

Global Alliance Seguros

Mozambique Insurance Analysis

May 2009

Security class	Rating scale	Currency	Rating	Rating watch	Expiry date
Claims paying ability	National	Metical	A	No	05/2010

Financial data:

(US\$'m Comparative)

	31/12/07	31/12/08
Mt/US\$ (avg)	25.75	24.24
Mt/US\$ (close)	23.75	25.18
Total assets	7.9	10.6
Total capital	3.7	4.1
Cash & equiv.	5.1	5.7
GPI	14.3	18.0
U/w result	1.8	0.1
NPAT	1.2	0.1
Op. cash flow	1.0	2.0
Market cap.		n.a.
Market share*		19.8%

*Based on estimated GPI at 31 December 2008

Fundamentals:

Global Alliance Seguros (GA) was registered in 1993, and has its head office situated in Maputo. The company has a composite licence to transact both non-life and life insurance, although up until now the insurer has only been exploring short term insurance. GA is a 99.4% owned subsidiary of Global Alliance Holdings. The bulk of the insurer's business is sourced from the corporate market, which includes the large multinationals and several large parastatals.

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Rating rationale

The rating is based on the following key factors:

- GA is a key participant in the Mozambican insurance market, boasting a vast product offering, strong branding and a high level of client support (including some of Mozambique's leading companies).
- Liquidity measures were considered to be adequate (although investment returns remain weak). Cash coverage is, however, expected to decline in F09, as additional funds are allocated to the completion of the insurer's new head office.
- The international solvency ratio has remained fairly stable over the past 3 years.
- The insurer's book reflects a high level of concentration, with motor representing almost half of NPI. Furthermore, the large losses reflected in this class resulted in a sharp drop in profitability in F08 (exacerbated by a jump in management expenses).
- The insurer's high level of costs undermines financial flexibility, particularly in a poor claims environment.
- Cognisance is also taken of GA's high concentration in terms of intermediaries, although client concentration is low.

Solvency and liquidity

Shareholders interest increased by 17% to Mt102m in F08, supported by unrealised gains of Mt13m. In comparison, NPI rose by a lower 7.5%, thereby supporting a 4 percentage point increase in GA's solvency margin to 53% in F08. Similarly, the financial base ratio increased to 74% in F08 from 65% previously. The XOL reinsurance programme, led by Munich Re, provides a maximum net retention per event amounting to US\$150,000. This equated to around 3.7% of the insurer's capital base as at FYE08. Cash and cash equivalents continued to comprise the bulk of the insurer's investments, and were posted at a review period high of Mt144m in F08 (F07: Mt120m). In addition, cash coverage of claims remained stable at around 21 months in F08.



Economic overview

Economic growth in Mozambique has registered fairly strong gains over recent years, mainly driven by foreign financed “mega-projects” and large aid inflows. This resulted in real GDP growth of 7.1% to US\$7.6bn in 2007, down slightly from 8% in 2006, due to oil price increases and a downturn in traditional exports. Mozambique’s GDP is largely dependent on the agriculture and manufacturing sector, together accounting for more than 40% of GDP contributions in 2006. However, diversification efforts are starting to materialise, particularly visible in double digit growth figures in the mining and transport segment.

A substantial trade imbalance persists although the opening of the Mozal aluminum smelter, the country’s largest foreign investment project to date, has increased export earnings. At the end of 2007, and after years of negotiations, the government took over Portugal’s majority share of the Cahora Bassa Hydroelectricity company, a dam that was not transferred to Mozambique at independence because of the ensuing civil war and unpaid debts. More power is needed for additional investment projects in titanium extraction & processing, the SASOL gas pipeline project (connecting Mozambique to South Africa) and garment manufacturing that could further close the import/export gap. Additional insurance opportunities, in particular marine, are expected to arise in the longer term following the rehabilitation of the Maputo Port. Mozambique’s once substantial foreign debt has been reduced through forgiveness and rescheduling under the International Monetary Fund’s Heavily Indebted Poor Countries (HIPC) and Enhanced HIPC initiatives, and is now at a manageable level.

Interest rates set by the central bank remained constant for almost a one year period to March 2008, with the standing deposit facility at 10.3% and overnight lending facility at 14.5%. These rates reduced to 13% and 7% respectively in February 2009, following an improved inflationary outlook.

	2002	2003	2004	2005	2006	2007	2008f
GDP growth (%)	9.2	6.5	7.9	8.4	8.0	7.1	7.0
GDP per capita (US\$)	228.0	248.3	297.9	335.8	338.1	368.7	399.7
Inflation (%)	16.8	13.5	12.6	6.4	13.2	7.9	5.7
Population	18.4	18.8	19.1	19.6	20.0	20.5	21.0

Source: IMF

Since the re-denomination of the local currency with the new Mozambique Metical, the currency has displayed a relatively stable exchange rate, fluctuating in a band of between Mt26.1/US\$ and

Mt23.8/US\$ in 2007, averaging Mt25.8/US\$ in that year. The currency deteriorated slightly in 2008, closing the year at Mt25.2/US\$.

In light of the above mentioned indicators and increased level of economic diversification, Mozambique’s economy appears well positioned for long term future growth. However, given the current global economic crisis, growth in new foreign direct investment is likely to diminish for the foreseeable future, thus hampering prospects of a declining trade deficit further and magnifying the need for sustainable organic growth in the medium term.

Operating environment

The Mozambiquan insurance industry encompasses six insurance companies and one reinsurer (ZimRe Mocambique, which entered the market in 2007). Based on an independent study undertaken, the volume of business generated by the participating companies was Mt2.2bn in 2007, or approximately US\$93m. This represents industry premium growth of 40% for the year, although the insurance penetration rate in the economy remains very low.

For a number of years, Seguradora Internacional De Mocambique (SIM), which is 90% owned by Banco Internacional de Mocambique, operated as the largest insurance company in terms of GPI. During 2007, however, following strong growth of 67%, Empresa Mocambicana de Seguros (EMOSE) reverted to the largest insurance company, with a market share of around 35%. This was followed closely by SIM with 32%. GA is comfortably the third largest insurer, accounting for roughly 20% of market GPI, with Hollard Seguros representing the bulk of the remainder, at 8.9%. In terms of shareholders funds, EMOSE reflects a level double that of SIM, at Mt1.1bn. Hollard is the third largest insurer by capitalisation, with Mt180m as at 31 December 2007, compared to GA with Mt87m.

With regards to the distribution between life and non-life premiums, the latest available data is from 2005, which indicates that non-life business accounted for 87% of total gross premium income in the industry. It is believed that subsequent strong growth in the short term insurance industry has diluted the life sectors contribution further. Based on the breakdown of non-life insurance sourced from the 2005 data, motor insurance contributed 43% of gross premiums, followed by fire & other damage at 18.5%. The motor account was also responsible for 73% of claims in 2005.

The largest insurers (EMOSE and SIM) have displayed high levels of prudent underwriting, allowing the other industry participants market access

through lower rates. GA has successfully secured the larger well-established corporate entities as clients. This has, however, resulted in a position whereby the company is often forced to defend its book of business from competitors.

Risk diversification¹

Commercial entities form the mainstay of GA's business, accounting for 89% of GPI in F08. With respect to personal lines, the insurer has not aggressively pursued this business due to the typically low penetration rates and affordability levels, although this appears to be improving. Multinational brokers derive the bulk of GA's business. In particular, the four largest intermediaries cumulatively sourced around 78% of GPI in F08. Direct sales accounted for 19% of premiums, representing strong growth over prior years (F07: 12%; F06: 10%). The largest client represented 8.5% of GPI in F08, with the five largest totalling 20%. The company continues to price annually although this has reduced to around 50%, with bi-annual and quarterly the preferred methods of policy issuance.

Gross premiums continued to be largely concentrated within the motor, fire and engineering books in F08. As motor premiums are largely retained (compared to the heavily reinsured fire and engineering classes), the motor book continued to dominate almost half of the overall net book, with WCA contributing a further 15% in F08.

	GPI (%)		NPI (%)	
	F07	F08	F07	F08
Motor	24.6	25.6	47.3	44.7
Fire	29.4	19.1	10.3	9.1
Engineering	13.5	21.9	7.9	8.5
WCA	6.9	8.2	13.1	15.4
Marine	1.9	4.8	1.7	2.4
Personal Acc.	2.6	3.7	1.7	2.6
Liability	6.0	4.4	2.8	1.2
Goods in transit	1.4	1.7	2.5	3.1
Toursure	2.8	2.8	5.4	4.9
Other*	10.9	7.8	7.3	8.1
Total	100.0	100.0	100.0	100.0

* Includes specialised liability and miscellaneous.

The insurer's financial performance is mainly driven by the heavily weighted motor class, which posted a Mt12m underwriting loss compared to a Mt14m profit in the previous year. While the bulk of motor claims were accident related (driven by rapidly increasing traffic congestion and deteriorating road infrastructure), this was also impacted by a spate of vehicle hijackings and theft. The fire class reflected a second consecutive large underwriting deficit, of

¹ It should be noted that the analysis by underwriting class is based on management accounts, which differ to the consolidated audited financial statements provided to GCR.

Mt4.6m compared to Mt6.8m in F07. Toursure remained profitable in F08 (Mt2m), albeit well down on the level of Mt6.6m generated in F07. The best performers in F08 were engineering, WCA and goods in transit, with all reflecting improved loss ratios and generating underwriting profits of Mt9.8m, Mt4.6m and Mt3.4m respectively. This was, however, insufficient in supporting the overall result (driven by the aforementioned motor and fire books), with the insurer reflecting a significant decline in the underwriting profit to Mt2.2m, compared to a Mt45m profit in F07.

Earned loss ratio (%)	Earned loss ratio	
	F07	F08
Motor	54.7	71.1
Fire	46.6	49.3
Engineering	2.4	0.8
WCA	62.5	32.9
Marine	36.7	44.9
Personal Acc.	8.7	29.0
Liability	(44.4)	11.7
Goods in transit	32.6	(10.7)
Toursure	9.1	23.2
Other*	27.5	88.4
Total	41.4	45.3

* Includes specialised liability and miscellaneous.

Reinsurance

Reinsurance protection on both proportional and non-proportional treaties is lead by Munich Mauritius Re with 25% participation, and includes Swiss Re (20%), Africa Re (20%), SCOR (17%), ARIG (10%) and ZEP Re (8%). Facultative cessions (combined fire and engineering) to reinsurers are capped at US\$5m (US\$15m retained).

Proportional treaties

	Reinsured's net retention	Total treaty capacity	Natural perils event limit
Fire first surplus	600,000	15m	50m
Eng. first surplus (material damage)	600,000	15m	50m
Eng. surplus (liability)	600,000	5m	n.a.
Liability surplus*	600,000	3m	n.a.

Note: A loss occurrence in respect of natural perils relates to individual losses arising out of and directly as a result of one and the same event.

*General & tenants public & products liability, employers liability, motor third party & passenger legal liability).

Non-proportional treaties

A general account excess of loss program has been structured into four layers that covers losses ranging between US\$150,000 and US\$12m. In addition to this, GA has also purchased general account catastrophe excess of loss reinsurance, providing for losses in excess of US\$12m up to US\$24m. Specific net retentions are, in turn, applicable by class (applicable to per risk and multiple risk events). The maximum per risk net retention amounts to US\$150,000 or Mt3.8m (based on current exchange

rates), which equates to 3.7% of the insurer's capital base as at FYE08.

	F07	F08
Premium ceded	188.6	242.6
Commissions received	(30.2)	(24.2)
Claims recovered	(127.0)	(41.3)
Net transfer / (recovery)	31.4	177.1

Reinsurance portfolio transfers increased markedly during F08, to Mt177m from Mt31m in F07. This follows a significant drop in reinsurance claim recoveries to 17% of premiums ceded (F07: 67%), driven by the sharp rise in motor related claims, which are largely retained. It is also noted that F07 includes large cyclone exposure recoveries.

Asset management

Cash and cash equivalents increased by 20% to Mt144m in F08, and accounted for a high 85% of total investments (F07: 86%) and 54% of total assets (F07: 64%). The overwhelming majority of cash holdings are held in US\$, specifically with Barclays and Standard Bank in Mozambique. The claims cash coverage ratio increased slightly to 21 months in F08 from 20 months in F07. Cognisance is taken of the poor investment returns available on cash holdings in Mozambiquan banks.

	F07		F08	
	Mtm	%	Mtm	%
Cash & cash equivalents	120.1	86.4	144.2	85.0
Listed equities	0.5	0.4	0.5	0.3
Bonds	0.3	0.3	0.4	0.2
Investment property	17.9	12.9	24.7	14.5
Other investments	18.7	13.6	25.5	15.0
Total investments	138.8	100.0	169.7	100.0

GA increased its property portfolio by Mt6.8m to Mt25m in F08. The investment comprises 2 key properties, namely:

- A guest house on Inhaca island that was completed in 2008 and will be utilised to generate rental income (cost: Mt13.1m); and
- a new head office for the insurer, of which Mt11.6m had been spent as at FYE08. Around US\$2m, or Mt52m is required to complete construction. This will significantly alter the company's balance sheet and liquidity profile. A portion of the premises will be utilised to generate rental income.

Solvency and reserving

Shareholders interest increased by 17% to Mt102m in F08, driven mainly by foreign exchange gains of Mt13m. In this regard, GA attained the minimum stipulated capital requirement of Mt100m as per a

recent regulatory revision. Growth in net premiums registered at a comparatively lower 7.5%, thereby resulting in an increase in the international solvency margin to 53%, from 49% in F07. The financial base ratio was also positively impacted, totaling 74% in F08 compared to 65% previously.

Both reserving ratios increased in F08, with net outstanding claims and the unearned premium reserve equating to 23% and 21% of NPI respectively (F07: 11% and 17%).

Financial performance

A 5-year financial synopsis is reflected at the back of this report and brief comment follows hereafter. The company's actual performance compared to the budget for F08 is presented in the table below.

	Actual	Budget	% of budget
Gross premium income	453.6	417.7	108.6
Reinsurance	(242.6)	(189.7)	127.9
Net premium income	193.1	228.0	84.7
Earned premium	185.1	211.0	87.7
Net claims	(82.8)	(81.0)	102.2
Net commission	(23.6)	(14.2)	166.2
Management expenses	(76.5)	(65.3)	117.2
Underwriting result	2.2	50.5	4.4
Key ratios			
GPI growth	18.3	13.4	
Retention ratio	44.3	54.6	
Earned loss ratio	44.7	38.4	
Management expense ratio	41.3	30.9	
Net commission ratio	12.8	6.7	
Underwriting ratio	1.2	23.9	

GPI came in ahead of expectations, totalling an 18% higher Mt454m in F08. This includes an amount of Mt48m (F07: Mt42m) relating to administration fees, which are fees charged over and above premiums (an industry convention). It is noted that the administration margin has decreased consistently over the last few years, which has impacted the operating line somewhat. This is mainly due to the fact that relatively lower administration fees are charged on the motor book, which has been a key driver of the overall book. Retention levels decreased in F08, to 44% from 49% in F07, thereby mitigating growth in earned premiums, which was posted at a 5% higher Mt185m in F08.

Claims incurred increased by 13% to Mt83m in F08, driven by the aforementioned rise in motor related claims, which are largely retained. As such, the insurer reported a 3 percentage point increase in the earned loss ratio to 45% in F08, above budget of 38%.

The delivery cost ratio increased by a significant 21 percentage points to 54% in F08, well above budget of 38%. This follows a 74% jump in management expenses to Mt77m, or 41% of earned premiums (F07: 25%). Included in this amount is staff costs of Mt42m (F07: Mt25m), or 55% of total expenses (F07: 57%). Accordingly, GA reported a marked deterioration in its underwriting performance, posting a much reduced Mt2.2m profit from a Mt45m profit previously. This also compares to a budgeted Mt51m underwriting profit. The underwriting margin registered at just 1% in F08 (F07: 26%). Overall, cognisance is taken of the exceptionally volatile underwriting/profit trend over the review period.

Exchange rate movements are treated as unrealised profits/losses by GCR. These arise from the fact that premiums are received in Rands and Dollars. These are held in hard currency until payment is made to reinsurers (ie. facultative business) - usually 45 days between receipt and payments, with the resulting gain/loss put to the income statement. In terms of foreign currency received at a certain rate that must be paid out at a fixed rate in future (ie quarterly treaty business), the gain/loss is recorded as an unrealised gain/loss to the income statement. Inclusive of unrealised exchange rate gains of Mt13m (F07: Mt0.1m loss), ROaE amounted to 16% in F08, well down on the previous level of 39%.

Future prospects

GA is budgeting for a 31% increase in gross premiums to Mt569m in F09 (inclusive of administration fees totaling Mt62m), driven by an expected participation in a number of large new projects being undertaken in Mozambique, as well as corrective pricing increases to overcome the relatively higher claims incidence in F08. Reinsurance cessions are forecast at similar levels to F08. Notwithstanding the aggressive growth forecasts, the loss ratio is expected to improve to 38%, below historical averages. Management expenses are expected to grow at a level slightly below earned premiums, with the expense ratio budgeted at a lower 39% (F08: 41%), which management has confirmed as a likely long term level. Given the growth envisaged and the improvement in claims, the insurer is forecasting a marked turnaround in underwriting performance in F09. The solvency margin is expected to total around 49%.

Table 8: Income statement (Mtm)	Actual YTD F09*	Budget F09	% of budget
Gross premium income	261.0	568.8	45.9
Reinsurance premiums	(142.1)	(310.1)	45.8
Net premium income	118.9	258.7	46.0
Earned premium	103.5	236.7	43.7
Net claims	(50.9)	(89.6)	56.8
Delivery costs	(44.7)	(121.3)	36.9
Underwriting result	7.9	25.8	30.6
Ratios (%)			
GPI growth	43.8	30.6	
Retention ratio	45.6	45.5	
Earned loss ratio	49.2	37.9	
Delivery cost ratio	43.2	51.3	
Underwriting ratio	7.6	10.8	
Solvency	n.a	49.4	

Note: Budget translated using an exchange rate of Mt26:US\$
*5 months to 31 May 2009.

Global Alliance Seguros

(Meticais in millions except as noted)

Year ended : 31 December	2004	2005	2006	2007	2008	
Income Statement						
Gross premium income (GPI)	214.9	269.1	339.1	368.2	435.6	
Reinsurance premiums	(107.5)	(166.7)	(206.6)	(188.6)	(242.6)	
Net Premium income (NPI)	107.4	102.4	132.5	179.6	193.1	
(Increase) / Decrease in insurance funds	(0.9)	(7.1)	(2.0)	(3.3)	(7.9)	
Net premiums earned	106.5	95.2	130.5	176.3	185.1	
Claims incurred	(48.4)	(38.2)	(59.8)	(73.6)	(82.8)	
Commission	(2.2)	(6.7)	(13.1)	(13.4)	(23.6)	
Management expenses	(34.6)	(50.3)	(48.6)	(44.1)	(76.5)	
Underwriting profit / (loss)	21.2	(0.0)	9.0	45.3	2.2	
Investment income	0.9	0.1	0.4	0.8	0.7	
Other income / (expenses)	0.0	0.8	0.7	(0.7)	5.7	
Taxation	0.0	(2.1)	(2.4)	(14.5)	(6.6)	
Net income after tax	22.1	(1.3)	7.7	30.9	2.0	
Unrealised gains / (losses)	(15.6)	5.7	(2.5)	(0.1)	13.0	
Balance Sheet						
Shareholders interest	62.5	66.9	71.8	87.2	102.0	
Insurance funds	15.5	22.6	27.5	29.9	40.0	
Other liabilities	103.8	133.6	139.1	69.5	124.1	
Total capital & liabilities	181.7	223.1	238.4	186.5	266.0	
Fixed assets	4.3	3.9	4.2	4.4	4.7	
Investments	0.7	4.8	7.7	18.7	25.5	
Cash and short term deposits	80.4	51.5	127.9	120.1	144.2	
Other current assets	96.3	162.9	98.6	43.4	91.6	
Total assets	181.7	223.1	238.4	186.5	266.0	
Key Ratios						
Solvency / Liquidity						
Shareholders funds / NPI	%	58.2	65.4	54.2	48.5	52.8
Financial base	%	72.6	87.4	75.0	65.1	73.5
Claims cash coverage	months	19.9	16.2	25.7	19.6	20.9
IBNR / EPI	%	4.2	5.1	5.8	5.5	5.3
Net outstanding claims / NPI	%	30.8	40.8	21.2	11.0	22.6
Insurance funds / NPI	%	14.4	22.1	20.8	16.6	20.7
Profitability						
ROaE (before foreign exchange gains / losses)	%	37.3	(2.0)	11.1	38.9	2.1
ROaE	%	10.9	6.9	7.4	38.8	15.9
Investment yield (including unrealised gains / losses)	%	(21.3)	8.5	(2.2)	0.5	8.9
Cash investment yield (average)	%	1.3	0.1	0.4	0.6	0.5
Efficiency / Growth						
GPI growth	%	10.1	25.2	26.0	8.6	18.3
Premiums reinsured / GPI	%	50.0	62.0	60.9	51.2	55.7
Earned loss ratio	%	45.5	40.1	45.8	41.7	44.7
Commissions / Earned premiums	%	2.1	7.1	10.0	7.6	12.8
Management expenses / Earned premiums	%	32.5	52.8	37.2	25.0	41.3
Underwriting result / Earned premiums	%	19.9	(0.0)	6.9	25.7	1.2
Trade ratio	%	80.1	100.0	93.1	74.3	98.8
Operating						
Effective tax rate	%	0.0	258.7	24.0	31.9	77.1

Note: Financial statements prior to 2007 restated to incorporate reduction of three zero's as per revised currency.