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THE ECONOMIC CASE FOR AN EMERGING REGIONAL INSURANCE HUB

By Fetooh Al Zayani & Kai-Uwe Schanz

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THE GULF COOPERATION COUNCIL (GCC) countries (Bahrain, Kuwait, Oman, Qatar, Saudi Arabia, United Arab Emirates) are on the radar screen of any aspiring international insurance and reinsurance organisation. Saturated home markets, the quest for diversification and uncertain short-term economic prospects in most developed countries serve as powerful incentives to explore the Middle Eastern insurance opportunity.

Strong economic growth

Since 2002, when energy prices started their spectacular rise, the GCC region's GDP has grown by 8% p.a. in real, inflation-adjusted terms. Qatar has recorded the best performance with an annual growth rate of 10%. This rate of expansion almost matches the BRIC (Brazil, Russia, India, China) countries' economic momentum (11% p.a.) This year, the GCC region's GDP is expected to reach the mark of $1 trillion.
GDP per capita comparisons further substantiate the GCC countries' economic virility: With more than $70,000 (2007) Qatar ranks third in the global league table, just behind Luxembourg and Norway. It is likely to have overtaken them in 2008 with a GDP per capita of some $80,000. The GCC average amounts to more than $20,000 compared with around $30,000 for Western Europe.

From a commercial insurance perspective one of the most appealing measures is "domestic investments in high-value projects". The projects pipeline in the GCC countries is worth around $1.6 trillion, considerably more than the region's combined GDP. In Qatar alone the projects market exceeds $140 billion. These dizzying numbers reflect local governments' energetic pursuit of a systematic economic diversification strategy aimed at building a sustainable base of wealth for their people – beyond hydrocarbon revenues which are poised to dry up sometime in the (not too distant) future. Even a fall of oil prices to below $100 per barrel would not be expected to adversely affect these economic master plans, as they are all based on more conservative assumptions.

Insurance: a tale of growth, profitability and increasing sophistication

This dynamic economic development has translated into a strong growth performance of the GCC's insurance markets. In nominal terms, they have expanded by around 20% p.a. since 2002. Again, Qatar has displayed an above-average performance with non-life premiums growing by more than 25% p.a. Despite this momentum the region's insurance business still accounts for only a fraction of the global market (see Table). With total non-life premiums of $7 billion and a global market share of 0.4% the GCC insurance market is comparable to India's or Turkey's. A look at non-life penetration, i.e. premiums as a share of GDP, reveals the enormous catch-up potential of the GCC insurance markets. Non-life premiums account for just one percent of GDP – as for example in China or Mexico. Based on the GCC countries' GDP per capita levels one would expect a non-life penetration closer to North America's (4.6%) and Europe's (3%). This somewhat counter-intuitive pattern is largely attributable to the nascent development stage of personal lines. The bulk of the region's insurance business is written in commercial lines. Incentives for private provisions against hazard risks have been historically low due to public schemes, strong family ties and cultural and religious reservations against the traditional notion and structure of insurance. Insurance awareness in general is hardly developed and product diversity remains highly limited. Personal lines, however, are set to experience significant growth going forward as compulsory insurance schemes (particularly in health and social security) gain in importance and Takaful insurance and reinsurance solutions become more prevalent. In the long-run, these dynamics are expected to lift non-life insurance penetration to levels seen in Europe, potentially boosting the share of the sector in overall GDP from 1% to around 3% (see Table).

The region's attractiveness goes beyond mere market expansion. Despite rapid growth and mounting competition non-life markets still offer decent margins. Even though there are no consistent data sources to be relied upon hard and soft intelligence suggests that underwriting is generally profitable, though volatile. Claims experience is relatively favourable reflecting low exposure to natural catastrophes and theft. Overall profitability of domestic players is driven by investment and reinsurance commission income as significant amounts of business are ceded (abroad).

Both top-line and bottom-line performance are expected to receive sustainable support from systematic governmental efforts aimed at enhancing the sophistication, efficiency and stability of regional insurance markets. Regulatory and supervisory standards, for example, are being revamped to meet best-in-class standards such as an integrated approach to financial services regulation and supervision, risk-based solvency requirements and a liberal market access regime allowing for majority stakes, the establishment of branches and access to government business. In this context, the QFC Authority just recently announced a major insurance initiative, the establishment of the Qatar Insurance Platform (QIP) (see Box).

The GCC non-life markets at a glance

Country	**Non-life premium volume in US $ millions** (2007)	**Share of world market in %** (2007)	**Non-life penetration** (premiums as % of GDP, 2007)
Bahrain	280	0.02	1.6
Kuwait	602	0.04	0.5
Oman	339	0.02	0.9
Qatar	608	0.04	0.9
Saudi Arabia	2,203	0.13	0.6
UAE	2,938	0.18	1.5
GCC Total	6,970	0.42	1.1

Source: Swiss Re, sigma no. 3/2008 and authors' own estimates

The Qatar Insurance Platform:
Boosting domestic efficiency and regional hub aspirations

The Qatar Insurance Platform (QIP) is a technology-based insurance trade fulfillment platform which will provide an electronic trading service, facilitate transaction workflow, deliver trade documentation and effective management information, and ultimately enable straight though processing capabilities.

The establishment of QIP will advance the sophistication and overall efficiency of Qatar's insurance industry. By attracting further insurance expertise to Qatar it will help deepen and broaden the local talent base. It will also bring together international insurers, reinsurers and brokers to conduct insurance trading activities through the platform.

The QIP initiative demonstrates Qatar's determination to develop into the region's leading insurance centre. As members of the QIP global insurers and reinsurers will enjoy swift and efficient access to a fast growing and profitable portfolio of GCC, Central and Southern Asian risks for structuring and placement.

The first phase of QIP will go live in a pilot operation in the 4th quarter of 2008

Reinsurance: robust underlying growth but significant structural changes ahead

The GCC countries' domestic insurers display a heavy reliance on reinsurance. Cession rates can range up to 65% to almost 100% for mega risks. This pattern of low risk retention reflects domestic insurers' limited capital base and insufficient scope for risk diversification within their relatively small home markets. However, cession rates are expected to decrease for at least three reasons: Regulators have started to impose higher capital levels; domestic shareholders increasingly push for adequate returns and capital-efficient reinsurance purchasing strategies; and the share of (compulsory and largely retained) medical business is expanding steadily.

Proportional treaty business is most prevalent and dominated by European reinsurers. They usually write cross-border business on a direct basis. The Europeans' dominance, however, is challenged by an increasing amount of domestic reinsurance capacity as well as new foreign competitors who set up locally. Against the backdrop of intensifying domestic competition and increasingly sophisticated reinsurance needs of local companies, it may pay off for reinsurers to consider a local presence. Such a move could help mitigate the impact of decreasing cession rates and improve their ability to successfully participate in the future growth of underlying primary insurance markets.

The bottom-line: eight reasons for locating in Qatar

The GCC region in general and Qatar in particular holds significant promise for foreign insurers and reinsurers. The specific case for Qatar is based on the following eight reasons:

First: Qatar boasts uniquely sustainable economic growth perspectives based on its huge natural gas reserves which are the world's third largest. Over $20 trillion of proven energy resources are to be monetised over the next 100 years. This vast base of natural resources differentiates Qatar from other countries in the region.

Second: Qatar offers foreign insurers and reinsurers full access to the domestic market – rather than just an off-shore location. This liberal regime is another differentiating factor in favour of Qatar.

Third: the emerging Qatar insurance centre enjoys strong and credible governmental support. The establishment of the Qatar Insurance Platform under the auspices of the Qatar Financial Centre Authority (see Box) serves as the most recent example.

Fourth: driven by the influx of world-class foreign companies, a sound domestic insurance cluster is developing. It will be boosted further by the strong pipeline of license applications with the QFC Authority and high-profile initiatives such as the Qatar Insurance Platform.

Fifth: Qatar's political, economic and historical ties are not confined to the Middle East but also extend to North Africa, Central and South Asia, making the country a formidable gateway to a wider region.

Sixth: Qatar offers a highly competitive operating cost environment, for example in terms of taxation, commercial real estate and the quality and quantity of air links.

Seventh: Qatar is committed to establishing world-class unified financial regulatory standards modeled along the lines of the UK Financial Services Authority.

Eighth: Qatar offers an attractive quality of living based on a sensitive balance between Western lifestyle and Arab heritage. This approach promises social and political stability on a sustainable basis, arguably the most important location factor for long-term oriented investors.

The case for Qatar as a regional insurance hub

- Sustainable economic growth prospects
- Liberal market access regime
- Strong and credible governmental support
- Emerging industry cluster
- Gateway to the Middle East and beyond
- Highly competitive operating cost environment
- World-class regulatory standards
- Attractive quality of living