

## CREDIT OPINION

27 July 2023

Update



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### RATINGS

#### Walaa Cooperative Insurance Company

Domicile	Saudi Arabia
Long Term Rating	A3
Type	Insurance Financial Strength - Fgn Curr
Outlook	Stable

Please see the [ratings section](#) at the end of this report for more information. The ratings and outlook shown reflect information as of the publication date.

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# Walaa Cooperative Insurance Company

## Update to credit analysis post rating affirmation

### Summary

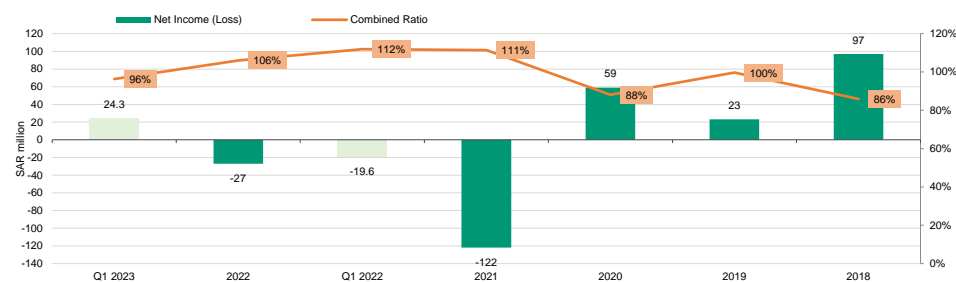
Walaa Cooperative Insurance Company (Walaa) is rated A3 for insurance financial strength (IFSR). Based in Saudi Arabia, Walaa is a top tier local insurer underwriting property and casualty as well as life insurance with its life portfolio growing post the merger with Metlife AIG ANB Insurance Company (Metlife AIG ANB) and more recently in 2022 post the SABB Takaful Company (SABB Takaful) merger.

Walaa's A3 IFSR reflects its strong market position and brand, as the fifth largest insurer in Saudi Arabia, and good business diversification that limits its exposure to the highly competitive and price-sensitive retail motor and medical lines. Walaa's financial profile is underpinned by strong asset quality, resulting from its conservative investment strategy, good capital and reserve adequacy, along with good financial flexibility given its low leverage and demonstrated access to capital. These strengths are offset by Walaa's lack of geographic diversification outside of Saudi Arabia and assertive growth strategy, that together have contributed to weak underwriting performance and pressure on capitalization over the past two years.

Furthermore, market wide weak underwriting performance in 2021 and 2022, driven by competitive pressures on premium rates and adverse claims developments, had a negative impact on Walaa's profitability, with its combined ratio deteriorating to 111% and 106% for 2021 and 2022, respectively, from 88% in 2020. More positively the recent results of Q1 2023 show that Walaa, alongside the wider market, has improved its underwriting performance with Walaa reporting a net income of SAR24.3 million for Q1 2023 compared to a net loss of SAR19.6 million for the same period last year.

Exhibit 1

### Walaa's profitability indicators



All combined ratios based on IFRS 4, on IFRS 17 basis Q1 2023 is 103% and Q1 2022 111%

Source: Moody's Investors Service and Company's filings

In 2021 in order to maintain the company's solvency margin as it pursues its growth plan for the next three to five years in the expanding Saudi insurance market, Walaa's board of directors recommended a SAR775 million (\$206 million) rights issue to increase the company's paid capital by 120%. The SABB Takaful merger and the related capital raise of SAR294 million raise was in line with the strategy recommended by the board. Going forward, we expect Walaa's improved underwriting performance and any future capital raise, to support strengthening capital adequacy.

### Credit strengths

- » Strong market position and brand in the Saudi Arabian insurance market
- » Strong asset quality, driven by a conservative investment strategy
- » Good capital adequacy level
- » Good reserve adequacy

### Credit challenges

- » Competitive Saudi Arabian property and casualty insurance market
- » Balancing business growth whilst maintaining good underwriting profitability

### Rating outlook

The stable rating outlook reflects Moody's expectation that Walaa will maintain good levels of profitability, will grow its business with underwriting discipline and adjust its growth plan if necessary to maintain its capital adequacy.

### Factors that could lead to an upgrade:

- » Strengthening of its market position, with for example, reaching a top three position in Saudi Arabia in terms of premiums revenues
- » Improved profitability, with return on capital of over 15% and combined ratio under 90%
- » Further business line diversification, with for example a more balanced mix of profit generating revenues between several major lines of business

### Factors that could lead to a downgrade:

- » Deterioration in capital adequacy, with for example, GUL exceeding 3.5x or business growth outpacing growth in capital
- » Deterioration in profitability, with return on capital remaining below 4% and combined ratios over 100%
- » Its market position in Saudi Arabia falling out of the top seven in terms of premiums
- » Deterioration in asset quality with high risk assets (HRA) as a percentage of consolidated equity of over 60%, or the loss of A-rated reinsurance support
- » Deterioration in reserve adequacy or increased level of reserve risk

This publication does not announce a credit rating action. For any credit ratings referenced in this publication, please see the issuer/deal page on <https://ratings.moody's.com> for the most updated credit rating action information and rating history.

## Key indicators

Exhibit 2

### Walaa Cooperative Insurance Company [1][2]

Walaa Cooperative Insurance Company [1][2]	2022	2021	2020	2019	2018
<b>As Reported (Saudi Riyal Millions)</b>					
Total Assets	4,882	3,447	2,880	2,033	1,997
Total Shareholders' Equity	1,069	813	925	670	682
Net Income (Loss) Attributable to Common Shareholders	(27)	(122)	59	23	97
Gross Premiums Written	2,642	2,339	1,473	1,215	1,105
Net Premiums Written	1,336	1,156	864	750	746
<b>Moody's Adjusted Ratios</b>					
High Risk Assets % Shareholders' Equity	37.5%	56.7%	31.5%	38.0%	23.9%
Reinsurance Recoverable % Shareholders' Equity	115.2%	145.6%	78.8%	62.4%	53.3%
Goodwill & Intangibles % Shareholders' Equity	15.8%	12.1%	9.1%	2.7%	3.7%
Gross Underwriting Leverage	3.4x	3.9x	2.2x	2.5x	2.3x
Return on Average Capital (ROC)	-3.2%	-13.9%	6.6%	2.8%	13.9%
Sharpe Ratio of ROC (5 yr.)	11.9%	48.3%	135.0%	471%	41.8%
Adv. (Fav.) Loss Dev. % Beg. Reserves	26.4%	55.5%	253.4%	-24.4%	-39.5%
Adjusted Financial Leverage	4.2%	4.7%	3.9%	3.6%	5.4%
Total Leverage	4.2%	4.7%	3.9%	3.6%	5.4%
Earnings Coverage	-7.2x	-127.4x	111.3x	NM	107.9x
Cash Flow Coverage	NA	NA	NA	NA	NA

[1] Information based on IFRS financial statements as of the fiscal year ended 31/12/2022. [2] Certain items may have been relabeled and/or reclassified for global consistency.

Sources: Moody's Investors Service and company filings

### Consideration of Accounting Changes: IFRS

The new insurance accounting regime, IFRS 17 and IFRS 9, is effective from 1 January 2023. The application of the new IFRS may significantly affect the overall presentation of financial statements as well as certain reported amounts, including shareholders' equity, insurance liabilities, revenue and net income. Scorecard metrics whose inputs are affected by the application of the new IFRS may result in values and unadjusted scores that are significantly different from what was reported under the company's legacy reporting. However, these will not directly affect Walaa's creditworthiness as the group's underlying economic position and performance remains unchanged.

### Profile

Walaa was incorporated in 2008 as a property and casualty insurer in Saudi Arabia. Headquartered in Al Khobar, Walaa has over 70 branches in Saudi Arabia and provides a broad range of general and health insurance lines of products within the country. It also sell life insurance products post the merger with Metlife AIG ANB in 2020.

### Detailed credit considerations

#### Market position and brand: Strong market position in Saudi Arabia

Walaa has a strong market position in Saudi with 5.1% market share and ranks as the 5th largest player in this market in 2022 (from 4th in 2021) by premiums having gross premiums written (GPW) of SAR2.6 billion. The market position has strengthened over the past couple of years, improving from 2019's 6th position with a market share of 3.2% which in itself was a significant improvement over the 11th position it held back in 2014.

The company has a wide branch network with around 70 branches over Saudi Arabia. In addition, the successful merger with Metlife AIG ANB has benefitted the market position of Walaa with the addition of other underwriting lines of health, protection and savings, which are key growth areas in Saudi Arabia. Furthermore, the additional successful merger with SABB Takaful will benefit Walaa with the addition of more protection and savings lines.

However we remain watchful of Walaa's continued growth as the Saudi insurance market is highly competitive, given the dominant position of the top 3 insurers which represented 61% of the market in terms of premiums in 2022 and the resulting weak underwriting performance and pressure on capitalization over the past two years.

### Product focus and diversification: Broad product diversification provides some offset to concentrated exposure to Saudi market

Walaa's GPW mix has lower concentration to medical and motor as seen in most GCC insurers with the 2022 mix of gross premiums written fairly diverse including medical (25% of GPW), energy (24%), motor (17%), property & engineering (14%), other P&C lines (12%) and protection & savings (8%).

In terms of product risk, the motor and medical portfolio generally presents low severity but high frequency risk. The company is also exposed to some negligible CAT risk arising from rare flood events, but it is sufficiently covered by A-rated reinsurance excess of loss cover across all LoBs. Additionally in terms of high severity risks (energy, property, casualty and engineering which contributed for 53% of GPW in 2022, Walaa's retention remains conservative.

In terms of geographic diversification, similar to most GCC peers, Walaa is concentrated to a single country. However Saudi Arabia benefits from a much larger population than other GCC countries, thus having more potential and geographic spread. We think Walaa will be able to reap the benefits of operating in a large country due to its extensive branch network.

The successful execution of its mergers with Metlife AIG ANB and SABB Takaful will give rise to benefits in the medium-long term with further diversification of its insurance revenues into protection and savings.

### Asset Quality: Equity investments decreased in 2022, and the mix of invested assets is still conservative

Walaa's strong quality of invested asset is a result of the management's decision to maintain strong regulatory solvency levels. About 50% of the invested assets was in cash and bank deposits as at YE 2022, up from 41% in 2021. Equity investments accounted for 22% of invested assets as at YE 2022, and fixed income investments were 28% of total investments whilst it continues to have no real estate exposure. The conservative investment profile remains a constant feature of the company. However, all investments are within Saudi Arabia and deposits are with local banks which leads to concentration risk albeit similar to Saudi peers.

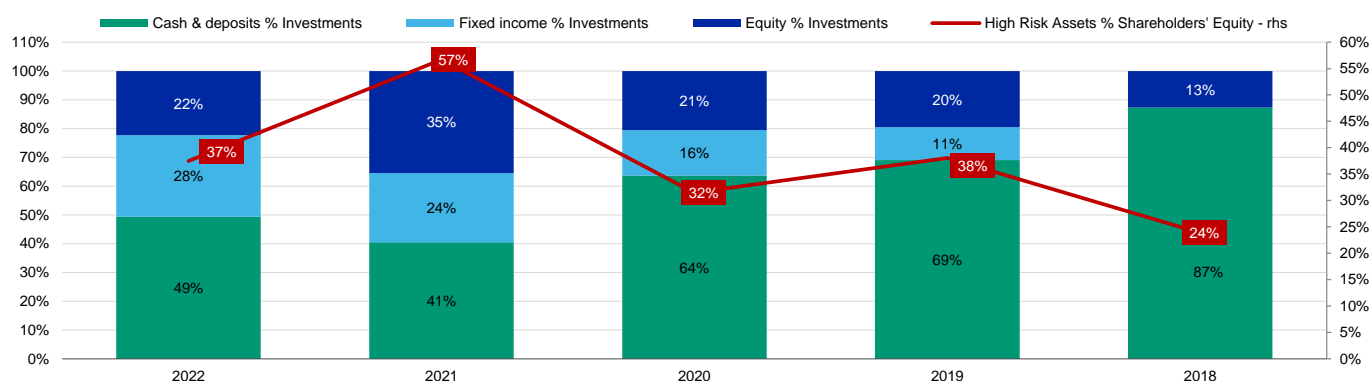
The HRA % of shareholders' equity was strong at 37.5% at YE 2022 and was lower than the 56.7% reported at YE 2021 due to improvement in shareholder's equity as well as reduction of high-risk assets (Exhibit 3). Reinsurance recoverable % of shareholders' equity decreased to 115.2% in 2022 from 145% in 2021.

Similar to most other Gulf Cooperation Council (GCC) insurers, Walaa has a strong reinsurance coverage from A rated reinsurers. The panel includes [Everest Re](#) (A1, STA), [Saudi Re](#) (A3, STA) and [SCOR](#) (A1, STA).

Goodwill and intangibles previously comprised of deferred acquisition costs however the ratio increased to 15.8% as at YE 2022 from 9.1% at YE 2020, with the increase largely on account of the goodwill recognised post the Metlife merger as well as other intangible assets from the SABB Takaful merger.

Exhibit 3

### Investment quality continues to be good, with lower equity exposure and high cash/fixed income



Source: Moody's Investors Service and Company's filings

### Capital Adequacy: Good capital driven by capital raise used to offset deterioration from underwriting pressures

As concerns capitalisation, we view Walaa's capital adequacy as good with gross underwriting leverage (GUL) of 3.4x in 2022. However, capital levels had deteriorated during 2021 and part of 2022 due to high premium growth and weak underwriting performance, against a backdrop of market-wide underwriting and pricing challenges.

Walaa's growth had been quite significant, with gross premiums increasing to SAR2.6 billion in 2022 from SAR1.5 billion in 2020, which together with weak underwriting performance resulted in capital adequacy initially weakening. As a result GUL deteriorated to 3.9x at YE 2021 from 2.2x at YE 2020 before reverting to an improving trend at the end of 2022 reaching 3.4x, following the merger with SABB Takaful and the related capital raise of SAR294 million.

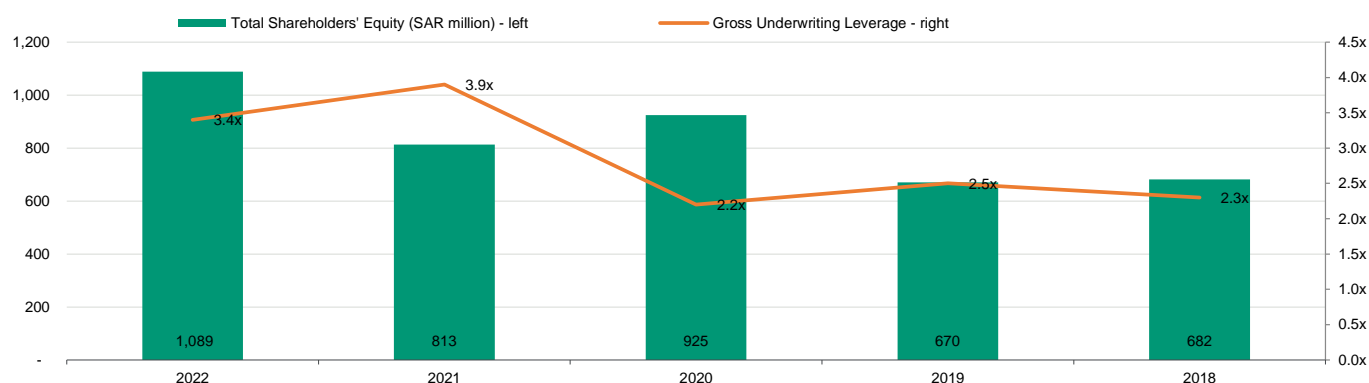
The SABB Takaful merger and capital raise was in line with the strategy recommended by the board to raise capital by SAR775 million as announced in 2021 to maintain the company's solvency margin as it pursues growth in the expanding Saudi insurance market.

Additionally, unlike most of its P&C peers in the wider GCC region, Walaa's capital adequacy is not pressured by a high risk investment portfolio.

Walaa's risk and capital management is credit positive because it aims to maintain the company's solvency margin as it pursues its growth plan for the next three to five years. Going forward, we expect Walaa's improved underwriting performance and any future capital raise, to support strengthening capital adequacy.

Exhibit 4

#### Walaa's capitalisation indicators



Source: Moody's Investors Service and Company's filings

The new IFRS 17 accounting regime will have a minimal impact on the Walaa's regulatory capital but will significantly alter its reported shareholders' equity. In its interim condensed financial statements for the three months period ended March 31, 2023 (Q1 2023), Walaa reported its December 31, 2022 shareholders' equity to have increased by SAR57 million. This is primarily due to the impact of IFRS 9 based revaluation of investments accounting for SAR45.3 million of the increase. The remaining SAR11.7 million increase was from IFRS 17's implementation of premium allocation approach (PAA) for its non-life products and under the Variable Fees Approach (VFA) for its life products impacting measurement of its insurance contract liabilities and reinsurance contract assets.

### Profitability: Under pressure in recent years from weak underwriting performance

Market wide weak underwriting performance in 2021 and 2022, driven by competitive pressures on premium rates and adverse claims developments, had a negative impact on Walaa's profitability, with its combined ratio deteriorating to 111% and 106% for 2021 and 2022, respectively, from 88% in 2020. This resulted in return on capital deteriorating to -13.9% and -3.2% in 2021 and 2022 respectively from 6.6% in 2020.

More positively the recent results of Q1 2023 show that Walaa, alongside the wider market, has improved its underwriting performance with Walaa reporting a net income of SAR24.3 million for Q1 2023 compared to a net loss of SAR19.6 million for the same period last year.

Whilst the 5-year average combined ratio remains modest at 98% (2022-2017), we remain watchful given the Saudi marketwide competitive pressures specifically in the non-life sector which Walaa is expected to remain exposed to.

**Reserve Adequacy: Actuarial-led reserving and focus on short-tailed lines of insurance moderates reserve risk**

The established sophistication from in-house and external actuarial led reserving setting and monitoring has benefitted reserve setting as well as adequacy and recently driven adequate pricing changes at Walaa. Furthermore, given the company's low severity, high frequency book and short-tailed products (especially on a net basis), reserving risk is generally considered low.

**Financial flexibility: Listed insurer with no leverage and demonstrated access to capital markets**

Walaa is listed in Saudi stock market. The main source of additional capital would be through the existing shareholders as the debt markets in Saudi remain relatively underdeveloped. However the lack of any existings borrowings along with its expanded business profile across non-life and life in a growing Saudi insurance market aids Walaa's funding flexibility and it has a track record of having been able to raise capital through a rights issue.

**Operating environment: Operate from Saudi Arabia**

Walaa operates exclusively in Saudi Arabia, which is rated A1 with a positive outlook. The credit strengths underpinning Saudi Arabia's A1 rating include 1) Moderate government and broader public sector debt burden; 2) Robust fiscal and foreign-currency reserve buffers and prudent banking regulation; and 3) High per-capita income, large stock of proved oil reserves and low extraction costs.

The credit challenges Saudi Arabia faces include 1) High economic and fiscal vulnerability to declines in oil demand and prices; 2) Longer-term risks stemming from global carbon transition; and 3) Political risks stemming from regional geopolitical tensions.

The insurance market is still in a developmental stage, with growth potentially volatile and with some large risk concentrations particularly to compulsory lines such as motor and medical. This along with oversupply of insurance products leads to significant levels of price competition. In addition to the pressures of competition, Saudi insurers are facing macroeconomic and regulatory headwinds which will continue to pressure the sector's profitability, liquidity and capital, making consolidation likely.

## ESG considerations

### Wala Cooperative Insurance Company's ESG Credit Impact Score is Moderately Negative CIS-3

Exhibit 5

#### ESG Credit Impact Score

# CIS-3

## Moderately Negative

For an issuer scored CIS-3 (Moderately Negative), its ESG attributes are overall considered as having a limited impact on the current rating, with greater potential for future negative impact over time. The negative influence of the overall ESG attributes on the rating is more pronounced compared to an issuer scored CIS-2.



Source: Moody's Investors Service

Wala Cooperative Insurance Company (Wala) has moderate exposure to ESG risks with **CIS-3**, reflecting limited impact of environmental, social risk, as well as moderate governance risks on its ratings to date. The company's enhancing risk management and governance practices mitigate its exposure to environmental and social risks, in particular carbon transition risk which is also mitigated to an extent by the time horizon over which this risk is expected to become more material. At the same time its high growth financial strategy poses challenges to performance.

Exhibit 6

#### ESG Issuer Profile Scores

ENVIRONMENTAL

# E-3

## Moderately Negative



SOCIAL

# S-3

## Moderately Negative



GOVERNANCE

# G-3

## Moderately Negative



Source: Moody's Investors Service

### Environmental

Wala faces moderate exposure to environmental risks, mainly because of carbon transition risk. Although the company has limited direct exposure to carbon-intensive sectors, it is indirectly exposed through its investment portfolio and insurance premiums that are linked to the Saudi Arabian economy which derives a significant portion of its revenues from the hydrocarbon industry. Physical climate risk is moderate in the GCC region with low levels of natural catastrophes historically, albeit that the frequency of severe weather events has been rising.

### Social

Wala has moderate social risk related to customer relations and demographic and societal trends. Customer relations risk arises as a result of its focus on retail insurance lines, handling of sensitive customer data, and increasing regulatory focus on insurers' customer conduct issues. Demographic and societal trends can make the operating environment more challenging, particularly for its life and medical insurance businesses where societal trends and government policy decisions can impact claim trends. The company's diversified product base and conservative reserving practices moderate these social risks to some extent.

### Governance

Wala faces moderate governance risks with enhanced risk management, policies and procedures as its high growth financial strategy poses challenges to performance. Albeit the management has a good track record of meeting its business objectives whilst maintaining

its focus on risk management and an appropriate financial strategy characterized by low leverage and good regulatory capital. The company has a widely diversified investor base and benefits from good board oversight due to its strong board including independent directors.

ESG Issuer Profile Scores and Credit Impact Scores for the rated entity/transaction are available on Moodys.com. In order to view the latest scores, please click [here](#) to go to the landing page for the entity/transaction on MDC and view the ESG Scores section.

## Rating methodology and scorecard factors

Exhibit 7

### Walaa Cooperative Insurance Company

Financial Strength Rating Scorecard [1][2]	Aaa	Aa	A	Baa	Ba	B	Caa	ScoreAdj	Score
Business Profile								A	A
<b>Market Position, Brand and Distribution (25%)</b>								A	A
-Relative Market Share Ratio			X						
-Underwriting Expenses % Net Premiums Written	18.7%								
<b>Product Focus and Diversification (10%)</b>								A	Baa
-Product Risk		X							
-P&C Insurance Product Diversification			X						
-Geographic Diversification									
Financial Profile								Baa	A
<b>Asset Quality (10%)</b>								Aa	A
-High Risk Assets % Shareholders' Equity		37.5%							
-Reinsurance Recoverable % Shareholders' Equity				115.2%					
-Goodwill & Intangibles % Shareholders' Equity	15.8%								
<b>Capital Adequacy (15%)</b>								A	A
-Gross Underwriting Leverage			3.4x						
<b>Profitability (15%)</b>								Ba	Baa
-Return on Capital (5 yr. avg.)				1.3%					
-Sharpe Ratio of ROC (5 yr.)					11.9%				
<b>Reserve Adequacy (10%)</b>								Caa	A
-Adv. (Fav.) Loss Dev. % Beg. Reserves (5 yr. wtd. avg.)							68.4%		
<b>Financial Flexibility (15%)</b>								A	A
-Adjusted Financial Leverage	4.2%								
-Total Leverage	4.2%								
-Earnings Coverage (5 yr. avg.)	21.1x								
-Cash Flow Coverage (5 yr. avg.)									
Operating Environment								Baa	Baa
Preliminary Standalone Outcome								Baa1	A3

[1] Information based on IFRS financial statements as of fiscal year ended 12/31/2022. [2] The Scorecard rating is an important component of the company's published rating, reflecting the standalone financial strength before other considerations (discussed above) are incorporated into the analysis.

Source: Moody's Investors Service

## Ratings

Exhibit 8

Category	Moody's Rating
<b>WALAA COOPERATIVE INSURANCE COMPANY</b>	
Rating Outlook	STA
Insurance Financial Strength	A3

Source: Moody's Investors Service



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