MOODY'S
INVESTORS SERVICE

Credit Opinion: KazExportGarant

Global Credit Research - 25 Aug 2011

Almaty, Kazakhstan

Ratings

Category	Moody's Rating
Rating Outlook	STA
Insurance Financial Strength	Baa2

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Key Indicators

KazExportGarant[1][2]

	2010	2009	2008	2007	2006
Total Assets (KZT Mil.)	12,850	9,630	9,383	9,073	8,460
Shareholders' Equity (KZT Mil.)	11,130	9,182	7,902	8,675	8,257
Net Income (KZT Mil.)	839	609	267	388	222
Gross Premiums Written (KZT Mil.)	406	458	255	263	212
Net Premiums Written (KZT Mil.)	296	286	236	240	132
High Risk Assets % Shareholders' Equity	58.8%	40.2%	49.9%	20.3%	8.8%
Reinsurance Recoverables % Shareholders' Equity	0.4%	1.3%	0.2%	0.2%	0.0%
Goodwill & Intangibles % Shareholders' Equity	0.0%	0.0%	0.0%	0.0%	0.1%
Gross Underwriting Leverage	0.0x	0.1x	0.0x	0.0x	0.0x
Return on Capital (1 yr.)	8.3%	7.1%	3.2%	4.6%	2.6%
Sharpe Ratio of ROC (5 yr.)	210.2%	205.6%	265.6%	---	---
Adv/(Fav) Dev. % Beg. Reserves (1 yr.)	8.2%	-20.3%	-32.4%	N/A	N/A
Adjusted Financial Leverage	0.7%	0.9%	1.0%	0.9%	3.6%
Total Leverage	0.7%	0.9%	1.0%	0.9%	3.6%
Earnings Coverage (1 yr.)	185.7x	144.0x	62.3x	87.5x	14.4x

[1] Information based on IFRS financial statements [2] 1 US$ = 145 KZT as at 31 Dec 2010

Opinion

SUMMARY RATING RATIONALE

KazExportGarant's Baa2 insurance financial strength rating (IFSR) reflects its very strong capitalisation, significant investments in Government debt and ownership by the Republic of Kazakhstan. In Moody's view, KazExportGarant is well positioned to tap into the profitable Kazakh reinsurance market by exploiting its strong capital base. The company is expected to achieve a level of profitability commensurate with its current rating through a combination of strong underwriting performance in reinsurance and a circumspect investment policy. Nevertheless, total premiums, both from export credit insurance and inward reinsurance, may remain low as a percentage of KazExportGarant's shareholders equity over the medium term.

At the same time, KazExportGarant has yet to demonstrate a track record of profitability and sound risk management. The current rating is predicated on a substantial enhancement of KazExportGarant's risk management systems and processes as the company's exposure increases. In addition, Moody's expects that the Republic of Kazakhstan will not withdraw substantial amounts of capital from the company as the exceptionally strong capitalisation is one of the key factors supporting the rating at its current level.

In accordance with Moody's GRI (Government Related Issuer) rating methodology, the rating of KazExportGarant reflects a combination of the following inputs: (i) Baseline credit assessment of 9 (on a scale of 1 to 21, where 1 represents the lowest credit risk), (ii) very high dependence (90%), reflecting the company's operating and financial proximity to the government and (iii) strong support (51-70%), reflecting the importance of KazExportGarant in its capacity as Export Credit Agency, offset by its reinsurance activities, business associated with more limited support from the government.

Credit Strengths

- Very strong capitalisation relative to current and prospective premiums written

- Investment policy focused on Kazakh government bonds, although KazExportGarant is increasingly investing in other asset classes

- 100% ownership by the Republic of Kazakhstan

- Well positioned to become a significant player in the profitable Kazakh reinsurance market

Credit Challenges

- The company has yet to prove it has a sustainable business model

- Profitability in export credit insurance and possibly inward reinsurance may be challenging to achieve

- The Kazakh reinsurance market can be expected to become increasingly competitive over time

- Comprehensive retrocession programme has yet to be put in place

- Overall profitability will be predicated on the company's ability to attain a high degree of underwriting acumen and sophisticated risk management

- KazExportGarant may accumulate a sizeable commercial credit and political risk exposure to the main trading partners of Kazakhstan, such as China, Russia, Iran and Central Asian countries

Recent Events

On 28th May 2010 the outlook on the rating was amended to Stable from Negative following a similar action on the Government of Kazakhstan.

Rating Outlook

The outlook is stable in line with the outlook on the Government of Kazakhstan.

What Could Change the Rating - Up

- Upgrade in the rating of the Republic of Kazakhstan

What Could Change the Rating - Down

- Decision of the Republic of Kazakhstan to withdraw capital from the company

- Substantial changes in the ownership structure

- Refocusing of the asset allocation strategy from Kazakh government bonds to more risky instruments

- Unsatisfactory underwriting performance, with a net loss at the underwriting level

Recent Results

In 2010, KazExportGarant reported Gross Premiums Written of KZT 406 million and net income of KZT 839 million, compared to KZT 458 million and KZT 609 million in 2009. Shareholders' equity was KZT 11,130 million as at 31 December 2010.

DETAILED RATING CONSIDERATIONS

KazExportGarant is a niche player in the Kazakh insurance market, focusing primarily on insurance of export credit and investment by Kazakh companies abroad. Premium volumes in this line are expected to remain low in the next few years as the majority of exporters prefer to retain credit risk. In 2009, the company reported GPW of KZT 70.5 million in this segment (versus KZT 33.9 million in 2008), and management expects that this figure will progressively increase.

The company also writes inward reinsurance, with 2010 reported GPW of KZT 307 million. In the last three years, property lines accounted for most of the reinsurance book, overtaking liability lines and is expected to play a greater role going forward, thanks to the growth of the Kazakh insurance market. By becoming an active player in the reinsurance market, the company is seeking to diversify its premium mix and enhance its earnings. However, the small size of the portfolio, as well as limited geographic diversification outside Kazakhstan, does not enable KazExportGarant to fully benefit from diversification effects.

In export credit insurance, KazExportGarant may accumulate a commercial credit and political risk exposure to China, Russia, Iran and Central Asian states (the main trading partners of Kazakhstan). Also, pricing in this line of business may be less than fully adequate.

KazExportGarant's investment policy is relatively conservative. As of 31 December 2010, 48% of invested assets were invested in Kazakh government bonds (Baa2 stable outlook). However, KazExportGarant has a long-term increasing exposure to Kazakh bank deposits and corporate bonds which in 2010 comprised 43% of investments. The portfolio is exposed to concentration risk. A default by the Kazakh government would almost certainly result in default by KazExportGarant. Another potential concern in the longer term is currency mismatch as some losses from the inward reinsurance business may be denominated in roubles or US dollars.

KazExportGarant's capitalisation is outstanding with a de minimis level of underwriting leverage (gross premiums written plus loss reserves divided by equity). This level of capital is fully adequate to sustain the prospective growth of the company. We do not expect that the Republic of Kazakhstan, sole shareholder of the company, will withdraw substantial amounts of capital from the company.

It is too early to make a definitive judgement about the profitability of the insurance activities, as KazExportGarant's business book is small and volatile. So far, the main revenue generator has been the investment income which reached KZT 643 million in 2010. While underwriting profitability has been historically modest, it should also be borne in mind that so is the level of exposure. Return on capital was 8.3% in 2010 compared to 7.1% in 2009.

KazExportGarant's carried reserves as of 31 December 2010 were KZT 99 million in comparison to total equity of KZT 11,130 million. The IBNR reserve was calculated on the basis of the directive of the National Bank of Kazakhstan at 10% of net written premiums. As of 31 December 2010, average reserve development for the last three years was a reserve release of 8.1% as per Moody's calculation (reserve strengthening/(releases) % beginning reserves). However, we note that the reserve development has been volatile.

KazExportGarant has no debt on its balance sheet. According to Kazakh law, insurance companies are not allowed to issue fixed-income securities, preference shares or similar instruments. Bank loans may not exceed 10% of shareholders' equity and must be repaid within three months. It is therefore unlikely that KazExportGarant will issue any debt in the foreseeable future, unless amendments to the law are introduced.

Other Considerations

In Moody's view, ownership by, and close association with, the Kazakh government is a strong credit positive for the company. KazExportGarant has been mandated by Kazakh government to assist in reaching certain national development goals, and its performance will be evaluated by the authorities based on criteria other than profitability. We therefore expect that the single most important driver of KazExportGarant's rating going forward will be the debt rating of the Republic of Kazakhstan.

Moody's continues to monitor support provided to KazExportGarant and other Kazakhstan GRIs by the Republic of Kazakhstan due to the uncertainty about the authorities' support for banks as well as several government-related institutions. At present the BCA of KazExportGarant is in line with the published rating, so reductions in support assumptions would not have an immediate impact