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Research Update:

Outlook On Saudi Arabia-Based Wala'a Cooperative Insurance Co. Revised To Positive; Ratings Affirmed At 'BBB+'

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Table Of Contents

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Overview

- In our view, Wala'a Cooperative Insurance Co. (Wala'a), which operates in the Saudi Arabia non-life insurance market, is a successful, growing insurer, that writes both commercial and retail lines.
- We view Wala'a's risk position at moderate, given management's ambitious growth and diversification plans, which may also include growth by acquisition should suitable opportunities arise.
- We are revising to positive from stable our outlook on our ratings on Wala'a, while affirming our 'BBB+' global, long-term financial strength rating, and our 'gcAA+' Gulf Cooperation Council regional scale financial strength rating.
- The positive outlook indicates that we could raise the ratings on Wala'a in the outlook period to mid-2020 if the company continues to perform strongly while prudently growing and diversifying its operations and steadily raising its capital base toward Saudi riyal 1.0 billion.

Rating Action

On Jan. 30, 2018, S&P Global Ratings revised to positive from stable the outlook on its insurer financial strength rating on Saudi Arabia-based Wala'a Cooperative Insurance Co. Ltd. (Wala'a), and affirmed the rating at 'BBB+'. At the same time, we affirmed our Gulf Cooperation Council regional scale financial strength rating at 'gcAA+'.

Rationale

Our ratings on Wala'a (which formerly traded as Saudi United Cooperative Insurance Co.) reflect our view that the company has established itself as a successful insurer in Saudi Arabia that principally writes commercial lines. Wala'a is Saudi Arabia's sixth-largest insurer (of 32) in terms of gross premiums, and fourth in terms of net income and capitalization. Although it is still somewhat modest in size by global standards, the company continues to grow steadily and profitably, and management is taking selective advantage of the business opportunities that arise as peer companies restructure their operations.

For full-year 2017, we estimate that Wala'a's gross premiums rose by about 10% to Saudi riyal (SAR) 1.1 billion (2016: SAR1.0 billion). Of this, about 25% was ceded to reinsurers, so we expect 2017 net premium income to be about SAR830 million (2016: SAR755 million). In the latest published interim report for end-September 2017, nine-month gross premiums of SAR801.8 million broke down as 61.8% motor (both retail and fleet), 10.8% property, 8.7% group medical, 8.0% engineering, and 10.7% other, largely commercial lines including accident and liability, marine, aviation, and energy. At the net level, after ceded reinsurance, retained premium income of SAR594.5 million to end-September 2017 was significantly more concentrated--82.8% motor, 11.6% group medical, 0.6% property, 0.4% engineering, and 4.6% other lines. We expect the full-year 2017 accounts, when published, to reflect a similar breakdown of business.

Meanwhile, net income for the first nine months of 2017 proved very satisfactory at SAR112.2 million (September 2016: SAR91.0 million) with a net claims ratio of 55.3% (September 2016: 55.8%) and a net expense ratio of 23.9%. This causes us to expect an equally satisfactory net combined ratio (claims + expenses / net premiums earned) of about 87% for 2017 (2016: 87.1%). In our view, this implies that Wala'a is successfully on track for achieving very robust technical results, supplemented by positive, if modest, returns on its low-risk, essentially cash-based investments. That said, it should be noted that none of our estimates above take into account the potential, industrywide impact of the newly-introduced value-added tax (VAT) at 5%, which may have to be levied against all Saudi Arabia-based insurers' existing unearned premium reserves.

In terms of Wala'a's financial risk profile, which we now assess as moderately strong by global standards, we note that the full retention of earnings in recent years--supplemented by a successful SAR200 million rights issue in 2015--had helped shareholders' funds rise to SAR546.4 million by end-September 2017 or, we estimate, to around SAR575 million by year-end 2017. Under our model, these figures suggest extremely strong capital adequacy under all realistic scenarios. Moreover, we would expect extremely strong capital adequacy ratios to be maintained, with retained earnings proving sufficient to maintain capital adequacy at extremely strong levels, despite ambitious planned business growth. That said, capital adequacy could be adversely affected if management were to make an acquisition in its domestic market--which we believe to be conceivable should a suitable opportunity arise.

At present, however, we incorporate the risks associated with Wala'a's possible growth by acquisition into our assessment of the risk position, which we regard as somewhat elevated. We nevertheless remain confident that senior management at Wala'a would not enter into any strategic venture without undertaking full and effective due diligence. Moreover, if the likely cost of any potential acquisition were to prove substantial, we would expect management to consider a further increase in capital so as to maintain its capital adequacy at extremely strong levels.

When undertaking our review of Wala'a, we also took into account its management and governance practices, which we now assess as satisfactory. It has particular strengths in strategic planning and standards of operational performance. Liquidity remains exceptional, given Wala'a's strongly positive cash flows and its largely cash-based investment strategies, with no debt or debt-servicing requirements. We also assessed Wala'a's enterprise risk management (ERM) practices and have found them to be entirely adequate for a company of still relatively modest size, which operates in a single jurisdiction selling predominantly straightforward contracts and exhibits a generally short-tail claims profile.

Outlook

The positive outlook reflects our belief that we could raise our rating on Wala'a by one notch during the outlook period to mid-2020 if current satisfactory trends continue in respect of earnings, business growth, diversification, and capital generation. Retained earnings are expected to prove sufficient to offset the capital strain of normal business, although we would expect management to consider raising additional capital if, for example, a specific acquisition were to be actively considered.

Upside scenario

We could raise our ratings on Wala'a if the company continues to successfully implement its strategies, thereby combining ongoing profitable business growth, greater diversification by line of business, and an increase in absolute levels of capitalization sufficient to create a capital platform equivalent to approximately SAR1.0 billion.

Downside scenario

The outlook could be revised to stable if capital adequacy at Wala'a were to decline without management taking effective remedial action, or if ongoing improvements in ERM controls were to fail to keep pace with any significant increase in the size or complexity of the insurer's operations

Ratings Score Snapshot

	To	From
Financial Strength Rating	BBB+/Positive/--	BBB+/Stable/--
Anchor	bbb+	bbb+
Business Risk Profile	Satisfactory	Satisfactory
IICRA	Intermediate	Intermediate
Competitive Position	Adequate	Adequate
Financial Risk Profile	Moderately strong	Upper adequate
Capital and Earnings	Strong	Moderately strong
Risk Position	Moderate risk	Moderate risk
Financial Flexibility	Adequate	Adequate
Modifiers	0	0
ERM and Management	0	0
Enterprise Risk Management	Adequate	Adequate
Management and Governance	Satisfactory	Fair
Holistic Analysis	0	0
Liquidity	Exceptional	Exceptional
Support	0	0
Group Support	0	0

	To	From
Government Support	0	0

IICRA--Insurance Industry And Country Risk Assessment

Related Criteria And Research

Related Criteria

- General Criteria: National And Regional Scale Credit Ratings - September 22,2014
- General Criteria: Group Rating Methodology - November 19,2013
- General Criteria: S&P Global Ratings' National And Regional Scale Mapping Tables - August 14,2017
- General Criteria: Use Of CreditWatch And Outlooks - September 14,2009
- General Criteria: Methodology: Management And Governance Credit Factors For Corporate Entities And Insurers - November 13,2012
- Criteria - Insurance - General: Enterprise Risk Management - May 07,2013
- Criteria - Insurance - General: Insurers: Rating Methodology - May 07,2013
- Criteria - Insurance - General: Refined Methodology And Assumptions For Analyzing Insurer Capital Adequacy Using The Risk-Based Insurance Capital Model - June 07,2010

Ratings List

	Rating	
	To	From
Wala'a Cooperative Insurance Co. Ltd.		
Financial Strength Rating		
Local Currency	BBB+/Positive/--	BBB+/Stable/--
Gulf Cooperative Council Regional Scale	gcAA+/--/--	gcAA+/--/--

Certain terms used in this report, particularly certain adjectives used to express our view on rating relevant factors, have specific meanings ascribed to them in our criteria, and should therefore be read in conjunction with such criteria. Please see Ratings Criteria at www.standardandpoors.com for further information. Complete ratings information is available to subscribers of RatingsDirect at www.capitaliq.com. All ratings affected by this rating action can be found on S&P Global Ratings' public website at www.standardandpoors.com. Use the Ratings search box located in the left column. Alternatively, call one of the following S&P Global Ratings numbers: Client Support Europe (44) 20-7176-7176; London Press Office (44) 20-7176-3605; Paris (33) 1-4420-6708; Frankfurt (49) 69-33-999-225; Stockholm (46) 8-440-5914; or Moscow 7 (495) 783-4009.

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