

Composite Reinsurer

## CONTINENTAL REINSURANCE PLC

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AMB#: 078723

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### BEST'S FINANCIAL STRENGTH RATING

Based on our opinion of the company's Financial Strength, it is assigned a Best's Financial Strength Rating of B+ (Good). The company's Financial Size Category is Class VII.

### RATING RATIONALE

**Rating Rationale:** The rating of Continental Reinsurance Plc (Continental Re) reflects its favourable underwriting performance record, its robust risk-adjusted capitalisation and a strong improvement in the technical expertise and experience of the company's board and senior management team following a number of key appointments. Additional positive rating factors include the improving quality of the company's reinsurance panel and its risk management practices, as well as a reduction in outstanding premium debtors as a percentage of gross written premiums (GWP).

Robust risk-adjusted capitalisation - Continental Re's premium income has grown rapidly over the last three years, following a capital injection in 2007, which increased shareholders' funds to over NGN 11 billion, from NGN 2.2 billion at year-end 2006. Although further strong premium growth is anticipated in 2011 and 2012, risk-adjusted capitalisation is expected to remain strong. The credit quality of Continental Re's outwards reinsurance programme continues to improve, with 98% of ceded premiums placed with reinsurers with a secure rating in 2010, compared to 81% in 2009.

Good underwriting results - To date, premium growth has not had an adverse impact on Continental Re's technical performance, and in 2010 the company achieved a solid non-life combined ratio of 79%. Although A.M. Best expects the combined ratio to deteriorate to between 80% and 85% over the next few years, underwriting results are expected to remain good, supported by improved risk management standards. Continental Re's overall performance is likely to continue to be affected by the write-off of premiums owed by debtors, which in 2010 reduced pre-tax profits by NGN 835 million. In common with peers in the region, Continental Re's volume of outstanding premium debtors is

high, but has reduced as a percentage of GWP from 61% in 2007 to 35% in 2010. Reducing this ratio further remains a key focus of management.

Good business profile - The company has a good business profile in Nigeria, being the only private local reinsurer and is developing its business profile in the rest of sub-Saharan Africa through the establishment of local offices. Non-life reinsurance business dominates Continental Re's portfolio, representing approximately 85% of GWP, the majority of which is written on a proportional basis.

**Best's Financial Strength Rating: B+**

**Outlook: Stable**

## **FIVE YEAR RATING HISTORY**

<u>Date</u>	<u>Best's FSR</u>
08/22/11	B+
08/10/10	B
06/19/09	B
09/02/08	B
10/29/07	B

## **BUSINESS REVIEW**

Based in Lagos, Nigeria, Continental Re has established a good position within the Nigerian Insurance market, as the only private local reinsurer. It is also developing its presence in the rest of sub-Saharan Africa and has offices in Cameroon, Kenya and Tunisia. The firm is in the advanced stages of establishing a subsidiary in Kenya and is seeking approval to establish a Tunisian branch. A.M. Best believes that the offices outside Nigeria have enabled Continental Re to manage its regional customers more effectively and to diversify its underwriting portfolio.

Continental Re has grown rapidly following a material capital injection in 2007. Gross premium income rose from NGN 2.8 billion in 2007 to NGN 11.6 billion in 2010, with an increase of approximately 50% in 2010 alone. Growth has been achieved across Africa and in all lines of business and is likely to be maintained in the near term, albeit at a slower pace than in the recent past.

In A.M. Best's opinion, Continental Re's insurance portfolio is fairly well diversified by line of business. In 2010, gross premiums written (GPW) was divided between the following lines: fire (including commercial property and engineering risks) (35%), general accident (including burglary/cash in transit, personal accident, fidelity guarantee and other miscellaneous risks) (17%), marine and aviation (13%), life (12%), liability (14%) and energy (9%). Geographically, 20 African countries accounted for 99% of gross premium revenue, with Nigeria accounting for the majority (66%). By regional

office, revenue was split between the following offices: Nigeria (69%), Cameroon (18%), Kenya (12%) and Tunisia (1%).

Continental Re's life business is all proportional treaty. For non-life, approximately 85% is proportional.

A.M. Best anticipates that as Continental Re continues to grow, diversification will improve both by line of business and geography.

## **FINANCIAL PERFORMANCE**

**Overall Earnings:** Continental Re achieved a profit before tax of NGN 1,585 million in 2010, split fairly evenly between underwriting earnings of NGN 769 million and investment earnings of NGN 798 million. This was an improvement on the NGN 980 million reported in 2009 which itself was up on the NGN 840 million reported in 2008. A further increase in overall earnings is anticipated in 2011, supported by an increase in premium income and higher investment income from a growing asset base.

**Underwriting Income:** In 2010, Continental Re reported an underwriting profit of NGN 769 million (2009: NGN 492 million), divided between a profit on life business of NGN 124 million and non-life earnings of NGN 646 million. Under local regulations a significant proportion of the surplus in the life business is allocated to a contingency reserve.

Technical performance has been good over the last three years, in spite of strong growth and in 2010 the company achieved a combined ratio for non-life business of 79.3% (2009: 82.4%). As Continental Re continues to grow its underwriting portfolio, further embedding of its improved risk management standards and procedures will be important to support the maintenance of underwriting discipline. If this is achieved, underwriting results are likely to remain good, although the combined ratio is expected to deteriorate modestly over the next few years to between 80% and 85%.

Continental Re's overall performance is likely to continue to be affected by the write-off of premiums owed by debtors, which in 2010 reduced pre-tax profits by NGN 835 million (NGN 275 million in 2009). In common with peers in the region, Continental Re's volume of outstanding premium debtors is high, but has reduced as a percentage of GWP from 61% in 2007 to 35% in 2010. Reducing this ratio further remains a key focus of management.

**Investment Income:** Continental Re's reported a modest investment return (including realised and unrealised gains and losses) in 2010 of 6.8% (5.1% in 2009). This should be evaluated in the context of the prevailing Nigerian inflation rate; 12% in 2010. This improved return reflects the move from cash to fixed income bonds together with reduced allocation to equities. The company's equity investments performed poorly in 2008 and 2009. The majority of invested assets are invested in either cash and cash equivalents or fixed interest securities (around 80% as at 31 December 2010).

## CAPITALIZATION

In 2007, Continental Re recapitalised, following the decision by the Nigerian National Insurance Commission (NAICOM) to impose on reinsurers a minimum absolute capital requirement of NGN 10 billion. The company listed on the Nigerian Stock Exchange (NSE) in the same year and its shareholding is made up largely by foreign investors (around 60%).

The capital injection increased shareholders' funds to over NGN 11 billion from NGN 2.2 billion at year end 2006 and has supported strong premium growth over the last three years. Although a further material increase in underwriting risk is anticipated in 2011 and 2012, risk-adjusted capitalisation is expected to remain strong. A.M. Best will continue to closely monitor the impact of premium growth on the company's performance and risk-adjusted capitalisation.

In the absence of appropriate third party catastrophe models, Continental Re conducts internal analysis to assess its underwriting portfolio's exposure to catastrophe risk. Its analysis indicates that Continental Re's largest probable maximum loss would result from a storm surge within Lagos, an event for which it has strong reinsurance protection. Exposure to catastrophic events is low throughout Nigeria due to the low level of insurance penetration.

**Reserve Quality:** Continental Re's reserving practices have improved significantly in recent years. In 2009, the company recruited a fully qualified actuary as Chief Risk Officer to oversee and improve its risk management.

An internal actuarial analysis of reserves was undertaken in 2009 and 2010, along with profitability analysis and an external actuarial review. Currently, non-life reserves are set at the higher of regulatory requirements, externally advised best estimate and internally assessed best estimate. At 31 December 2010, total non-life reserves held by Continental Re (unearned premium reserves plus outstanding claims reserves) were approximately equal to those calculated by the external actuary.

Life reserves are set in accordance with the opinion of independent actuaries. At year end 2010, the life fund had a reserve surplus of NGN 310 million (before the transfer to profit/loss) above the externally determined best estimate.

## LIQUIDITY

**Overall Liquidity:** Continental Re's liquidity is good. Over two thirds of the company's invested assets are held in liquid funds such as cash, deposits and quoted equities.

**Source of Information: Company Annual Report**

**Summarized Accounts as of December 31, 2010**

**US \$ per Local Currency Unit .00635 = 1 Nigerian Naira (NGN)**

## **STATEMENT OF INCOME**

	12/31/2010 NGN(000)	12/31/2010 USD(000)
General technical account:		
Reinsurance premiums assumed	10,253,976	65,113
Gross premiums written	10,253,976	65,113
Reinsurance ceded	867,955	5,512
Net premiums written	9,386,021	59,601
Increase/(decrease) in gross unearned premiums	820,610	5,211
Net premiums earned	8,565,411	54,390
Total underwriting income	8,565,411	54,390
Net claims paid	2,364,860	15,017
Net increase/(decrease) in claims provision	1,339,357	8,505
Net claims incurred	3,704,217	23,522
Management expenses	820,350	5,209
Acquisition expenses	2,560,696	16,260
Net operating expenses	3,381,046	21,470
Other technical expenses	834,646	5,300
Total underwriting expenses	7,919,909	50,291
Balance on general technical account	645,502	4,099
Life technical account:		
Gross premiums written	1,390,744	8,831
Net premiums written	1,390,744	8,831
Net premiums earned	1,390,744	8,831
Net investment income	31,986	203
Total revenue	1,422,730	9,034
Net claims paid	611,608	3,884
Net claims incurred	611,608	3,884
Net increase/(decrease) in long term business provision	174,446	1,108

Management expenses	217,199	1,379
Acquisition expenses	335,168	2,128
Net operating expenses	552,367	3,508
Other technical expenses	-39,642	-252
Total expenses	1,298,779	8,247
Balance on long-term technical account	123,951	787
Combined technical account:		
Reinsurance premiums assumed	10,253,976	65,113
Gross premiums written	11,644,720	73,944
Reinsurance ceded	867,955	5,512
Net premiums written	10,776,765	68,432
Increase/(decrease) in gross unearned premiums	820,610	5,211
Net premiums earned	9,956,155	63,222
Net investment income	31,986	203
Total revenue	9,988,141	63,425
Net claims paid	2,976,468	18,901
Net increase/(decrease) in claims provision	1,339,357	8,505
Net claims incurred	4,315,825	27,405
Net increase/(decrease) in long term business provision	174,446	1,108
Management expenses	1,037,549	6,588
Acquisition expenses	2,895,864	18,389
Net operating expenses	3,933,413	24,977
Other technical expenses	795,004	5,048
Total underwriting expenses	9,218,688	58,539
Balance on combined technical account	769,453	4,886
Non-technical account:		
Net investment income	621,063	3,944
Realised capital gains/(losses)	103,335	656
Unrealised capital gains/(losses)	74,023	470
Exchange gains/(losses)	14,727	94
Other income/(expense)	2,398	15
Profit/(loss) before tax	1,584,999	10,065
Taxation	354,766	2,253

Profit/(loss) after tax	1,230,233	7,812
Dividend to shareholders	570,500	3,623
Transfer to reserves	321,526	2,042
Retained Profit/(loss) for the financial year	338,207	2,148
Retained Profit/(loss) brought forward	635,747	4,037
Retained Profit/(loss) carried forward	973,954	6,185

## ASSETS

	12/31/2010 NGN(000)	12/31/2010 % of total	12/31/2010 USD(000)
Cash & deposits with credit institutions	6,582,607	35.0	41,800
Bonds & other fixed interest securities	4,080,619	21.7	25,912
Shares & other variable interest instruments	595,968	3.2	3,784
Liquid assets	11,259,194	59.9	71,496
Unquoted investments	1,234,091	6.6	7,836
Real Estate	1,557,834	8.3	9,892
Inter-company investments	1,998	0.0	13
Other investments	48,842	0.3	310
Total investments	14,101,959	75.0	89,547
Insurance/reinsurance debtors	4,090,112	21.8	25,972
Inter-company debtors	10,413	0.1	66
Other debtors	443,561	2.4	2,817
Total debtors	4,544,086	24.2	28,855
Fixed assets	115,926	0.6	736
Prepayments & accrued income	29,133	0.2	185
Total assets	18,791,104	100.0	119,324

## LIABILITIES

	12/31/2010 NGN(000)	12/31/2010 % of total	12/31/2010 USD(000)
Capital	5,186,372	27.6	32,933
Paid-up capital	5,186,372	27.6	32,933
Non-distributable reserves	3,915,451	20.8	24,863

Other reserves	1,543,679	8.2	9,802
Retained earnings	973,954	5.2	6,185
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Capital & surplus	11,619,456	61.8	73,784
Gross provision for unearned premiums	2,785,534	14.8	17,688
Gross provision for outstanding claims	2,223,453	11.8	14,119
Gross provision for long term business - life	747,758	4.0	4,748
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Total gross technical reserves	5,756,745	30.6	36,555
Insurance/reinsurance creditors	275,970	1.5	1,752
Inter-company creditors	338	0.0	2
Other creditors	503,846	2.7	3,199
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Total creditors	780,154	4.2	4,954
Accruals & deferred income	52,677	0.3	334
Other liabilities	582,072	3.1	3,696
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Total liabilities & surplus	18,791,104	100.0	119,324

## HISTORY

Continental Re commenced writing non-life business in 1987 and life business in 1990. The company became internationally owned in 2003 and its Cameroon office was opened in 2004. Continental Re recapitalised in February 2007 to become a NGN 10 billion company in response to new requirements of the National Insurance Commission (NAICOM). The company was also listed on the Nigerian Stock Exchange (NSE) on 30 May 2007.

During the recapitalisation, a total of USD 46.5 million was injected into Continental Re by a group led by Emerging Capital Partners and a further USD 9 million was provided by RP Capital Group, Genesis Emerging Markets Fund Limited and Investec Asset Management. Further amounts were also raised locally. This enabled Continental Re to meet its minimum capital requirements and gain approval to continue as a reinsurer to transact business within the Federal Republic of Nigeria.

## MANAGEMENT

Following re-capitalisation in 2007, Continental Re's management set ambitious growth targets for the company, requiring significant organisational changes. Senior members of staff have been recruited to manage and develop new lines of business within the company, as well as staff to manage and operate new offices in Kenya and Tunisia. New technical software is being implemented that will integrate underwriting, claims, retrocession and reinsurance accounting modules. A Chief Risk Officer was recruited in 2009 to strengthen internal risk management operations. A UK-based ERM consultant

assisted in the development of the ERM model in 2010 and an internal capital model is expected to be completed by the end of 2011.

A.M. Best views improvements to Continental Re's risk management framework positively, but does not expect risk management systems to be fully embedded within management's day-to-day decision making practices and for the technical developments to be fully realised for a number of years.

## REINSURANCE

The credit quality of Continental Re's retrocession programme has improved in recent years. In 2007 and 2008 only around half of the total outwards reinsurance exposure was placed with reinsurers rated at a secure level. The proportion of reinsurance ceded to securely rated reinsurers has increased to 98%, compared to 81% in the previous year.

Continental Re purchases non-proportional reinsurance protection to cover its various lines of business, with a different programme and panel of reinsurers in place for each line. Fire risks are covered by USD 18.5 million in excess of USD 1.5 million; marine and aviation risks are covered by USD 7 million in excess of USD 1 million; motor/accident risks are covered by USD 7.25 million in excess of USD 0.75 million; and energy risks are covered by USD 17.5 million in excess of USD 2.5 million.

## BALANCE SHEET ITEMS

	NGN (000) <u>2010</u>	NGN (000) <u>2009</u>	NGN (000) <u>2008</u>	NGN (000) <u>2007</u>	NGN (000) <u>2006</u>
Liquid assets	11,259,194	9,362,587	9,735,822	10,592,662	1,396,669
Total investments	14,101,959	11,436,794	10,968,553	11,452,435	2,266,364
Total assets	18,791,104	15,644,809	14,353,589	14,159,646	4,230,964
Gross technical reserves	5,756,745	3,422,326	1,976,829	1,132,248	1,178,032
Net technical reserves	5,756,745	3,422,326	1,976,829	1,132,248	1,178,032
Total liabilities	7,171,648	4,475,192	3,219,261	2,344,376	2,006,560
Capital & surplus	11,619,456	11,169,617	11,134,328	11,815,270	2,224,404

## INCOME STATEMENT ITEMS

	NGN (000) <u>2010</u>	NGN (000) <u>2009</u>	NGN (000) <u>2008</u>	NGN (000) <u>2007</u>	NGN (000) <u>2006</u>
Gross premiums written	11,644,720	7,403,914	5,275,296	2,806,337	2,611,599
Net premiums written	10,776,765	7,169,198	5,087,836	2,676,749	2,544,296
Balance on technical account(s)	769,453	492,032	200,547	534,835	219,655
Profit/(loss) before tax	1,584,999	979,814	839,150	1,008,292	326,038
Profit/(loss) after tax	1,230,233	905,217	754,989	878,535	247,047

## LIQUIDITY RATIOS (%)

	<u>2010</u>	<u>2009</u>	<u>2008</u>	<u>2007</u>	<u>2006</u>
Total debtors to total assets	24.2	25.4	22.7	18.6	45.5
Liquid assets to net technical reserves	195.6	273.6	492.5	935.5	118.6
Liquid assets to total liabilities	157.0	209.2	302.4	451.8	69.6
Total investments to total liabilities	196.6	255.6	340.7	488.5	112.9

## PROFITABILITY RATIOS (%)

	<u>2010</u>	<u>2009</u>	<u>2008</u>	<u>2007</u>	<u>2006</u>
Loss ratio	43.2	42.2	38.8	26.3	37.9
Operating expense ratio	36.0	40.1	41.8	49.3	53.2
Combined ratio	79.3	82.4	80.7	75.5	91.1
Other technical expense or (income) ratio	8.9	6.0	11.7	9.6	...
Net investment income ratio	7.3	17.5	31.4	31.5	7.1
Operating ratio	80.9	70.9	61.0	53.6	84.0
Benefits paid to net premiums written (Life)	56.5	26.4	38.6	22.8	25.4
Expense ratio (Life)	36.9	67.1	39.9	47.3	35.6
Return on net premiums written	11.4	12.6	14.8	32.8	9.7
Return on total assets	7.1	6.0	5.3	9.6	6.9
Return on capital & surplus	10.8	8.1	6.6	12.5	13.6