So far, 2011 has been a turbulent year for the Middle East, with political turmoil in many countries. There is no denying that the political protests and popular uprising in the majority of Arab countries have affected the insurance markets. However, the region is still considered attractive to reinsurers as insurance penetration is growing year-on-year, and economies across the region continue to develop despite the civil unrest.

Although insurance premiums are generally rising, financial performance is volatile. Despite this, major rating agencies consider the capitalisation of most local MENA insurers to be strong, so it remains a market with potential.

Hot topics
The hot topics of the past few months have been the question of strikes, riot and civil commotion risks (SRCC), what is covered under political risks and political violence policies, and what is excluded. Insurers, from as early as January, have been struggling to assess the damages caused by the so-called “Arab Spring” and to reach a consensus on how to define the events. With riots and protests continuing across the region, there is a need to get agreement on the insurance classification of these events.

The Insurance Federations in Tunisia and Egypt have classified the uprising in their countries as “civil commotion”, which is a commonly-purchased cover. There are various interpretations of the strikes, riots and civil commotion (SRCC) clauses and it is likely that major reinsurers will start to impose sub-limits and even exclusions of specific targets such as supermarkets, banks and public buildings. This issue is being complicated further by the supervisory authorities in Egypt and Tunisia and their recommendations for insurers to pay losses sustained during the uprising in these countries.

As a result of these uncertainties, the reinsurance industry is entering a difficult cycle, and reinsurers are likely to become more selective about their choice of clients. This means that insurers will be stricter about the level of coverage they are willing to offer. Most insurers in Egypt for instance, will cover no more than 25% of SRCC damages. Cover limitation is already imposed in North African countries, but is being resisted across the GCC. However, the GCC countries have also been affected by the Arab Spring – and the protests in Bahrain have impacted on its position as a financial centre – so how long the resistance to cover limitations can remain is in question.

State of the local markets
During 2011, technical results have deteriorated due to fierce competition across most of the MENA markets, and in few cases, financial returns have not been sufficient to cover the underwriting loss. The problem is being compounded by low investment returns due to the global financial crisis. The result is that insurers are relying more heavily than ever on reinsurance in order to keep retentions low. This trend is likely to continue as an increasing number of international reinsurers look to capitalise on the opportunity by building a presence in the MENA region, opening branches in either Dubai or Bahrain.

Alongside the international reinsurance market, there is a healthy local reinsurance and insurance market, in particular for the fire and engineering businesses, and it is estimated that the region’s capacity for these business exceeds US$1.5 billion. In this class of business, the London market is seldom approached to provide capacity as its terms are usually uncompetitive, but London remains a major market for a number of risks such as aviation, marine and very large industrial and construction risks.

Insurance penetration
There are a large number of local insurance companies in most MENA markets, but insurance penetration across
the region is still low. There are moves in some countries to bring in compulsory insurance for certain classes of business. For example, in Morocco, there are plans to make home insurance, natural catastrophe insurance for householders, contractors all-risks, decennial liability and basic medical insurance cover mandatory for the majority of the population. And in the GCC, the requirement for compulsory motor and medical insurance has pushed market premiums up.

Life insurance has also started to grow either through conventional insurance providers or through family takaful operators. For instance, three life insurers – Taamine Life Insurance, Caarama Assurance and Société de Prévoyance et de Santé – were recently set up in Algeria.

It was anticipated that takaful products would increase insurance penetration across the Arab world, but even with an increasing number of takaful operators, their market share is still low – albeit increasing year-on-year. Similarly, retakaful operators with large capital bases have found it difficult to generate enough premiums from the takaful business only, and some of these operators have been forced to start to underwrite conventional insurance business as well.

**Mergers and acquisitions likely**

Many are predicting that mergers and acquisitions will be the next step for both conventional and takaful insurers and reinsurers in the region. Many of the smaller family-owned insurance companies in the GCC are facing difficulties in growing their market share, and some of the largest companies are looking to diversify by entering new territories, either in the Arab world or in Asia.

In addition, investor confidence in the GCC countries has started to grow as the global economic turmoil starts to subside. In the UAE in 2011, there have been a number of new conventional and takaful companies that have listed on the stock market and subscriptions for these companies have been high.

**The impact of regulations and stricter controls**

There is a huge disparity in the various insurance regulations across the Arab world. In the GCC, these are still at an early stage of development, although in Saudi Arabia the advancement of regulations is encouraging. In addition, some of the North African markets are pushing for enhanced regulation.

For example, in Morocco, there is now an agreement between the government and the insurance sector to adopt a programme to progressively implement international accounting and good governance standards. Other measures are also being adopted, such as greater accountability of board directors, solvency margins and the establishment of asset-liability management processes, as well as implementing a regulatory framework in order to support the increase in insurance penetration and provide protection to policyholders.

As a result of these measures, it is predicted that the insurance market in Morocco will see premium income jump from $2.2 billion to $6 billion over the next five years. As well as starting to impose regulations, a number of MENA-based insurance companies are also beginning to apply a more risk-based approach to investment management and are taking a much stricter approach to underwriting control.

**The future for (re)insurance**

The greatest challenge for local insurance companies is going to be their ability to maintain profitability in the face of increasing competition from international companies, combined with lower investment income and less attractive reinsurance terms. In addition, it is likely that ongoing volatility among takaful operators will lead to a spate of mergers and acquisitions.

Personal lines insurance offers the greatest growth potential for the foreseeable future. This is likely to increase premium retention in the market as reinsurance is not required for this business.

Larger risks such as engineering and construction will no doubt continue to grow, especially in Saudi Arabia and Qatar, as there is an increasing number of large construction risks being undertaken and planned. It is on these risks that the reinsurance market will play a major role.

Perhaps the biggest issue on the horizon for the region for both reinsurers and insurers is the question of talent. Across the MENA region, there is a deficit of insurance skills and expertise – particularly in the GCC markets. Although there is pressure by the authorities to employ more nationals, employers are often unable to find local candidates with the appropriate profile. And young graduates are attracted to banking or government jobs rather than a career in the insurance industry, which means that the GCC will have to continue to rely on skilled foreign nationals from the Indian sub-continent and other Arab countries.

In our view, it is a key priority that GCC nationals play an increasing role in the local insurance workforce. There are initiatives in Bahrain, for example, to supply the market with well-qualified local people who can take over from foreign nationals, and this is proving successful particularly with women – they now account for a large proportion of the insurance workforce in Bahrain.

So despite turbulent times in the Arab world, the combination of low insurance penetration rates and the move to bring in mandatory insurances in some countries, mean that growth potential is strong. However, the knotty issues of the lack of technical expertise, the tough global trading environment, and the debate over what reinsurers and insurers will be willing to cover linked to the ongoing unrest across the region will continue to be major factors over the coming months.

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