



All of last year, Russian insurers eyed their Ukrainian colleagues with envy: a massive sell-off of insurance and banking assets was taking place in Ukraine. Against this background, the situation in Russia seemed at a deadlock. Western managers, responsible for expansion into Russia, lamented in private conversations that “the Russians want too much” for their companies and that the home office could not clearly determine its strategy. This was fuelled by the wild statements of local top managers, whose market speculating drove value estimates of Russian insurers ever higher and higher.

Then came the breakthrough: acquisition after acquisition on the Russian market. Not one of the market experts could have predicted this outcome.

# Gift — or Trojan

In their expansion plans, international players do not proceed from specific market conditions, but from global strategy dictated by shareholders. In itself, therefore, the massive buyout of top Russian insurance companies by foreigners is not something extraordinary. In the view of world experts, pure and simple, the time had come for insurance investment in Russia, all the more, since it was the only country left in the BRIC zone (Brazil-Russia-India-China) that yet had not had much foreign investment. The Ukrainian acquisitions came to seem a preparatory warming up before the main performance.

It then becomes clear, why this buying spree of Russian companies with developed networks. Primarily, it is to gain, in medium-term perspective, a strong position on the growing market, potentially

locking up tens of millions of clients. And, of course, at minimal expense.

Instant appraisals of the true market value of insurers are therefore not applicable to the ongoing race in the Russian market. All recent discussions in the press and among experts, on whether Allianz overpaid for ROSNO or not, or how much NASTA costs, are per se pointless.

Strategic investors are reserving places in the market in 2010 to 2012, anticipating its future growth and the consequent decline in the number of serious competitors – partly through mergers. An investor also assesses the business risks – for Russia, these are primarily political. The final price offered for an available insurer is the sum of all these calculations, appraisals and estimates multiplied by the competition: in a

global endurance race, one cannot let competitors get too far, or one may never catch up.

This approach definitely affects pricing: companies with the potential for rapid growth in market share have much higher value. The most visible sign of this is an insurer’s position in the region in terms of quantity and quality of operations: its level of premium written and the portfolio structure.

## Clusters and Networks

There are quite a few interesting peculiarities here. Russian companies differ much in penetration even within territories where they are represented. Moreover, the quality of management also varies greatly across the companies.

Shown in Graph 1 is the distribution of Russian insurers by number of regions served, and by average premium levels achieved

# Insurance

per region. The data clearly falls into three large market clusters, with sharply different indicators. The first represents companies with average premium per region of RUB80 million (EUR2.3 million) or more. This group includes the players with largest networks,

totalling 30 companies in all. Characteristically, even among these companies, the average premium indicator is highly variable – from RUB164 million (EUR4.8 million) per region for companies operating in 80 of the Russian federal subjects to less than half that – RUB79

million (below EUR2.3 million) for companies represented in only 61-70 regions.

The second cluster is wider (139 companies), consisting of insurers established in 11-60 regions. These are characterised by significantly lower average premium per re-

## Kings of the Hill

1. Rosgosstrakh entered deals with Kapital Insurance in Ukraine, where it acquired the latter's company, now renamed Providna, and in Russia – under an agreement on strategic cooperation with the aim of purchase. Although the Federal Antimonopoly Service (FAS) stopped this agreement as a violation of antitrust law, it did not stop the companies' relations. Insiders moreover confirm that Russky Mir should be put in this group, as well. Mutually complementary portfolios (mass lines of Rosgosstrakh and the rapidly growing corporate business of Kapital Insurance) give this group the best chance of taking the lead position.

2. Moscow Insurance Company (MSK) creates the Metropolitan Insurance Group. The company acquired Standard-

Reserve, then Moscow Re, and also set up a subsidiary MSK-Life, jointly with Vienna Insurance Group. Since the shareholders are Bank of Moscow and Moscow City Government, this group is very solid and, with one or two more acquisitions, will be able to compete for leading ranks.

3. Allianz, through its new division Allianz New Europe, gains full control over ROSNO and its branches, sweeps into Moscow for a press-conference with its East European top management and boldly claims future leadership in Russia. Shortly after, Allianz also acquired Progress-Garant.

4. NASTA, announcing over the past year negotiations with strategic investors, was 66% bought by the Zurich Financial Services (Zurich). The deal greatly enhanced Zurich's position in retail,

previously insignificant. Should Zurich pursue this direction, it could become a major player.

5. Finally, one of the co-owners of Ingosstrakh, Alexander Mamut, according to the media, sold his interest (about 40%) to a party affiliated with Petr Kellner, majority owner of Ceska Pojistovna, one of the major CEE insurers. Although representatives on all sides deny the imminent merger, media sources insist the deal has already taken place and predict forthcoming sale of Oleg Deripaska's stake in Ingosstrakh as well (about 60%). The most intriguing part of the story is that Ceska Pojistovna itself formed a CEE joint venture with Italian insurance giant, Generali. With its already strong position in Ukraine, Generali grows stronger in Russia and in Eastern Europe as a whole.



## Star Wannabes

1. AIG has been long present in Russia, like in many countries of the former USSR. Until recently, AIG's life branch was considered the model for Russian life insurance operation, whereas its non-life carrier AIG Insurance and Reinsurance was less prominent. Several years ago, AIG was considering purchase of a Russian insurer – the media mentioned in this connection VSK, ROSNO and Ingosstrakh, but no acquisition took place. Possibly, the decline in activity was tied to the departure of Maurice Greenberg and subsequent personnel changes. Nevertheless, AIG should not be eliminated from future contention as a potential leader in the Russian market.

2. Ergo, a branch of Munich Re, is less active than the other German insurer, Allianz. Although Ergo is studying offers from shareholders of Russian insurers, it apparently inclines to organic growth in Russia. Currently it operates two companies in Russia – Ergo Rus (non-life) and Ergo Life. In the medium-term, the group may strengthen its position, but it has little chance of leading without acquiring a few major insurers.

3. After a long interval, ING has accomplished a very impressive entrance into the life market, announcing large-scale investments in partnership with the EBRD and International Finance Corporation (IFC). The group had already established a bank in Russia, without a strong retail network, though, and a pension fund. ING's role in Russia in the coming years will depend on the life market development and ING Life's position in it. Since ING does not operate in non-life, companies

of the group are unlikely to enter the leading ranks in Russia for the next decade. The group will possibly acquire banking, pension and asset management operations.

4. Fortis, a powerful European player in banking, asset management, bancassurance and life insurance, achieved perhaps the most unusual entry into the Russian insurance market. After setting up a joint asset-management company with KIT-Finance, Fortis opened a life subsidiary Fortis Life Insurance. The company announced its main sales channel will be the Internet. It's possible that Fortis, mostly focused on bancassurance, is just taking time to consider banking acquisitions. Limiting its strategy to life insurance, again, will prevent the company from becoming competitive in the Russian market on the whole.

5. Although the ACE group has both life and non-life insurance companies in Russia, and even a stake in the Russian Reinsurance Company (purchased in 2006), it apparently intends to grow organically along with the Russian market. At least, the company has not revealed any ambitious development plans, nor appeared negotiating acquisition of a major local insurer. ACE seems to be still studying the market.

6. Vienna Insurance Group is one of the most aggressive East European players, but is also relatively inactive in Russia. Possibly, the group is for the time being satisfied with its cooperation with Moscow Insurance Company and the Bank of Moscow, or it may intend to act through TBIH. But, character is destiny, and the group will surely enter the limelight in the Russian market.

gion - RUB20-30 million (around EUR580,000-870,000), and this indicator is marked by lower dispersion. Insurers in this cluster have rather sharp distinctions. Here we find long-time market players who, for some reasons, lost ground in the leader race, along with more aggressive newcomers who rode last years' wave of MTPL insurance and the surge of investors' interest.

Finally, the third cluster contains the main bulk of insurers (688 companies). They do not apparently have regional ambitions: regional representation is quite weak (from 1 to 10 regions). Possibly as a consequence of this, these insurers have a higher average premium per region. This group, among others, includes a number of specialised insurers having probably the best chances for success of all companies in this category.

Graph 2 takes into account the loss ratio: it follows that the larger a company's network, the better is its loss ratio. In this way, the list of most lucrative players nicely matches the listed arrangement of these with developed networks.

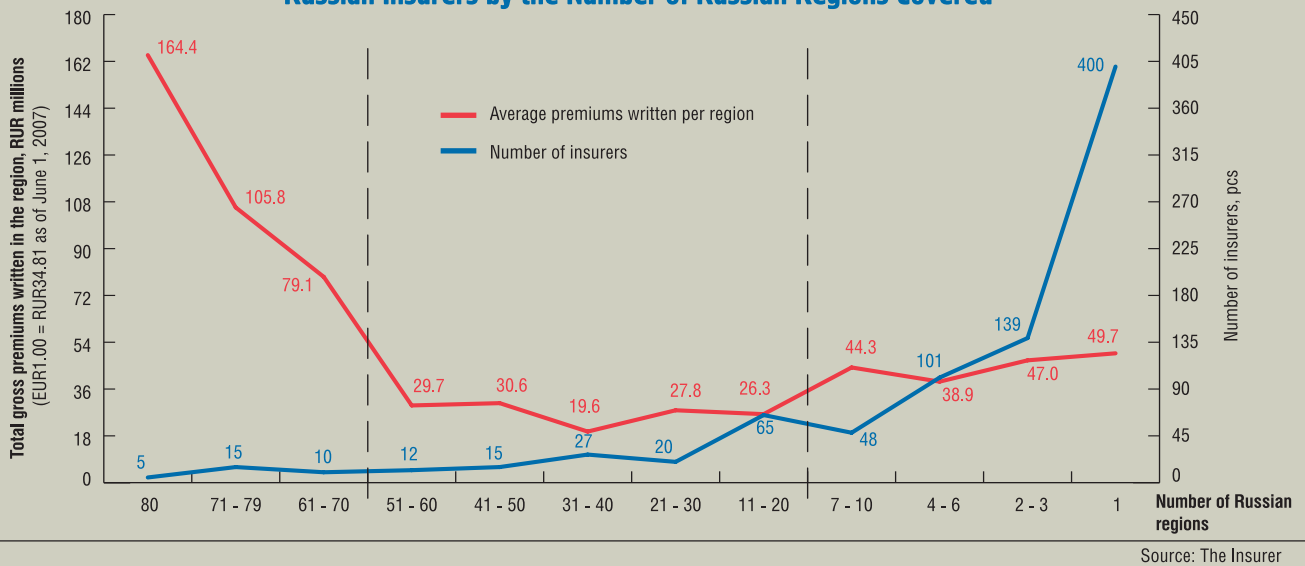
## Team Building

The recent deals and the influx of new players have strongly shifted the market's power structure (see insets). Some of the groups we mention below, however, have not been officially established. Some of the alliances represent our assumption, based on indirect information, and some may not come true. However, if we are judging correctly, the list of the strongest Russian market players will include the following companies. The best-positioned will apparently be the group Rosgosstrakh/Kapital Insurance/Russky

# Insurance

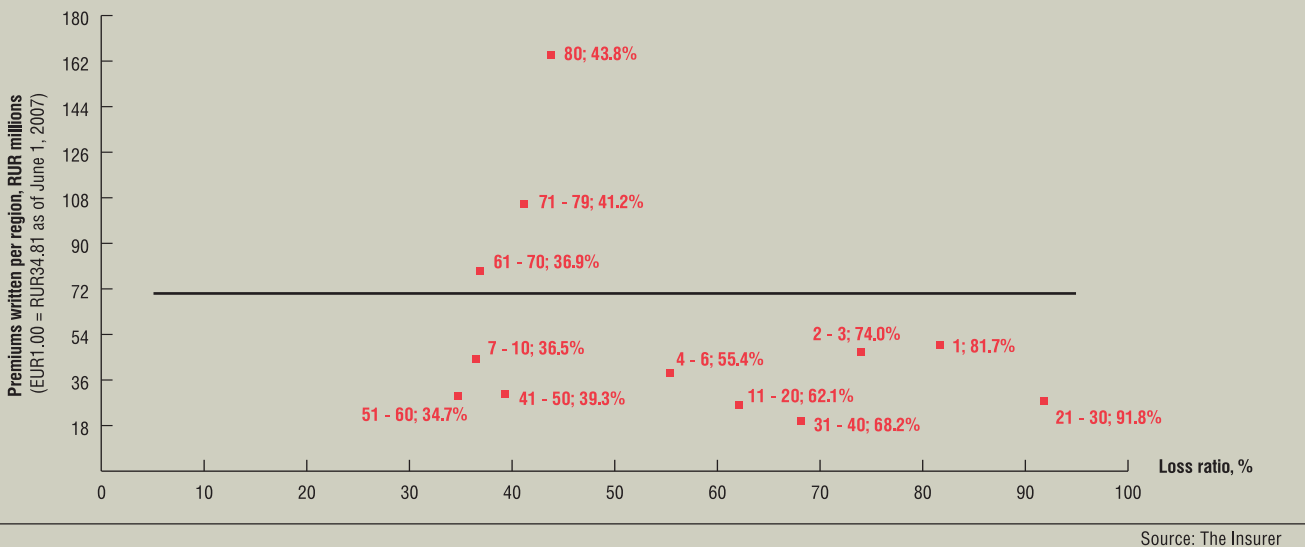
**Graph 1**

**Russian Insurers by the Number of Russian Regions Covered**



**Graph 2**

**Russian Insurers by the Number of Russian Regions Covered**



Mir. The Russian branch of Allianz also grows stronger. If the media is right in its reporting about negotiations of Ingosstrakh shareholders, another major league player will be Generali/Ceska Pojistovna/Ingosstrakh group. To date, none of the companies grouped around the

Bank of Moscow has yet announced its plans. If eventually they are joined by Vienna Insurance Group, they could become an impressive force, as well.

AIG seems more than a little cautious, after its earlier active interest in Russian companies. There is still,

however, more to be bought on the market, and the Americans may yet wake from their lethargy. The acquisition of NASTA has not yet made Zurich a leader in the Russian market, but the Swiss firm's appetite may grow over time. Still unclear is the strategy devised by the SOGAZ

## Tasty Morsels

1. The RESO group announced in late May it will launch an IPO. The first and very serious step was the sale of 10% of its member insurance company RESO Garantia to the European Bank for Reconstruction and Development (EBRD). There is every reason to believe that RESO Garantia has already gained attention of world insurance and financial holdings interested in Russia. If this asset falls into the hands of one of the current contenders, it would strongly tilt the scales to its benefit.

2. AlfaStrakhovanie recently began an internal restructuring clearly directed at increasing its investment appeal. The first step in this redesign was offering the

post of president to former vice-governor, Mikhail Bershadsky. The group, comprising a life and a non-life companies, is hardly capable of becoming a leader but will, no doubt, enhance an investor in the local market.

3. VSK Insurance House is another choice morsel among Russian insurance assets. The appointment of Sergey Almazov as CEO and Sergey Tsikalyuk as chairman of the board is also a sign of looming investors. The company is not badly constructed and, doubtless, a rather attractive asset for acquisition.

4. Soglassye is constantly increasing market share in its portfolio, trying to shake free of its captive past. This insurer is also drawing great interest from strate-

gic investors. Like AlfaStrakhovanie and VSK, Soglassye has little hope of becoming a market leader, but would strengthen any foreign insurer.

5. Experts connect the market position of MAKS with the influential official, minister of health Mikhail Zurabov. Although Zurabov's position has not looked stable lately, MAKS would also give an investor a sizeable share of the market.

6. A group of companies remains on display, but does little to attract investors. This is the National Insurance Group, Spasskiye Vorota, Zenit, Energogrant, Oranta, Yugoria, UralSib, Severnaya Kazna and Rossia. None of these companies is a sure pick in the leader competition, but a tangible asset.

group, but, with its financial and administrative potential, it could become a powerful player.

The second echelon includes Ergo, ING, Fortis, Ace, If, Uniqa, et al., and the number of acquisition targets (see inset Tasty Morsels) is lesser. As already mentioned, the fundamental quality assets among Russian insurers are the companies with major networks. Beyond these,

some captive and specialised companies may engender certain interest. Then, a number of insurers with networks averaging 20-40 branches could possibly also attract investors. The rest will most likely have to huddle in municipal/niche insurance lines or serve an HR nursery for larger companies – which will further ratchet up pressure on the regions.

Assessing insurers' value is becoming a popular trend, using a primitive formula based on a company's annual sales – an obvious sign of the all-out buying and selling spree. Rough estimates under this overly simplified approach show the total dollar value of the Russian market, after deducting for companies already in foreign ownership, amounted to US\$11-16.7

## On the Outside Looking In

1. AXA, one of the largest French insurers, has not as yet shown any interest in the Russian market. It has a small stake in insurer Rossia, remaining through Rossia's ownership changes rather as a symbolical evidence of AXA's presence in Russia. However, as the example of Generali has shown, the situation can shift drastically, should AXA start to see lucrative prospects in Russia. It is possible that the group will simply wait to see the develop-

ment results of French banks in Russia, especially since it is one of the major bancassurance players.

2. Metlife, one of the largest US life insurers, on the other hand, is openly interested in Russia. This interest, however, has not yet driven the company to decide upon entry into the Russian market. Even if it does enter, it will confine operations to the life insurance segment.

3. If, one of the largest Scandinavian insurers, has also been eyeing Russia

for a long time and has even opened a rep office. Its interest is focused on the Northwestern region, however, where the majority of Finnish and Swedish companies are operating.

4. Uniqa, another Austria-based insurer, is not as widely expanding as the Vienna Insurance Group. It has an obvious advantage in Russia – its affiliation with Raiffeisenbank. If Uniqa buys a company in Russia, it has the potential to rapidly grow premium volume through bancassurance.

# Insurance

## Rich Dad, Rich Kid

1. SOGAZ, a largest captive group with definite ambitions in the corporate sector, is most likely to remain a corporate insurer in the medium term. The group has a clear administrative resource, which Russian insurers are hardly able to counter. However, an aggressive appearance of a foreign large-scale insurer in the corporate market could threaten SOGAZ's position.

2. ZHASO (Railroad Joint-Stock Insurance Company) is the latest-appeared captive insurer. However, if the group succeeds in consolidation of all insurance assets along the railroads, it will start to look impressive. Moreover, due to the focus of its monopoly, ZHASO is

much closer to mass clientele than the oil, gas or metallurgical insurers. And, that is also a significant resource.

3. Sheksna group is strengthened by its client, steel mill Severstal with its branches. In all probability, if the group fails to expand its federal network, it may await the same fate as the insurer Leader. The latter, once a very attractive access to insurance of assets of RAO UES of Russia (Unified Energy Systems), lost appeal as soon as insurance modification at RAO UES left the company virtually without business.

4. The position of Surgutneftegaz, an oil captive insurer, is very similar to medium-term goals of Sheksna.

billion in 2006. The major companies with developed networks contributed the largest share of this price – US\$8.4-12 billion. In this valuation model, the price-tag of the Rosgosstrakh/Kapital Insurance/Russky Mir group amounted to US\$3.4-4.5 billion.

All of the estimates, of course, are far removed from precise evaluation in specific transactions. They are merely to show that the general level of financial resources needed to purchase key market players is not really very high. The appearance of two or three resolved players might deeply change the outline of market forces, especially if such a player joins efforts with one of the market leaders.

**Vadim Demchenko**

