Kuwait-Based Warba Insurance Co. Downgraded To 'BBB'; Outlook Negative

- In our opinion, Warba's competitive position has weakened due to a decline in premium income over the past two years, alongside pronounced earnings volatility emanating from both underwriting and investments.
- At the same time, Warba's liquidity and capital adequacy has deteriorated because of additional technical reserves created in 2017.
- Warba's management and governance--particularly given the audit qualifications in 2016 and major restatements in 2017--could create additional strain on the company's creditworthiness.
- We are therefore downgrading Warba to 'BBB' from 'BBB+'.
- The negative outlook points to a possible downgrade by one or more notches if Warba's capital adequacy and/or liquidity deteriorate further, or in the event of any severe governance deficiencies.

DUBAI (S&P Global Ratings) July 25, 2018--S&P Global Ratings today lowered its long-term issuer credit and financial strength ratings on Kuwait-based Warba
Insurance Co. K.S.C.P. to 'BBB' from 'BBB+'. The outlook is negative.

The downgrade points to our view that Warba's competitive position has gradually weakened over the past couple of years due to poor performance, both on the underwriting and investments levels. In 2016 and 2017, Warba recorded a drop in its gross written premium by 5% and 12%, respectively, and reported net losses amounting to Kuwaiti dinar (KWD) 1.9 million in 2016 and KWD0.8 million in 2017. Warba's five-year average net combined (loss and expense) ratio is about 106%, making it a technically unprofitable company. While Warba considers this GWP drop as its dedicated efforts to stop writing loss-making business in order to improve its net combined ratio, the upside of this exercise has yet to materialize.

Warba's 2017 audited financial statements highlighted a material restatement relating to 2016 numbers, whereby as a result of a reserve strengthening exercise, Warba's shareholder's equity as at Dec. 31, 2016, deteriorated to KWD34.2 million from KWD43.5 million. This affected Warba's previously robust capital adequacy and its liquidity profile.

Weak spots in Warba's management and governance structure have emerged due to financial reporting issues. In terms of Warba's accounting records, the 2016 audited financial statements included three qualifications with respect to deferred commission expense, life and medical reserves, and impairment on investments. While the 2017 audited financial statements did not have any qualifications, the major reclassifications and reserve volatility indicate weakness in its financial reporting standards and operational effectiveness.
Any further unexpected reclassifications or audit qualifications could result in a protracted period of financial reporting issues, which may indicate severe governance deficiencies.

The negative outlook reflects our view that Warba's capital adequacy, and liquidity may deteriorate further unless Warba's management implements an effective strategy to correct these profiles.

We could lower the ratings by one or more notches over the next two years if:

- Warba's capital adequacy and/or liquidity continue to deteriorate because of an additional reserve strengthening exercise, accounting reclassifications, or significant premium growth; or
- We assessed material weakness in Warba's management and governance framework due to its continued inability to resolve financial reporting issues.

We could revise our outlook to stable over the next two years if:

- Warba broadly maintains its market share, while technical results gradually improve and there is no further deterioration in Warba's capital adequacy and liquidity; or
- There are no further significant deficiencies in its management and governance structure whether in its financial reporting standards or its corporate strategy.