Kuwait-Based Warba Ins. Co. K.S.C. Assigned 'BBB' Ratings; Outlook Stable

- Kuwait-based multiline insurer Warba Insurance (Warba) has strong capitalization and good earnings. It has a good competitive position in Kuwait, albeit with a concentrated and marginal investment portfolio.
- We are assigning our 'BBB' insurer financial strength and counterparty credit ratings to Warba.
- The stable outlook reflects our expectations that the company's capitalization will remain strong, and that earnings will be good.

DUBAI (Standard & Poor's) Sept. 25, 2012--Standard & Poor's Ratings Services today assigned its 'BBB' insurer financial strength and counterparty credit ratings to Warba Ins. Co. KSC (Warba). The outlook is stable.

The ratings on Kuwait-based insurer Warba reflect its strong capitalization, good earnings, and good local competitive position. These strengths are constrained by the marginal quality and concentration of the investment portfolio, and, to a lesser extent, our assessment of enterprise risk management as weak.

Warba's capitalization is strong, and therefore a key strength for the rating.
Capitalization is supported by extremely strong capital adequacy, which we expect to continue and fully support the company's local expansion. In the medium term, we expect capital adequacy to strengthen and become less sensitive to asset value volatility in response to a managed shift in the company's investment strategy. This should see a fall in market risk capital demands. High utilization of reinsurance and material asset concentrations within the investment portfolio are negative aspects of capitalization.

Warba has a good competitive position in its domestic market, where it maintains a market share of 11%. One of Kuwait's original five national companies, Warba is listed and has very stable ownership. These factors support its access to business in the local market. We expect premium growth in 2012-2013 to be about 7%, in line with Kuwaiti market norms and reflective of Warba's good competitive position. Growth will likely be stronger in the life and medical lines.

Warba generates good earnings derived from its underwriting, which delivered a combined ratio in 2011 of 91%, against a five-year average of 86%. Returns on revenue are strong, averaging over 20%, and returns on equity (RoE) have averaged more than 4% in the last five years. However, RoE has weakened as both underwriting and investment yields have declined in response to rising competition and falling asset returns. Our base-case scenario is that the combined ratios will be lower than 95% and RoE will be about 3% over our two-year rating horizon.

The company's investment portfolio is marginal; it carries a significant equity and real estate focus (54% and 25% of total invested funds, respectively, at end-2011). The scale of these investments gives relatively high investment leverage at 73% of shareholder funds in 2011, and currently exposes the company to meaningful asset volatility. The equity investments are predominantly in local banks. Liquid assets give strong cover to net technical reserves at 5.6x, and net claims reserves are covered by cash deposits 2.8x.

While we assess enterprise risk management as weak, this is not currently a key ratings constraint in view of Warba's strong capitalization and local operational focus. Key weaknesses are the lack of any sophistication in establishing and formally monitoring risk appetite. That said, we expect risk management will develop favorably over the next two-to-three years, with the establishment of more definitive risk appetites for underwriting and investments.

The stable outlook reflects our expectation that Warba will maintain at least strong capitalization, and that earnings will continue to be good, for the next two years.

While we are unlikely to consider an upgrade over the next two years, upward ratings pressure could be prompted by reduced investment risk, enhancements to risk management practices, and improved earnings.

Negative rating action may arise if the company does not meet our expectations, and capital strength is materially eroded through underwriting loss or investment volatility.