

Eurasia

Taking risks and reaping the profits

Kazakhstan's insurance market is new territory and business is booming. Now the country's leading insurer is predicting earnings of \$500 million in the next five years.

On April 27 and 28 the Eurasia Insurance Company, Kazakhstan's leading company in the sector, will host a conference on the subject of risk management in Almaty, the country's booming business and financial center.

It is a subject of particular importance to the 500 top businesses who have been invited to attend. Because 90 percent of Kazakhstan businesses have no insurance against natural disasters – despite the fact that Almaty is situated in an earthquake-prone zone.

“The reason for this lack of coverage is not because it is unobtainable, but simply because the people of Kazakhstan are not used to buying insurance,” says Dr. Boris Umanov, the president of Eurasia. “Yet real estate in the city is more expensive than it is in Beverly Hills.”

He says that because of soaring real estate prices, a three-bedroom detached house in Almaty is now valued at \$1.5 million, whereas a similar one in Los Angeles might cost \$700,000.

Kazakhstan's wealth of oil and gas resources has enabled its economy to grow by 75 percent in the past seven years, making it the most economically successful of the former Soviet Union states. This, in turn, has sparked the surge in the value of real estate, but the insurance sector's market penetration is still estimated to be less than 1 percent.

Dr. Umanov says that when the country was part of the Soviet Union, there was no history of insurance, no literature or data on the subject and no specialists in the field. During that time he was a physicist specializing in mathematical statistics.

In the 1990s, however, he worked with several international insurance brokers and underwriters before establishing the Eurasia Insurance Company in 1995. It began with a staff of three and capital of only \$200,000. Today it has assets of more than \$120 million.

“We built up our assets by earning them, not by attracting new capital,” says Dr. Umanov. “We never made a rights issue. We never asked our shareholders to give us additional money.”

Insurance was a new concept in Kazakhstan. At one time there were 200

The modern architecture of Astana, Kazakhstan's capital, is reflective of the country's growing economy.

insurance companies but many fell by the wayside and today there are only 36. "Per capita insurance is still less than \$34 in Kazakhstan and the art of risk management is almost unknown," says Dr. Umanov.

Risk has been described as a measure of the possibility of deviation from the expected, and risk management as a discipline for dealing with uncertainty. It has a long history. When farmers began letting land lie fallow once every seven years and shippers began dividing their goods between several vessels to reduce the risk of total loss from shipwreck or pirates, they were early practitioners of risk management. Under communism, however, it was a lost art.

"Maybe some Kazakhstan banks have a risk management department, but none of the power plants, mining companies, oil refineries, shipping companies or other big companies have one," says Dr. Umanov.

In the past, he says, the scarcity of risk management departments could have been due to lack of money, but now that Kazakhstan's oil wealth is being realized, it is being ascribed to a lack of awareness.

Eurasia Insurance is the only Kazakhstan company that has an enterprise risk management department. "Risk management is integrated into all our business processes. We have a controlled risk-taking environment," says Dr. Umanov.

Kazakh people are receptive to the concept of insurance, but there is a lack of knowledge – hence Eurasia Insurance Company's April conference, which will be addressed by leading international experts.

This central Asian state is the world's ninth-largest country in land mass, with a population of only 15 million. It has prodigious oil, gas and mineral resources and is developing at a rapid pace.

For the moment, the extent of Kazakh companies' insurance coverage may be slight, but its rate of growth is relatively fast. The aggregate gross premium written by Kazakh insurers in 2000 was \$63 million. In 2004 it rose to \$307 million and last year it increased to \$501 million.

"People are becoming more confident in insurance companies," says Nazym Tulchinsky, the deputy chairman of



Dr. Boris Umanov, president of Eurasia

Eurasia. "People now are not asking: 'Should I have insurance?' They are asking: 'How do I have to be insured?'"

Yet, as the capitalization of the country's insurance companies has increased, their number has decreased. "As insurance is an activity concerned with the concentration of funds which determine the financial strength of the company, the best principle is 'the fewer the better,'" says Mr. Tulchinsky. "It is better if there are only ten insurance companies. These will be big insurers with huge capitalization that can meet their obligations in full."

Opponents of such an approach contend that a reduction in the number of insurance companies in the marketplace leads to less competition and an increase in tariffs. But, says Tulchinsky, insurance rates are not the subjective assessment of risk, but a mathematical, calculable value. Dumping on the market can lead a company to insolvency and one case of bankruptcy would undermine people's confidence.

Of Kazakhstan's 36 companies, Eurasia is by far the largest with 85 percent of the market profit. It recorded a profit last year of \$27 million.

The company's strength is reflected in terms of its risk retention.

Under Kazakhstan's insurance regulations, a company's obligations may not exceed 10 percent of the sum of its equity capital and insurance reserves.

"Eurasia's retention is now \$11 million, which is ten times more than that of an average insurance company in Kazakhstan," says Dr. Umanov. "Most small insurance companies here have to arrange extensive reinsurance from the West. Sometimes this is impossible because even big insurance companies in Switzerland, Britain or the United States know little about conditions in Kazakhstan and decline to take the risk.

"But Eurasia's retention rate is huge enough to insure all our obligations to all our clients. It helps us fill a gap between small local insurers and the international market.

"We feel pretty strong now because we operate not just in Kazakhstan but in Russia, Ukraine, South Korea, Turkey, Argentina and the Czech Republic. We know how to diversify our risk and how to concentrate on different lines of business," he says.

The company's four main areas of business are property, cargo, employers' liability and general third-party liability.

The Kazakh insurance industry is strictly regulated by the Financial Supervision Agency of Kazakhstan (FSA), which has established an effective set of regulations. A tariff system is in place whereby the minimum and maximum rates of premium are approved by the FSA for particular classes of insurance. This has facilitated the financial stability and solvency of the country's insurance companies and steady growth in the sector.

"We have a plan to increase our opportunities and our assets in the years ahead. We are going to make about \$500 million in the next four or five years and become the regional market leader," says Dr. Umanov. ♦

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Competition welcomed

What Kazakhstan's insurance industry learned from Hurricane Katrina

Hurricane Katrina and its aftermath dominated lunchtime discussions in the insurance companies of Kazakhstan just as much as it did in the U.S.

There were two reasons for this, says Dr. Boris Umanov, the president of the Eurasia Insurance Company, Kazakhstan's largest insurer: first, because Almaty, the country's business and finance center, is situated in an earthquake-prone location and, second, because the wording of some insurance policies held by businesses and homeowners in New Orleans raised questions of whether claims would be met.

"Sometimes damage occurs that is not covered by insurance policies," says Dr. Umanov. "This was the situation with Hurricane Katrina. The damage was caused by many reasons, including not only storm and winds, but also floods.

But some clients had not bought the coverage for flood risks. Hurricane Katrina triggered the discussion of the wording of insurance coverage. It is virtually impossible to distinguish damage caused by storm surge and rising tides from flood waters. This means that, strictly speaking, some insurers were not liable to pay out on such claims.

"However, I believe that there was some pressure on the international insurance companies to do so, not from a legal standpoint but from a political one, regardless of this uncertainty.

"This situation closely resembled the old Soviet way of doing things – when the communist system applied similar pressures. That was why Katrina was of such interest in insurance circles in Kazakhstan.

"I believe that in such cases if something has not been insured correctly there should be no obligation to pay. If payment is to be made, it should be made clearly as an *ex-gratia* gift, not as a legal duty."

Dr. Umanov is also critical of the requirement by the U.S. for every European insurer to deposit money in U.S. banks as collateral if they wish to reinsure American risks. "This is inappro-

priate because the Kazakhstan regulator doesn't require American insurers to put collateral against risks they underwrite for cedents here in Kazakhstan.

"Globalization has led Kazakhstan to become closer to the West. Everyone here can browse the Internet and read the international newspapers, but we look at the U.S. insurance industry with some confusion. For instance, the U.S. does not permit European reinsurers to enter the American market with the

Dr. Umanov would welcome American participation in Kazakhstan's insurance industry.

same conditions applied to their American counterparts. Every country protects its own market, but how can we join the World Trade Organization while also protecting our own economy?"

In spite of these arguments, Dr. Umanov would welcome American participation in Kazakhstan's insurance industry. "For the Eurasia Insurance Company it is very important to publicize Kazakhstan's new image and to welcome foreign competition," he says. ♦

Bright prospects

Legislation means that the insurance market can only grow stronger

Only 15 million people live in Kazakhstan, which is almost four times the size of Texas, so the Eurasia Insurance Company's main clients tend to be the oil and construction companies that are creating the state's ever increasing infrastructure. But the individual client base is growing.

"The market is very small, but every year the government is introducing new kinds of compulsory insurance legislation," says Dr. Boris Umanov, the company president.

"Last year it was compulsory employers' liability for damage to the life and health of an employee while at work. For the first two months we had 1,200 new clients. There was a line outside my

office and we worked 12 hours a day, for seven days a week.

"Although we have a relatively small population in a huge country, I see the future as a bright one for us," says Dr. Umanov. "We are finding new clients throughout Eastern Europe and Asia and, of course, in our neighboring countries because they have similar mentalities.

"The market is very small, but every year the government is introducing new kinds of compulsory insurance legislation."

Dr. Boris Umanov, president of Eurasia

"We have new clients now from Siberia, the Moscow region, Belorussia, Uzbekistan and Kyrgyzstan. We can see the entire Eurasian region as our original homeland, as our original working area."

Dr. Umanov says Eurasia Insurance's key qualities are the speed with which it accesses data and makes decisions, and its prompt payment of valid claims. "We have created a highly cost-efficient prod-

uct distribution system that gives us a competitive advantage. We have clear and strong control over the distribution system.

"Eurasia's products are tailor-made to each client's requests and requirements," he says. "We make decisions on a case-by-case basis. We analyze the past and project the future. We use sophisticated actuarial and statistical tools to calculate risks, not only correctly, but also quickly. Then we use our database to determine which risks are the most profitable and allocate Eurasia's capital accordingly."

Dr. Umanov says this requires good underwriting skills to make the premium perfectly correlated to the risk assumed. "Of course, that means we have comparatively higher expense structures, but the loss experience is better than that of our competitors.

"We are selective about which risks we are going to insure," he says. "Profitability is more important to us than volume. These policies have enabled us to be the most profitable insurer in the market for the last four consecutive years." ♦



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