

## ISSUER COMMENT

5 February 2020

✓ Rate this Research

### RATINGS

Insurance Financial Strength	A3
Rating Outlook	Negative

Source: Moody's Investors Service

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## Walaa Cooperative Insurance Company

Merger with Metlife AIG ANB will bring synergies, but poses short-term downside risks

On 28 January 2019, Walaa Cooperative Insurance Company (Walaa, A3 negative) confirmed that it plans to proceed with a merger with Metlife AIG ANB Insurance Company (Metlife AIG ANB), a small composite insurer in Saudi Arabia. The merger will be executed via a share swap that will increase Walaa's shareholder capital to an estimated SAR646.4 million from SAR528 million<sup>1</sup>.

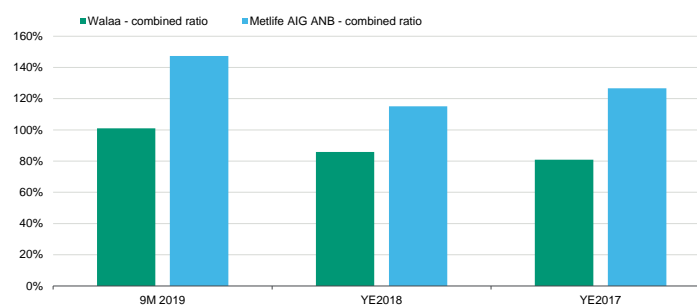
The merger poses some short-term downside risks to Walaa's underwriting profitability, as Metlife AIG ANB has recently reported weak underwriting results. As it strives to return the Metlife business to profitability, we expect the merged entity to also address deficiencies raised by the regulator, particularly concerning Metlife AIG ANB's internal controls and risk management. We [changed the outlook on Walaa to negative from stable on 2 July 2019](#) to reflect these risks.

Most of Metlife AIG ANB's premiums come from health insurance, a highly competitive line of business in Saudi Arabia with some exposure to protection and savings business. The company has recently reported weak underwriting results due to a combination of intense competition and underwriting inefficiency, with its combined ratio for the first nine months of 2019 deteriorating to 147% from 115% at year-end 2018 (Exhibit 1).

The consolidated impact of Metlife's weak financial performance on the merged entity's books will however be limited due to the company's small size. Metlife accounted for just 15% of Walaa's gross premiums in 2018. In addition, given Walaa's superior underwriting performance, we expect the enlarged group to take corrective action to return the Metlife book to profitability.

Exhibit 1

**Metlife AIG ANB has reported weak underwriting results in recent years**  
 Combined ratio (Moody's calculations)



Sources: Companies' annual reports, Quarterly reports and Moody's Investors Service

The merger will bring long-term benefits to Walaa if successfully executed, including diversification into protection and savings products. The company will also gain access to a new client and business-partner base. We expect demand for protection and savings lines to increase in the long term amid rising consumer awareness of these products. The government's plan to reduce subsidies to Saudi nationals are also supportive.

The merger will also add a bancassurance partner ([Arab National Bank](#), A2 stable) to Walaa's distribution mix, bringing further diversification benefits. The transaction will also generate operational efficiencies and cost savings as the merged entity starts sharing back office operations such as finance, IT and HR.

Walaa is strongly capitalised, and comfortably meets the regulatory solvency requirement. As of YE2018, it reported a gross underwriting leverage of 2.3x which is comparable to A-rated regional peers.

Its capitalisation benefited from an increase in paid up capital of SAR40 million via a rights issue in 2018, and has been reinforced further by retained profits, reflecting the company's no cash dividend strategy. While the merger may result in a marginal capital deterioration in the short-term due to losses at Metlife AIG ANB, we foresee no material impact on the merged entity. Overall, we expect its gross underwriting leverage to be around 2.5x to 3.0x in the medium term for the merged entity.

The merged entity will also benefit from a diversified shareholder mix, including new anchor investors such as [Metlife ALICO](#) (A3 stable), [Arab National Bank](#) (A2 stable) and [AIG](#) (Baa1 stable). Currently, Walaa has only one shareholder accounting for more than 5% of its share capital, IGI Insurance Company Limited.

#### Methodologies used:

- » [Property and Casualty Insurers Methodology](#)
- » [Life Insurers Methodology](#)

#### Moody's related publications

- » [Walaa Cooperative Insurance Company - Credit Opinion](#), July 2019

#### Endnotes

- 1 Excluding policyholders' surplus, which is included in Moody's consolidated equity

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