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Yearning for life

The worst days are now in the past for Ukrainian life insurance business. The market remains small but foreign companies with long-term prospects have already come to dominate it



The Stability Rating of Life Insurance Companies

Group A insurance companies

№	Company	2005												
		Net capital, thousand USD	Liquid assets, thousand USD	Liabilities' total, thousand USD	Profit from financial operations, thousand USD	Average financial investment, thousand USD	Net actuarial reserves, thousand USD	Equity/debt ratio	Assets' liquidity ratio	Insurance risk ratio	Inverse solvency ratio	Profitability	Changes in equity	
1.00	Upiter	4266.99	3099.58	453.29	258.77	153.21	187.92	0.06	6.84	0.09	0.11	0.02	0.95	
2.00	Veksel-Life	2435.84	2450.34	101.11	181.58	22.66	92.16	0.00	24.23	0.08	0.04	0.03	0.03	
3.00	Tekom-Life	2386.59	694.18	515.82	277.88	1673.03	515.25	0.00	1.35	0.19	0.22	0.08	0.08	
4.00	Lider-Life	4180.38	43.27	59.31	0.20	1928.22	54.10	0.34	0.73	0.02	0.01	-0.01	1.15	
5.00	PZU Ukraine Life Insurance	3457.52	3132.77	689.80	-122.50	255.50	617.21	0.04	4.54	0.36	0.20	-0.18	1.54	
6.00	Ukrgazprompolis Life	2046.34	2059.86	18.00	73.25	0.00	0.00	0.00	114.44	0.00	0.01	0.03	N/A	
7.00	Illichivska	2115.07	1867.19	56.26	273.41	2.51	22.34	0.01	33.19	0.02	0.03	0.14	-0.07	
8.00	Blakitny Polis	3247.70	4278.12	8881.07	783.70	1384.61	8321.80	1.05	0.48	1.61	2.73	0.29	0.41	
9.00	Alico AIG Life	2279.23	3552.79	15957.64	802.32	6446.99	10529.52	0.30	0.22	5.20	7.00	-2.09	0.01	
10.00	Garant-Life	2172.06	4935.52	6068.99	254.46	2660.34	5742.42	0.06	0.81	2.96	2.79	0.07	0.07	
Group total		28587.72	26113.62	32801.29	2783.07	14527.08	26082.71	0.19	18.68	1.05	1.31	-0.16	0.46	

Source: companies' data; calculations by Expert



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Fifty life insurance companies (ICs) are already operating in the Ukrainian market. In the first half of 2006 alone, six new companies have become registered.

However, the scale of their activity still lags far behind the ambitious social tasks that life insurance sector can potentially accomplish. By the end of June, life insurers have amassed actuarial reserves worth \$91m, which is still a mere 0.6% of household incomes, accumulated by the banks.

The two rivals

Accumulative insurance programmes, capable of competing with bank deposits, are yet to be offered by the majority of life insurance companies to Ukrainian households. This is due to the fact that the insurance companies still keep almost 39% of their reserves in banks (Fig. 9). Non-resident insurance companies, which comprise the backbone of the life insurance segment, are even less inclined to make competitive offers to households. The products that these companies put forward are all connected with long-term accumulation, which makes them prioritise stability over policy yield. Stability, in turn, is usually ensured by their parent companies' substantial assets. Currently, several foreign companies are in the process of dividing the Ukrainian market among themselves.

A major rivalry has unfolded between Alico AIG Life and Grawe Ukraine, the two companies that collected almost half of all life insurance premiums. As of 2005, Grawe Ukraine collected premiums worth \$9.7m, while Alico AIG amassed \$6.5m. The first half of 2006 saw the companies switching roles: with premiums reaching \$9.1m, Alico AIG surpassed Grawe

Ukraine, which collected \$7.5m. But both companies continued to quickly augment their premiums.

Grawe Ukraine belongs to Grazer Wechselseitige Versicherung AG, an Austrian holding company. This spring, in a joint effort with UkrSibbank, Grawe Ukraine became one of the first companies to offer Ukrainian households an accumulative insurance programme, which combines life insurance and accumulation of funds and which should have affected their collection of premiums.

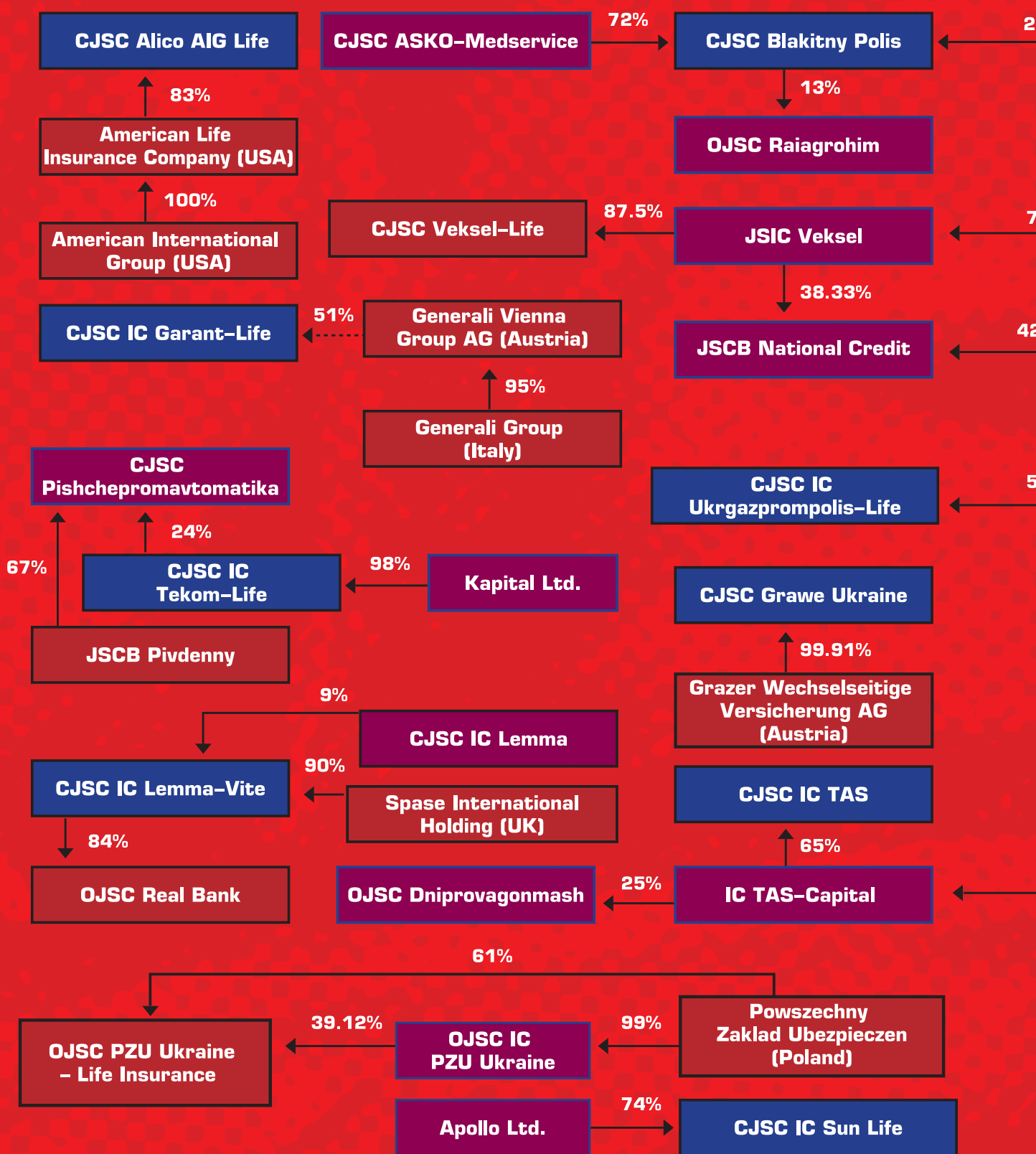
Alico AIG is directly owned by Alico, a company which is part of AIG, the world's largest insurance holding with capitalization exceeding \$150bn at the beginning of September 2006. In 2004–2005, the holding company survived a major scandal when it was accused of unethical interactions with an insurance broker and of inaccurate information disclosure. As a result of this controversy, the company dismissed its top-management and revised the annual report several times during the course of 2005. Recently, AIG and the US government managed to settle the matters out-of-court, and the company retained its position as the world's most expensive insurance holding. The strategy of the Ukrainian Alico AIG is surveyed through the completed questionnaires. The company is actively investing into its agency chain. In 2005 alone, its losses amounted to \$4.8m, which can be roughly compared with its customer acquisition costs. It is quite possible that losses are a part of the company's long-term strategy aimed at building up an agency chain and maximising the number of future clients. Therein lies the specificity of life insurance as a business — a contract is signed only once, but for an extended period of time.

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Table 5

	Changes in gross premiums written	Capacity to cover own risk	Return of investment	Intermediate integral indicator	Points for transparency	Points for number of insureds	Points for concentration of insurance payments	Points for acquisition costs	Integral indicator	Stability rating	First half of 2006				
											Net capital, thousand USD	Net premiums, thousand USD	Assets, thousand USD	Integral indicator	Stability rating
	0.10	0.51	1.69	1.60	0.90	1.00	0.90	0.90	1.17	Aaa	4366.57	141.23	4796.97	1.54	Aa
	N/A	1.97	8.01	1.30	0.95	1.00	1.00	1.00	1.24	Aaa	2447.29	151.05	2657.84	1.24	Aaa
	0.42	0.99	0.17	1.53	0.90	1.00	0.95	1.00	1.30	Aaa	2412.20	274.65	3137.15	1.43	Aaa
	254.79	1.00	0.00	1.45	0.90	1.00	1.00	1.00	1.31	Aaa	4140.36	129.49	4339.80	1.51	Aa
	5.44	0.96	-0.48	1.45	0.90	1.00	1.00	1.00	1.31	Aaa	3148.36	935.90	5445.05	1.77	Aa
	N/A	N/A	N/A	1.45	1.00	1.00	1.00	1.00	1.31	Aaa	2091.96	4.32	2126.00	1.37	Aaa
	N/A	1.00	108.72	1.45	0.95	1.00	1.00	1.00	1.38	Aaa	1930.50	159.23	2149.27	1.31	Aaa
	0.46	1.00	0.57	2.15	0.90	0.95	0.90	1.00	1.65	Aa	1853.62	2784.69	15282.50	2.27	Aa
	0.83	0.97	0.12	2.65	0.90	0.90	0.90	0.90	1.74	Aa	1405.13	9108.87	19574.02	1.81	Aa
	N/A	N/A	0.10	2.05	0.95	0.90	1.00	1.00	1.75	Aa	4348.00	2931.43	11642.46	1.49	Aaa
	43.67	1.05	13.21	—	—	—	—	—	—	—	28143.98	16620.85	71151.05	—	—

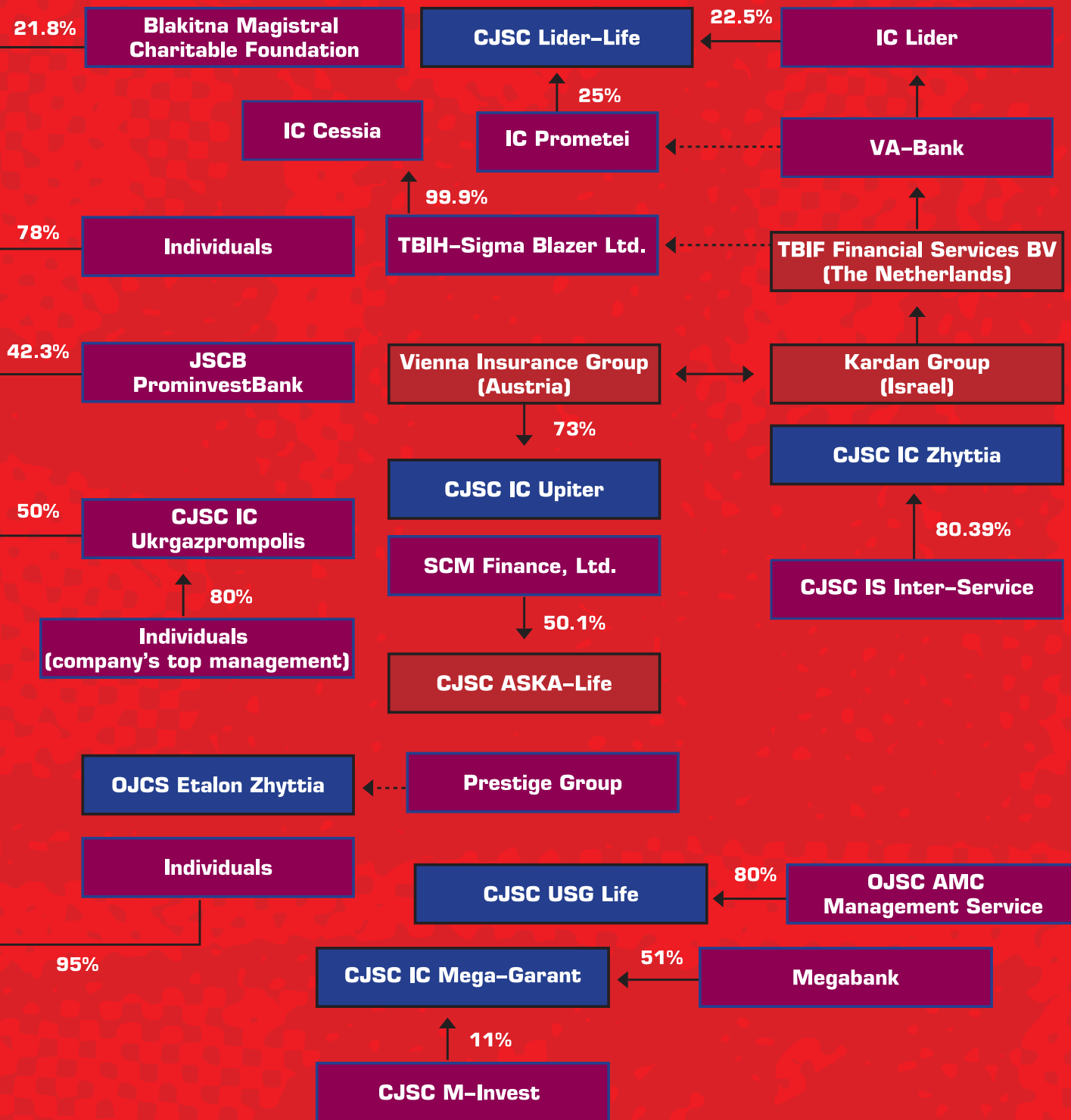
The corporate structure of life insurance companies



Sources: Stock Market Infrastructure Development Agency (ARIFR), companies' data

with assets exceeding USD 4m at the beginning of 2006

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- Life insurance companies registered in Ukraine
- Non-residents
- Residents

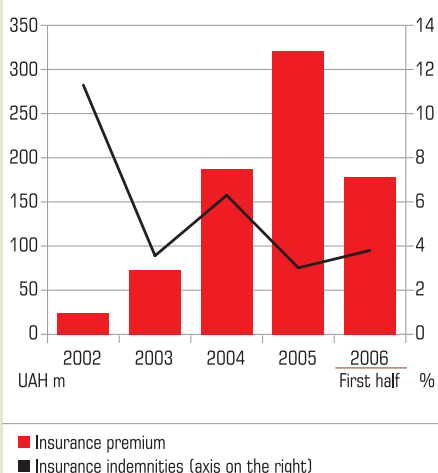
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Map 7

The life insurance market is still small,
but it is growing fast

Changes in life insurance premiums and indemnity
payments in Ukraine



Source: State Commission for Regulation
of Financial Services Markets of Ukraine

It will be difficult for Ukrainian insurers to compete

with foreigners who invest millions of dollars into their

companies' development

The transparent ten

Only ten life insurance companies offered us all the necessary data. Among Group A insurance companies, Upiter assumed the leading position. Together with Lider Life, a company that holds the fourth place, it is managed by VA-Bank's foreign shareholders and individuals affiliated with them. One of VA-Bank's major foreign shareholders is TBIF Financial Services B.V., which

belongs to the Israel-based Kardan Group. Last year, Kardan Group and Vienna Insurance Group (VIG) struck an agreement cementing their alliance in East European markets. As a result, VIG bought a 40% stake in one of the companies comprising Kardan Group. In Ukraine, VIG owns the Upiter IC. Prior to VIG's purchase of its controlling stake, the group used to control Upiter through its subsidiary struc-

The under-regulated regulator

Valery Alyoshin, the Head of the State Commission for Regulation of Financial Services Markets of Ukraine (Gosfinuslug of Ukraine):

— I am a strong supporter of the idea that the information regarding companies' state of affairs and their key indicators should be accessible for the scrutiny of the consumers and experts capable of professional assessment of the insurers' activities. Legislation is not the only inhibitor to our cause. Members of the State Commission for Regulation of Financial Services Markets have different positions with regard to this problem, while market subjects differ in their levels of readiness for information disclosure. A hasty solution may lead to negative consequences. Most importantly, up-to-date information is not available to the Commission because of our primitive technical facilities. We still have no consolidated database which could in the least provide monthly updates on the markets' trends, to say nothing of the daily analysis of financial statements.

When the National Bank of Ukraine was being set up, its financial capacities were virtually unlimited. The bank purchased the most advanced information systems and now has access to all the essential data. Unfortunately, our Commission has rather modest amounts of financing and technical facilities. We have upgraded one software product and have just started implementing it; however, we do not have enough funds to get the data collection process up and running.

— Perhaps you might consider supporting the idea of market participants transferring a certain part of their profit or turnover towards the maintenance of a market regulator?

— I am convinced that the activity of financial regulators must be sufficiently funded because both sides have incentives for dealing with a reliable regulator. Most importantly, the participants of the financial services market need a supervisor to rid the market of pests which corrupt its sector's image. The ideal solution — the amalgamation of financing from the two sources, namely, deductions from both the companies and the national budget — for the time being contradicts the Ukrainian legislation. It is essential to either change a section of the legislation that regulates financing of government organizations or alter the status of the Commission, so that it ceases to be a governmental organization.



UKRAINFORM

ture. It is still unclear what kind of policy TBIF Financial Services B.V. and VIG will adopt toward their subsidiaries in Ukraine and whether the latter will be affected by the aforementioned alliance agreement. A resolution should be reached by the end of September, following a meeting of the Lider Life IC shareholders. In any case, it is unlikely that the merger of two companies will lead to a monopoly: the companies' data reveal that the volume of premiums, collected over the first six months of 2006, does not exceed \$0.4m.

Garant-Life is the only company that has managed to improve its 2005 stability rating in the first half of 2006. At present, Generali, an Italian insurance holding company, is in the process of acquiring this IC, together with other units of Garant Group. Such a turn of events may incite Garant-Life's growth, especially considering that in 2005 this IC collected the third largest amount of premiums in the Ukrainian market. According to the company's data, its premiums collection for January-July

totals \$3.8m. At the beginning of July, Generali held assets worth €350bn, while at the same time its investment assets reached €310bn.

The patriots' burden

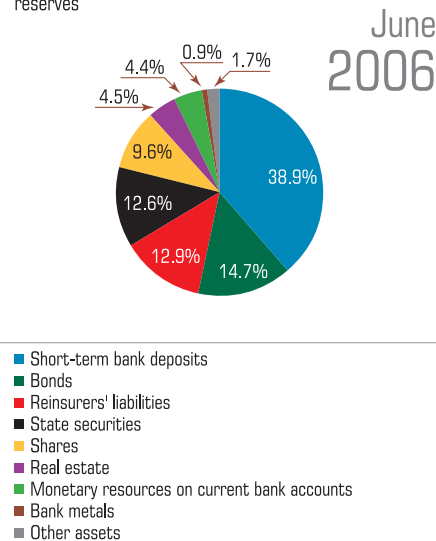
Grawe Ukraine, the leader of group C, is one of the few companies owned by non-residents. The ASKA-Life IC is part of Rinat Akhmetov's System Capital Management, while TAS belongs to the family of Sergey Tigipko, the former head of the National Bank of Ukraine. Lemma-Vite is officially controlled by the non-resident Spase International Holding. However, the directories of the US Securities and Exchange Commission and the UK Financial Services Authority contain no information about this company.

Etalon Zhyttia, another Group C leading company, is about to be acquired by a non-resident. Fortis, an international financial group, is purchasing this IC from the Aval bank. The deal is expected to be consummated in the last quarter of 2006.

Map 8

Insurers deposit their reserves in banks

The structure of life insurance companies' actuarial reserves



Source: State Commission for Regulation of Financial Services Markets of Ukraine

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— What do you think about setting up a mega-regulator in Ukraine by means of merging bank supervision, Gosfinuslug and Securities and Stock Market State Commission (GKTSBFR)?

— I have conflicting opinions on this issue. This prospect was considered at length when the law on financial services (in which the functions of the committee are specified) was under construction. There was a common understanding that a unified regulator would become an absolute necessity in five to ten years. But a demand for it has surfaced already and has to do primarily with the fact that we still mostly deal with financial conglomerates, which encompass banks, insurance companies, private retirement funds and credit unions.

I am not sure whether becoming independent from the National Bank is the top priority of the bank supervision department. Gaining independence will lead to problems faced by other commissions, namely, the problems of financing. For instance, administrators of the private retirement benefits market are fully controlled by Gosfinuslug, while asset management companies are accountable to GKTSBFR.

— Which side do you support in the conflict between private pension funds and insurers with regard to accumulation programmes?

— This widely publicised pseudo-conflict between the incipient market of private retirement funds (PRF) and the established one comprising life insurance companies has several dimensions. A certain concept of the pension reform has been adopted in Ukraine and has been enacted in two basic laws: on compulsory retirement insurance and on the non-state retirement benefits. These laws specify the functions, the role and the potential of the insurers and the PRFs. The behind-the-scenes attempts at modifying the conceptual base were interpreted as improper by the market. I am a strong supporter of the scenario in which both the insurance companies and the retirement funds belong to a single retirement system. One the other hand, I am against the Ukrainian retirement market welcoming products that have already been rejected by the West. Here I am talking about the defined payouts. If the decision has been legislatively confirmed to implement retirement schemes with defined contributions, it is now time to execute it.

— In Ukraine, the number of insurance companies exceeds four hundred. According to specialists, this is a very high number. Do you think that their numbers will continue to increase?

— Yes, the numbers of those wishing to start an insurance business in Ukraine do not seem to diminish. Every week, the Commission receives several applications for the registration of new companies. For us, it would be ideal to work within a consolidated market of companies that have knit a developed network among themselves. The insurance market is primarily appealing to investors because of its attractive taxation system, which, one the other hand, facilitates the so-called 'gray schemes'. Besides, the insurance market can serve as a springboard for breaking into other market segments. Thus, the purpose of setting up today's companies is their prompt subsequent sale, which eases the entry of foreign investors into the Ukrainian market.

— And will the market consolidate?

— By all means. The Ukrainian legislation does not impose any limits on the entry of foreign capital into the insurance market. Moreover, we have long ago abolished all limitations on the non-residents' participation in the share capital of any insurance company.

— As foreign players enter the market, will insurance companies' share capital become subject to stricter regulations?

— Sooner or later, this is exactly what will happen. However, new rules have to be specified in the new version of the Law on Insurance. If we come up with resolutions, inadequate for either the market or the legislators, the Commission will have to admit that its policies and initiatives are flawed.

— In other words, although as a specialist you understand that capitalisation has to be subject to stricter regulations, in practice you realise that the parliament will not support such a decision?

— Yes, but it is not capitalisation alone that matters. We have to make sure that growing capitalisation will encourage companies to develop high-quality insurance products. At present, it is essential to update the technology, bring down the clients' risks, make insurers' information more accessible and improve the qualification of personnel. Capitalisation growth may help companies achieve these goals.

■ Andrei Blinov, Svetlana Slesarchuk

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The Stability Rating of Life Insurance Companies

Table 6

Group C Insurance Companies

№	Company	2005								
		Assets, thousand USD	Shareholders' equity, thousand USD	Gross income, thousand USD	Equity/debt ratio, %	Assets' liquidity ratio, %	Inverse solvency ratio, %	Profitability ratio, %	Integral indicator	Stability rating
1	Grawe Ukraine	16,148.7	6,517.3	8,030.8	30.77	144.29	147.78	5.23	1.96	Ca
2	ASKA-Life	13,196.1	2,505.5	5,651.9	6.88	58.29	426.69	-26.60	2.51	Ca
3	Etalon Zhyttia (Etalon Plus)	5,098.1	3,506.6	3,225.8	0.38	299.47	45.39	20.90	1.65	Ca
4	Lemma-Vite	24,627.5	21,260.9	2,122.8	22.66	87.70	15.84	3.68	1.28	Caa
5	TAS (Privat Polis)	10,012.7	3,077.4	2,055.1	5.09	94.28	225.36	-18.63	2.84	Cbb
6	EKKO	2,843.5	2,164.6	1,359.4	0.62	17.94	31.36	5.08	2.22	Ca
7	Sun Life	5,794.3	5,521.7	799.3	97.22	137.09	4.94	3.43	1.64	Ca
8	Zhyttia	1,713.5	1,582.4	455.7	3.81	1258.94	8.28	9.69	1.37	Caa
9	Mega-Garant Life	3,880.3	2,654.7	303.4	13.85	42.89	46.17	8.16	2.17	Ca
10	Universal	2,734.6	2,043.5	202.3	29.74	61.25	33.82	-0.32	2.08	Ca
11	Insurance Planet	2,277.0	2,169.1	169.6	1.12	4.52	4.97	-0.39	2.04	Ca
12	DASK-Life	2,442.9	2,179.7	122.3	2.46	5.82	12.08	-1.82	2.04	Ca
13	UIG-Zhyttia	4,349.3	2,605.1	109.3	2.61	6.93	66.95	1.35	2.84	Ca
14	Life Traditions	2,237.9	2,180.4	34.0	0.08	66.23	2.64	3.65	1.40	Caa
15	Oranta-Life	2,034.7	2,008.0	16.3	0.27	253.89	1.33	-8.58	1.60	NR
16	Ukrainian Fire & Insurance Company - Life	2,121.5	2,081.2	13.4	0.06	334.32	1.94	0.37	1.40	NR
17	General Insurance Fund - Life	2,402.1	2,376.7	7.8	18.77	156.92	1.07	-1.62	1.60	NR
18	Finaco-Life	2,032.2	2,027.9	6.6	0.06	1115.98	0.21	-2.41	1.60	NR
19	Nadra-Life	1,601.8	1,587.1	3.0	0.07	25.44	0.93	-0.23	2.05	NR
20	Cross Clal Life	2,174.6	2,171.4	2.7	0.00	27.67	0.14	-0.19	2.05	NR
21	MBK-Life Insurance	2,083.2	2,082.5	1.3	0.20	35862.16	0.04	0.11	1.40	NR
22	Feniks-Life	2,169.6	2,167.8	1.0	0.03	358.43	0.08	-0.40	1.60	NR
23	Alliance Life Insurance	2,209.6	2,187.8	0.6	0.35	1.18	1.00	-0.31	2.05	NR
24	Ukrainian Industrial Insurance Company - Life	4,176.2	4,124.4	0.0	21.64	4.85	1.26	0.05	1.85	NR
25	Kredo-Life	152.0	152.0	0.0	0.21	N/A	0.00	-0.68	2.05	NR
26	UFA Group	2,151.0	2,151.0	0.0	0.00	N/A	0.00	-0.13	2.05	NR
27	Fokas Life	2,221.3	2,220.9	0.0	0.49	558110.00	0.02	0.27	1.40	NR
Group total		124,886.2	87,307.4	24,694.4	9.61	23941.46	40.01	-0.01	—	—

Sources: Stock Market Infrastructure Development Agency (ARIFR), companies' reports

The selection process

The process of rating the stability of life insurance companies is similar to that of rating the risk insurance companies: Expert RC (rating and analytical centre of Expert Ukraine) divided all the companies into Groups A, B and C. Not one company made it into Group B. Group A (Table 5) comprises the most transparent ICs. In addition to them, we analysed the data of another 35 companies, twenty-seven of which we included in our stability rating. However, in the process of data analysis we established that twelve out of these 27 companies hardly conducted any operations and four had a zero gross income. Companies with revenues below \$0.02m in 2005 were not included in the rating. Nevertheless, we included these companies in the rating table, as some of them began to show signs of life in the first half of 2006. Therefore, the second part of the Group C rating table (Table 6) represents the market benchwarmers who are ready to rush headlong into battle on the first order of their shareholders.

The technique used to calculate the integral stability indicator for life insurance companies is similar to the one used for the stability rating

calculations of the companies which offer general types of insurance. The aforementioned directive by the State Commission for Regulation of Financial Services Markets of Ukraine determines the calculation of the integral indicator on the basis of nine coefficients (the calculation of the rate of insurance and the net actuarial reserves/equity ratio partially lose their significance).

For Group A, we replicated the calculation specified by the regulator's assessment technique with a minor induced correction: companies' indicators were adjusted to their net equity. The resulting intermediate integral indicator was further adjusted to premium coefficients: companies received premiums (of zero to ten per cent) for the transparency of information disclosure, the number of insurers, the concentration of insurance payments, and the level of client acquisition costs. Premium coefficients were calculated on the basis of the additional indicators, provided by the companies in their questionnaires. Resulting coefficients were then compared to Group A mean values.

■ Vitaly Shapran

It will be difficult for Ukrainian insurers to compete with foreigners who invest millions of dollars into their companies' development. Additionally, they are acclaimed specialists in accumulative insurance and can use their authority — together with their parent companies' holdings — to guarantee the safety of their insureds' assets. In the accumulative insurance niche, a strong connection between Ukrainian insurers and the banking system is detrimental for the former as it increases their dependency on the bank deposits' yield, ascertaining that the companies' conditions for the allocation of funds will remain less attractive than the banks' offers. This problem will remain unresolved until the Ukrainian mortgage market gets off to a proper start and the insurers finally get a chance to work with the market issues of hypothecation certificates, mortgages, etc. Another prospective direction is the development of the consumer credit leveraged by life insurance policy. However, it is still too early to lift the restrictions on life insurance companies' reserve management — Ukrainians have not yet forgotten the mass-scale bankruptcy of national companies in 1994–1995.

■ A full version of the article is available on www.expertua.com