

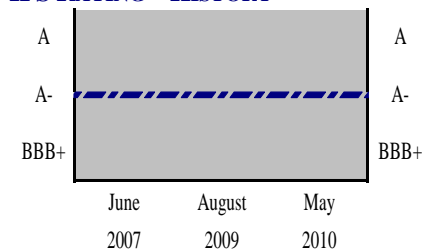


RATINGS (MAY 2010)

EAST WEST INSURANCE COMPANY LIMITED (EWI)

	NEW	PREVIOUS
Insurer Financial Strength (IFS)	A-	A-

IFS RATING – HISTORY



FINANCIAL DATA

PKR (mln)

	1Q10*	Dec-09	Dec-08
Total Equity	331	330	867
GPW	147	632	614
Net Profit / (loss)	2	(537)	266
Equity/NPW %	102	82	220
Liquid Assets/ Total Assets %	41	44	70

* Based on unaudited accounts for 3 months ended March 31, 2010.

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PROFILE

- EWI commenced operations as a general insurance company in 1983 and is listed on the Karachi Stock Exchange. Yunus family holds the majority shareholding (68% at end-09) in the company. The family also owns East West Life Assurance Company Limited (formerly Metropolitan Life Assurance Company of Pakistan Limited).
- Mian Mehboob Ahmad, having extensive exposure in the insurance sector, is the Chairman of BoD. The sponsors dominate the rest of the board with five out of the seven members including the CEO, belonging to the Yunus family.

RATING RATIONALE AND KEY RATING DRIVERS

- EWI's rating reflects the relative stability in the company's underwriting performance. At the same time, the rating factors in the company's high exposure to the market risk, aggravated by concentration in a single scrip that has already resulted in significant impairment loss. This has weakened the company's equity base, and consequently reduced risk absorption capacity. Meanwhile, increasingly competitive environment requires further strengthening of the risk management policies and management information system to sustain the company's profitability and market standing.
- The rating is dependent on rationalization of the investment portfolio in order to ensure a stable contribution towards the bottom-line, while improving the company's overall risk absorption capacity. Meanwhile, formulation and adoption of a cohesive strategy is vital for the company's growth. Any further material deterioration in the company's equity and/or significant decline in its overall profitability would negatively impact the rating.

ASSESSMENT

- EWI, unlike other non-captive insurance companies of similar size, that rely heavily on the motor business for volume growth, has a portfolio dominated by fire segment (around 57%), followed by a largely even distribution between marine (12%), motor (12%) and misc. (19%). In recent years the mix has changed in favor of the misc. segment owing to increased focus on the livestock and crop insurance segments, where the company has had relatively low loss experience. Within motor insurance, a sizeable portion of the business is derived from tractor insurance, which has remained a low risk segment.
- In 2009, gross premium written (GPW) registered marginal growth of 3% (2008: 22%) mainly on account of the economic slowdown further intensifying the competitive insurance landscape. The downtrend in both volume and value of trade on a YoY basis also impacted EWI's growth. Despite the slowdown in GPW, the company registered 11% increase in underwriting profitability owing to a considerable decline in loss ratio of motor and others segment on account of stringent claim verification procedures. However, the impact of underwriting profitability was diluted by impairment loss of PKR555mln, which rendered the bottom line of the company in red.
- During 2008, EWI had incurred significant impairment losses (PKR549mln) on its investments, recognition of which was deferred as per relaxation by the SECP. The effect of this deferment was evident in 2009 wherein EWI recognized sizeable impairment loss pertaining to CY08 and CY09. The investment portfolio remains concentrated in a single scrip (book value – PKR560mln – as percentage of total book value of investments: 71% at end-09), hence, subjecting EWI to substantial market risk. The management, cognizant of this fact, plans to diversify its investment portfolio in order to reduce high concentration. Divestment is expected to be completed within 2010. However, given subdued capital markets, the company has incurred additional impairment loss of around PKR85mln till 25-May during current year. Although EWI marginally increased its investments in government securities (2009: PKR33mln; 2008: PKR21mln), in absence of an effective investment strategy and policy, it would remain exposed to high market risk.
- Going forward, the company intends to continue its focus on fire segment while consolidating its existing branch network. The company is targeting GPW growth of around 15% in CY10 through penetration in the corporate, livestock, and crop insurance sectors. The management has historically followed a conservative stance towards risk; therefore, the intended expansion would require strengthening of the risk management framework and timely implementation of the upgraded software. Furthermore, penetration into corporate segment would require competing with larger insurance companies, which may be difficult for EWI considering its relatively weak brand franchise.
- EWI follows adequate risk management procedures and guidelines; however, it relies on fragmented IT resources and does not maintain any comprehensive documented standard operating guidelines, which may result in informal practices and lead to inappropriate pricing and undesired exposures. Cognizant of this situation, the management is in the process of developing in-house core software, which, once fully implemented, is expected to strengthen the internal control framework.
- EWI maintains adequate reinsurance arrangements for all of its segments with a significant cover from "A-" and above rated re-insurers. EWI's cession trend has been largely steady over the years (2009: 36.4%, 2008: 35.8%).
- Over the years, EWI had improved its risk absorption capacity on the back of a strong equity base emanating from significant capital market gains. However, in the absence of an effective investment strategy and requisite risk management systems, EWI was unable to capitalize on its relative strength. As a result, impairment loss on investments eroded EWI's risk absorption capacity (equity – 2009: PKR330mln; 2008: 867mln). Going forward, if the impairment drag continues, EWI's risk absorption capacity would remain under pressure.