QIC is erecting a 20-floor office block in Doha, and expects to occupy four or five floors, with the rest (75%) let to third parties. There is a QAR60 million capital commitment to this project, which it is management's intention to self-finance, although there is the option to use external finance. This project will secure cash flows and derive benefit from the booming Qatari development market. Standard & Poor's considers this project to be affordable to QIC without straining the company's ongoing liquidity or earnings.

Capitalization

Capitalization is considered very strong in terms of quality of capital and capital adequacy as assessed by Standard & Poor's risk-based capital model. Capital adequacy is expected to remain very strong despite the growth plans for the company. QIC's one-for-four rights issue in 2005 took advantage of the current very buoyant investment climate in the region, and the funds will help the real estate development. QIC's management believes that QIC will need no new capital to support the underwriting activities until gross premiums written reach QAR1.5 billion, which is not expected in the foreseeable rating time frame. Standard & Poor's expect that the very strong level of capital adequacy in percentage terms will moderate in the future, reflecting the company's underwriting risk expansion, although very strong capital adequacy should be maintained.

QIC is expected to continue its prudent reserving practices. Standard & Poor's does not expect any significant adverse reserve developments, either on a case-by-case basis or in the broader loss determination/legal liability development area. The company's exposure is essentially to short-tail risk, with loss triangulations pointing to an average development of less than three years, although engineering/hull risks can stretch to five years. There is no long-tail liability exposure. Losses are initially reserved at maximum, and international loss adjusters and reinsurers are fully involved throughout the claims process.

The nature of QIC's risk base and the international insurance market create a very highly leveraged reinsurance program, with QIC having ceded 77% of gross premiums written in 2004 (76% in 2003). Its portfolio of reinsurers is, however, diverse, amounting to about 20 companies, and includes the international leaders—Munich Reinsurance Co. (A+/Stable/—) and Swiss Reinsurance Co. (AA/Negative/A-1+)—as well as regional companies. Facultative protection accounts for 88% of reinsurance, and treaty 12%. Catastrophic energy losses are capped at QAR9 million net any one event, and QAR2.5 million any other event. Thus, current subscribed capital can absorb 16 energy loss events, while total shareholder funds at Dec. 31, 2004, can absorb more than 100 energy loss events.

Financial Flexibility

Table 4

Qatar Insurance Co. S.A.Q./Financial Statistics					
(000s QAR)	—Year ended Dec. 31—				
	2004	2003	2002	2001	2000
Total assets	1,754,928.0	1,313,078.0	973,362.0	850,069.0	673,613.0
Change in total assets (%)	33.6	34.9	14.5	26.2	7.6
Total equity	1,439,269.0	1,064,054.0	746,174.0	633,877.0	486,564.0
Change in adjusted equity (%)	35.3	42.6	17.7	30.3	4.5
Total capital	1,439,269.0	1,064,054.0	746,174.0	633,877.0	486,564.0
Group solvency measure (x)	63.9	61.0	43.3	38.1	32.8
Dividends/net income (%)	94.8	83.1	84.0	86.7	46.6
Investment leverage (incl. quasi capital) (%)	73.0	69.7	66.2	61.0	45.1
Liquid assets/technical reserves (%)	1,533.4	1,344.5	908.1	804.6	581.4
Reinsurance utilization ratio (%)	77.2	76.2	72.1	64.8	64.3
Technical reserves/net premium written (%)	76.9	84.6	91.0	82.4	82.5
Loss reserves/net premium written (%)	41.0	47.5	53.0	44.0	44.4
Net claims reserves/net claims incurred (%)	86.9	73.8	83.3	79.4	83.6
Net claims paid/ net claims incurred (%)	91.0	107.7	83.4	91.8	99.5

QAR—Qatari riyal.

Financial flexibility is strong relative to QIC's modest level of possible needs. This is supported by the success of the one-for-four rights issue in June 2005, which raised QAR600 million. Prior to this event, all of the company's capital growth following inception had been entirely internally financed through retained earnings. Historical and prospective operating performance is such that it is considered highly likely that any fund raising would be successful, particularly in light of the demand for investment opportunities in Qatar.

Of the current shareholders (which number 900), the largest are the State of Qatar (12.0%) and Qatar National Bank (not rated; 4.8%). Sixteen other shareholders (individuals and local companies) hold up to 2% apiece. Each director of QIC must hold 1% of shares. No international insurance group has any significant shareholding interest in QIC.

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