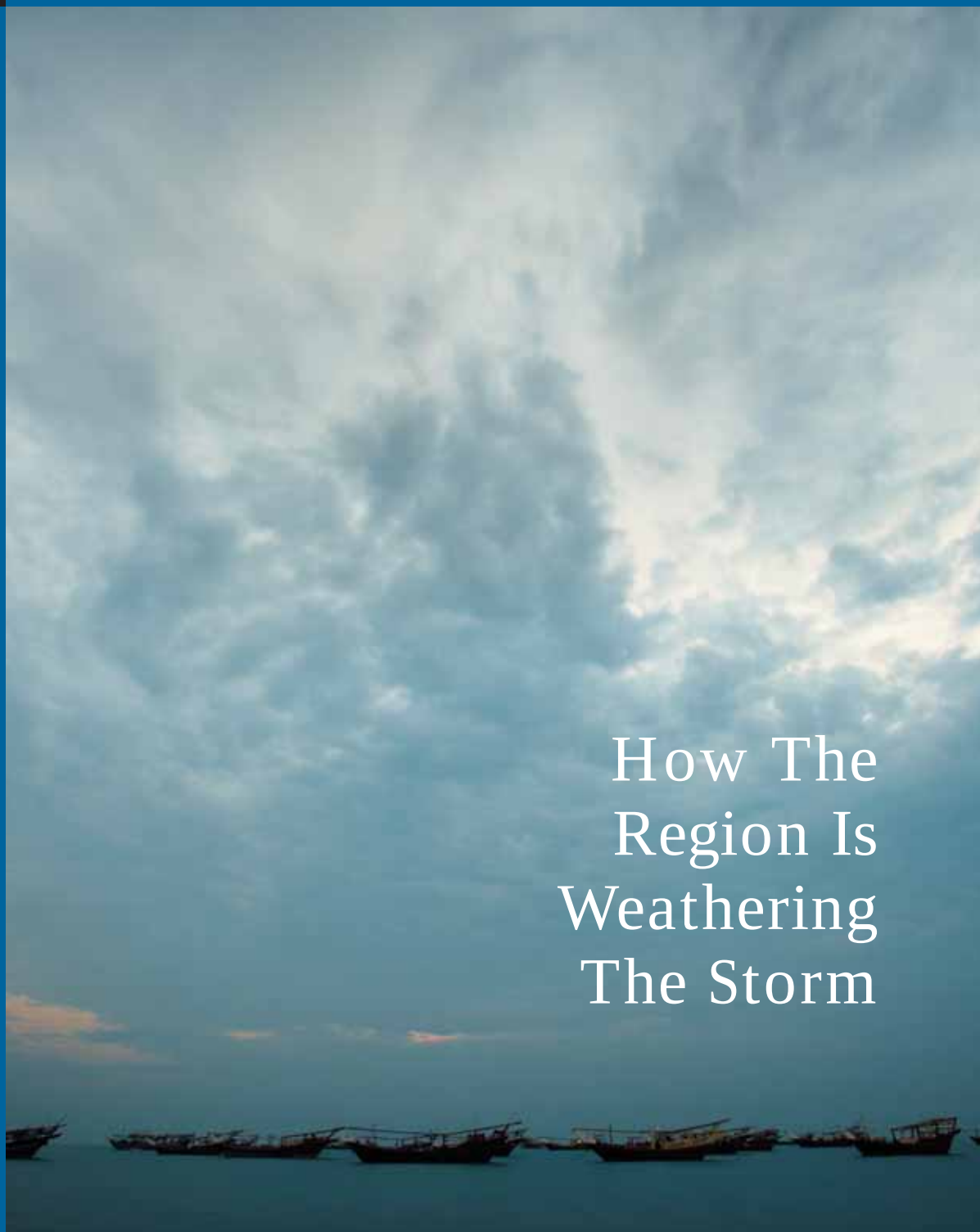
STANDARD &POOR'S

Gulf Cooperation Council Credit Survey



How The Region Is Weathering The Storm

June 2009



INTRODUCTION

STANDARD & POOR'S IS PLEASED to present its fourth Gulf Cooperation Council credit survey, which showcases our wide analytical coverage in the region.

The recent turbulence in global capital markets has affected the Gulf significantly, and in 2009 we expect the challenging credit environment to continue. Although the regional bond and loan markets came to a virtual standstill in the second half of 2008, successful rated sovereign bond issuance from the State of Qatar and the Emirate of Abu Dhabi provided a glimmer of hope in early 2009.

Despite the weak credit markets, our ratings universe has continued to grow. The larger telecom entities in the region—Saudi Telecom, Etisalat, and Qatar Telecom—are now rated. In addition, the Abu Dhabi-based commercial government entity Mubadala Development Co. PJSC obtained a rating as did the Tourism Development and Investment Co. of Abu Dhabi. We also added the sovereign rating on Ras al Khaimah and several new insurance ratings were assigned.

The challenging credit environment will continue to put pressure on some ratings and the number of ratings below 'BBB-' is increasing. Nevertheless, the efforts to develop deep, mature, and sophisticated capital markets require strong transparency, risk management, and corporate governance. We believe that, in developing the capital markets, ratings provide an important information tool for market participants. Through conference calls, dedicated events, and with ongoing improvements to our www.gcc.standardandpoors.com website we hope to contribute to improving information dissemination. Islamic finance is a sector that continues to grow in the region's capital markets. Our leading research on takaful and sukuk is presented in our third annual Islamic Finance credit survey, which can be downloaded from our website.

In 2009, the focus will be on credit fundamentals, default risk, and recovery. Our growing range of ratings, other information, and risk-management products will, we trust, help meet your information requirements. We hope you will find the material in this edition useful and we welcome inquiries from issuers or investors regarding Standard & Poor's and our ratings activity in the region. A list of key contacts appears at the back of the book.



JAN WILLEM PLANTAGIE
MANAGING DIRECTOR & REGIONAL MANAGER MIDDLE EAST
STANDARD & POOR'S

Cover: Fishing dhows under a stormy sky, just before sunrise.

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140 Qatar Insurance Co. S.A.Q.
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Entity	Foreign Currency Rating	Local Currency Rating
Abu Dhabi (Emirate of)	AA/Stable/A-1+	AA/Stable/A-1+
Bahrain (Kingdom of)	A/Stable/A-1	A/Stable/A-1
Kuwait (State of)	AA-/Stable/A-1+	AA-/Stable/A-1+
Oman (Sultanate of)	A/Stable/A-1	A/Stable/A-1
Qatar (State of)	AA-/Stable/A-1+	AA-/Stable/A-1+
Ras al Khaimah (Emirate of)	A/Stable/A-1	A/Stable/A-1
Saudi Arabia (Kingdom of)	AA-/Stable/A-1+	AA-/Stable/A-1+

Notes

**All ratings correct at May 19, 2009. For updated ratings information please see RatingsDirect.*



Financial Institutions

Entity	Issuer Credit Rating	Country
Abu Dhabi Commercial Bank	A/Stable/A-1	United Arab Emirates
Ahli United Bank B.S.C.	A-/Stable/A-2	Bahrain
Al Ahli Bank of Kuwait	BBB+/Watch Neg/A-2	Kuwait
Al Rajhi Bank	A/Stable/A-1	Saudi Arabia
Albaraka Banking Group (B.S.C)	BBB-/Stable/A-3	Bahrain
Arab Banking Corp. B.S.C.	BBB+/Stable/A-2	Bahrain
Arab National Bank	A/Stable/A-1	Saudi Arabia
Arcapita Bank B.S.C.	BB/Watch Neg/B	Bahrain
BankMuscat S.A.O.G.	BBB+/Stable/A-2	Oman
Banque Saudi Fransi	A/Stable/A-1	Saudi Arabia
BMI Bank B.S.C.	BBB-/Stable/A-3	Bahrain
Burgan Bank	BBB+/Watch Neg/A-2	Kuwait

Financial Institutions (cont.)

Entity	Issuer Credit Rating	Country
Commercial Bank of Kuwait	A-/Watch Neg/A-2	Kuwait
Commercial Bank of Qatar (The)	A-/Stable/A-2	Qatar
Doha Bank	A-/Stable/A-2	Qatar
Dubai Islamic Bank	A-/Watch Neg/A-2	United Arab Emirates
Emirates Bank International PJSC	A/Watch Neg/A-1	United Arab Emirates
Gulf Bank	A-/Watch Neg/A-2	Kuwait
Gulf Finance House	BBB-/Negative/A-3	Bahrain
Gulf International Bank B.S.C.	BBB+/Stable/A-2	Bahrain
Gulf Investment Corporation G.S.C.	BBB+/Watch Neg/A-2	Kuwait
International Banking Corp. (The)	SD/--/SD	Bahrain
Islamic Development Bank	AAA/Stable/A-1+	Saudi Arabia
Kuwait Finance House	A-/Watch Neg/A-2	Kuwait
Mashreqbank	A/Watch Neg/A-1	United Arab Emirates
National Bank of Abu Dhabi	A+/Stable/A-1	United Arab Emirates
National Bank of Dubai	A/Watch Neg/A-1	United Arab Emirates
National Bank of Kuwait S.A.K.	A+/Negative/A-1	Kuwait
National Commercial Bank (The)	A+/Stable/A-1	Saudi Arabia
Qatar National Bank	A+/Stable/A-1	Qatar
Riyad Bank	A+/Stable/A-1	Saudi Arabia
Samba Financial Group	A/Stable/A-1	Saudi Arabia
Saudi British Bank (The)	A/Stable/A-1	Saudi Arabia
Saudi Investment Bank (The)	A-/Stable/A-2	Saudi Arabia
Sharjah Islamic Bank	BBB/Stable/A-2	United Arab Emirates

Notes

**All ratings correct at May 19, 2009. For updated ratings information please see RatingsDirect.*



Insurance

Entity	Issuer Credit Rating	Country
Abu Dhabi National Insurance Co. (PSC)	A-/Stable/--	United Arab Emirates
Al-Ahleia Insurance Co. S.A.K.	BBB+/Negative/--	Kuwait
Al Buhaira National Insurance Co. (PSC)	BBB/Negative/--	United Arab Emirates
Arab Investment and Export Credit Guarantee Corporation (The)	AA-/Stable/--	Kuwait
Arab Orient Insurance Co. (PSC)	A/Watch Neg/--	United Arab Emirates
Bahrain Kuwait Insurance Co. BSC	BBB/Stable/--	Bahrain
Bahrain National Insurance Co. BSC	BBB+/Stable/--	Bahrain
Doha Insurance Co. Q.S.C.	BBB/Stable/--	Qatar
Dubai Islamic Insurance & Reinsurance Co. (Aman)	BBB/Negative/--	United Arab Emirates
Emirates Insurance Co. (PSC)	BBB+/Negative/--	United Arab Emirates
Gulf Insurance Co. K.S.C.	BBB+/Stable/--	Kuwait
Hannover ReTakaful B.S.C.	A/Stable/--	Bahrain
Kuwait Reinsurance Co. K.S.C.	BBB/Positive/--	Kuwait
National General Insurance Co. (PSC)	BBB/Stable/--	United Arab Emirates
Oman Insurance Co. (PSC)	A-/Watch Neg/--	United Arab Emirates
Oman United Insurance Co. S.A.O.G.	BBB/Stable/--	Oman
Qatar Insurance Co. International LLC	A/Stable/--	Qatar
Qatar Insurance Co. S.A.Q.	A/Stable/--	Qatar
Salama/Islamic Arab Insurance Co. (P.S.C.)	BBB+/Stable/--	United Arab Emirates
Saudi Re for Cooperative Reinsurance Co.	BBB+/Stable/--	Saudi Arabia
Takaful International Co. BSC	BBB/Stable/--	Bahrain
Takaful Re Ltd.	BBB/Stable/--	United Arab Emirates
Tawuniya/The Company for Cooperative Insurance	A/Negative/--	Saudi Arabia
Trust International Insurance & Reinsurance Co. B.S.C.(c) Trust Re	BBB/Positive/--	Bahrain
Wethaq Takaful Insurance Co. K.S.C. (Closed)	BBB-/Stable/--	Kuwait
Al Ain Ahlia Ins. Co. (Unsolicited Ratings)	BBBpi/--/--	United Arab Emirates
Al Dhafra Insurance Co. P.S.C. (Unsolicited Ratings)	BBBpi/--/--	United Arab Emirates
Al Khaleej Insurance & Reinsurance Co. Q.S.C. (Unsolicited Ratings)	BBBpi/--/--	Qatar
Al Sagr National Insurance Co. (Unsolicited Ratings)	BBBpi/--/--	United Arab Emirates
Kuwait Insurance Co. S.A.K. (Unsolicited Ratings)	BBpi/--/--	Kuwait
Qatar General Ins. & Reins. Co. S.A.Q. (Unsolicited Ratings)	BBBpi/--/--	Qatar
Ras Al-Khaimah National Ins Co. (Unsolicited Ratings)	BBBpi/--/--	United Arab Emirates
Warba Ins. Co. K.S.C. (Unsolicited Ratings)	BBBpi/--/--	Kuwait

Notes

**All ratings correct at May 19, 2009. pi—Public information. Unsolicited 'pi' ratings are based purely on public information. We may decide to add a company that has not requested an interactive rating to our unsolicited rating coverage if there is sufficient interest from brokers, insurance companies, and other subscribers to our ratings information.*



Project Finance/Utilities/Corporates

Entity	Issuer Credit Rating	Country
Abu Dhabi National Energy Company PJSC	AA-/Stable/A-1+	United Arab Emirates
Ajman Sewerage (Private) Co. Ltd.	BB(SPUR)/Watch Neg (bank loan)	United Arab Emirates
Aldar Properties PJSC	A-/Stable/A-2	United Arab Emirates
DIFC Investments LLC	A/Watch Neg/A-1	United Arab Emirates
DP World Ltd.	A/Watch Neg/A-1	United Arab Emirates
Dubai Holding Commercial Operations Group LLC	A/Watch Neg/--	United Arab Emirates
Dubai Multi Commodities Centre Authority	A-/Watch Neg/A-2	United Arab Emirates
Emaar Properties PJSC	BBB+/Watch Neg/--	United Arab Emirates
ETA Group	BB+/Negative/--	United Arab Emirates
Emirates Telecommunication Corp. (Etisalat)	A+/Stable/A-1	United Arab Emirates
International Petroleum Investment Company (IPIC)	AA/Stable/A-1+	United Arab Emirates
JAFZ Sukuk Ltd.	A/Watch Neg/A-1	United Arab Emirates
Jebel Ali Free Zone (FZE)	A/Watch Neg/A-1	United Arab Emirates
Kuwait Projects Co. (Holding) K.S.C.	BBB+/Stable/A-2	Kuwait
Mubadala Development Co. PJSC	AA/Stable/A-1+	United Arab Emirates
Nakilat Inc.	A+/Stable/--	Qatar
National Central Cooling Co. PJSC	BB/Developing/--	United Arab Emirates
Oman Power and Water Procurement Co. SAOC	A/Stable/--	Oman
Qatar Fertiliser Co. (S.A.Q.)	A+/Stable/--	Qatar
Qatar Petroleum	AA-/Stable/--	Qatar
Qatar Telecom (Qtel) Q.S.C.	A-/Stable/A-2	Qatar
Ras Laffan Liquefied Natural Gas Co. Ltd.	A/Stable (senior secured debt)	Qatar
Ras Laffan Liquefied Natural Gas Co. Ltd. (II)	A/Stable (senior secured debt)	Qatar
Ras Laffan Liquefied Natural Gas Co. Ltd. (3)	A/Stable (senior secured debt)	Qatar
Saad Group	BBB+/Stable/A-2	Saudi Arabia
Saad Trading, Contracting and Financial Services Co.	BBB+/Stable/A-2	Saudi Arabia
Saudi Basic Industries Corp.	A+/Stable/A-1	Saudi Arabia
Saudi Electric Co.	AA-/Stable/--	Saudi Arabia
Saudi Telecom Co.	A+/Stable/A-1	Saudi Arabia
Tabreed 06 Financing Corp.	BB (senior secured debt)	United Arab Emirates
Thor Asset Purchase (Cayman) Ltd.	A/Watch Neg (senior secured debt)	United Arab Emirates
Tourism Development and Investment Co.	AA/Stable/A-1+	United Arab Emirates
Sun Finance Ltd. class A sukuk certificates (issue rating)	A	United Arab Emirates
Sun Finance Ltd. class B sukuk certificates (issue rating)	BBB+	United Arab Emirates
Sun Finance Ltd. class C sukuk certificates (issue rating)	BBB-	United Arab Emirates

Notes

**All ratings correct at May 19, 2009.*

GCC Government Assets...

...Still Affording Protection Against The Global Downturn



PRIMARY CREDIT ANALYST:
FAROUK SOUSSA, PHD.,
DUBAI (971) 4709 6820
FAROUK_SOUSSA@STANDARDANDPOORS.COM

Editor's note: This article was originally published on RatingsDirect on May 5, 2009

This page: The skyline of Doha, Qatar, with the Museum of Islamic Art (designed by architect I.M.Pei) in the foreground.

STANDARD & POOR'S RATINGS SERVICES has been rating sovereigns in the Gulf Cooperation Council (GCC) region for the 13 years since we assigned Oman and Qatar ratings in the 'BBB' category in early 1996. Since that time, our coverage of GCC sovereigns has increased significantly with the State of Kuwait being rated in 1997, followed by the Kingdom of Bahrain (2002) and the Kingdom of Saudi Arabia (2003). Although the United Arab Emirates (UAE) is yet to be rated by Standard & Poor's, in the past couple of years we have seen interest in international credit ratings at the individual emirate level, with the Emirate of Abu Dhabi being rated in mid-2007, and the Emirate of Ras al Khaimah in early 2008.

The ratings performance of GCC sovereigns has been strong, primarily reflecting our view of their strengthening balance sheets and sound macroeconomic and fiscal policy. Since 1996, there have been 14 upgrades on GCC sovereign ratings, an average of three notches per credit if we exclude Abu Dhabi and Ras al Khaimah, which we started rating relatively recently. We have undertaken no downgrade of any GCC sovereign to date. The average rating of GCC countries currently stands at 'A+', with four sovereigns rated in the 'AA' category.

The outlook for all GCC sovereigns is currently stable, although we believe significant challenges lie in wait in 2009. These relate mainly to managing the impact of the downturn in the global economy, and from the associated fall in crude oil prices, upon which most GCC economies are highly dependent. In this report, we highlight what we consider will be some of the key credit developments to affect GCC economies in 2009.

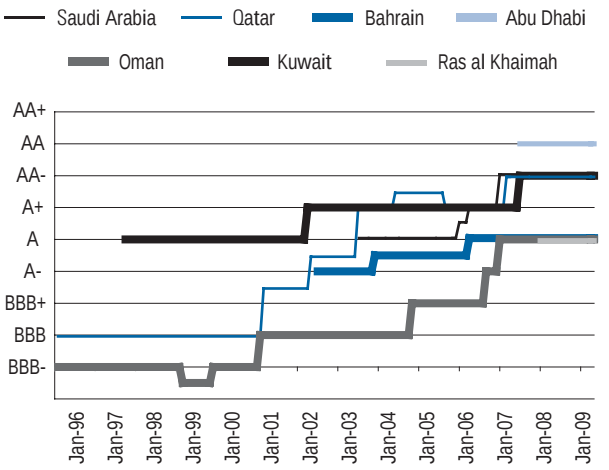
The Global Credit Crunch Bites

The reduction in global liquidity has in our view reduced the ability of GCC entities to raise financing in international capital markets, particularly for GCC-based corporates and banks. As the BIS data in chart 2 show, these GCC entities had become increasingly reliant on international financing, with the amount of debt issued in international markets increasing by a factor of around nine since 2005, peaking at almost $85 billion in September 2008. A similar pattern is evident with respect to borrowing by GCC entities from international banks, which is on a greater order of magnitude than their debt issuance. We expect the dip in both forms of financing seen in

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Chart 1

Gulf Cooperation Council Sovereign Credit Ratings History

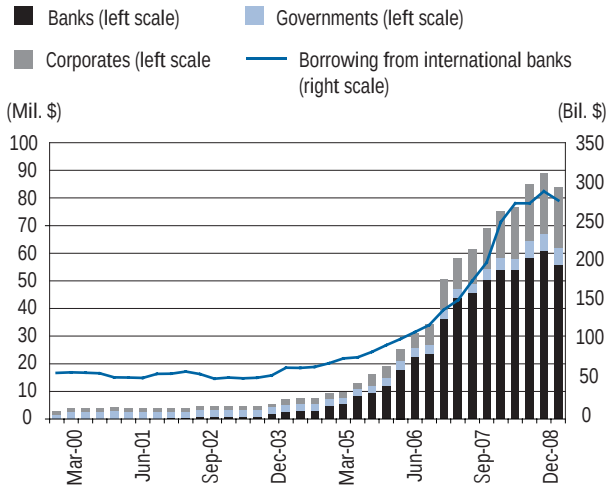


Source: Standard & Poor's

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Chart 2

Debt Issuance By GCC Governments, Corporates, And Banks



Source: BIS

© Standard & Poor's 2009.

December 2008 to continue in 2009, as we believe global markets and risk appetite will remain subdued relative to the past few years, notwithstanding recent successful global bond issues by the governments of Abu Dhabi and Qatar.

Almost three-quarters of the issuance shown in chart 2, and one-half of the bank borrowing, was done by UAE-based entities. Indeed, of all the countries in the GCC, we consider that the UAE, particularly the Emirate of Dubai, has experienced the most severe reversal in domestic liquidity conditions since mid-2008, prompting the Central Bank of the UAE to take offsetting measures (see "UAE Liquidity Squeeze Raises Questions Over Future Growth, But Credit Fundamentals Remain Sound," published Oct. 7, 2008, on RatingsDirect). Other GCC countries have also taken measures to provide for liquidity in their banking sectors and the economy more widely. The deterioration in financing conditions has meant that a large amount of private investment has been delayed due to lack of funding, putting greater onus on sovereigns to help in financing or indeed to take a more active role in implementing investment programs, particularly in infrastructure, in order to inject stimulus in the economy.

Fall In Global Asset Prices Erodes Net Assets And Raises Contingent Liabilities

While the credit crunch has hit the liabilities side of GCC countries' balance sheets, we believe the fall in global asset valuations, including in domestic GCC capital and real estate markets, has had a significant and detrimental effect on the value of their assets, resulting in lower net asset positions and higher contingent liabilities for GCC sovereigns.

Sovereign wealth funds (SWFs) across the region, but particularly in Qatar, Abu Dhabi, and Kuwait, have seen significantly negative returns on their sizeable foreign asset holdings over the past 18 months. While still very strong, we consider that the implied reduction in government net asset positions is nonetheless an erosion of one of the key credit strengths for these sovereigns. A notable exception to this has been Saudi Arabia, whose foreign assets have been in our view managed relatively conservatively by the Saudi Arabian Monetary Agency (SAMA). The value of Saudi Arabia's net foreign assets has risen to almost $440 billion by end-2008, from $300 billion the previous year.

We believe the fall in global asset valuations has also affected the sub-sovereign sectors, particularly banks and other financial institutions, whose exposures to real estate and equity have caused them to make significant write-downs on their investment portfolios in recent months. Different countries have taken different approaches to shore up the capital positions of their financial sectors. In Kuwait, a recently passed financial stabilization plan puts in place government guarantees on banks' provisioning for investment losses. Some measures in the plan are also intended to ease funding pressures at ailing investment companies, whose exposure to global asset markets and reliance on short-term wholesale financing have put significant pressures on this important pillar of the Kuwaiti financial system. In Abu Dhabi, the government announced earlier this year an injection of UAE dirhams (AED) 16 billion into its domestic-owned banks, while in Qatar, a mix

"Sovereign wealth funds (SWFs) across the region, but particularly in Qatar, Abu Dhabi, and Kuwait, have seen significantly negative returns on their sizeable foreign asset holdings over the past 18 months."

of equity injection and a government buy-out of banks' investment portfolios was carried out to shield the banking sector from any possible fallout. We consider that the net result of these developments is that the contingent liabilities of the government with respect to the banking sectors have risen appreciably. (For a detailed discussion of the GCC banking sector, please see the article "Tougher Environment Weakens Financial Profile Of Gulf Banks And Pressures Their Credit Ratings," on page 48 of this publication.)

The Fall In Oil Prices Will Affect Fiscal Outturns

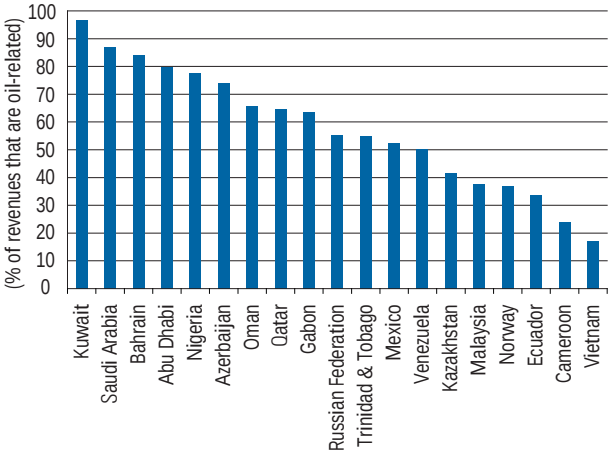
Related to the global economic downturn has been a two-thirds decline in oil prices since their peak in mid-2008. In order to give a context to the significance of such a decline on GCC sovereigns, chart 3 shows the actual contribution of oil revenues to total revenues in 2008 for the GCC and selected other oil exporters rated by Standard & Poor's. It shows that rated GCC sovereigns (excluding Ras al Khaimah, which has no oil resources) are among six of the eight sovereigns worldwide that are most dependent on oil revenues. A similar picture is true of the dependence of the overall economy on oil and gas production (please see the article "Oil Price Vulnerability Rankings: Strongest To Weakest," on page 24 of this publication).

In addition to the oil price decline, GCC countries, with the exception of Bahrain and Oman, are members of the Organisation of Petroleum Exporting Countries (OPEC) and are thus subject to OPEC's agreed oil production quotas. OPEC began to reduce these quotas in the autumn of 2008, with the aim of tempering the fall in oil prices. We therefore expect oil production to decline, with Saudi Arabia, the world's largest oil producer, expected to cut oil production most aggressively among the GCC countries, by as much as 20% in 2009.

We believe a combination of low oil prices and a decline in oil production will have a significant impact on fiscal outturns across the GCC. As chart 4 shows, we expect that the average GCC government balance will be barely positive in 2009, compared with surpluses in the order of 23% of GDP in the previous three years. We expect Saudi Arabia to fare the worst, as a combination of increased expenditure and reduced revenues will, in our view, result in a deficit of around 7% of GDP.

Chart 3

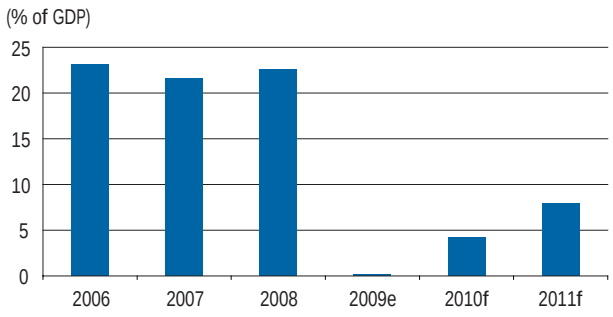
Dependence Of Government Revenues On The Oil Sector



© Standard & Poor's 2009.

Chart 4

Average General Government Balance For Rated GCC Sovereigns



e—Estimate. f—Forecast

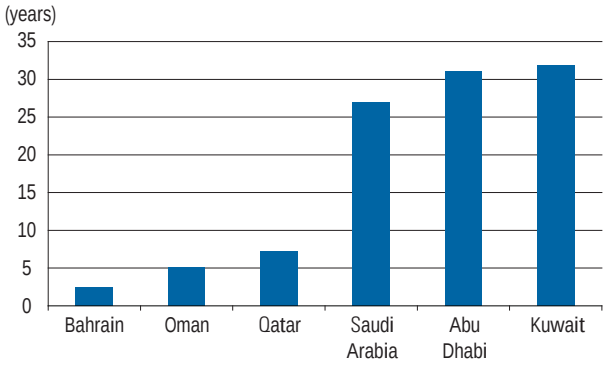
© Standard & Poor's 2009.

"We believe that the GCC region has not been immune to the impact of the global economic downturn… That said, we consider that GCC countries are well placed to ride out the turbulence, thanks primarily to their exceptional fiscal capacity to pursue counter-cyclical expansionary policy."

Chart 5

Gulf Cooperation Council Balance Sheet Strength

2009 net GG assets (% of GDP) / 10% of GDP fiscal deficit

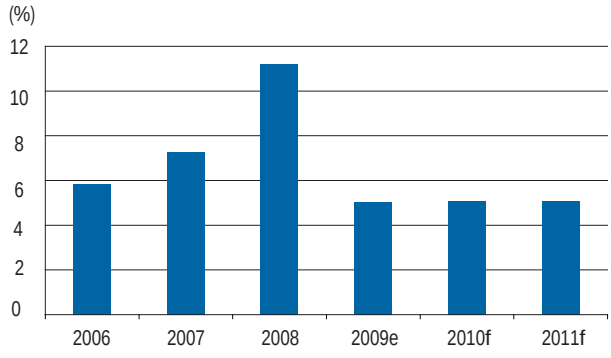


Note: This chart shows the number of years each of the GCC states can sustain a 10% of GDP fiscal deficit without resorting to borrowing, given the expected level of their assets (minus outstanding debt) in 2009.

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Chart 6

Gulf Cooperation Council Average CPI Growth



e—Estimate. f—Forecast

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But Fiscal Space Allows For Flexibility In Policy Response

That said, we do not consider that a weakening in fiscal outturns is necessarily a harbinger of deteriorating creditworthiness. In most cases, GCC countries have opted for a deliberately expansionary fiscal policy in order to counter the impact of the global economic downturn on the non-oil economy. Unlike in previous oil prices cycles in the 1970s and 1980s, GCC policy makers have by and large chosen to smooth government expenditure, which is a critical driver of the non-oil economy, opting to increase expenditure mainly in infrastructure projects. Saudi Arabia, for example, has opted to increase government expenditure by 16%, focusing on infrastructure spending, which will rise in 2009 by some 36%, the largest ever increase in infrastructure spending in that country. Similarly aggressive expansionary policies with a focus on infrastructure are evident in Abu Dhabi, Qatar, Oman, and Bahrain.

One exception to this has been Kuwait, whose budget for 2009/2010 envisages a substantial 36% decline in expenditure. While the majority of this decline is related to the exclusion of a one-off payment on social security that occurred in the previous year, it is notable that the budget still calls for a 27% decline in capital expenditure. We believe that Kuwait's fiscal policy therefore stands out as containing the least stimulus for the non-oil economy, although at the same time the fiscal balance is expected to be in surplus in 2009 as a result.

Further supporting GCC sovereign creditworthiness in the face of a deterioration in fiscal outturns is our view that GCC governments have exceptional fiscal space to implement such a policy. Chart 5 shows the number of years each of the GCC states can sustain a 10% of GDP fiscal deficit without resorting to borrowing, given the expected level of their assets (minus outstanding debt) in 2009. According to this metric, Bahrain and Oman are in the least comfortable positions, as their oil resources are more limited than other GCC states and they have therefore benefited relatively less from the windfall in high oil prices in terms of accumulation of assets. This relative weakness is reflected in the ratings on both countries, the lowest among GCC sovereigns. We estimate that Qatar has closer to seven years worth of 10% deficits that can be absorbed by its net assets, a figure which belies the fiscal strength of the sovereign, as a large share of previous surpluses have been re-invested in productive infrastructure, particularly

into the expansion of LNG production capacity. Consequently, we are of the view that revenues in Qatar will continue to rise strongly on the back of increased LNG production (which is not subject to OPEC quotas), and we expect that future surpluses will significantly strengthen the net asset position of the government in years to come.

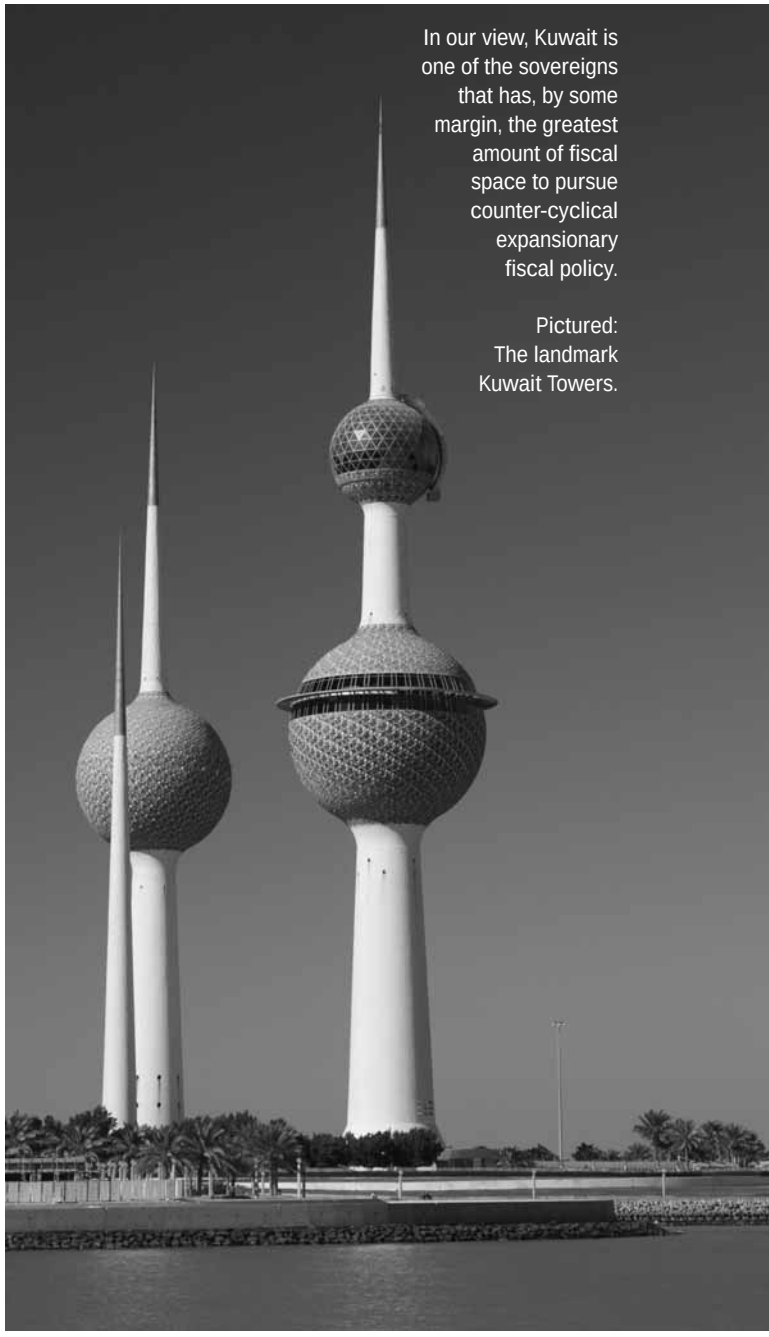
In our view, Saudi Arabia, Abu Dhabi, and Kuwait have by some margin the greatest amount of fiscal space to pursue counter-cyclical expansionary fiscal policy, and we forecast that each could sustain a 10% deficit without resorting to debt finance for at least 25 years. We consider this a key credit strength, one that is reflected in these sovereigns' position within our 'AA' ratings category.

Inflation Is On The Way Down

We believe a number of factors will contribute to significant downward pressures on inflation across the GCC throughout 2009. First, in our view, the fall in commodity prices, including food, will reduce domestic price inflation on staples. Second, we believe the recent strengthening of the U.S. dollar, to which all GCC countries are pegged (with the exception of Kuwait, which is partially pegged to the U.S. dollar) will reverse some of the "imported inflation" pressures that have been evident across the GCC. Finally, the catching up, and in some instances, overshooting of housing supply in certain GCC countries is already resulting in a reduction of rents on property, a key driver of inflation in many GCC countries over the past few years. As a result, we expect inflation rates across the GCC to come down from an average of over 10% in 2008, to around 5% in the medium term *(chart 6)*.

Diversification Remains A Key Goal

We believe that the GCC region has not been immune to the impact of the global economic downturn, with the fall in global liquidity and in oil prices posing significant challenges to all sovereigns in the region to a greater or lesser extent. That said, we consider that GCC countries are well placed to ride out the turbulence, thanks primarily to their exceptional fiscal capacity to pursue counter-cyclical expansionary policy. The non-oil economy, an important engine for future employment growth and diversification, remains a key priority in most GCC countries, and we believe that robust government expenditure will ensure that it is in large part shielded from the global economic downturn.



In our view, Kuwait is one of the sovereigns that has, by some margin, the greatest amount of fiscal space to pursue counter-cyclical expansionary fiscal policy.

Pictured: The landmark Kuwait Towers.

Debt Recovery For Creditors And The Law Of Insolvency In The United Arab Emirates

PRIMARY CREDIT ANALYST:
AGNES M DEPETIGNY
PARIS (33) 1 4420 6670
AGNES_DEPETIGNY@
STANDARDANDPOORS.COM

SECONDARY CREDIT ANALYST:
DAVID GILLMOR
LONDON (44) 20 7176 3673
DAVID_GILLMOR@
STANDARDANDPOORS.COM

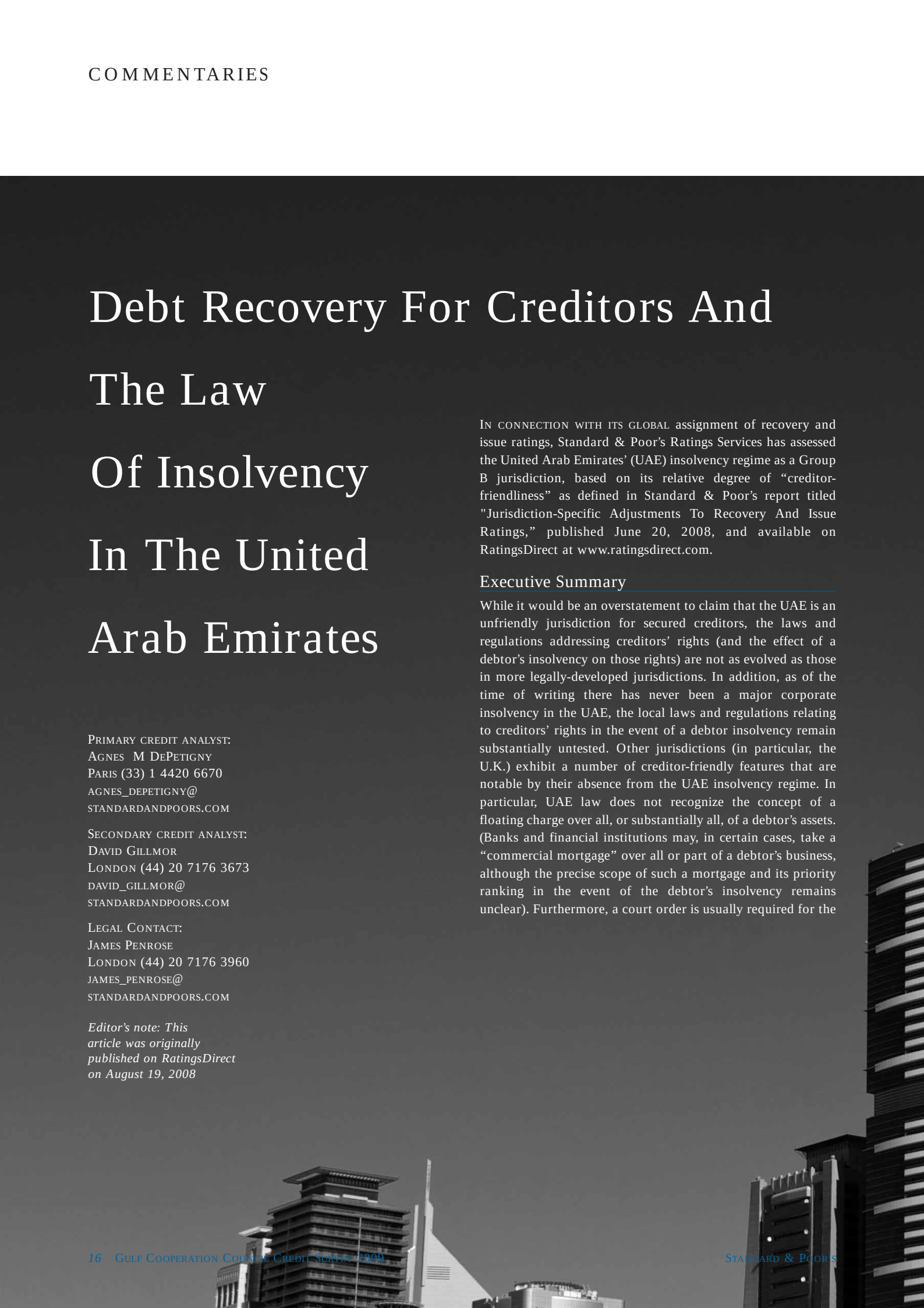
LEGAL CONTACT:
JAMES PENROSE
LONDON (44) 20 7176 3960
JAMES_PENROSE@
STANDARDANDPOORS.COM

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IN CONNECTION WITH ITS GLOBAL assignment of recovery and issue ratings, Standard & Poor's Ratings Services has assessed the United Arab Emirates' (UAE) insolvency regime as a Group B jurisdiction, based on its relative degree of "creditor-friendliness" as defined in Standard & Poor's report titled "Jurisdiction-Specific Adjustments To Recovery And Issue Ratings," published June 20, 2008, and available on RatingsDirect at www.ratingsdirect.com.

Executive Summary

While it would be an overstatement to claim that the UAE is an unfriendly jurisdiction for secured creditors, the laws and regulations addressing creditors' rights (and the effect of a debtor's insolvency on those rights) are not as evolved as those in more legally-developed jurisdictions. In addition, as of the time of writing there has never been a major corporate insolvency in the UAE, the local laws and regulations relating to creditors' rights in the event of a debtor insolvency remain substantially untested. Other jurisdictions (in particular, the U.K.) exhibit a number of creditor-friendly features that are notable by their absence from the UAE insolvency regime. In particular, UAE law does not recognize the concept of a floating charge over all, or substantially all, of a debtor's assets. (Banks and financial institutions may, in certain cases, take a "commercial mortgage" over all or part of a debtor's business, although the precise scope of such a mortgage and its priority ranking in the event of the debtor's insolvency remains unclear). Furthermore, a court order is usually required for the





enforcement of security in the UAE and UAE law makes no express provision for out-of-court sale or other "self help" procedures in respect of secured assets. In this context, any contractual right to appoint a receiver in respect of secured assets is unlikely to be enforceable without a court order, and the appointment of a receiver for the whole of a debtor's assets (such as an administrative receiver in the U.K.) is not possible.

The UAE insolvency laws have incorporated some limited debtor-friendly elements, such as a court-supervised rescue proceeding (known as "protective composition") under which creditors, including secured creditors, may be subject to a moratorium while the debtor attempts to reorganize. The fact that UAE laws and regulations are relatively untested, however, means that the insolvency process remains unpredictable. In addition, there is the possibility of government intervention in cases where a large-scale insolvency could be viewed as having a material effect on the financial system. UAE law makes express provision for a court to defer a declaration of bankruptcy—either of its own accord or on the application of the debtor company itself—if such deferral is in the interests of the national economy (there remains the potential for ad hoc intervention on the part of the government, particularly where the debtor is either a company created by decree (such as a local utility) or is government-owned).

While it is understood that the UAE government has been considering a new, more modern bankruptcy law for at least a year, no draft of such law has been published and no date for its publication (at least publicly) has been fixed. Historically,

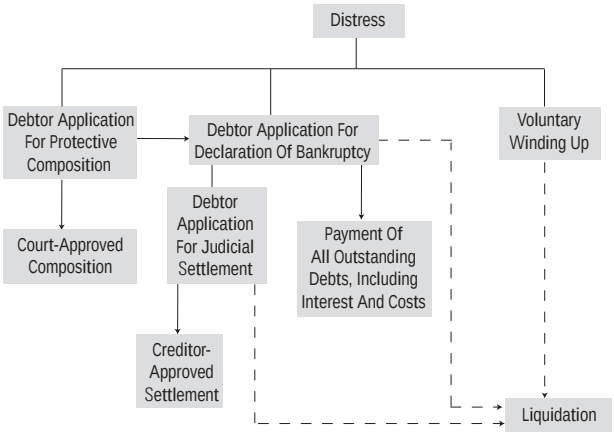
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informal restructurings not involving the judicial process have been popular. Due to the lack of anything but anecdotal evidence, however, these informal restructurings cannot serve as the basis for general conclusions.

In addition, it should be noted that there are a number of free zones in the UAE, including the Dubai International Financial Centre (DIFC). Each of the free zones has its own laws and regulations that cover, among other things, the formation and dissolution of companies. Therefore, when seeking to enforce debt claims or security interests against a company or other entity established in one of the free zones, specialist advice should be obtained.

Chart

The Insolvency Process In The UAE



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Introduction

While the creditworthiness of borrowers has always been of paramount concern to creditors, recent developments in the debt markets, including the deteriorating credit of some major corporate borrowers, the continuing growth of the collateralized debt obligation and credit default swap markets, as well as the recent credit crunch and the implementation of Basel II guidelines, have put a spotlight on creditors' prospects for recovery of principal and interest after a borrower default. From the creditors' perspective, it is no longer only a question of whether a particular borrower will default, but also whether (and to what extent) they will be repaid principal and interest after a default, and how long it will take. Standard & Poor's believes that the key to answering these questions begins with an assessment of how creditors may fare under the particular insolvency regime in having jurisdiction over all or a part of the borrower's insolvency proceedings.

This article reviews the distinctive characteristics of the UAE's insolvency regime from both a secured and unsecured creditor's perspective and assesses how these characteristics may affect post-default recovery prospects.

Overview Of The UAE's Insolvency Regime

The UAE's primary insolvency laws relating to companies appear in Federal Law No. 18 of 1993 (Commercial Transactions Law or CTL). The overriding objectives of the CTL include setting out a court-approved process for bankruptcy, composition, and liquidation.

As noted above, the CTL contains a court-approved process for protective compositions to prevent bankruptcy and winding up. As a result, any corporate debtor that has ceased paying its commercial debts as they fall due may apply to the court for protective composition, provided certain conditions (as outlined in further detail below) are fulfilled. Also, in the event that a declaration of bankruptcy is made without the debtor applying to the court for a protective composition, the court overseeing the bankruptcy must (unless special circumstances apply) invite those creditors whose claims have been either provisionally or finally accepted to discuss a judicial settlement of the debtor's claims with a view to allowing the debtor to continue as a going concern.

In the case of both a protective composition and a judicial settlement, the proposed arrangements may be implemented with the court's approval provided that at least a numerical majority of the creditors holding at least two-thirds of the corporate debtor's debts accept the terms of the composition. In practice, therefore, a dissenting minority of creditors may be bound to accept the terms of the composition. It may also be possible for a debtor to agree a composition with its creditors

"…recent developments in the debt markets…have put a spotlight on creditors' prospects for recovery of principal and interest after a borrower default."

without court approval before bankruptcy proceedings commence. However, there is no explicit provision in the CTL to this effect and the agreement of any creditor whose debts or other rights would be reduced or otherwise compromised under the terms of the arrangement would be required. There is little guidance (and no statutory constraint) on the relative length of an insolvency proceeding. Judges assigned to insolvency matters are not insolvency specialists, but are presumably versed in commercial law.

Some UAE-based companies have assets located in other jurisdictions in the region with different insolvency regimes, such as Bahrain, Kuwait, Oman, Qatar, and Saudi Arabia. Since the insolvency regimes in these jurisdictions will pose different challenges to creditors, these extra-national legal considerations may significantly affect debt recovery prospects for UAE-based entities, depending on the location and relative size of the assets. In these circumstances, Standard & Poor's approach for assessing the overall prospects for recovery may be to take a disaggregated view of recovery and consider the legal and insolvency regimes of the countries where these assets are domiciled.

DIFC

The DIFC has its own insolvency statute (a condensed version of the U.K. insolvency regime) and its own courts. In theory, DIFC proceedings are more creditor-friendly as its law and judges come from a common law background. Again, the lack of experience is a factor, as the DIFC courts have only a three-year operating history.

Process

The chart opposite illustrates the possible steps that may be taken in a UAE insolvency process. (It should again be noted that this chart is provisional because of the relatively untested nature of the UAE insolvency regime.)

Protective Composition

As noted above, in the event that a debtor ceases to be able to pay its debts as they fall due, it may apply to the court for a protective composition. From a debtor's perspective, the advantage of a protective arrangement with creditors is that the debtor's management may retain control of the business while composition proceedings are pending. If the application for the commencement of composition proceedings is accepted, however, the court is obliged to appoint one or more insolvency trustees to implement the composition. The CTL is unclear regarding how the insolvency trustee will replace the management in running the debtor's day-to-day affairs.

Compositions with creditors may conceivably involve debt-for-equity conversions, debt moratoriums, extended repayment schedules, "fresh" equity contributions, or, in the case of a group, its reorganization or merger. The only express restrictions on the proposed terms of a protective composition under the CTL are that the proposal must provide for payment of no less than 50% of the debts owed and the payment of such debts within three years of the ratification of the composition. There is, however, some uncertainty as to the application of the first of these requirements since the CTL does not specify whether the 50% debt repayment threshold applies in aggregate or to the debt owing to each individual creditor. Clearly, the approach of UAE courts to this provision could materially affect the protections applicable to dissenting creditors.

In order for a debtor to apply to the court for a protective composition, the debtor must have been continuously trading for at least a year prior to the application and during that period have fulfilled its obligations under the Federal Law No. 9 of 1984 (Commercial Companies Law), as well as the terms of its commercial business license from the Ministry of Economy and Planning. An application for protective composition should include the reasons for the disruption of the debtor's business and the terms of the proposed composition. Upon receiving the application, the court may place a moratorium on the enforcement of security interests granted and debts owed, by the debtor and may implement any other measures necessary to preserve and manage the debtor's debts until the court takes a decision on the proposed composition. The CTL requires a notice to be published in the local press confirming the opening of composition proceedings. All creditors must submit to the insolvency trustee proof of the debts owed to them by the debtor, along with details of any security or other protections that the creditors have covering those debts. Local creditors must submit details of their debts within 10 days from publication of the notice, while creditors based outside the UAE have a month to file.

"While it would be an overstatement to claim that the UAE is an unfriendly jurisdiction for secured creditors, the laws and regulations addressing creditors' rights (and the effect of a debtor's insolvency on those rights) are not as evolved as those in more legally-developed jurisdictions."

The CTL provides for formal deliberation between the creditors in relation to the proposed composition, under the oversight of a supervising judge although there is no fixed timetable within which the deliberations must occur. The court has the discretion to approve or reject the composition proposed by the debtor (whether or not with any amendments). In addition, in order for the composition to be effected, a majority of the debtor's creditors holding at least two-thirds of the debts of the debtor must agree to its terms. For this purpose, any creditor not voting on the proposed composition will not be counted in determining whether or not the required majority has been reached. In deciding whether or not to approve the composition, the supervising judge is likely to assess the debtor's assets and liabilities and review the creditor claims against the debtor with a view to determining the debtor's prospects of continuing as a successful going concern. There has, at the time of writing, never been a major corporate insolvency in the UAE and it is therefore difficult to predict the degree of scrutiny that a UAE court would apply to such applications, and the extent to which the court would, in practice, treat different creditors.

The court overseeing the bankruptcy has a general power under the CTL to order such measures as may be necessary for preserving or managing the debtor's property until a final decision on a protective composition is taken. This means that, in practice, the court may stay secured creditors from enforcing their security rights over the insolvent debtor's assets, particularly if the preservation of those assets increases the chance of the debtor continuing as a going concern.

Applying For A Declaration Of Bankruptcy

Creditors may initiate compulsory liquidation proceedings through an application to the court on the grounds that the debtor has failed to pay its commercial debts as they fall due "as a result of the debtor's unstable financial position and poor creditworthiness." The court is responsible for appointing a trustee in bankruptcy to administer the bankruptcy proceedings. It remains to be seen whether the local courts will accede to the recommendation of the creditor applying for a declaration of bankruptcy in deciding which firm to appoint as trustee in bankruptcy or whether the court will chose to make its own independent appointment. The CTL does not specify the time period within which a court must make a decision on an application by a creditor for a declaration of bankruptcy.

Compulsory Winding Up

In the case of a compulsory winding up, a creditors' committee is automatically formed by force of law on the declaration of bankruptcy by the court. The trustee in bankruptcy, or the liquidator (as applicable), will, if no judicial settlement is agreed, dispose of all the debtor's assets and apply the proceeds in the order of priority established by the CTL, as set out in further detail below. There is no statutory time limit on a compulsory liquidation proceeding.

In the case of a compulsory winding up, the CTL allows the creditors (presumably acting through the trustee in bankruptcy) to apply to the court to set aside past transactions that constitute an unfair preference. There are certain categories of preferential disposal (including gifts and early debt repayment) that are specified in the CTL as being unenforceable by the relevant disposees. In addition, any other transaction that was harmful to the debtor and was made at a time that the counterparty was aware that the debtor had ceased paying its commercial debts may be classified as a preferential transfer. In this context, there is a formal "suspect" period that begins on the date that the bankruptcy court deems the debtor to have ceased paying its debts as they fall due, before which transfers made by the debtor are safe from recharacterization as preferential transfers. While the CTL contains a power for the court to specify the date on which the debtor ceased paying its debts as they fell due, it also provides that the date must not be more than two years before the declaration of the debtor's bankruptcy. In practice, this means that the suspect period in relation to possible preferential transfers will extend no more than two years prior to the declaration of bankruptcy, although fraudulent transactions may still be subject to scrutiny notwithstanding the fact that they occurred prior to the cessation of payments.

Judicial Settlement

In the event a UAE court issues a declaration of bankruptcy in relation to a debtor before the debtor applies for a protective composition, the judge overseeing the bankruptcy must

commence judicial settlement proceedings. In this case, the creditors will debate the proposal submitted by the debtor following the publication of the debtor's schedule of debts, at such a time and place as the judge overseeing the bankruptcy may direct.

The bankruptcy trustee is responsible for producing a report to the settlement meeting, outlining, among other things, the state of the bankruptcy, the debtor's proposal for settlement, and the trustee's opinion of the proposals. In order for a settlement to be implemented, a majority of the debtor's creditors holding at least two-thirds of the debtor's debts, finally or provisionally accepted, must agree to the terms of the settlement. For this purpose, the CTL provides that nonattending creditors are deemed to have rejected the proposed settlement. There is, however, an express requirement under the CTL for the court to approve a judicial composition, which may provide a degree of protection to any dissenting minority. In the event that the requisite majority is not reached at the first settlement meeting, the CTL provides for a 10-day postponement before a second deliberation meeting. Creditors who agreed to the proposed settlement at the first meeting then have the option of not attending the second meeting, in which case their consent will remain effective unless there is a fundamental change to the settlement proposals. If those creditors attend the second meeting, however, they may withdraw their original consent. Although the CTL provides that a judicial settlement may be agreed with a debtor where the debtor is culpable in its own bankruptcy, it also explicitly provides that a settlement may not be made with a debtor convicted of fraudulent bankruptcy.

Forming A Creditors' Committee

In the event that, following an insolvent debtor's declaration of bankruptcy, the debtor's ordinary creditors cannot agree to the terms of a judicial settlement, a creditors' committee is automatically formed under the provisions of the CTL. Upon the formation of the creditors' committee, the creditors have the option to retain the current trustee in bankruptcy or appointing an alternative to act as the trustee of the creditors' committee. With the consent of three-quarters of the debtor's creditors (both numerically and with reference to the outstanding debt owed), the trustee appointed may make arrangements for the continuation of the debtor's business for such period as the creditors may specify. The trustee also has broad rights to sell the debtor's property, receive its debts, and make compositions with creditors. In the event that the creditors cannot agree on arrangements for the continuation of the debtor's business, the debtor will, barring any special court or government intervention, proceed to liquidation. It remains to be seen whether liquidations will be more common than compositions and judicial settlements in the UAE. The court may order compulsory liquidation at a creditor's request.

Voluntary Winding Up

As an alternative, debtors may voluntarily effect a voluntary winding, following an extraordinary general meeting of the debtor's shareholders under the terms of the Commercial Companies Law. There is no express requirement in the Commercial Companies Law for court approval to a voluntary liquidation. On a creditor's application, however, the court is likely to step in to oversee the process. In the case of a voluntary winding up, there is no formal process for creditors to appoint an inspection committee to oversee the liquidator's activities, although the liquidator will, in practice, be obliged to carry out its role in accordance with the provisions of the CTL, including those provisions regarding the ranking of debt and the treatment of security.

Security

In the UAE, security is commonly granted over certain types of corporate assets, including real estate, receivables, and shares, while the enforceability of security over some assets (including monies held in bank accounts with fluctuating balances) is untested. As a general rule, there are no legal requirements for the registration of security in order for security to be enforceable. Mortgages over land or a company's business (see below for additional details), however, must be registered with the Lands Department and with the relevant Emirate economic department in order to be enforceable.

As noted above, UAE law does not recognize the concept of a floating-charge. Banks and financial institutions are entitled to take a commercial mortgage over all or part of a company's business. These mortgages are often referred to as "Article 49 mortgages" as their existence derives from Article

49 of the CTL. Article 49 does not include any express restrictions on the types of companies over whose assets an Article 49 mortgage may be taken, but since Article 50 of the CTL states that it is a precondition to the enforceability of the mortgage that it is registered in the relevant commercial register within 21 days and renewed every five years, these mortgages will therefore only be viable in respect of companies that are registered in a register that maintains a system for recording commercial mortgage interests.

While the economic departments of the Emirates of Abu Dhabi, Dubai, Fujerah, and Sharjah maintain a commercial register in which such companies (and therefore such mortgages) must be registered, the other Emirates do not. Even in those Emirates in which it is possible to register a mortgage, there is a degree of uncertainty as to such mortgage's scope. In particular, Article 49 provides (in translation) that assets must be "categorically stated" to be covered by the mortgage. With this in mind, contents of a company's inventories and other assets that may be actively traded are unlikely to fall within the scope of the mortgage. Furthermore, the CTL does not specify whether the mortgage only applies to the business of the company, which it is licensed to carry on locally, and whether other corporate assets (including those held abroad) may fall outside the mortgage's scope if they are not an integral part of the particular business.

"Industrial Mortgages" over the business of a manufacturing or industrial company with an Industrial Licence have been expressly provided for by Federal Ministerial Decree No. 612 of 2000. At the time of writing, however, no registration system is in place which means, effectively, that such mortgages cannot yet be taken. It is unlikely that the UAE courts will enforce present security taken over future assets.

Since there has never been a major corporate insolvency in the UAE, it is difficult to provide guidance on the enforceability of secured property rights in the jurisdiction. It is possible that, depending upon the circumstances, the commencement of formal insolvency proceedings under the CTL may impair the ability of a secured creditor to effectively enforce its security. The CTL states that claims of holders of "general liens" over a debtor's property, along with claims of the debtor's ordinary creditors, are suspended from the date of the declaration of bankruptcy until such time as the court orders that the sale of the immoveable property of the debtor be suspended. It is possible that, for this purpose, a "general lien" would include an Article 49 mortgage, although there is no express statement in the CTL to this effect. The term may instead be intended to cover liens arising by force of law (for example, in relation to employee's wages or back taxes (see Priority Ranking In A Liquidation)). In addition, as noted above, the enforcement of security in the UAE is generally subject to a court order. In this context, it is unclear from the UAE insolvency laws the circumstances in which the court overseeing the bankruptcy may reject a debt claim submitted to the court. The CTL does, however, expressly specify that the bankruptcy judge has the power to deem a debt to be contested even if no objection has been presented to it. While creditors have an express right under the CTL to contest a decision on the part of the judge overseeing the bankruptcy to accept or reject a debt, the law does not contain a list of grounds on which this challenge may be made.

In many jurisdictions, receivership is an effective means for secured creditors to foreclose upon pledged security for the obligations owed to them in the event of a debtor's payment default and insolvency. A right to appoint a receiver is typically included in security documents and triggered by the occurrence of any one of a number of events of default. Events of default are likely to include insolvency and the appointment of a liquidator or other external administrator to the security provider. In other jurisdictions, a receiver is commonly appointed by a secured creditor in circumstances where the debtor is already insolvent or is nearing insolvency. In practice, since the CTL makes express reference to a need for court permission before the enforcement of either a mortgage or a pledge, self-help remedies, such as the appointment of a receiver, may, in practice, be unenforceable. In addition, while some other jurisdictions make provision for the appointment of an administrative receiver with broad management powers, who may take control over all or most of a debtor's assets, there is no equivalent provision under UAE law. It is possible that a UAE debtor may seek to challenge the appointment of a receiver on the grounds that such appointment is inconsistent with the role of the board of directors in managing its day-to-day affairs, as set out in the Commercial Companies Law.

The CTL suggests that secured creditors do not have an explicit right to vote on either a protective composition or a



judicial settlement in respect of any secured debts (although it is understood that secured creditors will have a right to vote in the relevant meetings in respect of any debts that exceed the value of their security). The fact that secured creditors do not have an explicit right to vote in composition or settlement proceedings indicates that their security rights have formal protection from any composition. In this context, the CTL expressly states that judicial settlement proceedings do not apply to creditors holding liens or pledges over the insolvent debtor's assets except in cases in which they choose to vote on the composition proceedings. In that case, they are deemed to have assigned their security, which will then fall into the debtor's general unsecured property for the purposes of the composition.

Priority Ranking In A Liquidation

The UAE's insolvency laws provide a degree of protection to the priority of secured creditors, although in practice the relevant provisions of the laws remain largely untested.

The UAE's insolvency laws are ambiguous about the position of secured creditors as a matter of priority ranking. On some occasions, the courts have given first priority to secured creditors, while in others the courts have preferred employee wage and tax claims over secured creditor claims. The following general order of payment priority in respect of unsecured creditors under the CTL should be read in that context. Even then, such priorities may be treated by the courts subjectively:

- Wages due to employees and other workers for the 30-day period immediately preceding the declaration of bankruptcy; then
- Specified categories of preferential claim, including rental due to lessors in respect of property leased to the debtor in respect of the year immediately preceding and the year immediately after the declaration of bankruptcy; and government tax claims up to two years preceding the declaration of bankruptcy (with the government being treated as an ordinary creditor for any prior back taxes), noting that the CTL does not specify how such claims will rank against each other; and then
- Unsecured creditors.

It is unclear from the CTL where the costs and expenses of the bankruptcy and the winding up will fall in the order of priority, but it is possible that these may rank just below the claims of secured creditors.

Consolidation

It is generally understood that the UAE recognizes that a debtor has a separate legal personality, distinct from its members, and that this principle would apply equally to a group of companies that are run as a single operational unit. However, in the absence of any express rule in the UAE's insolvency regime prohibiting the consolidation of the assets and liabilities of affiliated companies that are under liquidation, there is no precedent as to the manner in which group companies will be treated in the event of insolvency.

Creditor's Rights

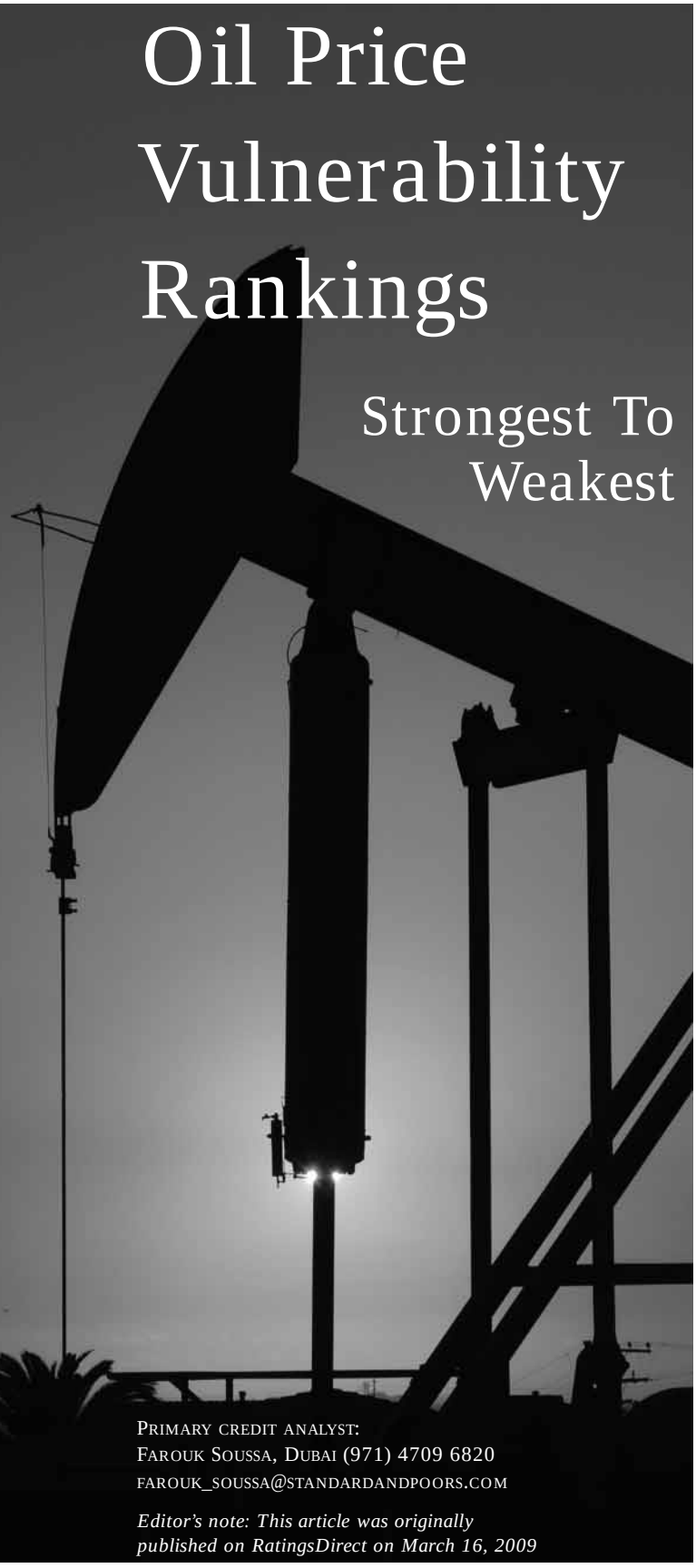
While the CTL seeks, in broad terms, to protect secured creditors' rights, secured creditors' ability to take "self help" actions against the debtor without court approval is limited. In addition, in respect of creditors holding certain types of security (for example, an Article 49 mortgage), a formal procedure for composition of creditors exists that will, in practice, result in delays in the enforcement of security and could result in an unfavorable restructuring plan.

There are few indications in local law as to whether the insolvency process is oriented more toward the liquidation of insolvent debtors than toward the rescue of debtors in distress. While the requirement of court approval for a protective composition offers some protection to unsecured creditors, the courts are, in practice, likely to have a broad discretion as to whether to approve a protective composition and the terms on which they are willing approve it. In addition, since there is no express requirement under the CTL for the court to approve a judicial composition after the declaration of bankruptcy, it is likely that such composition may override the interests of a dissenting minority.

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Oil Price Vulnerability Rankings

Strongest To Weakest



PRIMARY CREDIT ANALYST:
FAROUK SOUSSA, DUBAI (971) 4709 6820
FAROUK_SOUSSA@STANDARDANDPOORS.COM

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THE SHARP FALL IN OIL PRICES since mid-2008 has come as a welcome boon to oil-importing countries. Pressure had been mounting for several years on oil-importers' current accounts and, in some instances, fiscal balances, as oil prices continued to soar to record highs. This pressure has now eased substantially, with oil prices hovering below $50 per barrel and weaker global demand keeping the outlook for oil prices fairly subdued. The fall in oil prices has, in our view, also contributed to reduced inflationary pressures, which were becoming increasingly problematic the world over.

For oil-exporting countries, however, the drop in oil prices has been less welcome. Some are facing dramatic declines in their fiscal and external balances in 2009, along with much less exuberant growth or even declines in their net asset positions compared with 2008. To better understand the relative vulnerabilities of the oil-exporting countries to changes in oil prices, Standard & Poor's Ratings Services has devised a ranking index that we believe allows the reader to broadly compare the degree to which an individual oil-exporting country could be affected by falling oil prices.

The Relative Oil Price Vulnerability Index

The index we have proposed is a relative ranking of an oil-exporting country's vulnerability to falls in the global price of oil, taking into account three areas: The impact of falls in oil prices on economic output, on external balances, and on government finances. Table 1 lists the six key indicators that we used to gauge the impact on these three areas.

Relationship Between The Relative Oil Vulnerability Index And Sovereign Credit Ratings

Clearly, the economic, fiscal, and external considerations reflected in these rankings are incorporated in Standard & Poor's sovereign ratings. However, the correlation between the country rankings proposed in this report and their credit ratings is not high because a number of other factors enter our ratings analysis that are not considered in the vulnerability ranking, including political stability, a country's absolute level of wealth, and the overall state of a government's finances. Moreover, structural economic and fiscal factors can, in our ratings analysis, mitigate or exacerbate the overall vulnerability of an individual country to swings in oil prices in

Table 1: Key Indicators To Gauge Effect Of Oil Price Changes On Oil-Producing Countries

Indicator	Metric	Rationale
Economic impact		
1. Contribution of hydrocarbons to GDP	% of 2008 nominal GDP contributed by oil/gas	A simple measure of the hydro carbons sector to overall economic output and wealth
External impact		
2. Contribution of oil/gas exports to total exports	% of 2008 total exports represented by oil/gas	A simple metric of the importance of oil/gas to a country's external revenues
3. Current account balance assuming oil prices at $30/barrel	2008 current account balance assuming a $30 oil price	A measure of the state of a country's external balance at stressed oil price levels
Fiscal impact		
4. Contribution of oil/gas to total revenues	% of 2008 gvt. revenues represented by oil/gas revenues	A measure of a government's dependence on oil/gas revenues
5. Govt. fiscal balance assuming oil prices at $30 per barrel	2008 fiscal balance assuming a $30 oil price	A measure of the state of a government's fiscal balance at stressed oil price levels
6. Fiscal buffer	2008 total liquid assets cover of 2008 govt expenditure	A measure of the degree to which government's assets may help weather a fall in revenues

a way that we believe cannot be summarized in a general indicator such as the one set out in this report. The index should therefore be used as an indication of relative vulnerability that can give the reader a broad idea of the impact of oil price swings on oil-exporting countries.

The Rankings At A Glance

Table 2 *(see next page)* sets out our assessment of the relative rankings for each of the oil vulnerability index sub-categories, as well as the overall index. A value close to zero indicates our view that there will be a low relative impact of an oil price fall on the selected key indicators, while a value close to one indicates our view that there will be a high relative impact. Based on the above metrics, our analysis indicates that the three most vulnerable countries to a fall in oil prices rated by Standard & Poor's are Bahrain, Saudi Arabia, and Azerbaijan. We believe these sovereigns' high index score stems from the relative focus of these countries' economies, exports, and revenue streams on hydrocarbons, which in the case of Saudi Arabia outweighs, according to our metrics, the impact of a significant fiscal buffer.

The index indicates that the least vulnerable countries to a fall in oil prices are Norway, Cameroon, and Mexico, due to what we believe is a lower structural dependence on oil in the economy and government revenues, which in the case of Cameroon outweighs the lack of a fiscal buffer.

The relative rankings in this index of say, Saudi Arabia (rated AA-/Stable/A-1+) and Cameroon (B/Stable/B), are an indication of the importance of other factors in determining sovereign credit quality, such as political risk and the overall wealth of a country. Indeed, the rankings highlight the absence of a direct correlation between the above oil vulnerability indicators and sovereign creditworthiness.

"…our analysis indicates that the three most vulnerable countries to a fall in oil prices rated by Standard & Poor's are Bahrain, Saudi Arabia, and Azerbaijan…"

Rankings Of Oil-Exporting Countries For Individual Indicators

Contribution of hydrocarbons to GDP

A heavy concentration of economic activity in the hydrocarbons sector naturally tends to raise a country's vulnerability to a sharp fall in oil prices. According to our calculations, such a concentration was most pronounced in the oil-exporting countries of the Persian Gulf, with all but one (Nigeria) of the top five countries located in that region. At the other end of the spectrum are countries with a greater relative diversification in economic activity, such as Mexico, Cameroon and Kazakhstan.

Table 2: Oil Price Vulnerability Index Rankings

	Relative Economic Vulnerability Index	Relative External Vulnerability Index	Relative Fiscal Vulnerability Index	Relative Vulnerability Index Total Score
1. Bahrain	0.89	0.79	0.91	0.86
2. Saudi Arabia	1.00	0.69	0.61	0.77
3. Azerbaijan	0.70	0.70	0.79	0.73
4. Nigeria	0.42	0.84	0.70	0.65
5. Oman	0.48	0.67	0.75	0.63
6. Kuwait	0.70	0.49	0.70	0.63
7. Gabon	0.56	0.57	0.65	0.59
8. Qatar	0.70	0.54	0.48	0.57
9. Trinidad & Tobago	0.52	0.53	0.62	0.56
10. Venezuela	0.33	0.65	0.68	0.55
11. Ecuador	0.38	0.46	0.67	0.50
12. Russian Federation	0.21	0.43	0.71	0.45
13. Abu Dhabi	0.84	0.18	0.33	0.45
14. Kazakhstan	0.11	0.59	0.57	0.42
15. Vietnam	0.12	0.35	0.63	0.37
16. Malaysia	0.27	0.01	0.74	0.34
17. Norway	0.28	0.24	0.41	0.31
18. Cameroon	0.05	0.24	0.54	0.28
19. Mexico	0.00	0.14	0.67	0.27

Note

A value close to zero indicates our view that there will be a low relative impact of an oil price fall on the selected key indicators, while a value close to one indicates our view that there will be a high relative impact.

Table 3: Oil Price Vulnerability Index

Contribution Of Hydrocarbons To GDP

	Value
Saudi Arabia	1.00
Bahrain	0.89
Abu Dhabi	0.84
Azerbaijan	0.70
Qatar	0.70
Kuwait	0.70
Gabon	0.56
Trinidad & Tobago	0.52
Oman	0.48
Nigeria	0.42
Ecuador	0.38
Venezuela	0.33
Norway	0.28
Malaysia	0.27
Russian Federation	0.21
Vietnam	0.12
Kazakhstan	0.11
Cameroon	0.05
Mexico	0.00

Table 4: Oil Price Vulnerability Index

Contribution Of Oil And Gas Exports To Total Exports

	Value
Nigeria	1.00
Azerbaijan	0.97
Kuwait	0.96
Venezuela	0.95
Saudi Arabia	0.90
Qatar	0.81
Gabon	0.76
Oman	0.71
Trinidad & Tobago	0.68
Kazakhstan	0.61
Bahrain	0.58
Russian Federation	0.52
Ecuador	0.46
Norway	0.39
Abu Dhabi	0.34
Cameroon	0.20
Malaysia	0.01
Mexico	0.01
Vietnam	0.00

Contribution of oil/gas exports to total exports

Similarly, a greater concentration in exports of oil or gas products tends to render a country's external revenues more vulnerable to falls in oil prices. Here, countries such as Nigeria and Venezuela, which rank relatively favorably in our analysis in terms of economic concentration, rank among the most vulnerable due to their lack of non-oil exports. Abu Dhabi's appearance in these rankings—in the company of countries with diversified export bases such as Vietnam, Mexico, and Malaysia—is because external data for the emirate is collected at the United Arab Emirates level, and therefore takes into account the non-oil exports of Dubai and other non-oil exporting emirates.

Current account balance assuming oil prices at $30 per barrel

Lower oil prices and a reduction in external revenues is typically worse news for countries with otherwise vulnerable external balances. A static snapshot of what the 2008 current account balance would have looked like if oil prices were $30 per barrel does not take into account the ability of a given economy to adjust to a lower value of exports by reducing imports (especially when high oil prices are fuelling a domestic investment boom), but is in our view still a useful indicator of the possible vulnerability of external finances. Vietnam's high vulnerability score in this metric, given that oil and gas comprise a minimal share of its total exports, reflects the country's relatively high current account deficit in 2008.

Contribution of oil and gas to total revenues

Countries where the state has near total control of the hydrocarbons industry, and therefore benefits most from the hydrocarbons revenues, are also those countries which tend to be most vulnerable to a fall in oil prices. The evidence suggests to us that it is these countries that also have narrow revenue streams, with low or non-existent tax bases and alternative revenue sources. On this measure, the Gulf countries also rank relatively highly in our assessment compared with non-regional peers.

Government fiscal balance assuming oil prices at $30 per barrel

As with a country's external side, lower oil prices and a reduction in oil revenues is typically worse news for countries with otherwise vulnerable fiscal balances. A static snapshot of what the 2008 fiscal balance would have looked like if oil prices were $30 per barrel does not take into account the ability of a given government to adjust to lower revenues by reducing expenditures (again, this is particularly relevant where high oil prices are fuelling a domestic government-led investment boom), but is in our view still a useful indicator of the possible vulnerability of public finances.

Fiscal buffer

Even if a country is highly dependent on oil revenues, it can finance deficits in the near term if it has accumulated a large buffer of liquid assets. Such a country should, in our view, be able to smooth expenditure over the cycle while mitigating financing risks. On this measure, Gulf countries, which have accumulated sizeable net general government asset positions

Table 5: Oil Price Vulnerability Index

Current Account Balance Assuming Oil Prices At $30 Per Barrel	Value
Bahrain	1.00
Vietnam	0.71
Nigeria	0.67
Oman	0.62
Kazakhstan	0.58
Saudi Arabia	0.48
Ecuador	0.47
Azerbaijan	0.43
Trinidad & Tobago	0.38
Gabon	0.37
Venezuela	0.36
Russian Federation	0.33
Cameroon	0.28
Mexico	0.27
Qatar	0.27
Norway	0.10
Kuwait	0.03
Abu Dhabi	0.02
Malaysia	0.00

Table 6: Oil Price Vulnerability Index

Contribution Of Oil And Gas Exports To Total Revenues	Value
Kuwait	1.00
Saudi Arabia	0.88
Bahrain	0.84
Abu Dhabi	0.79
Nigeria	0.76
Azerbaijan	0.71
Oman	0.61
Qatar	0.60
Gabon	0.58
Russian Federation	0.48
Trinidad & Tobago	0.48
Mexico	0.45
Venezuela	0.42
Kazakhstan	0.31
Malaysia	0.26
Norway	0.25
Ecuador	0.21
Cameroon	0.09
Vietnam	0.00



over the past few years, rank more favorably than others (for more information see "How Sovereign Wealth Funds Are Underpinning Gulf States' Credit Quality," published June 5, 2008, on RatingsDirect).

The Oil Price Vulnerability Index In Context

This report outlines our opinion of the various pressure points of oil-producers to the recent decline in oil prices. Importantly, it indicates the overall degree of exposure particular countries have to oil prices, taking into account the relationship between oil prices and a country's economy, public finances, and external accounts. The results, however, should be viewed in the context of the wider economic and financial developments that continue to plague countries worldwide. For some countries in this report, the decline in oil prices has been compounded by limited access to investment capital or capital flight, the need to provide fiscal stimulus packages where domestic demand has slumped, and costs associated with support for domestic financial systems. Taken together, these factors have already had a negative effect on the sovereign ratings on several countries in this report in 2008 and 2009. In the absence of an improvement in the global economy and a rebound in oil prices, this pressure is likely to continue.

Table 7: Oil Price Vulnerability Index

Government Fiscal Balance Assuming Oil Prices At $30 Per Barrel	Value
Kuwait	1.00
Bahrain	0.91
Saudi Arabia	0.74
Malaysia	0.71
Azerbaijan	0.70
Trinidad & Tobago	0.66
Oman	0.64
Venezuela	0.58
Vietnam	0.53
Abu Dhabi	0.53
Ecuador	0.51
Russian Federation	0.49
Nigeria	0.38
Kazakhstan	0.31
Qatar	0.29
Mexico	0.24
Gabon	0.18
Cameroon	0.06
Norway	0.00

Table 8: Oil Price Vulnerability Index

Fiscal Buffer	Value
Vietnam	1.00
Malaysia	1.00
Cameroon	1.00
Mexico	0.99
Ecuador	0.97
Bahrain	0.95
Russian Federation	0.94
Gabon	0.92
Azerbaijan	0.88
Venezuela	0.87
Oman	0.87
Nigeria	0.84
Kazakhstan	0.84
Norway	0.70
Trinidad & Tobago	0.67
Qatar	0.51
Saudi Arabia	0.41
Kuwait	0.39
Abu Dhabi	0.00

Abu Dhabi (Emirate of)

PRIMARY CREDIT ANALYST: FAROUK SOUSSA, PHD., DUBAI (971) 4709 6820, FAROUK_SOUSSA@STANDARDANDPOORS.COM

SECONDARY CREDIT ANALYST: LUC MARCHAND, LONDON (44) 20 7176 7111, LUC_MARCHAND@STANDARDANDPOORS.COM

ISSUER CREDIT RATING (FOREIGN AND LOCAL CURRENCY): AA/STABLE/A-1+

PUBLICATION DATE: APRIL 8, 2009

Rationale

The ratings on the Emirate of Abu Dhabi are supported by the government's very strong asset position, which provides significant financial flexibility, the country's high level of political stability and wealth, underpinned by its rich resource endowment, and by policies that reinforce Abu Dhabi's integration with the global economy. The ratings are constrained by the geopolitical risks that face all sovereigns in the region, the limited disclosure on the government's assets, and growing contingent liabilities arising from the banking system and the public sector of the UAE as a whole.

The government of Abu Dhabi has accumulated substantial foreign and domestic assets, which are the product of a high resource endowment and prudent fiscal policies over past decades. Standard & Poor's Ratings Services estimates the government's net asset position to be more than 190% of GDP in 2008 and 231% in 2009—one of the highest among rated sovereigns. On the back of rising oil and investment income, the Emirate's budget has shown substantial surpluses over the past few years, although these are expected to diminish in future years as oil prices remain relatively subdued, and the government pursues countercyclical expenditure programs. The government's proactive diversification policies will continue, despite the global economic downturn, and the ambitious associated investment program will be financed by a combination of internal resources and external borrowing.

Per capita GDP, which we estimated at about $103,500 in 2008, is higher than that of 'AA' rated peers. Growth is supported by a track record of prudent macroeconomic policies, careful management of oil and gas resources, and proactive diversification policies. Over the next few years, government expenditure in infrastructure, real estate, and tourism projects will continue to be a key driver of growth as global economic activity remains subdued. The Emirate's oil and gas reserves are projected to last for at least another century at current production levels, with low production costs. Manufacturing and tourism are projected to complement the dominant hydrocarbon sector, while the government downsizes and looks to the private sector to create jobs for Abu Dhabi nationals.

Structural weaknesses and challenges remain, however. First, we believe the independent institutions, accountability, and transparency needed for the functioning of an efficient market economy are, by and large, still in the early stages of development. Second, rising debt in the public sector in the UAE as a whole, along with its complicated and close linkages with the private sector, create a dependence that suggests growing contingent liabilities for Abu Dhabi, as the wealthiest Emirate in the UAE, particularly as financing conditions have deteriorated markedly in recent months. Third, like other sovereigns in the region, Abu Dhabi is exposed to event risks such as a sharp escalation in hostilities between Iran and the West, or terrorist attacks. Such developments might raise risks in the UAE's banking and property sectors. Event risk and contingent liabilities are not expected to threaten political or social stability, and Abu Dhabi is capable of absorbing potential costs through existing government assets.

Outlook

The stable outlook on Abu Dhabi balances the Emirate's strong financial position and prudent policies against geopolitical risks, rising contingent liabilities, and potential impediments to growth stemming from undeveloped institutions. Significantly reduced geopolitical risk would be important in raising the rating in the future. Conversely, a sustained worsening of political and event risks, or a significant and sustained erosion of the government's asset position, would put the government's creditworthiness under pressure.

Bahrain (Kingdom of)

PRIMARY CREDIT ANALYST: REMY SALTERS, LONDON (44) 20 7176 7113, REMY_SALTERS@STANDARDANDPOORS.COM

SECONDARY CREDIT ANALYST: LUC MARCHAND, LONDON (44) 20 7176 7111, LUC_MARCHAND@STANDARDANDPOORS.COM

ISSUER CREDIT RATING (FOREIGN AND LOCAL CURRENCY): A/STABLE/A-1

PUBLICATION DATE: DECEMBER 17, 2008

Rationale

The ratings on the Kingdom of Bahrain reflect the government's net financial asset position and strong international alliances. These factors provide a counterbalance to high geopolitical risks (relative to the majority of other rated sovereigns), the Bahraini economy's vulnerability to external shocks, and the secular decline of its hydrocarbon resources.

Net of deposits, minority stakes in quoted companies, and other financial assets, we estimate the general government's net asset position at 24% of GDP in 2008. This is sharply down from estimates of around 65% a year ago, owing to the inclusion of only the most liquid assets, as well as past opacity on the composition of asset holdings. Nevertheless, it still compares well with a median net debt position of 22% of GDP for Bahrain's 'A' rated sovereign peers. Oil revenues were conservatively budgeted on the basis of a $40 oil price in 2008, and we expect there to be a general government surplus (including extra-budgetary expenditures) of 5% of GDP. According to our forecast, however, the fiscal position will swing to deficits of 3% of GDP or above in the period to 2011. Oil and gas revenues account for about 80% of total fiscal revenues.

A well developed and closely regulated financial system mitigates Bahrain's vulnerability to shifts in the real estate and stock markets. Some institutions have been affected by deleveraging in developed markets, but the main impact is likely to be felt via a slowdown in the important financial sector and wider economic activity. We assume per capita GDP growth near 3% over the next two years, but there are significant downside risks, particularly if financial services are more severely impacted and petroleum prices continue weakening.

Structural reforms continue, with a recent focus on the labor market, as well as the rationalization of public asset management. On the fiscal side, the ratio of expenditure to GDP has been declining in recent years. Further economic diversification remains a key structural need, particularly given the challenge of boosting private sector employment growth for Bahrainis as large cohorts enter the labor market in coming years.

Background geopolitical risks, and their possible ramifications for domestic stability, are partly mitigated by strong international alliances. Despite past efforts at political reform, the Shia majority remains disaffected with the Sunni-dominated government, and there could be further localized disturbances.

Outlook

The stable outlook balances the fiscal and external asset positions (notwithstanding significant issues surrounding data) against political risks, diminishing oil resources, and the challenge of carrying through structural reforms needed for economic diversification, in particular in education and the labor market. Success in improving human capital to underpin sustainable growth, addressing long-term energy needs, and reducing the pace of current expenditure growth could have a positive effect on the ratings. Conversely, the ratings would come under pressure if there was a sustained deterioration in fiscal or economic performance, or if reforms were to be postponed. The global financial crisis will pressure economic performance, via financial sector activity and a likely real estate correction, but we expect that the impact on systemic risk will be contained

Kuwait (State of)

PRIMARY CREDIT ANALYST: LUC MARCHAND, LONDON (44) 20 7176 7111, LUC_MARCHAND@STANDARDANDPOORS.COM

SECONDARY CREDIT ANALYST: FAROUK SOUSSA, PHD., DUBAI (971) 4709 6820, FAROUK_SOUSSA@STANDARDANDPOORS.COM

ISSUER CREDIT RATING (FOREIGN AND LOCAL CURRENCY): AA-/STABLE/A-1+

PUBLICATION DATE: MAY 19, 2009

Rationale

On May 19, 2009, Standard & Poor's Ratings Services affirmed its 'AA-/A-1+' sovereign credit ratings on the State of Kuwait. The outlook is stable.

The ratings on the State of Kuwait are supported by the sovereign's rich resource endowment which, combined with prudent policies, has enabled Kuwait to build very strong external and fiscal balance sheet positions in recent years. In our view, these strengths comfortably balance some short-term risks linked to the decline in oil prices, oil production cuts and lower non-oil real GDP growth, and increased contingent liabilities from the financial system.

Net external assets—primarily the accumulation of oil revenues held externally through Kuwait's sovereign wealth fund—are projected to reach 425% of current account receipts (CARs) in 2009, underscoring robust external balances. On the fiscal side, the government's net asset position is similarly robust, projected at about 250% of GDP by year-end 2009. These ratios are among the highest for sovereigns rated by Standard & Poor's, and firmly place the ratings on Kuwait in the 'AA' category.

Despite the decline in oil prices, the general government budget in Kuwait should, in our view, again record a surplus of about 12.3% of GDP in fiscal 2009–2010, down from an estimated 17.9% in 2008–2009 (including investment income). Moreover, the government debt burden is light, and paper is issued mainly for monetary policy purposes. With the impact of the cut due to OPEC quotas and slowdown of non-oil growth, overall GDP growth is forecast to turn to negative 1.0% in 2009, before recovering at about 2.3% in 2010.

Politics in Kuwait remain complex. Following the dissolution of parliament by the Emir in March, elections held in mid-May yielded few surprises and the political scene is likely to remain unchanged in the medium term, with frictions between the conservative parliamentary majority and the government significantly curtailing policy-making.

We expect that the recently enacted Financial Stability Law will be ratified by parliament. The plan is aimed at bolstering the financial system, which has been negatively affected by the global financial downturn. But Kuwait stands out among peers in not providing any additional fiscal boost to the economy. Indeed, the 2009/2010 budget envisages a 36% fall in expenditure, including a 24% decrease in capital expenditure. Although most of these cuts reflect a reduction in one-off expenditures that was present in the previous budget, it is clear that no additional fiscal stimulus was provided through the new budget. A number of planned infrastructure projects in the oil sector have been cancelled in recent months. While prudent from a fiscal viewpoint, these policies threaten, in our view, to exacerbate the cyclical downturn in the medium term given the predominance of government in economic activity.

Regional geopolitical risks remain high and weigh on the ratings. These risks are, however, partially mitigated by good international alliances, relative domestic social stability, and government assets.

Outlook

The stable outlook on Kuwait balances the government's strong financial position against elevated regional geopolitical risks, increased contingent liabilities and potential impediments to growth. Significantly reduced geopolitical risk would be important in raising the rating in the future. A stabilization of the relationship between the government and the parliament along with a political consensus on accelerating both private domestic and foreign investments should, in our view, alleviate major impediments to growth and would be a plus for the rating. Conversely, a sustained worsening of political and event risks, or a significant and sustained erosion of the government's asset position, could put Kuwait's creditworthiness under pressure.

Oman (Sultanate of)

PRIMARY CREDIT ANALYST: LUC MARCHAND, LONDON (44) 20 7176 7111, LUC_MARCHAND@STANDARDANDPOORS.COM

SECONDARY CREDIT ANALYST: REMY SALTERS, LONDON (44) 20 7176 7113, REMY_SALTERS@STANDARDANDPOORS.COM

ISSUER CREDIT RATING (FOREIGN AND LOCAL CURRENCY): A/STABLE/A-1

PUBLICATION DATE: MARCH 12, 2009

Rationale

The ratings on the Sultanate of Oman are supported by the government's strong fiscal position, together with the country's solid external finances and increasing wealth levels. They remain constrained by a heavy economic dependence on hydrocarbons, geopolitical tensions in the region, and, in the longer term, comparatively low visibility regarding policy direction under a succession scenario.

The government has prudently and transparently managed the windfall from a sustained period of high oil prices, leading to a general government surplus that we estimate at 8.8% of GDP in 2008. With the surpluses of the past few years, the general government's net asset position increased to about 42% of GDP at year-end 2008. This will be a crucial buffer to weather the negative impact on public finances of the expected sharp decrease in average oil prices in 2009. The general government budget will turn into a deficit of 4.9% of GDP, decreasing its estimated liquid assets (mostly managed externally) to an approximate $25 billion from about $27 billion in 2008. Government debt remains modest at an estimated 6% of GDP in 2009.

The Sultanate's external accounts and wealth levels have also strengthened. Net external assets are likely to reach 140% of current account receipts by 2009, while GDP per capita is projected to approach $16,244 by 2009, compared with less than $10,000 as recently as 2004.

After years of steady decline, the production of oil and condensates increased in 2008 and could increase moderately in 2009. Although a lasting stabilization or increase of oil production is not yet assured, the hydrocarbon sector has been boosted by increased liquefied natural gas (LNG) output. More fundamental diversification is provided by the strong growth of the tourism sector and new industrial facilities, many of which are owned by the private sector. The importance of gas feedstock in many of the planned industrial facilities, however, may act as a constraint if natural gas reserves disappoint on the downside. Successful diversification is all the more important as the country's demographic profile will require sustained job creation for the foreseeable future.

The ratings on Oman remain constrained by a high economic dependence on hydrocarbons, which constitute the vast majority of fiscal revenues and exports, and about 51% of GDP in 2008. On the political front, the key challenges to creditworthiness remain a high level of unemployment among Omanis and the prevailing geopolitical tensions across the region. We see inflationary pressures abating with the weakening of the economy, with an economic rebound expected to begin next year.

Outlook

The stable outlook is based on our expectation that the high level of government assets, the expected increasing LNG exports, and the growth of the nonhydrocarbon sector will continue to mitigate concerns stemming from the current decline in oil prices and the recent years' decline in crude oil production. The outlook also assumes that fiscal policy will remain oriented toward fulfilling Oman's development needs and limiting vulnerability to fluctuations in oil production and prices.

The ratings could be raised if the historical decline in crude oil output was reversed or if the government strengthened its domestic tax revenue base significantly—through the introduction of VAT, for example. Conversely, the ratings could come under downward pressure if the geopolitical or domestic political situation were to deteriorate sharply, or if government assets were to decline more quickly than we forecast.

Qatar (State of)

PRIMARY CREDIT ANALYST:
VERONIQUE PAILLAT-CHAYRIGUES, PARIS (33) 1 4420 6781, VERONIQUE_PAILLAT-CHAYRIGUES@STANDARDANDPOORS.COM

SECONDARY CREDIT ANALYSTS: FAROUK SOUSSA, PHD., DUBAI (971) 4709 6820, FAROUK_SOUSSA@STANDARDANDPOORS.COM
LUC MARCHAND, LONDON (44) 20 7176 7111, LUC_MARCHAND@STANDARDANDPOORS.COM

ISSUER CREDIT RATING (FOREIGN AND LOCAL CURRENCY): AA-/STABLE/A-1+

PUBLICATION DATE: FEBRUARY 20, 2009

Rationale

The ratings on Qatar are supported primarily by strong fiscal and external balance sheets, healthy economic prospects driven largely by the gas industry, and high per capita income. The ratings remain constrained by the geopolitical risks facing sovereigns in the Gulf region, and the country's capacity and institutional constraints which are higher than for other 'AA' rated sovereigns.

We expect Qatar's fiscal and external performances to remain strong, although 2009 should see lower surpluses than in previous years owing to declining energy prices. We project a healthy general government surplus of about 2.3% of GDP in fiscal year 2009–2010 (ending March 31, 2010), against an expected surplus of 17% of GDP in 2008–2009. With very low debt and large estimated assets in the various government funds, the state is expected to record a net asset position of about 54% of GDP in fiscal 2009–2010, compared with a 4% net debt position for the 'AA' median. On the external side, export revenues will drop sharply in 2009, and we expect the current account surplus will narrow to about 12% of GDP in 2009, down from an estimated 42% in 2008, before recovering to about 32% of GDP in 2010. External liquidity will remain abundant, also boosted by large investments inflows.

Despite rapid population growth, Qatar's GDP per capita, estimated at $80,300 in 2009, is among the world's highest—an impressive increase from $27,000 in 2001. The real economy is expected to continue booming at growth rates of above 10% annually over 2009–2011, compared with an estimated 17.6% in 2008, despite the deceleration in non-oil GDP growth. The key growth driver when growth elsewhere in the region subsides will be the near doubling of Qatar's already substantial output of liquefied natural gas. That said, the anticipated 50% drop in energy prices will weigh heavily on the nominal value of oil and gas output and we expect the economy to contract in dollar terms.

We expect inflation to ease to about 8% in 2009 and 2010 as global commodity prices fall, as the U.S. dollar strengthens, and as new property projects are completed, partly alleviating the country's severe housing shortage. This will ease capacity constraints that, combined with an expansionary budget, have fueled a jump in inflation to an average of 15.1% in 2008.

Despite improvements, accountability, transparency, and oversight of policy-making remain significantly weaker in Qatar than in most 'AA' rated sovereigns.

The geopolitical risks that Gulf States face remain the primary constraint on the ratings. Qatar is in a particularly delicate position with respect to Iran: it houses the large U.S. military presence on its soil while trying to adopt a moderate approach toward Iran, with which it shares the giant North Field gas reservoir. However, we consider that the risk of a U.S. attack on Iran, thus the risks to Qatar's hydrocarbon assets, has receded in light of the new U.S. administration's foreign policy.

Outlook

The stable outlook on Qatar balances the government's success in maintaining strong economic and fiscal performances against serious regional geopolitical risks.

Upward ratings momentum will depend primarily on the evolution of regional geopolitical risks. If there is progress in containing geopolitical pressures, institutional reforms remain on track, and economic growth continues, combined with further improvements in the general government net asset position, we could consider raising the ratings. Conversely, if geopolitical risk heightens, downward pressure on the ratings is possible.

Ras al Khaimah (Emirate of)

PRIMARY CREDIT ANALYST: FAROUK SOUSSA, PHD., DUBAI (971) 4709 6820, FAROUK_SOUSSA@STANDARDANDPOORS.COM

SECONDARY CREDIT ANALYST: BEN FAULKS, LONDON (44) 20 7176 7108, BEN_FAULKS@STANDARDANDPOORS.COM

ISSUER CREDIT RATING (FOREIGN AND LOCAL CURRENCY): A/STABLE/A-1

PUBLICATION DATE: FEBRUARY 17, 2009

Rationale

The ratings on the Emirate of Ras Al Khaimah (RAK), the northernmost of the seven emirates that comprise the United Arab Emirates (UAE), rest primarily on ongoing support from the federal government of the UAE and the likelihood of extraordinary support in the event of financial stress. The federal government, funded mostly by Abu Dhabi and underpinned by that emirate's oil wealth, meets almost all the current expenditure costs of the seven emirates that make up the UAE, while major capital costs are also borne at the federal level. Individual emirates, including RAK, have limited fiscal obligations—primarily related to local infrastructure and services and capital spending to develop emirate-level projects—and consequently substantial fiscal flexibility. In addition, the financial capacity of the UAE and the larger emirates, in particular Abu Dhabi, is ample to cover RAK's modest liabilities.

The ratings are underpinned by the relatively strong wealth enjoyed by RAK citizens, with GDP per capita expected at $16,200 in 2009, in line with the 'A' median (as in other Gulf sovereigns, this ratio is distorted by the presence of non-national workers who make up 58% of the population). Moreover, RAK's growth prospects appear relatively stable, with the overhaul of economic strategy since the appointment of Sheikh Saud bin Saqr al-Qasimi as Crown Prince in 2003 resulting in a substantial rise in investment and diversification of the economic base. RAK's modest debt represents around 24% of GDP at year-end 2008 and, taking into account the government's holdings of liquid assets, boasts a general government net asset position that we estimate at around 8% of GDP. That said, the predominance of equity stakes in local companies raises uncertainties over the valuation and liquidity of the portfolio in the event of domestic stress.

RAK's small, homogenous population, with relatively easy access to the ruling family, points to a more stable domestic political scene than in some regional peers. RAK's exposure to economic developments in the larger emirates and the region as a whole is a constraint on the rating. Strong economic growth in the region, and in particular the UAE, has been the principal driver of fast-rising demand for RAK's main industrial and mining products—cement, aggregate, ceramics, and glass—while the success of RAK's rapidly developing tourism and real estate sectors depends on continued strong demand for these services in the region, and in particular in Dubai. The recent decline in global and regional demand, including the cancellation of a number of construction projects in Dubai, will have an impact on RAK's near-term growth, although we expect an increase in demand from Abu Dhabi and other regional growth markets in the coming year to help offset some of the impact. We expect growth to slow to less than 5% in 2009, from an average of 10% over the previous three years.

Outlook

The stable outlook reflects the balance between the risks posed by geopolitical issues and RAK's exposure to the economic fortunes of the larger emirates and the broader region, with the near certainty of continued ongoing support from the federation and the strong likelihood of extraordinary support from the federation (backed by Abu Dhabi). Downward pressure on the rating could result from a deterioration in RAK's economic prospects beyond the decline we have projected for 2009, or a deterioration in Abu Dhabi's creditworthiness, which could affect our assessment of likely support to RAK from the federation. A positive rating action could follow an easing of regional geopolitical tensions, the successful implementation of RAK's development strategy, particularly with regard to real estate and tourism, or an improvement in Abu Dhabi's creditworthiness.

Saudi Arabia (Kingdom of)

PRIMARY CREDIT ANALYST: FAROUK SOUSSA, PHD., DUBAI (971) 4709 6820, FAROUK_SOUSSA@STANDARDANDPOORS.COM

SECONDARY CREDIT ANALYST: BEN FAULKS, LONDON (44) 20 7176 7108, BEN_FAULKS@STANDARDANDPOORS.COM

ISSUER CREDIT RATING (FOREIGN AND LOCAL CURRENCY): AA-/STABLE/A-1+

PUBLICATION DATE: APRIL 30, 2009

Rationale

The sovereign credit ratings on the Kingdom of Saudi Arabia primarily reflect the government's strong external and fiscal positions. Driven by high oil receipts over the past few years and the cautious approach of the Saudi Arabian Monetary Agency (SAMA) towards foreign reserves management, foreign reserves and liquid foreign assets managed by the SAMA stood at $438 billion at year-end 2008 (up from $136 billion in 2004), which is sufficient to cover about 33 months of current account payments (including private transfers). Furthermore, the central government has no external debt and has no plans to incur any.

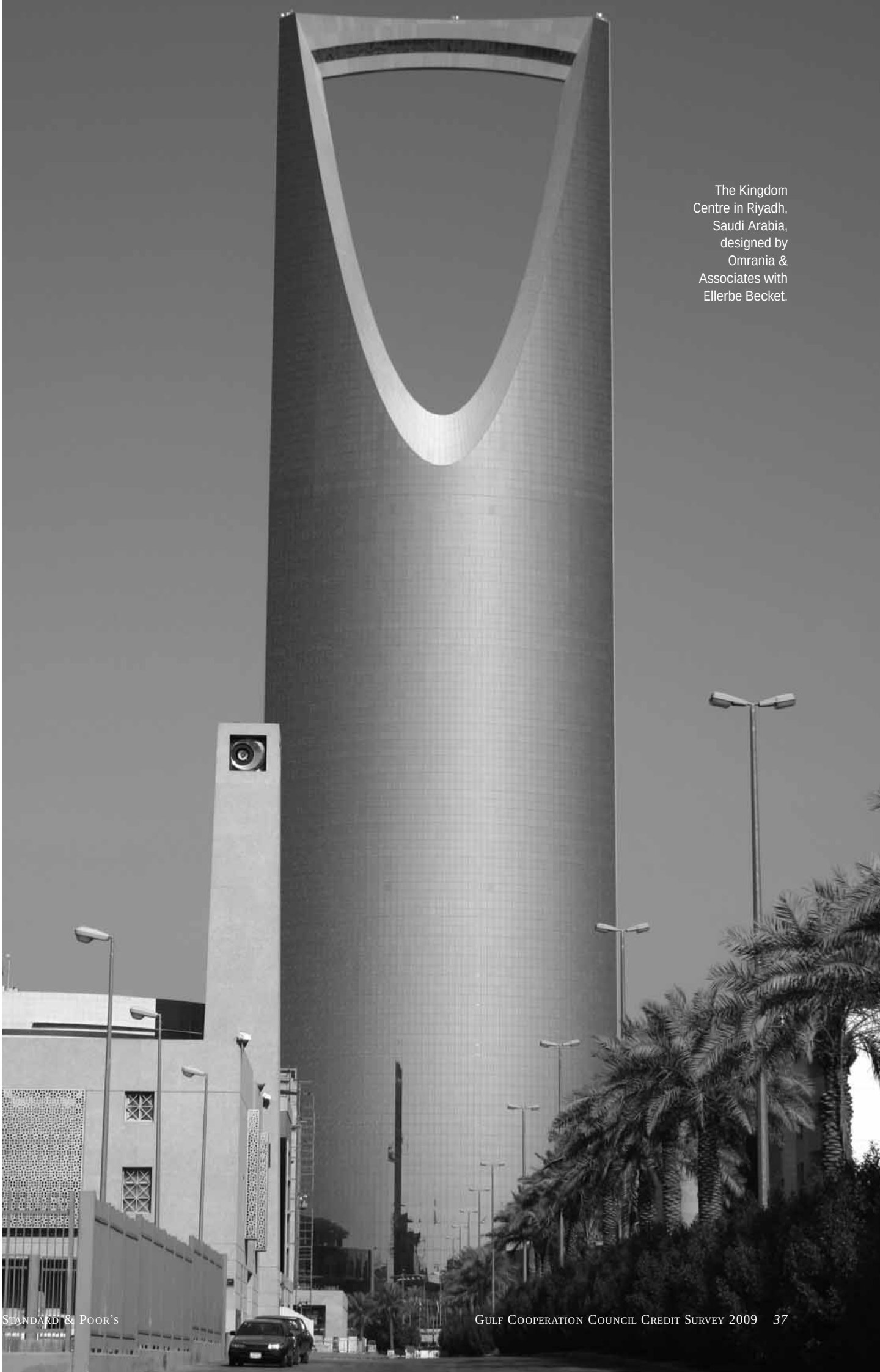
We expect fiscal outturns to weaken in 2009, in line with falling oil prices and revenues, and the government's deliberate countercyclical expansionary fiscal policy, with total expenditure expected to rise by 16% relative to the 2008 budget. Importantly, a large part of that rise will be due to greater infrastructure expenditure, which is budgeted to increase by over 36% in 2009. As a result, the general government balance, which has averaged a surplus of over 20% in the past four years, is expected to reverse to a deficit of almost 7% of GDP in 2009. We consider that Saudi Arabia has ample fiscal space to absorb this level of fiscal deficit in the medium term, with a general government net asset position of around 170% of GDP expected in 2009.

We believe Saudi Arabia's main domestic challenge is dealing with the country's demographic dynamics. One-half of the population is under 21, and thousands of youths enter the labor market each year, yet foreign workers are filling the vast majority of the new jobs created on the back of the current investment surge. These positions are either undesirable to Saudis (such as in construction work), or require skills that not many possess. In response, the authorities, often in partnership with the private sector, have established a number of new further education institutions and revived the overseas scholarship program. How successful these measures will be in increasing employment among nationals is yet to be seen, but the issue remains a top government priority. We believe that failure to resolve the unemployment problem may trigger mounting social pressures.

The ratings on the Kingdom are constrained mainly by the high levels of external geopolitical risks that affect all countries in the Gulf region. Continued tensions in Iraq and, more importantly, Iran, pose political and economic risks. In our opinion, although Saudi Arabia's stability is unlikely to be threatened, even in the event of conflict between Iran and the U.S. or Israel, any tensions could cause uncertainties that impede future investment and growth.

Outlook

The stable outlook reflects Saudi Arabia's exceptionally strong balance sheet and the government's success with its ambitious and broad-based reform effort on the one hand, and high regional geopolitical risks on the other. The ratings are likely to be raised if regional geopolitical risks abate or if progress is made in addressing social issues, particularly unemployment. Conversely, the sovereign's creditworthiness could come under downward pressure should there be a reversal in the fiscal discipline so far adhered to by the government, should the debt burden increase significantly, external liquidity be impaired, or domestic and regional political risks increase.



The Kingdom Centre in Riyadh, Saudi Arabia, designed by Omrania & Associates with Ellerbe Becket.

How The Credit Market Crisis Is Changing The World Of Banking



Executive Summary

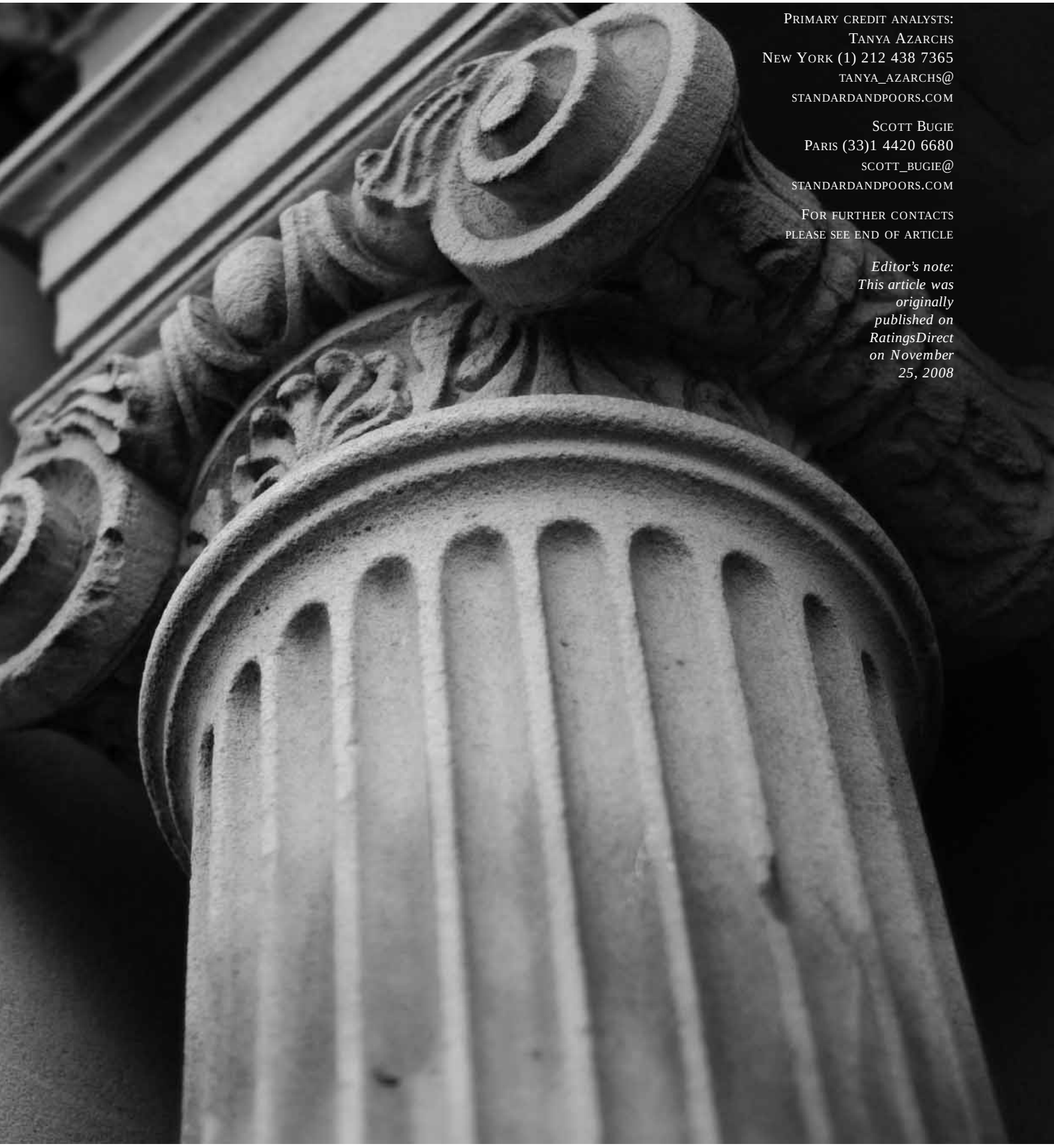
PROSPECTS FOR THE GLOBAL FINANCIAL system have rarely looked bleaker than they have for the past four months.

With the credit markets all but shut down and confidence in financial institutions seriously eroded, in Standard & Poor's Ratings Services' opinion, the concerted actions of governments worldwide have been instrumental in pulling the financial system back from the brink of a massive global collapse.

Even if capital markets stabilize, the impact on the real economy—on consumers and corporations—from the contraction in financing and from asset price declines that have already occurred will likely cause more delinquencies and defaults on loans. We expect that, in turn, to bring more earnings and other balance-sheet pressures on banks than they experienced during the troughs of most previous credit cycles.

This damaging series of events is already leading to the most profound changes in the banking industry since the Great Depression. Among the forces that appear likely to alter the nature of the financial services industry significantly are increasing calls for regulation, a wave of bank consolidations as stronger institutions acquire the seriously weakened, and a newfound coordination of global regulatory and central banking initiatives.

These changes, and our view that the global economy's outlook is worsening, are leading us at Standard & Poor's to reassess our view of the creditworthiness of financial institutions. It appears to us that the levels of losses for banks will be much greater than we originally envisioned in our ratings. Thus, our assessment of future industry risk is more pessimistic. In addition, we now believe that funding markets may be prone to periods of illiquidity in the future. Therefore, we are reassessing what we see as the vulnerability of the wholesale-funded banking model. >



PRIMARY CREDIT ANALYSTS:
TANYA AZARCHS
NEW YORK (1) 212 438 7365
TANYA_AZARCHS@
STANDARDANDPOORS.COM

SCOTT BUGIE
PARIS (33)1 4420 6680
SCOTT_BUGIE@
STANDARDANDPOORS.COM

FOR FURTHER CONTACTS
PLEASE SEE END OF ARTICLE

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On the other hand, governments have demonstrated a willingness to provide extraordinary support in the face of the market crisis to a degree that we had not previously anticipated. We will consider all of these factors in a global review of major mature-market financial institutions, which we expect to complete by year-end. In our analysis, we will look at individual institutions' prospects for deteriorating financial performance, but also recognize the significant support governments are providing to these banks. We believe that there could be negative rating actions as a result of this review, but they will likely be tempered by the reflection of government support.

The Factors Shaping The Future Of Banking

Governments generally are taking unprecedented actions more or less in concert worldwide to bring order to the banking sector. Seeking to restore confidence in financial institutions, they have backstopped the markets for repurchase agreements (repos), term loans, and commercial paper. Governments have allowed financial institutions to borrow against a wide variety of collateral to ensure the flow of funding, even as the credit markets retreated. Governments have recapitalized, and even nationalized, banks, and have offered to guarantee bank debt, generally during the next three years. At some point, we believe countries will seek to wean the sector off of these support mechanisms and search for ways to prevent another such crisis. We believe it will be difficult for governments to remove support until the financial markets have stabilized.

As a result of the market upheavals and the response of governments worldwide, we believe several factors will combine to change the face of the banking industry:

- Increased regulation;
- Consolidation of weaker entities;
- Fundamental reconsideration of the "originate to distribute" model;
- Adaptation to higher volatility; and
- Higher losses for this economic cycle.

Increased regulation is inevitable

In our view, the need for wide-ranging, extraordinary government support reflects the fragile state of the global banking industry. Calls for improvements in bank regulation are widespread. The recent government interventions reflect concerns that current bank capital, excluding government support, is not sufficient to carry the industry through the present, more stressful economic scenario.

Therefore, we believe that national regulators eventually may reevaluate the Basel II approach to assessing how much capital banks need to underpin credit risk amid extreme stress scenarios and risk in their trading and investment books. In the interim, regulators appear simply to be asking for higher capital ratios under the current methodology.

We believe other standards may change as well. Regulators and investors may require higher cash buffers, especially for wholesale-funded banks, as opposed to those that have substantial funding from retail deposits. They may also encourage less risk-taking, especially in banks' proprietary trading. Regulation of loan origination standards for residential real estate could facilitate the growth of covered bonds. All of these prudential standards, which will likely be the subject of worldwide policy deliberations, might help make the banking industry less risky, though it is too early for definitive conclusions.

We expect more types of previously unregulated financial institutions to come under bank regulatory oversight. In the U.S., for example, authorities are incorporating the large securities firms into the bank regulatory framework, and other finance companies, such as American Express Co., CIT Group Inc., and GMAC LLC, are also applying to become bank holding companies. In our view, this would be a positive factor in our industry risk assessments because the current two-tier system of regulated and unregulated institutions can create different sets of rules and irrational competition.

On another level, as part of their responsibilities as watchdogs for the financial system, the regulatory bodies may become more critical. Governments' roles in preventing periodic market seizures and crises of confidence that will likely arise may become permanent. Regulators may begin to favor more countercyclical reserves and measures to keep bubbles from forming, however difficult that is to achieve as a practical matter. Almost certainly, governments will attempt to improve the infrastructure of the securities markets to reduce systemic risks, possibly creating central clearinghouses for credit derivatives to reduce counterparty risk.

"In our view, the need for wide-ranging, extraordinary government support reflects the fragile state of the global banking industry. Calls for improvements in bank regulation are widespread."

CONSOLIDATION OF WEAKER ENTITIES

The downturn in the banking industry so far has spurred a wave of consolidation, often hastily arranged with government backing and rock-bottom prices. We believe more consolidation will occur as stronger groups absorb weaker institutions that are unable to survive the recession as independent entities. The stronger financial conglomerates can take advantage of "bargain prices". Some of this consolidation may be opportunistic and pragmatic. It may create banking groups so large and diversified that their failure would be unthinkable, increasing the potential need for government support in the future.

When conditions return closer to normal, this consolidation may lead to even wider differences in creditworthiness between the large, systemically important banks and the smaller institutions. The current ratings differential among regulated banks in certain mature-market economies is compressed because the smaller banks in these countries typically have not had the same problems as the large ones.

However, not all indicators point to consolidation in financial services. Some types of businesses (e.g., balance-sheet-intensive forms of investment banking, proprietary trading, and higher-risk securitizations) may become the province of a new breed of investment banking institution. We believe the larger hedge funds are building underwriting capacity and may be willing to buy big pieces of securitizations and make markets in certain high-risk securities. This could keep the competitive pressure on banks. Taken together with a focus on lower-risk activities and maintaining higher capital requirements, banks could look more like low-risk, low-return institutions.

At some point, regulators might consider the systemic risks that giant financial organizations pose to be unacceptably large and consequently seek to downsize the megabanks. In particular, the multinational model may prove awkward for regulators if they are forced to use their countries' tax revenues to rescue foreign operations. The markets may also pressure large, unwieldy institutions to break themselves up.

Near term, consolidation will likely happen either when stock prices have become very low or when governments offer assistance. Financing for acquisitions is difficult in the current market, and potential buyers' own stock prices are likely depressed. Even more important, given the general uncertainty surrounding asset values, acquirers are leery of potentially doubling up on their own risks by acquiring other troubled portfolios.

FUNDAMENTALLY RETHINKING THE "ORIGINATE TO DISTRIBUTE" MODEL

In our opinion, the fate of the securitization, or "originate to distribute," model is crucial to the industry's future returns. Robust liquidity conditions are critical to the securitization and syndicated loan markets. The ability to distribute risk means banks can put capital to use several times during the year rather than just once if banks retain these loans. This turnover of capital can boost banks' returns on equity (ROE). We believe that banks have not yet come to terms with the idea that they may have to keep their loan production entirely on their balance sheets. Nor do we think they are capitalized sufficiently to support the additional assets.

Securitization markets fund $10 trillion of assets in U.S. markets and $2 trillion in Europe. By comparison, U.S. banks have about $8 trillion of loans on their balance sheets. Bank balance sheets would have to swell dramatically to absorb all the assets that banks ordinarily securitize. Capital levels would have to climb even higher, even as banks now are trying to delever.

Thus, we believe the real reason banks are reluctant to retain loans is that the ROE for stand-alone loans is not at the level banks are used to. Historically, equity investors who paid 2x-3x book for a bank expected an ROE of more than 18%. Therefore, banks and investors will likely have to get reacquainted with the 14% ROEs they had 20 years ago.

In our opinion, there could be numerous ripple effects if this phenomenon occurs, ranging from reduced access to capital to higher loan pricing, which could limit borrowers' access to funds. This could restrict economic growth. Conversely, there may be other ways to "restart" the securitization markets, perhaps through primary securitization with more conservative standards, or with government support. The U.S. Treasury, for example, recently allocated a portion of the Troubled Asset Relief Program facility to guarantee the 'AAA' tranches of consumer securitizations (those backed with credit-card loans, auto loans, and student loans). We believe that several governments will try various schemes to restart the securitization markets that many observers believe are crucial to the future availability of credit.

"We believe that the turbulence in, and seizing up of, the debt markets during the past year may occur more frequently in the future if regulatory regimes are not aligned."

Governments may also impose new regulations on underwriting standards to underpin credit quality, like those incorporated in the European covered bond rules. So it seems to us that the "originate to distribute" model will remain viable, if to varying degrees in different regions. Securitization should revive, though it may be less aimed at reducing capital requirements and more on-balance-sheet, like covered bonds.

Current loan pricing indicates that wider spreads will likely compensate for some of the lower velocity of capital and higher capital requirements. We are skeptical that these will stick in more benign economic environments. More likely, banking will become a lower-risk, lower-volatility, but lower-return business. As long as risk-adjusted returns are strong, we don't believe we'll need to lower bank ratings. In any case, emphasizing in our credit analyses capital and risk-taking would naturally deemphasize the earnings component of a bank's credit profile. Banks' earnings are cyclical, so we believe the real issue is banks' potential losses in a recession and whether they have sufficient capital to withstand them.

Adapting to greater volatility

In many respects, the credit markets haven't had a crisis like the current one since the Great Depression. The dislocation of 1998 was comparatively limited in scope and duration, although in hindsight, it may have been a preview of what could come. It is now evident that the interconnection of the global financial system facilitates the transmission of troubles in one jurisdiction or market to others and increases the potential for system-wide upheavals. Securities are widely distributed to investors without regard to national boundaries, which made the global sale and acceptance of higher-yielding but new and sometimes untested instruments that much easier.

Similarly, synthetic equivalents—mostly in derivatives form—to cash instruments provide greater liquidity and greater pricing transparency on a variety of market instruments, but they multiply the number of players exposed to the risks in question. Funding is sourced worldwide, so that problems in one area can result in a withdrawal of liquidity in others. This interconnectedness seems to be one cost of a modern and global financial system. We believe that the turbulence in, and seizing up of, the debt markets during the past year may occur more frequently in the future if regulatory regimes are not aligned.

Higher losses for this economic cycle

We believe that the trough in many countries' business cycles during the next two years will be more severe than in previous cycles. This is because the economic expansion that preceded the current downturn created a significant overhang of debt in many countries, particularly in the household, construction, and leveraged loans segments. The ensuing dislocation in credit markets, and particularly the freeze in the securitization markets that had been dubbed by some commentators a "shadow banking system" because it became a substantial provider of credit, is intensifying the impact of what would otherwise be a reduction of excess debt.

Indeed, in the U.S., a painful correction in the household sector is already well under way. This downturn appears particularly difficult for the financial industry because, in addition to the asset-quality downturn, banks must manage a contraction of the structured finance markets and depressed capital markets that hurt their investment-banking businesses.

Implications For Ratings On Financial Institutions

The rapidly shifting operating environment for financial institutions has several implications for their creditworthiness:

- Our perception of industry risk is higher;
- We believe extreme high and lows in the credit cycle result in larger losses during the trough;
- Franchise stability and market confidence are critical components of credit;
- We will focus more on capital;
- Government support becomes explicit in our ratings;
- We view certain classes of securities as riskier.

Industry risk is higher

Industry risk is an important element of our analytical criteria (see "S&P's Banking Industry Country Risk Assessments: Global Annual Roundup," published on RatingsDirect Aug. 9, 2007). Among the factors in the operating environment that can affect bank stability are the competitive dynamics of the institutions in the market; the legal and regulatory framework governing critical aspects of financial institutions' behavior

and that of their customers; and the condition of borrowers. The lessons learned from the still-evolving financial crisis have led us to raise our assessment of bank industry risk. This will depress our stand-alone ratings on the banks. We believe more volatility in funding markets is likely, and with it an increase in the probability of systemic risk. Some of that will likely be triggered by volatility in asset prices that raises issues of confidence in bank balance sheets for market participants.

Also, although we don't believe that accelerating lifetime losses into current marks to market of the balance sheets is the right way to analyze loan books, we recognize that market participants frequently do so. We believe that can destabilize financial institutions in periods of financial stress. More near-term, access to capital and funding outside of government support is very difficult. Higher capital requirements and poor economic prospects could also depress returns and limit access to capital.

At the same time, we recognize that certain trends, if they materialize, may enhance financial institutions' creditworthiness. A more concentrated industry of more broadly diversified institutions should produce greater stability, ensuring government support for these larger, more systemically important banks. Certain weaker institutions with the riskiest practices are failing or are being acquired. This could support more rational risk pricing and help boost returns, at least temporarily. Higher capital levels in relation to risks are clearly also conducive to improved creditworthiness. These factors could eventually result in higher ratings.

Extreme highs and lows in the credit cycle result in greater losses during the trough

The protracted nature of the market dislocation and the rapidity and severity of asset deterioration have stressed financial institutions' earnings capacity and levels of capitalization. As a longer global recession becomes more probable, we expect higher levels of stress than those experienced during a typical business-cycle trough. This has the potential to change our ratings significantly.

To assess this critical element, we are projecting the losses we envision for financial institutions in mature market economies. We expect higher-than-typical losses for certain loans in U.S. institution portfolios (see "Rated U.S. Banks Likely To Weather Market Difficulties," published May 6, 2008, on RatingsDirect), and more ordinary peak-of-cycle losses elsewhere. Financial institutions with greater proportional exposures to riskier assets will likely suffer proportionally greater loan losses. Applying our loss projections of individual bank asset exposures will be important in differentiating bank creditworthiness.

Franchise stability and market confidence are critical components of credit

Our fundamental criteria on assessment of liquidity focus on the stability of funding sources, where core retail deposits are preferable to wholesale sources of funds, particularly if they are short term. However, we are reassessing the value of the mitigants to a reliance on wholesale funding: diversity of funding sources, asset liquidity, and matching of funding sources to asset liquidity. In light of our assessment that capital markets will be more prone to volatility in the future, we will have less tolerance in the ratings for reliance on short-term wholesale funding, and for relative confidence sensitivity of financial institutions' business models.

In our view, franchise stability and market confidence are important in the financial sector. Although most financial institutions are vulnerable to an erosion of confidence (because they are typically highly levered and fund most of their assets with debt), some wholesale banks and nonbank finance companies are more vulnerable than others depending on their business models and funding mix. For instance, specialist lenders that depend on short-term wholesale funding and financial institutions with large trading operations are particularly sensitive to an erosion of confidence.

Although we have always differentiated by institution type with regard to funding, we intend to apply the lessons learned during this dislocation to our analysis. Factors that indicate the relative degree of confidence sensitivity are:

- How much the bank's business model depends on a perception of strong creditworthiness (the higher the dependence, the more confidence-sensitive an institution is likely to be);
- Simplicity/transparency versus complexity/opacity of accounts (simple and transparent institutions are less confidence-sensitive than are complex and opaque institutions);

- Existence of explicit credit triggers in derivatives contracts and borrowing agreements (e.g., when collateral requirements increase upon a ratings downgrade);
- Wholesale versus retail funding (the higher the proportion of wholesale funding to total funding, the more confidence-sensitive an institution is likely to be).

We believe that financial institutions most exposed to volatile markets and loss of investor and counterparty confidence will likely continue to be vulnerable to loss of market access. Consequently, "sudden default" risk will likely remain a characteristic of financial institutions, although the significant measures of governments around the world to shore up funding markets should reduce this risk to some degree.

The investment banking businesses of securities trading and prime brokerages are particularly confidence-sensitive, because they require a high volume of daily cash, securities, and derivative transactions with counterparties to maintain inventory positions. Counterparties of these business lines want to be confident that trades will be settled in accordance with industry norms and that obligations under derivative contracts, including those to post collateral, will be met. A critically damaging development for investment banks is a loss of access to daily cash and derivative transactions at any price or collateral haircut.

Of course, for all banking institutions, a worst-case scenario due to erosion of confidence is a significant outflow of wholesale or retail customer deposits (a bank run). In our opinion, various governments' recent actions to raise or enact retail deposit protections, albeit temporarily, largely allay the concerns about bank runs.

Increased focus on capital adequacy

Banks worldwide have raised more than $500 billion of private capital in the form of equity and hybrid capital during the past 18 months. In light of the massive capital infusions and possible failings in regulatory measures of capital sufficiency (Basel I, II), we are placing more emphasis on risk-adjusted capital (RAC) measures. We are developing our own framework for assessing RAC that is more risk-sensitive than Basel I and more conservative in most cases than Basel II as it currently stands, particularly with regard to market risk capital and private equity risk (see "S&P Requests Comments On Its Global Risk-Adjusted Capital Framework For Financial Institutions," published April 15, 2008, on RatingsDirect).

Government support becomes explicit

Partly because of the confidence-sensitive nature of the banking industry, particularly in the context of highly developed capital markets, we view ongoing support from government authorities as an essential part of bank creditworthiness in good times and bad (see "External Support Key In Rating Private Sector Banks Worldwide," published Feb. 27, 2007, on RatingsDirect). This principally comes through prudential regulation and access to central bank liquidity, which mitigate the high leverage and funding mismatches inherent in bank business models. Without these benefits, bank balance sheets would be very different. We build this type of support in to our stand-alone ratings on banks in supportive countries. In our view, it is neither possible nor appropriate analytically to fully disentangle bank stand-alone creditworthiness from everyday external government support factors.

A stand-alone rating reflects a bank's strategies, performance, and prospects, including whatever government support or intervention the bank typically receives in the normal course of business. However, it excludes credit for any extraordinary government assistance or influence that might be expected in a crisis.

Due to the worsening situation in the financial sector, governments, central banks, and regulators in most mature economies have taken a wide range of support measures to alleviate funding constraints and bolster depositor confidence. These measures underpin the creditworthiness of most banks operating in those countries, and are consistent with our classification of the governments as "supportive" in that they promote system-wide stability through the regulatory, legal, and liquidity frameworks that delimit bank operations. Therefore, our stand-alone ratings also integrate these system-wide measures introduced to address near-term liquidity and funding concerns.

Excluded from our stand-alone credit analysis, however, is future specific government intervention for financial institutions under stress. Recently, many governments have

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intervened directly as a result of or in anticipation of deeper solvency pressures at specific institutions. This has taken the form of nationalization, direct investment, and promotion of private-sector mergers and acquisitions. We view the first two as the most meaningful and as indicators of a government's intention to provide further support.

When the actual or anticipated direct government aid is material and directed at a specific institution under stress, we typically lift the counterparty credit rating (CCR) of the aided institution above the institution's stand-alone creditworthiness. This will happen with increasing frequency for banks. In such cases, we intend to disclose the stand-alone ratings to better highlight the support we incorporate in the CCRs.

A banking institution's relative importance to a country's financial system and economy—its systemic importance—indicates the likelihood the institution will receive direct government support when under stress. To maintain stability in the financial sector, most governments have a policy objective to maintain the creditworthiness of systemically important banks at a level at which the banks can operate. That implies access to funding at a rate that permits an adequate spread on loans.

When governments directly aid specific financial institutions under stress, or make clear their willingness to support others that may require aid, we do not expect the CCR on the supported institutions to fall to a level that would preclude them from continuing profitable operations. Rather, as a result of increasing government support, we would expect to see fewer downgrades.

This means that, in cases of severe stress, the stand-alone rating may diverge substantially from the CCR. As governments withdraw direct aid (e.g., sell their bank shares) and the banks under severe stress convalesce, stand-alone ratings and the CCRs will converge (or the problem banks will not heal and be wound down). We expect this dynamic to play out during the next several years for many banking institutions.

Certain classes of securities look riskier

As we see new cases of resolutions of failed banks, and the way in which various classes of securities are dealt with, we may alter our ratings on those types of instruments to reflect different default probabilities. For example, we have traditionally rated investment-grade financial holding companies (excluding insurance company holding companies) one notch lower than their operating companies (two notches in noninvestment grade) to recognize the higher probability of default for the holding company. A stronger buyer may acquire the operating company in a regulatory-assisted transaction upon failure, whereas the holding company may be left behind.

In addition, on an ongoing basis, holding companies typically depend on the ability to upstream cash from their underlying subsidiaries, which regulators can curtail in the case of banks or brokers. We have seen no distinct pattern of resolutions that would cause us to change this notching convention at this time. In some instances holding-company creditors were distinctly disadvantaged, while in others both holding company and operating company creditors were rescued.

We expect regulators to balance the reactions of investors and the impact on confidence in the financial system with minimizing the cost of rescues for taxpayers. As we see different patterns emerge, and potentially more wholesale funding at the bank level treated more in line with that of the holding company, we will consider either widening or narrowing the notching.

Another riskier class of securities is hybrid capital securities. We typically rate hybrid capital securities of investment-grade financial institutions two notches under our CCR on the issuing institution. The lower issue rating reflects the payment deferral risk and the hybrid's deep subordination under liquidation.

In the more stressful environment that we project for the medium-term, the financial condition of a higher number of regulated financial institutions may erode to the point where regulators intervene and force suspension of hybrid payments. Or the institution itself could opt to suspend payment to preserve cash and capital. We are analyzing issuers' hybrid securities to assess if the issuer's stand-alone credit profile, the structure of the hybrids, and the regulatory practices concerning hybrid securities in the applicable jurisdiction combine to increase the risk of payment deferral. If we find this to be true, it would result in a hybrid issue rating that is three or more notches below the CCR on the issuer.

In identifying cases that warrant a wider gap between the CCR on the issuer and the issue rating on the hybrid securities, we assess the following indicators of heightened risk of deferral:

- The issuer has incurred material net losses recently, and its near-term financial prospects are poor.
- The issuer is at risk of breaching minimum regulatory capital requirements or other performance tests that would require special regulatory approval to continue payments on its hybrid securities.
- The issuer's creditworthiness erodes to a level that could materially affect its access to and cost of capital. In mature economies, this is often when the CCR falls below the 'A' category.
- The company has substantially cut or eliminated its common dividend. This means the issuer has already crossed a certain line as far as market perception is concerned.

Importantly, we view the issuer's stand-alone financial profile as the key indicator of potential pressure to defer payments on hybrid securities. In cases where our CCR on a financial institution is higher than the institution's stand-alone credit due to specific government intervention, we have widened the gap between the hybrid rating and the CCR. We generally believe that governments are less willing to support hybrid capital issues to the same extent as more senior obligations, as the nationalizations of Fannie Mae and Freddie Mac in the U.S. and Northern Rock PLC in the U.K. attest.

As financial performance recovers to more normal levels, we could raise the issue ratings and thus narrow the gap between the hybrid rating and the CCR. From this perspective, the issue ratings on hybrid capital securities are potentially more volatile than issue ratings on conventional debt issues.

Most outstanding Tier I hybrid capital securities of banking groups around the world have "intermediate-strong" equity content under our hybrid capital methodology (see "Hybrid Capital Handbook: September 2008 Edition," published September 15, 2008, on RatingsDirect). Based on a preliminary review, we believe that we will assign the same intermediate-strong classification to many of the new preferred shares that are part of the government support measures. This provisional conclusion is subject to our review of the specific terms and conditions defined in the documentation for actual issuances.

We include hybrid capital securities with intermediate-strong equity content in our key measure of adjusted total equity, to an amount equal to 33% of adjusted common equity, defined as tangible common equity plus retained earnings. We limit the amount of hybrid securities in our capital measures because of their fixed coupon payments and issuers' greater reluctance to defer hybrid payments compared with common dividends.

The Road Ahead

The global financial system is clearly going through some of the most profound changes since the Great Depression. Most market participants and observers did not expect the unprecedented rapidity of the unwinding of risk that had built up during the past decade. It appears that the concerted actions of central governments are pulling the global financial system back from an even more serious global dislocation. While the systemic risk appears to have been somewhat contained, two concerns remain: that this could instead be a false dawn and indeed systemic risk has not been contained; and that the losses related to the cyclical downturn and a global recession have not yet played out. During the next few weeks, we will undertake a portfolio review of major global issuers to assess the impact of these issues on the stand-alone and government-supported financial strength.

It is too soon to tell if this credit market crisis will lead to fundamental change in investor behavior and risk taking. To be sure, participants around the world will not easily forget the lessons learned. More regulation appears inevitable to many. In our opinion, the two-tier regulatory system was indeed one contributor to the buildup in risk. Risk premiums have returned, and private-sector liquidity has all but disappeared. How the latter is restored will have a significant impact on the future state of banking. Finally, banks and investors may fundamentally revisit risk appetite (credit, concentration, correlation, volatility, and complex on- and off-balance-sheet exposure) and risk management. For confidence to return to the financial system, these issues will have to be resolved to the satisfaction of the major participants. The stakes are high, but we have little doubt the markets will find a way to achieve that.



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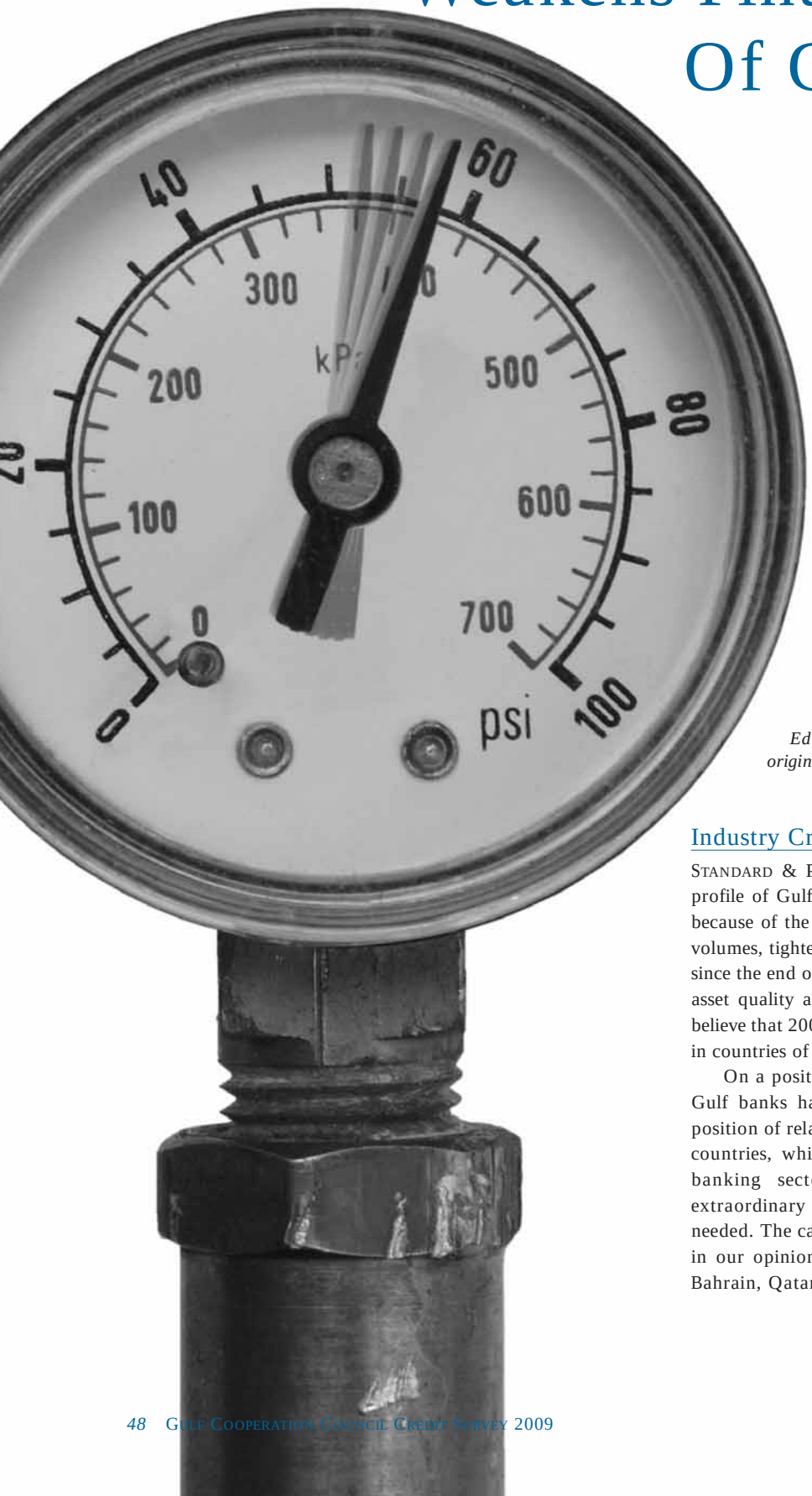
SECONDARY CREDIT ANALYSTS:

MICHAEL ZLOTNIK, FRANKFURT (49) 69 33 999 150
MICHAEL_ZLOTNIK@STANDARDANDPOORS.COM

RODRIGO QUINTANILLA, NEW YORK (1) 212 438 3090
RODRIGO_QUINTANILLA@STANDARDANDPOORS.COM

JAYAN U DHRU, NEW YORK (1) 212 438 7276
JAYAN_DHRU@STANDARDANDPOORS.COM

Tougher Environment Weakens Financial Profile Of Gulf Banks...



...And Pressures Their Credit Ratings

PRIMARY CREDIT ANALYSTS:

MOHAMED DAMAK, PARIS (33) 1 4420 7322,
MOHAMED_DAMAK@STANDARDANDPOORS.COM

EMMANUEL VOLLAND, PARIS (33) 1 4420 6696
EMMANUEL_VOLLAND@STANDARDANDPOORS.COM

Editor's note: This is an extract of an article that was originally published on RatingsDirect on April 29, 2009

Industry Credit Outlook

STANDARD & POOR'S RATINGS SERVICES expects that the credit profile of Gulf banks will likely deteriorate this year, notably because of the tougher operating environment, lower business volumes, tighter liquidity, and the regional stock market slump since the end of third-quarter 2008. We believe that as a result, asset quality and profitability are likely to suffer. Indeed, we believe that 2009 will prove to be a difficult year for most banks in countries of the Gulf Cooperation Council (GCC).

On a positive note, thanks to their good financial profile, Gulf banks have entered this tougher environment from a position of relative strength. In addition, we believe that GCC countries, which we classify as interventionist toward their banking sectors, have and will likely provide some extraordinary support to the systemically important banks if needed. The capacity of these countries to do so remains high in our opinion. The GCC comprises Saudi Arabia, Kuwait, Bahrain, Qatar, the United Arab Emirates (UAE), and Oman.

Economic conditions in the GCC rapidly deteriorated shortly after oil prices dropped from their peak in July 2008. At the same time, liquidity shrank because of rapid loan growth and the repatriation of foreign funds. In addition, stock markets in the region started to plummet in response to weaker economic and earnings prospects, a drop in investor confidence, and fall in business volumes. According to our estimations, real GDP growth in the GCC is likely to slow dramatically in 2009, by more than 50% from about 9.1% in 2008. However, Qatar is a special case. Because of its rapidly increasing gas exports, it is likely to show the highest real GDP growth, in excess of 10% in this year.

Gulf banks are carrying a high amount of new loans—including to the real estate sector and individuals—that the less supportive economic conditions are testing. The seriousness of the situation varies among the six GCC countries. We believe that the most resilient banking sectors are Saudi Arabia's and Qatar's. Under the most pressure are the banking sectors in the UAE, especially Dubai, and in Kuwait. This explains the several negative rating actions we recently carried out on banks in those countries. To date, the ratings on about one-third of GCC banks have negative outlooks or are on CreditWatch with negative implications. This suggests that additional negative rating actions could occur in 2009.

Financial Performance Is Set To Decline In 2009

While most of the commercial banks we rate in the Gulf had strong financial performances in 2008, this year's showing is set to be weaker. The fourth quarter was a turning point for banks in the Gulf as the regional economic slowdown quickly and strongly took hold. Indeed, several GCC banks showed a loss for fourth-quarter 2008 *(see table)*. The main reasons behind these losses were the increase in loan loss provisions (specific and general) and write-downs on investment portfolios—as a result of exposure to structured products or stock markets.

According to our estimations, core income generation declined sharply to 2.0% in 2008 from 2.9% on average in 2007. It is likely to falter further in 2009. Efficiency ratios—32.0% in 2008—are likely to remain strong by international standards but will clearly feel the pinch of lower business volumes and revenues. Cost of risk is likely to continue rising after picking up dramatically in 2008, particularly during the fourth quarter, to 20.1% from low levels in 2007 when new loan loss provisions and investment portfolio impairments were only 6.0% of total revenues. The recent deterioration was particularly visible in Kuwait where cost of risk rose to 30.3% in 2008 from 5.4% in 2007 for the banks that we rate.

In our view, this situation could be exacerbated by a hard landing of the real estate sector, notably for banks based in the Emirate of Dubai (not rated), or a continued decline in local stock markets, which could have effects on Gulf banks' profitability.

Tougher Environment Reduces Business Prospects

Weaker economic prospects, coupled with the decline in liquidity, are set to trigger a major slowdown in loan growth at GCC banks after four years of expansion. This is likely to put a greater drag on some economic sectors, like real estate and construction, which were among the main contributors of growth at GCC banks in the recent past. These two sectors represent about 17% of total loans for the banks that we rate—and a key source of risk. We consider retail loans in the Gulf to

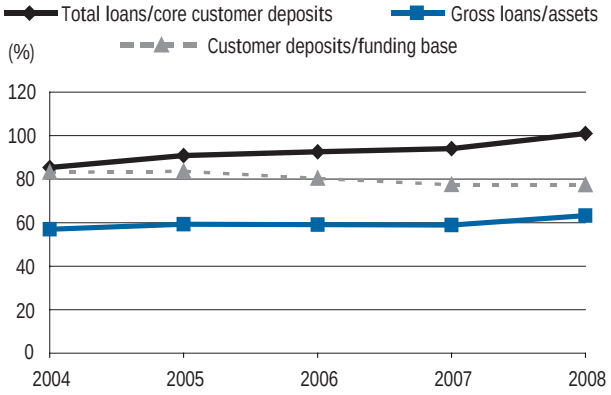
Gulf Banks With Losses In Fourth Quarter 2008

(Mil. $)	2008 Net profit/loss	4Q2008 loss
Gulf Bank	(1,238)	(1,534)
National Commercial Bank	542	(665)
Kuwait Finance House	540	(219)
Burgan Bank	130	(94)
Al Ahli Bank of Kuwait	158	(84)
Abu Dhabi Commercial Bank	337	(72)
Ahli United Bank	256	(24)
Saudi Investment Bank	137	(24)
BMI Bank	(8)	(18)
Commercial Bank of Kuwait	347	(14)
Sharjah Islamic Bank	63	(15)
Gulf Finance House	292	(10)
Gulf Investment Corporation*	N.A.	N.A.
Gulf International Bank	(396)	(248)
Arab Banking Corporation	(880)	(28)

**No data published but we believe that the bank will make a loss in 2008.*

Chart 1

Leverage Indicators For Gulf Banks That Standard & Poor's Rates (2004–2008)

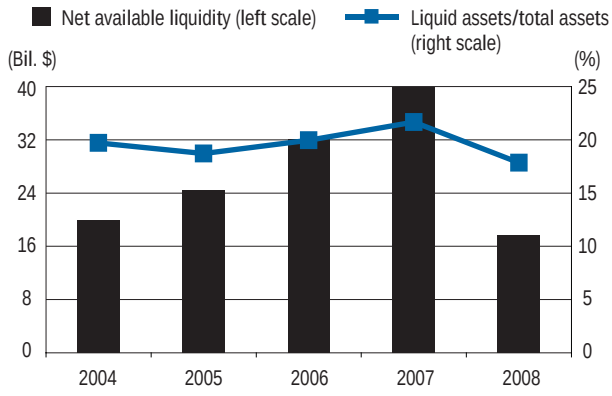


Source: Standard & Poor's

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Chart 2

Liquidity Indicators For Gulf Banks That Standard & Poor's Rates (2004–2008)



Source: Standard & Poor's

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be of relatively limited risk because salary assignments usually but not systematically back them. However, we have noticed some signs of stress on loans in the subsegment of expatriates, who are among the hardest-hit by the economic slowdown.

Liquidity Has Declined And Maturity Mismatches Remain High

The funding profile of Gulf banks is becoming increasingly constrained mainly because of faster loan than deposit growth. Their ratio of loans to deposits has been increasing over the past years and now slightly exceeds 100% for the banks that we rate in the region *(see chart 1)*. Taking into account new constraints on recourse to other funding sources, in particular the widening of spreads and liquidity dry-up on international markets, Gulf banks' flexibility to grow appears reduced, in our view. On a positive note, some GCC governments injected liquidity into their banking systems so that they may be better able to support local economies.

Gulf banks continue to show high contractual maturity mismatches. However, we believe the historical high stability of domestic deposits and large amount of public sector deposits partly mitigate this as a funding profile weakness. Deposit volatility may nevertheless increase as price competition stiffens.

Liquidity tightened last year at many Gulf banks as hot money—inflows from speculation about the depegging of some GCC currencies from the U.S. dollar—evaporated but lending growth continued to climb, reducing their ability to withstand additional shocks *(chart 2)*. The most affected GCC country was the UAE where the ratio of liquid assets to total assets declined to 14.5% at year-end 2008 from 24.9% the previous year. On Dec. 31, 2008, 17.8% of Gulf bank assets were in liquid forms, down from 21.6% at year-end 2007. We believe that this ratio is likely to decline further in 2009 or at best stabilize. To restore confidence and preserve liquidity in their banking systems, regulators took several initiatives. In addition, we understand that most banks have set much lower targets for loan growth, in a move to preserve liquidity indicators.

Asset Quality Is On A Downward Trend

Until the end of September, we considered that asset quality was strong and showed few signs of stress. That picture is changing rapidly. An increasing number of loans are expected to experience difficulties. For that reason, some banks have

"Weaker economic prospects, coupled with the decline in liquidity, are set to trigger a major slowdown in loan growth at GCC banks after four years of expansion. This is likely to put a greater drag on some economic sectors, like real estate and construction…"

decided to take substantial general loan loss provisions in anticipation of rising amounts of nonperforming loans (NPLs).

In addition, we see two immediate sources of stress for domestic banks in two countries:

- The real estate sector in Dubai. The market is more speculative; prices skyrocketed over the past couple of years and started to fall in the second half of 2008. Real estate-related loans account for about 20% of total loans for the Dubai-based banks that we rate, and a hard landing for this sector could significantly affect the NPL figures of these banks.
- Ailing domestic investment companies in Kuwait. They will most likely be a source of significant pressure on asset quality indicators for most domestic banks *(see details in the section below)*.

At year-end 2008, Gulf banks' asset quality indicators were still strong *(see chart 3)*. The ratio of NPLs to total loans averaged 2.2%, compared with 2.1% at year-end 2007. While loan portfolios swelled, NPL stocks remained relatively stable, underpinned not only by good economic conditions in past years but also by banks' improving credit underwriting and monitoring systems. NPL coverage by loan loss provisions stood at a high 155.2% at year-end 2008. We expect Gulf banks' asset quality indicators to decline significantly in 2009.

Kuwaiti Banks' Exposure To Distressed Local Investment Companies Are Signs Of Stress

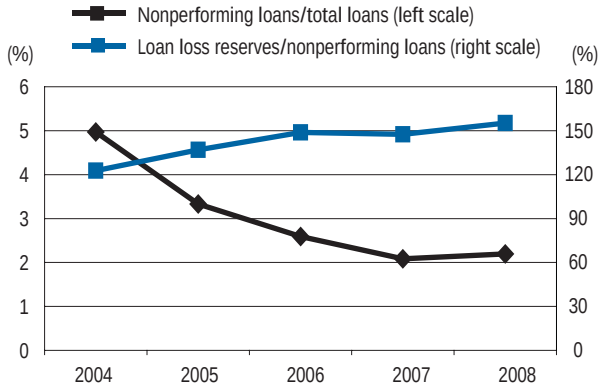
Numerous local investment companies, largely active in the real estate and plummeting stock markets segments, are facing major liquidity and perhaps solvency problems, and we understand that they are in discussions with their creditors to restructure their debt obligations. As a result, banks in Kuwait exposed to these companies took sizable provisions that hurt bottom-line results in the fourth quarter of 2008. In February, we placed five Kuwaiti banks on CreditWatch with negative implications. In our opinion, their exposure to these companies, amid deteriorating operating conditions, will likely weaken their stand-alone credit profiles (see "Various Kuwaiti Banks Placed On CreditWatch Negative On Large Exposure To Investment Companies," published Feb. 16, 2009).

Most of the Kuwaiti banks that we rate report gross loan exposures to these institutions ranging from 40% to 100% of their adjusted total equity base, while collateral (mostly in the form of shares) held against these loans vary from 30% to 60%. The only exception is National Bank of Kuwait S.A.K. (A+/Negative/A-1), which displays a much lower loan exposure to these companies.

The government prepared and approved a financial stability package in April to smooth the impact of the crisis on local commercial banks and investment companies. We are currently reviewing the form, magnitude, and potential benefit of this package on the stand-alone credit profiles of the Kuwaiti banks that we rate. However, renewed political tensions between the parliament—that will reconvene soon after elections in early May—and government may jeopardize implementation of the package, since the parliament has veto power.

Chart 3

Asset Quality Indicators For Gulf Banks That Standard & Poor's Rates (2004–2008)



Source: Standard & Poor's

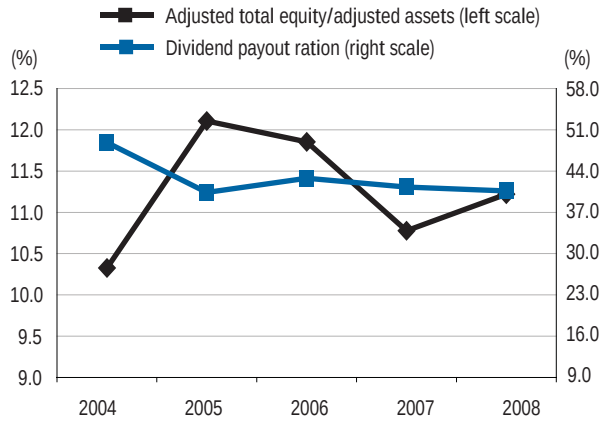
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The Gulf Investment Banks That We Rate Are Under Pressure

Several GCC investment banks or private equity firms are facing funding and liquidity problems because of the nature of their assets and their wholesale funding profile. Standard & Poor's rates three players in this field: Gulf Finance House

Chart 4

Capitalization Indicators For Gulf Banks That Standard & Poor's Rates (2004–2008)



Source: Standard & Poor's

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Gulf Region Sovereign Ratings And BICRAs

Country	FC credit rating	BICRA
Bahrain (Kingdom of)	A/Stable/A-1	5
Kuwait (State of)	AA-/Stable/A-1+	4
Oman (Sultanate of)	A/Stable/A-1	5
Qatar (State of)	AA-/Stable/A-1+	4
Saudi Arabia (Kingdom of)	AA-/Stable/A-1+	3
United Arab Emirates	Not rated	4
Abu Dhabi (Emirate of)	AA/Stable/A-1+	--
Emirate of Ras Al Khaimah	A/Stable/A-1	--

Source: Standard & Poor's. BICRA—Banking Industry Country Risk Assessments. FC—Foreign currency.

(BBB-/Negative/A-3), Arcapita Bank (BB/Watch Neg/B), and Global Investment House KSCC (SD/--/SD). We had rated Investcorp Bank B.S.C. but withdrew the ratings Jan. 28, 2009, at the bank's request after they were lowered to 'BB+' and kept on CreditWatch with negative implications.

Relatively short-term sources dominate the funding profile of these institutions, while their investments are illiquid by nature. We understand that the value of these investments has declined because of global market conditions. Investcorp, for example, announced a significant loss following its exit from some of its hedge fund investments. We understand that some of these banks are implementing corrective measures to improve their weakened liquidity and reduce their leverage, however.

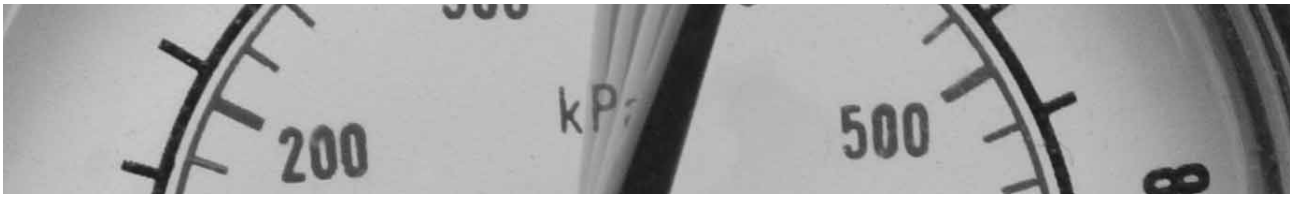
Capitalization Is Set Remain Adequate Thanks To Above-Average Financial Flexibility

Despite a rapid increase in risk assets, capitalization at Gulf banks increased slightly in 2008 *(chart 4)*. The ratio of adjusted total equity (ATE) to adjusted assets reached 11.2% on Dec. 31, 2008, up from 10.8% at year-end 2007. Moreover, we expect that most banks will lower their dividend payout ratios in 2009 to keep their capital ratios at adequate levels to face unexpected problems. Some banks also increased their capital last year. Riyad Bank was the best example; it raised $3.5 billion of new capital in June 2008.

Gulf banks tend to benefit from above-average financial flexibility, as demonstrated by several capital and deposit injections over the past three years. Banks in Qatar, for example, are benefiting from capital injections from the Qatar Investment Authority. Banks in Abu Dhabi have also benefited from capital injections from Abu Dhabi Investment Council.

Extraordinary Expected Government Support Is An Important Rating Factor In The GCC

The willingness as well as capacity of GCC countries to provide extraordinary support to their banks is high in our view. Indeed, these countries have provided significant support, when it was needed, over the past several years. Standard & Poor's classifies the GCC countries as "interventionist" toward their banking sectors, reflecting our opinion that there is high probability that they would extend some extraordinary



support to "systemically important" banks in case of need. However for Bahrain, this classification applies only to its retail banks, not to wholesale banks registered in the kingdom but operating principally outside it.

GCC governments have so far reacted differently in the type, form, and size of the support they have extended and announced to date. This reflects the varying extent of the problems in each country and the degree of impact on their banking systems. However, we perceive timeliness of support as less predictable, for example, because of high political tensions in Kuwait. Systemwide support packages or measures that Gulf authorities have taken to date include:

- Deposit guarantees in Saudi Arabia, the UAE, and Kuwait, but backed by a legal framework only in Kuwait;
- Reduction in reserve requirements to increase liquidity (Saudi Arabia);
- Relaxation of regulation (including the loan-to-deposit ratio in Kuwait and the regulatory lending ratio in Oman);
- Increasing the range of securities eligible for repurchase agreements (UAE);
- Swap facility to ease dollar liquidity (Saudi Arabia);
- Injection of liquidity or capital (Abu Dhabi, UAE, and Qatar);
- Transfer of funds from sovereign wealth funds to central bank as a liquidity cushion for problematic banks (Oman, although no bank so far has used it); and
- Purchases of shares from the equity portfolios of local banks to protect their capital and revenues from stock market volatility (Qatar).

Governments have also intervened to help specific banks, such as Arab Banking Corp. B.S.C., with an injection of $1.1 billion in capital in 2008; Gulf International Bank B.S.C., injection of $1.0 billion in capital in 2008 and transfer from bank to shareholders of a $4.8 billion securities portfolio; Gulf Investment Corporation G.S.C., injection of $1.1 billion currently in process; and Gulf Bank, injection of $416 million in capital.

Our Negative Rating Actions In The Past Six Months

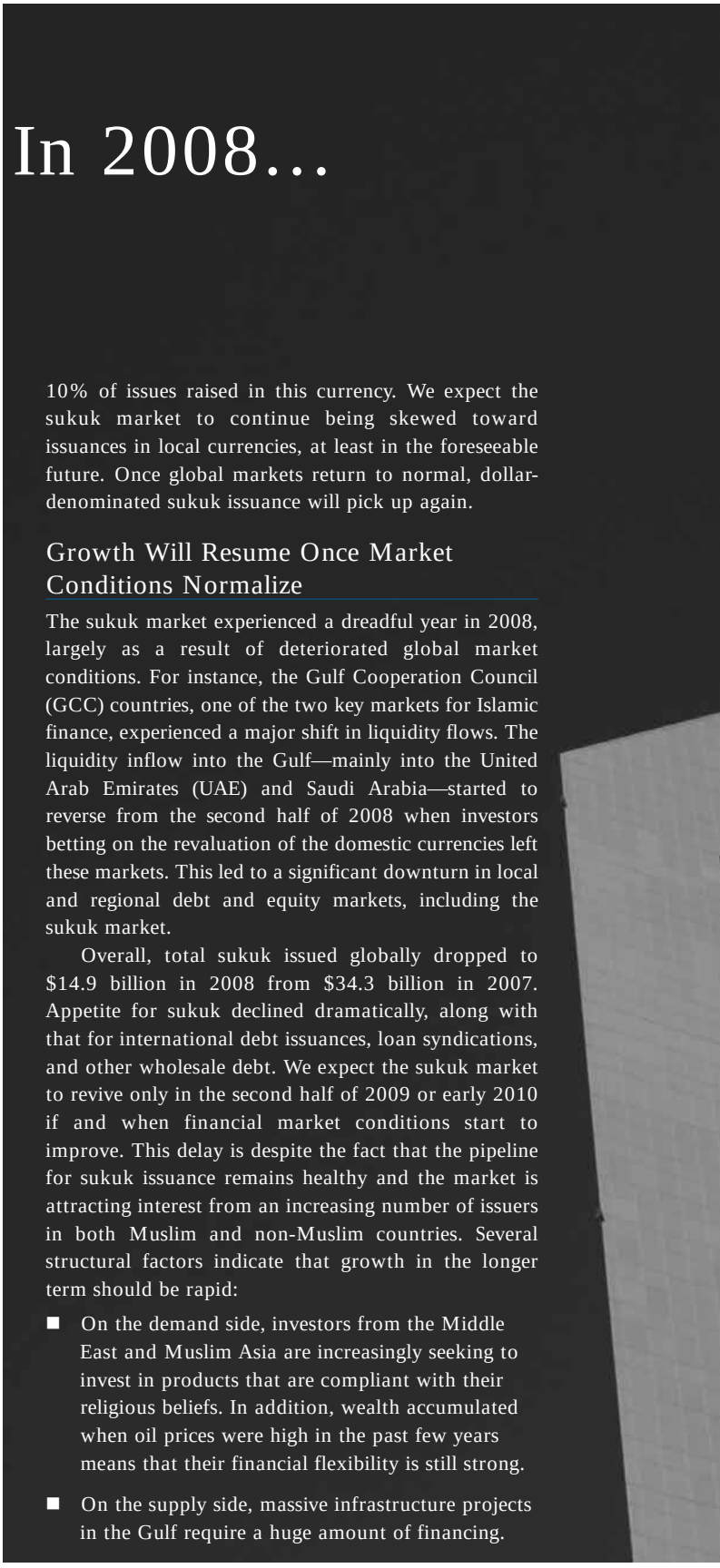
Over the past six months, Standard & Poor's has taken several negative rating actions on the Gulf banks we rate.

These rating actions largely reflect a tougher operating environment that is challenging growth, profitability, and asset quality. They also take into account bank-specific factors, such as for Kuwaiti banks and Bahrain's private equity firms. We do not exclude further negative ratings actions if operating conditions degrade further or if weaknesses at specific banks emerge. To date, the ratings on about one-third of the GCC banks we rate carry a negative outlook or are on CreditWatch with negative implications.

Standard & Poor's analyzes the credit standing of a financial institution in the context of the broad political, economic, regulatory, and legal environment in which it operates. We synthesize this wide-ranging analysis of the environment into a single BICRA, which reflects the strengths and weaknesses of a country's banking system relative to those in other countries. BICRAs classify countries into 10 groups ranging from the strongest banking system (Group 1) to the weakest (Group 10) from a credit perspective. For GCC countries, BICRA scores range from 5 to 3 (*see table opposite*).

The detailed report card, which includes a list of rated companies, their counterparty credit ratings, and credit comments, as well as a list of recent rating actions, can be found in the full article on RatingsDirect.

Sukuk Market Declined Sharply In 2008...



THE SUKUK MARKET DECLINED SHARPLY in 2008 as a result of global market turmoil, drying up of liquidity, widening of credit spreads, and investors' wait-and-see attitude. Although difficult to measure, part of this decline could also have been due to comments about the Sharia compliance of some sukuk by the Accounting and Auditing Organization for Islamic Financial Institutions. More than 45% of sukuk issued in 2008 were "ijara" (lease financing), most probably as a direct consequence of the debate about Sharia compliance among some scholars. The value of sukuk issued in 2008 dropped by more than 56% compared with 2007, to $14.9 billion. Standard & Poor's Ratings Services does not expect the market to start reviving before the second half of 2009 or early 2010.

Standard & Poor's considers that long-term prospects for the sukuk market remain strong, however. Although volumes dropped dramatically in 2008, the sukuk market attracted about the same number of issuers. Conservative estimates of the pipeline of sukuk that have been talked about or announced are in excess of $45 billion. Several factors support sustainable growth of this market, including increasing popularity of Sharia-compliant products and government openness to Islamic finance, massive investment and financing needs in the Gulf, and issuers' desire to tap investors from the Middle East and Muslim Asia. Issuers from more than 20 countries have expressed interest in issuing, or announced their intention to issue, sukuk, and we anticipate that several new sovereigns will enter the market.

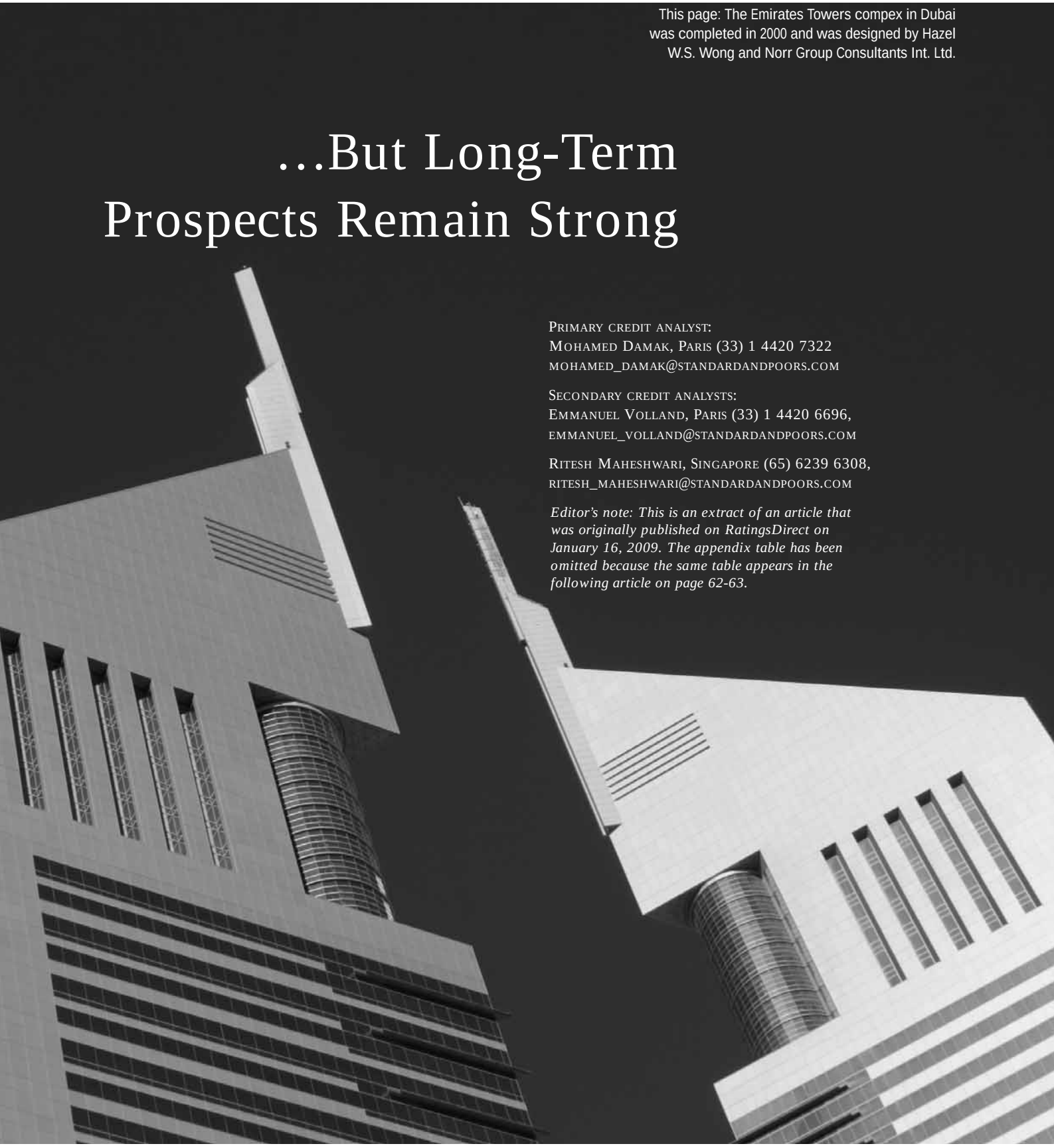
To date, Standard & Poor's has rated 27 sukuk (or sukuk programs), the bulk of which are ijara or "musharaka" (venture capital financing). (Please see our "Glossary Of Islamic Finance Terms," published Jan. 7, 2008, on RatingsDirect.) Credit spreads on sukuk have followed the same trend as for conventional bonds, with a sharp widening in the past 12 months. The average size of the sukuk issued last year declined significantly, partly due to the lower appetite of investors. At the same time, the U.S. dollar lost is place as the currency of choice for sukuk, with only about 10% of issues raised in this currency. We expect the sukuk market to continue being skewed toward issuances in local currencies, at least in the foreseeable future. Once global markets return to normal, dollar-denominated sukuk issuance will pick up again.

Growth Will Resume Once Market Conditions Normalize

The sukuk market experienced a dreadful year in 2008, largely as a result of deteriorated global market conditions. For instance, the Gulf Cooperation Council (GCC) countries, one of the two key markets for Islamic finance, experienced a major shift in liquidity flows. The liquidity inflow into the Gulf—mainly into the United Arab Emirates (UAE) and Saudi Arabia—started to reverse from the second half of 2008 when investors betting on the revaluation of the domestic currencies left these markets. This led to a significant downturn in local and regional debt and equity markets, including the sukuk market.

Overall, total sukuk issued globally dropped to $14.9 billion in 2008 from $34.3 billion in 2007. Appetite for sukuk declined dramatically, along with that for international debt issuances, loan syndications, and other wholesale debt. We expect the sukuk market to revive only in the second half of 2009 or early 2010 if and when financial market conditions start to improve. This delay is despite the fact that the pipeline for sukuk issuance remains healthy and the market is attracting interest from an increasing number of issuers in both Muslim and non-Muslim countries. Several structural factors indicate that growth in the longer term should be rapid:

- On the demand side, investors from the Middle East and Muslim Asia are increasingly seeking to invest in products that are compliant with their religious beliefs. In addition, wealth accumulated when oil prices were high in the past few years means that their financial flexibility is still strong.
- On the supply side, massive infrastructure projects in the Gulf require a huge amount of financing.



This page: The Emirates Towers compex in Dubai was completed in 2000 and was designed by Hazel W.S. Wong and Norr Group Consultants Int. Ltd.

...But Long-Term Prospects Remain Strong

PRIMARY CREDIT ANALYST:
MOHAMED DAMAK, PARIS (33) 1 4420 7322
MOHAMED_DAMAK@STANDARDANDPOORS.COM

SECONDARY CREDIT ANALYSTS:
EMMANUEL VOLLAND, PARIS (33) 1 4420 6696,
EMMANUEL_VOLLAND@STANDARDANDPOORS.COM

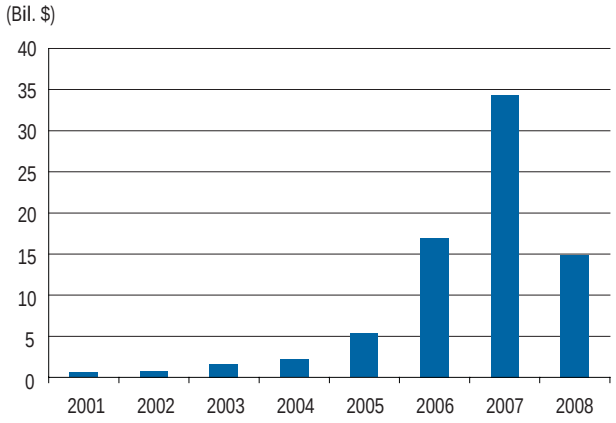
RITESH MAHESHWARI, SINGAPORE (65) 6239 6308,
RITESH_MAHESHWARI@STANDARDANDPOORS.COM

Editor's note: This is an extract of an article that was originally published on RatingsDirect on January 16, 2009. The appendix table has been omitted because the same table appears in the following article on page 62-63.

Standard & Poor's became the first major agency to assign ratings to sukuk instruments in 2002 (Malaysia Sukuk) and we remain at the forefront of developing an analytical framework for evaluating innovative Islamic issuers and instruments. S&P currently has ratings on 12 Islamic financial institutions and 22 sukuk issues representing nearly $15 billion in global issuance. S&P Index Services offers a powerful and expanding lineup of 30 benchmark and investable Shariah indices to enable Islamic investors to slice and dice their exposure by country, region, size, style, and sector.

Chart 1

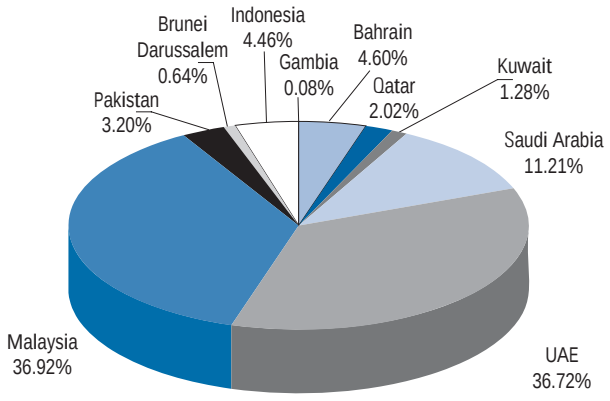
Total Sukuk Issuance 2001–2008



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Chart 2

Global Sukuk Issuance By Country In 2008



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Conventional borrowers are also seeking to diversify their investor base. They want to attract funding from investors as the crisis continues to widen and access to wholesale funding sources remains constrained.

- Governments' and regulators' openness to Islamic finance is increasing around the world. We observe this trend not only in Muslim countries but also in non-Muslim countries such as the United Kingdom (AAA/Stable/A-1+), the European country most supportive of Islamic finance.
- Financial institutions are seeking to better balance their funding, especially in the Gulf where short-term funding sources typically dominate and maturities are increasing on the asset side.

Last year clearly showed that the sukuk market is connected to global debt markets. Islamic finance is one component of global finance and is exposed to the ups and downs of international funding markets. Therefore, we expect the revival of the sukuk market to start more or less at the same time as that of the conventional capital markets.

The Club Of Sukuk Issuers Is Widening

One of the few positive developments for the sukuk market in 2008 has been its continuous geographic diversification. It is attracting issuers from an increasing number of countries and this trend is set to continue. Issuers from more than 20 countries have expressed interest in issuing, or announced their intention to issue, sukuk. Therefore, Standard & Poor's expects the market to continue globalizing.

We expect more sovereign issuers to join the club in 2009. We understand that the Republic of Singapore (AAA/Stable/A-1+), the Republic of Indonesia (local currency BB+/Stable/B; foreign currency BB-/Stable/B), the Republic of Kazakhstan (local currency BBB/Negative/A-3; foreign currency BBB-/Negative/A-3), and the State of Qatar (AA-/Stable/A-1+), among others, plan to issue sukuk. Sovereign issuances should support the construction of a yield curve and introduce benchmarks for private issuers in these countries, boosting the growth of the sukuk market.

Malaysian and UAE-based issuers continued to drive the sukuk market, with more than 70% of total issuance coming from these two countries in 2008. Authorities' support for

"We expect the sukuk market to revive only in the second half of 2009 or early 2010 if and when financial market conditions start to improve. This delay is despite the fact that the pipeline for sukuk issuance remains healthy…"

Islamic finance and openness to foreign investors are the key elements behind these figures. Other GCC and Asian countries are set to increase their contribution to the growth of the market in the future thanks to huge financing and investment needs in the GCC, as well as sovereign issuance and support for Islamic finance development.

In 2008, the largest sukuk was issued out of Saudi Arabia by Saudi Basic Industries Corp. (SABIC, A+/Stable/A-1) for a total amount of Saudi Arabian riyal 5 billion ($1.3 billion). The structure of this sukuk was very innovative. Under an asset transfer agreement, SABIC transferred certain rights and obligations for specific marketing agreements to SABIC Sukuk LLC, a 100% subsidiary. These represent SABIC Sukuk LLC's underlying assets, and it will hold them as a custodian for the benefit of the sukuk holders. The sukuk assets should generate the necessary cash flows to cover periodic payments to the sukuk holders. SABIC will be required to purchase the sukuk from the sukuk holders when they exercise their right to redeem their sukuk. Therefore, we have equalized the ratings on the sukuk with those on SABIC.

The other large sukuk, denominated in local currency, were issued out of the UAE, by Aldar Properties PJSC (A-/Stable/A-2), Nakheel PJSC, Dubai Electricity and Water Authority, and Sorouh Abu Dhabi Real Estate LLC. The sukuk issued by Sorouh (Sun Finance Ltd. Class A, B, and C) was the first sukuk with no credit enhancement that we have rated. We believe that the potential for asset-backed sukuk continues to be strong despite the currently weak investor interest in structured products.

U.S. Dollar Is No Longer The Currency Of Choice For Sukuk Issuance

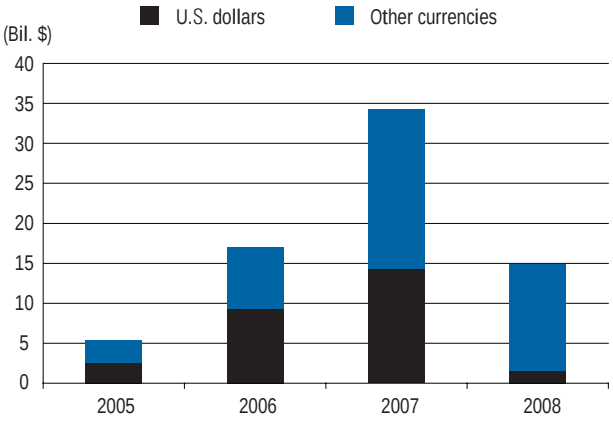
The U.S. dollar lost its leadership position in sukuk issuance in 2008, with only about 10% of issuance in this currency. The credit crisis meant that sukuk issuers had to attract domestic investors instead of international investors. Issuers deserted international markets and concentrated on local markets where liquidity was more abundant and the appetite for Sharia-compliant instruments stronger. In addition, investors betting that some GCC governments would de-peg their currencies from the dollar converted their funds into local currencies and placed them on local and regional debt and capital markets. In the end, the governments did not de-peg their currencies, however, and currently five out of the six GCC countries' currencies are pegged to the U.S. dollar. Standard & Poor's expects the sukuk market to continue being skewed toward issuance in local currencies in the foreseeable future, with only a limited portion being issued in dollars. Some of the sovereign sukuk to be issued in 2009 or 2010 will be both in local and foreign currencies (mainly the U.S. dollar). Once market conditions return to normal, dollar-denominated sukuk will regain a stronger position, however.

Standard & Poor's Role In The Market For Sukuk

Our role is to provide market participants with independent and objective opinions about the creditworthiness of issuers and issues—including those involving sukuk. We don't comment on the Sharia compliance of a particular issue or issuer. Our ratings don't constitute a recommendation to sell, buy, or hold a particular security—whether it is Sharia compliant or not. Instead, our ratings help investors to make informed decisions and issuers to access debt markets and benchmark their creditworthiness against peers'.

Chart 3

Global Sukuk Issuance By Currency (2005–2008)



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Rated Gulf Islamic Financial Institutions And Takaful Companies Have Shown Resilience To Global Market Dislocation...

PRIMARY CREDIT ANALYST: MOHAMED DAMAK, PARIS (33) 1 4420 7322, MOHAMED_DAMAK@STANDARDANDPOORS.COM

SECONDARY CREDIT ANALYSTS:
EMMANUEL VOLLAND, PARIS (33) 1 4420 6696, EMMANUEL_VOLLAND@STANDARDANDPOORS.COM

NEIL GOSRANI, LONDON (44) 20 7176 7112, NEIL_GOSRANI@STANDARDANDPOORS.COM

GLOBAL FINANCIAL MARKET DISRUPTION, the liquidity crunch, slowing economies, and sharply falling stock markets have adversely affected recent performance at numerous financial institutions around the world. Standard & Poor's Ratings Services believes that Islamic financial institutions (IFIs) have felt the repercussions less because Sharia law prohibits interest-based financial products. In other words, IFIs didn't invest in some impaired asset classes that have hampered many conventional banks' financial profiles and performance.

We note, however, the squeeze that current market conditions are putting on many Islamic banks and takaful insurance companies. For instance, we see as sources of stress the liquidity dry-up, mounting pressure on the real estate sector in the Gulf Cooperation Council (GCC) countries, the sharp correction in regional stock markets, and certain investments made by IFIs—mainly investment banks—in European or U.S companies and real estate. In our opinion, most IFIs should be equipped to weather this financial downturn and keep the effects on their financial profiles at manageable levels. However, like their conventional peers, IFIs stand to post weaker financial performance and asset quality indicators, in our view, in the coming quarters. Among others, we see the real estate sector slide as one of the chief sources of risk for IFIs.

Our Recent Rating Actions On Islamic Banks

We have taken various negative rating actions over the past three months on both conventional and Islamic banks, largely because of the impact of the deteriorating economic landscape on these entities. When it comes to Islamic banks in GCC countries, we have:

- Lowered the long- and short-term counterparty credit ratings on Dubai Islamic Bank to 'A-/A-2' from 'A/A-1' and revised the outlook to negative from stable;
- Revised the outlook on Sharjah Islamic Bank to stable from positive and affirmed the 'BBB/A-2' ratings;
- Revised the outlook on Gulf Finance House to negative from stable and affirmed the 'BBB-/A-3' ratings;
- Put the 'A-' long-term rating on Kuwait Finance House on CreditWatch with negative implications and affirmed the 'A-2' short-term rating; and
- Lowered the ratings on Arcapita Bank B.S.C. to 'BB+/B' from 'BBB/A-2' and placed them on CreditWatch with negative implications.

We See No Exposure To Structured Products For IFIs

Sharia principles prohibit IFIs from handling interest-based products, which are the main foundation of structured financial instruments. Consequently, IFIs have no exposure to these instruments. We note that IFIs, unlike certain of their conventional counterparts, have not had to book write-downs corresponding to the falling market value of these assets. In the first nine months of 2008, commercial Islamic banks that we rate continued to exhibit strong profitability in our view, reporting an average return on assets (ROA) of 3.1% in the period. These banks appear to have benefited from the supportive economic environment that prevailed in the first half of 2008, their good efficiency, and low cost of risk. Their average ROA at end-September 2008 compares with 3.7% at year-end 2007, when we observe that banks' revenues were inflated by an unsustainable brokerage income flow and rapid growth in loan portfolios. In the months to come, we believe that rated IFIs' financial performance will deteriorate because we expect them to book some market-related provisions covering their exposure to the dropping values of stock markets and to Sharia-compliant investment products (mainly sukuk notes and funds). In the next few quarters, the anticipated slowdown in loan growth, inflated cost of funding, and increase in cost of risk also stand to test IFIs' performance.

...But They Are Not Risk Immune

Liquidity Is Drying Up And Funding Costs Are Increasing

Events over the past 18 months have triggered a sharp decline in available liquidity around the globe. Investors have adopted a wait-and-see stance, reducing their risk appetites and seeking higher returns. In the Gulf region, home to most IFIs that we rate, we note that the "hot" money inflow into GCC countries in anticipation of a possible revaluation of Gulf local currencies—the currencies of five of the six GCC countries are pegged to the dollar—ceased and rapidly reversed in 2008. At the same time, loan growth remained high in the first nine months of the year. Like their conventional peers, IFIs were ill prepared, in our view, to enter an environment where liquidity became scarce and cost of funds increased.

Still, GCC countries have announced that they stand ready to support their financial systems if needed. The Central Bank of the United Arab Emirates (UAE) set up a liquidity facility totaling United Arab Emirate dirham (AED) 50 billion ($13.6 billion), and the finance ministry placed additional deposits of AED70 billion ($19 billion) to ease liquidity pressure on banks operating in the UAE. We believe that providing support to IFIs is more complicated than for conventional banks, because governments can't use the same mechanisms as those for conventional institutions. For instance, interest-based repo facilities or traditional deposits aren't Sharia compliant. The UAE has based its support to IFIs on wakala, which has required some time to implement.

The still-adequate liquidity that we understand is available at rated Islamic commercial banks partially mitigates liquidity risk. On Sept. 30, 2008, these banks recorded, according to our estimates, a ratio of liquid assets to total assets of 19.9%. We understand that this ratio continued to decline in the final quarter of 2008, however, albeit remaining adequate. We note that rated IFIs rely heavily on their customer deposits to finance their loan portfolios; we estimate that these IFIs recorded a ratio of total loans to deposits of 94.2% on Sept. 30, 2008. We expect the liquidity crunch to constrain growth at conventional and Islamic banks in the Gulf and to increase their cost of funding. We also believe that a decline in loan offerings could accelerate the correction in the real estate market. This sector is one of the main sources of risk for the region's banks, including Islamic institutions, in our view.

We understand that IFIs' instruments for managing liquidity are scarce compared with those of conventional counterparts. IFIs generally place any excess available liquidity with other international or local banks through Sharia-compliant instruments (mainly international murabaha). The market for sukuk notes remains fairly illiquid because no developed secondary market exists. We understand that investments in sukuk are mainly classified as held to maturity. We are of the view that IFIs could take advantage of the current challenging times to innovate and broaden the offering of acceptable instruments for liquidity management.

Lack Of Liquidity Is Squeezing Sukuk Issuance

A look at sukuk market performance in 2008 shows the dent that the liquidity crunch has made in issuance. Total sukuk issuance worldwide reportedly declined to $14.9 billion in 2008, compared with more than $34.3 billion a year earlier. Still, we continue to foresee positive prospects for the sukuk market in the long term. Turning to the coming quarters, however, we expect sukuk issuance to recover, at the earliest, during the second half of 2009 or, most probably, in 2010. Although volumes dropped steeply in 2008, we note that the sukuk market attracted about the same number of issuers. The

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"In our view, several factors support the sukuk market's sustainable growth, including the increasing popularity of Sharia-compliant financial instruments, governments' increasing openness to Islamic finance around the world, substantial investment and financing needs in the Gulf, and issuers' desire to tap investors from the Middle East and Muslim Asia."

market's estimates of the current pipeline of potential sukuk issues are in excess of $45 billion. In our view, several factors support the sukuk market's sustainable growth, including the increasing popularity of Sharia-compliant financial instruments, governments' increasing openness to Islamic finance around the world, substantial investment and financing needs in the Gulf, and issuers' desire to tap investors from the Middle East and Muslim Asia. We understand that issuers from more than 20 countries have expressed interest in issuing, or have announced their intention to issue sukuk. We also anticipate that several additional sovereign issuers could enter the market.

Sharp Stock Market Correction Also Fuels Risks For IFIs

Liquidity management is challenging for IFIs due to the lack of liquid Sharia-compliant asset classes, as we mentioned above. Certain Islamic banks consequently invested in equities, exposing themselves to the correction in stock markets in recent quarters. We believe that the correction's effects on rated IFIs are likely to be relatively limited, from a solvency perspective. The Islamic banks we rate carry relatively low exposure to stock markets, amounting to less than 5% of total reported assets on Sept. 30, 2008. Capitalization is also strong, as shown by the ratio of adjusted total equity (ATE) to assets for the commercial Islamic banks that we rate, at 16.5% on Sept. 30, 2008.

Stock market volatility is not new in the region. Gulf stock markets experienced a pronounced correction in 2006, when the region's banking systems displayed resilience. The magnitude of the 2008 fall is greater than past declines, however. We consequently expect to see marked negative effects on profitability of rated IFIs in the fourth quarter of 2008, possibly spilling over into the ensuing quarters.

Value Of Islamic Private Equity Firms' Investments In Europe And The U.S. Poised To Drop

Islamic investment banks that operate largely as private equity firms are also, in our view, feeling the impact of global market conditions because they have invested in the real estate markets and companies outside the Gulf region, through private equity transactions. We believe that falling real estate prices, the credit crunch, and the economic recession in Europe and the U.S. are set to lessen the value of these investments and push these Islamic investment banks to either enlist their generally sophisticated clients' support to share any losses or to write down losses to preserve their reputations. We expect any potential losses to translate into lower financial performance at these banks, compared with results delivered over the past couple of years. Indeed, because we see investors deserting alternative asset classes, at least for the moment, we believe that rated IFIs' ability to place or exit deals will be significantly strained. The adverse impact on their profitability and liquidity could also be material, in addition to the expected negative revaluation of their investment portfolios and the increase in cost of funds since these institutions are wholesale funded. Effectively illustrating this is Arcapita Bank, which has reported significantly deteriorated liquidity and where we expect 2009 financial performance to decline versus historical levels. Arcapita is currently implementing a set of corrective measures; we believe that the impact of these measures will contribute to our assessment of the bank's credit profile.

IFIs Are Not Risk Free

IFIs take risks: One of the pillars of Islamic finance states that all the participants in a transaction must share the risks and rewards (see Appendix below). For further details on our views on the risks associated with IFIs, from a rating perspective, see "Risk Management For Islamic Financial Institutions: A Rating Perspective," published Jan. 15, 2008, on RatingsDirect. In this report, we focus on various risks that IFIs face in the current environment. The major risk arises from their exposure to the real estate sector and is common to IFIs and their conventional counterparts. We note that real estate financing in the Gulf grew considerably over the past three years.

According to Islamic finance principles, all transactions must be backed by a tangible asset. Therefore, one of the preferred asset classes of Islamic banks is real estate. We calculate total direct exposure to the real estate sector for IFIs that we rate at the equivalent of about 20% of total loans, which, in our opinion, is high and makes IFIs vulnerable to the correction in this previously fast-growing sector. In addition, we believe that certain loans to individuals granted by Islamic banks were used to finance real estate transactions. We

consequently expect potentially significant negative repercussions on asset quality and profitability at rated IFIs if the ongoing correction in the real estate sector in GCC countries, and especially in the Emirate of Dubai, continues.

A second risk stems from certain Islamic banks' reliance on profit-sharing investment accounts (PSIA) for funding in an environment where competition to attract deposits is stiff and remuneration has increased. IFIs have some lines of defense, however, primarily in the form of profit equalization reserves that we believe they could constitute in profitable years to cover for declines in less profitable years. Moreover, we understand that IFIs could reduce mudarib fees and use investment risk reserves to cover unexpected losses on investments or financing made on behalf of PSIA holders. To date, we understand the Islamic banks that we rate have constituted a fairly limited amount of profit equalization and investment risk reserves to reduce PSIA risk.

Takaful Insurance Displays Strong Resilience

Takaful insurers and reinsurers have so far demonstrated resilience to toughening market conditions, and we expect this to continue. We attribute their resilience to sufficient liquidity flows—in part due to reportedly higher new business—to service normal claims levels, and to capital adequacy, which, despite being affected in the current climate, remains supportive of the ratings across the sector. These positives are, in our view, partially offset by an investment focus on assets currently experiencing considerable volatility and high reliance on reinsurance capacity.

Takaful and retakaful players, although established for some time now, have achieved critical mass only in the past few years, during which we have witnessed increasing interest and acceptance of their business model. Attesting to this is these insurers' reported rapid growth in gross premiums written, which we believe is driven by consumers switching from conventional insurance or entering the takaful market for the first time, including for life takaful products; the differences in conventional and takaful insurance products; a widening range of takaful business lines; and legislative changes favorable to takaful insurance activity. We note that this growth, combined with a stable claims environment, has provided takaful and retakaful operators with a steady cash inflow through which to settle claims.

Claims settlement appears further supported by operators' liquid investment portfolios in both participant and shareholder funds. The liquid investment portfolios reflect the largely short-term nature of their business. Investment portfolios' assets range from low-risk murabaha (bank term deposits) to high-risk nonlisted equities, but we believe they currently comfortably exceed net outstanding claims. For this to continue to be the case, however, markets must remain liquid enough to allow the pricing of such assets. Credit risk, through market volatility and uncertainty in asset pricing, could lead to reduced earnings in the takaful segment, with lower investment income combined with high use of reinsurance protection—both regional and international—for certain risks. However, takaful and retakaful insurers' generally adequate-to-strong capital adequacy relative to risks written is, in our opinion, a significant compensating factor.

Appendix: The Five Pillars Of Islamic Finance

IFIs must abide by the five pillars of Islamic finance, which are:

- *The ban on interest*: Interest must not be charged or paid on any financial transaction, as interest (or the intrinsic value of the money) is deemed unlawful by Sharia.
- *The ban on uncertainty or speculation*: Uncertainty in contractual terms and conditions is forbidden. However, risk taking is allowed when all the terms and conditions are clear and known to all parties.
- *The ban on financing certain economic sectors*: Financing of industries deemed unlawful by Sharia—such as weapons, pork, and gambling—is forbidden.
- *The profit- and loss-sharing principle*: Parties to a financial transaction must share in the risks and rewards attached to it.
- *The asset-backing principle*: Each financial transaction must refer to a tangible, identifiable underlying asset.

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Table: Islamic Issues And Issuers Rated By Standard & Poor's*

Issue credit ratings

Originator	Date of first rating	Issue amount (mil. $)	Long-term rating
Central Bank of Bahrain Sukuk	Various	995	A
DIB Sukuk Co. Ltd.	Feb. 15, 2007	750	A-
DP World Sukuk Ltd. (DP World)	June 27, 2007	1,500	A+
Dubai Sukuk Centre Ltd.	May 25, 2007	1,250	A+
East Cameron Gas Company Sukuk	July 31, 2006	166	CC/Watch Neg
EIB Sukuk Co. Ltd. (Emirates Bank International)	May 15, 2007	1,000	A
GFH Sukuk Ltd. (Gulf Finance House)	June 26, 2007	1,000	BBB-
Gold Sukuk dmcc (Dubai Multi Commodities Centre Authority)	April 11, 2005	200	A
Golden Belt 1 B.S.C.	April 18, 2007	650	BBB+
IDB Trust Services Ltd. (Islamic Development Bank)	May 20, 2005	1,000	AAA
JAFZ Sukuk Ltd.	Nov. 8, 2007	AED7.5 billion	A+
Loehmann's Capital Corp. (Loehmann's Holdings Inc.)	Sept. 22, 2004	110	CCC-
MBB Sukuk Inc.	April 11, 2007	300	BBB+
Pakistan International Sukuk Co.	Dec. 23, 2004	600	CCC+
Qatar Global Sukuk QSC	Sept. 10, 2003	700	AA-
RAK Capital (Emirates of Ras Al Khaimah)	May 6, 2008	2,000	A
Sarawak Corporate Sukuk Inc.	Nov. 30, 2004	350	A-
Saudi Basic Industries Corp.	Various	SAR16 billion	A+
Sharjah Islamic Bank Sukuk	Sept. 12, 2006	255	BBB
Stichting Sachsen-Anhalt Trust	July 9, 2004	130	AA-
Sukuk Funding (No.2) Ltd. (Aldar Properties PJSC)	May 22, 2008	AED3.8 billion	A-
Sun Finance Ltd. (Sorouh Abu Dhabi Real Estate LLC)	July 21, 2008	AED4 billion	A/BBB+/BBB-
Tabreed 06 Financing Corp. (National Central Cooling Co. PJSC)	June 15, 2006	200	BB
Tabreed 08 Financing Corp. (National Central Cooling Co. PJSC)	Dec. 2, 2008	AED1.7 billion	B
Tadamun Services Berhad (Islamic Development Bank)	July 17, 2008	MYR1 billion	AAA
Total		**22,338**	

Notes

**Data as of Feb. 20, 2009. AED—United Arab Emirates dirham. SAR—Saudi Arabian riyal. MYR—Malaysian ringgit.*



Related Research On RatingsDirect

The opinions expressed in this article are based on our rating methodology for Islamic financial institutions. Please see the articles below for further information.

The Meaning Of Ratings For Islamic Financial Institutions, Oct. 25, 2006

Credit FAQ: An Introduction To Islamic Finance, Nov. 14, 2006

S&P Launches Stability Ratings For Islamic Banks Offering Profit-Sharing Investment Accounts, Sept. 21, 2007

Glossary of Islamic Finance Terms, Jan. 7, 2008

Risk Management For Islamic Financial Institutions: A Rating Perspective, Jan. 15, 2008

Table: Islamic Issues And Issuers Rated By Standard & Poor's* (cont..)

Issuer credit ratings

Issuer	Date of first rating	Country	Long-term rating
Albaraka Banking Group (B.S.C.)	March 21, 2007	Bahrain	BBB-
Al Rajhi Bank	Oct. 5, 2005	Saudi Arabia	A
Arcapita Bank B.S.C.	Nov. 16, 2006	Bahrain	BB+/Watch Neg
B.E.S.T. Reinsurance Co.	Sept. 2, 1997	Tunisia	BBB+
Dubai Islamic Bank	Oct. 18, 2006	United Arab Emirates	A-
Dubai Islamic Insurance & Reinsurance Co. (Aman)	Nov. 17, 2008	United Arab Emirates	BBB
Gulf Finance House	Aug. 7, 2006	Bahrain	BBB-
Hannover ReTakaful B.S.C.	Dec. 4, 2007	Bahrain	A
Islamic Development Bank	Dec. 19, 2002	Saudi Arabia	AAA
Kuwait Finance House	Aug. 24, 2004	Kuwait	A-/Watch Neg
Salama/Islamic Arab Insurance Co. (P.S.C.)	May 24, 2007	United Arab Emirates	BBB+
Sharjah Islamic Bank	Sept. 6, 2006	United Arab Emirates	BBB
Takaful International Co. BSC	Dec. 22, 2008	Bahrain	BBB
Takaful Re Ltd.	Oct. 31, 2006	United Arab Emirates	BBB
Wethaq Takaful Insurance Co. K. S. C. (Closed)	Sept. 22, 2008	Kuwait	BBB-

Notes

**Data as of Feb. 20, 2009. AED—United Arab Emirates dirham. SAR—Saudi Arabian riyal. MYR—Malaysian ringgit.*

Abu Dhabi Commercial Bank

PRIMARY CREDIT ANALYST: EMMANUEL VOLLAND, PARIS (33) 1 4420 6696, EMMANUEL_VOLLAND@STANDARDANDPOORS.COM

SECONDARY CREDIT ANALYST: PAUL-HENRI PRUVOST, LONDON (44) 20 7176 7210, PAUL-HENRI_PRUVOST@STANDARDANDPOORS.COM

ISSUER CREDIT RATING: A/STABLE/A-1

PUBLICATION DATE: JULY 23, 2008

Rationale

The ratings on Abu Dhabi Commercial Bank (ADCB) reflect the bank's majority ownership by and privileged relationship with the government of the oil-rich Emirate of Abu Dhabi (AA/Stable/A-1+), improving domestic commercial position, increasing revenue diversification, and adequate financial performance. At the same time, the ratings are constrained by the bank's narrow domestic market—triggering high concentration risks—fast-growing loan portfolio, and increasing competition. The recent acquisition of a 25% stake in Malaysia-based RHB Capital Group (RHB Cap, not rated) for $1.2 billion had a neutral effect on the ratings on ADCB. Although this investment has a sound rationale and provides ADCB with some revenue diversification, core capitalization now stands below those of similarly rated regional peers.

ADCB is one of the largest banks in the United Arab Emirates (UAE, not rated), with total assets of $35.0 billion at June 30, 2008. The Abu Dhabi government has a 64.8% stake in ADCB through Abu Dhabi Investment Council (ADIC), while members of the ruling family hold at least an additional 10%. Standard & Poor's Ratings Services considers that the bank's ownership structure and importance to Abu Dhabi's economy mean that government support in case of need would be very strong. The long-term rating on ADCB (considered as a government-related entity {GRE} under our methodology) is, therefore, two notches higher than the bank's stand-alone creditworthiness.

A very supportive economic environment, an aggressive commercial strategy, and a strengthened enterprise risk management framework have helped enhance ADCB's financial performance in the past three years. The bank's return on equity (ROE) was 21.1% in 2007, down slightly as previous years' had been boosted by exceptional gains. We expect the bank's profitability to remain relatively stable in the medium term. While revenue diversification is set to improve, costs are set to increase rapidly. ADCB's asset quality indicators have remained strong in the past three years, with a ratio of nonperforming loans (NPLs) to total loans of 1.5% at June 30, 2008. Coverage of NPLs by provisions stood at 100%. Lending has increased dramatically in the past three years and concentration in the loan portfolio is high—though partially compensated for by the fact that the largest exposures are mainly to government entities (or related individuals) and well secured by collateral.

ADCB's funding and liquidity are adequate. The bank has access to a substantial base of customer deposits and benefits from large deposits from the Abu Dhabi government and public entities (representing about 50% of its total customer deposits). However, ADCB has a sizable deposit concentration and maturity mismatch, and wide swings in its deposit base can occur from time to time. The bank is addressing this issue by rapidly increasing its wholesale long-term funding, including through a $7.5 billion Euro medium-term note (EMTN) program and syndicated loans.

Core capital measures fell significantly after the investment in RHB Cap, although the issuance of UAE dirham (AED) 4.8 billion of short-dated mandatory convertible securities (eligible for high equity content) allows for stable adjusted total equity (ATE) and regulatory capital ratios. Although we expect rapid growth in lending to put pressure on capital ratios, having the government of Abu Dhabi as a majority shareholder provides ADCB with financial flexibility.

Outlook

The stable outlook balances Standard & Poor's expectation that ADCB will retain its good financial profile with the bank's aggressive expansion strategy and weaker capitalization than regional peers. A change in ADCB's ownership structure and weaker links with ADIC and the Abu Dhabi government, or any significant further deterioration in capital ratios, would have a negative impact on the ratings. We could raise the ratings, however, if the bank further enlarges its customer franchise, reduces its concentration risks, and strengthens its capitalization.

Ahli United Bank B.S.C.

PRIMARY CREDIT ANALYST: GOEKSENIN KARAGOEZ, PARIS (33) 1 4420 6724, GOEKSENIN_KARAGOEZ@STANDARDANDPOORS.COM

SECONDARY CREDIT ANALYST: EMMANUEL VOLLAND, PARIS (33) 1 4420 6696, EMMANUEL_VOLLAND@STANDARDANDPOORS.COM

ISSUER CREDIT RATING: A-/STABLE/A-2

PUBLICATION DATE: APRIL 28, 2009

Rationale

The ratings on Bahrain-based Ahli United Bank B.S.C. (AUB) reflect its leading commercial position in the Kingdom of Bahrain (A/Stable/A-1), better geographic diversification than for regional peers, and strong asset quality indicators. The ratings are constrained by the bank's capitalization, which is below that of regional peers, exposure to the real estate sector in a weakened operating environment, and reliance on wholesale funding. The long-term rating on AUB, a government-related entity (GRE) under our methodology, includes a one-notch uplift above its stand-alone credit profile. This reflects Standard & Poor's Ratings Services' expectation of a strong likelihood of extraordinary government support in case of need, given the bank's systemic importance stemming from its leading market position. We classify Bahrain as interventionist toward its banking sector, though our policy in the country only applies to retail banks (like AUB) that we consider systemically important.

AUB is a full-fledged commercial banking group providing corporate, retail, treasury, and private banking services. It is registered in Bahrain, where it is among the largest retail banks, but also operates in Kuwait, Qatar, the U.K., Egypt, Oman, and Iraq through subsidiaries or managed affiliates. With total assets of $23.6 billion on Dec. 31, 2008, AUB is among the 20 largest banking groups in the Gulf. It is also one of the very few players to have good geographic diversification, although this creates additional challenges for risk management and operating efficiency. The group's adequate enterprise risk management—in our assessment—and proven ability to integrate acquisitions nevertheless positions it well to handle these challenges.

AUB's core profitability has been steadily improving since 2005 but still lags that of best-performing regional peers. Return on assets decreased to 1.3% in 2008, despite the increase in interest margin and business volumes, due to a large increase in provisions (specific and general) owing to the deterioration in the operating environment. The bank's asset quality indicators remain strong, with a ratio of nonperforming loans (NPLs) to total loans of 1.9% at year-end 2008. Coverage of problem loans is adequate at 111.5% on the same date. However, the performance of its unseasoned loan portfolio—including to the real estate sector—remains to be seen in light of the weakened environment.

Loan leverage increased to 59.4% on Dec. 31, 2008, putting pressure on the bank's funding and liquidity. The ratio of customer loans to customer deposits has been improving in recent quarters but remains close to 100%. Funding benefits from large deposits from shareholders, which nevertheless exhibits reliance on wholesale deposits. AUB models its capital policy on that of banks in Organization for Economic Cooperation and Development (OECD) countries, which results in a lower capitalization than for regional peers and more aggressive use of Tier 2 subordinated debt. Although AUB has high regulatory capital ratios, with a total capital adequacy ratio (under Basel II) of 13.8% on Dec. 31, 2008, Standard & Poor's measures of capital for the bank are much lower. The ratio of adjusted total equity (ATE) to adjusted assets stood at a low 5.8% on the same date.

Outlook

The stable outlook reflects Standard & Poor's expectations that AUB will maintain its leading commercial position in Bahrain and good geographic diversification, but also a capitalization and profitability level below that of peers'. The future direction of the ratings will largely depend on the bank's capitalization, the main constrain on the ratings, and its ability to maintain the current level of asset quality. A material decline in capitalization or deterioration in liquidity would put downward pressure on the ratings. We could raise ratings if capital ratios increase substantially and at the same time the group maintains its good asset quality and strengthens its funding and liquidity profile.

Al Ahli Bank of Kuwait

PRIMARY CREDIT ANALYST: PAUL-HENRI PRUVOST, LONDON (44) 20 7176 7210, PAUL-HENRI_PRUVOST@STANDARDANDPOORS.COM

SECONDARY CREDIT ANALYST: NICOLAS HARDY, PARIS (33) 1 4420 7318, NICOLAS_HARDY@STANDARDANDPOORS.COM

ISSUER CREDIT RATING: BBB+/WATCH NEG/A-2

PUBLICATION DATE: MARCH 31, 2009

Rationale

The ratings on Al Ahli Bank of Kuwait (ABK) are primarily constrained by its limited size and a less supportive operating environment. The latter led to the fallout of local investment companies—to which ABK is highly exposed relative to its equity base—and should further weaken asset quality, earnings performance, and lead to higher concentration levels on both sides of the balance sheet. Supporting the ratings is the bank's still satisfactory capital position, expected resiliency in core operating income performance, and strategic flexibility amid the economic downturn. Standard & Poor's Ratings Services considers ABK to be a government-related entity, since it is a systemically important bank in the State of Kuwait (AA-/Stable/A-1+), which we classify as "interventionist" toward its banking system. The long-term counterparty credit rating on ABK is therefore one notch higher than its stand-alone creditworthiness. This reflects our expectation that the probability of the Kuwaiti government providing extraordinary timely support to ABK if needed is very high.

With total consolidated assets of Kuwaiti dinar (KWD) 3.0 billion ($10.4 billion), ABK is a mid size commercial bank by local and regional standards, with about 90% of its assets based in Kuwait. ABK's former strategy of aggressive expansion—to break into the top tier of local banks—is under review in light of the strong shift in the local operating environment. The former has indeed become less conducive for growth as the combination of dwindling oil prices and the global financial crisis effectively started to take its toll on the local corporate creditworthiness and private sector deposit base.

We expect ABK to focus on managing the downturn by protecting its current standing in its core corporate banking activity, rather than aggressively pursuing market shares. This strategy should encompass a deposit-driven component, leveraging on overseas branches, and increasing the domestic network. Despite a fast-decelerating trend, loans significantly outgrew core customer deposits in 2008. This resulted in a high 72.8% loans-to-deposits ratio in 2008, and an increasing recourse to higher-priced and more volatile wholesale deposits. This negative development on the funding profile and cost of funds fronts is partially mitigated by the flow of lower-priced deposits from Kuwaiti government-related entities.

The length and magnitude of the deterioration in the operating environment remains unclear. ABK's core operating performance resiliency will largely be dependent upon the government's ability to step in by providing local banks with lending opportunities through sustained government spending, adequate funding, and assistance to absorb the consequences of the local investment companies' fallout. The latter—and early signs of asset quality deterioration in a loan book that grew quickly over the past three years—also began to take its toll on ABK's financial performance in 2008 through sizable impairments and additional general provisions. This trend should persist and potentially weaken apparent satisfactory asset quality and capitalization levels.

CreditWatch

To resolve the CreditWatch placement, we will analyze the bank's detailed exposure to the investment companies (on a gross and net basis) and assess the expected impact on its stand-alone credit profile. We also need to analyze and assess the impact of the government's support package and measure the extent to which it mitigates risks. Also important is the extent of the local economy's slowdown and its impact on the bank's asset quality and financial performance. We expect to reassess the CreditWatch status shortly, following consideration of the above factors. In our opinion, we do not anticipate the ratings on the bank to be downgraded by more than one or two notches, assuming that significant government support will materialize.

Al Rajhi Bank

PRIMARY CREDIT ANALYST: NICOLAS HARDY, PARIS (33) 1 4420 7318, NICOLAS_HARDY@STANDARDANDPOORS.COM

SECONDARY CREDIT ANALYST: PAUL-HENRI PRUVOST, LONDON (44) 20 7176 7210, PAUL-HENRI_PRUVOST@STANDARDANDPOORS.COM

ISSUER CREDIT RATING: A/STABLE/A-1

PUBLICATION DATE: DECEMBER 24, 2008

Rationale

The ratings on Saudi Arabia-based Al Rajhi Bank reflect the bank's healthy customer franchise in the domestic retail sector, superior and sustained profitability, concentrations in loans and deposits that are lower than peers', and strong capitalization. The ratings are constrained by the bank's low business and geographic diversification and large maturity mismatch. In addition, the bank will have to operate in a more difficult environment due to lower oil prices and increasing competitive pressure.

Al Rajhi is the third-largest bank in terms of assets in the Kingdom of Saudi Arabia (AA-/Stable/A-1+). With the most extensive distribution network in the kingdom (about 430 branches), the bank has built up the widest demand deposit base. Given its size and retail entrenchment, Standard & Poor's Ratings Services considers Al Rajhi to be a systemically important bank in Saudi Arabia, which we classify as "interventionist" toward its banking sector. Reflecting our opinion that extraordinary government support would be likely in case of need, we uplift the long-term rating on the bank one notch above its stand-alone creditworthiness.

Al Rajhi is among the most profitable banks in the Gulf. Its robust profitability has been largely driven by increasing business volumes, high margins, and low labor costs. The bank has benefited from strong momentum in the Saudi economy and is well positioned to weather expected pressure due to its historical focus on its core retail domestic market.

Asset quality is satisfactory, with a ratio of nonperforming loans (NPLs) to gross loans of 2.6% on Sept. 30, 2008. Coverage by provisions is high at more than 130% on the same date. The NPL ratio is set to decline in fourth-quarter 2008 to a level close to the average for peers, as a result of active write-offs. Al Rajhi relies mainly on short-term retail deposits for funding and therefore maturity mismatches are material, as for most banks in the region. Business and geographic diversification remains limited, despite a recent foray into Asian Muslim markets through its Malaysian subsidiary established in 2006. Al Rajhi faces the challenge of widening the scope of its business lines by enhancing its corporate and investment banking capabilities in a more competitive market, while maintaining its strong financial profile and performance. Capitalization is among the strongest in Saudi Arabia and the whole Middle East. The bank intends to keep its dividend payout policy conservative, to alleviate further pressure on capital coming from the recent rapid growth of risk assets and the likely deterioration of the economic environment.

Outlook

The stable outlook reflects our expectation that Al Rajhi will retain its strong financial profile and leading commercial position in retail banking, despite increasing competition. We could raise the ratings if the bank materially improves business diversification out of retail lending, geographic diversification proves successful, and it further widens the funding mix to reduce maturity mismatches. The ratings may come under pressure if asset quality or capitalization weakens dramatically.

Albaraka Banking Group (B.S.C.)

PRIMARY CREDIT ANALYST: PAUL-HENRI PRUVOST, LONDON (44) 20 7176 7210, PAUL-HENRI_PRUVOST@STANDARDANDPOORS.COM

SECONDARY CREDIT ANALYST: EMMANUEL VOLLAND, PARIS (33) 1 4420 6696, EMMANUEL_VOLLAND@STANDARDANDPOORS.COM

ISSUER CREDIT RATING: BBB-/STABLE/A-3

PUBLICATION DATE: MAY 28, 2008

Rationale

The ratings on Albaraka Banking Group (B.S.C.) (ABG) reflect the group's geographic diversification, as a fully fledged Islamic banking group, good liquidity profile, and satisfactory capitalization. The current ratings are assigned to ABG—the bank holding company incorporated in Bahrain consolidating subsidiaries spanning 12 countries. They reflect ABG's stand-alone creditworthiness and do not factor in potential external support from shareholders or authorities. The group's fragmented business model, only adequate asset quality, challenging funding mix, and below regional average profitability offset these positive factors. ABG's main challenges are to develop its customer franchise, enhance profitability, and control risks, with the parent bank and its units becoming a more cohesive group.

With total assets of $10.1 billion at year-end 2007, ABG is a large banking group operating in the Middle East and North Africa, primarily engaged in retail and corporate banking. Despite its good geographic coverage, ABG lacks a strong home core market. Its main subsidiaries are based in Turkey, Jordan, and Algeria. Other ABG subsidiaries are small niche players in their respective markets. Future plans include further foray into new markets in the Middle East and the Muslim region of Asia.

ABG's main shareholders, Saudi-based conglomerate Dallah Albaraka Group (Dallah; not rated) and its founder, Sheikh Saleh Abdullah Kamel, owned a combined 54.8% stake at Dec. 31, 2007, a neutral factor for the ratings. Standard & Poor's Ratings Services, however, acknowledges that majority shareholders have been supportive to ABG in the past. The corporate governance framework is adequate and is continuously enhanced, although the group's structure makes it challenging to effectively control risks and reach economies of scale.

ABG finances the bulk of its loan portfolio with Sharia-compliant funding instruments, called profit-sharing investment accounts (PSIAs). Although a positive factor in theory, as customers should share in the group's profits or losses, this funding mix could prove detrimental in case of a major stress, triggering pressure on liquidity. ABG's liquidity profile is satisfactory, however, as about 29% of assets was considered liquid at year-end 2007.

ABG's asset quality is only adequate, although improving. The ratio of nonperforming assets (NPAs) to total financing stood at 6.3% at Dec. 31, 2007. Loan loss reserve (LLR) coverage is also only adequate, at 50.6% at the same date. About 45% of total NPAs come from its subsidiary in Egypt. Given existing collateral and recovery prospects in Egypt, high growth in assets, and a cautious lending policy, we expect the group's NPA ratio to trend downward in the short term, however.

ABG's profitability, with return on assets (ROA) and return on equity (ROE) in 2007 reaching 1.8% and 12.5%, respectively, is only adequate compared with that of banks operating in the Gulf. ABG's revenues are still dependent on its main subsidiaries, with limited ability to extract large economies of scale. Capitalization is satisfactory, although we expect it to decline along with ABG's planned growth.

Outlook

The stable outlook factors in ABG's endeavor to implement common risk management practices, address its asset-quality problems in Egypt, and extract larger economies of scale. The ratings could be raised if ABG's sources of profitability further diversify, efficiency improves, funding profile strengthens, and asset quality shows a longer track record of improvement. On the contrary, the ratings could be lowered if capitalization or liquidity comes under significant pressure; if asset quality materially deteriorates; or if ABG fails to effectively implement common practices among its various units.

Arab Banking Corp. B.S.C.

PRIMARY CREDIT ANALYST: GOEKSENIN KARAGOEZ, PARIS (33) 1 4420 6724, GOEKSENIN_KARAGOEZ@STANDARDANDPOORS.COM

SECONDARY CREDIT ANALYST: EMMANUEL VOLLAND, PARIS (33) 1 4420 6696, EMMANUEL_VOLLAND@STANDARDANDPOORS.COM

ISSUER CREDIT RATING: BBB+/STABLE/A-2

PUBLICATION DATE: APRIL 28, 2009

Rationale

The ratings on Arab Banking Corp. B.S.C. (ABC) reflect the group's strong wholesale customer franchise in the Arab world, high support from principal shareholders, good loan quality, and reduced market risk. Negative rating factors include the lack of a strong core home market, low profitability, a short-term and concentrated wholesale funding profile, and important challenges ahead to the revised group's business strategy. ABC's shareholding structure—dominated by the Kuwait Investment Authority, the Central Bank of Libya, and the Abu Dhabi Investment Authority—is a positive rating factor. The long-term rating on the bank includes a one-notch uplift from its stand-alone credit profile, based on Standard & Poor's Ratings Services' expectation that support from principal shareholders is highly likely in case of need. Shareholders demonstrated their commitment by increasing ABC's capital by $1.1 billion in June 2008. ABC allocated $1.0 billion in provisions for its impaired assets (including $733 million against structured investment vehicles and collateralized debt obligations) which led the bank to report a loss of $880 million for 2008, triggering the need for a capital increase.

ABC's strategic focus is on developing its Arab roots, with a stronger emphasis on the retail segment, with the parent bank and its units now operating as a more cohesive group. The shift toward retail appears ambitious and the group's track record in this segment is short with mixed results. Loan quality is good and on a par with regional peers', with a ratio of nonperforming loans to total loans of 1.9% at year-end 2008. The provisioning policy is conservative.

ABC's core profitability still compares unfavorably with peers', owing to the bank's business mix which lacks a retail franchise and relies on costly wholesale funding that limits interest margins. ABC reported a $32 million net profit in the first quarter of 2009. We do not expect a material improvement in the foreseeable future as business volumes are likely to decline due to the global recession. On the other hand, we believe that the downside risk has lessened considerably now that the bank has derisked its balance sheet.

The parent company's reliance on short-term funding, including repurchase agreements, is significant and a negative rating factor. ABC is using its securities portfolio (about 50% guaranteed by U.S. government agencies). The group also benefits from historically sticky deposits from regional institutions—including its shareholders, governments, and central banks—which we take as a comforting factor.

The large write-downs on the securities portfolio and aforementioned unrealized losses recognized as equity hurt the group's capitalization, but capital subsequently rebounded after the $1.1 billion capital increase. At 8.8% at end-2008, the ratio of adjusted total equity to adjusted assets is adequate and on a par with similarly rated peers' in the Gulf.

Outlook

The stable outlook reflects the substantial decrease in market risks and our expectations that the bank will maintain its adequate asset quality and capitalization. Nevertheless, the bank will find it difficult to increase business diversification in a less benign economic environment. We could lower the ratings if the group's funding and liquidity profile, core profitability, or capitalization show signs of weakening. Although unlikely in the foreseeable future, we could raise the ratings if the group can significantly strengthen its profitability and funding profile, while limiting its risk appetite.

Arab National Bank

PRIMARY CREDIT ANALYST: NICOLAS HARDY, PARIS (33) 1 4420 7318, NICOLAS_HARDY@STANDARDANDPOORS.COM

SECONDARY CREDIT ANALYST: MOHAMED DAMAK, PARIS (33) 1 4420 7322, MOHAMED_DAMAK@STANDARDANDPOORS.COM

ISSUER CREDIT RATING: A/STABLE/A-1

PUBLICATION DATE: APRIL 22, 2009

Rationale

The ratings on Saudi Arabia-based Arab National Bank (ANB) reflect the bank's strong and resilient financial performance, robust asset quality, and satisfactory liquidity. These strengths are somewhat offset by ANB's largely untested loan portfolio that has been growing rapidly in recent years, the bank's increasingly competitive environment, and uncertainties related to its international expansion. The long-term rating on ANB, classified as a systemically important bank in an interventionist country under Standard & Poor's Ratings Services' methodology, includes a one-notch uplift to reflect our expectation of strong likelihood of government support in case of need.

ANB is the seventh-largest bank in the Kingdom of Saudi Arabia (AA-/Stable/A-1+), with about 10% of system assets. Jordan-based Arab Bank PLC (BBB/Stable/A-3) has a 40% stake in ANB and is committed to its Saudi affiliate. Arab Bank PLC is the main entity of Arab Bank Group. Standard & Poor's rates some other group entities outside Jordan A-/Stable/A-2. Together with its parent, ANB submitted in 2008 a bid to acquire Egypt-based Banque du Caire (not rated). The auction was ultimately cancelled by the Egyptian authorities, but this strategic move illustrates the bank's readiness to seize business opportunities that may well enhance business diversification but also, in our opinion, weaken its financial profile.

ANB's profitability is strong and appears resilient to the weakening in the operating environment. The bank's return on assets stood at 2.3% in 2008. Profitability has been under pressure in the past two years as a result of the Saudi stock market correction in 2006 and some impairments in ANB's securities portfolio after the global market dislocation. However, ANB's exposure to structured investment products is limited and we do not expect this exposure to weigh on the bank's financial profile. ANB's liquidity is satisfactory, with about 12% of assets held in liquid forms (cash and interbank deposits) and more than two-thirds of its securities portfolio invested in Saudi government bonds that can be easily repoed in case of need.

ANB enjoys robust asset quality indicators. The bank's nonperforming assets (NPA) ratio fell to a low 0.5% of total loans, while loan loss reserves covered nonperforming loans (NPLs) by more than 2x on December 31, 2008. Like those of peers, ANB's loan portfolio, which has nearly doubled between 2005 and 2008, has not been tested through a full economic cycle, though.

ANB's capitalization is adequate for its risk profile, with a ratio of adjusted total equity to adjusted assets of 9.8% at year-end 2008. The bank's conservative dividend policy is expected to soften a potential fall in capital, if growth of risk assets resumes.

Outlook

The stable outlook reflects Standard & Poor's expectation that ANB will maintain its strong performance, despite the more difficult economic environment in Saudi Arabia. We could raise the ratings if the bank makes significant and sustained progress in diversification or boosts capital ratios substantially. However, the ratings could come under pressure if ANB's profitability starts to erode significantly, or if capital ratios or asset quality deteriorate markedly and the bank's approach toward geographic expansion proves more aggressive than we now expect.

Arcapita Bank B.S.C.

PRIMARY CREDIT ANALYST: MOHAMED DAMAK, PARIS (33) 1 4420 7322, MOHAMED_DAMAK@STANDARDANDPOORS.COM

SECONDARY CREDIT ANALYST: EMMANUEL VOLLAND, PARIS (33) 1 4420 6696, EMMANUEL_VOLLAND@STANDARDANDPOORS.COM

ISSUER CREDIT RATING: BB/WATCH NEG/B

PUBLICATION DATE: APRIL 6, 2009

Rationale

On April 6, 2009, Standard & Poor's Ratings Services lowered its long-term counterparty credit rating on Bahrain-based Arcapita Bank to 'BB' from 'BB+' and kept the rating on CreditWatch with negative implications where it was initially placed on Jan. 28, 2009. At the same time, Standard & Poor's affirmed its 'B' short-term rating on Arcapita.

The rating action reflects the very weak investment climate, which has challenged Arcapita's business model and has decreased the value of its assets in Standard & Poor's view. In this light, we believe Arcapita's leverage indicators have weakened, which has put pressure on its credit profile. Arcapita has reported that it is implementing a set of measures to reduce its leverage and improve its liquidity position. It has already:

- Raised $300 million through two-year facilities from strategic investors;
- Raised $100 million of capital from a strategic shareholder in the Gulf; and
- Sold and leased-back its head office and a related piece of land in a $400 million transaction.

We believe these measures have alleviated Arcapita's immediate short-term liquidity pressure. Additional initiatives the bank reports that it will implement in the near term include a rights issue and an extension of its debt maturity profile.

In our view, if the bank successfully completes the rights issue, this would, all other factors being equal, support the current rating. However, we still believe that the business climate will remain challenging and that there is a potential for write-downs in Arcapita's investment portfolio. The rating reflects Arcapita's stand-alone credit profile and does not include any uplift for extraordinary external support. At the same time, Standard & Poor's recognizes that support from shareholders has been significant and Arcapita's financial flexibility is a positive rating factor.

Arcapita's financial leverage (as measured by, among other indicators, the ratio of net debt to portfolio value and the ratio of adjusted total equity to portfolio value) increased in 2008. During 2009, this leverage has been decreasing and we expect it to come down further if and when the bank completes the rights issue. At the same time, we believe that the current environment is making it very difficult to reduce leverage, through placement or exit, even though Arcapita has been successful in placing some investments in recent months. The current environment is, in our view, making funding cost reduction very challenging. Consequently, Standard & Poor's expects Arcapita's financial performance to be weak in 2009 owing to the gloomy outlook for private equity, investors' limited appetite for alternative assets, and the deteriorating economic conditions in the U.S. and Europe—the two major regions of Arcapita's investments.

CreditWatch

Arcapita's capacity to execute the planned remaining measures to reduce leverage will be critical for the ratings in the short term. The successful implementation of these measures, all other factors being equal, should support the current ratings. However, we would lower the long-term rating by one notch if Arcapita is unable to raise the amount of the planned capital increase or in any other way improve its financial position to bring it in line with rating expectations. We expect to resolve the CreditWatch status in the next few weeks, following consideration of the above factors.

BankMuscat S.A.O.G.

PRIMARY CREDIT ANALYST: GOEKSENIN KARAGOEZ, PARIS (33) 1 4420 6724, GOEKSENIN_KARAGOEZ@STANDARDANDPOORS.COM

SECONDARY CREDIT ANALYSTS:
PAUL-HENRI PRUVOST, LONDON (44) 20 7176 7210, PAUL-HENRI_PRUVOST@STANDARDANDPOORS.COM;
EMMANUEL VOLLAND, PARIS (33) 1 4420 6696, EMMANUEL_VOLLAND@STANDARDANDPOORS.COM

ISSUER CREDIT RATING: BBB+/STABLE/A-2

PUBLICATION DATE: JANUARY 29, 2009

Rationale

The ratings on BankMuscat S.A.O.G. reflect a dominant commercial position in its domestic market, as well as sustained and good financial performance and asset quality. Negative rating factors include its limited geographic and business diversification outside the small and concentrated Omani economy, an only-adequate funding position, and the risks and challenges of its rapid geographic expansion that is pressuring capitalization. The long-term rating on BankMuscat is one notch higher than the bank's stand-alone creditworthiness to reflect our expectation of strong likelihood of extraordinary support, in case of need, from the Sultanate of Oman (A/Stable/A-1)—BankMuscat's largest single shareholder directly and indirectly controlling about 40% of its capital. We consider the sultanate to be interventionist toward its banking sector, and BankMuscat a systemically important bank. We therefore classify the bank as a government-related entity (GRE).

With total consolidated assets of $14.5 billion on Sept. 30, 2008, BankMuscat is a midsize universal bank by regional standards, but commands a market share of about 40% in both loans and deposits in Oman. BankMuscat is strengthening its franchise and reducing reliance on its small home market through cross-border acquisitions. Locally, the bank plans to strengthen its presence across the board. The international expansion strategy is ambitious and aggressive given BankMuscat's traditionally cautious risk profile. Apart from organic growth in the region, the bank wishes to leverage the international strategy at its Bahraini subsidiary, BMI Bank B.S.C. (BBB-/Stable/A-3), while making further forays in high-risk countries such as Pakistan (foreign currency CCC+/Developing/C; local currency B-/Negative/C). Although this rapid international expansion is contributing to increasingly diversified revenues, risk control overseas now represents a bigger challenge.

Profitability is good—thanks to high volumes and margins—and is likely to remain resilient in a less supportive environment. Asset quality measures are good. Nevertheless, the large consumer loan portfolio, representing about 40% of total loans, has risen fast recently and still has to demonstrate its resilience to more adverse conditions, especially after the recent correction in the local stock market. Fundamentals remain sound in Oman; however, it is unclear how much lending will slow amid tighter operating conditions. These factors therefore point to a potential heightening of credit risk.

BankMuscat's funding profile, which shows some reliance on wholesale funding, is only adequate by regional standards. The customer loans-to-core customer deposits ratio has consistently been above 100% over recent years—a negative factor in a period of liquidity tightening. We expect BankMuscat to continue exploring alternative funding strategies to tackle this issue.

Outlook

The stable outlook balances the more difficult operating environment and pressure on funding with our expectations that BankMuscat will remain the dominant player in Oman. We expect the bank's ownership structure to remain broadly stable, with no weakening of links with the Omani government. We could consider a positive rating action if BankMuscat demonstrates a resilient financial profile and commercial position while it expands overseas and amid a tougher and more competitive environment, further diversifies its revenue base, and materially improves its funding profile. Conversely, negative pressure on the ratings would stem from a material deterioration in capitalization, funding, or asset quality, or the bank's inability to control risks in its overseas network.

Banque Saudi Fransi

PRIMARY CREDIT ANALYST: NICOLAS HARDY, PARIS (33) 1 4420 7318, NICOLAS_HARDY@STANDARDANDPOORS.COM

SECONDARY CREDIT ANALYST: FRANCOIS MONEGER, PARIS (33) 1 4420 6688, FRANCOIS_MONEGER@STANDARDANDPOORS.COM

ISSUER CREDIT RATING: A/STABLE/A-1

PUBLICATION DATE: APRIL 22, 2009

Rationale

The ratings on Saudi Arabia-based Banque Saudi Fransi (BSF) reflect its good market position, low risk profile, strong financial performance, and technical support from being part of group Crédit Agricole (main entity: Crédit Agricole S.A.; AA-/Stable/A-1+) through its parent, Calyon (AA-/Stable/A-1+). The long-term rating on BSF, a government-related entity (GRE) under Standard & Poor's Ratings Services' methodology, includes a one-notch uplift above the stand-alone credit profile. This reflects our expectation of strong likelihood of extraordinary government support if needed, given the bank's systemic importance, which mainly stems from its domestic market position and importance to the economy of the Kingdom of Saudi Arabia (AA-/Stable/A-1+). The ratings are constrained by credit risk related to the loan portfolio that has been growing rapidly until recently and remains to be tested through a full economic cycle, concentration risks, and limited diversification outside corporate finance, the bank's historical core market.

BSF is 31.1% owned by French corporate and investment bank Calyon, which is fully owned by Crédit Agricole (CASA). BSF benefits from a technical service agreement with its French parent. Calyon also seconds key senior staff to its Saudi affiliate. The extent to which Calyon would support its affiliate depends on commercial and financial considerations. In many stressful scenarios, support would be likely, but cannot be assumed in all circumstances. Therefore, we give no uplift to the ratings for this potential support.

BSF is the sixth-largest bank in Saudi Arabia, with total assets of Saudi Arabian riyal (SAR) 125 billion ($33.6 billion) on Dec. 31, 2008. BSF is a significant player in the Saudi banking system, but its overall commercial position is only average. Traditionally focused on corporate banking, so far the main driver of its profitability, BSF is less entrenched in the lucrative retail segment than most of its domestic peers and is now actively building on synergies with Crédit Agricole group to reduce this gap.

BSF's lending book has been growing rapidly in the recent past (35% in 2008), thanks to the buoyant Saudi economy and waves of new projects for its corporate clients, and asset quality indicators have improved.

However, we have noticed a slight reversal by the end of 2008, with the ratio of nonperforming loans to total loans standing at 0.93%, compared with 0.72% a year before. Asset quality indicators are likely to continue deteriorating systemwide because customers are facing a more challenging environment. We nevertheless expect the deterioration to be limited at the bank level. It is still unclear at that stage if government spending, aiming to upgrade the country's infrastructure, will fully compensate for the economic slowdown. BSF's corporate loan book displays some concentration by name and sector, a feature shared by all Saudi banks active in this segment, while loan leverage is higher than the domestic average. The slowdown of the local economy, and consequently a more cautious approach toward lending growth, should alleviate some pressure on funding. The ratio of loans to customer deposits stood at 88% at year-end 2008, compared with 82% a year ago.

The bank's financial performance remains strong, with return on equity at 24.5% for 2008. BSF's return on assets has shown some signs of erosion, declining to 2.5% in 2008 from 4.1% in 2006, as a result of stiffening competition and a sizable reduction of brokerage-related revenues related to the Saudi stock market correction. Liquidity is satisfactory, with 22% of assets invested in securities, mainly in Saudi government bonds that can easily be repoed and 8% of assets held in liquid forms (cash and interbank deposits) on Dec. 31, 2008.

BSF's capitalization remains sound, although it declined in line with the rapid growth of risk assets. The negative trend was limited due to a conservative dividend policy. On Dec. 31, 2008, adjusted total equity stood at 9.6% of adjusted total assets, in line with that of most domestic peers. The bank's sound capital base serves as a cushion against concentration risks that are difficult to overcome within the undiversified Saudi economy.

Outlook

The stable outlook reflects our expectation that BSF will protect its market position and maintain its strong financial performance. The ratings are constrained by structural weaknesses in the Saudi economy and the bank's limited diversification compared with that of international banks. The ratings could come under pressure if BSF's appetite for risk increases, market share erodes significantly, quality of core earnings declines, or capitalization or asset quality deteriorate materially. We could raise the ratings if the bank's asset quality indicators prove resilient to the Saudi economic slowdown, and solid earnings allow the bank to further strengthen its capitalization and enhance its market position.

BMI Bank B.S.C.

PRIMARY CREDIT ANALYST: GOEKSENIN KARAGOEZ, PARIS (33) 1 4420 6724, GOEKSENIN_KARAGOEZ@STANDARDANDPOORS.COM

SECONDARY CREDIT ANALYSTS:
PAUL-HENRI PRUVOST, LONDON (44) 20 7176 7210, PAUL-HENRI_PRUVOST@STANDARDANDPOORS.COM
EMMANUEL VOLLAND, PARIS (33) 1 4420 6696, EMMANUEL_VOLLAND@STANDARDANDPOORS.COM

ISSUER CREDIT RATING: BBB-/STABLE/A-3

PUBLICATION DATE: JANUARY 27, 2009

Rationale

The ratings on BMI Bank B.S.C. reflect its ownership structure, strong capitalization, and limited market risk. BMI is 49% owned and controlled by BankMuscat S.A.O.G. (BBB+/Stable/A-2), which is itself controlled by the Sultanate of Oman (A/Stable/A-1). Standard & Poor's Ratings Services considers that BMI's part ownership by, close cooperation with, and strategic importance to BankMuscat mean that strong support would be highly likely in case of need. The good track record of support also underpins our opinion. BMI's long-term rating is therefore two notches above the bank's stand-alone creditworthiness. The ratings are constrained by BMI's small size and limited track record, high concentration risk and recent fast growth in lending, and weak funding profile. They already factor in BMI's planned provision for a €10 million exposure on Iceland-based Landsbanki (not rated).

BMI is a small commercial bank in the Kingdom of Bahrain (A/Stable/A-1). Major recent developments include the appointment of a new management team in 2007, and a $250 million capital injection in early 2008 to support the bank's domestic and cross-border growth. The bank made significant improvements last year to enterprise risk management (ERM) in continuing to overhaul its framework, but it is unclear how the bank will roll out new policies and how effective they will be. The loan portfolio grew about 90% in 2008 and the more difficult environment has increased credit risk materially. However, the bank has recently decided to shift to a more conservative strategy by changing its business mix and slowing growth at the expense of short-term profitability.

Fast-paced growth also puts additional pressure on an already weak funding profile. Indeed, BMI's limited franchise in the small Bahraini market means it has limited access to customer deposits and must rely heavily on wholesale funding. Our concerns are lessened by the parent's significant funding support of BMI and its plan to limit growth in 2009.

Financial performance is satisfactory, although heavily skewed toward interest income. Volumes have risen fast in 2008, but BMI's margins have been constrained by a higher cost of funds due to a heavy reliance on interbank deposits and losses at its newly launched domestic and overseas operations. BMI's exposure to the nationalized Landsbanki stands to trigger significant provisions, hurting the bank's bottom-line results. On a positive note, capitalization remains strong subsequent to the sizable capital injection in 2008 and is likely to become stronger over the medium term.

Outlook

The stable outlook balances BMI's strong capital position, the commitment from BankMuscat, improvements in its risk management, weak funding profile, limited commercial position, and challenging overseas expansion. We could consider a positive rating action if the bank materially improves its funding profile, establishes a stronger and sustainable domestic market position, and achieves greater business diversification—resulting in higher and more sustainable financial performance. Conversely, the ratings would be under negative pressure if the bank's funding profile deteriorates materially, asset quality worsens significantly, or international expansion proves riskier than we currently expect. Although not likely, a weakening of the links with BankMuscat would also have a negative impact on the ratings.

Burgan Bank

PRIMARY CREDIT ANALYST: PAUL-HENRI PRUVOST, LONDON (44) 20 7176 7210, PAUL-HENRI_PRUVOST@STANDARDANDPOORS.COM

SECONDARY CREDIT ANALYST: NICOLAS HARDY, PARIS (33) 1 4420 7318, NICOLAS_HARDY@STANDARDANDPOORS.COM

ISSUER CREDIT RATING: BBB+/WATCH NEG/A-2

PUBLICATION DATE: MARCH 31, 2009

Rationale

The ratings on Burgan Bank are primarily constrained by the uncertainty relative to its expansion strategy, weakened capital levels, and concerns on trend in asset quality, notably in the real estate and investment companies' segments. The latter are due to the less supportive Kuwaiti operating environment that led to the fallout of investment companies—to which Burgan is highly exposed relative to its equity base and uncertainty pertaining to the form of the government's support package. Supporting rating factors include a still satisfactory funding and liquidity profile, expected resiliency in core operating performance, and clearer strategic focus. Standard & Poor's Ratings Services considers Burgan to be a systemically important bank in the State of Kuwait (AA-/Stable/A-1+), which we classify as "interventionist" toward its banking system. The long-term counterparty credit rating on Burgan is therefore one notch higher than its stand-alone credit profile, to reflect our very high expectation that the Kuwaiti government would provide extraordinary support to Burgan if needed. The bank is therefore considered as a Government Related Entity (GRE) under our methodology.

With total consolidated assets of Kuwaiti dinar (KWD) 3.9 billion ($13.4 billion) at Dec. 31, 2008, Burgan is a midsize commercial bank by local and regional standards, with about 70% of its consolidated assets based in Kuwait. In 2008, Burgan revealed an ambitious expansion strategy based on the acquisition of stakes held by Bahrain-based United Gulf Bank (UGB; not rated), an investment banking institution also majority-owned by Kuwait Projects Co. (Holding) K.S.C. (KIPCO; BBB+/Stable/A-2). The first milestone was reached by securing majority ownership in Jordan Kuwait Bank (JKB; not rated) in July 2008, which now accounts for about one-fifth of Burgan's consolidated assets. We expect Burgan to continue part of its overseas expansion in the coming quarters, although its financing remains largely unclear and could further impact a weakened—and just adequate—capital position. Although we expect the geographic expansion strategy to benefit Burgan's business profile and earnings diversification in the long term, the bank's ability to replicate its tight risk management practices—to limit credit and operational risks in higher-risk countries—will prove challenging.

Burgan's funding and liquidity profile remained adequate in 2008. However, the Kuwaiti operating environment became far less conducive for growth during the second half of 2008 as dwindling oil prices and the global financial crisis started to take its toll on the local corporate creditworthiness and private sector deposit base. The length and magnitude of the deterioration in the operating environment remains even more unclear. We also express some concern about the bank's exposure to the local real estate and construction sectors, which accounts for about 40% of its domestic sector.

Financial performance will rely on the government's ability to step in by providing local banks with lending opportunities through sustained government spending, adequate funding, and assistance to absorb the consequences of the local investment companies' fallout. The latter, and early signs of weakening asset quality in a loan book that grew quickly in recent years, also began to show on Burgan's financial performance in 2008 through sizable, but voluntary, additional general provisioning. The trend should persist in future quarters, but we take some comfort from Burgan's conservative and high coverage levels.

CreditWatch

Burgan Bank was placed on CreditWatch with negative implications on Feb. 16, 2009. To resolve the CreditWatch placement, Standard & Poor's will analyze the bank's detailed exposure to the investment companies (on a gross and net basis) and assess the expected impact on its stand-alone credit profile. We also need to analyze and assess the impact of the government's support package and measure the extent to which it mitigates risks. Other important factors to take into account are the extent of the local economy slowdown, its impact on the bank's asset quality and financial performance, as well as the upcoming completion of the banks' expansion strategy. We expect to reassess the CreditWatch status in the coming weeks following consideration of the above factors. In our opinion, we do not anticipate the bank to be downgraded by more than one or two notches, assuming that significant government support will materialize.

Commercial Bank of Kuwait

PRIMARY CREDIT ANALYST: NICOLAS HARDY, PARIS (33) 1 4420 7318, NICOLAS_HARDY@STANDARDANDPOORS.COM

SECONDARY CREDIT ANALYST: PAUL-HENRI PRUVOST, LONDON (44) 20 7176 7210, PAUL-HENRI_PRUVOST@STANDARDANDPOORS.COM

ISSUER CREDIT RATING: A-/WATCH NEG/A-2

PUBLICATION DATE: APRIL 29, 2009

Rationale

The ratings on Commercial Bank of Kuwait (CBK) reflect the bank's good commercial position, strong revenue generating capacity, and adequate capitalization. The long-term rating on CBK, a government-related entity (GRE) under Standard & Poor's Ratings Services' methodology, includes a one-notch uplift above its stand-alone credit profile. This reflects our expectation of the strong likelihood of extraordinary government support in case of need, given the bank's systemic importance, which mainly stems from its leading market position. Offsetting these positive factors are concentration risks in a mono-industrial economy, including significant exposures to the local real estate sector and distressed local investment companies, a growing reliance on wholesale funding, and limited business and geographic diversification.

On Feb. 16, 2009, Standard & Poor's placed its long-term rating on CBK on CreditWatch with negative implications. At the same time, the 'A-2' short-term counterparty credit rating was affirmed (see "Various Kuwaiti Banks Placed On CreditWatch Negative On Large Exposure To Investment Companies," published Feb. 16, 2009, on RatingsDirect). This rating action reflects our expectation that the bank's exposure to the distressed local investment companies sector and rapidly deteriorating local real estate market is likely to weaken its stand-alone credit profile amid an already weakening operating environment. This exposure represented about 13% of gross loans and 71% of adjusted total equity (ATE), and 23.7% of gross loans or 139% of ATE, respectively, on Dec. 31, 2008. We understand that the Kuwaiti government is about to implement supportive measures to stabilize the local financial markets, including the commercial banking sector. If approved and executed, the support package would improve the bank's operating environment and therefore help its stand-alone credit profile. With Kuwaiti dinar (KWD) 4.3 billion ($15.8 billion) in total assets at year-end 2008, CBK ranked No. 4 among banks in the State of Kuwait (AA-/Stable/A-1+), with a market share of about 11%.

CBK's profitability over the past five years has been strong while growth of risk assets has been rapid. The loan book, which has doubled since the end of 2005, has yet to be tested through a full economic cycle. As customer deposits do not fully fund loans, the bank relies on the regional interbank market. Return on assets declined to 2.3% in 2008 from 3.3% in 2007, due to the higher cost of credit risk recognized during the fourth quarter, in addition to some limited impairment of investment securities. Return on equity also declined but remained high at 26.6% for 2008. Although nonperforming loans (NPLs) are higher than regional peers', at 5.2% of total gross loans on Dec. 31, 2008, the bulk are preinvasion (that is, dating before August 1990). These NPLs are fully covered by specific loss reserves and therefore do not affect the bank's current risk profile. Postliberation NPLs (dating after February 1991) accounted for a low 1.7% of total gross loans at the same date, strongly covered.

The bank's adequate capitalization is a positive rating factor. We understand that the management's intention to grow overseas has been put on hold due to the current global market conditions.

CreditWatch

To resolve the CreditWatch placement, Standard & Poor's will analyze the bank's detailed exposure to the investment companies (on a gross and net basis) and assess the expected impact on its stand-alone credit profile. We also need to analyze and assess the impact of the government's support package and measure the extent to which it mitigates risks. Lastly, additional important factors we will take into account are the extent of the local economy slowdown and its impact on asset quality and financial performance. We expect to reassess the CreditWatch status in the coming weeks or months following consideration of the above factors. In our opinion, we do not anticipate the ratings on the bank to be lowered by more than one or two notches, assuming that significant government support will materialize.

Commercial Bank of Qatar (The)

PRIMARY CREDIT ANALYST: MOHAMED DAMAK, PARIS (33) 1 4420 7322, MOHAMED_DAMAK@STANDARDANDPOORS.COM

SECONDARY CREDIT ANALYST: EKATERINA TROFIMOVA, PARIS (33) 1 4420 6786, EKATERINA_TROFIMOVA@STANDARDANDPOORS.COM

ISSUER CREDIT RATING: A-/STABLE/A-2

PUBLICATION DATE: MARCH 11, 2009

Rationale

The ratings on The Commercial Bank of Qatar (CBQ) reflect the bank's good commercial position, satisfactory financial profile, and improving geographic diversification. The ratings are constrained by the bank's less supportive operating environment, narrow domestic market with high concentration risks, and rapid loan growth. Standard & Poor's Ratings Services considers CBQ to be a systemically important bank in the State of Qatar (AA-/Stable/A-1+), which we classify as "interventionist" toward its banking system. Therefore, the long-term rating on CBQ is one notch above the bank's stand-alone credit profile, reflecting our expectation of the high likelihood of exceptional support in case of need.

The second-largest bank in Qatar, CBQ is a midsize player by regional standards, with assets totaling Qatari riyal (QAR) 61.3 billion ($16.8 billion) at year-end 2008. The bank acquired a 40% stake in Sharjah-based United Arab Bank (UAB; not rated) in 2007 and previously bought a 34.8% stake in National Bank of Oman (NBO; not rated). While these purchases have improved CBQ's geographic diversification, the risk profile of these institutions is higher than that of CBQ's domestic core businesses.

With the acquisitions, CBQ's capitalization declined, because Standard & Poor's deducts equity in unconsolidated subsidiaries from its adjusted total equity (ATE) calculation. But thanks to a capital hike in 2008, capitalization recovered to an adequate ratio of ATE to total assets of 8.7% at year-end 2008. In January 2009, CBQ also benefited from a QAR807 million capital injection from the Qatar Investment Authority (QIA, not rated), which plans to make another capital increase of the same amount by the end of the year.

CBQ's operating environment is becoming less supportive because of the global financial crisis and its impact on the oil and non-oil sectors in Qatar. Standard & Poor's expects this trend to trigger a limited deterioration of CBQ's asset quality and financial performance. Although weakening, the bank's funding and liquidity profile is adequate. While maturity mismatches have been increasing in the past five years, the stability of customer deposits and the high contribution of the government and its related entities to funding (42.4% at year-end 2008) mitigate the related risk.

Outlook

The stable outlook balances CBQ's good commercial position and satisfactory financial profile with its less supportive operating environment. We would lower the ratings if the bank's liquidity, profitability, or asset quality deteriorate more rapidly than we now expect or if the credit profile of the bank's associates weakens significantly. We see limited room for a positive rating action in the foreseeable future. In the longer term, we could raise the ratings if CBQ strengthens its financial profile, reduces concentration risk, and demonstrates its ability to limit and control risks at its associates.

Doha Bank

PRIMARY CREDIT ANALYST: MOHAMED DAMAK, PARIS (33) 1 4420 7322, MOHAMED_DAMAK@STANDARDANDPOORS.COM

SECONDARY CREDIT ANALYST: EKATERINA TROFIMOVA, PARIS (33) 1 4420 6786, EKATERINA_TROFIMOVA@STANDARDANDPOORS.COM

ISSUER CREDIT RATING: A-/STABLE/A-2

PUBLICATION DATE: NOVEMBER 6, 2008

Rationale

The ratings on Qatar-based Doha Bank (DB) reflect its good market position; above average, albeit potentially volatile, financial performance; and strong capitalization. Rating constraints are the bank's very fast growth, significant exposure to the real estate sector and local and regional stock markets, concentration risks in a narrow domestic market, and the fierce competition in its operating environment. Standard & Poor's Ratings Services considers DB as systemically important to the State of Qatar (AA-/Stable/A-1+) and we expect government support to be forthcoming should the need arise. Therefore, the long-term rating on the bank includes a one-notch uplift from its stand-alone creditworthiness.

The third-largest bank in Qatar, DB remains a midsize financial institution by regional standards, with assets totaling Qatari riyal (QAR) 37.5 billion ($10.3 billion) on Sept. 30, 2008. DB's organic growth has been very rapid over the past three years amid highly supportive economic conditions. This growth remains untested by a sharp economic downturn or a shock in the real estate sector—one of the main sources of the bank's growth. Nevertheless, we do not expect a domestic downturn or real estate shock as part of our base case scenario, even though the global economic environment is becoming more challenging and we cannot rule out potential contagion to Qatar.

DB's financial performance is stellar, albeit potentially volatile given the bank's high exposure to local and regional stock markets—about 18% of its adjusted total equity (ATE) on Sept. 30, 2008. It is possible that DB will have to constitute provisions for this exposure in light of the slump in local and regional stock markets over the past three months. On Sept. 30, 2008, the bank's revaluation reserves were negative QAR242.9 million. Ample margins, strong efficiency, and low cost of risk continue to support DB's profitability. Nonperforming loan (NPL) ratios are in line with the regional average standing at 2.0% on Sept. 30, 2008, while NPL coverage by specific provisions is below the regional average at 62.9%. In contrast with the corporate banking books of rated peers, DB's book displays limited exposures to the government sector and is skewed toward more lucrative retail and private sector family businesses, the latter being more risky.

DB's liquidity is just adequate with 13.7% in liquid forms and about 50% of the bank's portfolio placed in government bonds on Sept. 30, 2008. The bank enjoys good access to government and retail deposits but maturity mismatches are high. Therefore, DB resorted to wholesale funding through the issuance of subordinated debt—$340 million in 2006—and a syndicated loan—$350 million in 2007. The bank plans to continue accessing wholesale funding when market conditions return to normal through the issuance of sukuk (financial certificates similar to bonds and compliant with Islamic law).

DB's capitalization is strong for its risk profile. Despite its diversified shareholding structure, the bank benefits from strong financial flexibility as demonstrated by the recent rights issue—about QAR1.1 billion—that was oversubscribed. In the future, DB plans to issue global depositary receipts (GDR) to accompany asset growth and finance strategic acquisitions outside its home country.

Outlook

The stable outlook balances DB's good financial profile with the risks attached to the bank's exposure to the real estate sector and operation in an untested environment where competition is high. We could raise the ratings if the bank succeeds in enhancing funding granularity and further diversifying its activities across business lines and regions while keeping the same financial profile. The ratings could come under pressure if profitability deteriorates significantly, or economic conditions worsen in Qatar, or if there is a shock on the real estate market, or if the bank's geographic expansion proves more aggressive than we expected.

Dubai Islamic Bank

PRIMARY CREDIT ANALYST: MOHAMED DAMAK, PARIS (33) 1 4420 7322, MOHAMED_DAMAK@STANDARDANDPOORS.COM

SECONDARY CREDIT ANALYST: EMMANUEL VOLLAND, PARIS (33) 1 4420 6696, EMMANUEL_VOLLAND@STANDARDANDPOORS.COM

ISSUER CREDIT RATING: A-/WATCH NEG/A-2

PUBLICATION DATE: APRIL 6, 2009

Rationale

The ratings on Dubai Islamic Bank (DIB), based in the United Arab Emirates (UAE, not rated), reflect the bank's adequate financial performance, just adequate liquidity, and good capitalization. Partially offsetting these positive factors are DIB's weakening operating environment, high exposure to the domestic real estate sector, and rapid loan growth, as well as the fierce competition in the banking sector in the Emirate of Dubai (not rated). The long-term rating on DIB is two notches above the bank's stand-alone credit profile to reflect Standard & Poor's Ratings Services' expectation of strong likelihood of support from the Emirate of Dubai, the bank's largest shareholder, in case of need. We classify DIB as a government-related entity (GRE) under our methodology.

Standard & Poor's placed its long-term counterparty credit rating on DIB on CreditWatch with negative implications on March 17, 2009. This action reflects our growing concerns regarding the impact on the banking sector of the economic downturn in Dubai.

With total assets of United Arab Emirates dirham (AED) 85.0 billion on Dec. 31, 2008, DIB controls a market share of about 8% of the UAE banking system's total deposits. The bank is heavily exposed to the real estate sector—its historical core competence—representing more than one-quarter of the bank's assets and 2.7x of adjusted total equity on Dec. 31, 2008. Standard & Poor's views this exposure as an important source of risk in light of the ongoing correction in the sector. DIB's asset quality is therefore under pressure, and provisioning needs are growing, putting the bank's profitability at risk. DIB's exposure to the stock market is another source of risk as shown by the steep decline in revaluation reserves which reached negative AED888.7 million at year-end 2008 compared with AED1.0 billion at year-end 2007. Moreover, the bank took about AED500 million in its profit and loss statement as provisions and revaluation loss on investments in 2008. The bank may need to take more provisions if the Dubai Financial Market is not stabilized. In addition, DIB has taken no provisions on the decline of the market value of some of its affiliates, because these are accounted for as associated companies. Standard & Poor's views negatively this decision because it may lead to future impairments.

DIB's funding profile appears adequate, with a ratio of loans to deposits of 81.1% on Dec. 31, 2008, which is significantly lower than rated peers'. DIB's immediately available liquidity declined significantly in 2008 and reached 6.4% of total assets at year-end 2008 compared with 22.9% at year-end 2007. Nevertheless, the bank has a large portfolio of sukuk that can be used as a source of emergency liquidity if needed. In addition, we expect the central bank to provide DIB with extraordinary liquidity support should the need arise, owing to our view that DIB is systemically important and that the authorities are interventionist toward their banking system. DIB's capitalization is good for the bank's risk profile, and the dividend payout is somewhat conservative.

CreditWatch

To resolve the CreditWatch placement, Standard & Poor's will assess the expected impact of the deteriorating economic and real estate sector conditions on the financial profile of DIB. We will also update our assessment of the government of Dubai's willingness and capacity to provide extraordinary support to the bank in case of need, in light of the changing environment and its related impact on the bank's creditworthiness. After consideration of these elements, we expect to resolve the CreditWatch status in the coming six weeks. We do not anticipate lowering the ratings on DIB by more than one notch, based on our current expectations.

Emirates Bank International PJSC

PRIMARY CREDIT ANALYST: PAUL-HENRI PRUVOST, LONDON (44) 20 7176 7210, PAUL-HENRI_PRUVOST@STANDARDANDPOORS.COM

SECONDARY CREDIT ANALYST: MOHAMED DAMAK, PARIS (33) 1 4420 7322, MOHAMED_DAMAK@STANDARDANDPOORS.COM

ISSUER CREDIT RATING: A/WATCH NEG/A-1

PUBLICATION DATE: APRIL 22, 2009

Rationale

The ratings on Emirates Bank International PJSC (EBI) reflect the bank's sound financial performance, improving business diversification, and strong market position in the United Arab Emirates (UAE, not rated). These factors are somewhat offset by EBI's exposure to the Emirate of Dubai's (not rated) economy; high geographic concentration; and recent fast growth in assets, which has put strong pressure on funding and capitalization. The long-term rating on EBI is two notches above the bank's stand-alone credit profile to reflect Standard & Poor's Ratings Services' expectation of strong likelihood of support from the authorities, in case of need. EBI is classified as a government related entity under our methodology. EBI is wholly-owned by Emirates NBD PJSC (ENBD, not rated), which acts as the holding company for both EBI and National Bank of Dubai (NBD, A/Watch Neg/A-1). ENBD is in turn 56% owned by the government of Dubai.

Standard & Poor's placed its long-term counterparty credit rating on EBI on CreditWatch with negative implications on March, 17, 2009, due to our concerns on the economic conditions and real estate sector in Dubai.

With $51.9 billion of total assets on Dec. 31, 2008, EBI is one of the largest banks in the UAE. We expect EBI's commercial position to be enhanced following the effective completion of the planned merger with NBD—scheduled for the second quarter of 2009.

Given the weakening operating environment in Dubai, we consider the combination of fast loan growth in recent years and sustained high concentration by sectors and names as heightening credit risk. EBI is exposed to the local real estate sector, with related assets representing about 2x of its adjusted total equity. This exposure is viewed as a key source of risk in light of the ongoing correction in the sector. Given a less supportive environment, we deem EBI's strong asset quality to be under pressure. This will ultimately put pressure on EBI's profitability in 2009, as provisioning on the loan book and investment portfolio may increase in a context of slowing business growth and equity markets correction. EBI's loan-to-deposit ratio has been higher than peers in recent years as the bank's funding profile is more diversified, with higher access to wholesale funding. This is a negative rating factor in a period of tight access to the wholesale market and fierce competition to attract customer deposits. Pressure on funding is nevertheless partially offset by the injection of government funds into the domestic banking system.

Fast growth in risk assets in recent years has also steadily put pressure on capitalization that is now below domestic average. EBI's revaluation reserves registered a steep decline to enter negative territory in 2008 as a result of the deterioration in credit spreads and stock markets throughout the year. On a positive note, we understand that ENBD is planning to increase its capital through a Tier I injection in the near future. ENBD's regulatory capital ratio should also benefit from the expected conversion into Tier II capital of the combined UAE dirham 12.6 billion of deposits received by EBI and NBD from the Federal authorities.

CreditWatch

To resolve the CreditWatch placement, Standard & Poor's will assess the expected impact of the deteriorating economic and real estate sector conditions on EBI's financial profile. We will also update our assessment of the Dubai government's willingness and capacity to provide extraordinary support to the bank if needed, in light of the changing environment and its related impact on the bank's credit profile. After consideration of these elements, we expect to resolve the CreditWatch status in the coming six weeks. We do not anticipate to lower the ratings on the bank by more than one notch, based on our current expectations.

Gulf Bank

PRIMARY CREDIT ANALYST: PAUL-HENRI PRUVOST, LONDON (44) 20 7176 7210, PAUL-HENRI_PRUVOST@STANDARDANDPOORS.COM

SECONDARY CREDIT ANALYSTS:
NICOLAS HARDY, PARIS (33) 1 4420 7318, NICOLAS_HARDY@STANDARDANDPOORS.COM
EMMANUEL VOLLAND, PARIS (33) 1 4420 6696, EMMANUEL_VOLLAND@STANDARDANDPOORS.COM

ISSUER CREDIT RATING: A-/WATCH NEG/A-2

PUBLICATION DATE: APRIL 27, 2009

Rationale

The ratings on Gulf Bank are primarily constrained by the weakened economic conditions in Kuwait, putting pressure on the bank's profitability and asset quality, its lack of geographic diversification, and high concentrations in lending. Positive rating factors are the bank's strong commercial position as the second-largest bank in Kuwait, as well as its systemic importance and government support that enabled it to maintain adequate funding and liquidity and restore capitalization. On Feb. 16, 2009, Standard & Poor's Ratings Services maintained its 'A-' long- and 'A-2' short-term counterparty credit ratings on Gulf Bank on CreditWatch with negative implications, where they had originally been placed on Oct. 27, 2008.

We consider Gulf Bank to be a systemically important bank in the State of Kuwait (AA-/Stable/A-1+), which we classify as interventionist toward its banking system. The long-term counterparty credit rating on Gulf Bank is therefore one notch higher than its stand-alone credit profile, to reflect our high expectation that the Kuwaiti government would provide extraordinary support to the bank if needed. This expectation has been fully met since October 2008, with authorities providing strong funding and capital support to Gulf Bank after it incurred a Kuwaiti dinar (KWD) 375 million total loss, out of which KWD268 million were related to customers' dealings in derivatives contracts through the bank and the remainder being a mix of impairment on investment securities and loan provisions. Gulf Bank is classified as a government-related entity under our methodology. Gulf Bank increased its capital in early 2009 to restore equity at the pre-event level, with a Tier 1 and total capital-adequacy ratios standing at 10.1% and 13.8%, respectively, at Jan. 31, 2009. Core shareholders broadly maintained their original stakes as expected, while Kuwait Investment Authority (KIA; not rated) bought the unsubscribed rights issue to gain a 16% stake.

The current scope of the CreditWatch placement with negative implications encompasses both our ongoing review of the event that occurred in October 2008, as well as our concerns linked to the bank's large exposure to troubled local investment companies. (For more information see "Various Kuwaiti Banks Placed On CreditWatch Negative On Large Exposure To Investment Companies," published on Feb. 16, 2009, on RatingsDirect.) The Kuwaiti operating environment became far less conducive since the second half of 2008 as dwindling oil prices and the global financial crisis started to take its toll on the local corporate creditworthiness and private sector deposit base. The length and magnitude of the deterioration in the operating environment remains unclear and could further take its toll on Kuwaiti banks' asset quality and profitability. Specific to Gulf Bank, the nonperforming loans ratio jumped to 12.7% at Dec. 31, 2008. This was largely inflated by the classification of a KWD201 million related exposure linked to the derivative contracts that generated massive losses.

CreditWatch

To resolve the CreditWatch placement, Standard & Poor's will assess the expected impact of the current market conditions on the bank's financial profile, and analyze its revised strategy and quality of its risk management practices. We will also assess the expected mitigating effect on Kuwaiti banks' risks of the government's stability package amid the local economy slowdown. We expect to reassess the CreditWatch status in the coming weeks following consideration of the above factors. In our opinion, we do not anticipate the ratings on Gulf Bank to be lowered by more than one or two notches.

Gulf Finance House

PRIMARY CREDIT ANALYST: EMMANUEL VOLLAND, PARIS (33) 1 4420 6696, EMMANUEL_VOLLAND@STANDARDANDPOORS.COM

SECONDARY CREDIT ANALYST: MOHAMED DAMAK, PARIS (33) 1 4420 7322, MOHAMED_DAMAK@STANDARDANDPOORS.COM

ISSUER CREDIT RATING: BBB-/NEGATIVE/A-3

PUBLICATION DATE: JANUARY 26, 2009.

Rationale

On Jan. 26, 2009, Standard & Poor's Ratings Services revised its outlook on Bahrain-based Gulf Finance House (GFH) to negative from stable. At the same time, we affirmed the 'BBB-/A-3' long- and short-term counterparty credit ratings on the bank.

The outlook revision reflects the increasingly difficult environment in which the bank operates, which is likely to limit its capacity to execute new transactions and therefore lead to a weaker financial performance. In addition, the value of GFH's own investments, largely illiquid by nature, is set to decline. On a positive note, we believe that the nature of these assets means that they are less subject to marked-to-market deterioration than those of GFH's peers.

The ratings on GFH reflect its good financial performance, low and flexible cost base, adequate liquidity position, and satisfactory capitalization. These positive factors are balanced, however, by the bank's low business diversification, high financial leverage (as measured by the ratio of net debt to estimated portfolio value), significant reputation and concentration risks, and potential for earnings volatility. The ratings reflect the bank's stand-alone creditworthiness and do not incorporate any uplift for external support.

GFH is an Islamic wholesale investment bank based in the Kingdom of Bahrain (A/Stable/A-1). Its main focus and area of expertise is economic infrastructure projects, capitalizing on reforms to liberalize and diversify some emerging market economies. With total assets of $3.5 billion on Sept. 30, 2008, GFH is a small institution compared with international peers and therefore is more exposed to concentration risks. Geographic and sector concentration are high, as the bank is capitalizing on mushrooming infrastructure, real estate, and industrial projects across the region. As it relies on only a few market-sensitive business lines and transactions, the bank has a limited cushion against the current economic downturn, which is resulting in investment opportunities and investor appetite shrinking and assets becoming illiquid and reducing in value.

GFH has recorded very strong financial performance since its inception in 1999. Net profit reached $302.4 million in the first nine months of 2008, on the back of few large transactions. The bank's funding and liquidity profile is adequate. It is currently a net placer of funds in the interbank market and medium-term debt matures only in 2010 and 2012. Capitalization was down in 2007 because of rapid asset growth and a large dividend distribution, and is now only satisfactory, with adjusted total equity (ATE) at 21.5% of adjusted assets on Sept. 30, 2008. We consider the bank's leverage to be high. In addition, we consider the bank's assets to be relatively illiquid, limiting its capacity to reduce leverage.

Outlook

The negative outlook reflects our expectation that the deteriorated environment—limiting investment placements and exits and putting pressure on the value of GFH's own investments and financial performance—will linger through 2009. We will lower the ratings if the bank's leverage increases, or if it is not able to consolidate its liquidity profile and achieve adequate profitability. We could revise the outlook back to stable if we see an improvement in investment leverage metrics and a demonstration of the bank's capacity to maintain adequate profitability. There is very limited potential for an upgrade in the foreseeable future, as it would require a significant improvement in the bank's leverage, recurring income stream, and funding and liquidity profiles.

Gulf International Bank B.S.C.

PRIMARY CREDIT ANALYST: GOEKSENIN KARAGOEZ, PARIS (33) 1 4420 6724, GOEKSENIN_KARAGOEZ@STANDARDANDPOORS.COM

SECONDARY CREDIT ANALYST: EMMANUEL VOLLAND, PARIS (33) 1 4420 6696, EMMANUEL_VOLLAND@STANDARDANDPOORS.COM

ISSUER CREDIT RATING: BBB+/STABLE/A-2

PUBLICATION DATE: APRIL 14, 2009

Rationale

On April 14, 2009, Standard & Poor's Ratings Services affirmed its 'BBB+' long-term counterparty credit rating on Bahrain-based Gulf International Bank B.S.C. (GIB) and removed it from CreditWatch negative where it was initially placed on Feb. 10, 2009. At the same time, the 'A-2' short-term counterparty credit rating was affirmed. The outlook is stable.

The rating action reflects the recent sale (effective as at Dec. 31, 2008) of a significant portion of GIB's investment securities portfolio to its shareholders. The sale of $4.8 billion of securities, mainly asset-backed, had a positive impact on GIB's asset quality, liquidity, and capitalization. We also factored in the bank's intention to further reduce its leverage and strengthen its funding profile.

The ratings on GIB reflect the bank's strong ownership structure, adequate asset quality (although assets are geographically concentrated), and improved liquidity and capitalization. The ratings on the bank are constrained by its weak profitability, reliance on short-term wholesale funding, and challenges regarding the bank's future strategy. The bank intends to amend its business model and improve its funding profile but its ability to achieve this has yet to be demonstrated.

The long-term rating on GIB is two notches above the bank's stand-alone credit profile, to reflect our view that extraordinary support from shareholders is very likely. The Saudi Arabia Monetary Agency (SAMA, the central bank) and Public Investment Fund (PIF), two public institutions in Saudi Arabia (AA-/Stable/A-1+), together own a majority stake in GIB. The other shareholders are the remaining five Gulf Cooperation Council (GCC) member countries. The bank has not disclosed how much each shareholder contributed to the security sale. The bank will announce the impact of this transaction on its ownership structure in the coming weeks, but SAMA and PIF will remain the controlling bodies. We consider GIB as a commercial government-related entity (GRE), while we classify Saudi Arabia as interventionist toward its banking sector. While GIB's role appears to be of limited importance for its shareholders, we believe that the links are very strong through its ownership and board representation, funding and capital support, and reputation risk.

We remain cautious on the future operational financial performance of GIB, as it could face a decrease in business volumes (trade finance, syndicated loans, and project finance) that would weigh on its fees and commissions. We also expect an increase—from extremely low levels—in credit risk cost on the bank's corporate loan book. Still, our earning forecast indicates that the bank should return to a profit in 2009.

GIB is a merchant bank focusing on the Gulf market. Its target clients are governments, public and private sector corporations, financial institutions, and multinational companies active in the region. Services to these clients include project and trade finance, corporate advisory, asset and fund management, and treasury products. GIB is also an active player in the syndicated loan market and has been developing its Islamic banking business.

Outlook

The stable outlook reflects our belief that GIB will continue to benefit from strong support from shareholders and maintain its improved asset quality and capitalization. We could lower the ratings if the bank fails to adjust its business model to the new environment and maintain the adequate quality of its loan book and a satisfactory capitalization. An upgrade would require a significant improvement in the bank's funding profile, the implementation of a business model that could generate adequate, sustainable profitability, and the maintenance of satisfactory asset quality and capitalization.

Gulf Investment Corporation G.S.C.

PRIMARY CREDIT ANALYST: PAUL-HENRI PRUVOST, LONDON (44) 20 7176 7210, PAUL-HENRI_PRUVOST@STANDARDANDPOORS.COM

SECONDARY CREDIT ANALYST: EMMANUEL VOLLAND, PARIS (33) 1 4420 6696, EMMANUEL_VOLLAND@STANDARDANDPOORS.COM

ISSUER CREDIT RATING: BBB+/WATCH NEG/A-2

PUBLICATION DATE: FEBRUARY 9, 2009

Rationale

On Feb. 9, 2009, Standard & Poor's Ratings Services lowered its long-term counterparty credit rating on Kuwait-based Gulf Investment Corporation G.S.C. (GIC) to 'BBB+' from 'A-'. At the same time, Standard & Poor's placed its 'BBB+/A-2' long- and short-term counterparty credit ratings on GIC on CreditWatch with negative implications.

The rating action reflects the material negative impact on GIC's business and financial profile of the global and regional market conditions. The company's stand-alone credit profile is therefore weaker than previously assessed. The sharp downturn in global and regional markets throughout 2008—with a faster and greater-than-expected deterioration during the second half—is expected to lead to significant losses for GIC due to large write-downs and provisions against its various investment portfolios.

In addition, revaluation reserves on its available-for-sale portfolio will turn negative. We understand that the company is currently raising significant additional capital to support its financial profile. However, while the capital increase had been called by the board in October 2008, we note that part of it has not yet been paid in by some shareholders. This suggests that coordination among the consortium of shareholders is not optimal and raises some concerns regarding willingness and timeliness of support. Importantly, the capital increase in itself will not address the longer-term issue of the sustainability of GIC's business model. Therefore, the rating action also reflects our view that the company's business profile has weakened and that its current business model makes the institution's performance susceptible to cyclical pressures. While liquidity drought has been observed in recent months in the Gulf region, GIC has good access to large deposits from its shareholders and public sector entities from the Gulf Cooperation Council (GCC) region, and chiefly from the State of Kuwait (AA-/Stable/A-1+).

The long-term rating on GIC—a commercial government-related entity under our methodology—is currently one notch higher than its stand-alone credit profile, reflecting its ownership structure and our expectation that it is likely to receive extraordinary support. GIC is equally owned by the six member states of the GCC. While GIC appears to have a limited important role for its shareholders, we believe that the links are strong through the full ownership, board representation, funding support, and reputation risk. At the same time, we noticed that the current capital raising exercise has been protracted.

GIC is a wholesale investment company whose corporate mission is to provide financial services that support the development of private enterprise and economic growth in the Gulf region. This activity effectively represents less than 20% of total assets through its principal investing portfolio, comprising holdings in about 45 names, with minority shares in most of them. Through its global markets activities, GIC is also active in corporate treasury activities, investments for its own accounts, and fund management for third parties.

CreditWatch

GIC's capacity to rebuild its capital base, deleverage its balance sheet, and reshape its business model to allow for better and less volatile earnings generation will be critical for the ratings. We expect to resolve the CreditWatch status in the coming weeks following consideration of the above factors and further review conducted with the company. We do not expect the final ratings to be lowered by more than two notches.

International Banking Corp. (The)

PRIMARY CREDIT ANALYST: EMMANUEL VOLLAND, PARIS (33) 1 4420 6696, EMMANUEL_VOLLAND@STANDARDANDPOORS.COM

SECONDARY CREDIT ANALYST: MOHAMED DAMAK, PARIS (33) 1 4420 7322, MOHAMED_DAMAK@STANDARDANDPOORS.COM

ISSUER CREDIT RATING: SD/--/SD

PUBLICATION DATE: MAY 12, 2009

Rationale

On May 12, 2009, Standard & Poor's Ratings Services lowered its long- and short-term counterparty credit ratings on Bahrain-based The International Banking Corp. (TIBC) to 'SD/SD' (selective default, meaning payments may not be made on some financial obligations) from 'BBB-/A-3'. TIBC is fully owned by Ahmad Hamad Algosaibi & Brothers Company (the Algosaibi Group, not rated).

The rating action follows TIBC's decision not to fulfill its obligations toward some of its bank creditors. We understand from conversations with the CEO of TIBC and with employees of the Algosaibi Group that there is a high likelihood that the Algosaibi Group will implement a groupwide debt restructuring that will include TIBC. We believe that TIBC has defaulted on some of its bank debt since the beginning of May 2009, despite the fact that TIBC holds a large equity portfolio (mainly made up of shares listed in Saudi Arabia) valued at more than $400 million on Dec. 31, 2008. The Algosaibi Group considers these strategic decisions to be aggressive defensive protection measures. We see them as a conscious decision not to honor debt payments according to initial terms and conditions while still being able to do so.

TIBC is a small wholesale bank registered in Bahrain with total assets of $3.8 billion on Dec. 31, 2008. The Algosaibi Group, based in Saudi Arabia's Eastern Province, is active in financial services, bottling and distribution, can manufacturing, real estate investment, hotels, shipping, and contracting. Owing to TIBC's ownership by, and close cooperation with, the Algosaibi Group, we had concluded that backing from the Algosaibi Group in times of difficulty would be extremely strong and classified TIBC as a core entity of the Algosaibi Group. The Algosaibi Group formalized this commitment through a letter of comfort to TIBC and offered support through capital injections available on several occasions. Nevertheless, most recently, the Algosaibi Group has not provided exceptional support as we had expected.

Standard & Poor's will continue to follow the developments at TIBC and at the Algosaibi Group level and adjust its ratings on TIBC as appropriate.

Islamic Development Bank

PRIMARY CREDIT ANALYST: FAROUK SOUSSA, PHD., LONDON (44) 20-7176-7104, FAROUK_SOUSSA@STANDARDANDPOORS.COM

ISSUER CREDIT RATING: AAA/STABLE/A-1+

PUBLICATION DATE: DECEMBER 16, 2008

Rationale

The ratings on the Islamic Development Bank are supported by:

- Very strong capitalization. The Islamic Development Bank Ordinary Capital Resources (ISDB) had shareholders' equity of Special Drawing Rights (SDR) 5.3 billion at year-end 1428H (hijra year; the end of the latest Islamic calendar year, corresponding to Jan. 9, 2008), exceeding the financing provided to member countries and other recipients;
- Strong liquidity. ISDB's cash and placements with banks equaled more than 16% of total assets at year-end 1428H, and assets with maturities of less than 12 months exceeded liabilities by around 20% of total assets;
- A development-related asset portfolio that has performed well despite the large share of loans to borrowers (mainly public sector) in relatively high-risk countries, reflecting (in part) the preferred creditor treatment ISDB has generally received from its member countries; and
- Expected continued preferred creditor treatment and other support from shareholders. ISDB is a prominent institution in the rapidly growing Islamic finance industry, and it performs a number of Islamic-finance-related and other tasks that are highly valued by its member countries.

The Islamic Development Bank was established in 1973 as a specialized institution of the Organization of Islamic Conferences (OIC), an international organization of 56 predominantly Muslim countries (including Palestine) established in 1969. Twenty-nine countries participated in the initial capital subscription; by year-end 1428H, membership had expanded to 56 countries on four continents.

The Islamic Development Bank has evolved into the linchpin of the Islamic Development Bank Group, which includes other affiliates and funds that are involved in an unusually wide range of activities. Standard & Poor's Ratings Services' ratings apply only to Ordinary Capital Resources, which includes the subscribed capital of the bank and its retained earnings.

Similar to that of other multilateral development finance institutions (MDFIs), the bank's mandate calls for it to foster economic development and social progress. However, this is to be done not only in member countries, but also in Muslim communities in nonmember countries—and in a manner compliant with the principles of Islamic banking, which are based upon the Shari'ah.

ISDB's gross development-related assets (DRA)—those assets resulting from the bank's murabaha, trade, lease, installment sales, and similar financings; loans; and equity investments, including those in subsidiaries and funds—were 80% of total assets at year-end 1428H. While much of ISDB's DRA is in unrated countries or those with relatively low foreign currency sovereign credit ratings, the sovereign risk embedded in ISDB's DRA portfolio historically has been mitigated by the preferred creditor treatment the bank has generally received from its member countries. To mitigate private sector risk, ISDB typically obtains bank guarantees or other collateral. Overdue payments at year-end 1428H were SDR56 million, around 1.4% of development-related exposure (DRE; DRA plus guarantees), and were more than covered by provisions for losses on operational assets of almost SDR115 million.

By year-end 1428H, two securitizations of a portion of ISDB's operating assets had been completed, the first in 2003 for US$400 million and the second (under a US$1 billion program) in 2005 for US$500 million. All payments under

these securitizations are, in effect, guaranteed by ISDB; because of this, the assets remain on ISDB's balance sheet, with the corresponding liabilities-side entry being sukuk liabilities, which were SDR573 million at year-end 1428H. A third securitization, a Ringitt sukuk issued in Malaysia, has been completed since the end of 1428H.

In addition to the historically strong performance of ISDB's DRE, the bank has consistently maintained an unusually high risk-bearing capacity relative to its DRE: its ratio of provisions for losses plus shareholders' equity (narrow risk-bearing capacity [NRBC]) to DRE was more than 100% at year-end 1428H. This is the highest such ratio among rated MDFIs as of their latest fiscal year ends, and it means that all of ISDB's DRE could be written off against NRBC without the institution becoming insolvent.

ISDB's net income jumped by 32% during 1428H to SDR164 million from SDR123 million one year earlier, mainly due to increased income from operational assets. Income increased on an underlying basis, primarily as a result of a higher mark up; ISDB's return on average assets plus guarantees rose to 2.5% in 1428H from 2.1% one year earlier, and its return on average shareholders' equity rose to 3.2% from 2.6%.

ISDB is unique among rated MDFIs in having no borrowings on its balance sheet and thus no debt-service payments, and at year-end 1428H its assets maturing within one year exceeded its liabilities by around 20% of total assets.

Outlook

The outlook for ISDB's rating is stable. The bank's capital position is extremely strong and its liquidity ample. The 2006 decision of its board of governors to substantially increase its paid-in capital is a sign of current shareholder support unique among 'AAA' MDFIs.



Kuwait Finance House

PRIMARY CREDIT ANALYST: NICOLAS HARDY, PARIS (33) 1 4420 7318, NICOLAS_HARDY@STANDARDANDPOORS.COM

SECONDARY CREDIT ANALYST: PAUL-HENRI PRUVOST, LONDON (44) 20 7176 7210, PAUL-HENRI_PRUVOST@STANDARDANDPOORS.COM

ISSUER CREDIT RATING: A-/WATCH NEG/A-2

PUBLICATION DATE: MARCH 31, 2009

Rationale

The ratings on Kuwait Finance House (KFH) reflect its significant government ownership and strong expected support from the government of the State of Kuwait (AA-/Stable/A-1+) in case of need, as well as the bank's strong customer franchise in the country, leading commercial position in Islamic banking, adequate capital buffer, good liquidity position, and broader diversification than for domestic competitors.

The long-term rating includes a one-notch uplift from the bank's stand-alone credit profile to reflect Standard & Poor's Ratings Services' expectation that extraordinary support from the government, KFH's largest single shareholder, would be likely in case of need.

The bank's credit weaknesses include significantly weakened asset quality indicators. This is mainly due to the bank's exposure to local investment companies and a more challenging operating environment. In addition, the bank carries a large exposure to the real estate sector, a high appetite for overseas growth despite a much less favorable global environment, an enterprise risk management framework that is no longer commensurate with the group's risk appetite and geographically enlarged operating base.

With total assets of $38.6 billion at year-end 2008, KFH is the No. 2 bank in Kuwait and one of the largest Islamic banks in the world. An extensive branch network and high customer loyalty have enabled the bank to capture the largest retail customer franchise of any bank in the country. The bank's leading commercial position, particularly in retail banking, generates high returns. Competition in the Islamic financial industry is mounting, however, and the bank's management has continued to express his willingness to seize the first-mover advantage in countries where Islamic banking is growing. The bank already controls relatively large subsidiaries in Bahrain, Turkey, and Malaysia. Its operations in Malaysia started in 2005 and we consider this the first step in a wider strategy to expand business in Asian Muslim countries. This still aggressive overseas expansion strategy, through either an expanding physical network or direct investment, is likely to bring its own share of risk amid the deteriorating operating environment. KFH controls and manages a wide range of specialized entities in various sectors, which contribute to earnings diversification. In our opinion, the risk management architecture is not sufficiently aligned with the recent growth and geographic spread of risk assets and the bank's sizable risk appetite. The bank's exposure to the Kuwaiti investment companies sector, in addition to the deteriorating business environment, has been weighing heavily on asset quality indicators. Nonperforming loans (NPLs) to lending facilities soared to 10.3% at year-end 2008 from 3.1% the previous year. A jump in provisions lead to a decline in profitability, with return on assets (ROA) and return on equity (ROE) declining to 1.8% and 11.8% in 2008 from 4.3% and 31.5% in 2007. The bank's exposure to real estate markets, in Kuwait and abroad, is a significant source of risk. On a positive note, KFH's liquidity position and capitalization ratios remain strong.

CreditWatch

To resolve the CreditWatch placement, we will analyze the bank's detailed exposure to the investment companies (on a gross and net basis) and assess the expected impact on its stand-alone credit profile. We also need to analyze and assess the impact of the government's support package and measure the extent to which it mitigates risks.

Additional important factors are the extent of the local economy's slowdown and its impact on the bank's asset quality and financial performance. We expect to reassess the CreditWatch status shortly, following consideration of the above factors. In our opinion, we do not anticipate the ratings on the bank to be downgraded by more than one or two notches, assuming that significant government support will materialize.

Mashreqbank

PRIMARY CREDIT ANALYST: MOHAMED DAMAK, PARIS (33) 1 4420 7322, MOHAMED_DAMAK@STANDARDANDPOORS.COM

SECONDARY CREDIT ANALYST: EMMANUEL VOLLAND, PARIS (33) 1 4420 6696, EMMANUEL_VOLLAND@STANDARDANDPOORS.COM

ISSUER CREDIT RATING: A/WATCH NEG/A-1

PUBLICATION DATE: APRIL 6, 2009

Rationale

On March 17, 2009, Standard & Poor's Ratings Services placed its long- and short-term counterparty credit ratings on Mashreqbank (Mashreq), based in the United Arab Emirates (UAE, not rated), on CreditWatch with negative implications. This action reflects our growing concerns regarding the impact on the banking sector of the economic downturn in the Emirate of Dubai (not rated).

The ratings on Mashreq reflect the bank's good commercial position, above average financial profile, and just adequate liquidity. Negative rating factors are the weakening operating environment and high competitive pressures in Mashreq's core market, as well as the bank's low geographic diversification. Standard & Poor's considers Mashreq a systemically important bank in the UAE. We also consider the UAE as interventionist with regard to its banking sector. Thus, we consider Mashreq as a Government Related Entity (GRE) under our methodology and the long-term rating is one notch above its stand-alone credit profile, reflecting our expectation of high likelihood of government support in case of need.

With total assets of UAE dirham (AED) 93.2 billion on Dec. 31, 2008, Mashreq is one of the largest banks in the UAE. It is 87.7% owned by the Al-Ghurair family and is the only bank among its domestic peers not owned by the government or ruling families. Mashreq is also one of the few regional banks with no sizable concentration in its loan book.

Mashreq's financial profile is above average in our opinion. The bank displays adequate profitability and strong asset quality indicators. Nevertheless, its operating environment is weakening rapidly. Therefore, we expect deterioration in these indicators. On a positive note, Mashreq has been setting aside general provisions over the past five years creating a strong cushion that helps alleviate the pressure on its asset quality and profitability.

Mashreq's liquidity is just adequate, with 16.4% of assets placed in liquid forms at year-end 2008. The bank's liquidity position has deteriorated materially compared with that in 2007, as strong loan growth has not been matched by similar growth in deposits. The bulk of the bank's securities portfolio is of high quality, however, and can be used for repo transactions—something Mashreq has already done in the past. In addition, we understand that Mashreq is focusing on restoring its liquidity position by attracting new deposits and drastically reducing loan growth. Mashreq's capitalization is solid despite the rapid growth of risk assets. The adjusted total equity (ATE) to total assets ratio reached 10.8% as of year-end 2008, backed by a very conservative dividend policy that we expect to continue in the future.

CreditWatch

To resolve the CreditWatch placement, Standard & Poor's will assess the expected impact of the deteriorating economic conditions and real estate sector on the financial profile of Mashreq. We will also update our assessment of the government of Dubai's willingness and capacity to provide extraordinary support to the bank in case of need, in light of the changing environment and its related impact on the bank's creditworthiness. After consideration of these elements, we expect to resolve the CreditWatch status in the coming six weeks. We do not anticipate lowering the ratings on Mashreq by more than one notch, based on our current expectations.

National Bank of Abu Dhabi

PRIMARY CREDIT ANALYST: EMMANUEL VOLLAND, PARIS (33) 1 4420 6696, EMMANUEL_VOLLAND@STANDARDANDPOORS.COM

SECONDARY CREDIT ANALYST: PAUL-HENRI PRUVOST, LONDON (44) 20 7176 7210, PAUL-HENRI_PRUVOST@STANDARDANDPOORS.COM

ISSUER CREDIT RATING: A+/STABLE/A-1

PUBLICATION DATE: APRIL 15, 2009

Rationale

The ratings on National Bank of Abu Dhabi (NBAD) reflect its ownership by and special relationship with the government of the oil-rich Emirate of Abu Dhabi (AA/Stable/A-1+), strong domestic commercial position, robust profitability, and good asset quality. The ratings are constrained by the bank's narrow domestic market with increasing competition, large concentrations, and rapid loan growth in a weakening operating environment.

NBAD is the second largest bank in the United Arab Emirates (not rated) with total assets of UAE dirham (AED) 164.7 billion ($44.8 billion) on Dec. 31, 2008, and an overall market share of about 12%. The bank has a leading position in corporate banking and is rapidly growing its retail banking business. Although small in absolute terms, its customer franchise is among the strongest in the UAE. The government of Abu Dhabi has a 70.5% stake in NBAD through the Abu Dhabi Investment Council (ADIC; not rated). Standard & Poor's Ratings Services considers that the bank's ownership structure, importance to Abu Dhabi's economy, and flagship bank status mean that government support in times of difficulty would be very strong. Consequently, the rating on the bank (classified as a government-related entity under our methodology) is higher than its stand-alone credit profile.

Loans to the government and public sector entities account for about 35% of the bank's lending, and are considered relatively low risk. When these loans are excluded, the bank's loan leverage stands at less than 45%. On the liability side, government and public sector entities account for more than 60% of customer deposits.

NBAD has a satisfactory funding and liquidity profile, although it deteriorated during the previous years, as loan growth outpaced deposit growth. The ratio of customer loans to customer deposits exceeded 100% for the first time in 2008. In addition, large swings in its deposit base can occur from time to time due to the large concentration in its deposit base. Like other regional banks, NBAD has a significant maturity mismatch, with most of its funding being short term. Even if deposit rollover and retention have been historically very high, the bank is addressing this issue through alternative funding strategies.

Profitability is high and has benefited from the robust economic environment of the past five years. The bank's performance was very strong in 2008, with return on equity (ROE) of almost 25%. The bank's asset quality is also among the strongest in the Gulf region, with a ratio of nonperforming loans (NPLs) to total loans of 1.0% on Dec. 31, 2008, with a solid coverage ratio by provisions of 144.6%. The bank benefits from significant lending to the low-risk domestic public sector, and relies on strong credit procedures. The superior credit profile of the domestic public sector mitigates to a large extent the bank's concentration risk. NBAD's rapid expansion and the recent weakening of the operating environment are expected to weigh on its asset quality, although it should remain manageable. While asset quality would also suffer from the fall of the domestic real estate market, the bank's conservative valuation and collateral policies are strong mitigating factors.

Capital ratios are adequate. Adjusted total equity (ATE) as a percentage of adjusted assets stood at 8.4% on Dec. 31, 2008. NBAD's payout has fallen in recent years, allowing large earnings retention. Standard & Poor's expects the bank's capital position to remain adequate in the medium term. Regulatory capital ratios should benefit from recently announced government support measures.

Outlook

The stable outlook reflects our expectation that NBAD will maintain its leading commercial position and sound financial profile. The bank's leading domestic position appears well secured, enabling it to mitigate risks linked to the restricted playing field of the non-oil private sector and maintain satisfactory operating profitability. A change of ownership structure leading to a weakening of the links between NBAD and the Abu Dhabi government would negatively affect the ratings, as would a material deterioration in asset quality or capitalization.

National Bank of Dubai

PRIMARY CREDIT ANALYST: PAUL-HENRI PRUVOST, LONDON (44) 20 7176 7210, PAUL-HENRI_PRUVOST@STANDARDANDPOORS.COM

SECONDARY CREDIT ANALYST: MOHAMED DAMAK, PARIS (33) 1 4420 7322, MOHAMED_DAMAK@STANDARDANDPOORS.COM

ISSUER CREDIT RATING: A/WATCH NEG/A-1

PUBLICATION DATE: APRIL 22, 2009

Rationale

The ratings on National Bank of Dubai (NBD) largely reflect its adequate risk profile and financial performance. Negative rating factors include the bank's limited customer franchise, significant concentration risks, increasing competition, and exposure to the weakening operating environment in the Emirate of Dubai (not rated). The long-term rating on NBD is two notches above the bank's stand-alone credit profile to reflect Standard & Poor's Ratings Services' expectation of strong likelihood of support from the authorities, in case of need. NBD is classified as a government related entity under our methodology. EBI is wholly-owned by Emirates NBD PJSC (ENBD; not rated), which acts as the holding company for both Emirates Bank International PJSC (EBI, A/Watch Neg/A-1) and NBD. ENBD is in turn 56% owned by the government of Dubai.

Standard & Poor's placed its long-term counterparty credit rating on NBD on CreditWatch with negative implications on March 17, 2009, due to our growing concerns on the economic environment in Dubai and its impact on NBD.

With total assets of $27.6 billion on Dec. 31, 2008, NBD controls a market share of about 6% of the United Arab Emirates banking system's total deposits. Operating mainly in Dubai, the bank holds a market position weaker than leading banks, as it entered the mass-market segment at a later stage. NBD's commercial position is expected to benefit from the effective completion of the planned merger with EBI—scheduled for the second quarter of 2009.

Given the weakening operating environment in Dubai, we consider the combination of fast loan growth until mid-year 2008 and sustained high concentration by sectors and names as heightening credit risk. NBD is exposed to the local real estate sector, with related assets exceeding 1x adjusted total equity on Dec. 31, 2008. This exposure is viewed as an important source of risk in light of the ongoing correction in the sector, although NBD is exposed to a lower extent than domestic rated peers.

Given a less supportive environment, we deem NBD's asset quality to be under pressure. This will ultimately put pressure on the bank's profitability as provisioning on both the loan book and investment portfolio is expected to increase in a context of slowing business growth and equity markets correction. NBD's funding and liquidity have also deteriorated, with a loan-to-deposit ratio now standing above similarly rated peers in the region. Pressure coming from fierce competition to attract customer deposits is partially offset by the injection of government funds into the domestic banking system.

NBD's capitalization is only adequate given its risk profile. In addition, NBD's revaluation reserves registered a steep decline to enter significant negative territory in 2008 as a result of the prolonged deterioration in credit spreads and stock markets throughout the year. On a positive note, we understand that ENBD is planning to increase its capital through a Tier 1 injection in the near future. ENBD's regulatory capital ratio should also benefit from the expected conversion into Tier 2 capital of the combined UAE dirham 12.6 billion of deposits received by NBD and EBI from the Federal authorities.

CreditWatch

To resolve the CreditWatch placement, Standard & Poor's will assess the expected impact of the deteriorating economic and real estate sector conditions on the financial profile of NBD. We will also update our assessment of the government of Dubai's willingness and capacity to provide extraordinary support to the bank in case of need, in light of the changing environment and its related impact on the bank's credit profile. After consideration of these elements, we expect to resolve the CreditWatch status in the coming six weeks. We do not anticipate to lower the ratings on the bank by more than one notch, based on our current expectations.

National Bank of Kuwait S.A.K.

PRIMARY CREDIT ANALYST: PAUL-HENRI PRUVOST, LONDON (44) 20 7176 7210, PAUL-HENRI_PRUVOST@STANDARDANDPOORS.COM

SECONDARY CREDIT ANALYSTS:
EMMANUEL VOLLAND, PARIS (33) 1 4420 6696, EMMANUEL_VOLLAND@STANDARDANDPOORS.COM
NICOLAS HARDY, PARIS (33) 1 4420 7318, NICOLAS_HARDY@STANDARDANDPOORS.COM

ISSUER CREDIT RATING: A+/NEGATIVE/A-1

PUBLICATION DATE: FEBRUARY 17, 2009

Rationale

On Feb. 16, 2009, Standard & Poor's Ratings Services revised its outlook on National Bank of Kuwait S.A.K. (NBK) to negative from stable. At the same time, the 'A+/A-1' long- and short-term counterparty credit ratings on the bank were affirmed.

The outlook revision reflects the weakening environment in which NBK operates, which is expected to put pressure on the bank's asset quality, financial performance, and ultimately on its stand-alone credit profile.

Although NBK has less exposure to problematic Kuwaiti investment companies than its domestic peers (see article "Various Kuwaiti Banks Placed On CreditWatch Negative On Large Exposure To Investment Companies," published Feb. 16, 2009 on RatingsDirect), we believe that this could increase pressure on its asset quality and profitability. In addition, oil prices and the domestic stock market have declined dramatically, and the global slowdown has had a negative impact on domestic economic growth (1.4% expected in 2009) and credit markets. The long-term rating on NBK, which we consider a government-related entity (GRE), is one notch higher than its stand-alone credit profile to reflect our expectation of extraordinary support from the government (classified as interventionist toward its banking sector) in case of need.

NBK is the largest bank in the State of Kuwait (AA-/Stable/A-1+), with total consolidated assets of $41.3 billion at year-end 2008. The bank has a consistent track record of leading domestic market share. It recently undertook a rapid overseas expansion to offset the major challenge of operating in an essentially mono-industrial country that is highly sensitive to oil-price fluctuations. We believe that the bank's rapid expansion strategy—notably in Turkey and Egypt—carries potential risks, especially at a time of global economic downturn.

NBK's funding profile has weakened over the past two years. The share of core deposits in its funding has steadily reduced, while loan growth has been significant. The loans-to-core (nonbank) customer deposits ratio reached 130% at year-end 2008 (albeit still within the 85% regulatory limit set by the Central Bank of Kuwait). As with other Kuwaiti banks, NBK benefits from the injection of deposits by GREs, and is expecting its international network to gradually raise more core customer deposits. We will therefore monitor the bank's ability to strengthen its deposit base.

NBK's exposure to local investment companies appears manageable and, in our opinion, does not pose a threat to the bank's stand-alone credit profile. Its gross exposure is relatively limited, at about 12% of adjusted total equity (ATE). Nevertheless, the impact of the economic slowdown on the local corporate segment and some sectors such as real estate and construction (20% of NBK's lending at year-end 2008) is expected to lead to a deterioration in asset quality and profitability.

The bank's ratio of nonperforming loans (NPLs) remained sound at 2.0% of gross loans at Dec. 31, 2008. NBK allocated significant provisions during the fourth quarter of 2008, anticipating some asset quality deterioration, thereby strengthening its NPL coverage by loan loss reserves to a conservative 1.8x. We take comfort from NBK's adequate underwriting policy and the low-risk profile of its personal loans that account for almost one third of its total loan portfolio. The bank's financial performance demonstrates a long and consistent track record of strength. Nevertheless, we consider that a repeat of this robust financial performance is unlikely, at least in the near term, as further provisioning may be required and lending remains subdued.

NBK's capitalization remains high—with ATE at 12.5% of adjusted assets at year-end 2008—and underpins its current financial profile. Capital ratios compare favorably with those of large international and regional banks and are expected to remain a key strength.

Outlook

The negative outlook reflects our expectation that the bank's stand-alone credit profile will be pressured by the weakening operating environment. The ratings on the bank could be lowered if asset quality and profitability were to deteriorate materially over the coming quarters, or in the event that its funding profile weakens. Further overseas expansion that could increase the bank's risk profile or weaken its capitalization would also be considered a negative rating factor. We would revise the outlook back to stable if the bank were to demonstrate sufficient profitability and asset quality resilience through the economic downturn and if it is able to improve its funding profile.

National Commercial Bank (The)

PRIMARY CREDIT ANALYST: NICOLAS HARDY, PARIS (33) 1 4420 7318, NICOLAS_HARDY@STANDARDANDPOORS.COM

SECONDARY CREDIT ANALYST: FRANCOIS MONEGER, PARIS (33) 1 4420 6688, FRANCOIS_MONEGER@STANDARDANDPOORS.COM

ISSUER CREDIT RATING: A+/STABLE/A-1

PUBLICATION DATE: APRIL 27, 2009

Rationale

The ratings on Saudi Arabia-based The National Commercial Bank (NCB) reflect the bank's majority ownership by the Saudi government, leading commercial position, and strong financial profile stemming from its solid capitalization and ample liquidity. Partially offsetting these positive factors are the bank's recent rapid loan growth—mainly in the corporate sector—declining but still significant exposure to market risk, and very limited geographic diversification. The long-term rating on NCB is two notches higher than the bank's stand-alone credit profile, reflecting Standard & Poor's Ratings Services' expectation of the strong likelihood of government support if needed, given NCB's ownership structure and importance to the Saudi Arabian banking system. We therefore classify the bank as a government-related entity (GRE). We consider the Kingdom of Saudi Arabia (AA-/Stable/A-1+) as "interventionist" toward its banking system.

With total assets of Saudi Arabian riyal (SAR) 221.8 billion on Dec. 31, 2008, NCB enjoys a leading position in the Saudi banking system, ranking No. 1 in total assets and with a controlling market share of about one-fifth in assets and customer deposits. Over the past couple of years, the bank's loan portfolio has been growing rapidly and remains untested under adverse economic conditions. Loans to customers only accounted for about 50% of assets at year-end 2008, significantly below the local peer average. With the slowdown of the local economy, NCB faces the challenge of redefining its strategy to invest safely its abundant liquidity. The bank has recently expanded operations in the Republic of Turkey (BB-/Negative/B), acquiring a 64.7% stake in Türkiye Finans Katilim Bankasi (TFKB, not rated) for SAR4.4 billion. Standard & Poor's expects the bank's foreign operations to contribute only marginally to its revenues in the coming years.

In 2008, NCB took sizable provisions on its available for sale investment portfolio and posted an impairment loss on goodwill mainly related to its Turkish subsidiary, which together badly dented its bottom-line profitability. The ratio of core earnings to average adjusted assets declined to 1.6% from 3.3% in 2007. Nevertheless, NCB's good efficiency, low cost of credit risk, and high proportion of free funds continue to support its profitability. The bank's entrenchment in low-risk and lucrative retail banking in Saudi Arabia is a key driver behind strong operating revenues. The bank also enjoys longstanding relationships with most top-tier Saudi corporations, including government-related entities, and is willing to focus on government-sponsored projects. NCB's exposure to market risk has declined significantly but remains above the regional average. At year-end 2008, the bank had an exposure to structured credits and hedge funds of SAR8.4 billion, or 36.2% of adjusted total equity. It aims to reduce this portfolio and concentrate on lower-risk securities, such as government paper. The bank may have to take additional provisions against its securities portfolio, in addition to a likely deterioration of asset quality systemwide, weakening its short-term financial performance. However, we do not expect this to significantly erode the bank's solvency, because NCB is strongly capitalized. In addition, having the government as a majority shareholder is positive for the bank's financial flexibility.

Outlook

The stable outlook reflects our expectation that NCB will maintain its strong domestic franchise and solid operating revenues. The ratings could come under downward pressure if market risk proves to be higher than we assume, or if capital ratios or asset quality indicators deteriorate significantly. We could raise the ratings if the bank is able to sustain a track record of strong and stable financial performance, while keeping capitalization and credit risk under control.

Qatar National Bank

PRIMARY CREDIT ANALYST: MOHAMED DAMAK, PARIS (33) 1 4420 7322, MOHAMED_DAMAK@STANDARDANDPOORS.COM

SECONDARY CREDIT ANALYST: EKATERINA TROFIMOVA, PARIS (33) 1 4420 6786, EKATERINA_TROFIMOVA@STANDARDANDPOORS.COM

ISSUER CREDIT RATING: A+/STABLE/A-1

PUBLICATION DATE: MARCH 4, 2009

Rationale

The ratings on Qatar National Bank (QNB) reflect the bank's leading position in its domestic market, ownership structure dominated by the State of Qatar (AA-/Stable/A-1+), and good financial profile. These positive factors are somewhat offset by QNB's less supportive operating environment, geographic expansion in some countries that are riskier than the bank's core market of Qatar, and reliance on short-term deposits for funding. Standard & Poor's Ratings Services classifies QNB as a highly systemically important bank in the State of Qatar, which we consider interventionist toward its banking system. Therefore, and given the ownership structure of QNB, the long-term counterparty credit rating on the bank is two notches above its stand-alone credit profile, reflecting our expectation of strong likelihood of extraordinary government support in case of need.

QNB controls about 40% of the Qatari banking system's assets. The bank is strongly entrenched domestically in both the retail and corporate segments. QNB boasts a good financial profile displaying a strong financial performance; good asset quality and liquidity profile; and strong financial flexibility. Nevertheless, the bank's operating environment is becoming less supportive than in the past. As a result, Standard & Poor's expects some manageable consequences for QNB's asset quality indicators, provisioning needs, and financial performance.

The bank's asset and liability composition still reflects the narrowness of the Qatari economy, with a large portion consisting of exposure to the government and its related entities. QNB has started to diversify geographically, focusing on other Middle Eastern and North African countries which are riskier than Qatar. On a positive note, the bank enjoys strong financial flexibility. Capitalization remains just adequate for QNB's risk profile but dividend policy is set to remain somewhat conservative.

Outlook

The stable outlook reflects our expectation that QNB will retain its dominant commercial position and solid financial profile, with no major change in the shareholding structure. We see limited potential for an upgrade in the foreseeable future given the less supportive operating environment. However, the ratings could come under pressure if links with the government weaken; financial performance, capital ratios, or asset quality deteriorate more than we anticipate; or geographic expansion risks materialize.

Riyad Bank

PRIMARY CREDIT ANALYST: PAUL-HENRI PRUVOST, LONDON (44) 20 7176 7210, PAUL-HENRI_PRUVOST@STANDARDANDPOORS.COM

SECONDARY CREDIT ANALYST: EMMANUEL VOLLAND, PARIS (33) 1 4420 6696, EMMANUEL_VOLLAND@STANDARDANDPOORS.COM

ISSUER CREDIT RATING: A+/STABLE/A-1

PUBLICATION DATE: JULY 31, 2008

Rationale

The ratings on Saudi Arabia-based Riyad Bank (Riyad) reflect its superior capitalization, strong domestic market position, good funding and liquidity profile, and strong asset quality. The long-term counterparty credit rating on Riyad (considered as a government related entity (GRE) under our methodology, as a systemically important bank) is one notch higher than its stand-alone creditworthiness, to reflect our expectation of the strong likelihood of extraordinary support from the government (classified as interventionist toward its banking sector) if needed. The ratings are constrained by fast growth in the loan portfolio, largely untested by an economic downturn; concentration risk, as most of its operations take place in an economy largely reliant on oil prices and government spending; and earnings mix still skewed toward interest income, amid heightened competition.

Riyad's adjusted total equity (ATE)-to-assets ratio was boosted by a $3.5 billion capital increase in June 2008, to 17.8% at June 30, 2008. This should enable Riyad to rapidly expand its corporate loan book, especially through an increased participation in the syndicated loan and project finance markets. The capital position should remain strong over the medium term, despite expected fast growth in risk assets. Standard & Poor' Ratings Services also factors in our expectation that the bank's overall conservative risk appetite will remain unchanged and the risk management framework will continue to improve.

Riyad is the fourth-largest bank in the Kingdom of Saudi Arabia (AA-/Stable/A-1+), with total assets of Saudi Arabian riyal (SAR) 144.1 billion ($38.5 billion) at June 30, 2008. The bank has a solid customer franchise and market position in the corporate and retail segments, with a distinctive position in asset management. It is fully owned by Saudi shareholders, with government and semi-government public institutions owning slightly more than 50% of the shares.

Riyad's financial performance has been relatively more resilient to the 2006 stock market collapse than its domestic peers. At the same time, profitability tends to be in a lower bracket, with lower margins and efficiency. We, nevertheless, expect Riyad's financial performance to remain strong, with a gradual increase in noninterest income compensating the cost increase incurred by the growth plan.

The bank's asset quality is strong with a ratio of nonperforming loans (NPLs) to total loans of 0.8% at mid-year 2008 (excluding repossessed properties as settlement for bad loans), with NPLs more than fully covered by provisions. Liquidity and funding are also strong and benefited from the capital increase.

Outlook

The stable outlook reflects our expectation that Riyad will retain its leading commercial position and maintain its conservative risk profile and domestically-focused strategy. Assuming the bank maintains its current financial profile, the ratings could be raised under the combination of a better diversified business profile and structural improvements in the Saudi macro-economic environment. The former would include significant economic diversification and liberalization and the establishment of a stronger credit culture among domestic corporate borrowers. We see limited room for further upgrades in the short to medium term, however. If earnings generation, capitalization, or asset quality were to deteriorate sharply, the ratings would come under downward pressure. A significant shift in risk appetite would also be a negative rating factor.

Samba Financial Group

PRIMARY CREDIT ANALYST: NICOLAS HARDY, PARIS (33) 1 4420 7318, NICOLAS_HARDY@STANDARDANDPOORS.COM

SECONDARY CREDIT ANALYST: PAUL-HENRI PRUVOST, LONDON (44) 20 7176 7210, PAUL-HENRI_PRUVOST@STANDARDANDPOORS.COM

ISSUER CREDIT RATING: A/STABLE/A-1

PUBLICATION DATE: DECEMBER 22, 2008

Rationale

The ratings on Samba Financial Group are supported by the bank's strong commercial position in the Kingdom of Saudi Arabia (AA-/Stable/A-1+), robust profitability, and good funding and liquidity. The long-term rating includes uplift of one notch above the bank's stand-alone creditworthiness. This reflects Standard & Poor's Ratings Services' view that the government, which we consider as "interventionist" toward its banking sector, would likely provide extraordinary assistance to systemically important banks, including Samba, in case of need. The ratings are constrained by concentration risks, the more difficult operating environment due to lower oil prices, and mounting competition.

Samba is one of Saudi Arabia's leading banks, with total assets of Saudi Arabian riyal (SAR) 187.1 billion ($49.9 billion) on Sept. 30, 2008. It is almost wholly owned by Saudi shareholders, with public institutions owning 44.5% at the same date. The bank has a solid franchise and strong brand recognition, despite its limited branch network of 65 outlets throughout the kingdom.

One of the most profitable banks in the Gulf, Samba had net profit of SAR3.6 billion for the first nine months of 2008 (annualized 2.8% return on assets or ROA), supported by robust economic conditions during the first half of the year. The bank reports a high interest margin because about 35% of customer deposits are noninterest bearing, as well as the bank's significant contribution from noninterest revenues, strong efficiency, and low cost of risk in its lending book. We expect Samba's profitability to remain solid, although core revenues have started to adjust to the more challenging operating environment.

Asset quality has improved rapidly over the past five years to reach robust levels by regional standards. Nonperforming loans (NPLs) represented 1.7% of total gross loans on Sept. 30, 2008. Loans are concentrated by name and geography, however. Samba used to be a pure domestic player but appetite for geographic expansion in emerging markets has been high during the past two years and is set to remain so. Samba entered Pakistan in March 2007 with a limited $100 million investment in Crescent Commercial Bank (CCB; not rated) recently rebranded and renamed as Samba Bank Ltd., and then turned to Egypt (foreign currency: BB+/Stable/B) to contemplate a more significant investment when it considered bidding for state-owned Banque du Caire (not rated).

The bank's liquidity profile remains strong, as loan leverage—51.5% on Sept. 30, 2008—even decreased despite strong asset growth since 2006. About 75% of the investment portfolio is invested in domestic and foreign government paper, most of which is easily able to be repoed. Deposits fully fund lending, but funding overall still heavily relies on short-term but stable deposits. Deposit concentration by customer is high, a feature shared by all Saudi banks. Samba's funding profile slightly improved after it raised long-term debt through a series of medium-term instruments, but is unlikely to improve any further in the short term.

Like most of its local peers, capitalization ratios have tightened along with the increase in risk assets, but Samba's ratios remain solid. Adjusted total equity (ATE) stood at 10.2% of total assets on Sept. 30, 2008. We expect capital ratios to stabilize because the bank's operating environment is appearing much less supportive.

Outlook

The stable outlook reflects our expectation that Samba will retain its leading commercial position and balanced risk profile, with no major change in the shareholding structure. We also expect the bank's financial profile to show resilience to the changing business environment. We see little room for an upgrade in the short term given current market conditions, but we reckon that Samba is well equipped to weather increasingly challenging operating conditions. If capital ratios fall, asset quality deteriorates drastically, or international expansion becomes excessively aggressive, the ratings would come under downward pressure.

Saudi British Bank (The)

PRIMARY CREDIT ANALYST: NICOLAS HARDY, PARIS (33) 1 4420 7318, NICOLAS_HARDY@STANDARDANDPOORS.COM

SECONDARY CREDIT ANALYST: FRANCOIS MONEGER, PARIS (33) 1 4420 6688, FRANCOIS_MONEGER@STANDARDANDPOORS.COM

ISSUER CREDIT RATING: A/STABLE/A-1

PUBLICATION DATE: APRIL 30, 2009

Rationale

The ratings on Saudi Arabia-based The Saudi British Bank (SABB) reflect its strong and resilient financial performance, 40% ownership by HSBC Holdings B.V., strong asset quality, and adequate capitalization. The long-term rating on SABB benefits from a one-notch uplift from its stand-alone credit profile to reflect Standard & Poor's Ratings Services' expectation of strong likelihood of support from HSBC Holdings B.V.'s parent, the HSBC group (HSBC; ultimate holding company HSBC Holdings PLC, AA-/Negative/A-1+) in case of need, given SABB's strategic importance to HSBC. Offsetting these positive factors are the bank's higher-than-average growth appetite and concentration risks in a deteriorating and relatively undiversified operating environment, as well as its dependence on foreign management expertise.

SABB is the fifth-largest bank in total assets in the Kingdom of Saudi Arabia (AA-/Stable/A-1+) and benefits from an extensive technical-assistance agreement with HSBC. A flexible and innovative player—but also an aggressive competitor—SABB delivers customers high quality products and services. Traditionally focused on corporate banking, in which it is a leading player, SABB is less entrenched in the local lucrative retail segment than its larger domestic peers. SABB's overall commercial position is therefore only average, with a market share of about 10% in loans and deposits.

Building on its know-how and HSBC's technical support, SABB has been growing very rapidly in recent years, with an assets growth rate outpacing most of its peers'.

Credit risk stemming from structural concentrations in the loan book dominates SABB's risk profile, a feature shared with peers active in the corporate segment. Asset quality is strong but likely to deteriorate, as corporate and retail customers now face a much more challenging economic environment. We expect this deterioration to be manageable, however. The bank's funding profile is adequate, despite concentrations and maturity mismatches.

The bank posted a good financial performance in 2008, thanks to the increased volume of corporate lending, good cost control, and limited cost of risk. Going forward, the bank is likely to benefit from the repricing of assets, although sound lending opportunities, like government sponsored projects, may become scarcer, depending on government spending. As clients deleverage, Saudi government debt matures, and the bank's approach toward lending becomes more restrictive, the bank will have no choice but to invest part of its liquidity in lower-yielding assets. The bank's ambition to focus on fee generating products like trade finance and retail banking services may prove difficult to implement. Core earnings quality stands to improve as the volume of activities at the recently-launched subsidiaries and associates increases, but we do not expect this diversification to provide material benefits in the short term.

SABB's capital ratios are adequate by international and regional standards, but remain lower than peers' because of the rapid growth of risk assets in recent years and a tighter capital management policy influenced by the parent's benchmarks.

Outlook

The stable outlook reflects our expectation that SABB will maintain its solid earnings stream and favorable market position, as well as continuing to benefit from HSBC's technical support. To a certain extent, the Saudi economy's structural weaknesses constrain the ratings on SABB. We could lower the ratings if the bank's relatively high growth appetite leads to excessive risk concentration in corporate lending, if credit risk materializes as a consequence of a persistent deterioration of the volatile and oil dependent Saudi economy, or if HSBC's multifaceted support appears to weaken. We could raise the ratings if the bank's financial performance proves resilient to the negative change in the environment, notably through increased revenue diversification, and allows the bank to strengthen its business and financial profile, including boosting its capitalization, or if a significant change in the shareholding structure further asserts the commitment of HSBC or the Saudi government.

Saudi Investment Bank (The)

PRIMARY CREDIT ANALYST: PAUL-HENRI PRUVOST, LONDON (44) 20 7176 7210, PAUL-HENRI_PRUVOST@STANDARDANDPOORS.COM

SECONDARY CREDIT ANALYST: EMMANUEL VOLLAND, PARIS (33) 1 4420 6696, EMMANUEL_VOLLAND@STANDARDANDPOORS.COM

ISSUER CREDIT RATING: A-/STABLE/A-2

PUBLICATION DATE: JUNE 5, 2008

Rationale

The ratings on The Saudi Investment Bank (SAIB) reflect its good and resilient financial performance, good asset quality supported by a conservative strategy, satisfactory liquidity profile, and good capitalization. The bank's limited customer franchise and weaker market position than domestic peers', significant concentration risks, and limited geographic diversification offset the positive factors. The long-term rating on SAIB (considered as a government-related entity (GRE) under our methodology) is one notch higher than the bank's stand-alone creditworthiness, to reflect our expectation of the strong likelihood of extraordinary support from the government (classified as interventionist toward its banking sector) in case of need. The bank is 90%-owned by Saudi shareholders, including 38.7% by the Kingdom of Saudi Arabia (AA-/Stable/A-1+), through public institutions.

SAIB is one of the smallest banks in Saudi Arabia, with total assets of Saudi Arabian riyal (SAR) 46.1 billion ($12.3 billion) at March 31, 2008. As its original business was medium-term financing of industrial projects, SAIB did not develop its customer franchise and branch network (27 branches) as fast as competitors. The bank's current drive toward retail banking is diversifying revenues and the loan portfolio, but concentration risks are still high. The 20 largest exposures represented about 1.5x adjusted total equity (ATE) at Dec. 31, 2007. Risks are mitigated, however, as these exposures are mainly to top-tier domestic corporates and government institutions. The 10 largest deposits represented about 40% of total deposits at the same date. SAIB is currently considering acquiring a stake into Bahrain-based Islamic lender Albaraka Banking Group (B.S.C.) (ABG; BBB-/Stable/A-3).

The combined effect of declining brokerage and asset management-related fees, nonrecurrence of sizable securities gains, and impairment on its structured products portfolio dealt a blow to SAIB's financial performance in 2007. Core earnings remained satisfactory, however, and we expect the bank to resume its long-term trend growth in profitability and efficiency after the distortions of these past three years. This should be supported by its limited risk appetite, good cost control, and conservative management. Overall, profitability measures remain satisfactory and in-line with the current ratings on the bank.

SAIB has a satisfactory liquidity profile. Customer deposits represented 149% of total net loans at Dec. 31, 2007. SAIB is well capitalized given its risk profile. ATE represented 14.4% of adjusted assets at year-end 2007. Quality of capital is strong, almost entirely composed of Tier 1. The bank intends to maintain strong capital ratios.

Outlook

The stable outlook reflects Standard & Poor's expectations that SAIB will maintain its good financial profile and performance. We could raise the ratings if SAIB markedly expands its franchise while maintaining a moderate risk profile and appetite. Conversely, the ratings could come under downward pressure if core earnings deteriorate markedly, capital ratios fall, or asset quality drops. Eventually, we would reassess the current ratings on SAIB, should the deal with ABG materialize.

Sharjah Islamic Bank

PRIMARY CREDIT ANALYST: MOHAMED DAMAK, PARIS (33) 1 4420 7322, MOHAMED_DAMAK@STANDARDANDPOORS.COM

SECONDARY CREDIT ANALYST: EMMANUEL VOLLAND, PARIS (33) 1 4420 6696, EMMANUEL_VOLLAND@STANDARDANDPOORS.COM

ISSUER CREDIT RATING: BBB/STABLE/A-2

PUBLICATION DATE: DECEMBER 23, 2008

Rationale

The ratings on Sharjah Islamic Bank (SIB) reflect its strong capitalization, good financial performance, and ownership structure that is dominated by the government of the Emirate of Sharjah (not rated). Offsetting these positive factors are the bank's small size, high lending concentration, and rapid loan growth untested by a sharp economic downturn. The long-term rating on SIB is one notch higher than the bank's stand-alone credit quality. This reflects Standard & Poor's Ratings Services' expectation that the Sharjah government—which owns 30.7% of SIB—is likely to provide some support if needed. Given its strong relationship with the government, SIB appears to be the flagship bank of the emirate. We classify SIB as a government-related entity (GRE) under our methodology.

With total assets of United Arab Emirates dirham (AED) 15.6 billion on Sept. 30, 2008, SIB is a small bank by regional standards. The bank continues to display good financial performance despite recent stock market falls and the slump in liquidity in the emirates' banking system. SIB's equity market exposure is relatively limited and not expected to materially affect the bank's financial performance. The bank also remains relatively liquid and has received new deposits from the United Arab Emirates' and Sharjah governments, which underline the interventionist nature of United Arab Emirates authorities and the government support we factor into the ratings on SIB.

SIB continues to exhibit a superior level of capitalization, with a ratio of adjusted total equity to total assets of 26.4% on Sept. 30, 2008. The bank has good financial flexibility, as demonstrated by the recent capital increase that has helped SIB to maintain stable capitalization despite sharp growth of its assets.

Outlook

The stable outlook balances SIB's good financial profile and commitment from the Sharjah government with the deterioration in the bank's operating environment. We would revise the ratings downward if the bank's liquidity, financial performance, or capitalization decline materially. A negative rating action could also result from any weakening in links with the government of Sharjah. We could raise the ratings—assuming the operating environment recovers—if the bank successfully strengthens its business profile, including through diversifying and reducing concentration risks, with no significant deterioration in capital and financial performance.

The Qatari Insurance Sector In 2009: Short-Term Weaknesses Offset By Long-Term Strengths

PRIMARY CREDIT ANALYST:
DAVID ANTHONY, LONDON (44) 20 7176 7010
DAVID_ANTHONY@STANDARDANDPOORS.COM

SECONDARY CREDIT ANALYSTS:
NEIL GOSRANI, LONDON (44) 20 7176 7112
NEIL_GOSRANI@STANDARDANDPOORS.COM

JAN WILLEM PLANTAGIE, DUBAI (971) 4709 6810
JAN_PLANTAGIE@STANDARDANDPOORS.COM

WHEN THE STATE OF QATAR'S (AA-/STABLE/A-1+) economic prospects are considered alongside the specific strengths, weaknesses, opportunities, and threats confronting the local insurance sector, Standard & Poor's Ratings Services concludes that it is reasonable to be guardedly optimistic for the medium- and longer-term future of the Qatari insurance sector, despite some of the current economic and industry uncertainties discussed in this report.

With the wealth of insurers as well as banks tending to rise and fall in line with the fortunes of their local economy, it is of more than just academic interest to note how GDP has developed in Qatar in recent years, with nominal GDP approaching Qatari riyal (QAR) 300 billion in 2008, or almost double the level of 2005. In per capita terms, this implies some QAR275,000 of revenue per head of population—one of the highest levels in the world. It is on this until recently robust, albeit oil and gas-dependent economic base that the country's nascent aviation, marine, construction, and financial services infrastructure is today being built.

Qatari Insurance Sector: Strengths, Weaknesses, Opportunities, And Threats

In the short term, however, the Doha Stock Market DSM20 Index is, in January 2009, down nearly 50% on the peak of 12,629 reached in June 2008 (or down by approximately 28% (from an Index number of 9,580.45 to 6,886.12) over the 12 months to Dec. 31, 2008). Meanwhile, the share prices of



This page: Known locally as the Zig-Zag Towers, these buildings add visual drama to the Qatari skyline.



Editor's note: This article was originally published on RatingsDirect on January 26, 2009

"…given the still reasonably benign economic context that prevailed for Qatar's insurers until the end of last year, it is not surprising that the five national market leaders have seen spectacular growth in premium volumes and in overall earnings…"

Qatar's own listed insurers are themselves mostly down about 60% on last summer's highs, and the Qatar Insurance Index is down about 40% for the 12 months to Dec. 31, 2008, from a high of 11,690.43 on Jan. 14, 2008, to 4,960.37 by the year end. This suggests that both Qatar and its insurance companies have proven far from immune to global financial influences. Moreover, even though current infrastructure spending continues, perhaps fewer new developments will be agreed in coming months while the economic situation remains unclear and while oil remains below the approximately $75 per barrel rate that seems to be preferred by many budget planners.

The concern today, as the new year gets underway, is that the local economy will maintain the appearance of "business as usual" for another six months or so, driven by the momentum of existing committed spending and the completion of old projects. However, economic activity may start to slow down more visibly in the second half of this year as the pipeline begins to clear of active new developments. Moreover, this downturn in local, regional, and international investment markets is not just an external event unrelated to the ongoing activities of insurers. As the soon-to-be-published accounts for 2008 will show, most insurers have suffered significant, albeit largely unrealized, losses on the asset side of their balance sheets during the fourth quarter, and overall solvency will likely be visibly lower than that reported as of September 2008.

Nevertheless, given the still reasonably benign economic context that prevailed for Qatar's insurers until the end of last year, it is not surprising that the five national market leaders *(see table 1)* have seen spectacular growth in premium volumes and in overall earnings, with their gross premium income increasing in 2007 alone by 27.2%, net premiums by 42.4%, and their net income by 50.4%—a trend that continued strongly in 2008. Meanwhile, at the time of writing, we lack detailed, publicly available financial information on the other, nonlisted domestic players to discuss the performance of the private insurers active in Qatar. However, for reference, the private players include the Qatar Petroleum captive, Al Koot Ins. & Reins. Co., Arabia Ins. Co. Ltd., Libano-Suisse Ins. Co., National Ins. Co. of Egypt, American Life Ins. Co. (ALICO), and, finally, Atlas Assurance Co. Ltd., which is under the control of Libano-Suisse. Each of these private companies generally enjoys much lower premium volumes than the listed majors. Nevertheless, there is no reason to believe that these unlisted companies have not also been benefiting recently from growth and reasonable results, even though the national companies probably still enjoy a market share of over 80% of the local market's premium income.

In addition to the general information conveyed by the numbers in table 2, one initially inconspicuous feature merits attention, notably the difference between gross and net premium

Table 1: Qatari Insurance Sector—Strengths, Weaknesses, Opportunities, And Threats

Strengths	Weaknesses
Very strong long-term economic fundamentals	Small country, small albeit growing population
Authorities supportive of the insurance sector	Reliance on foreign reinsurers to carry major risks
Qatar a hub for intl. aviation and marine transport	Low fixed tariffs on motor third-party liability
Attractive time zone between Europe and Asia	Good state healthcare for all inhibits health insurance
High ongoing infrastructure spending by state	Little demand for long-term lines (life & pensions)
Opportunities	**Threats**
Potential compulsory health cover for foreigners	Powerful new foreign entrants access market via QFC
Generally high growth in insurable activities	Competition from other regional financial centres
Ability to expand into other GCC markets	Inflation: impact on claims and expenses
Takaful policies to attract new retail business	Most local insurers small even by regional standards
Qatar a possible centre for captive insurance?	Regional economic, social, and geopolitical risks

Table 2: Key Indicators Of Listed National Insurers In Qatar (Mil. QAR)

Company (year established)	Standard & Poor's rating*	Gross premiums 2007	Gross premiums 2006	% change 2007/ 2006	Net pre-miums 2007	Net pre-miums 2006	Net income 2007	Net income 2006	Equity 2007
Qatar Insurance Co. S.A.Q. (QIC) (1964)	A/Stable/--	1,518.40	1,192.60	27.3	703.5	456.9	522.4	388.2	3,495.70
Qatar General Ins. & Reins. Co. (1978)	BBBpi (unsolicited rating)	818.4	602.7	35.8	234.9	179.4	127.5	60.3	1,164.80
Doha Insurance Co. Q.S.C. (1999)	BBB/Stable/--	252.6	201.9	25.1	65.5	55.1	44.5	26.8	302.7
Al Khaleej Insurance & Reinsurance Co. Q.S.C. (1978)	BBBpi (unsolicited rating)	252.3	209.2	20.6	114.9	85.4	83.4	35.6	568.4
Qatar Islamic Insurance Co. (1994)	NR	159.4	153.6	3.8	95.1	75.6	44.4	35.9	287
Totals		**3,001.1**	**2,360.0**	**0.3**	**1,213.9**	**852.4**	**822.2**	**546.8**	**5,818.6**

*Source: Standard & Poor's analysis of company annual reports and accounts. *At Jan. 15, 2009. NR—Not rated.*

Table 3: Position Of Listed Qatari Insurers At Sept. 30, 2008 And 2007

(Mil. QAR, except share prices)	Equity Sept. 30, 2008	Equity Sept. 30, 2007	Net premiums Sept. 30, 2008	Net premiums Sept. 30, 2007	Net income Sept. 30, 2008	Net income Sept. 30, 2007	Max. share price	Min. share price 2008
Qatar Insurance Co. S.A.Q.	3,136.6	2,967.2	773.9	562.6	531.6	337.8	236.9	87
Qatar General Ins. & Reins. Co. S.A.Q.	1,288.2	1,164.8	216.0	187.5	250.0	87.3	142.0	80
Al Khaleej Insurance & Reinsurance Co. Q.S.C.	561.6	531.1	86.6	86.2	108.6	55.9	103.5	36.5
Doha Insurance Co. Q.S.C.	425.4	261.5	64.4	51.1	47.1	34.1	59.0	20.6
Qatar Islamic Insurance Co.	301.7	253.3	137.3	134.4	57.4	31.4	88.4	29.1
Totals:	**5,713.5**	**5,177.9**	**1,223.3**	**968**	**994.7**	**546.5**	**629.8**	**253.2**

Note: Totals adjusted to assume QIIC net premiums at 60% of stated gross amount.

income, a difference which suggests that about 60% of the market's total premium income is being transferred out of the country to foreign reinsurers. This high level of cessions reflects the sector's heavy reliance on foreign reinsurers when tendering for domestic commercial and industrial risks, many of which are energy, aviation, and marine-related, and, as such, are too large for the relatively limited capacity of the country's national insurers. Although this comprehensive protection against major industrial losses is in many ways desirable, there remains a concern that local insurers risk becoming technically dependent on the capacity and expertise of the global reinsurance community, and that local management could inadvertently lapse into the passive role of commission-seeking fronting insurer, with insufficient analysis or understanding of the underlying exposures and their pricing. Indeed, even now, some insurers would risk being excluded from the highly profitable commercial and industrial sectors in which they specialize if, for whatever reason, they lost the support of their reinsurers.

Turning to table 3, the most recently published, Sept. 30, 2008 results suggest a continuation of the very positive growth trend of the listed companies, with net premiums up 26.4%, net income up 82.0%, and capitalization up 19.1%. The only factor that has started to decline was the respective share prices, and this decline then further accelerated during October

and November as local and international stock markets suffered a significant downturn. Indeed, the minimum levels indicated in the table were reached in late November or early December 2008, and there has been some slight recovery since that time. This general decline in insurance values seems to be more driven by the general pessimism of investors than by any specific concerns over the insurers' specific performance fundamentals, although the fall in insurers' own investment assets—where some insurers have suffered more severely than others—must be a concern, particularly when the uncertain valuation of some Qatari and other regional property developments is taken into account alongside the actual fall in share prices.

Other Features Of The Market

Low fixed tariff for motor third-party liability

There are also other concerns that affect the Qatari insurance community. First and foremost is the capping by the authorities of the compulsory third-party vehicle liability tariff at a level which has remained unchanged since 1994, notably between QAR250 and QAR350 for saloon cars (dependent upon engine capacity) and a scale starting at just QAR500 for lorries. During the intervening period, for example, the blood money payment for death due to motor accident has continually escalated to what is now QAR200,000—while the toll of road accidents has risen inexorably and inflation has jumped, even though the latter now seems to be abating.

The good news is that the Ministry of the Interior is now said to be inclined to review motor liability tariffs. The less welcome news, however, is that in the interim, the motor insurance account remains the principal point of contact between insurers and the vast majority of their retail customers. Insurers therefore have to be able to offer compulsory third-party liability (TPL) as a potential "loss leader" if they wish to cross-sell additional covers. However, the losses have inhibited the willingness of some insurers to open branches across Qatar or to facilitate customer access to them by telephone or Internet lest they attract clients only interested in unattractive TPL cover. Over time, this reticence toward the retail sector has occasionally turned almost into hostility, and quality of customer service has probably suffered as a result. The concern must be that if professional insurers cannot promise the customer good service and attractive products, then why should policyholders not turn to a bank to obtain their car, travel, and other simple insurance requirements? Perhaps the recent formation of Doha Bank Assurance Co., which has been licensed by the Qatar Financial Centre Regulatory Authority (QFCRA), can be considered as a wake-up call for the entire Qatari insurance community.

Takaful

At another level, explicitly Sharia-compliant takaful insurers would normally have a degree of competitive advantage in targeting retail customers who will often be attracted by the promise of an "ethical" policy. However, compulsory under-pricing on the TPL account reduces overall underwriting performance even at takaful companies, and significantly reduces the profits on the policyholder account that are available for distribution to policyholders. This means that, far from being rewarded with a decent bonus, the careful, claims-free takaful policyholder risks merely subsidizing the losses generated by bad drivers, a phenomenon that may eventually undermine an essential principle of takaful insurance. However, if eventually freed from the losses associated with TPL, it is probable that we shall see much greater interest in takaful insurance in Qatar, and possibly in family takaful (life & savings) in particular. However, as all the existing national insurers have either already set up a takaful operation or are in the process of doing so, any significant move toward takaful and away from traditional insurance need not prove overly threatening in its implications for existing insurance providers as they too will simply write more business through their takaful offshoots.

Captive insurance

Other concerns affecting the insurance sector are many and varied, but include certain aspects of official policy that have had unintended consequences for local insurers. For example, the creation of a captive insurer, Al Koot, by Qatar Petroleum (AA-/Stable/--) in 2003, may have reduced the energy company's insurance expenses and given it direct access to the global reinsurance market. However, the move also potentially



placed a substantial proportion of the country's premium income beyond the reach of the national insurers, although in practice Al Koot for the moment seems prepared to continue to share some of this premium income locally.

Qatar Financial Centre (QFC)

A second example of an initiative that has affected the local sector was the creation in 2005 of the QFC. Now up and running, the QFC is proving successful in establishing a financial services hub in Qatar that can compete with the likes of the Bahrain Financial Harbour (BFH) and the Dubai International Financial Centre (DIFC). However, to make the QFC attractive relative to these longer-established regional rivals, the authorities have not only allowed 100% foreign ownership, but have also given QFC-based insurers the right to bid for domestic, "onshore" business. This ability to quote for local business is a major attraction of the QFC, and one not shared by insurers in either the BFH or the DIFC. However, this means that Qatari insurers now increasingly have to compete against some very finely priced quotations from QFC-based insurers such as AXA Gulf, Zurich International Life, and AIG MEMSA. Although this potent competitive threat may bring longer-term advantages to the commercial health of the sector, the short-term effects constitute a further competitive threat for Qatar's locally established insurers who could previously offset underperformance in retail against satisfactory overall earnings on the commercial and industrial accounts.

Aiming for unified regulation

The QFC has also introduced a further complication into the marketplace with its new, somewhat Anglo-Saxon style regulatory function enforced by the QFCRA. Although this regulatory framework appears prudential and comprehensive, it has nonetheless created tensions relative to the existing supervisory regime applied internally by the Ministry of Finance, Economy & Commerce. It remains to be seen whether the QFCRA will be called upon to provide a single regulatory function, as many expect to happen by 2010. However, a unified regulator enforcing a clear and effective regulatory regime would clearly be a desirable goal.

Health insurance

A final example of an unintended impediment to local business development is the excellent quality of health provision available not only to local nationals, but also to expatriates, where the payment of QAR100 buys them a card that gives access to the world class facilities of the Hamad Medical Hospital. The problem for Qatar's insurers is that whereas health insurance is growing into a major activity for insurers elsewhere in the Gulf Cooperation Council (GCC), development is stifled in Qatar by the State's provision of good, cheap care for nearly all. It would consequently come as little surprise to find substance to the frequent rumors that Qatar will come more into line with its GCC peers by introducing compulsory medical insurance for expatriates and their dependents. The growing number of new, private clinics will facilitate the creation of a proper market for health care in Qatar and will at the same time help alleviate the government's budgetary pressures while opening up an important new line of business for insurers.

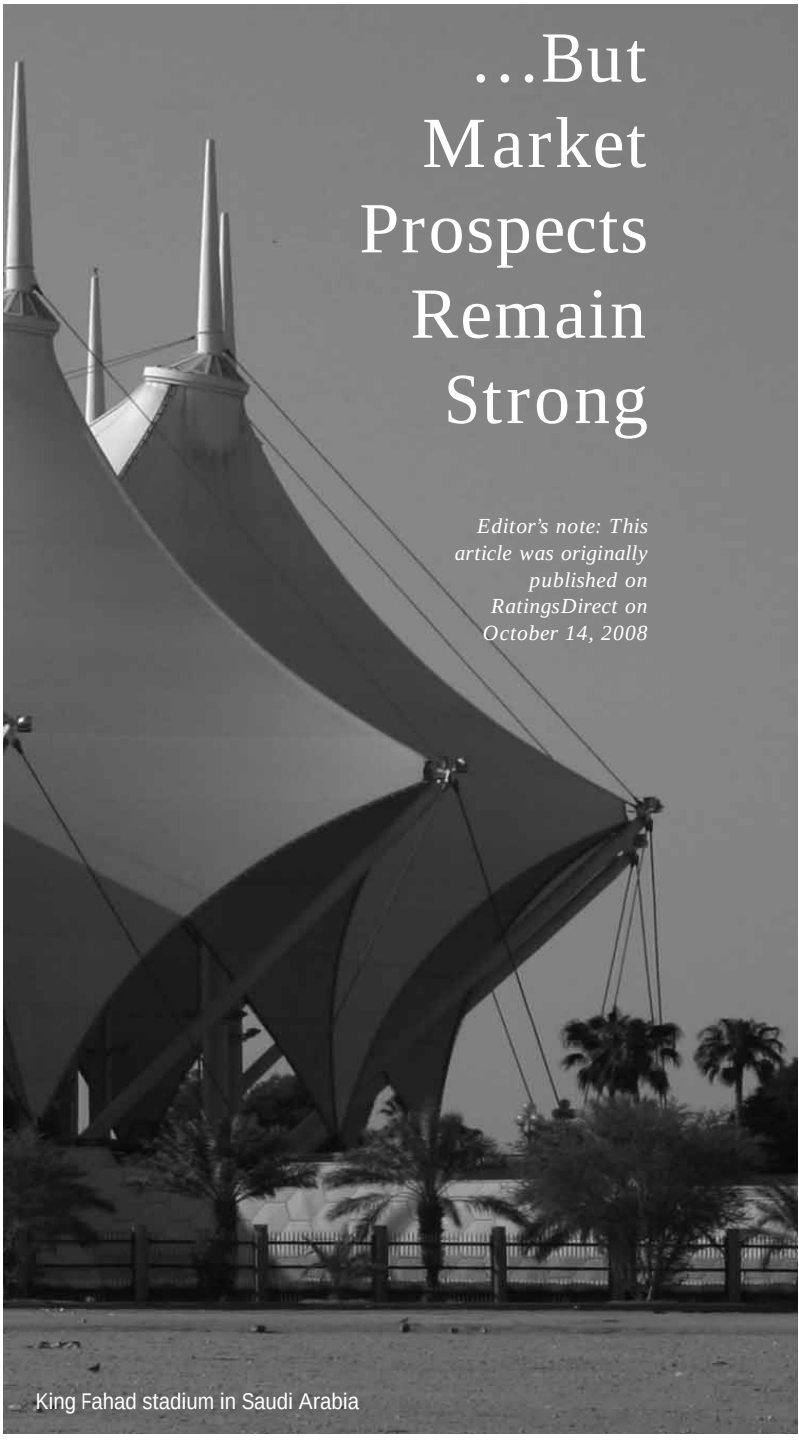
Prospects

Perhaps due to the constraints of an increasingly competitive Qatari insurance marketplace, it is interesting to see that local companies have been making a concerted effort to develop an international dimension to their operations. Consequently, we today see Doha Insurance discussing a possible joint-venture in Yemen, Qatar Islamic operating in Pakistan and Syria, Qatar General in Dubai, and market leader QIC active across most of the rest of the GCC, as well as beyond. Thus, although Qatar is indeed an attractive long-term market for insurers, it is a signal of growing maturity and confidence that even the market leaders—like the Swiss and Dutch a century before them—are starting to feel the need to adopt more internationally diversified business strategies.

Insurance And Reinsurance In The Kingdom of Saudi Arabia: Economic And Industry Risks Exist…

…But Market Prospects Remain Strong

Editor's note: This article was originally published on RatingsDirect on October 14, 2008


King Fahad stadium in Saudi Arabia

STANDARD & POOR'S BELIEVES THAT INSURANCE and reinsurance in the Kingdom of Saudi Arabia (KSA; AA-/Stable/A-1+) entered a new era of strength and opportunity in 2008, despite some inevitable short-term uncertainties during the recent transitional period from an unregulated to a regulated marketplace. During the past three years, most of the 100 or so unregulated, offshore insurers that traditionally made up much of the Kingdom's insurance market have ceased trading in Saudi Arabia. Those that wished to remain active in the Saudi market have had to comply with the new regulations by bringing their local operations onshore. The resulting, newly established KSA operations have had to be listed on the Riyadh Tadawul stock exchange and a majority of their equity has had to be Saudi-owned. An additional aspect of the new regulations has been to force insurers to structure their operations to implicitly comply with Sharia law. This means operating along cooperative insurance lines, with separate shareholder and policyholder accounts. Insurers have also had to adopt the authorities' newly defined regulations on minimum capitalization, corporate governance, market conduct, and employment of Saudi citizens.

These regulations, originally laid down in the Cooperative Insurance Companies Law of July 2003, are now being enforced by the insurance (and banking) supervisor, the Saudi Arabian Monetary Agency (SAMA), and this has led some 42 companies to contact SAMA to seek a license to incorporate and operate locally, of which 25 have either completed or are well-advanced in the approval process *(see table 1)*. With only a few exceptions, such as Malath Co-Operative Ins. & Reins. Co., SABB and Saudi Re for Cooperative Reinsurance Co. (Saudi Re; BBB+/Stable/--), most of these "new" companies are far from being start-ups, except in a purely legal sense. In practice, they are the direct successors of previously offshore operations, and most have inherited management, staff, premises, branding, and customers similar to those that they previously enjoyed when operating as offshore companies. Indeed, insurers such as Mediterranean & Gulf Coop. Ins. & Reins. Co. (MedGulf), Salama Co-Operative Ins. Co., Saudi Arabian Co-Operative Ins. Co. (SAICO), and others have antecedents in the Saudi market that go back decades, as has the market leader, Tawuniya/The Company for Cooperative Insurance (A/Stable/-).

PRIMARY CREDIT ANALYST:
DAVID ANTHONY
LONDON, (44) 20 7176 7010
DAVID_ANTHONY@STANDARDANDPOORS.COM

ADDITIONAL CONTACT:
INSURANCE RATINGS EUROPE,
INSURANCEINTERACTIVE_EUROPE@
STANDARDANDPOORS. COM

Economic Background To The KSA Insurance Market

Although detailed, publicly available market data regarding the new insurers and reinsurers in the Kingdom is still somewhat scarce, even a cursory overview of the macroeconomic and demographic factors relating to the country suggests that the insurance and reinsurance sectors have huge potential for successful growth in the medium and long term. For example, according to figures monitored by MEED magazine *(see table 2)*, the KSA expects to spend at least $564.9 billion on planned major projects. At the very least, this spending implies an inevitable expansion in insurable activity and thus the probability of significant growth in premium volumes in the years ahead. Such statistics lend some credibility to the optimistic claims of certain Saudi insurers, who forecast total market premiums reaching Saudi Arabian riyal (SAR) 30 billion ($8 billion) by the middle of the next decade.

Meanwhile, the population and GDP of Saudi Arabia dominates that of other Gulf Cooperation Council (GCC) members, with some 20 million nationals supplemented by a large force of foreign workers and their dependents *(see table 3)*. As for the levels of insurance premium available within the Kingdom, SAMA has recently published statistics indicating that the entire sector generated some SAR8.6 billion ($2.3 billion) of gross premiums in 2007, of which by far the largest lines were health and motor at SAR3.1 billion and SAR2.4 billion, respectively, or 64% of the total *(see table 4)*.

Some observers may have expected energy-related lines to be more prominent, but it should be borne in mind that much of the Kingdom's energy and energy infrastructure is controlled by Saudi Aramco, which channels virtually all of its insurance requirements through its captive, Stellar Insurance Ltd. (AA-/Stable/--), which is currently based in Bermuda. Stellar, in turn, directly accesses the global reinsurance markets for its protection needs.

However, even with the "leakage" of insurance premium through this and other offshore captives (which appear to have been unaffected by the new insurance regulations), large premium volumes are still available domestically and, equally importantly, they continue to grow rapidly, thereby creating realistic business opportunities for those newly incorporated insurers and reinsurers still endeavoring to enter the market.

Table 3 shows that total available premium in Saudi Arabia grew by 24% between 2006 and 2007. Admittedly, these very high rates of premium growth have been inflated by the introduction of compulsory motor and, more gradually, compulsory health insurance for foreign residents in recent years but, even prospectively, most observers expect to see year-on-year growth in total gross premium income approaching 20%, even if an element of this growth is fueled by inflation.

Insurance penetration and density calculations give final indicators of the market's potential. Insurance penetration, notably gross written premiums as a percentage of GDP, reached 0.61% in 2007, up 14.4% on the previous year. Similarly, insurance density (that is, per capita spending on insurance/population) grew by 20.9% in 2007 to reach $95. Nevertheless, although the rates of growth are strong, the absolute levels still remain far below those regularly seen in Western and some Asian markets, where penetration ratios range from 5% to 9% and density levels can reach as high as $3,287 (source: SIGMA).

New Regulations Will Increase Capacity

The generally increased levels of capitalization that the IPO process is bringing to all the newly incorporated companies is leading to increased capacity at the individual insurance company level, and a probable need to build up business volumes to generate satisfactory profits to remunerate the expanded shareholder base. It therefore seems reasonable to expect these insurers to seek to protect and develop their market presence, although they are not expected to overtake the market's dominant leader, Tawuniya. The latter will undoubtedly face further loss of market share and staff in favor of its newly incorporated rivals. Nevertheless, the growing level of good-quality insurable and reinsurable activity available in the Kingdom suggests that business volumes and technical operating performance at the leading companies will remain at least satisfactory. Standard & Poor's is still convinced that strong technical and overall earnings are a far better indicator of underlying performance and success at an insurer than market share percentages alone.

Despite the legal, accounting, capital, and ownership upheaval caused by the need to conform to the new

"Despite the legal, accounting, capital, and ownership upheaval caused by the need to conform to the new regulations, Standard & Poor's expects to see many former offshore companies display substantial continuity as regards management, strategy, staffing, and operations, with little visible interruption at the client-facing end of their activities."

Table 1: Insurers And Reinsurers In The Kingdom Of Saudi Arabia As Of September 2008

Companies that had received their license to operate from SAMA and were already listed on the Tadawulas by September 2008:
Tawuniya/The Company for Cooperative Insurance (A/Stable/--)
Mediterranean & Gulf Co-Op. Ins. & Reins. Co. (MedGulf)
Malath Co-Op Ins. & Reins. Co.
Saudi Arabian Co-Op. Ins. Co. (SAICO)
Al Ahli Takaful Co. (ATC)
SABB Takaful Co.
Arabian Shield Co-Op Ins. Co.
Salama Co-Op Ins. Co.
Gulf Union Co-Op Ins. Co.
Saudi Fransi Co-Op Assurance (Allianz SF)
Sanad for Co-Op Ins. & Reins. Co.
Trade Union Co-Op Ins. Co.
Al Sagr Co. for Co-Op Ins.
Saudi Indian Co. for Co-Op. Ins.
Arabia Ins. Co-Op Co.
Saudi United Co-Op Ins. Co. (Wala'a Ins.)
BUPA Arabia for Co-Op. Ins. Co.
Saudi Re for Cooperative Reinsurance Co. (Saudi Re; BBB+/Stable/--)
Companies that were awaiting their license to operate and were already listed:
Al Ahlia Co-Op. Ins. Co. (Al-Ahlia)
Allied Co-Op. Ins. Group (ACIG)
United Co-Op. Ass. Co. (UCA)
Companies that were awaiting their license to operate and were not yet listed
Wiqaya Takaful Ins. & Reins. Co.
Al Rajhi Co. for Co-Op. Ins.
AXA Co-Op. Ins. Co.
Ace Arabia Co-Op. Ins. Co.
SAMA—Saudi Arabian Monetary Agency..

regulations, Standard & Poor's expects to see many former offshore companies display substantial continuity as regards management, strategy, staffing, and operations, with little visible interruption at the client-facing end of their activities. As such, we will normally analyze them as established companies and not as genuine start-ups, except where a start-up analysis is clearly appropriate in the absence of even a pro forma historical track record for the Saudi book of business.

Despite the impressive growth potential and the current surge of companies seeking to participate in the KSA insurance market, the sector itself remains essentially skewed toward a limited number of activities. Table 4 shows that 60.0% of 2007 gross premiums related to general insurance, 35.7% to health, and just 3.8% to life assurance-type protection and savings. Net of the SAR3.0 billion of premium ceded to reinsurers, the bias is even more apparent; a full 84% of the whole market's net retained premiums of SAR5.5 billion related almost equally to the two compulsory lines of health and motor *(see table 5)*.

Narrow Focus Of The Market Limits Strategic Choice

It seems to Standard & Poor's that local insurers have only a limited number of strategic choices, none of them easy. They can aim for volume in the highly competitive, administratively demanding areas of health and motor, or use their niche technical skills to pursue higher margins on much lower volumes in fire, engineering, marine, accident, and liability. The only other alternatives are to take on the banks, fund managers, the local stock exchange, and other investment outlets such as property to attract savings money into the insurance sector by offering the prospect of attractive capital gains potential, or to attempt to join the cut-and-thrust of the international reinsurance markets by accessing a sliver of the 35.4% of national gross premium income that is currently being ceded to reinsurers.

No single approach guarantees success, particularly as the regulatory minimum capital requirements now applicable and the ongoing enthusiasm of local IPO investors means that many of the newly listed insurers now commencing operations are extremely well capitalized relative to likely business volumes. In other words, many of the new providers will have too much capital to be able to afford to pursue a small niche strategy

Table 2: Gulf Projects

(Mil. $)	Sept. 8, 2008	Sept. 8, 2007	Percentage change year-on-year
Kingdom of Bahrain	43,599	31,435	38.7
State of Kuwait	296,319	252,662	17.3
Sultanate of Oman	92,401	46,016	100.8
State of Qatar	205,479	142,466	44.2
Kingdom of Saudi Arabia	564,872	363,278	55.5
United Arab Emirates	967,947	662,984	46.0
Gulf Cooperation Council total	**2,170,617**	**1,498,841**	**44.8**
Islamic Republic of Iran	251,543	106,350	136.5
Republic of Iraq	79,526	25,747	208.9
Gulf total	**2,501,686**	**1,630,938**	**53.4**

Source: Middle East Business Intelligence (MEED).

Table 3: Comparative Demographic And GDP Data For Gulf Cooperation Council And Other World Regions

	Pop (mil.)	Pop (%) growth	2007 GDP (bil. $)	GDP growth (%)	GDP per capita ($000s)	Agriculture (%)	Industry (%)	Services (%)
Kingdom of Bahrain	0.8	1.3	24.6	6.6	34.7	0.3	43.6	56.0
State of Kuwait	2.6	3.6	138.6	5.6	55.3	0.4	54.7	44.9
Sultanate of Oman	3.3	3.2	61.2	5.3	19.1	2.2	38.3	59.5
State of Qatar	0.9	2.3	57.7	7.8	75.9	0.1	73.5	26.4
Kingdom of Saudi Arabia	28.2	1.9	572.2	4.7	20.7	3.0	61.8	35.2
United Arab Emirates	4.6	3.8	145.8	8.5	55.2	1.8	59.3	38.9
Gulf Cooperation Council total	**40.4**	**—**	**1,000.1**	**—**	**30.0**	**1.3**	**55.2**	**43.5**
The Russian Federation	141.0	(0.5)	2,076.0	8.1	14.6	4.6	39.1	56.3
U.S.	304.0	0.9	13,860.0	2.2	46.0	0.9	20.6	78.5
E.U.	491.0	0.1	14,450.0	3.0	32.9	2.0	27.1	70.7
World	**6,700.0**	**1.2**	**65,820.0**	**5.2**	**10.0**	**4.0**	**32.0**	**64.0**

Source: United States Central Intelligence Agency.

while still adequately rewarding their shareholders, unless a significant part of earnings comes from investment income, with all the attendant risks that an aggressive investment strategy inevitably brings.

HEALTH INSURANCE HAS ENORMOUS GROWTH POTENTIAL

Looking at the marketplace line by line, health insurance (the largest sector by premium volume) may well be the most interesting for many, if not most insurers at present. Growth has been rapid since 2006 as the authorities introduced compulsory health cover gradually, starting with large employers of expatriate workers and their dependents, and working down to smaller employers. The Ministry of Health, working through the Cooperative Health Insurance Council (CHIC), has robustly promoted compulsory health insurance. Its dual objectives were to reduce spiraling national healthcare costs and to improve the quality of service in healthcare provision through competition. Interestingly, companies that are now obliged to provide health cover to their foreign workers and their families have often found it equitable to extend similar coverage to their Saudi national employees.

In the light of this experience, there is currently much debate in Saudi Arabia concerning the extension, despite the government's recent, much-improved budgetary position, of compulsory health cover to the whole of the Saudi population. Compulsory cover for local nationals could be gradually introduced if, for example, the requirement was extended to encompass all employees, foreign and local, working in the private sector or, ultimately, if public sector employers were also required to provide their staff with health insurance. Were such requirements to be introduced, as many confidently expect, the health insurance sector could easily continue to see steady long-term growth, beyond a doubling or even tripling of the 2007 gross health premium volume of SAR3.1 billion over the next decade.

For its part, Standard & Poor's acknowledges the considerable commercial potential for insurers in the health care sector in Saudi Arabia, although the sector appears to be already well-served on a direct basis by the existing leading insurers, and by specialist health providers such as BUPA Arabia. Even those existing insurers that lack sufficient infrastructure to administer a large health book on their own often feel it necessary to offer the line as an accommodation to their corporate clients. They have almost invariably achieved this through the extensive use of third-party administrators, of which about half a dozen already operate in the Kingdom.

Standard & Poor's believes that no insurer active in Saudi Arabia in 2008 can afford to ignore the health sector when the related premiums are rising toward half the total net premium in the whole market. Competition is likely to become intense, particularly for major and prestige group health accounts. For the moment, at least, the larger medical insurers are all still managing to achieve sound, but reducing, underwriting profits on the line. That said, in other parts of the world health insurance is often problematic because insureds can have a seemingly insatiable appetite for treatment and also because when things go wrong, the intensely personal nature of health care can lead to dissatisfaction by influential individuals. These people then "punish" the insurer by withdrawing other business that they control. In other words, the successful health insurer needs to be able to walk a tightrope between being too generous and too tough in the settlement of claims.

MOTOR MUST REPAIR THE REPUTATIONAL DAMAGE CAUSED BY UNREGULATED INSURERS

After decades of dominating the KSA insurance market in local premium volume terms, motor insurance has now slipped into second place behind health. Motor is also arguably the most competitive sector of the market. The main impetus to volume is the now-compulsory requirement for third-party liability cover, although comprehensive cover is also becoming more common. Before the explosive growth of the health insurance sector, compulsory motor had traditionally been at the core of the retail market, and still represents the primary point of contact between the individual and the insurance industry.

The nature of motor cover in the previously unregulated market caused many individuals to develop a jaundiced view of insurance. Too often, insurers offered poor service and a cavalier approach to the payment of claims. Indeed, many of the smaller motor insurers that have now been appropriately eliminated by the advent of regulation used to do little more than sell the physical insurance documentation that the police would ask for in the event of an accident or when renewing a driving license.

Not surprisingly, this cheap "protection" served to undermine the economic base of the motor insurance sector, with the realistic premiums charged by professional providers

"Looking at the marketplace line by line, health insurance (the largest sector by premium volume) may well be the most interesting for many, if not most insurers at present. Growth has been rapid since 2006…"

Table 4: Gross Written Premiums By Line Of Business In The Kingdom Of Saudi Arabia, 2006–2007

	2007		2006		
Line of business	**(Mil. SAR)**	**Total (%)**	**(Mil. SAR)**	**Total (%)**	**Growth 2006-07 (%)**
Health	3,065	36	2,222	32	38
Motor	2,440	28	1,920	28	27
Property	742	9	769	11	(4)
Accident and liability (and other)	577	7	580	8	0
Marine	532	6	431	6	23
Engineering	480	6	544	8	(12)
Protection and savings	327	4	218	3	50
Energy	305	4	127	2	141
Aviation	115	1	126	2	(9)
Total	**8,583**	**100**	**6,937**	**100**	**24**

Source: Saudi Arabian Monetary Agency (Insurance Supervision Dept.) Market Survey Report, 2007. SAR—Saudi Arabian riyal.

appearing prohibitively expensive. Fortunately, the removal of the unprofessional element means that the current generation of providers can now attempt to charge economic rates that vary according to the type of risk.

Standard & Poor's nevertheless notes that the motor account is also the area where the new, explicitly Sharia-compliant takaful insurance providers may enjoy a real competitive advantage. Because motor cover reaches so deeply into the population, it encounters a mass clientele that will often have an innate dislike of insurance based on poor experiences under the old, unregulated regime. Moreover, with this clientele, the position can be further confused by considerations of what does and what does not comply with Sharia law. Assuming that actual pricing is more or less equal, it is these buyers of motor cover that will most likely, on balance, opt for the comfort and ethical security of a product that is explicitly marketed as takaful.

Life protection and savings products remain marginal

As in many countries of the world, it is the banks, rather than insurers, that are most readily associated with savings products. Similarly, such are the opportunities for direct investments in local property and stocks and shares, that there is only negligible demand for insurance-wrapped savings products, particularly as there is little need to shelter income from capital gains taxes. Nevertheless, some insurers are keen to explore and develop opportunities for protection products, in particular the term-life cover required of borrowers lest they die before a loan has been repaid. The recent difficulties affecting some foreign providers of sophisticated protection covers and asset management services may create some limited opportunities for Saudi insurers to expand in the life protection and savings space. However, as tables 4, 5, and 6 show, savings and protection still represents a minor part of the overall insurance sector, at just 3.8% of gross and 4.8% of net premiums.

Pure Reinsurance Comes Onshore

Following its licensing in July 2008, Saudi Re (BBB+/Stable/--) became the first dedicated reinsurer to commence underwriting in the KSA. Until this time, all pure reinsurance capacity in the Kingdom had been provided by offshore regional and, more particularly, international and global reinsurers. Meanwhile, those other KSA-based insurers that also have a license to write reinsurance (hence the reference to "reinsurance" in their company names) are expected to use the license only to write co-insurance which, in Saudi Arabia, is technically handled as if it were reinsurance. Given that no other applications for pure

Table 5: Net Written Premiums By Line Of Business In The Kingdom Of Saudi Arabia, 2006–2007

	2007		2006		
Line of business	(Mil. SAR)	Total (%)	(Mil. SAR)	Total (%)	Growth 2006-07 (%)
Health	2,403	43	1,843	42	30
Motor	2,297	41	1,814	42	27
Protection and savings	267	5	153	4	74
Accident and liability (and other)	219	4	243	6	(10)
Marine	170	3	124	3	37
Engineering	98	2	84	2	16
Property	84	2	81	2	4
Aviation	4	0	4	0	(17)
Energy	2	0	0	0	—
Total	5,544	100	4,347	100	37

Source: Saudi Arabian Monetary Agency (Insurance Supervision Dept.) Market Survey Report, 2007. SAR—Saudi Arabian riyal.

Table 6: Gross Claims Paid By Line Of Business In The Kingdom Of Saudi Arabia, 2005–2007

	2007		2006		2005	
Line of business	(Mil. SAR)	Total (%)	(Mil. SAR)	Total (%)	(Mil. SAR)	Total (%)
Health	1,898	47	1,240	41	963	38
Motor	1,218	30	1,010	33	882	35
Protection and savings	38	1	35	1	45	2
Accident and liability (and other)	170	4	170	6	112	4
Marine	166	4	155	5	240	9
Engineering	219	5	102	3	78	3
Property	283	7	300	10	218	9
Aviation	63	2	18	1	13	1
Energy	6	0	9	0	1	0
Total	**4,061**	**100**	**3,040**	**100**	**2,552**	**100**

Source: Saudi Arabian Monetary Agency (Insurance Supervision Dept.) Market Survey Report, 2007. SAR—Saudi Arabian riyal.

reinsurance licenses are currently before SAMA, it appears likely that Saudi Re will enjoy both a "first mover" advantage and also an undisputed local market position for at least the next 18 to 24 months. Nevertheless, we expect that in due course at least one or two additional reinsurers will also seek to set up in the Kingdom.

Given the current surplus of capacity in global reinsurance markets, the creation of indigenous reinsurers within the Kingdom may at first appear surprising. However, the authorities are known to be keen to develop a fully-fledged reinsurance as well as insurance infrastructure within the country. They aim to improve the sophistication of the local market, create skilled employment opportunities for nationals, and to help keep at least a part of the enormous sums currently leaving the country in the form of ceded reinsurance premiums within the Kingdom. As tables 7 and 8 show, as a whole, the GCC region exports over half its markets' gross premium income to reinsurers, with Saudi Arabia transferring SAR3.0 billion in 2007 (35.4% of its gross premiums), excluding the additional cessions made by captives.

Incentives exist for potential entrants to the reinsurance market

Reinsurers considering incorporation within the Kingdom are attracted by the potential to tap at least a part of the ceded premium flow and by the significant regulatory incentives. Such incentives already include local regulations imposing a

Table 7: Gulf Cooperation Council Reinsurance Markets (2006 Data)

Country	Insurance premium (mil. $)	Ceded to reinsurers (%)	Reinsurance premium (mil.$)
United Arab Emirates	2,726	55	1,499
Kingdom of Saudi Arabia	1,850	37	690
State of Kuwait	628	60	377
State of Qatar	573	58	332
Sultanate of Oman	349	64	223
Kingdom of Bahrain	308	56	173
Total	**6,434**	**51**	**3,288**

Source: Logic Management Consulting Research.

Table 8: Kingdom of Saudi Arabia Insurer Retention Ratios By Line Of Business, 2005–2007

(%)	2007	2006	2005
Health	78.4	82.9	80.8
Motor	94.1	94.5	93.7
Marine	31.9	28.8	29.5
Engineering	20.3	15.5	19.2
Property/fire	11.3	10.5	10.8
Aviation	3.1	3.4	2.9
Energy	0.8	0.0	0.1
Accident and liability (and other)	38.0	42.0	43.1
Total	**64.6**	**62.4**	**60.9**

Source: Saudi Arabian Monetary Agency (Insurance Supervision Dept.) Market Survey Report, 2007.

5% withholding tax on premiums ceded to foreign reinsurers, and there is also a slightly ambiguous and currently unenforced regulatory requirement that KSA-based insurers should seek to place at least 30% of their reinsurance locally, unless they receive a written waiver from the authorities.

Although Standard & Poor's would not expect SAMA to oblige local companies to place a full 30% of their cessions with just one local reinsurer, Saudi Re is nonetheless expected to benefit from these fiscal and regulatory incentives. Moreover, as additional reinsurers set up in the Kingdom and cedants gain a choice of local reinsurance providers, it becomes easier to believe that the 30% local reinsurance requirement will be much more actively enforced.

Strong Regulation Brings Strong Prospects

The KSA's December 2005 membership of the World Trade Organization may have provided the necessary catalyst for the regulatory changes now being seen in the insurance sector. However, Standard & Poor's believes that the real reason behind the current restructuring of the market is the authorities' genuine desire to provide the country with the modern financial infrastructure it needs to service the increasingly diverse and complex needs of its steadily diversifying economy of $572.2 billion of GDP as of 2007, as well as the requirements of a young and rapidly growing population.

Given the limited number of Saudi insurance ratings currently in the public domain, it is difficult to discuss an outlook for the Kingdom's insurance and reinsurance sectors in ratings terms. However, in the medium to long term, Standard & Poor's is optimistic concerning the very good and even strong prospects of those companies that it has so far had an opportunity to consider in detail. Insurers, like banks, tend to prosper when the economy in which they principally operate is strong.

Nevertheless, in the short term, market conditions are likely to remain very competitive, particularly in the main lines of health and motor, and this inevitably encourages caution. Indeed, after the euphoria among Saudi investors regarding the insurance sector IPOs of the last 18 months caused the stock price of the new issues to soar, it is salutary to observe that the Tadawul Insurance Index declined by 58.9% during the nine months to Sept. 30, 2008. By contrast, the Tadawul All-Share Index fell by only 32.4% over the same period. Both indices have fallen further since then *(see table 9)*, but are expected to recover somewhat.

We take comfort from the belief that SAMA will not long tolerate the behavior of any management team that seeks growth in market share through persistent, excessively low tariffs. That said, we are nonetheless finding that the very strong capitalization that KSA-based insurers often enjoy is being somewhat offset in our analysis by cumulative concerns over the increasingly competitive nature of the marketplace, by the difficulties most companies face in recruiting and retaining skilled senior and operational staff, and also by some insurers' controlled but still significant investment exposure to volatile equity and property markets.

Meanwhile, as a country, Saudi Arabia itself will also face challenges as it seeks to further diversify its economy away from a dependence on energy-related activities. In particular, the creation of appropriate and sustainable employment for an already large, young and still rapidly growing population remains a major social and political imperative. Today, over half the population of Saudi Arabia is estimated to be below the age of 21 and many thousands of young men attempt to join the workforce every year.

As long as social, political, or geopolitical issues do not intrude to destabilize the likely evolution, Standard & Poor's believes that there are excellent prospects for the successful development of a well-regulated, thriving domestic and regional insurance and reinsurance infrastructure. This will help service the needs of the economy while at the same time creating valuable career opportunities for Saudi nationals. That said, insurers are not always held in high esteem either as employers or as service providers, and the industry must organize itself to improve its image in the retail sector by better explaining the value and, to some extent, the ethical acceptability of their products and services. In the interim, the suspicion remains that unless a given type of insurance cover is made compulsory, too many Saudi citizens will simply not buy it.

Prospectively, the search for market share and a critical mass of revenue by the Kingdom's many new-entrant insurance providers will inevitably lead to yet more competitive pressures and to some soft pricing, particularly for prestigious corporate accounts. Consequently, during the newly reformed sector's



Table 9: Tadawul Stock Exchange Data On Listed KSA Insurance And Reinsurance Companies

(In order of listing date)	Total shares issued (Mil. SAR)	Free float on Tadawul (Mil. SAR)	Free float (%)	Market capitalization as of Sept. 30, 2008 (Mil. SAR)	Closing share price as of Sept. 30, 2008 (SAR)	Closing share price as of Dec. 31, 2007 (SAR)
Tawuniya/The Company for Cooperative Insurance	50	29.5	59.1	3,200	64.00	150.25
Malath Co-Op. Ins. & Reins. Co.	30	14.2	47.5	2,850	95.00	152.75
Mediterranean & Gulf Co-Op. Ins. & Reins. Co. (MedGulf)	80	19.2	24.1	1,716	21.45	54.75
Saudi Fransi Co-Op. Assurance (Allianz SF)	10	3.1	31.0	495	49.50	115.50
Salama Co-Op. Ins. Co.	10	4.0	40.0	570	57.00	98.00
Saudi United Co-Op. Ins. Co. (Wala'a Ins.)	20	8.0	40.0	316	15.80	63.00
Arabian Shield Co-Op. Ins. Co.	20	8.0	40.0	320	16.00	64.25
SABB Takaful Co.	10	3.5	35.0	437	43.70	116.50
Sanad for Co-Op. Ins. & Reins. Co.	20	8.0	40.0	380	19.00	59.50
Saudi Arabian Co-Op. Ins. Co. (SAICO)	10	4.0	40.0	342	34.20	140.75
Saudi Indian Co. for Co-Op. Ins.	10	4.0	40.0	490	49.00	106.75
Gulf Union Co-Op. Ins. Co.	22	8.8	40.0	348	15.80	60.75
Al Ahli Takaful Co. (ATC)	10	2.6	26.5	538	53.75	145.25
Al Ahlia Co-Op. Ins. Co. (Al-Ahlia)	10	4.0	40.0	339	33.90	119.00
Allied Co-Op. Ins. Group (ACIG)	10	4.0	40.0	339	33.90	100.75
Arabia Ins. Co-Op. Co.	20	8.0	40.0	316	15.80	N/A
Trade Union Co-Op. Ins. Co.	25	10.5	42.0	350	14.00	N/A
Al Sagr Co. for Co-Op. Ins.	20	8.4	42.0	295	14.75	N/A
United Co-Op. Ass. Co. (UCA)	20	8.0	40.0	564	28.20	N/A
Saudi Re for Cooperative Reinsurance Co.	100	40.0	40.0	1,090	10.90	N/A
BUPA Arabia for Co-Op. Ins. Co.	40	16.0	40.0	558	13.95	N/A

Source: Data extracted from Saudi stock exchange (Tadawul) Web site. N/A—Not applicable.

current development phase, Standard & Poor's expects to see some volatility in major client relationships, staff, and bottom-line earnings before a clearer landscape starts to emerge in which it will be possible to better identify the likely winners and losers in the new marketplace.

However, even some of the weaker players will still be able to buy time, despite consistent underperformance, because of their relatively easy access to additional capital or, in some instances, by privileged access to the business of their major shareholders. At some point soon, and with the likely encouragement of the authorities, Standard & Poor's expects to see some significant moves toward consolidation of the marketplace, with a concentration of market share in the accounts of the top 15 or so insurers, even if the total number of licensed companies continues to climb to well in excess of 30.



Growing Opportunities For Insurance And Reinsurance In The Sultanate of Oman

EVEN NOW, 2007 IS STILL REMEMBERED as a tempestuous year for the Sultanate of Oman—both literally and figuratively. The country saw euphoria in the investment markets, with local share indices rising more than 60% during the year. Yet it also saw the suffering and loss wrought by Cyclone Gonu, which cast a temporary underwriting shadow over the bright investment climate. Today, Omani insurers and regulators are still trying to rationalize their operations after this testing experience. Nevertheless, the Sultanate was lucky: oil, gas, and investment revenues remained at record levels, and the cyclone dissipated at sea, reducing the damage that could have been caused had it made landfall. The cyclone, a one-in-100-year event (the last having occurred in 1891), caused mostly flood damage and business interruption. All the same, Gonu still caused between Omani rial (OMR) 3 billion and OMR4 billion of economic loss, of which OMR245 million (approximately $600 million) was insured.

Inevitably, the Gonu claims were not shared evenly across the sector and the level of retained losses clearly hurt the two or three unrated non-life insurers particularly hard hit through their commercial, industrial, and government-related business accounts. Despite the financial pain, market intelligence following the cyclone indicates that the insurance community performed commendably in maintaining customer services and claims handling. Whatever the future brings, Oman's insurers and regulators can be content that they have been put to the test and not found wanting. Meanwhile, the population of over 2.6 million, which has often appeared skeptical of the benefits of insurance, may now be a little less so.

Despite the 2007 losses, the Sultanate of Oman, with its strong sovereign rating of A/Stable/A-1, can still legitimately claim to have much to commend it to insurers and reinsurers. Traditionally, its economy has been based on agriculture, fishing, and maritime activities, and these still provide a livelihood for over half the population. However, the development of tourism for the affluent and the exploitation of the country's modest but valuable oil and now gas resources have long since overtaken these sectors in economic terms. Oil and gas exports now provide almost all of Oman's fiscal revenues and exports, and just under half of its projected 2008 per capita gross domestic product of $17,000.

Over the last two decades, Oman has developed a thriving domestic retail and commercial insurance sector, comprising what the authorities formally classify as 11 "national" and nine "foreign" insurers, as well as some 16 authorized insurance brokers. Year-on-year growth in total market premiums is also attractive at a healthy 15% a year on average, fueled by the Sultanate's booming economy and by its burgeoning population. These factors helped generate total non-life market premiums of OMR137.0 million in 2007, up 15.9% on the OMR118.2 million of 2006. Life premiums added a further OMR31.7 million of income in 2007, up 21.6% on the OMR26.0 million of the previous year. That said, rising inflation has fueled some of the growth; as elsewhere in the region, inflation is a growing issue and in Oman now exceeds 10% a year by some estimates.

Fortunately for the prospects of local insurers and reinsurers, insurable activity goes well beyond a concentrated dependence on oil and gas. Of the market's total retained non-life net written premiums of OMR64.8 million in 2007 (that is, inclusive of all local and foreign inward business, but net of foreign outward reinsurance of OMR75.5 million), 76.6% of the net premiums related to motor, 4.5% to property, 4.9% to marine, and the balance of 14.0% to what the regulatory returns describe as "other." This includes lines such as commercial, industrial, and energy. "National" Omani companies wrote 73.8% of these total non-life net premiums, while foreign-controlled insurers operating locally generated the remainder.

Inward non-life premiums written totaled OMR140.2 million in 2007. Of these, half (OMR70.0 million) were then ceded abroad. As these cessions tend to represent good quality business, the leading players could support further growth by using their stronger balance sheets and ratings to permit somewhat higher retentions, where appropriate.

Diversified sources of revenue apart, Omani insurers also derive strength from the generally supportive and pragmatic stance of the Sultanate's government agencies. These are rightly keen to maintain a vibrant insurance sector, not only to protect the country's population and assets, but also to help develop its financial infrastructure, while at the same time creating professional job opportunities for its young and still rapidly growing population. In particular, insurers can take comfort from the supervisory infrastructure that supports the local insurance and reinsurance sector. Oman's regulator, the Capital Markets Authority (CMA) is one of the most respected in the



PRIMARY CREDIT ANALYST:
DAVID ANTHONY
LONDON (44) 20 7176 7010,
DAVID_ANTHONY@STANDARDANDPOORS.COM

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Opposite: Sur, a city on the coast of the Gulf of Oman, was badly affected by Cyclone Gonu in June 2007.

region. Its reputation was further confirmed by its quiet but effective counsel of insurers in the wake of Cyclone Gonu, and by its patient efforts to codify international best practice into a set of prudential regulations encompassing solvency, corporate governance, and market conduct.

Although the CMA supports the insurance sector for which it is responsible, it is not explicitly protective. Oman has been a member of the World Trade Organization (WTO) since late in 2000 and has signed a free trade agreement with the U.S. Therefore, neither regulators nor insurers can have any illusions; their future will be characterized by competition, fueled by liberalization and globalization. This being the case, the CMA continues to urge local insurers to adopt international best practice and to prepare for steadily increasing competition from foreign companies. In an Omani insurance context, "foreign" essentially implies providers from other Gulf Cooperation Council (GCC) countries, although as table 2 shows, several international majors have a presence in Oman. Usually, these international companies target a specialist line of business or one of the expatriate communities working in Oman.

Standard & Poor's Ratings Services expects the regulatory framework to change to come into line with emerging norms across the GCC region. The CMA has previously set aside plans for a radical overhaul of the local insurance law and instead has continued to adapt the 1979 regulations on a piecemeal basis as a pragmatic, interim solution. In due course, we expect that a new body of largely pan-GCC insurance law will be promulgated, possibly along lines not dissimilar to the newly applied insurance regulations originally unveiled in neighboring Saudi Arabia in 2003. These seek local incorporation and listing of all insurers, and prudent minimum and risk-based solvency requirements. Whatever emerges, we expect the Omani authorities to maintain their pragmatic stance, and while prudence will no doubt remain at the core of any prospective insurance legislation, the CMA is most unlikely to impose on the local industry any unnecessarily restrictive requirements that could impede its successful development.

Inevitably, some aspects of the regulations cause friction. For example, some insurers continue to lobby the CMA to limit the number of new operating licenses issued, although the Sultanate's treaty obligations would render any such limitation problematic. Another issue that became a particular subject for debate in 2007 was the regulation of investment holdings through asset concentration limits. As equity values soared, insurers found themselves breaching regulatory investment limits, which forced them to sell strongly performing equities in order to replace them with alternative, less-buoyant assets. The CMA is likely to compromise here by moving as quickly as possible toward a risk-based form of solvency assessment. Eventually, this will allow companies to underwrite and invest as they see fit, but with the regulations imposing far higher capital requirements against riskier positions, whether on the investment or on the underwriting side.

A third area of concern for some retail insurers has been the CMA's introduction of a unified motor policy, which came into effect on July 1, 2008. The policy is designed to help unsophisticated consumers compare offerings from different insurers while at the same time avoiding the risk of them choosing a policy made cheaper by means of short-sighted exclusions such as "storm, tempest, and flood," This not-uncommon practice left too many Omanis without cover against the effects of the Gonu. The inevitable downside of a unified policy, of course, is that it could further reinforce the tendency of too many of Oman's retail insurers to offer a largely undifferentiated suite of products to the customer, with the competition coming in the form of price-cutting alone, rather than through service or product sophistication.

An interesting side-effect of the unified policy has been that it has already led some insurers to adopt a much more selective approach to motor underwriting, with significantly higher tariffs for young and other accident-prone drivers than was the case previously. The danger here is that some of the smaller and more-recent entrants into the insurance market, which are naturally keen to build up their market shares, may take on too much of this higher-risk motor business, creating for themselves an uneconomically priced, concentrated book of high-risk exposures.

The CMA has also changed certain regulations, such as articles 32 and 34b of the insurance code. The cumulative effect of these regulations was to direct government business toward the "national" insurers, even if they were more expensive than foreign providers, and to oblige the lead local insurer to offer to share such business with other national companies. In practice, this seemingly benign arrangement for locally owned companies led to frequent and occasionally

Table 1: Summary Of Estimates of "National" Insurers Established In Oman At Year-End 2007

(OMR 000's)	Rating	Total assets	Total investments	Gross direct premiums	Total non-life net premiums written	Number of policies
Dhofar Insurance Co.	NR	90,979	38,548	45,614	12,970	349,769
Oman United Insurance	'BBB'	44,211	32,458	25,989	13,008	115,838
Al Ahlia Insurance Co.	NR	34,256	20,794	16,907	8,530	121,925
National Life Insurance	NR	27,492	24,356	13,254	—	14,798
Falcon Insurance Co.	NR	19,578	6,660	5,596	1,183	13,018
Royal & Sun Alliance	NR	17,692	9,853	10,007	6,031	21,766
Al Madina Gulf Ins. Co.	NR	15,964	9,867	3,711	2,599	9,391
Oman & Qatar Ins. Co.	NR	12,195	7,641	5,768	3,191	20,218
Muscat Insurance Co.	NR	8,303	4,747	5,823	306	5,117
Muscat Life Insurance	NR	6,867	5,471	4,161	—	265
Vision Insurance Co.	NR	—	—	—	—	—
Total		**277,538**	**160,396**	**136,831**	**47,818**	**672,105**

OMR—Omani rial. Source: CMA Insurance Market Review, 2006–2007. NR—Not rated.

Table 2: Summary Of Estimates of "Foreign" Insurers Established In Oman At Year-End 2007

(OMR 000's)	Rating	Total assets	Total investments	Gross direct premiums	Total non-life net premiums written	Number of policies
American Life Ins. Co.	NR	36,902	34,330	7,907	660	13,122
The New India Assurance Co.	NR	15,868	14,682	10,810	8,519	42,061
Arabia Insurance Co. S.A.L.	NR	11,993	8,501	4,466	2,478	12,405
AXA Insurance Gulf (BSC)	NR	8,854	4,828	6,334	4,332	20,452
Al Nisr Insurance Co. SLA	NR	3,208	1,021	1,180	813	8,068
Iran Insurance Co.	NR	1,420	1,228	185	137	210
Life Ins. Corp. Intl. E.C.	NR	799	317	930	—	836
AIG MEMSA Ins. Co.	NR	—	—	—	—	—
Oman Ins. Co. (Branch)	NR	—	—	—	—	—
Total	**NR**	**79,044**	**64,909**	**31,811**	**16,939**	**97,154**

OMR—Omani rial. NR—Not rated. Source: CMA Insurance Market Review, 2006–2007.

"Diversified sources of revenue apart, Omani insurers also derive strength from the generally supportive and pragmatic stance of the Sultanate's government agencies. These are rightly keen to maintain a vibrant insurance sector, not only to protect the country's population and assets, but also to help develop its financial infrastructure…"

serious disputes when the leader was accused of delays in notifying the detail of some very large risks. As a consequence, some insurers were unclear as to whether or not they were on risk for a share of some very large policies, and consequently whether or not they needed to put in place additional reinsurance protections.

Now that these regulations relating to the sharing of business have been scrapped, the leader is free to retain all of the risk if it so chooses, though the continuation of article 57 means that parties looking to cede surplus risks must still offer them domestically before looking to reinsure them cross-border.

Muscat's insurance circles have predictably been discussing all the possible options for co-insurance and reinsurance. Interestingly, 2008 has at last seen the long-mooted formation of Oman Re, an autonomous operation that nonetheless enjoys the strong financial support of the local market leader. It would be an exaggeration to say that Oman—or even the GCC—has an absolute need for locally based reinsurers, given the ample capacity available from the global reinsurance market. However, it is fair to suggest that local insurers and supervisors may nonetheless welcome the creation of a pool of local reinsurance expertise.

With insurers currently ceding half the country's gross premium income to reinsurers abroad, a plausible case can be made to encourage the retention of more of this premium within the Sultanate. However, even the creation of Oman Re is unlikely to end the current reliance on foreign reinsurers because no local or start-up reinsurer can risk assuming exposures as large and concentrated as the major energy and infrastructure risks that Oman's insurers currently have to cede internationally. Therefore, we expect that Oman Re will serve more as a useful complement to the work of other regional and international reinsurers without posing a significant competitive challenge to them.

Overall, therefore, the Sultanate of Oman can be said to represent an interesting and steadily growing market for general insurance and reinsurance business, life and, more particularly, for health covers. True, the region is subject to various geopolitical risks and natural perils, but these are largely offset by the opportunities inherent in the combination of strong economic and demographic growth. Meanwhile, neighboring Yemen has started to open up and develop its infrastructure. Over the longer term, this may create opportunities that some Omani insurers and reinsurers will wish to consider, albeit very cautiously.

Although the revenue and performance ratios and projections look attractive, the absolute size of the Oman insurance market remains relatively modest by many international standards. Therefore, we expect that although international majors will continue to target "big ticket" Omani energy and infrastructure risks, as well as more-sophisticated specialty requirements, the local retail and small commercial sectors will remain largely the preserve of indigenous and regional insurers, notably companies that can realistically aspire to build sufficient local scale to operate cheaply and efficiently.

Prospectively, some Omani insurers will opt to increase their absolute levels of activity by expanding into other GCC markets, just as Oman United Insurance Co. S.A.O.G. has done with its current move into Qatar. Other, smaller Omani insurers may have to concede that the only realistic way to develop their activities is to merge with a local competitor or a GCC-based peer, thereby pooling their human and financial resources before seeking to tackle new horizons.

Oman Insurance Market Loss Ratios 2007 & 2006

Loss ratios (%)	2007	2006
Marine		
National Cos	22	21
Foreign Cos	20	37
Property		
National Cos	666	34
Foreign Cos	2,245	86
Motor		
National Cos	150	83
Foreign Cos	106	76
Other		
National Cos	85	10
Foreign Cos	52	19

Source: CMA Insurance Market Review, 2006–2007.

Standard & Poor's Approach To Rating Takaful And Retakaful (Islamic Re/Insurance) Companies

PRIMARY CREDIT ANALYST:
KEVIN WILLIS, LONDON (44) 20 7176 7085
KEVIN_WILLIS@STANDARDANDPOORS.COM

SECONDARY CREDIT ANALYSTS:
NIGEL BOND, LONDON (44) 20 7176 7063,
NIGEL_BOND@STANDARDANDPOORS.COM

NEIL GOSRANI, LONDON (44) 20 7176 7112
NEIL_GOSRANI@STANDARDANDPOORS.COM

Editor's note: Standard & Poor's Ratings Services is refining and adapting its methodology and assumptions for Rating Takaful And Retakaful (Islamic Re/Insurance) Companies related to "Criteria: Principles of Corporate and Government Ratings," which we published on June 26, 2007, on RatingsDirect at www.ratingsdirect.com and Standard & Poor's Web site at www.standardandpoors.com. We are publishing this article to help market participants better understand our approach to analyzing Takaful And Retakaful (Islamic Re/Insurance) Companies.

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Introduction

The past five years have seen takaful (Islamic insurance) grow from a niche product servicing relatively limited demand—both by geography and client—to become a mainstream risk management offering. Particularly well established in the Far East, especially Malaysia and Indonesia, it is now growing rapidly in the Arab world, and expanding across Europe. With the development of takaful, the growth of retakaful was seen as inevitable as a necessary and Sharia compliant version of reinsurance.

Standard & Poor's Ratings Services has rated a number of Islamic insurers and reinsurers. In this article, we comment on the way that our rating criteria have been adapted to address the particularities of this product.

We note that our ratings on takaful and retakaful companies do not address Sharia compliance. A Standard & Poor's insurer financial strength rating is a current opinion of the financial security characteristics of an insurance organization with respect to its ability to pay under its insurance policies and contracts in accordance with their terms. We treat the mechanisms employed to deliver Islamic insurance solutions in a Sharia-compliant model as being a management decision over the operation of the company business model. The religious context itself is not part of the credit rating decision.

The Analytical Categories

Standard & Poor's insurer financial strength ratings generally focus on the following categories of analysis:

- Industry and economic risk,
- Management and strategy,
- Competitive position,
- Enterprise risk management,
- Earnings,
- Investments,
- Liquidity,
- Capitalization, and
- Financial flexibility.

Generally, no single category dominates the assignment of or action on a rating. Relevant rating factors may include how well, in our view, the capital base is managed and how robust it is to absorb likely earnings volatility, and how the earnings stream is suited, in our opinion, to support liquid assets to enable prompt claims settlement.

Standard & Poor's generally publishes a detailed commentary in support of each rating, covering each of the analytical categories highlighted above. Below, we identify those aspects of the (re)takaful business model that may be subject to specific consideration, or special treatment in Standard & Poor's analysis.

Industry And Economic Risk

We consider the effectiveness of the regulatory regime that the (re)takaful company is working within. Insurance supervisory bodies set minimum operational standards at some level to minimize the risk of insurance company failure, but typically regulation in any domicile only draws a line, below which companies may not operate. How far above those minimum standards a company chooses to operate is entirely a decision



for owners/management. We observe that no special regulatory treatment is currently given to the (re)takaful sector relative to the conventional equivalents. International insurance supervisors, we understand, are generally consistent in their view that the (re)takaful business model is, for their purposes, a "normal" insurance model and should be regulated consistent with other insurance models in terms of solvency/capital adequacy requirement and regulatory filings.

We assess economic risk by reference to Standard & Poor's sovereign ratings, and may adapt our assessment to reflect the likely potential demand for Islamic insurance in the operational domicile. For instance, we believe that countries with a large Islamic community are likely to have stronger economic/business drivers than where the Islamic population is smaller. We also consider this factor under the Competitive Position section.

Competitive Position

Under this category, Standard & Poor's seeks to assess the ability of the current and targeted business source to provide a lasting, profitable revenue stream to the insurer. We believe at this stage that takaful is still a developing business that has to prove itself against conventional insurance structures. However, contribution (premium) growth has typically been very rapid, which raises the question, in our view, whether the management and the systems of (re)takaful companies have the ability to keep up with this growth, and whether they have adequate capital availability to properly support it. Where takaful companies are in direct competition with conventional insurers, as indeed most are, Standard & Poor's generally assesses evidence of product demand and persistence before giving an opinion. The takaful model typically includes a profit-share component to contributors as a necessary component, and to date we view the effectiveness of this client tie-in to future income for relatively new companies as unproven.

As Islamic entities, takaful companies' income streams can be constrained by the application of strict Sharia compliance to the nature of the risks being offered. We understand that in some circumstances, the risks accepted will be broken down into Sharia compliant and noncompliant components, with any profits from the latter being donated to charity, or eliminated in some form.

Management And Strategy

Here we form a view on the skills of the management team in setting an effective operational framework to support the business development. Given the hybrid nature of the (re-)takaful structure, we also seek to understand how the goals of the takaful members, which are generally more focused on risk sharing, align with the goals of the shareholders, whose motives are usually more profit oriented.

Enterprise Risk Management

Enterprise Risk Management (ERM) is an adjunct to Management and Strategy, encompassing an assessment of the risk appetite and control framework of the company. In this regard, Standard & Poor's approach to takaful companies is generally no different than to "conventional" insurance companies.

Earnings

The assessment of the earnings quality for takaful companies can be more complex than for other companies in our view because of the often separate reporting of financial statements for takaful fund members and shareholders. As noted above, the concept behind takaful is mutual risk sharing, or cooperative risk pool participation. The takaful funds, paid for by member contributions bear the losses of the individual member. This, of course, is the original insurance model: the many pay for the losses of the few. At the technical level, therefore, we consider that underwriting earnings may be expected to be more marginal in terms of profit contribution over the long term, as members may expect lower risk pricing on this shared risk basis, or a profit share distribution at some point from any surpluses.

We note that the majority of takaful companies operate the wakala (or agency) model of technical fund management, under which the operational costs are borne by the shareholder, and recovered through a wakala fee levied on the takaful fund. This fee is usually set in advance of the underwriting year, and agreed with the Sharia council, often as a percentage of contributions. In measuring the performance of the takaful underwriting account, Standard & Poor's will generally replace the wakala fee with the actual operational costs borne by the operator. We

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Standard & Poor's Approach To Rating Takaful And Retakaful (Islamic Re/Insurance) Companies (cont.)

believe this gives a more comparable assessment of underwriting performance against conventional insurers, through analysis of the classic technical measures of gross and net combined ratios. A further factor we consider is the relationship between the wakala fee and the operational costs; any margin could, we think, represent a meaningful profit for the shareholder, or subsidy to the takaful fund.

One of the paramount features seen in the takaful model is that any deficit on the takaful fund is solely the responsibility of the members to fund. Nevertheless, under this hybrid structure, the shareholders will usually provide a cost-free loan (qaad hassan) to the fund to finance any shortfall, recoverable from future surpluses. This therefore puts the onus on the operator to price takaful risks correctly to enable the fund to meet claims liabilities. As part of our rating analysis we assess how likely underwriting will be profitable over the long term, so as to provide a flow of funds to finance claims liabilities and growth.

The takaful funds also earn income from the invested assets. However, these invested assets are usually again managed by the operator, who takes a profit share from this activity—the mudharib share.

Typically, the shareholder income statement reflects investment income earned on shareholder assets, the mudharib share and wakala fee from the takaful fund, less any operational costs. In its narrow sense, these items provide return to shareholders. However, Standard & Poor's also includes the surplus (deficit) from the takaful fund, as calculated above, to measure a "conventional equivalent" return on equity.

Investments And Liquidity

Standard & Poor's analysis in these two categories is generally no different for takaful companies than for conventional insurance companies. We form a view on the credit and market risk qualities of the chosen investment portfolio, and the quality of its structure and management. The portfolio structures are likely to be very different for the takaful fund assets and the shareholder funds assets and we assess the strengths and weaknesses of both.

Capitalization

Capital adequacy

Standard & Poor's generally uses its risk-based capital adequacy model to assess the capital quality of the company. The key adaptation is to offset any takaful fund deficit against the shareholders' capital in our analysis, as we understand that the shareholders are obliged to offer support for any such shortfall. Similarly, we will generally include any takaful fund surplus as part of the capital base.

Reinsurance

There are no notable adaptations for this component of our analysis, but we observe that Sharia boards are increasingly expecting takaful companies to seek Islamic reinsurance (retakaful) and availability may become an issue.

Reserving

Again, there are no notable adaptations for this component. Insurance is protection against the unknown, and we therefore look to determine to what extent there exist, in our view, conservative loss assessment processes that bear comparison with peers, and are vetted by independent actuaries, both general and family takaful funds.

Financial Flexibility

Standard & Poor's will also assess to what extent a company's management is able to demonstrate its ability to raise money to support the entity. Shareholder funds are, in our view, the backbone of the business, and we generally assume them to be fully defrayable against any fund deficit, based on the respective qaad hassan loan facility. Typically under this facility, if a deficit on a takaful fund cannot be replenished, then the assets of the shareholders will be called upon to make good any shortfalls.

Related Article On RatingsDirect

Principles Of Corporate And Government Ratings, June 26, 2007.

Abu Dhabi National Insurance Co. (PSC)

PRIMARY CREDIT ANALYST: KEVIN WILLIS, LONDON (44) 20 7176 7085, KEVIN_WILLIS@STANDARDANDPOORS.COM

SECONDARY CREDIT ANALYST: ROWENA POTTER, LONDON (44) 20 7176 7070, ROWENA_POTTER@STANDARDANDPOORS.COM

ISSUER CREDIT RATING: A-/STABLE/--

PUBLICATION DATE: AUGUST 18, 2008

Rationale

The ratings on United Arab Emirates-based insurer Abu Dhabi National Insurance Co. (PSC) (ADNIC) reflect its very strong capitalization, strong earnings, and very strong liquidity. These strengths are in part offset by the very high dependence on reinsurance, both to protect the earnings and to promote the competitive position, and the relative narrowness of the competitive position derived largely within Abu Dhabi.

ADNIC has very strong capitalization and of high quality, driven by extremely strong risk-based capital adequacy per Standard & Poor's Ratings Services' model. Its capital has been grown entirely through internal resources.

ADNIC has sustained a strong level of profitable earnings, with a five-year average combined ratio of 61%, with only moderate volatility around this. Return on equity in 2007 was strong at 17.1% (11.3% excluding realized/unrealized asset gains).

ADNIC has very strong liquidity. Its policy is to maintain bank deposits at a very prudent minimum of 100% of gross technical reserves; at June 2008 this was 102% (111% at December 2007). Further, the key banks used by ADNIC are all strongly rated.

ADNIC has high reinsurance dependence. Its core risks comprise high value assets and it therefore cedes a significant proportion of these, maintaining an average net utilization of almost 70%. However, its key partners are very strongly rated and their presence adds favorably to ADNIC's competitive position.

ADNIC's competitive position is strong. It is the leading insurer in Abu Dhabi and it has excellent access to this emirate's key risks. With Abu Dhabi contributing 61% to total premium, and 39% from northern Emirates, ADNIC's overall position lacks the regional diversity that its peers are now developing. Standard & Poor's believes this to be a key challenge for the company.

Outlook

The outlook is stable. ADNIC will maintain very strong capitalization with strong operating results, delivering a combined ratio better than 75%. Enterprise risk management will take a more important profile and the company will move to more explicitly adopt risk tolerances and appetites, especially within the investment portfolio. ADNIC will reduce its reinsurance dependence, aiming for net retention of 39% overall. Liquidity will remain very strong. Abu Dhabi will continue as the core operational base, but management will look for more regional opportunities, including acquisitions.

Positive rating action will be prompted by greater diversity in competitive position and enhanced implementation of enterprise risk management. Negative rating action could be taken if the competitive position stagnates, or with a significant weakening of earnings and/or capitalization.

Al-Ahleia Insurance Co. S.A.K.

PRIMARY CREDIT ANALYST: KEVIN WILLIS, LONDON (44) 20 7176 7085, KEVIN_WILLIS@STANDARDANDPOORS.COM

SECONDARY CREDIT ANALYST: WOLFGANG RIEF, FRANKFURT (49) 69 33 999 190, WOLFGANG_RIEF@STANDARDANDPOORS.COM

ISSUER CREDIT RATING: BBB+/NEGATIVE/--

PUBLICATION DATE: OCTOBER 9, 2008

Rationale

On Oct. 9, 2008, Standard & Poor's Ratings Services revised its outlook on Kuwait-based composite insurer Al Ahleia Insurance Co. S.A.K. (Al–Ahleia) to negative from stable on investment leverage and asset concentration risk concerns. At the same time, it affirmed the 'BBB+' counterparty credit and insurer financial strength ratings.

The ratings on Kuwaiti life, health, and non-life insurer Al-Ahleia reflect the company's strong operating performance, strong liquidity, and good capitalization. These strengths are partially offset by Al-Ahleia's high investment leverage, which creates some capital strain, and the generic local industry risks of geographical concentration of both underwriting and assets in a single, energy-based economy.

Al-Ahleia's underwriting performance has been consistently strong at both gross and net levels and, aided by a steady investment yield and realized asset gains, has delivered returns on equity (ROE) comfortably in excess of 15%. Standard & Poor's expects future underwriting performance to remain strong, deriving from the commercial accounts focus.

Al-Ahleia's strong liquidity reflects the overall coverage of technical reserves of 6x by readily liquid assets, although much of this surplus is in equities.

Good capitalization is based on Al-Ahleia's quality of capital, good risk-based capital adequacy, satisfactory reserving, and the diversity of the company's reinsurance protections. Capitalization weakened in 2008 because of increased investment concentration in equity markets, in part funded by bank loans, not compensated by the growth in net worth, but we expect this to improve in the near future. Equity investment leverage on June 30, 2008, was very high at 137% (150% in December 2007).

Al-Ahleia's investment portfolio carries a high degree of Kuwaiti asset concentration and particularly market risk. Although the company has a conservative investment philosophy, equity concentrations rose sharply in the first quarter of 2008 and the company is increasingly exposed to equity market volatility.

Outlook

Standard & Poor's has revised the outlook to negative. This reflects uncertainty as to whether Al-Ahleia will reduce the high equity exposure and asset concentrations, which are in part funded by bank loans, in the near future. Al-Ahleia's capital adequacy is currently strained by these holdings and capitalization is no longer the key rating support it was previously. The company's good competitive position in Kuwait will be profitably developed. The underwriting performance will remain strong, with the gross and net combined ratios continuing to be comfortably below 90%. We expect the investment portfolio to remain Kuwaiti-focused and heavily exposed to equities, but single-asset concentrations and leverage will reduce in near future, easing pressure on capitalization.

The rating may be lowered if the high level of equity leverage and asset concentrations are not reduced in the near future. If this uncertainty is dealt with, the outlook may revert to stable.

Al Buhaira National Insurance Co. (PSC)

PRIMARY CREDIT ANALYST: NIGEL BOND, LONDON (44) 20 7176 7063, NIGEL_BOND@STANDARDANDPOORS.COM

SECONDARY CREDIT ANALYST: KEVIN WILLIS, LONDON (44) 20 7176 7085, KEVIN_WILLIS@STANDARDANDPOORS.COM

ISSUER CREDIT RATING: BBB/NEGATIVE/--

PUBLICATION DATE: SEPTEMBER 17, 2008

Rationale

The ratings on United Arab Emirates-based composite insurer Al Buhaira National Insurance Co. (PSC) (ABNIC), the parent company and core operating entity of ABNIC Group, reflect the group's strong operating performance, strong capitalization, and good competitive position. Offsetting factors are its marginal investment profile and lack of clear risk tolerances, particularly in its investment risk management.

Over the past seven years, ABNIC Group has consistently delivered an extremely strong underwriting performance, with a net combined ratio of 61% or less each year. However, this is partly because of the significant commission it receives from reinsurers. Moreover, the net loss ratio has been deteriorating steadily and was very high in 2007, although it had noticeably improved in the first half of 2008. Due to its high-risk investment portfolio, the group's investment performance, and therefore its overall operating performance, has been volatile and we expect it to remain so.

ABNIC Group's strong capitalization is based on its extremely strong capital adequacy and adequate reserves, offset by its high use of reinsurance (60% in 2007), high investment leverage (118% on June 30, 2008), and increased debt leverage (34% on June 30, 2008) that is largely composed of bank overdrafts.

ABNIC Group has built up its business by offering a wide range of products and a high level of service across multiple distribution channels throughout the United Arab Emirates (UAE). The group's competitive position is strong in its core domestic market of Sharjah, where it is one of only two "national" insurers. Elsewhere in the UAE, however, its competitive position is not as strong because it does not have "national" insurer status outside Sharjah. This restricts its access to some business, particularly in Abu Dhabi.

ABNIC Group has a consistently high exposure to property and equities, which accounted for 51% and 25% of investments (including affiliates), respectively, at June 30, 2008. Moreover, its head office alone accounted for 17% of investments, a significant concentration risk. Partially mitigating this high-risk investment profile, however, is the group's extremely strong capital adequacy and, to a lesser extent, its good liquidity.

The lack of clear risk tolerances, particularly in ABNIC Group's investment risk management, is a weakness. This is, however, partially relieved by the sustained strength of the group's capital and the relative stability of its underwriting performance. Moreover, many other aspects of its risk management, such as its underwriting risk controls, are considered adequate.

Outlook

The negative outlook reflects Standard & Poor's Ratings Services increased concern about ABNIC Group's debt leverage and the short-term nature of its borrowing. The ratings may be lowered, therefore, if the debt leverage exceeds 45%. A stable outlook is possible if the debt leverage stabilizes or the short-term nature of the borrowing is significantly reduced.

Standard & Poor's expects ABNIC Group's capital adequacy to remain at least strong. We also expect its growth will all be organic and within the UAE, and its investment portfolio will remain heavily exposed to property and equities. We expect ABNIC Group to enhance its enterprise risk management, especially its risk tolerance, but the scope and speed of this enhancement is uncertain.

Arab Investment and Export Credit Guarantee Corporation (The)

PRIMARY CREDIT ANALYST: KEVIN WILLIS, LONDON (44) 20 7176 7085, KEVIN_WILLIS@STANDARDANDPOORS.COM

SECONDARY CREDIT ANALYST: REMY SALTERS, LONDON (44) 20 7176 7113, REMY_SALTERS@STANDARDANDPOORS.COM

ISSUER CREDIT RATING: AA-/STABLE/--

PUBLICATION DATE: APRIL 20, 2009

Rationale

The ratings on Kuwait-based The Arab Investment and Export Credit Guarantee Corporation (Dhaman) reflect its very strong capitalization, strong financial flexibility derived from its status as a supranational entity, and strong liquidity. A constraint on the ratings is the undeveloped nature of the credit insurance market in the region. Dhaman's key objective is to promote both the flow of Arab investments among member countries and Arab exports worldwide.

As is typical of highly rated supranationals, Dhaman is very strongly capitalized, with very high quality of capital, and no debt finance. Current capital adequacy is extremely strong, with net worth on Dec. 31, 2008 equivalent to 29% of total annual gross insured exposure. We expect capitalization to remain very strong, although it will weaken over time as transaction volume grows.

Dhaman has strong financial flexibility, reflecting its supranational status. The ultimate beneficiaries of its core business activities of political (investment) risk insurance and export credit guarantees are its member government states. Sovereign ratings on the six Gulf Cooperation Council (GCC) countries range from A/Stable/-- to AA-/Stable/--. These countries held 22% of the company's shares directly, and sovereign-owned pan-Arab funds held 53% at year-end 2008. Standard & Poor's Ratings Services expects Dhaman's members to respond to future capital and liquidity needs. Dhaman's ability to demonstrate favorable creditor status in its shareholder relationships helps it recover claims from some of its less creditworthy clients and member states.

At year-end 2008, available liquid assets covered almost 68% of gross outstanding insured exposures (90% in 2007), which is an extremely strong level of cover. This will continue to decline as business volume increases, but will remain strong.

The rating is, to some extent, constrained by the immaturity of Arab region trade markets for the company's services as a political and export credit risk insurer. The potential for adverse economic conditions in some of the target (shareholder) markets is balanced by the structures within Dhaman's convention that provide supranational support and loss recovery.

Outlook

The stable outlook reflects Standard & Poor's expectation that Dhaman will continue to be very strongly capitalized as business volume increases, meeting its primary goal of servicing Arab regional economic growth. It will continue to benefit from shareholder support. Although not a key factor in the rating, the company will use its adequate profitability to support its expansion. Liquidity will continue to be strong and will be reinforced in 2009 by the receipt of outstanding moneys from member countries, but we expect liquidity strength will diminish in the medium to long term as transaction volume rises.

Negative rating action could follow any wavering of shareholder support, or ability, to provide financial flexibility resulting in material weakening of capital adequacy or liquidity. Positive rating action is unlikely in the medium term.

Arab Orient Insurance Co. (PSC)

PRIMARY CREDIT ANALYST: KEVIN WILLIS, LONDON (44) 20 7176 7085, KEVIN_WILLIS@STANDARDANDPOORS.COM

SECONDARY CREDIT ANALYST: NIGEL BOND, LONDON (44) 20 7176 7063, NIGEL_BOND@STANDARDANDPOORS.COM

ISSUER CREDIT RATING: A/WATCH NEG/--

PUBLICATION DATE: MAY 13, 2009

Rationale

On May 13, 2009, Standard & Poor's Ratings Services placed its 'A' long-term counterparty credit and insurer financial strength ratings on Dubai-based non-life insurer Arab Orient Insurance Co. (PSC) on CreditWatch with negative implications.

The CreditWatch placement reflects our concerns that Arab Orient's parent, the Al-Futtaim Group (not rated), is heavily exposed to the deteriorating operating environment in Dubai.

Similar concerns have led to Standard & Poor's taking negative rating actions recently on various corporates (see "Ratings On Dubai Government-Related Entities Put On Creditwatch Negative On Uncertainty Over Support," published April 30, 2009, on RatingsDirect) and banks ("Four Dubai-Based Banks Long-Term Ratings Placed On CreditWatch Negative On Deteriorating Operating Environment," published March 17, 2009).

The ratings on Arab Orient reflect the company's strong capitalization and consistently very strong and stable earnings, accompanied by prudential asset management with very strong liquidity. Management is a positive rating factor through its prudential risk discipline. These factors are partially offset by Arab Orient's high use of reinsurance and the concentration risk from banking counterparties.

CreditWatch

In our view, it is likely that the resolution of the CreditWatch placements on the corporates and banks mentioned above will heavily influence the resolution of the CreditWatch on Arab Orient. Resolution is therefore expected within the next 90 days, and may result in a downgrade of one notch, at the most.

Bahrain Kuwait Insurance Co. BSC

PRIMARY CREDIT ANALYST: ALI KARAKUYU, LONDON (44) 20 7176 7301, ALI_KARAKUYU@STANDARDANDPOORS.COM

SECONDARY CREDIT ANALYST: NIGEL BOND, LONDON (44) 20 7176 7063, NIGEL_BOND@STANDARDANDPOORS.COM

ISSUER CREDIT RATING: BBB/STABLE/--

PUBLICATION DATE: MARCH 31, 2009.

Rationale

On March 31, 2009, Standard & Poor's Ratings Services revised to stable from positive its outlook on Kuwait-based non-life insurer Gulf Insurance Co. K.S.C. (Gulf Insurance), the parent company and a core operating entity of the composite insurer, Gulf Insurance Group (the group). At the same time, the 'BBB+' long-term counterparty credit and insurer financial strength ratings were affirmed.

The outlook revision reflects the group's inability to meet our expectations about capital adequacy and enterprise risk management (ERM) in order to warrant a higher rating.

The ratings reflect our assessment of the group's 'strong' (all terms in single quotes are defined in "Interpreting Insurer Financial Strength Ratings In Light Of Improving Insurer Supervision," published on March 20, 2009, on RatingsDirect) operating performance and 'strong' competitive position. These positive factors are offset by our assessment of Gulf Insurance Group's 'weak', but improving, ERM, and its investment risk profile, which in our view is very high and leads to volatile capital adequacy. Moreover, capital adequacy as measured by our capital adequacy model, is in our view currently barely 'good' and therefore inconsistent with the rating.

Operating performance is underpinned by an underwriting performance that should, in our opinion, remain consistently 'strong', as the focus on profitability offsets an expected slight deterioration as the mix of business moves increasingly toward personal lines and as competition increases.

Gulf Insurance Group is in our opinion a leading life and non-life insurer in its core market of Kuwait through broad product offerings and good service and distribution. It also benefits from its status as a national insurer. Despite increasing competition within Kuwait, we expect the group to maintain its leading domestic competitive position. Furthermore, it is already a leading exponent of regional expansion and, over time, Standard & Poor's expects it to derive a greater proportion of its premiums and profits from life business, personal business, and beyond Kuwait, as it reaps the benefits of targeted diversification.

Guided by Ernst & Young, Gulf Insurance Group is working toward developing an effective ERM framework. Importantly, the group is close to finalizing its risk appetite, which Standard & Poor's expects to be used to manage risk more effectively. Nevertheless, we believe the major improvements to Gulf Insurance Group's ERM will take time to introduce and implement. A positive assessment by Standard & Poor's of their impact on the risk profile of the group is important if the ratings were to be raised in the future.

Gulf Insurance Group's investment portfolio is heavily exposed to equities, particularly domestic equities, which we believe causes the group's capital adequacy to be volatile. Capital adequacy has weakened over the past few months as the regional stock markets have fallen, and as measured by our capital adequacy model, is currently barely 'good' and therefore inconsistent with the rating.

Outlook

The ratings on Gulf Insurance are significantly influenced by, but not directly linked to, the ratings on Kuwait Projects Co. (Holding) K.S.C. (BBB+/Stable/A-2), the ultimate parent. Subject to this, the stable outlook reflects Standard & Poor's current expectation that Gulf Insurance Group will continue to improve its ERM, that its capital adequacy, although it will remain volatile, will not deteriorate significantly, and that its net combined ratio in 2009 will be less than 95%.

Given the historical volatility of the investment performance and capital adequacy of the group, it is unlikely that the ratings will be raised unless Gulf Insurance Group successfully introduces clear risk tolerances, especially for asset risks, and Standard & Poor's positively assesses the impact of these on the risk profile of the group. Failure to meet the above expectations could lead to negative rating action.

Bahrain National Insurance Co. BSC

PRIMARY CREDIT ANALYST: ALI KARAKUYU, LONDON (44) 20 7176 7301, ALI_KARAKUYU@STANDARDANDPOORS.COM

SECONDARY CREDIT ANALYST: NIGEL BOND, LONDON (44) 20 7176 7063, NIGEL_BOND@STANDARDANDPOORS.COM

ISSUER CREDIT RATING: BBB+/STABLE/--

PUBLICATION DATE: AUGUST 26, 2008

Rationale

The ratings on Bahrain-based insurer Bahrain National Insurance Co. BSC (BNI) reflect the company's strong operating performance, strong capitalization, and strong investments. These positive factors are partially offset, however, by the company's competitive position, which is restricted to the small Bahraini market, as well as by its significant dependence on reinsurance protection when assuming large risks.

Operating performance is a key strength for the ratings, based on a strong underwriting and investment performance. In 2007 BNI's net combined ratio increased, albeit to a still strong level, to 82% (compared to 66.0% in 2006 which benefited from reserve releases) leading to a net profit of Bahrain dinar (BHD) 3.9 million (BHD4.2 million in 2006). For the half year ended June 30, 2008, Bahrain National Holding Co. BSC (BNHC), BNI's parent company reported a net profit of BHD2.3 million and a strong combined ratio of about 76% at June 2008.

BNI's capitalization is strong, underpinned by a strong level of risk-based capital adequacy and prudent reserving. Nevertheless, Standard & Poor's Ratings Services views the absolute size of shareholders' funds as small at BHD24.4 million in 2007. By ceding 57% of its gross premium to reinsurers, BNI does display a significant degree of dependency on the quality of its reinsurance. However, this level of reinsurance is considered appropriate and is required in view of the small absolute size of shareholders' funds in relation to the commercial risks the company is assuming.

BNI has strong investments and liquidity. It has consistently maintained a very liquid investment portfolio, a high but controlled exposure to equities, and relatively low credit, and an acceptable level of market risk; although the increased exposure to the associated companies exerts pressure on both the quality of investments and the liquidity of the company.

BNI is the market leader in the Kingdom of Bahrain (A/Stable/A-1) with a large market share of about 20%. Nevertheless, BNI's position is restricted to this relatively small market. BNI may be challenged in the medium term as competition increases with the entry of new companies. The company intends to expand its insurance operations regionally in the Gulf markets, but this expansion is unlikely to be material in the medium term. While BNHC's investments in noninsurance operations in the region aids diversification, it does involve some execution risk.

Outlook

The stable outlook reflects Standard & Poor's expectation that BNI will maintain its operating performance and capitalization at a strong level. BNI is expected to maintain its market position without materially compromising on profitability.

A positive rating action is dependent on successful business diversification outside the Bahraini market. The ratings may come under pressure in the event of a failure to meet performance expectations and/or a weakening of the company's capital adequacy to a level below its current ratings.

Doha Insurance Co. Q.S.C.

PRIMARY CREDIT ANALYST: NEIL GOSRANI, LONDON (44) 020 7176 7112, NEIL_GOSRANI@STANDARDANDPOORS.COM

SECONDARY CREDIT ANALYST: DAVID ANTHONY, LONDON (44) 20 7176 7010, DAVID_ANTHONY@STANDARDANDPOORS.COM

ISSUER CREDIT RATING: BBB/STABLE/--

PUBLICATION DATE: JUNE 27, 2008

Rationale

The ratings on Qatar-based Doha Insurance Co. Q.S.C. (Doha) reflect its strong capitalization, strong financial flexibility, good and improving operating performance, and good and improving competitive position. Factors partially offsetting this are a high concentration of investments in the domestic market, particularly property, high dependence on reinsurance, and the limited development of risk management practices in line with growth and expansion.

Standard & Poor's Ratings Services considers Doha's capitalization as strong, supported by extremely strong capital adequacy and prudent reserving. It was further enhanced by a successful rights issue, which closed on May 8, 2008, and raised about Qatari riyal (QAR) 132 million.

Financial flexibility is strong relative to likely prospective needs. Although we expect internal capital generation to be the focus in coming years, the company's listing on the Doha Securities Market, together with low financial leverage, will enable Doha to access capital markets and bank funding in case of need.

Operating performance is good and improving. Doha's net combined ratio hit a five-year low of 63%, while return on revenue (ROR) and return on equity (ROE) hit five-year highs of 37% and 29%, respectively. Business growth is strong, but appears to be stabilizing, with annual change in gross premiums written (GPW) of 25% the lowest in four years.

Competitive position is good and improving, supported by a focus on profitable commercial lines and client relationship management as well as forthcoming diversification and increased capacity through entering agreements with regional insurers. Doha's retail business is centered on developing health and takaful lines where it retains a greater portion of risk and maintains greater control over risk pricing. This also applies to motor, although Doha has sought to limit its exposure to this segment. Doha's competitive position is constrained by its reliance on the increasingly competitive Qatari insurance market and concentrated exposure to aviation risks.

Doha's investment portfolio continues to produce acceptable total investment returns (8.1% in 2007), but is a relative ratings weakness due to its concentrations in domestic securities and commercial property, in particular through the development of property at Energy City and equities on the Doha Securities Market (DSM), which are potentially subject to high volatility. Concentration risk is partially offset by Doha's strong capitalization and Standard & Poor's expects the portfolio to benefit from a greater geographical spread of assets over the short term.

The nature of Doha's risk base and the international insurance market create a very highly leveraged reinsurance program, with Doha having ceded 74% of GPW in 2007 (73% in 2006). This is mitigated by a well-diversified and highly rated reinsurance panel and by the fact that Doha fully retains most of its smaller risks.

Risk management is adequate for Doha's size and current risk profile with risks being measured on a discreet basis. This is expected to come under pressure as the company grows and diversifies and the need for a holistic view of risks faced by the company gains greater weight.

Outlook

The stable outlook on Doha reflects Standard & Poor's expectation that Doha will continue to strengthen its competitive position based on its commercial specialism and controlled retail diversification. We expect to see continued strength in operating performance with per annual GPW growth averaging 15% over the next three years combined with stable underwriting performance. We expect capitalization and financial flexibility to remain strong beyond the ratings horizon. Standard & Poor's also expects support from reinsurers to remain unchanged. We also expect risk management practices to evolve with the growth of the company. Positive ratings momentum may emerge with greater balance in Doha's investment portfolio and the continuation of current positive operating trends. Adverse ratings momentum is considered unlikely, but may result from execution risk arising from property development.

Dubai Islamic Insurance & Reinsurance Co. (Aman)

PRIMARY CREDIT ANALYST: LOTFI ELBARHDADI, PARIS (33) 1 4420 6730, LOTFI_ELBARHDADI@STANDARDANDPOORS.COM

SECONDARY CREDIT ANALYST: DAVID ANTHONY, LONDON (44) 20 7176 7010, DAVID_ANTHONY@STANDARDANDPOORS.COM

ISSUER CREDIT RATING: BBB/NEGATIVE/--

PUBLICATION DATE: MARCH 9, 2009

Rationale

On March 9, 2009, Standard & Poor's Ratings Services revised its outlook on Dubai-based insurer Dubai Islamic Insurance & Reinsurance Co. (Aman) to negative from stable. At the same time, we affirmed the 'BBB' long-term counterparty credit and insurer financial strength ratings on Aman.

The outlook revision reflects the increasing pressure on Aman's risk-adjusted capital adequacy, arising mainly from the continuing decline in investment markets in the Gulf region. Aman's investment strategy exacerbated this pressure, as the company concentrated its investments in the Dubai equity markets, particularly in stocks of financial institutions and real estate operators, which suffered sharp declines over the past four months. Moreover, Aman's gross premium income grew more than we had expected, by a substantial 66% (55% net of reinsurance). This has put further pressure on capital adequacy, as capital requirements have risen due to higher underwriting exposure, while adjusted capital has fallen. Meanwhile Aman has mitigated the capital needed to support its growing underwriting exposure by conservatively using reinsurance protection.

Positive rating factors include Aman's good competitive position, good technical earnings, and good financial flexibility. Based on the company's preliminary results for 2008, Aman continues to deliver sound growth and business diversification, and its underwriting results appear to have improved compared with those of the past two years, evidencing good quality underwriting. We still consider Aman's ability to access capital sources as good, due to its large retail shareholder base and the presence of supportive individual and institutional investors within the core shareholder base.

Outlook

The negative outlook reflects our opinion that Aman may not restore its capital adequacy to levels supportive of a 'BBB' rating during 2009 and 2010, owing to investment market uncertainties. We expect Aman to maintain its good underwriting earnings.

We expect Aman to grow at least 25% in 2009, on a gross and net of reinsurance basis. We expect Aman's dividend and capital policy to help the company restore its good capitalization, particularly taking into account its growth and its investment risks.

We expect Aman to maintain a net combined ratio that is less than 95% 2009, reflecting prudent pricing and underwriting.

We expect Aman to continue to dilute the sector and single-name concentrations of its investments, as the size of its investments grows, to mitigate the volatility of its earnings and capitalization. We do not expect Aman to realize the substantial unrealized investment losses recorded at year-end 2008, because of its low needs to sell assets to pay its obligations. We expect reorientation of premium inflows toward less risky assets during 2009 to alleviate earnings volatility.

We could lower the ratings if capitalization does not recover during the next two years, if operating performance worsens, or if the company experiences long-term asset write-downs or losses. We could revise the outlook to stable during the same period if the company successfully restores its capital adequacy to good levels, while maintaining its good underwriting performance and prudent business mix.

Emirates Insurance Co. (PSC)

PRIMARY CREDIT ANALYST: KEVIN WILLIS, LONDON (44) 20 7176 7085, KEVIN_WILLIS@STANDARDANDPOORS.COM

SECONDARY CREDIT ANALYST: ROWENA POTTER, LONDON (44) 20 7176 7070, ROWENA_POTTER@STANDARDANDPOORS.COM

ISSUER CREDIT RATING: BBB+/NEGATIVE/--

PUBLICATION DATE: MARCH 4, 2009

Rationale

On March 4, 2009, Standard & Poor's Ratings Services revised its outlook on Abu Dhabi-based Emirates Insurance Co. (PSC) (EIC) to negative from stable in response to the heavy decline in the company's capital adequacy at Dec. 31, 2008, and the heightened volatility in the value of its investment portfolio, which may have a further negative impact on its capital adequacy. At the same time, the 'BBB+' long-term counterparty credit and insurer financial strength ratings were affirmed.

On Feb. 23, 2009, EIC announced a 42.6% fall in its shareholder funds as at Dec. 31, 2008, compared with Dec. 31, 2007. This material movement reflects a reduction of 87% in investment revaluation reserves to United Arab Emirates dirham (AED) 92.9 million at the end of 2008, from AED714.5 million at the end of 2007. Nevertheless, despite this material weakening of capital adequacy, Standard & Poor's continues to assess EIC's capitalization as in line with the rating.

The ratings on EIC reflect its strong technical earnings. In 2008, excluding asset value movements, EIC again showed a strong underwriting performance, with a net combined ratio of 78% compared with 64% in 2007. This deterioration reflects a decline in commission receipts following lower reinsurance utilization.

Also, the strength of liquidity has been maintained. Bank deposits and cash at December 2008 represent 99% of total net technical reserves, and if tradable investments (mostly equities) are included, technical reserve liquidity remains strong.

Reinsurance dependence, although still high, reduced in 2008, with utilization falling in 2008 to 67% from 71% in 2007.

Outlook

The negative outlook reflects our opinion that the ratings will be lowered if capital adequacy continues to decline materially in the currently volatile investment market. The outlook could revert to stable if EIC can show that its capital adequacy has been restored to a rating strength. Positive rating action may be taken if the investment portfolio is actively de-risked, capitalization sustained at a strong level, and earnings maintain their strength.

Gulf Insurance Co. K.S.C.

PRIMARY CREDIT ANALYST: NIGEL BOND, LONDON (44) 20 7176 7063, NIGEL_BOND@STANDARDANDPOORS.COM

SECONDARY CREDIT ANALYST: KEVIN WILLIS, LONDON (44) 20 7176 7085, KEVIN_WILLIS@STANDARDANDPOORS.COM

ISSUER CREDIT RATING: BBB+/STABLE/--

PUBLICATION DATE: MARCH 31, 2009

Rationale

On March 31, 2009, Standard & Poor's Ratings Services revised to stable from positive its outlook on Kuwait-based non-life insurer Gulf Insurance Co. K.S.C. (Gulf Insurance), the parent company and a core operating entity of the composite insurer, Gulf Insurance Group (the group). At the same time, the 'BBB+' long-term counterparty credit and insurer financial strength ratings were affirmed.

The outlook revision reflects the group's inability to meet our expectations about capital adequacy and enterprise risk management (ERM) in order to warrant a higher rating.

The ratings reflect our assessment of the group's 'strong' (all terms in single quotes are defined in "Interpreting Insurer Financial Strength Ratings In Light Of Improving Insurer Supervision," published on March 20, 2009, on RatingsDirect) operating performance and 'strong' competitive position. These positive factors are offset by our assessment of Gulf Insurance Group's 'weak', but improving, ERM, and its investment risk profile, which in our view is very high and leads to volatile capital adequacy. Moreover, capital adequacy as measured by our capital adequacy model, is in our view currently barely 'good' and therefore inconsistent with the rating.

Operating performance is underpinned by an underwriting performance that should, in our opinion, remain consistently 'strong', as the focus on profitability offsets an expected slight deterioration as the mix of business moves increasingly toward personal lines and as competition increases.

Gulf Insurance Group is in our opinion a leading life and non-life insurer in its core market of Kuwait through broad product offerings and good service and distribution. It also benefits from its status as a national insurer. Despite increasing competition within Kuwait, we expect the group to maintain its leading domestic competitive position. Furthermore, it is already a leading exponent of regional expansion and, over time, Standard & Poor's expects it to derive a greater proportion of its premiums and profits from life business, personal business, and beyond Kuwait, as it reaps the benefits of targeted diversification.

Guided by Ernst & Young, Gulf Insurance Group is working toward developing an effective ERM framework. Importantly, the group is close to finalizing its risk appetite, which Standard & Poor's expects to be used to manage risk more effectively. Nevertheless, we believe the major improvements to Gulf Insurance Group's ERM will take time to introduce and implement. A positive assessment by Standard & Poor's of their impact on the risk profile of the group is important if the ratings were to be raised in the future.

Gulf Insurance Group's investment portfolio is heavily exposed to equities, particularly domestic equities, which we believe causes the group's capital adequacy to be volatile. Capital adequacy has weakened over the past few months as the regional stock markets have fallen, and as measured by our capital adequacy model, is currently barely 'good' and therefore inconsistent with the rating.

Outlook

The ratings on Gulf Insurance are significantly influenced by, but not directly linked to, the ratings on Kuwait Projects Co. (Holding) K.S.C. (BBB+/Stable/A-2), the ultimate parent. Subject to this, the stable outlook reflects Standard & Poor's current expectation that Gulf Insurance Group will continue to improve its ERM, that its capital adequacy, although it will remain volatile, will not deteriorate significantly, and that its net combined ratio in 2009 will be less than 95%.

Given the historical volatility of the investment performance and capital adequacy of the group, it is unlikely that the ratings will be raised unless Gulf Insurance Group successfully introduces clear risk tolerances, especially for asset risks, and Standard & Poor's positively assesses the impact of these on the risk profile of the group. Failure to meet the above expectations could lead to negative rating action.

Hannover ReTakaful B.S.C.

PRIMARY CREDIT ANALYST: NEIL GOSRANI, LONDON (44) 20 7176 7112, NEIL_GOSRANI@STANDARDANDPOORS.COM

SECONDARY CREDIT ANALYST: KEVIN WILLIS, LONDON (44) 20 7176 7085, KEVIN_WILLIS@STANDARDANDPOORS.COM

ISSUER CREDIT RATING: A/STABLE/--

PUBLICATION DATE: DECEMBER 12, 2008

Rationale

The ratings on Bahrain-based retakaful reinsurer Hannover ReTakaful B.S.C reflect its strategic importance to its parent, Hannover Rueckversicherung AG (Hannover Re, or the group; AA-/Stable/--). The ratings also reflect Hannover ReTakaful's conservative investment portfolio and strategy, and strong capitalization, which are partially offset by its modest competitive position in the global reinsurance markets and by start-up strain, which will affect earnings in the short term.

The ratings on Hannover ReTakaful are supported by the ratings on its parent. Standard & Poor's Ratings Services considers Hannover ReTakaful to be strategically important to the Hannover Re group. This support is demonstrated through reinsurance and stop-loss agreements, arranged with the parent. Furthermore, the experienced management team came from within the group.

Hannover ReTakaful's investment policies and procedures are viewed as strong, with clear guidelines in place to comply with both internal and Sharia requirements. The key objective of the investment policy is preservation of capital, with a steady, calculable return.

Capitalization is strong based on extremely strong capital adequacy, adequate reserving practices, and the existence of a group-supported retrocession program. We expect capitalization to at least remain in line with the rating for the medium term.

Hannover ReTakaful's competitive position is modest in the context of the global reinsurance markets. This is reflective of its start-up status and the underdeveloped nature of the retakaful segment of reinsurance. These weaknesses are offset by Hannover ReTakaful's ability to leverage the group's expertise within the reinsurance markets, brand, established relationships, and financial strength and capacity. Within the underdeveloped retakaful markets, Hannover ReTakaful has a good presence.

Hannover ReTakaful remains at an early stage in its development and operates in a highly underdeveloped market. The company has revised its initially bullish view on premium growth and reflects the requirement for operators to gain widespread acceptance in the market by developing full and comparable product offerings across business lines. In 2007, the company reported gross written premiums (GWP) of $15.2 million and a net loss ratio of 76%. Hannover ReTakaful's long-term prospects, therefore, are dependent on market development and the acceptance of the retakaful concept.

Outlook

The stable outlook on Hannover ReTakaful reflects our expectation that the company will continue to be supported by Hannover Re group both implicitly and explicitly. Competitive position is expected to improve with Hannover ReTakaful's growing presence in the retakaful markets. We expect Hannover ReTakaful's competitive strengths to translate to strong business growth. Its target of $70 million in GWP by 2011 is viewed as reasonable given the expected growth in takaful and therefore retakaful markets in the Gulf region. Technical performance is expected to reflect conservative reserving and a stabilization in expenses, leading to a gradual fall in the combined ratio from its current peak of 136%, reflecting start-up costs and a large proportion of incurred but not reported claims. We expect capitalization to at least remain in line with the rating for the medium term.

Kuwait Reinsurance Co. K.S.C.

PRIMARY CREDIT ANALYST: MATTHEW DAY, LONDON (44) 20 7176 7044, MATTHEW_DAY@STANDARDANDPOORS.COM

SECONDARY CREDIT ANALYST: NIGEL BOND, LONDON (44) 20 7176 7063, NIGEL_BOND@STANDARDANDPOORS.COM

ISSUER CREDIT RATING: BBB/POSITIVE/--

PUBLICATION DATE: SEPTEMBER 22, 2008

Rationale

The ratings on Kuwait Reinsurance Co. K.S.C. (Kuwait Re) reflect its very strong capitalization, enhanced risk management and strategy, and strong investments, partially offset by its marginal underwriting performance and an adequate, if constrained, competitive position. Kuwait Re is essentially a non-life reinsurer, with gross premiums written of about $39.8 million in 2007.

Standard & Poor's Ratings Services views Kuwait Re's capitalization as very strong. We base this view on the company's excellent capital adequacy, very good capital quality, continued prudent reserving, and appropriate use of retrocession.

Kuwait Re has strong investments and liquidity. It has consistently maintained a very liquid investment portfolio, a reasonably high but controlled exposure to equities, and relatively low credit and market risk. However, the increased exposure to the Kuwaiti property market exerts pressure on both the quality of investments and the company's liquidity profile.

Kuwait Re's operating performance remains marginal, although we have seen improvements, and the continuation of these will be key to the rating on Kuwait Re. The operating performance improvements are due to the increasing scale and improved expense management. Furthermore, its relatively large investment portfolio has enabled it to report a net profit since at least 2001. We expect Kuwait Re's underwriting performance to continue to improve, achieving a combined ratio of below 100% in 2008.

Kuwait Re has an adequate regional competitive position. It is positioned as a small regional reinsurer with no significant pricing power. It does, however, have the benefit of having Transatlantic Reinsurance Co. (Transatlantic Re; AA-/Negative/--) as its major shareholder and a business partner. Kuwait Re and Transatlantic Re are working together to expand into new geographic areas and diversify risk acceptance, thereby improving Kuwait Re's competitive position, which to date has been dependent on long-standing business relationships.

Outlook

The positive outlook reflects our expectation that the company's improved underwriting performance will be maintained at sub-100% combined ratio levels.

Kuwait Re has taken an increasingly technical approach to its underwriting, driven by the recent management changes. The increasingly technical approach supports our positive outlook on this company.

Capitalization should remain at least strong, driven principally by an excellent (although falling) capital surplus at the 'AAA' level. Investments and liquidity are also expected to remain strong.

If Kuwait Re achieves its targets and establishes a track record of underwriting profitability across the rating horizon, then the ratings could be raised. Failure to successfully improve underwriting profitability, or a negative shift in the competitive environment for Kuwait Re would put downward pressure on the ratings.

National General Insurance Co. (PSC)

PRIMARY CREDIT ANALYST: WOLFGANG RIEF, FRANKFURT (49) 69 33 999 190, WOLFGANG_RIEF@STANDARDANDPOORS.COM

SECONDARY CREDIT ANALYST: KEVIN WILLIS, LONDON (44) 20 7176 7085, KEVIN_WILLIS@STANDARDANDPOORS.COM

ISSUER CREDIT RATING: BBB/STABLE/--

PUBLICATION DATE: JANUARY 30, 2009

Rationale

The ratings on Dubai-based insurer National General Insurance Co. (PSC) (NGI) reflect the company's strong capitalization and strong underwriting and earnings track record. These strengths are partly offset by NGI's medium size in the United Arab Emirates' (UAE) insurance market and by investment concentration risks in the currently very volatile local market.

Standard & Poor's Ratings Services still considers NGI's capitalization to be strong, although it has weakened somewhat because, in line with the market, the company is under pressure from the current financial and economic market dislocations. Excellent quality of capital and prudent reserving support NGI's capitalization. The key risks to capital arise from the locally concentrated investment portfolio and NGI's quite high dependence on reinsurance, although the latter is mitigated by sound and diversified reinsurance protection. NGI has a strong underwriting and earnings track record, having reported strong underwriting profits at both gross and net levels for many years. For the first nine months of 2008, net premiums increased by 30% and the underwriting result by 31%, indicating the continuation of stable underwriting results. Net income, however, decreased by 8%, owing to unrealized losses that were only partly offset by fair-value gains on investment properties.

NGI is a midsize player in the rapidly expanding, but very competitive, UAE insurance market. It benefits from its favored status as insurance provider to its key shareholder group clients, in particular, Emirates Bank International PJSC (A/Negative/A-1) and its related group companies (collectively, the Emirates Banking Group; EBG), as well as the National Bank of Dubai (NBD; A/Negative/A-1), which merged with EBG in 2008 to form Emirates NBD. In addition, the company is working with experienced and successful international insurers and reinsurers to develop and distribute new business lines.

NGI's investment policy focuses strongly on local markets, and although historically this has delivered a high return relative to cost, there is material exposure to the highly volatile UAE equity and real estate markets, which reflects the impact of the difficult global macroeconomic and financing environment on the Emirate of Dubai.

Outlook

The stable outlook reflects our expectation that NGI will maintain capitalization that is strong enough to support the company's anticipated rapid future growth.

Standard & Poor's expects NGI to enhance its competitive position within the Dubai insurance market by developing its relationship with EBG and NBD. Growth should at least keep pace with the market as distribution and product capabilities expand. We expect any deterioration in NGI's underwriting performance to be minimal and the net combined ratio to be lower than 80% for 2008 and in 2009. We expect the shareholders' return to be depressed in the short term because of the poor investment markets. The company's assets are likely to continue to reflect good liquidity and provide good coverage for technical and other liabilities.

Positive ratings momentum may emerge if further benefits from NGI's strategic partnership with Aviva PLC (core operating entities rated AA-/Stable/--) become more visible and its risk-management capabilities continue to improve, owing to closer cooperation with EBG. We consider adverse ratings momentum unlikely, but it could be prompted by deterioration of earnings or capitalization.

Oman Insurance Co. (PSC)

PRIMARY CREDIT ANALYST: NIGEL BOND, LONDON (44) 20 7176 7063, NIGEL_BOND@STANDARDANDPOORS.COM

SECONDARY CREDIT ANALYST: KEVIN WILLIS, LONDON (44) 20 7176 7085, KEVIN_WILLIS@STANDARDANDPOORS.COM

ISSUER CREDIT RATING: A-/WATCH NEG/--

PUBLICATION DATE: MARCH 18, 2009

Rationale

On March 18, 2009, Standard & Poor's Ratings Services placed its 'A-' long-term counterparty credit and insurer financial strength ratings on United Arab Emirates (UAE)-based composite insurer Oman Insurance Co. (PSC) on CreditWatch with negative implications. The CreditWatch placement follows the placement of the long-term counterparty credit rating on Oman Insurance's parent, UAE-based Mashreqbank (A/Watch Neg/A-1), on CreditWatch with negative implications on March 17, 2009 (see "Four Dubai-Based Banks Long-Term Ratings Placed On Creditwatch Negative On Deteriorating Operating Environment"). Under our criteria, the rating action on Oman Insurance should have occurred simultaneously with that on Mashreqbank and this article both notes that fact and places Oman Insurance at the appropriate rating.

CreditWatch

We expect to resolve the CreditWatch status in the coming six weeks. We do not anticipate to lower the ratings on Mashreqbank by more than one notch, based on our current expectations. As a strategically important subsidiary of Mashreqbank, the ratings on Oman Insurance benefit from group support and we therefore do not expect to lower them by more than one notch.

Oman United Insurance Co. S.A.O.G.

PRIMARY CREDIT ANALYST: KEVIN WILLIS, LONDON (44) 20 7176 7085, KEVIN_WILLIS@STANDARDANDPOORS.COM

SECONDARY CREDIT ANALYST: DAVID ANTHONY, LONDON (44) 20 7176 7010, DAVID_ANTHONY@STANDARDANDPOORS.COM

ISSUER CREDIT RATING: BBB/STABLE/--

PUBLICATION DATE: MAY 30, 2008

Rationale

The ratings on Oman-based insurer Oman United Insurance Co. S.A.O.G. (OUIC) reflect the company's strong earnings, very good capitalization, and good competitive position in the Omani market. These factors are partially offset by OUIC's highly concentrated investment portfolio, as well as the moderately high economic and industry risk in the small and concentrated Omani economy.

Standard & Poor's Ratings Services still considers operating performance fundamentally strong and a support for the rating, despite significant losses from Cyclone Gonu in 2007, which pushed the net combined ratio up to 134% from 91% in 2006. Unrealized gains contributed to a strong return on equity (ROE) of 23.4% but excluding these, ROE fell to 1.3%. The five-year average is strong at 21%.

We view capitalization as very good. Reserving is prudent, and because OUIC's risk portfolio focuses on personal/retail lines, its dependence on reinsurance is moderate and below that of most Gulf Cooperation Council (GCC) peers.

Standard & Poor's considers OUIC's competitive position good and improving as a result of initiatives the company is taking. The company's business profile is weighted toward the personal lines market, which has less strong earnings potential, but a likelihood of greater stability. OUIC plans to gradually strengthen its position in commercial lines and is taking steps in 2008 to extend its market presence across Oman.

Economic and industry risk in Oman is viewed as moderately high, and to some extent affects our view of OUIC's competitive position and capitalization. Omani regulators have allowed four new "national" insurance companies to be created since 2004. New entrants have introduced additional capacity to the market and have substantially increased price competition for local risks.

In line with Omani regulation, OUIC's investment portfolio is concentrated on the Omani economy. Additionally, OUIC's investment portfolio contains high levels of concentration on individual issuers. This may expose the company to operational volatility, and we therefore view it as a relative rating weakness.

Outlook

The stable outlook on OUIC reflects our expectation that the company will retain its competitive standing in the Omani market. Personal lines (in particular, motor and individual life cover) and small commercial business (loan protection) will benefit from OUIC's cooperation agreement with local finance companies. Growth above the market average will emanate from new distribution initiatives. We expect capitalization to remain very good. We also expect OUIC to generate attractive earnings, broadly in line with the levels achieved before Cyclone Gonu. The combined ratio should be below 100%, subject only to further extreme events. Standard & Poor's does not consider recent senior management changes at OUIC to be a negative factor, as long as the company maintains its strategy and current prudent risk appetite.

Positive rating movement will likely be achieved through a strengthening of OUIC's competitive position with new product and distribution initiatives accompanied by stronger earnings. Negative rating action will be prompted by any deterioration in OUIC's competitive position and in its underwriting performance.

Qatar Insurance Co. International LLC

PRIMARY CREDIT ANALYST: NEIL GOSRANI, LONDON (44) 020 7176 7112, NEIL_GOSRANI@STANDARDANDPOORS.COM

SECONDARY CREDIT ANALYST: DAVID ANTHONY, LONDON (44) 20 7176 7010, DAVID_ANTHONY@STANDARDANDPOORS.COM

ISSUER CREDIT RATING: A/STABLE/--

PUBLICATION DATE: DECEMBER 10, 2007

Rationale

On Dec. 10, 2007, Standard & Poor's Ratings Services assigned its 'A' long-term insurer financial strength rating to Qatar Financial Center-based Qatar Insurance Co. International LLC (QIC International). The outlook is stable.

The rating on QICI is based on a guarantee provided by Qatar-based Qatar Insurance Co. S.A.Q. (QIC; A/Stable/--). The guarantee meets our guarantee criteria. Standard & Poor's expects the rating on QIC International to move in lockstep with that on QIC.

QIC International is a subsidiary of QIC. It has been established in the Qatar Financial Center as an operating company for QIC's international branches, subsidiary holdings and inward reinsurance business.

Outlook

The stable outlook on QIC International reflects the stable outlook on its guarantor, QIC.

Qatar Insurance Co. S.A.Q.

PRIMARY CREDIT ANALYST: NEIL GOSRANI, LONDON (44) 020 7176 7112, NEIL_GOSRANI@STANDARDANDPOORS.COM

SECONDARY CREDIT ANALYST: DAVID ANTHONY, LONDON (44) 20 7176 7010, DAVID_ANTHONY@STANDARDANDPOORS.COM

ISSUER CREDIT RATING: A/STABLE/--

PUBLICATION DATE: JULY 21, 2008

Rationale

The ratings for Qatar-based insurer Qatar Insurance Co. SAQ (QIC) reflect the company's extremely strong capital adequacy, strong competitive position, and very strong operating performance. These strengths are partially offset by high, but reducing use of reinsurance; local concentration of the investment portfolio, particularly in equities; and economic and industry risk inherent to the Gulf region.

QIC's capital adequacy is extremely strong, and therefore a key rating strength. Standard & Poor's Ratings Services expects QIC's capital adequacy to remain at least very strong, supported by the continuing strength of retained earnings.

Competitive position is strong as a result of QIC's dominant position domestically. It maintained its market share at 50.6% of the market and also developed its presence regionally and internationally. In addition to expanding geographically, QIC aims to take advantage of changing regulations and increased retail awareness in its domestic market to exploit new opportunities.

Operating performance continues to reflect QIC's domestic strength and geographic diversification. Its operating result increasing by 34% to Qatari riyal (QAR) 483 million in 2007. Underwriting income and investment performance continue to be highly profitable.

Key weaknesses are a high level of reinsurance utilization for certain lines of business and a locally focused investment portfolio. These are somewhat offset by the gradual increase in retentions and steady investment portfolio diversification. In addition, the high level of volatility within the Gulf region presents inherent economic and industry risks.

Outlook

The stable outlook reflects Standard & Poor's expectation that QIC will maintain its strong operating performance, with gross premiums written (GPW) growth of around 20%-25% per year over the medium term, combined with continued diversification of revenues and earnings. We expect technical performance to remain strong, with a three-year average combined ratio of around 70%. We also expect business retention to stabilize around 45%-50%, but it will continue to vary substantially by type of business. Competitive position is likely to be enhanced by introducing new lines of business domestically and the development of QIC's regional and international operations. We expect QIC to continue developing operations in Malta as well as a base in the Far East, and to prepare some of its Gulf Cooperation Council (GCC) branches for an IPO.

A revision of the outlook on QIC to positive may result from strong, successful, and sustainable diversification, better quality and more diversified investments, and a reduction in the economic risks of the region. A revision of the outlook to negative, although unlikely at this stage, may occur if quality of earnings declines, market conditions deteriorate, or financial strength weakens.

Salama/Islamic Arab Insurance Co. (P.S.C.)

PRIMARY CREDIT ANALYST: DAVID ANTHONY, LONDON (44) 20 7176 7010, DAVID_ANTHONY@STANDARDANDPOORS.COM

SECONDARY CREDIT ANALYST: LOTFI ELBARHDADI, PARIS (33) 1 4420 6730, LOTFI_ELBARHDADI@STANDARDANDPOORS.COM

ISSUER CREDIT RATING: BBB+/STABLE/--

PUBLICATION DATE: JANUARY 29, 2009

Rationale

The ratings on Salama/Islamic Arab Insurance Co. (P.S.C.) (Salama/IAIC) of Dubai, United Arab Emirates (UAE), reflect its strong financial and good business profiles, which are based on reasonably strong earnings, capitalization, and liquidity; a good, increasingly diversified competitive position; and good investments and financial flexibility. Together with its subsidiaries, Salama/IAIC also benefits from the support of influential UAE and Saudi Arabia-based shareholders. Our principal concern is management's somewhat aggressive investment strategies in a region where asset values can be very volatile. Some uncertainty also surrounds the group's strategies for expansion, though no major moves are currently expected. If successful, the group will further diversify both revenues and earnings. However, competition is considerable and it may be several years before the success of any planned or opportunistic expansion becomes fully evident.

Meanwhile, Salama/IAIC has proven strength in the provision of explicitly Sharia-compliant (takaful) insurance in the UAE (13% of group gross premiums in 2007) as well as contributions from takaful subsidiaries in Algeria (8%), Senegal (3%), Egypt (2%), and affiliates in Saudi Arabia and Jordan. However, a full 74% of 2007 gross premiums were written by the 100% owned, Sharia-compliant reinsurance (retakaful) subsidiary, B.E.S.T. Reinsurance Co. (BEST Re; BBB+/Stable/--). Standard & Poor's Ratings Services has assessed BEST Re as strategically core to the Salama group. It writes largely proportional reinsurance in over 70 countries, principally in the Islamic states of Asia, the Middle East, and Africa. Each group operation specializes in general, non-life business but all are seeking to develop their still-modest life and health activities.

Reasonably strong operating performance is demonstrated by the group's net combined ratio of 84% in 2007, and three-year average of 84%. Similarly, the consolidated return on revenue (ROR) was a commendable 24% in 2007, while return on equity (ROE) was just over 11%.

Capitalization remains strong, and risk-based capitalization extremely strong, with consolidated net assets of $388.4 million, net premiums of $208.1 million, and a consequent solvency ratio of 186.6%.

Outlook

The stable outlook reflects Standard & Poor's expectation that the group will maintain financial ratios and risk management standards at least consistent with the current ratings. Prospectively, we do not expect combined ratios for the group to rise above the low 90% range, while ROR should exceed 15%, and ROE should remain stable at approximately 12%.

Capitalization, meanwhile, will remain strong, with extremely strong outcomes against Standard & Poor's risk-based capital model. Reserving and use of reinsurance protection will remain prudent, while the use of debt capital will be modest.

Although the revenue contribution from BEST Re will remain dominant for some years to come, we expect the growth of operations in the UAE, Saudi Arabia, and elsewhere to bring steadily greater diversification to the group's sources of income. Investment strategies are expected to remain somewhat aggressive.

Upward pressure on the ratings will increase if growing and increasingly diversified revenues are matched by increasingly strong and diversified earnings. Meanwhile, downward pressure could build up were rapid growth to dilute underwriting standards or capitalization, or if enterprise risk management fails to keep up with the increasing size and complexity of the group.

Saudi Re for Cooperative Reinsurance Co.

PRIMARY CREDIT ANALYST: DAVID ANTHONY, LONDON (44) 20 7176 7010, DAVID_ANTHONY@STANDARDANDPOORS.COM

SECONDARY CREDIT ANALYST: MATTHEW DAY, LONDON (44) 20 7176 7044, MATTHEW_DAY@STANDARDANDPOORS.COM

ISSUER CREDIT RATING: BBB+/STABLE/--

PUBLICATION DATE: NOVEMBER 20, 2008

Rationale

The ratings on Saudi-Arabia-based reinsurer Saudi Re for Cooperative Reinsurance Co. reflect the company's expert and influential management and main board teams, its broad-based and supportive shareholders, its strong paid-up capitalization of SAR1 billion ($267 million), and the attractive potential that the new company enjoys for rapid, sustainable growth, particularly in the Kingdom of Saudi Arabia (KSA), but also in neighboring Gulf Cooperation Council (GCC), Middle Eastern, and North African reinsurance markets.

The main offsetting weakness is inevitably the lack of track record. It remains to be seen to what extent the new company will succeed in establishing a strong competitive position while maintaining appropriate pricing and margins sufficient to generate a strong operating performance. Saudi Re is nevertheless expected to enjoy immediate competitive strengths in its home market.

Saudi Re is a start-up reinsurance company based in Riyadh. It has been actively under formation since 2006 and successfully listed on the Tadawul stock exchange in Riyadh in March 2008, prior to receiving its operating license in July 2008 and commencing underwriting in August 2008. Its strategy aims to promote diversification through an initial focus on proportional treaty business in the Middle East and North Africa, particularly motor and health in the KSA, while also selectively writing facultative risks across the region.

Outlook

The stable outlook reflects Standard & Poor's view that although Saudi Re enjoys attractive prospects for relatively rapid success, it is still too soon to credit the new company with overall financial strength characteristics clearly consistent with a higher rating range. Although the absolute strength of Saudi Re's prospective business position and earnings remains unproven, both are expected to be at least good, and to have the potential to become strong.

We expect net combined ratios to be no higher than 95% and return on revenues to be around 10%. Meanwhile, Standard & Poor's expects the company's capitalization, investments, liquidity, and financial flexibility to remain at least strong over the next five years, even as the new company expands. At the same time, the enterprise risk management processes already in place are expected to keep adequate pace with the company's operations as these develop in scale and in complexity.

The ratings could be raised by one notch once there is clear evidence that Saudi Re is successfully establishing a strong, diversified, and sustainable business position in its core market of Saudi Arabia, while generating appropriate underwriting and operating profits overall. Less likely, the ratings could come under negative pressure if Standard & Poor's finds that actual performance has slipped significantly relative to the start-up company's stated targets and objectives.

Takaful International Co. BSC

PRIMARY CREDIT ANALYST: KEVIN WILLIS, LONDON (44) 20 7176 7085, KEVIN_WILLIS@STANDARDANDPOORS.COM

SECONDARY CREDIT ANALYST: WOLFGANG RIEF, FRANKFURT (49) 69 33 999 190, WOLFGANG_RIEF@STANDARDANDPOORS.COM

ISSUER CREDIT RATING: BBB/STABLE/--

PUBLICATION DATE: JANUARY 29, 2009

Rationale

The ratings on Bahrain-based composite insurer Takaful International Co. BSC (TIC) reflect good operating performance and good financial flexibility. These positive factors are partially offset by the absolute small size of the company, operating in the relatively small Gulf Cooperation Council (GCC) market of Bahrain, and only adequate capitalization at the current level.

TIC has a good earnings record, from both its takaful (Islamic insurance) fund in terms of underwriting performance, and the overall shareholders' return on a conventional accounting basis. Technical earnings are expected to improve as the currently strong business growth delivers economies of scale. However, poor investment market conditions will depress shareholder returns in the short term.

TIC has good financial flexibility, supported by the TIC board's planned capital injection in 2009, which is agreed with its key shareholders to finance the growth of the company. Standard & Poor's Ratings Services expects this will be made sometime in the first half of 2009.

TIC currently has adequate capitalization, but Standard & Poor's expects it to be reinforced in 2009, giving strong capital adequacy. Quality of capital is good, with negligible soft components, but overall the level of capitalization is sensitive to investment market volatility.

In absolute terms, TIC is a small company, with total assets equivalent to $45 million at Sept. 30, 2008. However, it is an important member of the Bahraini insurance market, where its share has grown materially, with generally market level technical performances on all lines of business.

Outlook

The outlook is stable. TIC is expected to reinforce its current capitalization in 2009, thereby supporting its growing business base and expanding competitive position. Earnings will continue to be good, with the takaful fund continuing to deliver surpluses for members. The assets will reflect good liquidity and provide cover to technical and other liabilities. TIC's competitive position will grow within Bahrain, but will remain focused on this relatively small market.

Positive rating action is unlikely in the rating horizon. Negative rating action would be prompted by failure to strengthen capitalization in the first half of 2009, to a position where capital adequacy was strong. Negative rating action would also result from any weakening of its earnings or competitive position.

Takaful Re Ltd.

PRIMARY CREDIT ANALYST: NEIL GOSRANI, LONDON (44) 20 7176 7112, NEIL_GOSRANI@STANDARDANDPOORS.COM

SECONDARY CREDIT ANALYST: KEVIN WILLIS, LONDON (44) 20 7176 7085, KEVIN_WILLIS@STANDARDANDPOORS.COM

ISSUER CREDIT RATING: BBB/STABLE/--

PUBLICATION DATE: DECEMBER 23, 2008

Rationale

The ratings on Dubai-based reinsurer Takaful Re. Ltd. (TRL) reflect its strong capitalization, supportive shareholder base, and knowledgeable and experienced management team. These positive factors are partially offset, however, by the high execution risk faced by TRL, the still underdeveloped takaful market segment, and TRL's developing competitive position.

TRL's capitalization is strong, and therefore a key strength for the ratings. This is based on the company's extremely strong capital adequacy as measured by Standard & Poor's Ratings Services' risk-based capital model, low reliance on retrocession, and competent reserving practices.

TRL's influential shareholder base is viewed as a supportive factor for the development of its competitive position during its start-up phase. Although TRL is viewed as strategically important to its major shareholder, Arab Insurance Group (B.S.C.) (Arig; BBB/Stable/--), there is no support factored into the current ratings.

Management is viewed as knowledgeable with considerable experience of both conventional and takaful insurance markets. This is viewed as supportive of the ratings given the anticipated greater operational independence from its principal shareholder. This is further enhanced by outreach activities by senior management of the company by contributing to the development and understanding of takaful.

Execution risk is viewed as high but reducing with TRL developing a track record in managing growth in volume of retakaful business. This follows Arig's management of a historical, small retakaful portfolio. TRL achieved gross written premiums (GWP) of $20.4 million in 2007 and $34.5 million to September 2008, and a net loss ratio of 55% and 58%, respectively. A high level of growth is expected to continue in 2009. However, the company's ability to manage underwriting and capital through difficult market cycles is unproven.

Industry risk is viewed as moderately high due to an underdeveloped regional insurance market. Whilst the takaful segment holds significant potential, the competitive environment is viewed as challenging as direct takaful operators still need to get widespread acceptance in the market by developing full and comparable product offerings across business lines. The successful development of the retakaful market will, therefore, depend on the success of the direct market.

TRL's competitive position is viewed as potentially good, although the company is still at an early stage of its development.

Outlook

The stable outlook on TRL reflects our expectation that the company will continue to be supported by its shareholders, enabling the company's competitive position within the retakaful segment to grow. Standard & Poor's expects TRL's business flow prospectively to strengthen, and to at least track direct market growth. Although technical results are expected to remain stable, earnings for 2008 are expected to be impacted by a negative investment income as a result of capital market volatility. Arig, as majority shareholder and dominant service provider acts as a constraint on upwards movement on the ratings. A revision of the outlook to negative is considered remote over the ratings horizon, but would be driven by concerns regarding the ratings on Arig or a weakening in its competitive position relative to its peers.

Tawuniya/The Company for Cooperative Insurance

PRIMARY CREDIT ANALYST: NEIL GOSRANI, LONDON (44) 20 7176 7112, NEIL_GOSRANI@STANDARDANDPOORS.COM

SECONDARY CREDIT ANALYST: DAVID ANTHONY, LONDON (44) 20 7176 7010, DAVID_ANTHONY@STANDARDANDPOORS.COM

ISSUER CREDIT RATING: A/NEGATIVE/--

PUBLICATION DATE: MARCH 31, 2009

Rationale

On March 31, 2009, Standard & Poor's Ratings Services revised its outlook on Riyadh-based insurer Tawuniya/The Company for Cooperative Insurance (Tawuniya) to negative from stable. At the same time, the 'A' long-term counterparty credit and insurer financial strength ratings on Tawuniya were affirmed.

The outlook revision reflects our view that continued weakness in global and local equity markets has placed downward pressure on Tawuniya's risk-adjusted capital adequacy and significantly reduced income from its asset portfolio. This reduced asset base is indicated by the negative change in fair-value reserves of Saudi Arabian riyal (SAR) 339 million and net losses on investments of SAR121 million. Nevertheless, Standard & Poor's expects Tawuniya to maintain its lead position in the Saudi Arabian insurance sector and that technical operating performance will remain strong. In our view, this should permit retained earnings to help return capitalization to strong levels over the medium term.

Tawuniya's overall pretax profit in 2008 fell to SAR73 million from SAR568 million the previous year. This, together with falls in investment income, realized losses, and a dividend payment in 2008, reduced shareholders' equity by 42% to SAR1,073 million from SAR1,846 million in 2007.

Capital adequacy, which we now view as good, has benefited from the positive steps taken in 2008 by management to moderate the equity bias of its overall asset portfolio. In addition, the reported gross premium growth of 23% (27% net of reinsurance), reflective of the rapidly growing Saudi market, has increased the capital requirements as a result of increased exposure while adjusted capital has fallen. Overall capitalization is viewed as good, supported by prudent and stable reserves with technical reserves/net premium remaining stable at around 86% over the past five years. In addition, reported reinsurance usage and support remains unchanged at around 40%.

Operating performance remains strong with a reported combined ratio of 84.2% and an underwriting result of SAR181 million for 2008, which was in line with our expectations. Return on equity and return on revenue of 7.4% and 15.1%, respectively, fell below what we anticipated, although this view reflects investment devaluation rather than core underwriting results.

The ratings on Tawuniya continue to reflect our view of the strong competitive position, strong underwriting earnings, and positive management and corporate strategy. Offsetting factors are what we see as the relative decline of the company's capital adequacy through its exposure to equity market risks combined with an increase in underwriting exposures.

Outlook

The negative outlook reflects our view that the ratings will be lowered if capital adequacy continues to decline materially due to volatile equity markets. A revision of the outlook to stable could be achieved if Tawuniya can restore risk-adjusted capital adequacy to a strong level. An outlook revision to stable is also likely to be dependent on an easing in financial market conditions.

Competitive pressures are likely to remain high as newly licensed players continue to enter the market. This is expected to increase the demand for highly skilled Saudi nationals to meet "Saudization" quotas. Nevertheless, we expect Tawuniya to remain the dominant player in the Saudi market for the foreseeable future and for staff attrition levels to remain under control.

We believe there is limited opportunity for the ratings on Tawuniya to be raised further until the market achieves some measure of stability. The ratings may be negatively affected in the event of any material weakening of risk-adjusted capital adequacy. Also, although not expected, any significant deterioration in earnings would also inevitably create downward pressure on the ratings.

Trust International Insurance & Reinsurance Co. B.S.C. (c) Trust Re

PRIMARY CREDIT ANALYST: NIGEL BOND, LONDON (44) 20 7176 7063, NIGEL_BOND@STANDARDANDPOORS.COM

SECONDARY CREDIT ANALYST: KEVIN WILLIS, LONDON (44) 20 7176 7085, KEVIN_WILLIS@STANDARDANDPOORS.COM

ISSUER CREDIT RATING: BBB/POSITIVE/--

PUBLICATION DATE: DECEMBER 29, 2008

Rationale

The ratings on Bahrain-based non-life reinsurer Trust International Insurance & Reinsurance Co. B.S.C. (c) Trust Re (Trust Re or the company) reflect Standard & Poor's Ratings Services' view that the company is the core operating entity of Trust Re Group (the group). The ratings, therefore, reflect the group's strong capitalization, strong operating performance, good competitive position, and adequate enterprise risk management (ERM). Its improving, but only adequate, investments and its high dependence on reinsurance temper these positive factors.

Trust Re Group's capitalization reflects its extremely strong, if volatile, capital adequacy, and its very strong reserves, offset by its high, but declining, use of reinsurance. The quality of reinsurers used is generally high.

Trust Re Group has enhanced its shareholder value considerably over the past five reported years, in part through consistently very profitable underwriting, but largely through very high investment returns. Despite increasing competition and a rise in the number of large losses, the net combined ratio is expected to stay below 100% in 2008, reflecting disciplined pricing by the company. The quality of the overall operating performance is reduced by the volatility of the investment performance and the significant benefit derived from reinsurance commissions, both of which should diminish in importance in future.

Although small by global standards, the company is a long-established, well-known reinsurer in the Middle East with a rapidly increasing presence in Asia. It has grown quickly (and profitably) over the last four years, reflecting its geographic expansion, higher capacity, and growth in its primary insurance markets. Its strengths are its long-term commitment to its chosen regions, good service and acknowledged expertise, its strong relationships, and the benefits of having a variety of strategic partners. Its business is also well diversified. Nevertheless, Trust Re faces increasing competitive pressure, and its high, albeit declining, dependence on reinsurance is viewed as a weakness.

Trust Re Group's investment portfolio remains heavily exposed to equities and property—in particular to one equity and one property development—and lacks diversification. In mitigation, however, it should be noted that capital adequacy is extremely strong, which allows the group to adopt a higher risk investment strategy.

ERM has improved, and is now assessed as adequate. The establishment of a risk management department with a non-life actuary at its helm has led to a significant improvement in ERM over the past year or so.

Outlook

The positive outlook reflects Standard & Poor's expectation that Trust Re Group will continue to develop its ERM. We also expect the group's long-term underwriting performance to remain profitable, despite strong premium growth, that its capital adequacy will remain extremely strong, and that the company's use of reinsurance will diminish to about 60% in 2008 (excluding the Trust Underwriting Ltd. (TUL) quota share). The group's investment risk profile should also reduce slightly as equity investment is likely to be limited and as property investment continues.

Positive rating actions are likely if Trust Re Group continues to meet our expectations. Negative rating actions may be taken if underwriting performance or capital adequacy deteriorates beyond expectations.

Wethaq Takaful Insurance Co. K.S.C. (Closed)

PRIMARY CREDIT ANALYST: LOTFI ELBARHDADI, PARIS (33) 1 4420 6730, LOTFI_ELBARHDADI@STANDARDANDPOORS.COM

SECONDARY CREDIT ANALYST: DAVID ANTHONY, LONDON (44) 20 7176 7010, DAVID_ANTHONY@STANDARDANDPOORS.COM

ISSUER CREDIT RATING: BBB-/STABLE/--

PUBLICATION DATE: OCTOBER 16, 2008

Rationale

The ratings on Kuwait-based Wethaq Takaful Insurance Co. K.S.C. (Closed) (Wethaq) reflect its strong capitalization and good financial flexibility. Offsetting factors are a marginal competitive position, aggressive investment strategy, and only adequate earnings.

Capitalization supports the ratings thanks to strong capital adequacy and substantial use of reinsurance. Capital adequacy is strong according to Standard & Poor's Ratings Services' risk-adjusted capital model, with a capital base sufficiently covering the heavy capital requirements stemming from equity investments. A small capital base and insufficient business diversification mean that capital adequacy can be highly volatile, however.

Financial flexibility is good relative to Wethaq's modest needs, thanks to implicit shareholder support. Wethaq fits well with its main shareholder's Islamic finance strategy, and should benefit from shareholder support if the need arises. Wethaq's only adequate earnings potential constrains financial flexibility, however.

The competitive position is a weakness for the rating owing to Wethaq's very small size overall and dependence on reinsurance capacities. The company has not yet reached a critical size in its local market and cedes most of its business excluding motor. Mitigating this weakness is its focus on the niche, fast-growing takaful (Islamic Sharia-compliant insurance) business. Wethaq's links with its principal shareholder also offer good growth prospects and should help enhance Wethaq's penetration of the local and regional takaful markets.

Wethaq invests heavily in local equities and particularly nonlisted equities and funds. This weakens the company's financial profile, although the investments yielded adequate returns in the past five years. The company has not yet developed solid risk management practices to monitor its equity exposures, and relies mostly on its shareholder's expertise in that field.

Operating performance is adequate due to investment income and good loss ratios, reflecting the company's prudent pricing. The company's small premium volumes prevent it from sufficiently covering its expenses and expose it to prospective earnings volatility. Reinsurance costs also weigh on the company's earnings generation capacity, although reinsurance contributes to earnings stability.

Outlook

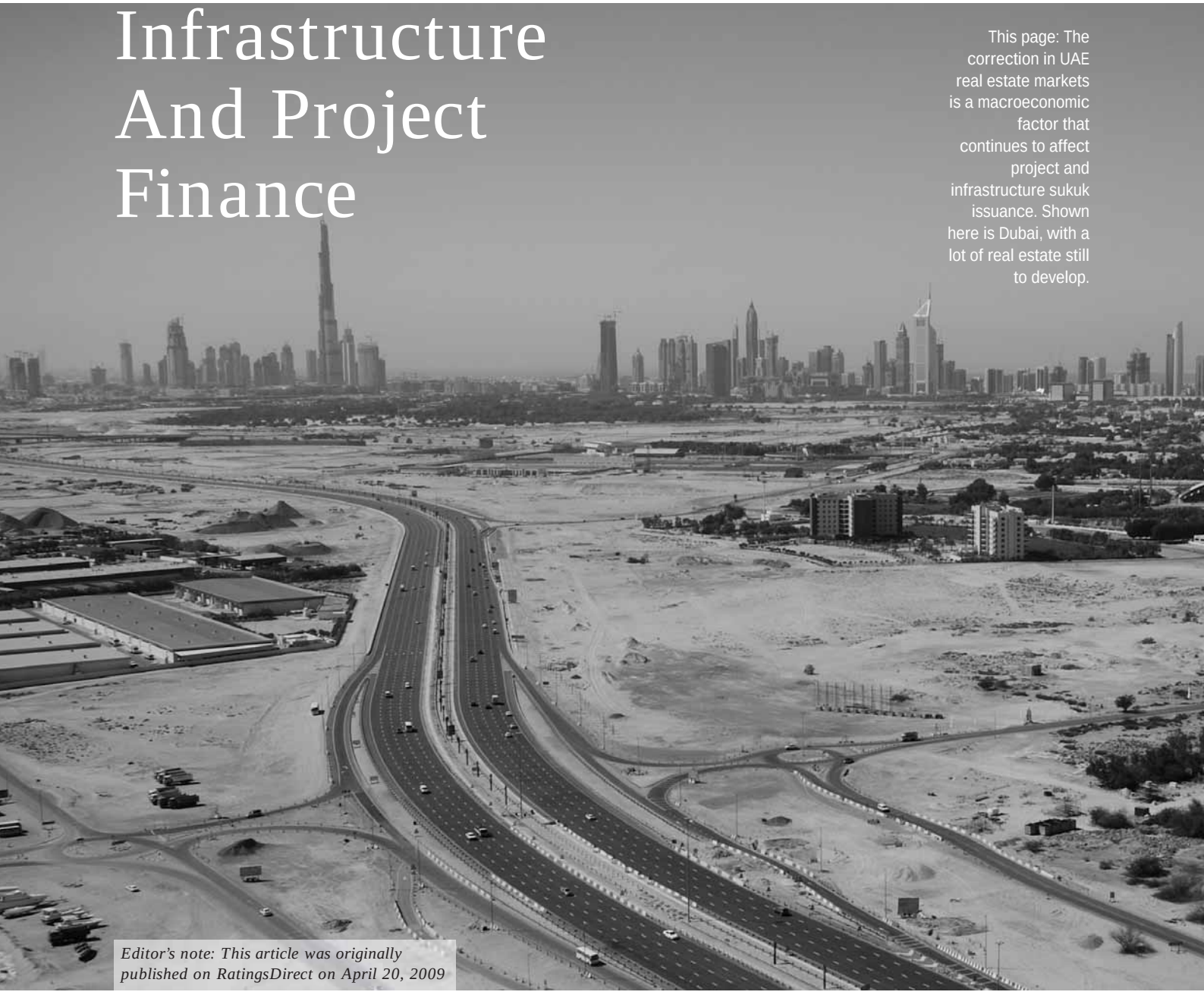
The stable outlook reflects our expectation that Wethaq will maintain strong capitalization and good financial flexibility, while gradually improving its earnings quality in 2009 and 2010. We expect Wethaq's competitive position to remain marginal over the same horizon, although we expect much higher growth compared with that of the past five years.

Wethaq should achieve at least 30% growth per year in 2009 and 2010, while premiums for 2008 should be at the same level as those for 2007. We expect Wethaq's shareholder to remain committed to supporting the company's growth and maintaining strong capitalization. The company should also reach a 95% net combined ratio in 2009 and 2010, while we expect the combined ratio for 2008 to be less than 105%. The company should reduce its cost ratios to 30% in 2009 and 2010.

Owing to Wethaq's current profile, an upgrade is unlikely over the rating horizon. We would however change the outlook to negative if the company does not reach the above-mentioned operating performance levels and growth targets in 2008 and 2009. Any apparent change in the shareholder's support for Wethaq would also result in a negative rating action.

PROJECT FINANCE
CORPORATES
UTILITIES
COMMENTARY

Islamic Sukuk Come Of Age In Infrastructure And Project Finance



This page: The correction in UAE real estate markets is a macroeconomic factor that continues to affect project and infrastructure sukuk issuance. Shown here is Dubai, with a lot of real estate still to develop.

Editor's note: This article was originally published on RatingsDirect on April 20, 2009

PRIMARY CREDIT ANALYST:
KARIM NASSIF, LONDON (44) 20 7176 3677
KARIM_NASSIF@STANDARDANDPOORS.COM

SECONDARY CREDIT ANALYSTS:
JONATHAN MANLEY, LONDON (44) 20 7176 3952
JONATHAN_MANLEY@STANDARDANDPOORS.COM

JAMES PENROSE, LONDON (44) 20 7176 3960
JAMES_PENROSE@STANDARDANDPOORS.COM



SUKUK TRANSACTIONS, INCLUDING NONRECOURSE financings, appear to be gaining traction in the Gulf region for project and infrastructure funding as investors become familiar with their features and flexibility. While the global economic slowdown may have curtailed the uptake of these transactions for now, investor appetite should recover in line with the business cycle. At the same time, however, the continued success of project and infrastructure sukuk will in Standard & Poor's Ratings Services' opinion require the resolution of outstanding compliance and security related issues.

In the time since we last reported on our rated infrastructure and project finance sukuk (see article titled "Credit FAQ: Project Finance Sukuk," published Nov. 16, 2007, on RatingsDirect), we have assigned a rating to the Tabreed 08 Financing Corp. convertible sukuk. This transaction features sharia-compliant trust certificates that are mandatorily exchangeable into ordinary shares of National Central Cooling Co. PJSC (Tabreed; BB/Developing/--). We've also rated Sun Finance Ltd. (a United Arab Emirates {UAE} dirham-based securitization of receivables from the sale of plots of land on the Shams Abu Dhabi development on Al Reem Island).

These transactions notwithstanding, project and infrastructure sukuk issuance in the Gulf has stalled. After years of rapid growth, the past few quarters have been difficult in the Gulf Cooperation Council (GCC) states and the project and infrastructure sukuk markets have not grown in 2008 to the levels anticipated. Nevertheless, the Tabreed 08 and Sun Finance issues may provide a basis for future infrastructure and project finance sukuk.

Global Slowdown And Local Factors Crimp Sukuk Issuance

The market's anticipated growth of sukuk (including those for infrastructure and project finance) failed to materialize in 2008, total sukuk issuance falling 56% to $14.9 billion compared with the previous year. That said, the value of Standard & Poor's rated project and infrastructure sukuk was broadly similar in both 2007 and 2008.

We believe that the underperformance in sukuk issuance is due in large part to the effects of the global economic downturn, specifically its influence on capital market issuance in GCC states. We are of the view, however, that

"…project and infrastructure sukuk issuance in the Gulf has stalled. After years of rapid growth, the past few quarters have been difficult in the Gulf Cooperation Council (GCC) states…Nevertheless, the Tabreed 08 and Sun Finance issues may provide a basis for future infrastructure and project finance sukuk."

notwithstanding the current state of the financial markets, the GCC will be the focus of most infrastructure and project finance sukuk activity in the short to medium term. This is because sukuk funding structures provide an alternative to the traditional bank financing that shows no immediate signs of return in the currently dislocated financial markets.

LOCAL FACTORS CURB INVESTOR APPETITE FOR SUKUK

The effects of the global downturn aside, the GCC region has its own contributing macroeconomic factors that continue to affect project and infrastructure sukuk issuance, namely:

High costs of financing. In our experience, the costs of structuring and issuing sukuk remain high relative to conventional bank loans and bond issuance. Legal and accounting fees contribute to this higher cost structure, as does uncertainty regarding the perceived risk associated with these instruments. Moreover, the lack of standard structures, perceived differences in approach to sharia compliance, and a relatively illiquid secondary market may, in our view, discourage investor appetite for sukuk.

Predominantly local investor appeal. In 2006 and 2007, there were a number of sukuk placed with international investors, including those of DP World Ltd. (A/Negative/A-1) and Tabreed. In 2008, by contrast, the reduced appetite for sukuk saw many issues taken up by local investors and denominated in local currencies. Furthermore, foreign currency-denominated, cross-border-placed sukuk remain more expensive than their locally placed counterparts. This is due to withholding tax payments applicable to cross-border transactions, on which investors demand a compensating coupon. Finally, we understand that uncertainty over the prevalent practice of pegging GCC state currencies to the U.S. dollar may also make foreign-currency denominated sukuk less attractive than those issued locally. As a consequence, local currency sukuk have been dominant. The relative degree of liquidity tightening in these local markets compared with levels a year earlier also contributed to funding costs.

Real estate downturn. The correction in UAE real estate markets, particularly in Dubai in the second half of 2008, suggests that government-related developers, utilities, and infrastructure companies reliant on third-party construction might be revising their financial and business models to reflect new market circumstances. This, in turn, suggests that funding of discretionary capital expenditures in the second half of 2008 through sukuk issues is likely to have been indirectly affected.

Hydrocarbon prices. The reduction in oil prices from around $128 per barrel at the end of June 2008 to around $40 per barrel at the end of December has, in our view, dampened wealth expectations in the GCC. This, in turn, has likely affected expansion plans for government entities by placing more scrutiny on the projects that should progress. Cheaper oil prices may have also affected local issuer and investor appetite for infrastructure and project finance sukuk.

Accounting issues. In our view, the February 2008 announcement by the Accounting and Auditing Organization for Islamic Financial Institutions (AAOFI), which addressed the issue of whether bonds structured with no transfer of collateral were sharia-compliant, contributed to market uncertainty. We understand anecdotally that the AAOFI's position may have prompted investors to seek a "risk premium" for particular sukuk transactions and, consequently, to a lull in issuance. We are not aware of any subsequent action taken by the AAOFI.

Despite these developments, high-profile sukuk issuance continues in the region. Both the Saudi Electricity Co. and Dubai Electricity and Water Authority issued sukuk in late 2007 and during 2008 to fund capital expansion in Saudi Arabia and Dubai , respectively. Sukuk-based financing remains the most attractive means of raising funding for medium- and long-term capital costs for GCC issuers. It forms the basis of a number of high-profile, hydrocarbon-related GCC project transactions, often split equally with debt-based bond and bank financing. As the Islamic infrastructure and project finance market develops, we anticipate there will be more transactions funded exclusively by sharia-complaint means.

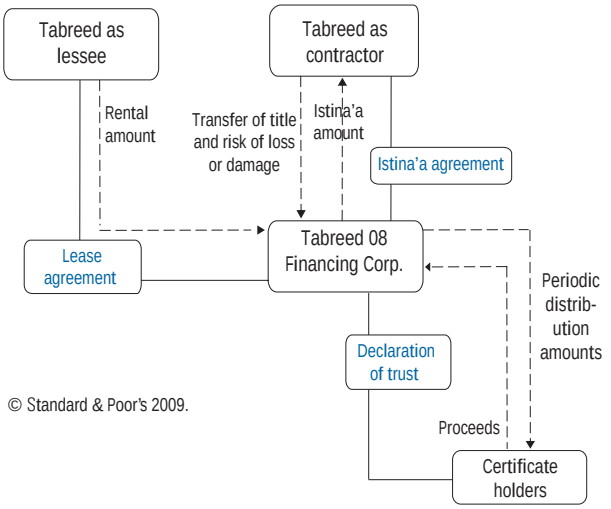
The Sukuk Instrument Proves Adaptable

In our opinion, sukuks have proven adaptable to complex infrastructure financings, as evidenced in the Tabreed 08 and Sun Finance projects.

It's our understanding that one of the purposes of the Tabreed 08 sukuk, for instance, was to raise financing for Tabreed's capital facilities expansion without increasing leverage. Tabreed 08 issued nondeferrable, deeply subordinated, and mandatory convertible ijara sukuk notes. In

Chart 1

Tabreed 08 Financing Corp. Transaction Structure



practice, annual profits are distributed to Tabreed 08, which services the notes over three years prior to conversion. Principal and interest payments are subordinated to all of the parent company's other debt obligations (unless expressly qualified as more junior) and ranked at the time of issuance senior only to common shares. Although the Tabreed 08 notes have sufficient debt-like characteristics to enable them to be rated, Standard & Poor's treats the principal amount of the notes as equity in order to calculate Tabreed's financial ratios. Similarly, we treat coupon payments as dividends for the purpose of our analysis. Since the Tabreed 08 issue, we have also rated convertible notes issued by Abu Dhabi National Energy Company PJSC (TAQA; AA-/Stable/A-1+). However, these were not structured as Islamic convertible notes.

We believe that once conditions improve in the financial markets, infrastructure developers seeking high equity treatment for capital market issuance may continue to employ sharia-compliant convertible notes to fund their capital needs. As we discuss below, Sun Finance, a construction financing backed by property receivables, has in our opinion already helped to extend the boundaries of nonrecourse project and infrastructure sukuk financings.

Recent Transactions Point The Way Forward

Our analytical approach to rating infrastructure and project finance sukuk is illustrated in the following transactions:

TABREED 08 FINANCING CORP.

Tabreed 08 is a special purpose entity wholly owned by Tabreed. Its sukuk issuance is being used to fund the construction of district cooling plants. The structure of this transaction makes use of both an ijara (sale and leaseback) and istisna (construction and delivery) agreement *(see chart 1)*. In fact, the Tabreed 08 structure resembles that of the Tabreed 06 Financing Corp. senior secured sukuk that we rated in June 2006, although there are some important differences.

At closing, Tabreed 08 purchased the cooling plants (or a part thereof) from Tabreed and entered into a lease arrangement, with Tabreed as lessee. Tabreed distributes annual profits (lease payments) to the issuer. Those monies are used by the issuer to service the coupon payments on the notes over the first three years. The proceeds of the sukuk issuance fund construction of the plants, while Tabreed will buy back the cooling plants from Tabreed 08 at maturity at a price payable in Tabreed shares, hence the convertible nature of the instrument.

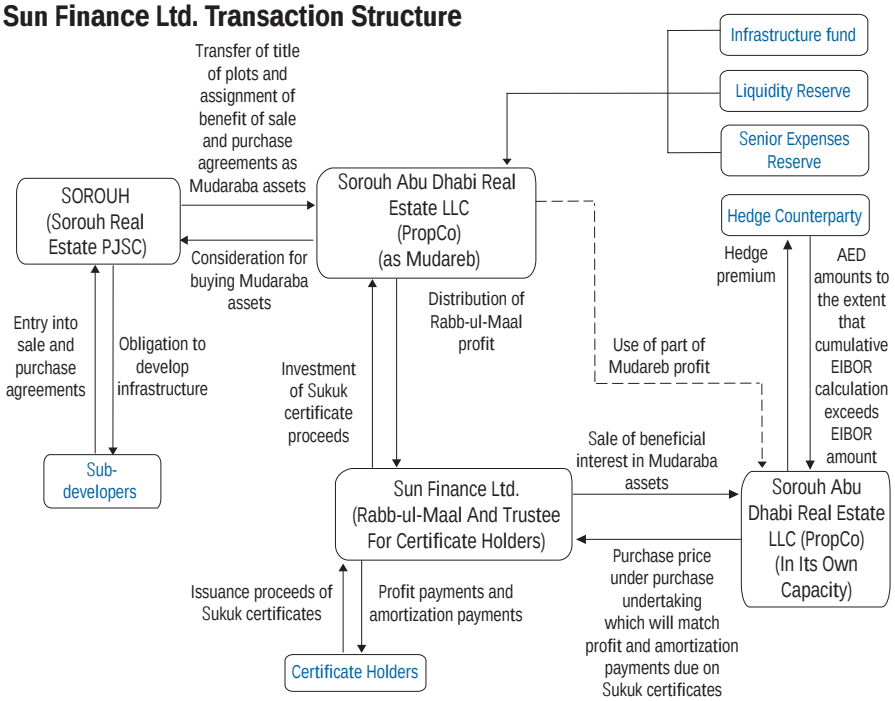
By contrast, in the Tabreed 06 transaction Tabreed will buy the cooling plants through exercising the purchase undertaking that in turn ultimately redeems the notes.

The following points of comparison exist between the "debt-like" features of the Tabreed 06 sukuk and the "equity-like" features of the Tabreed 08 sukuk:

- Under the Tabreed 08 sukuk, all lease payments are subordinated under normal circumstances to other senior creditors of Tabreed, as well as in the event of a payment default. This subordination of the Tabreed 08 sukuk includes its subordination to payment of the Tabreed 06 sukuk.
- Under the Tabreed 08 sukuk, consistent with its equity-like characteristics, lease payments service only the sukuk coupon, not principal. This contrasts with the Tabreed 06 senior sukuk purchase mechanism, which provides for payment of interest and principal on maturity via exercise of the purchase undertaking.

Chart 2

Sun Finance Ltd. Transaction Structure



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Standard & Poor's assigns a high equity content to the Tabreed 08 notes for three main reasons: They mandatorily convert into ordinary shares of Tabreed in three years; coupon payments are generally subordinated to Tabreed's other debt obligations; and the notes currently rank senior only to common shares. The notes were originally rated two notches lower than the long-term corporate credit rating on Tabreed. This is because of their subordination and to reflect the market risk resulting from the relative evolution of the share price and of the conversion ratio of the notes.

Since the ratings were assigned on April 14, 2008, the long-term rating on Tabreed has been lowered to 'BB' with a developing outlook. Following the downgrade in December 2008, we increased the differential between Tabreed's long-term rating and the Tabreed 08 convertible notes to three notches from two to reflect the latter's lower recovery potential.

Sun Finance Ltd.

The purpose of the Sun Finance securitization is to allow Sorouh Real Estate PJSC (Sorouh; not rated) to monetize future cash flows from the sale of real estate plots to property developers. Sorouh applied the proceeds of the monetization toward funding the utility infrastructure for two sites. One is Shams Abu Dhabi, a 170-hectare development on Al Reem Island, and the other is the Saraya development in Abu Dhabi's central business district.



In essence, there are three principle parties involved in this transaction: Sorouh, a project developer that sells the plots; Sorouh Abu Dhabi Real Estate LLC (Propco), that purchases the plots and, in turn, sells them to individual developers; and Sun Finance (Issuer) that issues the Al-Mudaraba Al-Muqayyada certificates to investors.

The transaction is capitalized by Sun Finance applying the certificate proceeds toward a mudareb (investor of capital). The certificate proceeds amount to the Issuer's beneficial interest in the mudareb. Propco, effectively a partner in the mudareb, buys the plots from Sorouh, sells them to the developers, and puts the purchase price toward the investors' (that is, trust certificate holders') returns and funding for the infrastructure works.

As payments from the developers come in through plot sales, ownership of the land incrementally shifts to the developers. In turn, Propco incrementally purchases the Issuer's beneficial interest in the mudaraba (trust) as it receives funds from plot sales, thereby amortizing the certificates (see chart 2). When a plot sale payment is received, Propco releases the relevant plot to the developer.

The Sun Finance transaction shares similarities with the DP World transaction. In that transaction, cash flow movement occurs in the following manner: First, investors pay the issue price for the sukuk and Dubai World Sukuk Ltd. (in its capacity as rab el-maal, or provider of capital) applies the proceeds as the capital of the mudareba, pursuant to a mudareba agreement entered into between the issuer and DP World (the latter acting in its capacity as the mudareb). Second, the mudareb invests the capital of the mudareba in DP World's business activities, in accordance with an agreed sharia-compliant investment plan prepared by the mudareb. The plan is designed to generate "profits," which will be used to service the notes. If insufficient profit is generated, DP World (in its capacity as mudareb) will be required to provide sharia-compliant funding to meet the payments in full.

The basis of repayment is the "profit" generated by the mudareba (or joint investment trust). If the mudareba does not generate enough "profit," DP World is required to provide funds to meet the shortfall in returns generated by the mudareba. DP World does this by exercising the purchase undertaking. For this reason, credit risk is linked not only to the mudareba, but also to DP World.

In comparing the Sun Finance and DP World transactions, we make several observations. One observation is that should DP World prove unable to generate sufficient profits to service the certificates, certificate holders have recourse to a purchase undertaking by DP World for the amounts due under the certificates. Therefore, the rating on the transaction is constrained by the rating on DP World. In Sun Finance, the Propco purchase undertaking is backed solely by the sale proceeds from the real estate plots. If plots are not sold or purchase prices not achieved, Propco will likely not be in a position to meet is obligations under the purchase undertaking. The Issuer's ability to service the certificates lies ultimately in the ability of Propco to sell and be paid for the plots. The significance of this feature is that the credit quality of Sorouh is effectively not an issue once the sale of the plots to Propco is completed, effectively making the Sun Finance transaction a nonrecourse sukuk.

Sun Finance features both senior and subordinated certificates. Standard & Poor's notes that the structure benefits from a fatw'a to the effect that it's sharia-compliant, although we do not verify shariah compliance.

The structure of the Sun Finance transaction reflects certain aspects of our project finance criteria. That said, we do not view it as a traditional project financing. This is because the transaction has much in common with structured financings such as residential mortgage-backed securitizations and corporate securitizations.

Differences between the Sun Finance transaction and more traditional types of project financing include the nature of the special purpose entity, attributes of the Issuer, the security structure, and payment flows.

Propco is 99%-owned by the chairman and managing director of Sorouh, the remaining 1% being held by an independent director. In the event of a payment default by Sorouh, transaction documentation indicates that the 99% share would be transferred to the independent director, who would then own 100% of Propco. Based on the information available, Standard & Poor's takes comfort that this structure is enforceable under applicable law.

As with the DP World transaction, investors do not have security as much as they hold a beneficial ownership interest in the mudareb. We understand that such interest is not the same as outright legal ownership. While the Issuer has a fixed and floating charge under U.K. law over the assets of Propco, there

is some question as to whether such charge would be enforceable in the UAE where the assets are located. In practice, we believe that the fixed and floating charge would likely only provide lenders with recourse to offshore assets of Propco. As noted above, in the event of the insolvency of Sorouh, the issuer is entitled to instruct the independent director to force a sale of the assets held by Propco. In summary, there is a degree of legal and country risk in each transaction.

Finally, in the Sun Finance transaction, the plots are not sold to the Issuer but to Propco. On a plot sale, the Issuer is paid through an onshore cash management agreement. Typically, offshore accounts are established where sale proceeds are deposited. Payments are made from such accounts to investors and back onshore.

Standard & Poor's ratings on structures such as Sun Finance and DP World rely on the economic fundamentals of such transactions as well as their structural and legal aspects.

Will Sukuk Flexibility Lead To Greater Take-Up In The Future?

In 2008, the project and infrastructure asset class accounted for around $1.6 billion (10%) of the $14.9 billion of sukuk issues that came to market. In 2009, the development of the sukuk market will depend on economic recovery, increases in oil and gas prices, and the stabilization of real estate markets in the GCC.

In our opinion, there are four important considerations that need to be addressed for sukuk financing to become a major component of project and infrastructure funding in the Gulf as well as in other markets such as Malaysia, Indonesia, Pakistan, and Gambia:

- Greater clarity in transaction structures. Improved documentation, increased standardization, and lower overall complexity;
- Consensus among Islamic scholars around the world, including better issuer and investor education about sukuk and sharia compliance generally;
- A liquid secondary market; and
- A more predictable legal framework. There is a lack of clarity of local law in a number of markets where sukuk issuance is prevalent. In particular, we consider that there are issues surrounding the enforceability of collateral.

Infrastructure financing needs remain significant in GCC states. According to The Middle East Economic Digest, about $2 trillion of planned and anticipated project and infrastructure financings will be undertaken in the region by 2020. Meanwhile, there remains the more immediate concern of refinancing existing bank loans, which may prove difficult given the reduced appetite for bank lending.

Many of the principles inherent in project financings are found in Islamic finance transactions. Consequently, as project financing matures as an asset class in the Gulf, we believe Islamic finance will continue to adapt to traditional project structures. Similarly, we see Islamic finance structures being applied to public-private partnerships, and independent water and power projects as these programs evolve in the Middle East.

We believe that the use of nonrecourse finance vehicles may continue to be used in securitizing future payment streams and providing short-term liquidity. We observe that securitization and monetization structures are assisting developers such as Sorouh in removing the immediate debt burden of such financings off their balance sheets. However, there's no track record of sukuk enforcements to date, and the issue of effective legal ownership of assets between a company and its related sovereign have yet to be tested.

In fact, the first infrastructure sukuks rated by Standard & Poor's such as Tabreed 06 and Tabreed 08, are more akin to corporate financing rather than project financing. Furthermore, on a corporate basis it's unlikely that there would be a significant difference in the risk component between a sukuk and secured corporate lending, assuming that the same underlying assets constitute security under the two different issues. It's possible, however, that by having less off-balance-sheet and derivative type counterparty risks, a sukuk transaction could be considered less exposed than a secured transaction with the same underlying assets.

Ultimately, the flexibility of the sukuk instrument may hold key to it increasing its share in financial markets. Although most sukuk issues so far have been debt-like, their ability to be structured as an equity instrument through convertibility means they could access a much wider investor base than traditional loan financing.

Abu Dhabi National Energy Company PJSC

PRIMARY CREDIT ANALYST: KARIM NASSIF, LONDON (44) 20 7176 3677, KARIM_NASSIF@STANDARDANDPOORS.COM

SECONDARY CREDIT ANALYSTS:
JONATHAN MANLEY, LONDON (44) 20 7176 3952, JONATHAN_MANLEY@STANDARDANDPOORS.COM
LUC MARCHAND, LONDON (44) 20 7176 7111, LUC_MARCHAND@STANDARDANDPOORS.COM

ISSUER CREDIT RATING: AA-/STABLE/A-1+

PUBLICATION DATE: JULY 24, 2008

Rationale

The ratings on Abu Dhabi National Energy Company PJSC (TAQA) reflect the company's position as a key entity in the economy of the Emirate of Abu Dhabi (AA/Stable/A-1+) as the majority owner in critical power and water desalination assets, and its importance as a vehicle for global investment and public policy. As a result, the ratings reflect our expectation of ongoing implicit sovereign support (although there are no formal guarantees) and the company's status as a government-related entity (GRE). We apply a one-notch differential between the rating of the Emirate and TAQA to reflect this support.

State support for TAQA is demonstrated in three ways. First, by the Emirate's, or its related entities', 75.1% ownership of TAQA. The company has issued Arab Emirate dirham (AED) 4.15 billion in convertible notes in July 2008 to help support ongoing funding needs. We do not anticipate that the notes, which will be converted into shares before the end of September 2008, will result in a material change in government ownership.

State support is also represented by TAQA's majority ownership of critical water and power assets that provide about 85% of the Emirate's power generation and 90% of its water desalination capacity. Finally, support is evidenced by the company's position as a vehicle for the Emirate to make overseas investments under the Abu Dhabi brand.

TAQA continues to seek investment opportunities outside the United Arab Emirates (UAE), witness the announcement by its wholly owned subsidiary, TAQA Bratani, in July 2008 of a sale and purchase agreement with Shell U.K. Ltd. (part of Royal Dutch Shell PLC; AA/Positive/A-1+) and Esso Exploration and Production (UK) Ltd. (part of Exxon Mobil Corp.; AAA/Stable/A-1+) to acquire operating licenses for six offshore fields and two nonoperated sub-sea tie-backs situated in the North Sea. The continued debt financing of such acquisitions is likely to both expose the company to greater risk and reduce the overall importance of the existing Emirate infrastructure assets within the investment portfolio.

TAQA's stand-alone credit quality (excluding any benefit of implicit government support) is in the 'BB' category. It is underpinned by the company's weak business profile, which we expect will be exposed (about equally in terms of revenues and EBITDA) to the oil and gas sector as well as the power business over the short to medium term. Stand-alone creditworthiness is also underpinned by TAQA's aggressive financial profile, witness the company's negative free cash flows over the short to medium term. That said, the latter are somewhat offset by stable long-term cash flows from the power business. Overall, we believe the main credit issues center on the company's limited track record, its need to successfully integrate recently acquired acquisitions, and its aggressive financial profile.

In the financial year ended Dec. 31, 2007, TAQA reported a strong 72% growth in revenues to AED8.33 billion, largely driven by acquisitions undertaken during the year. Profits before tax increased by 39% to AED1.31 billion. Cash flow from operations remained insufficient to fund capital expenditures, with negative free operating cash flows of AED2.92 billion.

As a result, TAQA's credit metrics remain weak, but in line with the previous year. EBIT interest coverage was 1.4x, debt to EBITDA was 11.9x, and debt to equity was 86.7%. What's more, results for the first quarter of 2008 (which factor in the Canadian oil and gas acquisitions executed at the end of 2007) point to more than a trebling of revenues compared with the same period in 2007, although the high acquisition costs have led to a continued decline in cash balances.

We will continue to focus on the credit quality of the underlying investment portfolio and the strength of the relationship with the Emirate as critical elements driving the ratings.

Outlook

The stable outlook reflects our expectation that there will be no major changes in the implicit government support given to TAQA as a GRE. This implies that the state will support the company in the event of financial distress if existing or future investments do not perform in line with expectations.

The outlook would be revised to negative or ratings downgraded if there is any weakening of the actual or implied sovereign support to the company. The ratings would be raised or the outlook revised to positive following a similar action on the rating or outlook on the sovereign, or if the sovereign was to enhance its support for the company.

PROJECT FINANCE
CORPORATES
UTILITIES

Ajman Sewerage (Private) Co. Ltd

PRIMARY CREDIT ANALYST: KARIM NASSIF, LONDON (44) 20 7176 3677, KARIM_NASSIF@STANDARDANDPOORS.COM

SECONDARY CREDIT ANALYSTS:
ALEXANDRE DE LESTRANGE, PARIS (33) 1 4420 7316, ALEXANDRE_DELESTRANGE@STANDARDANDPOORS.COM
JONATHAN MANLEY, LONDON (44) 20 7176 3952, JONATHAN_MANLEY@STANDARDANDPOORS.COM

ISSUE CREDIT RATING: A/NEGATIVE

PUBLICATION DATE: FEBRUARY 5, 2009

Rationale

On Feb. 5, 2009, we lowered our underlying rating on the $100 million senior secured bank loan issued by Ajman Sewerage (Private) Co. Ltd. to 'BB' from 'BBB'. The rating remains on CreditWatch with negative implications, where it was placed on Sept. 22, 2008, as a result of our view of the weaker-than-expected collection rates for connection and service fees in 2008 and ongoing delays to the construction program.

The insured 'A' long-term rating and the negative outlook on the loan reflect our assessment of the irrevocable and unconditional guarantee provided by Ambac Assurance U.K. Ltd. (A/Negative/--) of scheduled interest and principal on the loan and will be revised in line with any changes to the rating or outlook on Ambac.

The rating actions reflect Standard & Poor's opinion of the project's weaker financial profile than originally expected, which we understand is a result of lower collections from connection and service fees during 2008. (Lower collections exclude a one-off payment of United Arab Emirates dirham {AED} 37 million from the government of Ajman to Ajman Sewerage in September 2008 to reflect revised tariffs.) We expect lower collections also for 2009 and over the short to medium term. In our view, the weaker financial profile is also caused by the ongoing delay and potential increased cost of the construction program.

The CreditWatch placement reflects our view of the continued uncertainty regarding: the level of collections from connection/service fees relative to the "cure plan" financial model over the next three months; the degree of enforcement action undertaken by the government to improve collections; and the uncertainty over the likely capital expenditure required to meet actual completion and to fully extend the network to all registered properties in the concession area over time together with its financial impact on the project. It also reflects uncertainty as to whether an additional, two-month extension to the proposed substantial completion date (to April 6, 2009) will be granted by the independent engineer and whether Ajman Sewerage's current target date of July 2009 for actual completion (four months later than substantial completion) will be met.

Due to weaker anticipated fee collections, we believe the project's liquidity position has deteriorated, which has resulted in increased reliance on third-party funding sources, albeit these are committed and were anticipated to be partly drawn in the initial forecasts. We understand that these sources include sponsor subordinated loans of AED30 million (to fund debt service and expansion reserves) and a cumulative drawdown of AED58 million until 2012 under a yearly capped AED50 million revolving operating period guarantee from the government of Ajman. This is, we are told, in addition to the AED80 million construction bank guarantee from the state anticipated to be drawn down upon substantial completion.

In our view, the project's financial profile has weakened considerably, demonstrated by the expected annual debt service coverage ratio (DSCR) of 1.15x in January 2010 on a six-month look-back basis. This is only slightly above the 1.05x level that would constitute an event of default. Using Standard & Poor's project finance criteria definition of "DSCR" (which excludes sponsor funding and cash balances), we expect that the project's DSCR is likely to be below 1x until July 2011.

As a result, we believe the project has limited flexibility for underperformance against the "cure plan" financial model in terms of anticipated revenue collection or additional costs.

We understand that on Jan. 22, 2009, Ajman Sewerage agreed to a cure plan with its lender (ING Bank N.V.) and the controlling creditor, Ambac Assurance U.K. Ltd. The plan is based on what we believe are significantly more conservative assumptions on collection rates than had been previously assumed in Ajman Sewerage's 2006 financial forecasts. In our view, a key element of the cure plan is an agreement to revise the definition of "DSCR" to include sponsor funding and cash balances until July 2012. We understand that this revision would allow Ajman Sewerage to avoid a breach in the DSCR (on a six-month look-back basis) when it is due to be first tested in January 2010. We note that the cure plan also factors in the achievement of substantial completion on the outstanding construction works in February 2009 (extended from the original target date of Oct. 6, 2008). Under the cure plan, we understand that monthly cash balances are not anticipated to fall below a minimum level of AED3 million through 2012. The cure plan, if delivered by the project, would, in our opinion, result in an improvement in the project's financial profile to at least 1.2x (under Standard & Poor's definition) by 2012.

We understand that the current collection rate for connections to properties has been as low as 38% against an expected minimum of 60% under the 2006 projections. We have also observed significantly weaker service fee collection than anticipated due to both a low invoicing rate and low collection rate. We understand that only 50% of connected properties are currently being invoiced due to high vacancy rates as well as a number of properties still being under construction; this compares with a vacancy rate of 7% assumed in the original forecasts. We had previously understood from Ajman Sewerage that collection rates were due to improve, backed by increased support for enforcement action by the government. Although we understand that some initial action has resulted in a small number of disconnections, there does not appear to have been further comprehensive developments in the enforcement process.

We understand that on Jan. 21, 2009, Halcrow, the independent engineer, assessed that Ajman Sewerage had passed the main tests to meet substantial completion, except for the completion of the network infrastructure. We understand from Ajman Sewerage that the network infrastructure is essentially complete except for minor works. We understand that the engineering, procurement, and construction contractor has requested from the independent engineer a further delay to the substantial completion date to April 6, 2009, on the grounds of force majeure, although in practice we are told that Ajman Sewerage expects to achieve substantial completion by March 6, 2009. A decision by the independent engineer to extend the substantial completion date is due in the coming days.

Under the concession agreement, we note that Ajman Sewerage is required to connect any property registered within the initial concession area. Given the significant growth in properties over 2007/2008 (estimated at about 25% compared with initial forecasts of 5.75% over the period), Ajman Sewerage anticipates under the cure plan that over the 2009–2026 period it will carry out additional capital expenditure expansion works on the main treatment plant and network of AED219 million more than what was envisaged in the initial forecasts. Any additional property growth (more than the revised levels assumed in the cure plan over the short to medium term) could lead to a significant increase in costs if such properties require extensive additions to the infrastructure. The timing and full cost of additional works have not yet been verified by any independent technical reports, although Ajman Sewerage has made certain assumptions that generally spread out such costs over the medium to long term in the cure plan. We assume that any such required expenditure would not adversely affect the project's currently weakening financial profile.

The underlying rating on the bank loan reflects our opinion regarding the construction risk in delivering the completed project, the past reluctance of residents to pay for such services, and what is in our view a comparatively weak financial structure and covenant package. The underlying rating also reflects our view of the state support given to the project through specified payments and liquidity as well as the supportive concession agreement with inflation-adjusted tariffs. Another supportive factor is the company's monopoly position in providing a critical service to the Emirate.

Recovery analysis

The senior secured bank loan has a recovery rating of '3', indicating our expectation of meaningful (50%-70%) recovery of principal for senior secured lenders in the event of a payment default. This, in turn, reflects our expectation regarding the recovery of revenues based on current collection rates. The rating assumes that the completion and commissioning of the plant and network will be supported by revenue guarantees from the government.

CreditWatch

We will review the CreditWatch placement in the next three months as further information on collections of service and connection fees is available. In addition, achievement of the construction works is key.

We may lower the rating by more than one notch if we do not see an improvement in collections to the levels anticipated in the cure plan and/or if the construction program has ongoing delays or increased costs. The rating may also be lowered if the level or timeliness of sponsor and/or government financial support is not provided in full and in a timely manner as anticipated in the cure plan.

PROJECT FINANCE
CORPORATES
UTILITIES

Aldar Properties PJSC

PRIMARY CREDIT ANALYST: ALF STENQVIST, STOCKHOLM (46) 8 440 5925, ALF_STENQVIST@STANDARDANDPOORS.COM

SECONDARY CREDIT ANALYSTS:
FAROUK SOUSSA, PHD., DUBAI (971) 4709 6820, FAROUK_SOUSSA@STANDARDANDPOORS.COM
MOHAMMED FAYEK, LONDON (44) 20 7176 3408, MOHAMMED_FAYEK@STANDARDANDPOORS.COM

ISSUER CREDIT RATING: A-/STABLE/A-2

PUBLICATION DATE: FEBRUARY 5, 2009

Rationale

The ratings on United Arab Emirates (UAE)-based property developer Aldar Properties PJSC reflect the group's strong market position in the Abu Dhabi property development market, large land bank, close relationship with the government in project planning, and growing investment property portfolio (albeit currently small). Constraining rating factors include huge funding needs for project development, high debt levels, signs of softening in the Abu Dhabi real estate market, construction risk, and the group's limited operating history. In addition, the ratings reflect our expectation of strong support from the government of the emirate of Abu Dhabi (AA/Stable/A-1+), reflecting its involvement in Aldar and the group's importance to the government's strategy of diversifying the economy. Accordingly, the long-term rating includes a three-notch uplift from the standalone assessment of 'BBB-'.

Key business and profitability developments

Aldar's sales increased significantly in 2008, to UAE Dirham (AED) 4,978 million ($1.3 billion) from AED1,227 million in 2007. The increase is explained by a very high level of sales of land plots, as the group's own project developments are still in an early phase. Aldar generated an additional AED6,440 million of revenues from the sale of properties under construction during 2008, which will be recognized in future periods according to the group's accounting standards. As the group's land bank has been essentially granted by the government, Aldar's margins are high; its gross profit margin was above 50% in 2008. However, we expect margins to decrease in the medium term, as Aldar intends to retain most of its commercial property developments to build up more recurring and stable income from its investment property portfolio, although this comes with a lower margin. Although the Abu Dhabi property markets are historically undersupplied, there are signs of softening demand and price decreases, which could negatively impact Aldar's development plans and profit prospects in the near term.

Key cash flow and capital structure developments

Aldar's ambitious development plans, especially for building up its investment portfolio, require large capital needs and create significant cash outflows. In 2008, operating cash flows before capital expenditures were about AED1.5 billion compared with project spending of almost AED15 billion, of which most was investment in properties under development for future rentals once completed. We expect cash outflows to remain well in excess of cash inflows in the near term, although the magnitude will depend on the pace Aldar chooses to go ahead with its project plans.

Aldar has an aggressive financial risk profile. This is a result of the group's large use of debt funding for its project developments, which results in weak credit measures. Positively, Aldar has an adequate liquidity position, which will act as a cushion in withstanding softening property markets in the near term. Aldar's loan arrangements include a long-term government loan facility with favorable terms and a partly converted convertible sukuk bond with further conversion to equity likely. There is also some cushion in the group's large land bank, as Aldar sells plots of land to third-party developers to partly finance its own developments. Such sales could be accelerated if necessary, although they would be dependent on market demand.

Liquidity

We expect Aldar to continue to have adequate liquidity resources, which is of key importance given expected negative cash flows over the next few years. The group's strategy is to have available liquidity covering at least 12 months of upcoming cash needs. On Dec. 31, 2008, the group had about AED11 billion in unused committed facilities, of which a major part was a loan facility from the government. In addition, Aldar had about AED12 billion in cash and equivalents, although a major part of this will be used to fund large-scale project developments over the near term. The funds have been raised largely through long-term borrowings, and short-term debt stood at AED 2.7 billion on Dec. 31, 2008. To execute its

development plans, Aldar will, however, be dependent on further external funding, which we expect the group to be able to manage. In addition, Aldar builds its projects in phases, which can be postponed if necessary.

Recovery analysis

We have assigned our 'A-' long-term senior unsecured debt rating to AED 3.75 billion in sukuk al-ijara certificates issued by special purpose vehicle Sukuk Funding (No.2) Ltd. The ratings are equalized with the long-term ratings on Aldar. This reflects limited, contractually senior liabilities and structural subordination issues. Aldar's future lending is expected to be on an unsecured basis. Under a purchase agreement, the issuer will purchase a 50-year head lease interest on a plot of land (lease assets) from Aldar. The issuer will then lease the land to Aldar for periodic lease payments equal to the return due under the certificates. Although sukuk investors have no direct claim over Aldar's assets, they benefit from a purchase undertaking which could be exercised on the scheduled dissolution date or in an event of dissolution whereby Aldar is required to purchase the lease assets. Under Standard & Poor's sukuk rating methodology, the sukuk qualifies for full credit enhancement, which entails equalizing the issue rating with those on Aldar.

Outlook

The stable outlook reflects our expectations that Aldar will continue to play an important role in real estate development in Abu Dhabi, and will continue to have material government ownership, factors which are likely to result in continuing government support.

The rating could be raised if the government were to increase its ownership to a majority stake, or if the group significantly strengthened its financial risk profile. It could be lowered if government support were to weaken. Weaker-than-expected demand growth resulting in oversupply in the Abu Dhabi real estate market or failure to execute projects could also pressure the ratings.



PROJECT FINANCE
CORPORATES
UTILITIES

DIFC Investments LLC
DP World Ltd.
Dubai Holding Commercial Operations Group LLC
Dubai Multi Commodities Centre Authority
Emaar Properties PJSC
JAFZ Sukuk Ltd.
Jebel Ali Free Zone (FZE)
Thor Asset Purchase (Cayman) Ltd.

PRIMARY CREDIT ANALYST: FAROUK SOUSSA, PHD., DUBAI (971) 4709 6820, FAROUK_SOUSSA@STANDARDANDPOORS.COM

SECONDARY CREDIT ANALYST: ANDREAS KINDAHL, STOCKHOLM (46) 8 440 5907, ANDREAS_KINDAHL@STANDARDANDPOORS.COM

ADDITIONAL CONTACTS:
ALF STENQVIST, STOCKHOLM (46) 8 440 5925, ALF_STENQVIST@STANDARDANDPOORS.COM
ALEXANDRE DE LESTRANGE, PARIS (33) 1 4420 7316, ALEXANDRE_DELESTRANGE@STANDARDANDPOORS.COM
CHRISTIAN ESTERS, CFA, FRANKFURT (49) 69 33 999 242, CHRISTIAN_ESTERS@STANDARDANDPOORS.COM

PUBLICATION DATE: APRIL 30, 2009

Rationale

On April 30, 2009, Standard & Poor's Ratings Services placed the ratings on the following Dubai-based government-related entities (GREs) on CreditWatch with negative implications: DIFC Investments LLC, DP World Ltd., Jebel Ali Free Zone (FZE), the Dubai Multi Commodities Centre Authority (DMCC), Dubai Holding Commercial Operations Group LLC (DHCOG), and Emaar Properties PJSC (collectively, "the Rated GREs"). In addition, we placed the notes issued by Thor Asset Purchase (Cayman) Ltd. (Thor), which are securitized by cash flows from a revolving pool of existing and future receivables originated by Dubai Electricity and Water Authority (DEWA; not rated), as well as the notes issued by JAFZ Sukuk Ltd. (collectively, "The Notes"), on CreditWatch with negative implications (see Ratings List below).

The CreditWatch placements reflect our opinion of the likelihood of downgrades of the Rated GREs and The Notes if the potential for extraordinary government support to the Rated GREs and The Notes is not affirmed by the government of Dubai. The need for Dubai government support is potentially increasing in the face of deteriorating fundamentals for some of the Rated GREs.

The action results from our learning that a review of debt strategy at Nakheel (not rated), a material subsidiary of government-owned Dubai World (also not rated) and a key Dubai-based GRE, may include the possibility of a debt exchange. Recent media reports indicate that Nakheel is opening a dialogue with existing holders of its $3.5 billion sukuk coming due in December 2009, with a view to restructuring the debt. Standard & Poor's has discussed these reports with Dubai World and has been told that "all options" in dealing with outstanding liabilities are being considered as part of an ongoing review, including a restructuring.

Standard & Poor's has also invited comment from the government of Dubai, which has declined to either refute the possibility of a debt restructuring at any of its Rated GREs or to provide clear assurances that all debt obligations of the Rated GREs will be met in a full and timely manner as per their original terms.

The primary reason the mere possibility of a debt restructuring in an unrated Dubai-based GRE has been sufficient to trigger a review of all our Rated GREs and The Notes is due to the fact that such a possibility stands at odds with our prior expectation that the government of Dubai is committed to providing extraordinary support to its key GREs, including the Rated GREs, in order to allow them to service their respective obligations in a full and timely manner. This expectation is based in part on repeated representations to Standard & Poor's and to the public by senior government officials and other highly placed individuals, that the government of Dubai is committed to providing such extraordinary support.

In accordance with our published criteria, a GRE is rated between the inclusive bounds formed by the GRE's stand-alone

credit profile and the government rating, with the placement along this rating spectrum a function of our assessment of the potential for extraordinary government support (see "Rating Government-Related Entities: A Primer," published on June 14, 2006, on RatingsDirect). All of the Rated GREs reflect government creditworthiness more than stand-alone credit profiles, though this may shift should the government's support commitment ebb. In our view, the consideration of a debt restructuring in any key GRE, particularly if it were deemed to be "distressed", increases the uncertainty as to Dubai's intention to provide adequate support in times of stress.

CreditWatch

At this stage, we have not had confirmation as to Nakheel or the government's intentions with respect to Nakheel's outstanding sukuk. The CreditWatch placement will hold for the duration of our review, which will focus on confirming these intentions, and then assessing the impact this may or may not have on our view of the likelihood of extraordinary government support with respect to The Notes, and each Rated GRE and its respective obligations. We will resolve the CreditWatch placement once the analysis is complete. There isa significant likelihood that the review may result in the downgrade of one or more Rated GREs or The Notes by one or more notches, depending on our assessment of the likelihood of support on a case-by-case basis, and on the stand-alone creditworthiness of each Rated GRE and its respective obligations.

Ratings List

DIFC Investments LLC
Issuer Credit Rating: A/Watch Neg/A-1

DP World Ltd.
Issuer Credit Rating: A/Watch Neg/A-1

Jebel Ali Free Zone (FZE)
Issuer Credit Rating: A/Watch Neg/A-1

JAFZ Sukuk Ltd.
Issuer Credit Rating: A/Watch Neg/A-1

Dubai Holding Commercial Operations Group LLC
Issuer Credit Rating: A/Watch Neg/--

Dubai Multi Commodities Centre Authority
Issuer Credit Rating: A-/Watch Neg/A-2

Emaar Properties PJSC
Issuer Credit Rating: BBB+/Watch Neg/--

N.B.—This list does not contain all ratings affected.

ETA Group

PRIMARY CREDIT ANALYST: STUART CLEMENTS, LONDON (44) 20 7176 7012, STUART_CLEMENTS@STANDARDANDPOORS.COM
SECONDARY CREDIT ANALYST: ALF STENQVIST, STOCKHOLM (46) 8 440 5925, ALF_STENQVIST@STANDARDANDPOORS.COM
RECOVERY ANALYST: FLORENCE DEVEVEY, MADRID (34) 91 788 7236, FLORENCE_DEVEVEY@STANDARDANDPOORS.COM
ISSUER CREDIT RATING: BB+/NEGATIVE/--
PUBLICATION DATE: MARCH 9, 2009

Rationale

On March 9, 2009, Standard & Poor's Ratings Services lowered its long-term corporate credit rating on Dubai-based industrial conglomerate ETA Group to 'BB+' from 'BBB-'. The outlook is negative.

At the same time, the debt rating on the group's $300 million senior unsecured bank loan due 2012, for which subsidiaries Emirates Trading Agency LLC, ETA Star Holdings Ltd., and Associated Construction and Investments Co. LLC are the joint borrowers, was also lowered to 'BB+' from 'BBB-'. A recovery rating of '4' has been assigned to the loan, indicating our expectation of an average (30%-50%) recovery in the event of payment default. The ratings were removed from CreditWatch where they were placed with negative implications on Nov. 20, 2008.

The downgrade reflects our expectation of a significant increase in financial leverage for the year ending 2008, and a weakening of the financial profile to a level below our expectations for the previous 'BBB-' rating. The downgrade also reflects our belief that ETA may struggle to meet financial covenants in the short term and that this may put additional pressure on liquidity, at a time when banking markets are also less favorable. It also reflects our view that the adverse economic conditions will continue to present a challenging environment for ETA's mainly cyclical businesses. The rating continues to include a one-notch uplift to reflect implicit support as a result of ETA's 52% ownership by, and close relationship with, the Al Ghurair family.

ETA's debt levels have risen significantly in recent years to fund the increasing working capital and capital investments that have fueled the company's rapid growth. While increasing profitability and cash generation had partially mitigated the impact on leverage, key credit measures have now weakened following a downturn in some of ETA's key markets. We believe that funds from operations (FFO) to adjusted debt for the fiscal year to Dec. 31, 2008, will fall to about 11% from 19%, and that adjusted debt to adjusted EBITDA will deteriorate to over 6.5x from 5.2x in 2007. ETA management have now embarked on a program focused on improving the financial profile through a reduced capital expenditure program, temporarily restricted dividend policy, and through the disposal of selected noncore assets. While we believe this will have a positive effect, we think a recovery in the financial risk profile may be partially offset by the weaker economic environment.

ETA continues to have a satisfactory business risk profile underpinned by stable contractual businesses with significant order backlog predominantly with large well-established or government-related entities. It also has a good mix of complementary business divisions, creating opportunities for synergies, strong positions in its key markets, and good diversity of earnings. However, we believe that the continuing global economic slowdown is having an adverse effect on overall demand and pricing in the company's main markets in India, China, and the Gulf Cooperation Council. While the significant contract backlog should help soften the impact this may have on trading performance in the short term at some of its key businesses; shipping, commodity trading, cement manufacturing, property development, and car trading are all considered to be more sensitive to economic conditions. At the current 'BB+' rating we would expect to see ETA maintain a FFO to adjusted debt ratio in the range of 15%-20% and an adjusted debt to EBITDA ratio of less than 4.5x.

Liquidity

While we have some concerns over tight covenant levels, we perceive ETA's overall liquidity as adequate. At Dec. 31, 2008, we understand ETA had UAE dirham (AED) 1.24 billion of debt maturing in 2009. At the same time, it had unrestricted cash and equivalents of AED1.0 billion, marketable securities of AED198.4 million, and headroom of almost AED2.83 billion in committed banking facilities to meet its liquidity needs. ETA's credit facilities include financial covenants, which may be at risk of breach following the increase in leverage for fiscal year ending Dec. 31, 2008. However, we understand that ETA continues to benefit from strong support from its local banks. We believe that unless covenants are revised, headroom in 2009 will remain tight.

Recovery Analysis

We assigned a recovery rating of '4' to the $300 million unsecured loan taken on by joint borrowers Emirates Trading Agency LLC, Associated Construction and Investments Co.

LLC, and ETA Star Holdings Ltd., indicating our expectation of average (30%-50%) recovery for unsecured creditors in the event of a payment default. The issue-level rating on this debt is 'BB+', in line with the corporate credit rating on the group.

The recovery rating is constrained by the unsecured nature of the loan, as well as the potential exposure post default to the yet untested UAE insolvency regime, which we view as potentially unfavorable for secured and unsecured creditors.

At the same time, the recovery rating reflects the guarantees provided to the $300 million unsecured lenders by some of the operating companies, whose combined EBITDA currently accounts for about 75% of the group's EBITDA. The recovery rating is further supported by ETA's leading market positions in most of the markets in which it operates and its satisfactory business risk profile, which underpin our valuation of the company as a going concern. This results in a stressed enterprise value of about $2.1 billion at our simulated point of default in 2012.

After taking out about $400 million of priority liabilities—consisting of enforcement costs and finance leases—as well as about $1 billion equivalent of secured debt, we have estimated that the recoveries for the $300 million unsecured lenders will be in the 30%-50% range, which equates to a recovery of '4'. This reflects two key assumptions that we have made for our recovery calculations. First, we have assumed that the guarantees of the operating companies will be effective, giving the lenders of the $300 million loan an unsecured claim at the guarantors' level. Secondly, we have prudently assumed that the split of the unsecured debt and of the asset value between guarantors and nonguarantors of the loan is similar to that of the EBITDA split (the combined EBITDA of the guarantors account for about 75% of the group's EBITDA). Under these assumptions, we have allocated about 25% of the $700 million residual enterprise value to the unsecured debt holders at the nonguarantor level (assumed to represent 25% of total unsecured lenders), and 75% of the $700 million residual enterprise value to the pari passu $300 million lenders and unsecured debt holders at guarantors level.

For a detailed analysis, please see article titled "Recovery Report: ETA Group Recovery Rating Profile," published today on RatingsDirect.

Outlook

The negative outlook reflects our concern that management's efforts to reduce debt levels and improve the financial profile may be hampered by the difficult economic conditions and the adverse impact this is likely to have on some of ETA's cyclical businesses. It also reflects our negative industry outlook for most of the core sectors within which ETA operates. The rating continues to assume that there is no change to ETA's shareholding and that the group's close relationship with the Al Ghurair family will continue. A deterioration in liquidity, or a failure to return leverage ratios to our expected range for the rating, in the near-term, could result in a negative rating action. This could be due to weaker-than-expected cash flows from asset disposals or due to a further weakening of the group's major markets. Upside potential is currently limited, given the weak trading environment and financial profile, but would likely be related to a combination of a successful asset disposal program and better-than-expected trading performance that led to strong cash generation, debt reduction, and an improvement in the financial risk profile.

Emirates Telecommunications Corp. (Etisalat)

PRIMARY CREDIT ANALYST: MICHAEL O'BRIEN, LONDON (44) 20 7176 3561, MICHAEL_OBRIEN@STANDARDANDPOORS.COM

SECONDARY CREDIT ANALYST:
LEANDRO DE TORRES ZABALA, MADRID (34) 91 389 6965, LEANDRO_DETORRESZABALA@STANDARDANDPOORS.COM

ISSUER CREDIT RATING: A+/STABLE/A-1

PUBLICATION DATE: MAY 7, 2009

Rationale

The ratings on Emirates Telecommunications Corp. (Etisalat), the former incumbent fixed-line and leading mobile telecommunications operator in the United Arab Emirates (UAE), are supported by the company's leading market position in both fixed and mobile telephony in the UAE telecoms market, despite the introduction of competition in 2007. Etisalat's profitability levels are strong, with an EBITDA margin of 63.8% for the 12 months ended March 31, 2009. Furthermore, it generates strong cash flows and maintains good financial flexibility, backed by a portfolio of growing overseas assets, the value of which has increased significantly. The ratings also factor in implicit state support (Etisalat is 60% state-owned), given that the government has not advocated significant liberalization of the market to date and strategically assists the company in developing abroad, in partnership with other UAE government-related entities. We recognize Etisalat's strategic importance to the state as a provider of key communications infrastructure and as a flagship national company; therefore, the corporate credit rating includes a one-notch uplift from our stand-alone assessment of the company's credit quality.

The ratings are constrained, however, by potential further regulatory changes, which may impair Etisalat's domestic competitive position. Possible developments in the medium term include the granting of further licenses in an environment where traditional fixed-line service revenues are stagnating or falling gradually. In addition, a high percentage of profits are paid out as dividends and royalties, and this can moderate financial flexibility. Finally, there is uncertainty over the credit impact of potential future mergers and acquisitions activity abroad in emerging markets as part of Etisalat's strategic goal of maintaining high growth rates. This is despite the company's significant financial flexibility to undertake such activities, which could lead to a measured increase in leverage from existing low levels.

KEY BUSINESS AND PROFITABILITY DEVELOPMENTS

Year-on-year revenue growth of 13% in the first quarter of 2009 was robust and in line with rating expectations. However, the level of growth throughout the portfolio of 18 markets could moderate in the following quarters due to macroeconomic weakening, a slowdown in population growth in the UAE, or foreign exchange volatility in certain of Etisalat's markets. This effect was seen in the weaker sequential quarterly revenue growth of 1% compared with the fourth quarter of 2008. EBITDA continued to grow, reaching 1.9% year on year in the first quarter. However, lower margins in the company's markets outside the UAE and start-up costs in newer markets may dampen margins in future quarters. In September 2008, the company announced it would purchase 45% of Indian mobile operator Swan Telecom Private Ltd. for $900 million, and in January 2009 announced its 49% participation in the third mobile license in Iran.

KEY CASH FLOW AND CAPITAL-STRUCTURE DEVELOPMENTS

Etisalat continued to generate substantial cash flows in the first quarter of 2009, in line with our expectations. The company reported 5% year-on-year growth in adjusted free operating cash flow (FOCF) to UAE dirham (AED) 7.8 billion for the 12 months ended March 31, 2009. This was achieved via a reduction in capital expenditures in the quarter and lower finance costs, offsetting a 4.4% decrease in operating cash due to lower working capital inflows.

Etisalat's financial policy to date has been conservative. It is only relatively recently that the company used debt to partially fund its investments in Saudi Arabia, Pakistan, Egypt, Indonesia, and West Africa. We do not expect Etisalat to exceed board-approved peak leverage levels of 2.5x debt to EBITDA at any time. We generally anticipate leverage to be 1x–2x or lower, although Etisalat currently retains considerable headroom regarding these expectations. The company's leverage may increase slightly, depending on the choice of funding of the various investments that Etisalat is

undertaking, for example in India and Iran. Nevertheless, ratings headroom should, in our view, remain sufficient. Based on the current capital structure—which includes adjusted total debt on March 31, 2009, of AED6.3 billion ($1.7 billion)—adjusted debt to EBITDA (not including any cash netting) for the 12 months ended March 31, 2009, was 0.4x. In the same period, FOCF to debt was 124.9%, contributing to modest financial risk.

Short-term credit factors

The 'A-1' short-term rating is supported by Etisalat's strong liquidity, net cash position, and good financial flexibility for its needs. On March 31, 2009, liquidity resources included cash and cash equivalents of AED14.6 billion, of which AED2.5 billion was located overseas.

Etisalat had short-term debt maturities of AED664 million on March 31, 2009. The company also had short-term liabilities of AED2.4 billion relating to amounts payable on the acquisition of investments and licenses, most of which relates to investments in Pakistan. A final dividend for 2008 of AED2.0 billion was paid in April 2009, after an interim dividend of AED1.5 billion in August 2008.

We expect recurrent strong FOCF generation to remain a significant source of financing. FOCF reached AED3.5 billion in the first quarter of 2009, driven primarily by lower capital expenditures, compared with AED3.0 billion a year earlier. However, FOCF might not be sufficient if Etisalat were to undertake large acquisitions or other corporate activities while continuing to pay substantial dividends and royalties. In this case, we would expect the company to fund its requirements with the issuance of new debt, or to co-invest with other parties. That said, we believe that the company has adequate financial flexibility at the rating level to fund the Swan Telecom transaction in India for $900 million and to develop its business in Iran. This entails purchasing a license for 300 million, of which Etisalat will pay 49%.

Outlook

The stable outlook reflects our view that Etisalat is likely to remain committed to a conservative financial policy and that FOCF generation in its domestic business will remain robust in the face of any changes that might occur in the market. Such changes might include increased competition, macroeconomic weakness, or further liberalization. We also anticipate that Etisalat will make and absorb with relative ease investments in fiber-optic network.

In our view, the proportion of funds from operations to debt is likely to remain above 40% and adjusted debt to EBITDA should stay between 1x and 2x. Any weakening would need to be temporary to avoid pressure on the ratings. Etisalat's main credit protection ratios are above expectations for the rating level, given the relatively low level of debt on the balance sheet, and therefore offer the company the financial flexibility it needs for its investment plans, in our view.

The ratings could be negatively affected if the company were to accelerate its growth plan or transform itself through acquisitions. The ratings could also be adversely affected if Etisalat were to adopt a more aggressive financial policy or suffer from a substantial negative effect on financial performance as a result of unforeseen regulatory decisions. We do not envisage upside to the ratings at this stage, given the risks and dynamics associated with the telecoms industry and the company's willingness to increase leverage for potential foreign acquisitions. Nevertheless, moderation in dividends or a revision of Etisalat's financial policy to lower peak leverage levels could add weight to a potential upward rating movement.

PROJECT FINANCE
CORPORATES
UTILITIES

International Petroleum Investment Company

PRIMARY CREDIT ANALYST: FAROUK SOUSSA, PHD., DUBAI (971) 4709 6820, FAROUK_SOUSSA@STANDARDANDPOORS.COM

SECONDARY CREDIT ANALYST:
KARL NIETVELT, PARIS (33) 1 4420 6751, KARL_NIETVELT@STANDARDANDPOORS.COM

ISSUER CREDIT RATING: AA/STABLE/A-1+

PUBLICATION DATE: APRIL 27, 2009

Rationale

On April 27, 2009, Standard & Poor's Rating Services assigned its 'AA' long-term and 'A-1+' short-term corporate credit ratings to the 100% state-owned International Petroleum Investment Company (IPIC), based in Abu Dhabi, in the United Arab Emirates (UAE). The outlook is stable.

The ratings on IPIC have been equalized with those on the government of Abu Dhabi. Although the Abu Dhabi government has not formally guaranteed IPIC's liabilities, the group has a high-profile policy role in undertaking international investments with some technological or other benefit for the Abu Dhabi economy or for the national oil company ADNOC, and is set to play a central role in the development of the domestic petrochemicals industry. In addition, IPIC has a second clear government mandate with respect to some strategic national projects, such as the construction of the domestic crude oil pipeline (ADCOP), or diplomatic investments (Parco, Al Falah fund). This, coupled with IPIC's operational and managerial proximity to the Abu Dhabi government and repeated governmental capital increases, leads Standard & Poor's to conclude that the government has the capacity and willingness to continue to provide substantial ongoing support to IPIC's operations, and extraordinary support to intervene in a timely manner if the company were to face financial difficulties.

The ratings on the Emirate of Abu Dhabi are supported by the government's very strong asset position, which provides significant financial flexibility; the country's high level of political stability and wealth, underpinned by its rich resource endowment; and by policies that reinforce Abu Dhabi's integration with the global economy. The ratings are constrained by the geopolitical risks that all sovereigns in the region face, the limited disclosure on the government's assets, and increasing contingent liabilities arising from the banking system and the UAE's public sector as a whole.

In terms of stand-alone credit profile, IPIC has a high appetite for acquisitions and sizeable debt funding. Unlike most private-sector holding companies, IPIC's investment policies are very long term and not focused on short-term liquidity or dividend coverage. A key strength of IPIC's portfolio is asset quality, with its most important investments, such as Cepsa, OMV, Borealis, and EDP, seen as having strong credit features. At the same time, exposure to the cyclical downstream sector remains a key risk factor, with refining and petrochemical companies such as Hyundai Oilbank and Nova Chemicals seen as exposed. Although IPIC targets international oil and gas investments, it recently expanded significantly in other sectors through its 71.2% owned subsidiary Aabar. Aabar is a more diversified sub-holding with investments primarily outside the oil and gas sector. While providing diversity, we view Aabar as having a higher risk profile.

IPIC's stand-alone financial profile is viewed as intermediate when factoring in ongoing government support (in terms of repeated capital injections in late 2008 and additional ones expected in the near term, as well as access to liquidity and bank support). That said, IPIC's stand-alone debt leverage is viewed as aggressive, with loan-to-value levels expected to be in the order of 50%. Factoring in IPIC's various recent multi-billion acquisitions, we expect its holding company debt to climb to $9.5 billion in the near term, in addition to sizeable debt at the Aabar sub-holding. Although the pace of IPIC's 2008–2009 acquisitions is viewed as exceptional, we do expect IPIC to remain growth oriented but equally backed by significant government funding.

Outlook

The stable outlook reflects our view that IPIC will remain strategically important and operationally close to the government of Abu Dhabi, and will continue to benefit from substantial ongoing support to its operations. Any lowering in the credit rating on the government of Abu Dhabi, or any indication that the government's commitment to IPIC is weakening, would result in a lower credit rating on the company. A higher rating could result from improvement in the credit quality of the Emirate of Abu Dhabi, to which the underlying credit risk of IPIC is linked.

Kuwait Projects Co. (Holding) K.S.C.

PRIMARY CREDIT ANALYST: ANDREAS KINDAHL, STOCKHOLM (46) 8 440 5907, ANDREAS_KINDAHL@STANDARDANDPOORS.COM

SECONDARY CREDIT ANALYST: MOHAMMED FAYEK, LONDON (44) 20 7176 3408, MOHAMMED_FAYEK@STANDARDANDPOORS.COM

ISSUER CREDIT RATING: BBB+/STABLE/A-2

PUBLICATION DATE: NOVEMBER 28, 2008

Rationale

The ratings on Kuwait-based operating holding company Kuwait Projects Co. (Holding) K.S.C. (KIPCO) primarily reflect the financial flexibility offered by the group's sizable portfolio of listed equity investments and the good average credit quality of its investments. They are constrained by the concentration of the group's investments in Gulf Cooperation Council (GCC) countries and the Kuwaiti financial sector, as well as reduced portfolio liquidity owing to its focus on controlling stakes in its holdings. On Sept. 30, 2008, KIPCO, at a deconsolidated holding company level, had net debt of $575 million (including guaranteed debt at regional satellite pay-TV platform Gulf DTH LDC (Showtime; not rated).

KIPCO is controlled by Al Futtooh Holding Co. K.S.C. (Closed), which is connected to Kuwait's ruling Al Sabah family and has been supportive of KIPCO in the past. The rating incorporates a one-notch uplift from the group's standalone credit risk in accordance with Standard & Poor's Ratings Services' government-related entities criteria.

KIPCO has controlling stakes in:

- Kuwaiti retail and commercial bank Burgan Bank (52.8% effective ownership; BBB+/Stable/A-2);
- Composite insurer Gulf Insurance Co. K.S.C. (GIC; 68.6%; local currency BBB+/Positive/--);
- Universal bank United Gulf Bank B.S.C. (UGB; 88%; not rated); and
- Showtime (78.2%).

KIPCO's investment strategy has gradually changed from a focus on minority, but influential stakes, to achieving majority and controlling stakes in its core holdings. Consequently, the immediate liquidity and diversity of the group's investment portfolio is reduced and KIPCO's credit quality is increasingly dependent on the credit quality of its consolidated core holdings. As a majority shareholder, however, KIPCO has better control over dividend flows from its core holdings. In addition, we believe that KIPCO's holdings will continue to have good growth potential, primarily driven by regional expansion and healthy economic growth in the region. Moreover, some of its investments control listed and highly diverse investment portfolios, adding to the liquidity and diversity of the consolidated group.

Despite drastically falling equity values, KIPCO's financial profile remains relatively strong. On Oct. 23, 2008, net debt (including guaranteed debt for Showtime) represented about 16% of KIPCO's estimated portfolio value, adequately in line with the expectations for the rating (maximum 25%). This is likely to have fallen further since then, however. Because of the extreme uncertainty and volatility plaguing the global equity markets currently, we expect KIPCO to be very restrictive in its investment activity in the near-term, as the company's headroom under the 25% loan-to-value (LTV) rating threshold is diminishing.

SHORT-TERM RATING FACTORS

The 'A-2' short-term rating reflects the satisfactory liquidity and the financial flexibility provided by KIPCO's listed investments. In addition to its listed equity investments, KIPCO held $0.8 billion in cash on its balance sheet and had access to $199 million through committed back up credit facilities and $246 million in money market lines on Sept. 30, 2008. The money market lines and credit facilities all have a maturity of less than one year, however, which is a weakness compared with rated peers. We expect the group to continue to extend its debt maturity profile, including backup credit facilities, in order to minimize refinancing risk.

The group aims to limit debt maturing within 12 months to 20% of total debt. Although the group was slightly above

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Kuwait Projects Co. (Holding) K.S.C. (cont.)

that level on Sept. 30, 2008, it is because of relatively low debt levels and a large bond maturity ($230 million) in November 2008, which has already been refinanced through a $350 million club deal that matures in 2011. The club deal contains financial covenants, under which KIPCO currently has ample headroom, even despite the substantial fall in equity values in the last months.

KIPCO's euro medium-term note program includes a cross-default clause with its core holdings (excluding Showtime), which remains a concern. Currently, potential exposure is primarily with UGB, whose credit quality is deemed to be lower than that of KIPCO, Burgan Bank, and GIC.

Outlook

The stable outlook primarily reflects our expectations that KIPCO will maintain sufficient balance sheet flexibility (LTV below 25%). This is a key rating factor, as choppy equity markets lead to high volatility in the group's asset valuations and asset coverage ratios. We also expect that KIPCO will be very careful and prudent in its investment selection process, to maintain investment portfolio quality.

We expect KIPCO to maintain cash flow coverage of interest and interest plus expenses at minimum levels of 2x and 1.5x, respectively. These ratios were comfortably met as of Sept. 30, 2008.

Upward potential in the ratings is restricted by KIPCO's current exposure to controlling stakes in a few major investments within the financial sector in the GCC region, which constrains portfolio liquidity and diversification.

Downward pressure on the ratings could come from any unexpected changes to the ownership structure of the company, portfolio shifts toward higher-risk investments, or from any breach of the commitment to stay within the 25% LVT ratio.

Mubadala Development Co. PJSC

Primary Credit Analyst: Farouk Soussa, PhD., London (44) 20-7176-7104, farouk_soussa@standardandpoors.com

Secondary Credit Analyst: Andreas Kindahl, Stockholm (46) 8-440-5907, andreas_kindahl@standardandpoors.com

Issuer Credit Rating: AA/Stable/A-1+

Publication date: September 25, 2008

Rationale

The ratings on Mubadala Development Co. PJSC (Mubadala) have been equalized with those on the Government of Abu Dhabi. Although the Abu Dhabi Government has not formally guaranteed Mubadala's liabilities, the group has a high-profile policy role in diversifying the Abu Dhabi economy. This, coupled with Mubadala's operational proximity to the Abu Dhabi government, leads Standard & Poor's to conclude that the government has the capacity and willingness to continue to provide substantial ongoing support to Mubadala's operations, and to intervene in a timely manner if the company were to face financial difficulties.

The ratings on the Emirate of Abu Dhabi are supported by the government's very strong asset position, which provides significant financial flexibility; the country's high level of political stability and wealth, underpinned by its rich resource endowment; and by policies that reinforce Abu Dhabi's integration with the global economy. The ratings are constrained by the geopolitical risks that all sovereigns in the region face, the limited disclosure on the government's assets, and increasing contingent liabilities arising from the banking system and the UAE's public sector as a whole.

Mubadala's stand-alone risk profile benefits from an increasingly diversified business portfolio, ample and stable access to equity capital from the government, and other strong ongoing business support from the Abu Dhabi Government (for example, land grants and project sourcing). Constraints on the group's risk profile include considerable project execution, investment, and operational risks arising from the rapid rate of expansion, concerns for softening local real estate markets, and a weakening economy in the Gulf Cooperation Council (GCC) over the longer term.

Reflecting its core mission and role of developing and diversifying the Abu Dhabi economy, Mubadala's portfolio focuses on the GCC, and Abu Dhabi in particular, and is expanding rapidly. Although it faces significant funding needs as it implements its ambitious investment plan over the coming years, we do not expect the group to find it difficult to raise capital, thanks to its government shareholder.

Outlook

The stable outlook reflects our view that Mubadala will remain strategically important and operationally close to the Government of Abu Dhabi, and will continue to benefit from substantial ongoing support to its operations. Any lowering in the credit rating on the Government of Abu Dhabi, or any indication that the government's commitment to Mubadala is weakening, would result in a lower credit rating on the company. A higher rating could result from improvement in the credit quality of the Emirate of Abu Dhabi, to which the underlying credit risk of Mubadala is linked.

PROJECT FINANCE
CORPORATES
UTILITIES

Nakilat Inc.

PRIMARY CREDIT ANALYST: KARIM NASSIF, LONDON (44) 20 7176 3677, KARIM_NASSIF@STANDARDANDPOORS.COM

SECONDARY CREDIT ANALYST:
ALEXANDRE DE LESTRANGE, PARIS (33) 1 4420 7316, ALEXANDRE_DELESTRANGE@STANDARDANDPOORS.COM

ISSUER CREDIT RATING: A+/STABLE/--

PUBLICATION DATE: APRIL 2, 2009

Rationale

The ratings on Qatar-based Nakilat Inc., the wholly owned liquefied natural gas (LNG) shipping subsidiary of Qatar Gas Transport Co. Ltd. (QGTC), reflect its strategic importance to the State of Qatar (AA-/Stable/A-1+) as a key element in the LNG value chain. Nakilat and QGTC transport the majority of Qatar's LNG. As a result, we analyze Nakilat according to government-related entity (GRE) criteria, using a "top down" approach starting with the sovereign credit rating.

Our long-term rating on Nakilat is one notch lower than that on Qatar. The differential reflects the absence of explicit financial state support in the form of a guarantee or equivalent. However, we do factor in the implicit state support for Nakilat, its ownership, and its critical role in Qatar's LNG chain.

Nakilat was established for the sole purpose of acquiring a fleet of LNG vessels to provide shipping services to four Qatari LNG producers (the charterers). Initially, the fleet was to comprise 27 vessels, but this has been cut to 25.

The corporate credit and long-term debt ratings reflect the following key credit strengths:

- The Qatari government will ultimately determine Nakilat's future and the development of the state's LNG sector as it exercises control through Qatar Petroleum (QP; AA-/Stable/--) over the charterers, Nakilat, and Nakilat's customers. Furthermore, the state aims to have a direct involvement in regasification terminals. Therefore, Nakilat has an indispensable position in Qatar's LNG value chain.
- Time-charter contracts, which are long-term, fixed-price, and availability-based, will likely provide stable revenues for 25 years, underpin future debt service, and mitigate refinancing risk in 2025 on the commercial bank loan. Additional potential refinancing risk in 2019 as a result of new financing to be launched in the coming months should also be somewhat mitigated through the nature of charter contracts.
- Although only one of the four LNG projects that act as a charterer—Ras Laffan Liquefied Natural Gas Co. Ltd. (3)—is rated, the involvement in the charter party of strong sponsors, along with QP, adds strength to the charterers' credit quality. The sponsors include Royal Dutch Shell PLC (AA+/Stable/A-1+), Exxon Mobil Corp. (AAA/Stable/A-1+), and ConocoPhillips (A/Stable/A-1). The charter payments rank nearer the top of the charterers' cash waterfall than payment of the charterers' project debt.
- Nakilat's wholly owned, special purpose companies, each of which owns a single vessel, have entered into fixed-price, turnkey shipbuilding contracts (SBCs) with major Korean shipbuilders, including Hyundai, Samsung, and Daewoo. The SBCs are supported by refund guarantees from highly rated counterparties including Korea Development Bank (foreign currency A/Negative/A-1), Export-Import Bank of Korea (Kexim; foreign currency A/Stable/A-1), and New Hampshire Insurance Co. (A+/Watch Neg/--).

These strengths are offset by the following credit risks:

- Nakilat is wholly dependent on the charterers and their ability to successfully build and operate LNG facilities and manage their exposure, under various contracts, to LNG buyers. Charterer QatarGas 4 (QG4) amended the delivery dates by about two to five months on three vessels. Nevertheless, Nakilat expects full compensation for this delay.
- Nakilat is more highly leveraged than the financing structure of the charterers' underlying projects (although this is typical for shipping finance). The current financial structure carries greater refinancing risk than under the initial financing executed in December 2006. This is due to the increase in size of the commercial bank facility based on the second issuance conducted in July/August 2008. Minimum debt service coverage ratios, including Standard and Poor's assumptions about new financing that the company is contemplating in 2009, are 1.28x for senior debt and 1.15x for total debt, including the level of senior and subordinated debt service to total cash available for debt service for the life of the transaction.
- Charter revenues are susceptible to deductions for off-hire periods. In addition, political risk associated with the Gulf region could affect LNG supply across the chain.

- Qatari bankruptcy law is only just being developed and remains untested, although it should be relatively easy to enforce the mortgages over the vessels in other territories' waters.

Key business and profitability developments

In August 2008, Nakilat raised $1.5 billion of debt under its existing financing program for the second stage of its LNG shipbuilding plan. This involves the construction of nine additional vessels, bringing the total fleet to 25. However, no bond financing was raised as had been originally anticipated. Therefore, the company has a funding requirement of approximately $940 million by the end of June 2010 to cover the completion of all 25 vessels by that time.

Based on recent discussions with the company, we understand that the $940 million financing requirement is now likely to be raised through a mixture of senior and subordinated debt in one or more tranches, one of which may be shariah-compliant. We believe that the company is in discussions with financing parties regarding its third tranche of debt. We expect financial close on this tranche by the end of May 2009.

On a stand-alone basis (that is, ignoring the potential for extraordinary government support), we consider that Nakilat's creditworthiness would be in the high speculative-grade category. This reflects the company's strong business characteristics and its aggressive financial profile. Nakilat's business profile is underpinned by its strategic role in LNG, its availability-based payment mechanism, strong sponsors and charterers, and shipbuilding contracting arrangements. These strengths are partially offset by Nakilat's exposure to business risk at QGTC, uncertainty over security enforcement, and some comparative weaknesses in the secured debt structure, such as covenants in force in the event of a default. Nakilat's aggressive financial profile is underpinned by weak liquidity, high leverage, and high refinancing exposure, although this is partly offset by strong hedging arrangements and the resilience of cash flows under a variety of operational stresses.

Key cash flow and capital-structure developments

Nakilat's financial structure is akin to those typically seen in a project financing. The initial years are characterized by significant capital outlays while the LNG vessels are built.

Liquidity

We consider Nakilat's liquidity to be weak, given the remaining committed capital expenditure for 2009 of approximately US$1.2 billion. On Feb. 17, 2009, Nakilat had drawn US$5.15 billion of its US$5.76 billion committed funding in place. Based on Nakilat's contractor payment profile, the company is likely to have fully utilized its committed facilities by end-June 2009.

Between July 1 and Dec. 31, 2009, the company will need to make contractor payments of about US$510 million, with approximately US$382 million falling due in the fourth quarter. This indicates that Nakilat needs to arrange additional funding of US$510 million to US$560 million by the end of June 2009 to cover its obligations for the year.

A failure to raise new funding could result in a deferral of the vessel construction program. This could result in a breach of the company's contractual obligation to the Korean shipyards and its charterers and, consequently, delay the receipt of operational revenues. However, we consider this scenario unlikely, given Nakilat's success in raising significant bank financing in 2008 and its strategic importance to the Qatari state. We will monitor the agreement of the new facilities, which are expected in May 2009. In the event that these are not agreed, we believe that additional support from QGTC and/or the State of Qatar would be provided in a timely and sufficient manner to ensure adequate liquidity for Nakilat over the ensuing seven to eight months. Contractor payments of about US$200 million due between Jan. 1 and July 31, 2010, are likely to be funded through subsequent debt issues.

Outlook

The stable outlook reflects our view that Nakilat remains a pivotal element in Qatar's strategy to develop its LNG sector and that, in the event of financial distress, the Qatari government would provide timely support for Nakilat's debt. We expect Nakilat's liquidity situation to improve by May 2009, through funding from external sources or from QGTC and/or the State of Qatar. If Nakilat were unable to improve its liquidity by May we could review our rating approach, which could have negative implications for the ratings. Ultimately, the ratings continue to be underpinned by the credit quality of the sovereign and its national LNG sector strategy.

PROJECT FINANCE
CORPORATES
UTILITIES

National Central Cooling Co.

PRIMARY CREDIT ANALYST: KARIM NASSIF, LONDON (44) 20 7176 3677, KARIM_NASSIF@STANDARDANDPOORS.COM

SECONDARY CREDIT ANALYST:
ALEXANDRE DE LESTRANGE, PARIS (33) 1 4420 7316, ALEXANDRE_DELESTRANGE@STANDARDANDPOORS.COM

ISSUER CREDIT RATING: BB/DEVELOPING/--

PUBLICATION DATE: MARCH 23, 2009

Rationale

The rating on Abu Dhabi-based National Central Cooling Co. PJSC (Tabreed) reflects the company's dominant position in district cooling in the United Arab Emirates (UAE); a revenue stream based on stable long-term contracts; a strong need for the company's product; and ongoing support from, and increased ownership by, UAE government entities. These credit strengths are offset by Tabreed's highly leveraged financial profile, characterized by its weak liquidity in the face of significant refinancing requirements in 2009 and projected negative free cash flows beyond 2010. The ongoing construction risk of developing new cooling plant capacity, and the weaker-than-anticipated performance of the Cooling business also weaken the company's credit profile.

Standard & Poor's Ratings Services uses its criteria for government-related entities (GREs) to determine the corporate credit rating on the company. (For further details see the article titled "Rating Government-Related Entities: A Primer," published on RatingsDirect on June 14, 2006.) This bottom-up analysis results in a one-notch uplift to the rating as a result of the potential extraordinary government support available to Tabreed. On a stand-alone basis, without any extraordinary support from the Emirate of Abu Dhabi (AA/Stable/A-1+), Tabreed's rating is 'BB-'.

We continue to consider the potential for additional notches for government support. This could occur, for example, if the Abu Dhabi-owned investment company, Mubadala Development Co. PJSC (AA/Stable/A-1+) and/or the Abu Dhabi government are willing to extend more explicit and timely financial support for Tabreed, particularly in relation to the company's liquidity needs.

In part, Tabreed's highly leveraged financial profile is the result of a significant capital expenditure program over the short term (about UAE dirham (AED) 2.3 billion in 2009 alone), relative to expected operating cash flows of about AED400 million to AED420 million in 2009.

Tabreed's operating cash flows over the first two months of 2009 were supplemented by capital expenditure reimbursement payments from joint venture partners of about AED400 million. These, in tandem with a nine-month $35 million working capital facility signed at the end of December 2008 have funded capital expenditures and debt service over the first two months of the year. Tabreed's base case for 2009 incorporates no additional revenue from asset sales to joint ventures or any other parties. Furthermore, for the company to continue to meet 2009 capital expenditures it will need to secure additional funds of about AED1.5 billion from external sources. Tabreed expects to finalize a medium-term facility of AED1.5 billion by April 2009.

The company successfully refinanced its AED367 million 2004 sukuk, which was due on March 2, 2009. This was achieved predominantly through a two-year AED368 million unsecured ijara sukuk issuance. The refinancing facility, which was signed at the end of February 2009, has similar financial covenants to Tabreed's other financing agreements.

Liquidity

We consider Tabreed's liquidity position to be very weak, reflecting a progressive decline over the past year, mainly as a result of the company's significant capital expenditures. On Feb. 28, 2009, Tabreed had an unaudited cash balance of AED285 million (down from AED697 million on Dec. 31, 2008). The company expects to generate about AED400 million of operating cash flows during the full year 2009 (excluding capital reimbursement amounts from joint ventures). As of Feb. 28, 2009, Tabreed had fully utilized all its committed facilities.

The company will have to make coupon payments of AED124 million in May under its Tabreed 2008 convertible and has a repayment obligation of $35 million (AED149 million) in respect of the previously mentioned facility.

If Tabreed were to fail to issue the AED1.5 billion facility in time, this could lead to uncertainty over its ability to meet contractual payments to contractors and threaten the company's ability to meet its debt service obligations in the coming months.

Assuming the successful issuance of this facility, we anticipate that net month-end cash balances will be close to zero from the end of May to the end of December 2009. Tabreed expects drawings under the planned facility to commence in May 2009 and to be spread in roughly equal amounts for the remainder of the year.

We understand that Tabreed is also in discussions with its existing banking partners for further lines of financing and liquidity.

We consider Tabreed's recent success in obtaining credit lines to meet its Sukuk 2004 obligation, and clarity in identifying financing needs for the remainder of the year, as positive first steps toward meeting the company's liquidity requirements in 2009. However, Tabreed remains in a very difficult position at this point.

Outlook

The developing outlook reflects a number of uncertainties, such as the potential sale of assets to the Aldar/Tabreed joint venture, the relative success of obtaining additional medium-term committed facilities in the very short term, and the effect of any revised business model implemented during the year. A downgrade could occur if Tabreed were unable to obtain the necessary AED1.5 billion medium-term financing by mid-April 2009, or if our assessment of the company's liquidity position in mid-April leaves us uncertain as to whether it will be able to finance its debt obligations that fall due in the coming months.

The scope for an upgrade resulting from an improvement in operating performance is limited in the short term. However, further tangible evidence of timely government support could lead us to consider a further one-notch uplift for government support.

We understand that Tabreed is still considering a new business model. Under this model, the company would create a new asset holding company, into which it would divest existing and future cooling assets. We will continue to monitor the potential effect of the implementation of any new model on the ratings.



PROJECT FINANCE
CORPORATES
UTILITIES

Oman Power and Water Procurement Co. SAOC

PRIMARY CREDIT ANALYST: MARK J DAVIDSON, LONDON (44) 20 7176 6306, MARK_J_DAVIDSON@STANDARDANDPOORS.COM

SECONDARY CREDIT ANALYST: FAROUK SOUSSA, PHD., DUBAI (971) 4709 6820, FAROUK_SOUSSA@STANDARDANDPOORS.COM

ISSUER CREDIT RATING: A/STABLE/--

PUBLICATION DATE: MARCH 12, 2009

Rationale

The ratings on regulated procurement and supply company Oman Power and Water Procurement Co. SAOC (OPWP) are equalized with the ratings on the Sultanate of Oman (A/Stable/A-1), reflecting Standard & Poor's Ratings Services' opinion that the likelihood of extraordinary government support is extremely high. This opinion is supported by OPWP's unique and strategically important role as the sole bulk buyer and bulk seller of electricity and related desalinated water in Oman, and its 100% ownership by the Sultanate of Oman through the Ministry of Finance and the Electricity Holding Co. SAOC (EHC).

These strengths are modestly offset by the relatively new and untested regulatory framework, which has only been in place since 2005, and over the longer term, the increase in counterparty risk as Oman's distribution companies are privatized.

Standard & Poor's analyzes OPWP using the criteria for government-related entities and views the company as a public-policy-based entity benefiting from implicit and explicit government support. OPWP must remain wholly owned by the government indefinitely, under Article (14) of the Law for the Regulation and Privatization of the Electricity and Related Water Sector (Sector Law). OPWP's obligations are not explicitly guaranteed, but under Article (67) of the Sector Law, the Ministry of Finance must provide adequate finance to enable OPWP to undertake its operations. Therefore, the rating on OPWP is equalized with that on the Sultanate of Oman to reflect this. In addition, OPWP benefits from ongoing support from EHC, which provides it with liquidity support and accounting services.

Business and profitability

OPWP's revenues are fully regulated by Oman's Authority for Electricity Regulation, under a transparent cost-recovery tariff that allows full pass-through of procurement costs under normal circumstances. The authority is required to give OPWP at least 10 years' notice if it wishes to terminate the company's license.

OPWP publishes financial statements once a year. Given its public policy role, profitability is not a core objective for the company. In the year ending Dec. 31, 2007, OPWP reported revenues of Omani rial (OMR) 214 million ($556 million), which mainly comprised regulated bulk supply tariffs from customers in electricity and desalinated water. These revenues were closely offset by capacity and output costs, and administrative expenses, to result in a net profit of OMR1.3 million.

Cash flow and credit ratios

OPWP's credit protection measures are strong. The company has a short-term balance sheet, dominated by accounts payable and receivable, reflecting procurement costs from generators and desalinators, and receivables from electricity suppliers and water departments. OPWP itself has no production facilities and is in fact prohibited under the terms of its license from engaging in the generation of electricity and/or the desalination of water. OPWP requires no external long-term debt financing, which results in very strong credit ratios.

Liquidity

OPWP has a strong liquidity position. The company incurs no capital expenditure and has no long-term debt; demand on its liquidity arises mainly from timing differences between payments to generators and desalinators and receipts from electricity suppliers and water suppliers. OPWP also has a seasonal pattern of cash flows as tariffs increase significantly in the summer months. These working capital needs are usually covered by existing cash balances and short-term funding from EHC, but in addition OPWP also has access to an OMR10 million ($26 million) overdraft facility from BankMuscat S.A.O.G. (BBB+/Stable/A-2), which is sparingly used. The facility expires in September 2009, but we are of the opinion it will be renewed.

Outlook

The stable outlook factors in continued strong implicit and explicit support from the Sultanate of Oman. It also takes into account our expectation that the tariff regime will remain supportive and that OPWP will not engage in any nonregulated activities without approval from the Authority for Electricity Regulation.

A change in rating or outlook on OPWP would likely result from a change in the rating or outlook on the Sultanate of Oman. Similarly, any change in the relationship between OPWP and the sovereign or in OPWP's singular policy-based mandate could have negative rating implications.

Qatar Fertiliser Co. (S.A.Q.)

PRIMARY CREDIT ANALYST: SOPHIA DEDEMADIS, LONDON (44) 20 7176 7013, SOPHIA_DEDEMADIS@STANDARDANDPOORS.COM

SECONDARY CREDIT ANALYST: TOBIAS MOCK, CFA, FRANKFURT (49) 69 33 999 126, TOBIAS_MOCK@STANDARDANDPOORS.COM

ISSUER CREDIT RATING: A+/STABLE/--

PUBLICATION DATE: NOVEMBER 10, 2008

Rationale

The rating on Qatar-based fertilizer producer Qatar Fertiliser Co. (S.A.Q.) (QAFCO) reflects the strong ongoing support provided to QAFCO by its majority owner, the State of Qatar (AA-/Stable/A-1+). The rating reflects the company's favorable cost position—underpinned by low feedstock prices obtained from Qatar Petroleum (QP; AA-/Stable/--)—and strong financial profile. QAFCO also benefits from an integrated, strategically located facility that allows access to Asian and African markets and ensures significant economies of scale.

The government of Qatar owns 53% of the company via QP and the holding company Industries Qatar. Standard & Poor's Ratings Services considers QAFCO to be a government-related entity (GRE). Accordingly, we apply a two-notch rating uplift to the stand-alone rating of 'A-' under our bottom-up approach, reflecting our expectation that the state would provide extraordinary support if required.

The rating is constrained by QAFCO's relative scale versus its peers. The company has low product diversification, does not own a global distribution network, and focuses its production on a single site. It is also subject to the price cyclicality of the global commodity market for nitrogen-based fertilizers.

For the nine months ended Sept. 30, 2008, QAFCO posted revenues of Qatari riyal (QAR) 5.2 billion, which was ahead of projections, with margins remaining high at close to 80%. Throughout the period, the company was able to benefit from strong nitrogen fertilizer prices—specifically urea. Despite the recent reduction in nitrogen fertilizer prices at the beginning of the fourth quarter, the underlying characteristics of the agrochemicals industry are expected to remain favorable until 2010-2011. At that time, a significant increase in capacity—including that of QAFCO—is planned to come on line.

Construction of the company's planned capacity increase, "QAFCO-5 train," remains on schedule and is expected to become operational in 2011. QAFCO has a firm lump-sum contract for this project, thereby mitigating the risk of cost overruns. Once complete, the company estimates that QAFCO-5 will increase its overall capacity by more than 50%.

LIQUIITY

Liquidity remains strong. At Sept. 30, 2008, on-balance-sheet cash totaled QAR4.8 billion, compared with QAR1.0 billion of long-term debt. Furthermore, robust cash flows offset significant fluctuations in working capital that result from the seasonality of the industry. QAFCO's already impressive cash flow generation has benefited significantly from the high prices of urea.

The company continues to maintain a very conservative financial policy, so we expect that the additional cash flows will be applied toward the buildout of QAFCO-5, therefore reducing the use of the term debt facility. As part of the fifth train buildout, QAFCO has put in place a $500 million revolving credit facility to provide additional liquidity if necessary. However, we expect this facility to remain undrawn during the expansion phase.

Outlook

The stable outlook reflects our expectation that QAFCO will maintain its satisfactory business risk profile, supported by continued strong funds from operations generation. Additionally, we expect QAFCO to sustain financial credit protection ratios in line with a modest risk profile with FFO/debt of over 45% and total debt to capital below 35% throughout the investment phase of the expansion of its production plant.

A failure to execute the business plan due to an unforeseen sustained weakness in urea pricing or delays in the QAFCO-5 buildout could result in downward pressure on the rating. We do not consider that QAFCO's close links with the State of Qatar are likely to change in the foreseeable future. Equally, we do not see major drivers of upward rating movement at present.

PROJECT FINANCE
CORPORATES
UTILITIES

Qatar Petroleum

PRIMARY CREDIT ANALYST: LUC MARCHAND, LONDON (44) 20 7176 7111, LUC_MARCHAND@STANDARDANDPOORS.COM

SECONDARY CREDIT ANALYST: FAROUK SOUSSA, PHD., LONDON (44) 20 7176 7104, FAROUK_SOUSSA@STANDARDANDPOORS.COM

ISSUER CREDIT RATING: AA-/STABLE/--

PUBLICATION DATE: FEBRUARY 16, 2009

Rationale

The 'AA-' long-term foreign currency issuer credit rating on Qatar Petroleum (QP), Qatar's national oil and gas company, reflects the ratings on the State of Qatar (AA-/Stable/A-1+), its sole shareholder. The long-term foreign currency ratings on the two entities are equalized in view of QP's close links with the government and its strategic importance to the national economy.

The rating on QP reflects its key role in the government of Qatar's development plans. In addition, the government has placed key ministers at the top of QP's management structure. QP is the most important contributor to Qatar's economy and state budget, with oil and gas revenues, mostly raised from QP, comprising about 70% of total general government revenues for fiscal 2007–2008 (ended March 31, 2008). One of the main strategic development targets of the government is to expand the oil, gas, and petrochemical sectors that are QP's main areas of production and export. Furthermore, QP has a cash-call account with the Ministry of Finance and its balance can go either way, thereby shifting liquidity from one entity to the other. Nevertheless, QP has its own accounts, which are separate from the state budget and are audited and published.

In 2007, QP produced about 850,000 barrels per day (bpd) of crude oil, while liquefied natural gas (LNG) exports (including the share of minorities) rose to 27.8 million metric tons. The company is in the middle of a massive investment program, as Qatar is seeking to expand its LNG exports to 77.4 million metric tons by 2011.

QP's overall revenues are highly sensitive to oil price fluctuations, as the bulk of LNG pricing is linked to oil prices (and in the future will be linked to some spot gas market pricing). Sales revenues increased in 2007 by 16.6%, after a 32.8% increase in 2006, mainly due to favorable crude oil prices. Reflecting this pick-up in sales, and despite a 38.2% increase in operational expenses, adjusted EBITDA increased by 35.5% in 2007 from its 2006 level. With higher interest payment expenditures, adjusted EBIT interest coverage (excluding non-recourse debt) decreased to 28.4x, from 34.4x in 2006. Due to significant borrowing expected in 2008-2009 to increase capacity in the production of oil, gas, and gas-related products, leverage will continue to rise, raising interest payments. However, this will be more than balanced by much higher LNG exports expected in 2008–2009.

Over the past few years, QP and its subsidiaries and joint ventures have incurred significant debts to finance the development and expansion of LNG and other projects. The company's consolidated debt figures reflect the sum of its pro-rata shares in the various subsidiaries and joint ventures. Recently, QP increased its consolidated debt (recourse and non-recourse) to slightly more than $15.6 billion at year-end 2007, from $11.4 billion in 2006. On the basis of current loan commitments, loan repayments due in 2008 are expected to be $0.7 billion. The company's cash increased to a comfortable $8.5 billion at year-end 2007, from $6.4 billion at year-end 2006.

The increase in debt in the past few years is balanced by the $4.1 billion increase in book equity in 2005, and the fact that a significant share of QP's debt is non-recourse (about 43.0% in 2007), with this share expected to increase further in the next few years. As a result, QP's adjusted total debt (excluding non-recourse debt) to capital increased in 2005–2007 but remained at a reasonable 35.7% in 2007, compared to 21.6% in 2005. Assuming a decrease in recourse debt in the next few years and the same level of capital in 2008–2012, adjusted total debt to capital would decrease to about 34.0% in 2012 from the 40% expected in 2008.

Outlook

The stable outlook on QP mirrors that on the State of Qatar. It also assumes the continuation of a prudent financial policy regarding leverage and reinvestment of the current revenues windfall. For the foreseeable future, no changes are expected in the policy and institutional framework that would weaken the company's significant role in the government's development plans, or in its crucial importance for both the budget and the economy.

The current favorable hydrocarbon pricing environment should help fund QP's heavy capital expenditures in the coming years. As a result, Standard & Poor's Ratings Services expects increases in net debt to be gradual and limited, while future cash flow generation will benefit from the forecast jump in LNG exports. We therefore expect credit ratios to remain strong in the future, even if prices moderate over the medium term.

Qatar Telecom (Qtel) Q.S.C.

PRIMARY CREDIT ANALYST: MICHAEL O'BRIEN, LONDON (44) 20 7176 3561, MICHAEL_OBRIEN@STANDARDANDPOORS.COM

SECONDARY CREDIT ANALYST: SIMON REDMOND, LONDON (44) 20 7176 3683, SIMON_REDMOND@STANDARDANDPOORS.COM

ISSUER CREDIT RATING: A-/STABLE/A-2

PUBLICATION DATE: JANUARY 27, 2009

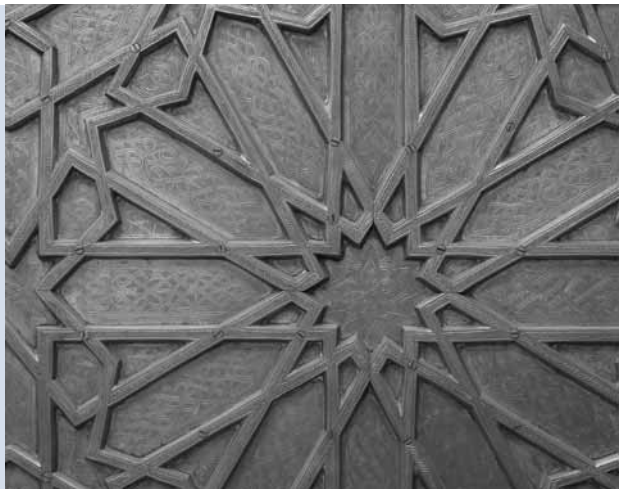
Rationale

The ratings on Qatar Telecom (Qtel) Q.S.C., the incumbent fixed-line and mobile telecommunications operator in the State of Qatar (AA-/Stable/A-1+) are supported by Qtel's current monopoly market position and strong cash flow generation in fixed and mobile telephony in the Qatari telecoms market, despite upcoming competition in 2009 from Vodafone Qatar, a subsidiary of Vodafone Group PLC (A-/Stable/A-2). We expect continuing population growth in Qatar to drive demand for telecoms services while competition is introduced. Qtel's profitability is strong, with an adjusted consolidated EBITDA margin of 46.5% in the 12 months ended Sept. 30, 2008. Ratings support also comes from international diversification in 16 countries, covering: established operations in neighboring Gulf Cooperation Council (GCC) countries including Kuwait and Oman; and riskier emerging markets such as Indonesia, Iraq, Algeria, and Tunisia. We expect overseas assets to contribute to the bulk of Qtel's consolidated cash flows in future, due to the size of the respective markets. The ratings also factor in implicit state support (Qtel is 68% owned by the Qatari government and government-related entities), given that the government has not advocated a significant liberalization of the market to date and strategically assists Qtel in developing abroad.

We recognize Qtel's strategic importance to the state as a provider of key communications infrastructure and as a flagship national company. The state has also provided tangible financial support to Qtel, most recently via its participation in Qtel's Qatari riyal (QAR) 5.86 billion ($1.6 billion) rights issue in June 2008 to help fund acquisitions. As a result, the corporate credit rating includes a two-notch uplift from our stand-alone rating assessment.

The ratings are constrained by the company's relatively high leverage. In line with its board-approved maximum leverage policy of 3.5x consolidated net debt to EBITDA, which provides headroom in relation to bank loan covenants, Qtel has

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Qatar Telecom (Qtel) Q.S.C. (continued)

relied on debt financing to fund its rapid overseas expansion more heavily than regional peers such as Emirates Telecommunications Corp. (Etisalat; A+/Stable/A-1) and Saudi Telecom Co. (foreign currency: A+/Stable/A-1). This is due to the relatively lower amount of cash flow support available from its domestic market, which has a low (1.5 million) but growing population to fund Qtel's emerging market growth. At Sept. 30, 2008, consolidated debt (adjusted by Standard & Poor's for leases, guarantees, and letters of credit) was QAR29.8 billion, compared with QAR1.0 billion at the end of 2006.

Based on the current capital structure, adjusted debt to EBITDA for the 12 months to Sept. 30, 2008, was 3.6x, and adjusted free operating cash flow (FOCF) to debt was 3.0%, contributing to intermediate financial risk. Leverage on a proportionate consolidated basis is more than 4.0x, and significantly higher at the parent company level (about 6.0x), where the bulk of consolidated debt is located. Considerable dividend leakage weighs on the consolidated figures due to Qtel's current 40.8% stake in PT Indosat Tbk. (Indosat; BB/Stable/--) and its 51% stake in National Mobile Telecommunications Co. K.S.C. (Wataniya Telecom), which holds several of Qtel's large overseas assets.

Additional constraints on the ratings include a cross-default clause to material subsidiaries included in Qtel's bank loan documentation that could provide an incentive for the company to ensure that no default occurs in its large emerging market assets, including Indosat. Exposure to varied country risks, significant competitive pressure outside of its domestic market, and uncertainty over the effects of potential future mergers and acquisitions (M&A) activity also weigh on the ratings, although we expect consolidated leverage to decrease over time.

Liquidity

The 'A-2' short-term rating is supported by Qtel's adequate liquidity. At Sept. 30, 2008, liquidity resources included consolidated bank balances and cash of QAR7.1 billion, of which approximately 35% was at the parent company level in Qatar. The company also had QAR3.9 billion ($1.1 billion) of committed undrawn facilities, of which QAR2.6 billion was available at Qtel in Qatar.

Qtel's short-term debt maturities totaled QAR1.7 billion at Sept. 30, 2008, and the group will need to refinance a $2 billion credit facility at the end of 2009. Other cash outgoings in the coming months relate to the potential purchase of an incremental 25% stake in Indosat, for which the company currently has sufficient funds. In addition, dividends of QAR1.5 billion—100% of the nominal share value—will be paid during 2009 on the 2008 results. Qtel will likely need to refinance at least some of its $2 billion debt due at year-end 2009 to maintain adequate liquidity headroom.

We expect FOCF generation to remain an important source of financing. However, FOCF might not be sufficient if Qtel were to undertake large acquisitions or other corporate activities while continuing to pay substantial dividends and royalties. In this case, we would expect Qtel to fund its requirements by issuing new debt, or co-invest with other parties. The public listing of stakes in Indosat and Wataniya Telecom increases their liquidity and Qtel's ability to monetize them in any eventual sale.

Outlook

The stable outlook reflects our expectation that Qtel will remain committed to its financial policy and that FOCF generation in its domestic business will remain robust in the face of any market changes, including increased competition or further liberalization. We also expect the risk profile of its emerging market assets to moderate over time and to provide increasing cash flows to Qtel.

We expect consolidated adjusted funds from operations to debt to improve to more than 25% and adjusted consolidated debt to EBITDA to move toward and remain within the 2x-3x range. Any weakening in these metrics would need to be temporary to avoid pressure on the ratings. Qtel currently has relatively limited headroom to increase leverage above existing levels, and a substantial increase would need to be temporary in nature.

A more accelerated growth plan or company transformation through acquisition—accompanied by a more aggressive financial policy or a substantial negative effect on financial performance as a result of unforeseen regulatory decisions or materialization of country risks—could negatively affect the ratings. Upside is not anticipated at this stage, given the risks and dynamics associated with the telecoms industry and the company's willingness to increase leverage for potential foreign acquisitions in emerging markets.

Ras Laffan Liquefied Natural Gas Co. Ltd.

PRIMARY CREDIT ANALYST: ALEXANDRE DE LESTRANGE, PARIS (33) 1 4420 7316, ALEXANDRE_DELESTRANGE@STANDARDANDPOORS.COM

SECONDARY CREDIT ANALYST: KARIM NASSIF, LONDON (44) 20 7176 3677, KARIM_NASSIF@STANDARDANDPOORS.COM

SENIOR SECURED DEBT RATING: A/STABLE

PUBLICATION DATE: MAY 4, 2009

Rationale

The ratings on Qatar-based liquefied natural gas (LNG) facility operator Ras Laffan Liquefied Natural Gas Co. Ltd. reflect the project's strong commercial position, with a 25-year take-or-pay sale and purchase agreement with Korea Gas Corp. (Kogas, A-/Stable/--) for up to 4.92 million tons per annum (mmtpa) of LNG (out of an annual capacity of about 6.6 mmtpa). Also supportive are Ras Laffan's position as one of the world's lowest-cost sources of LNG; its commercially proven production technology, which is used without any significant operating problems; that an offshore New York State trustee receives all revenues from Kogas and others in U.S. dollars, and pays all expenses, debt service, and equity distributions; access to Qatar Petroleum's (QP; AA-/Stable/--) North Field's gas field, which ensures that the project will not confront gas reserve depletion risk; and the project's high debt service coverage ratios (DSCRs).

These strengths are offset by potential long-term market and commodity price uncertainty and the possibility that Kogas, the project's sole contractual long-term LNG offtaker, could legally defer LNG shipments up to 10% of annual contract quantity in total. Other negative rating factors include the possibility that conflict in the Middle East could temporarily impair LNG production and deliveries beyond six months, the period that the debt service reserve fund covers, and that heightened awareness over potential security threats has reduced the amount of insurance coverage that Ras Laffan can secure to $500 million for terrorism and sabotage damage to its onshore facilities.

KEY BUSINESS AND PROFITABILITY DEVELOPMENTS

During 2008, Ras Laffan achieved production of 6.72 million tons of LNG, less than in 2007 due to planned shutdowns during the year. The project continued to experience very strong demand for its products and this, combined with record oil prices (with an average of $102 per barrel) resulted in record revenues and profitability.

The project posted an operating profit of $4.6 billion in 2008, up 49% over 2007 on net sales of $6.57 billion (up 40%), including the delivery of 107 LNG cargoes.

The project's budget for 2009 assumes an average price of $68.67 per barrel, well above our assumptions of $40, and the sale of 113 LNG cargoes in 2009 of which 79 under the Kogas GSPA (gas sale and purchase agreement). We understand that over the first quarter of 2009, sales were made on an average barrel price in the upper part of the $40-$50 range, while the project was able to sell its entire output (LNG as well as condensate, sulfur, and other by-products).

While the outlook remains unclear for the rest of 2009, we believe the project is in a solid position to withstand prolonged depressed prices and low volumes as we understand it benefits from long-term contracts, a diversified destination and product mix, and a very low breakeven price (about $10 per barrel).

KEY CASH FLOW AND CAPITAL-STRUCTURE DEVELOPMENTS

The project's operating cash flow available for debt service (after capital expenditures) reached a record $4.76 billion compared to an annual debt service of about $214 million.

Ras Laffan's excellent financial performance has exceeded pro forma numbers during the past three years. DSCRs as per the documentation were about 9.8x in 2006, 15.6x in 2007, and 24x in 2008. If calculated according to our criteria these ratios would be marginally lower, as we consider cash flow after capital expenditures available for debt service (for instance, for 2008 the ratio calculated that way would be 23.7x).

The expected shortfall in revenues in 2009 will lead to reduced cash flow available for debt service. However, we expect the DSCR to remain strong and above 5x in 2009 under our average price assumption. Operating expenditures are predominantly comprised of royalties, which are indexed to international crude oil prices, while debt service obligations will be moderately up, at a forecast $282 million in 2009, reflecting the September 2009 $80 million first of a series of 10 equal semiannual payments on the $800 million bond maturing in 2014.

Outlook

The continuing solid financial and operational performance of Ras Laffan, favorable Korean and global LNG demand fundamentals, Exxon Mobil's $200 million contingent price support, and deepening sponsor commitment to QP's LNG development all support a stable outlook.

We could lower the rating if Korean LNG demand falls to a level that would suggest a material reduction in purchase volumes from Kogas, or if operational performance or global LNG markets deteriorate to the extent that cash flows envisioned from third-party sales do not occur. Opportunities for upgrades are limited, given the exposure of project cash flow to oil price uncertainty and, to a lesser degree, to spot markets.

PROJECT FINANCE
CORPORATES
UTILITIES

Ras Laffan Liquefied Natural Gas Co. Ltd. (II)

PRIMARY CREDIT ANALYST: KARIM NASSIF, LONDON (44) 20 7176 3677, KARIM_NASSIF@STANDARDANDPOORS.COM

SECONDARY CREDIT ANALYSTS:
ALEXANDRE DE LESTRANGE, PARIS (33) 1 4420 7316, ALEXANDRE_DELESTRANGE@STANDARDANDPOORS.COM
JONATHAN MANLEY, LONDON (44) 20 7176 3952, JONATHAN_MANLEY@STANDARDANDPOORS.COM

SENIOR SECURED DEBT RATING: A/STABLE

PUBLICATION DATE: SEPTEMBER 15, 2008

Rationale

The $1.4 billion senior secured Series A bonds due 2020 and $850 million Series B bonds due 2027, issued by Qatar-based Ras Laffan Liquefied Natural Gas Co. Ltd. (II) (RasGas II) and Ras Laffan Liquefied Natural Gas Co. Ltd. (3) (RasGas 3) (together RasGas) are rated 'A'. The $1.55 billion senior secured bonds issued by RasGas 3 (comprising $750 million Series C bonds due 2016 and $800 million Series D bonds due 2027) are also rated 'A'. The outlooks on all ratings are stable.

The debt is being used to finance the design, construction, and operation of five liquefied natural gas (LNG) facilities (trains) in the State of Qatar (AA-/Stable/A-1+). Standard & Poor's Ratings Services analyses RasGas on a stand-alone basis using its project finance criteria.

The 'A' rating reflects the following credit weaknesses:

- LNG revenues are potentially volatile, owing to price links between LNG sale and purchase agreements (SPA) from RasGas and global oil-price benchmarks (and some European gas benchmarks).
- Counterparty risk exposure is high given that many SPA counterparties have lower credit quality than RasGas. The group relies on third parties and the project sponsors to complete large infrastructure projects to support LNG sales.
- RasGas has seen some small slippages in the construction program for trains 6 and 7. These delays have largely been attributed to resource constraints resulting from the overheated Middle East construction market as well as some procurement delays.
- RasGas II will be exposed to indemnity payments and will continue to be dependent on the spot LNG market sales if the Adriatic terminal in Italy, which supports an SPA with Edison SpA (BBB+/Stable/A-2), is not completed by mid-2009. Commercial operations on the Adriatic terminal are expected to commence in the first quarter of 2009.
- Market risk stems from the lack of a finalized executed SPA with an affiliate of Exxon Mobil Corp. (AAA/Stable/A-1+) for the remaining output of trains 6 and 7.
- There remains the threat of a conflict in the Middle East that could disrupt LNG production and delay deliveries beyond six months—the period for which the debt service reserve could be used to meet debt obligations. This risk is, however, largely compensated by cash flows available at the central government level (net assets are estimated at 72.2% of GDP in 2008) and at Qatar Petroleum (QP {AA-/Stable/--}; funds from operations of $7.8 billion at the end of 2007), as well as operating cash flows at the RasGas level.

The following credit strengths offset the above weaknesses at the 'A' rating level:

- Sales volume risk is largely eliminated by the presence of long-term SPAs, which cover the majority of production from trains 3, 4, and 5.
- Sponsor support is strong. The RasGas expansion is likely to generate a high proportion of income at QP from 2010 (coinciding with completion of trains 6 and 7), and will represent a significant proportion of Exxon Mobil's total share in Qatari projects.
- Construction risk for the onshore and offshore packages of RasGas has been reduced through the project's use of fixed-price, date-certain engineering, procurement, and construction arrangements.
- There is good product revenue diversification, with about 67% of revenues coming from LNG sales and about 33% coming from LNG by-products. In addition, there is good geographic diversity of revenues in markets.
- RasGas has a competitive cost structure, which results in forecast debt service coverage ratios (DSCR) greater than 3x under most stress scenarios.
- Shipping availability risk is low, as sufficient shipbuilding capacity has been secured from experienced South Korean yards to meet delivery requirements under existing and expected ex-ship SPAs.
- Technological and operational risks are relatively low for trains 6 and 7 as they represent an extension of similar technology and design employed on trains 3, 4, and 5

despite the fact that these will represent some of the largest trains employed worldwide. In addition, trains 3, 4, and 5 are already operating in line with, or are exceeding, the sponsors' expectations.

Year-end results for financial 2007 show revenues at $6.6 billion, up 44% on the previous financial year, and profit before taxes at $3.3 billion, up by 46% year on year. As a result, the project recorded DSCRs of 9.2x for 2007. This better-than-expected performance was driven mainly by higher global oil prices and a buoyant market for sales of condensate and other by-products. The (unaudited) financial results for the six months to end-June 2008 also point to strong growth in revenues compared with the same period the previous year.

Construction costs associated with trains 6 and 7 are broadly in line with the 2007 business plan forecasts, although there have been small reported slippages in the construction schedule. We expect these delays to have a limited effect on RasGas' medium-term financial profile. We will, however, continue to monitor construction progress and any business or financial impact the delays could have on the RasGas project.

Recovery analysis

The senior secured bonds issued by RasGas II and RasGas 3 have a recovery rating of '1', indicating Standard & Poor's expectation of very high (90%-100%) recovery of principal in the event of a payment default. To date, there has been limited experience regarding default, loss, or recovery in this sector and in Qatar.

For the full recovery analysis, please refer to the article titled "Transaction Update: Ras Laffan Liquefied Natural Gas Co. Ltd. (3)," published Sept. 12, 2008, on RatingsDirect.

Outlook

The stable outlook reflects that construction at RasGas, and at associated third-party terminals and ships, is largely on schedule. It also reflects the likelihood of favorable natural gas fundamentals in RasGas' target markets over the next five years, good spot market sales potential over the next three years, and strong operational performance. We expect the remainder of the 15.6 million tons per annum (mtpa) output of trains 6 and 7 not covered by contracts with Korean Gas Co., Chinese Petroleum Corp., and Petronet to be accounted for by a long-term SPA with an affiliate of Exxon Mobil, or other parties of reasonable credit standing.

The outlook could be revised to negative, or the ratings lowered, if the delays at trains 6 or 7, or at the regasification terminal in Italy, increase and adversely affect the project's financial profile. The ratings could also be lowered if offtaker credit quality declines materially, if SPAs come under price pressure, or if global LNG markets deteriorate.

There is limited scope for a rating upgrade or outlook revision to positive until the construction of trains 6 and 7 is complete.

PROJECT FINANCE
CORPORATES
UTILITIES

Ras Laffan Liquefied Natural Gas Co. Ltd. (3)

PRIMARY CREDIT ANALYST: KARIM NASSIF, LONDON (44) 20 7176 3677, KARIM_NASSIF@STANDARDANDPOORS.COM

SECONDARY CREDIT ANALYSTS:
ALEXANDRE DE LESTRANGE, PARIS (33) 1 4420 7316, ALEXANDRE_DELESTRANGE@STANDARDANDPOORS.COM
JONATHAN MANLEY, LONDON (44) 20 7176 3952, JONATHAN_MANLEY@STANDARDANDPOORS.COM

SENIOR SECURED DEBT RATING: A/STABLE

PUBLICATION DATE: SEPTEMBER 12, 2008

Rationale

The $1.4 billion senior secured Series A bonds due 2020 and $850 million Series B bonds due 2027, issued by Qatar-based Ras Laffan Liquefied Natural Gas Co. Ltd. (II) (RasGas II) and Ras Laffan Liquefied Natural Gas Co. Ltd. (3) (RasGas 3) (together RasGas) are rated 'A'. The $1.55 billion senior secured bonds issued by RasGas 3 (comprising $750 million Series C bonds due 2016 and $800 million Series D bonds due 2027) are also rated 'A'. The outlooks on all ratings are stable.

The debt is being used to finance the design, construction, and operation of five liquefied natural gas (LNG) facilities (trains) in the State of Qatar (AA-/Stable/A-1+). Standard & Poor's Ratings Services analyses RasGas on a stand-alone basis using its project finance criteria.

The 'A' rating reflects the following credit weaknesses:

- LNG revenues are potentially volatile, owing to price links between LNG sale and purchase agreements (SPA) from RasGas and global oil-price benchmarks (and some European gas benchmarks).
- Counterparty risk exposure is high given that many SPA counterparties have lower credit quality than RasGas. The group relies on third parties and the project sponsors to complete large infrastructure projects to support LNG sales.
- RasGas has seen some small slippages in the construction program for trains 6 and 7. These delays have largely been attributed to resource constraints resulting from the overheated Middle East construction market as well as some procurement delays.
- RasGas II will be exposed to indemnity payments and will continue to be dependent on the spot LNG market sales if the Adriatic terminal in Italy, which supports an SPA with Edison SpA (BBB+/Stable/A-2), is not completed by mid-2009. Commercial operations on the Adriatic terminal are expected to commence in the first quarter of 2009.
- Market risk stems from the lack of a finalized executed SPA with an affiliate of Exxon Mobil Corp. (AAA/Stable/A-1+) for the remaining output of trains 6 and 7.
- There remains the threat of a conflict in the Middle East that could disrupt LNG production and delay deliveries beyond six months--the period for which the debt service reserve could be used to meet debt obligations. This risk is, however, largely compensated by cash flows available at the central government level (net assets are estimated at 72.2% of GDP in 2008) and at Qatar Petroleum (QP {AA-/Stable/--}; funds from operations of $7.8 billion at the end of 2007), as well as operating cash flows at the RasGas level.

The following credit strengths offset the above weaknesses at the 'A' rating level:

- Sales volume risk is largely eliminated by the presence of long-term SPAs, which cover the majority of production from trains 3, 4, and 5.
- Sponsor support is strong. The RasGas expansion is likely to generate a high proportion of income at QP from 2010 (coinciding with completion of trains 6 and 7), and will represent a significant proportion of Exxon Mobil's total share in Qatari projects.
- Construction risk for the onshore and offshore packages of RasGas has been reduced through the project's use of fixed-price, date-certain engineering, procurement, and construction (EPC) arrangements.
- There is good product revenue diversification, with about 67% of revenues coming from LNG sales and about 33% coming from LNG by-products. In addition, there is good geographic diversity of revenues in markets.
- RasGas has a competitive cost structure, which results in forecast debt service coverage ratios (DSCR) greater than 3x under most stress scenarios.
- Shipping availability risk is low, as sufficient shipbuilding capacity has been secured from experienced South Korean yards to meet delivery requirements under existing and expected ex-ship SPAs.
- Technological and operational risks are relatively low for trains 6 and 7 as they represent an extension of similar technology and design employed on trains 3, 4, and 5

despite the fact that these will represent some of the largest trains employed worldwide. In addition, trains 3, 4, and 5 are already operating in line with, or are exceeding, the sponsors' expectations.

Year-end results for financial 2007 show revenues at $6.6 billion, up 44% on the previous financial year, and profit before taxes at $3.3 billion, up by 46% year on year. As a result, the project recorded DSCRs of 9.2x for 2007. This better-than-expected performance was driven mainly by higher global oil prices and a buoyant market for sales of condensate and other by-products. The (unaudited) financial results for the six months to end-June 2008 also point to strong growth in revenues compared with the same period the previous year.

Construction costs associated with trains 6 and 7 are broadly in line with the 2007 business plan forecasts, although there have been small reported slippages in the construction schedule. We expect these delays to have a limited effect on RasGas' medium-term financial profile. We will, however, continue to monitor construction progress and any business or financial impact the delays could have on the RasGas project.

Recovery analysis

The senior secured bonds issued by RasGas II and RasGas 3 have a recovery rating of '1', indicating Standard & Poor's expectation of very high (90%-100%) recovery of principal in the event of a payment default. To date, there has been limited experience regarding default, loss, or recovery in this sector and in Qatar.

For the full recovery analysis, please see the article titled "Transaction Update: Ras Laffan Liquefied Natural Gas Co. Ltd. (3)," published Sept. 12, 2008, on RatingsDirect.

Outlook

The stable outlook reflects that construction at RasGas, and at associated third-party terminals and ships, is largely on schedule. It also reflects the likelihood of favorable natural gas fundamentals in RasGas' target markets over the next five years, good spot market sales potential over the next three years, and strong operational performance. We expect the remainder of the 15.6 million tons per annum (mtpa) output of trains 6 and 7 not covered by contracts with Korean Gas Co. (Kogas), Chinese Petroleum Corp., and Petronet to be accounted for by a long-term SPA with an affiliate of Exxon Mobil, or other parties of reasonable credit standing.

The outlook could be revised to negative, or the ratings lowered, if the delays at trains 6 or 7, or at the regasification terminal in Italy, increase and adversely affect the project's financial profile. The ratings could also be lowered if offtaker credit quality declines materially, if SPAs come under price pressure, or if global LNG markets deteriorate.

There is limited scope for a rating upgrade or outlook revision to positive until the construction of trains 6 and 7 is complete.

Saad Group

PRIMARY CREDIT ANALYST: MOHAMMED FAYEK, LONDON (44) 20 7176 3408, MOHAMMED_FAYEK@STANDARDANDPOORS.COM

SECONDARY CREDIT ANALYSTS:
TOBIAS MOCK, CFA, FRANKFURT (49) 69 33 999 126, TOBIAS_MOCK@STANDARDANDPOORS.COM
PETER TUVING, STOCKHOLM (46) 8 440 5913, PETER_TUVING@STANDARDANDPOORS.COM

ISSUER CREDIT RATING: BBB+/STABLE/A-2

PUBLICATION DATE: NOVEMBER 27, 2008

Rationale

The ratings on Saudi Arabia-based Saad Group reflect its substantial liquid investment portfolio, its strong position in the growing Gulf Cooperation Council and in asset classes that are prospering, and the proven support it enjoys from shareholders. Ratings are constrained by the group's intermediate financial profile, the volatility of its portfolio, and the concentration of its equity holdings within the financial services industry.

The group continues to improve its capital structure and reduce its adjusted debt levels despite losses incurred on financial investments under weakening global capital markets. This was evident by the reduction of adjusted debt levels to asset value to 24% as of June 30, 2008, from 27% in December 2007. The improvement in Saad Group's capital structure is attributable to the substantial equity injections totaling about $1.7 billion by the group's main shareholder, a move that demonstrates his continued commitment to the group.

Despite net losses of about $1.1 billion on financial investments, the group's overall asset base increased to $31.3 billion by mid-year 2008, from $28.8 billion in 2007. This was mostly due to shareholder contributions of protective equity put options worth about $0.9 billion, real estate investment properties for $450 million, and $235 million in cash among other contributions. The group also benefited from fair value gains of about $780 million in its real estate portfolio during the six months ended June 30, 2008. Standard & Poor's Ratings Services recognizes the credit strength, geographic diversity, and liquidity of the group's investment portfolio. The group's portfolio showed substantial resilience relative to comparable holdings, despite having a high concentration within global banking securities which recently witnessed substantial deterioration across international markets.

Saad Group is a conglomeration of international financial services, manufacturing facilities, investment companies, health care, education, and real estate development. Among the group's key credit strengths is the support of its main shareholder. The ratings are constrained by Saad's financial leverage and its exposure to market volatility, where nearly 50% of the group's total assets are invested in securities with a focus on financial institutions. In the coming years, the group also plans significant investment in new real estate for rental projects.

The group represented by far the largest asset and liability base for its main shareholder at Dec. 31, 2006. In 2007, however, an investment vehicle owned by the main shareholder had built up substantial assets and liabilities with a focus on security investments in financial institutions. We do not expect this entity to have any direct implications for the Saad Group because of its nonrecourse nature, but there is a limited possibility of indirect implications.

Interest income, rental income, and accrued dividends from investments in securities covered Saad's interest expenses by 183% during the first half of 2008. Rental income is expected to grow further in the coming years, as substantial investments in real estate are planned. This will provide a higher stable income stream for the group, and extraordinary dividends from some investment securities will increase total dividends received.

Liquidity

At June 30, 2008, Saad Group had a cash position of $7.6 billion and $1.9 billion of committed undrawn facilities, with short-term facility utilization of about $3.2 billion.

The maturity profile of the group's liabilities has also improved as a result of obtaining $5.55 billion in revolving credit facilities. Of this, $5.3 billion was drawn at June 30, 2008, under Saad Trading, Contracting and Financial Services Co. (STCFSC) and Saad Investments Co. Ltd. (SICL), as well as through a $650 million sukuk issued by Golden Belt 1 B.S.C. and by raising a $440 million murabaha facility under Awal Bank.

In addition, at June 30, 2008, the group's investment securities had a value of $15.1 billion (including a protective equity put option worth $953 million).

Outlook

The stable outlook reflects our expectation that the Saad Group will maintain a net debt to adjusted portfolio value of less than 30%, and balance its growth plans in real estate development and manufacturing activities to maintain intermediate leverage. The stable outlook also factors in the expected continued support from the group's main shareholder.

The potential for a rating upgrade is constrained by leverage and volatility in the portfolio value. Continued weakening of equity markets or a more aggressive growth strategy and subsequently higher leverage for the group could have negative implications for the rating.

Saad Trading, Contracting and Financial Services Co.

PRIMARY CREDIT ANALYST: MOHAMMED FAYEK, LONDON (44) 20 7176 3408, MOHAMMED_FAYEK@STANDARDANDPOORS.COM

SECONDARY CREDIT ANALYSTS:
TOBIAS MOCK, CFA, FRANKFURT (49) 69 33 999 126, TOBIAS_MOCK@STANDARDANDPOORS.COM
PETER TUVING, STOCKHOLM (46) 8 440 5913, PETER_TUVING@STANDARDANDPOORS.COM

ISSUER CREDIT RATING: BBB+/STABLE/A-2

PUBLICATION DATE: NOVEMBER 27, 2008

Rationale

The ratings on Saudi Arabia-based Saad Trading, Contracting and Financial Services Co. (STCFSC) reflect its strategic importance within the Saad Group (BBB+/Stable/A-2). This stems from its substantial investment holdings in blue chip Saudi and international banks, significant real estate assets, and highly integrated construction and manufacturing business in Saudi Arabia. STCFSC had total assets of about Saudi Arabian riyal (SAR) 48.3 billion ($12.9 billion) on June 30, 2008.

Saad Group is a conglomeration of international financial services, manufacturing facilities, investment companies, health care, education, and real estate development. The group's credit strengths include strong support from its shareholders. Saad Group had total assets of $31.3 billion on June 30, 2008.

STCFSC faces the typical risks associated with property development: significant upfront investment needs; failure to achieve the necessary high occupancy for an adequate return on assets; or failure to adapt quickly enough to changing market dynamics. The company has managed these risks well in the past, though with high vertical integration, which has been a clear strategic advantage for STCFSC for many years. STCFSC's business risk profile benefits from positive demographic and social trends for the real estate business and banking environment in the Gulf countries. This provides a good basis for STCFSC's strategy to further expand in exclusive real estate property and remain focused on security investments in the banking sector. STCFSC has a clear strategy regarding its exposure to long-term security investments in the banking sector; most investments are rated at least 'A'.

Standard & Poor's Ratings Services expects dividends from STCFSC's investments in securities and rental income to continue to comfortably cover net interest expense for financial debt. We also expect funds from operations (FFO) to debt to remain above 10% in the coming years, despite significant investment plans. STCFSC continues to be cash positive as of June 30, 2008, holding more cash than debt. STCFSC has substantially less leverage than the Saad Group as a whole, which held net debt to adjusted portfolio value of 24% as of June 30, 2008.

LIQUIDITY

On June 30, 2008, STCFSC had a cash position of SAR15.2 billion ($4.1 billion) and $1.0 billion available in undrawn committed credit lines. In addition, its investment securities had an asset value of about SAR10.3 billion ($2.7 billion) on June 30, 2008. The company's debt maturity profile remains favorable: about 89% of liabilities were of long-term nature on June 30, 2008 (89% in 2007 and 32% in 2006).

Outlook

The stable outlook reflects our expectation that STCFSC will remain core to the Saad Group. We expect the Saad Group to maintain a net debt to estimated portfolio value of below 30% and balance its growth plans in real estate development and manufacturing activities to maintain intermediate leverage. The potential for a rating upgrade is constrained by leverage, volatility in the portfolio value due to substantial equity investments, and ambitious plans to expand the finance business. A continued weakening of equity markets, or a more aggressive growth strategy and subsequently higher leverage for the Saad Group, could have negative implications for the rating.

PROJECT FINANCE
CORPORATES
UTILITIES

Saudi Basic Industries Corp.

PRIMARY CREDIT ANALYST: TOBIAS MOCK, CFA, FRANKFURT (49) 69 33 999 126, TOBIAS_MOCK@STANDARDANDPOORS.COM

SECONDARY CREDIT ANALYST: TREVOR PRITCHARD, LONDON (44) 20 7176 3737, TREVOR_PRITCHARD@STANDARDANDPOORS.COM

ISSUER CREDIT RATING: A+/STABLE/A-1

PUBLICATION DATE: JANUARY 22, 2009

Rationale

On Jan. 22, 2009, Standard & Poor's Ratings Services affirmed its 'A+' long-term and 'A-1' short-term corporate credit ratings on Saudi Arabia-based petrochemicals producer Saudi Basic Industries Corp. (SABIC). The outlook is stable.

The affirmation reflects SABIC's solid balance sheet, strong cost position in the industry, and still sound profitability despite a material decline in the fourth quarter of 2008. It also reflects our expectations that the company might benefit from shareholder support in a continuously weak operating environment.

According to preliminary results, SABIC's 2008 operating profits declined 60%, excluding exceptional items (84% including the exceptional items). This substantial decline reflects a combination of several factors in fourth-quarter 2008, which we expect to have affected most of the chemical industry. First, the industry experienced a rapid decline in demand and volumes sold of a greater magnitude than in past downturns. This was due to customer de-stocking in anticipation that rapidly declining oil-related input costs will reduce selling prices. Second, meaningful production cuts at key customer industries, such as automotive and construction, intensified the impact of negative volumes. We expect de-stocking to continue in the first quarter of 2009 and that the very high level of uncertainty about underlying fundamental demand for 2009 will remain until April or May.

The ratings on SABIC reflect its leading market and cost positions in basic and commodity chemicals. It is the world's No.2 producer of ethylene and the No.3 producer of polyethylene. SABIC is the Gulf region's largest steel producer, with capacity in excess of five million metric tons (mmt). The company had sales of Saudi Arabian riyal (SAR) 152 billion ($40.3 billion) over the 12 months ended Dec. 31, 2008.

SABIC derives its competitive advantage mainly from its access to natural gas at a fixed price significantly below market levels outside the Middle East and its strong infrastructure at large industrial sites at Al-Jubail and Yanbu. In addition, its favorable geographic location allows it to serve fast-growing Asian markets alongside its established European and North American markets. The currently low oil price, however, has somewhat diminished SABIC's competitive advantage in the industry because its main competitors are now also benefitting from lower feedstock costs than in most of 2008.

The Kingdom of Saudi Arabia (AA-/Stable/A-1+) owns 70% of SABIC and provides part of its current funding needs through state-owned investment funds. The company is of key strategic importance to Saudi Arabia because it contributes to the value of the country's huge hydrocarbon feedstock reserves, provides an increasing number of jobs, and aids further industrialization of other chemical industries in the Gulf region. We recognize this strategic importance with a one-notch uplift to the standalone rating. We regard it as likely that in the event of a continuously weak economic environment SABIC could benefit from state support.

The ratings are constrained by the cyclicality and high capital intensity of SABIC's petrochemicals and steel-production business units and the execution risks associated with investments planned up to 2010. By 2012, SABIC intends to increase its production capacity to more than 80 mmt from about 56 mmt for the year ended Dec. 31, 2008. The company plans to expand its ethylene capacity by more than 50% by year-end 2010 to become the world's largest ethylene producer. We expect it to invest about $12.5 billion in new production facilities between 2009 and 2010. SABIC's largest production facilities under construction are Yansab and Saudi Kayan, which are scheduled to come on stream in 2009 and 2010, respectively.

Short-term credit factors

The short-term rating on SABIC is 'A-1', reflecting the group's good liquidity position. Apart from cash holdings of about SAR50 billion as at Dec. 31, 2008, the group has access to about SAR3 billion in undrawn committed credit lines. This comfortably covered all short-term debt obligations of about SAR4 billion at the end of 2008.

We expect operating cash flow generation to be negatively affected by lower prices for petrochemicals and lower production volumes. However, we expect SABIC to be able to offset the volume decline because it will bring a new plant on stream in 2009 (Yansab) and benefit from increased production capacity in the years ahead when Saudi-Kayan starts its operations. This should improve profitability and cash flows from operations compared with the weak levels achieved in fourth-quarter 2008. We expect free operating cash flow (after capital expenditure) to rise sufficiently as a result of working capital reductions in 2009 to cover dividend payments. However, uncertainty about underlying demand for petrochemicals is high for the time being.

Outlook

The stable outlook reflects our expectation that SABIC will continue to keep its competitive advantage, with feedstock prices significantly below market levels, and successfully execute its large investment program. We expect SABIC to continue with its moderate financial policy and maintain cash flow protection ratios at adequate levels for the rating for the duration of the ongoing market downturn, which is expected to result in a significant weakening of profit margins in 2009 and 2010. We expect funds from operations to debt to remain at about 55% and debt to EBITDA to stay below 1.5x on average over the petrochemical cycle. However, we do not expect the company to achieve these targets in the trough of the cycle.

A further accelerated growth path, accompanied by a more aggressive financial policy; a substantial increase in ethane prices in Saudi Arabia; or a significant drop in growth expectations in China could cause an imbalance of supply and demand and trigger a negative rating action. Ratings upside is currently quite limited because of the cyclical nature of the petrochemical business and the negative outlook for the coming two years for that sector.

PROJECT FINANCE
CORPORATES
UTILITIES

Saudi Electric Co.

PRIMARY CREDIT ANALYST: KARIM NASSIF, LONDON (44) 20 7176 3677, KARIM_NASSIF@STANDARDANDPOORS.COM

SECONDARY CREDIT ANALYSTS:
PETER KERNAN, LONDON (44) 20 7176 3618, PETER_KERNAN@STANDARDANDPOORS.COM
FAROUK SOUSSA, PHD., DUBAI (971) 4709 6820, FAROUK_SOUSSA@STANDARDANDPOORS.COM

ISSUER CREDIT RATING: AA-/STABLE/--

PUBLICATION DATE: APRIL 21, 2009

Rationale

The rating on Saudi Electric Co. (SEC) reflects the company's continuing key role in the economy of the Kingdom of Saudi Arabia (AA-/Stable/A-1+) and the intention of the Saudi government to remain supportive of SEC's credit quality. As a consequence, the long-term issuer credit rating factors in explicit state support and has been equalized with that on the state. The rating also benefits from strong forecast growth in electricity demand, as well as SEC's quasi-monopoly position in electricity generation and its monopoly position in electricity transmission and distribution services. Further rating strengths include the company's strong historical and current capitalization levels and robust debt coverage ratios, although capitalization relative to debt and debt coverage ratios are likely to weaken over the short to medium term.

These strengths are offset by SEC's progressively declining stand-alone liquidity level; high commitments under its capital expenditures program, which is expected to result in a deterioration of debt coverage ratios; regulatory risk affecting its three key business segments; and uncertainty relating to the treatment of accrued payables on SEC's balance sheet owed to oil company Saudi Aramco. In addition, SEC currently struggles to maintain a peak load capacity margin as demonstrated by brownouts (drops in voltage) and will continue to face challenges in this regard in the short term. Medium- to long-term plans, however, should ensure adequate capacity margins as long as its capital expenditures program progresses successfully.

We analyze SEC using its criteria for government-related entities (GREs) and views the company as a public-policy entity that benefits from implicit and explicit state support—albeit without an explicit financial guarantee. Our current assessment of SEC's stand-alone creditworthiness (absent extraordinary government support) is in the upper 'BBB' category.

SEC's audited results for the 12 months ending Dec. 31, 2008, point to revenue growth of 6.9%—slightly ahead of growth at the same point the previous year. Standard & Poor's adjusted operating profit (before interest and tax), on the other hand, fell by around Saudi Arabian riyal (SAR) 240 million over the same period to SAR977 million. The adjusted operating profit margin, meanwhile, fell to 4.4% from 5.8%. This was largely due to a 12.5% increase in operating and maintenance costs, as along with a 10.9% increase in fuel costs. Operating costs continue to be affected by high inflation, particularly in terms of salaries.

Accrued payables in relation to unpaid fuel purchased from Saudi Aramco increased to SAR38.2 billion at Dec. 31, 2008, from SAR32.2 billion a year earlier. Ongoing discussions between the Saudi government and SEC continue regarding a total solution for the power sector, which we anticipate would include a discussion surrounding possible tariff rebalancing and the resolution of the issue of SEC's accruing payables.

In addition, the government pledge of SAR19 billion in payments relating to the settlement of all accrued receivables arising from the period of SEC's inception in 2000 until fourth-quarter 2006 is soon to expire. These payments, which extend over three years between the fourth quarter of 2006 and the third quarter of 2009, have to date been paid on time and in full.

The company expects to invest about SAR60 billion over 2009–2011, which in our view will lead to a deterioration of its financial metrics.

Liquidity

We consider that SEC has adequate liquidity for the rating, as we believe that potential support from the Saudi government mitigates SEC's liquidity risk. On a stand-alone basis, however, we view the company's liquidity as weak when considering its capital expenditure commitments in 2009. That said, we anticipate that there will be some flexibility in implementing the full capital expenditure program during 2009.

SEC's stand-alone liquidity is more than sufficient to meet its debt obligations between April 1 and Dec. 31, 2009. We anticipate that these debt obligations will include approximately SAR555 million in repayments, largely skewed toward the end of the year. Over the medium term, however, the company's significant committed capital expenditure program presents a significant potential drain on its cash and available short-term balances.

In 2008, SEC spent SAR22.2 billion on investing activities, leading to a reduction in cash balances of SAR4.3 billion. As a consequence, SEC's available cash and cash equivalents declined to SAR1.2 billion on Dec. 31 from SAR5.6 billion at the start of the year. We anticipate that the company will continue to implement a policy of maintaining at least SAR1.0 billion of cash and cash equivalent at all times. We also assume that it will put in place sufficient medium-term financing in a timely manner for its significant capital expenditures program. On Dec. 31, 2008, the company had cash balances of SAR1.2 billion and unutilized short-term revolving facilities of SAR1.0 billion. On the same date, the company also had unutilized committed amounts of SAR646 million under its medium-term Murabaha facility.

Outlook

The stable outlook on SEC factors in continued strong implicit and explicit state support from the government of Saudi Arabia. The outlook also reflects our expectation that SEC will continue to benefit from direct and timely financial support from the government in case of need. We anticipate that the tariff regime will remain supportive and that SEC's outstanding working capital issues will be resolved in the near term.

The rating on SEC will most likely move in line with that on the government of Saudi Arabia if we observe no change in the level of state support. Such movement will not happen automatically, however, and the rating on SEC will be subject to a separate review. Any evidence of weakening government support, an announcement of privatization, or exposure to a higher level of competition could pressure the rating and result in a revision of our analytical approach to government support for SEC. Similarly, any change in government support that we believe would negatively affect SEC's payables, tariffs, or future funding plans could lead to a rating review.

Rating upside could arise if the rating on the sovereign were to improve, subject to SEC maintaining its current strong business and financial links to the state.

PROJECT FINANCE
CORPORATES
UTILITIES

Saudi Telecom Co.

PRIMARY CREDIT ANALYST: MICHAEL O'BRIEN, LONDON (44) 20 7176 3561, MICHAEL_OBRIEN@STANDARDANDPOORS.COM

SECONDARY CREDIT ANALYST: RAAM RATNAM, LONDON (44) 20 7176 7066, RAAM_RATNAM@STANDARDANDPOORS.COM

ISSUER CREDIT RATING: A+/STABLE/A-1

PUBLICATION DATE: JANUARY 15, 2009

Rationale

The ratings on Saudi Telecom Co. (STC), the former incumbent fixed-line and mobile telecommunications operator in the Kingdom of Saudi Arabia (AA-/Stable/A-1+), are supported by its leading market position in the recently liberalized Saudi telecoms market with a difficult-to-replicate national network, implicit state support, high operating profitability margins, and underlying strong cash flows. STC's financial policy remains conservative, as the company only recently used debt to partially fund its initial overseas investments.

The ratings are constrained, however, by potential further regulatory changes, which may negatively affect the company's competitive position and market shares, including, for example, higher competition following the entrance of a third mobile operator in the Saudi market in 2008. In addition, revenue growth in STC's fixed-line division is stagnant due to fixed-to-mobile traffic substitution, low broadband penetration, and modest domestic growth overall due to increased competition. Substantial investment is also required to further upgrade the company's fixed-line network, although broadband availability has increased significantly over the past 15 months.

The Saudi telecoms market offers the potential for STC to maintain its position through incremental growth in broadband connections, which are currently at a low level. The ratings are further supported by the cash flows derived from its mobile telecoms operation, which had a 61% subscriber market share and a 75% revenue market share at the end of 2007. This division made a major contribution toward achieving the benefits of economies of scale and high profitability margins for the company.

STC is 70%-owned by the Saudi Arabian government, and a further stake of about 13% is owned by government-related entities. The company is of strategic importance to the state as a provider of key communications infrastructure. Standard & Poor's Ratings Services recognizes this strategic importance and has notched up the corporate credit rating on STC by one notch from the stand-alone rating.

STC retains substantial financial flexibility to undertake inorganic growth activities abroad, although uncertainty remains over the credit impact of such actions. Following the purchase of a 35% stake in Oger Telecom Ltd. for $2.6 billion (SAR9.8 billion), STC's adjusted debt increased substantially—as expected—to SAR26.2 billion at Sept. 30, 2008. As a result, the ratio of consolidated adjusted debt to EBITDA was 1.3x for the 12 months ended Sept. 30, 2008.

LIQUIDITY

The 'A-1' short-term rating is supported by STC's strong liquidity and good financial flexibility for its needs. At Sept. 30, 2008, liquidity resources included cash and cash equivalents of SAR7.6 billion. In addition, the company has available undrawn portions of its existing medium-term facilities with local banks totaling SAR3.5 billion, with a relatively extended amortizing maturity profile.

Debt maturities within one year at Sept. 30, 2008, amounted to SAR4.7 billion. Other cash payments in the third quarter included interim dividends of SAR2.0 billion. In April 2008, the company raised a 10-year, SAR9.5 billion Murabaha facility to fund the purchase of a 35% stake in Oger Telecom.

We expect the company's underlying strong free operating cash flow (FOCF) generation to continue over the next few years and remain a key source of funds for financing any significant investments. In 2008, FOCF has proved insufficient to cover large acquisitions such as the Oger Telecom stake while the company continues to pay substantial dividends. As expected, we now see STC funding its requirements with new

debt issuance, within the limits of its financial policy. The company's liquidity policy stipulates that it will have sufficient cash available to meet projected business needs with minimum cash coverage on a rolling 12-month basis.

Outlook

The stable outlook reflects our expectation that STC will remain committed to its conservative financial policy and that the Saudi Arabian government will retain its controlling stake in the company.

We expect STC's funds from operations (FFO) to debt to remain above 50% on average, and adjusted debt to EBITDA to remain at 1x-2x, assuming the company broadly maintains its strong domestic position. Any deviation toward higher leverage of more than 2x would need to be temporary to avoid pressure on the ratings. STC's key credit protection ratios are now moving toward long-term expectations for the rating level, given the increase in debt during 2008. Nevertheless, the company still retains financial flexibility for its investment plans, within the boundaries of its financial policy.

The ratings could come under pressure from a more accelerated growth path—either organically or through acquisitions—accompanied by a more aggressive financial policy, a substantial negative impact on the company's financial performance as a result of regulatory decisions, or more intensive competition. Upside for the ratings is limited at this stage, given the risks and dynamics associated with the telecoms industry. Such risks include likely increased competition for STC in its domestic market and a willingness to increase leverage for potential foreign acquisitions, some of which would require support or funding from STC in the early stages of their development.

PROJECT FINANCE
CORPORATES
UTILITIES

Tourism Development and Investment Co.

PRIMARY CREDIT ANALYST: FAROUK SOUSSA, PHD., DUBAI (971) 4709 6820, FAROUK_SOUSSA@STANDARDANDPOORS.COM

SECONDARY CREDIT ANALYST: ALF STENQVIST, STOCKHOLM (46) 8 440 5925, ALF_STENQVIST@STANDARDANDPOORS.COM

ISSUER CREDIT RATING: AA/STABLE/A-1+

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Rationale

On March 2, 2009, Standard & Poor's Ratings Services assigned its 'AA' long-term and 'A-1+' short-term corporate credit ratings to the Tourism Development and Investment Company (TDIC), based in Abu Dhabi, in the United Arab Emirates (UAE). The outlook is stable.

The ratings on TDIC have been equalized with those on the government of Abu Dhabi, which has sole ownership of the company through the Abu Dhabi Tourism Authority (ADTA). Although the Abu Dhabi government has not formally guaranteed TDIC's liabilities, the company has a high-profile policy role in diversifying the Abu Dhabi economy through its real estate and tourism activities. This, coupled with TDIC's operational proximity to the Abu Dhabi government, leads Standard & Poor's to conclude that the government has the capacity and willingness to continue to provide substantial ongoing support to TDIC's operations, and to intervene in a timely manner if the company were to face financial difficulties.

The ratings on the Emirate of Abu Dhabi are supported by the government's very strong asset position, which provides significant financial flexibility; the country's high level of political stability and wealth, underpinned by its rich resource endowment; and by policies that reinforce Abu Dhabi's integration with the global economy. The ratings are constrained by the geopolitical risks that all sovereigns in the region face, the limited disclosure on the government's assets, and increasing contingent liabilities arising from the banking system and the UAE's public sector as a whole.

TDIC is the second largest property developer in Abu Dhabi in terms of land bank. The group started its operations in 2005 and large planned projects are still in the start-up phase, which explains the low reported sales of only UAE dirham (AED) 35 million ($10 million) in 2007, while total assets were AED21 billion. TDIC benefits from land grants and other subsidies from the government, which reduces the inherent speculative risk of property development. Because of the magnitude of projects planned by TDIC and other Abu Dhabi developers over the near to medium term, there is, however, significant risk of over supply as demand has softened in recent months. There is also inherent construction risk, and TDIC has a limited track record.

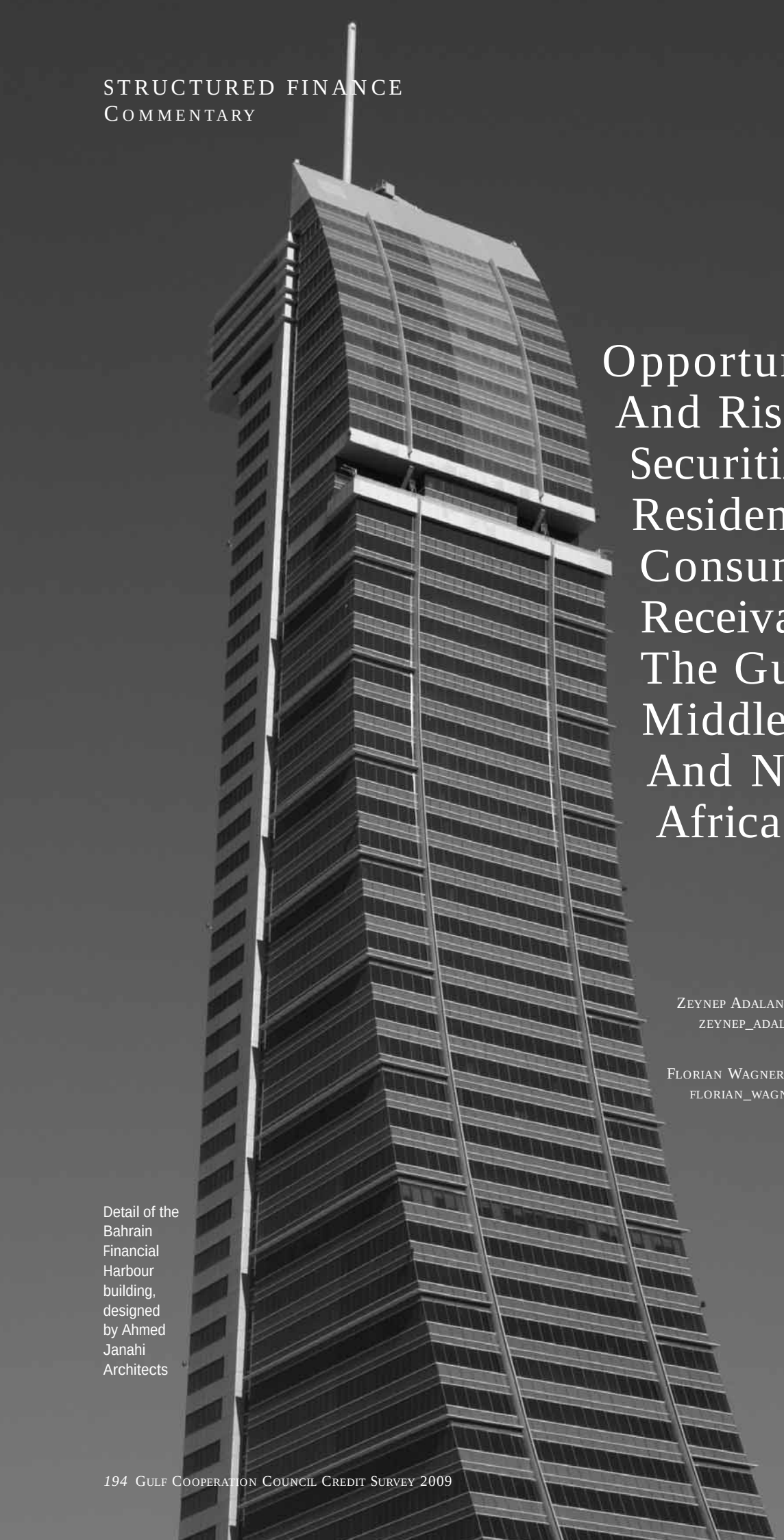
TDIC's financial risk profile is negatively affected by large capital spending on projects over the near term, resulting in significant cash outflows and increased debt levels. However, the credit implications of TDIC's weak financials and short track record in a high risk business pale against the government's history of support for government-related entities. This is evidenced by the absence of any bankruptcies in recent years. For these reasons, and those stated above, Standard & Poor's views TDIC debt as being tantamount to that of the government.

Outlook

The stable outlook reflects our view that TDIC will remain strategically important and operationally close to the government of Abu Dhabi, and will continue to benefit from substantial ongoing support to its operations, and, if the need arises, extraordinary financial support. Any lowering in the credit rating on the government of Abu Dhabi, or any indication that the government's commitment to TDIC is weakening, would result in a lower credit rating on the company. A higher rating could result from improvement in the credit quality of the Emirate of Abu Dhabi, to which the underlying credit risk of TDIC is linked.



The Abu Dhabi Corniche, a recent multi-use development.



Opportunities And Risks In Securitization Of Residential And Consumer Receivables In The Gulf, Middle East, And North Africa

PRIMARY CREDIT ANALYSTS:
ZEYNEP ADALAN, LONDON (44) 20 7176 3703
ZEYNEP_ADALAN@STANDARDANDPOORS.COM

LEGAL CONTACT:
FLORIAN WAGNER, LONDON (44) 20 7176 3738
FLORIAN_WAGNER@STANDARDANDPOORS.COM

Detail of the Bahrain Financial Harbour building, designed by Ahmed Janahi Architects

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IN RECENT YEARS THERE HAS BEEN GROWING interest in the securitization of receivables backed by assets in member countries of the Gulf Cooperation Council (GCC), as well as more broadly across the different countries of the Middle East and North Africa region (MENA). Securitization of receivables in these regions presents challenges in terms of the credit, cash flow, structural, and legal characteristics of such transactions.

Nonetheless, by assuming a cautious approach to mitigating such risks, while simultaneously undertaking a prudent assessment and consideration of local market practices, securitization notes backed by such assets could potentially achieve ratings commensurate with the overall risk profile of the transaction. As residential and consumer lending volumes continue to grow at a rapid pace in this region, Standard & Poor's Ratings Services expects to see increased innovation by local market participants striving to achieve such a balance between risks and their mitigation.

This article examines some of the opportunities and risks presented by securitization in the GCC/MENA regions. The scope and limitations for treatment of this topic are as follows:

- It focuses on residential and consumer receivables, as opposed to commercial or corporate receivables.
- As such, its focus is naturally also limited to existing-asset receivables, as opposed to future flow receivables.
- The issues addressed are those of securitization, and consequently the sharia-compliance of either the underlying assets or the actual special-purpose entity (SPE) are not addressed except insofar as this relates to the process of securitizing those assets.
- Similarly, because the focus of the article is not the sharia-compliance of either the underlying assets or structures, it does not specifically discuss sukuk except to the extent that this is pertinent.

GCC/MENA Residential And Consumer Assets: Market Overview

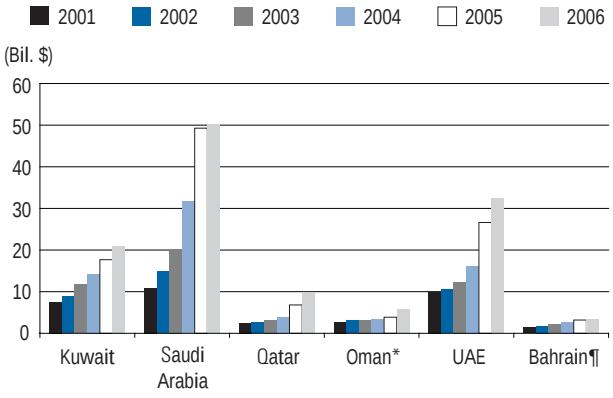
The securitization of residential and consumer receivables is generally driven by a confluence of three factors—growth in lending that drives the origination of these receivables, this same growth outstripping conventional funding sources (e.g., deposits, wholesale funding) for such lending, and the economic feasibility of achieving a net positive funding position versus the yield on those receivables. In the context of the GCC/MENA region, the first of these factors (growth in lending) is a primary consideration in the growth of the market, the second (funding needs) is a secondary driver, while the third (economic feasibility) is the most challenging given current market conditions.

Given the relative significance of these factors, it is initially worth focusing on the growth in consumer lending. There is not extensive data across the GCC/MENA region that segments aggregate consumer lending volumes or outstanding balances into such categories as mortgages, auto loans, personal loans, etc. However, there is broader data available on consumer lending in some countries or regions (for instance, certain GCC member states), which demonstrates that there has been impressive credit growth in the region, especially in the period 2005–2006 *(see chart 1)*.

A similar trend is demonstrated when narrowing the focus to a single country; for instance, the growth of personal lending for consumption purposes in the United Arab Emirates (UAE) is illustrated in chart 2.

Chart 1

Retail Loans In The GCC

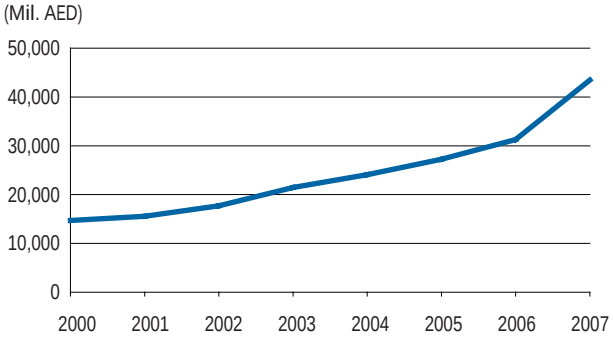


* Projected year-end figure for 2006. ¶Excluding wholesale and Islamic banks.

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Chart 2

Personal Loans For Consumption Purposes In The UAE: Banks' Gross Credit To Residents

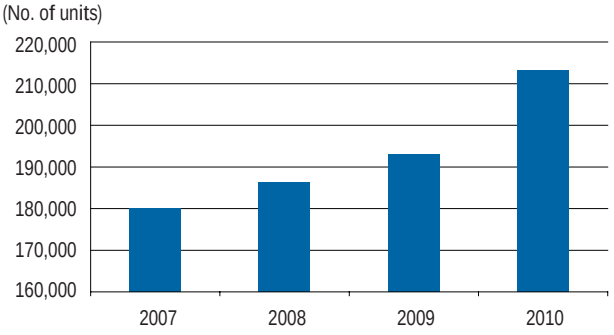


Source: Central Bank of the UAE

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Chart 3

Growth In Cumulative Residential Supply In Abu Dhabi



Source: Colliers.

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Shifting the focus from retail and personal lending in general to lending specifically for residential purposes, a similar trend can be perceived. The principal driver behind this growth in residential lending has been the fast growth in residential construction, which has accelerated rapidly throughout the region in recent years. We expect this trend to continue unabated, at least in the immediate future. For instance, chart 3 shows the growth in cumulative supply of residential properties in Abu Dhabi projected through 2010. While Abu Dhabi is probably among the emirates of the UAE with the most residential construction underway, other emirates (such as Dubai) and other GCC countries (such as Oman) are also experiencing a rapid acceleration in the supply of residential properties.

The accelerated construction of residential properties, combined with the introduction of more precisely defined residential lending volumes and mortgage regulations in a number of countries, has driven growth in residential lending to fund the purchase of these properties. A large proportion of this lending is to domestic nationals of the countries in question; for instance, chart 4 illustrates the growth in aggregate value of real estate mortgage loans to residents in the UAE, which has witnessed dramatic growth—especially in the period 2004-2007.

However, there has been a concurrent increase in the growth of real estate mortgage loans to nonresidents *(see chart 5)*, driven both by the increased inflow of expatriate workers and the recently expanded flexibility allowed to expatriates to purchase property in certain emirates (for instance, Dubai).

Two of the factors mentioned above—the introduction of mortgage lending regulations and the liberalization of property ownership for expatriates—are worth elaborating upon further. For instance, in Saudi Arabia we expect a new mortgage law to contribute to the emergence of a more active mortgage market with the participation of domestic lenders. Likewise, in Dubai, growth in residential lending was previously hampered by a lack of legislative clarity and restrictions on the ownership of property by nonnationals. However, in recent years we have seen an increase in legislative clarity and greater flexibility of property ownership for nonnationals, for instance by allowing freehold ownership in various designated areas, which has had a strong impact on

demand for residential real estate. Similarly, Qatar, Oman, and Bahrain now allow nonnationals to purchase properties in select designated areas.

Of course, the growth and expansion outlined above also carries risks with it. For instance, in some jurisdictions there may be a potential oversupply of residential properties, many of them aimed at a similar buyer segment (for instance, luxury apartments for overseas investors), and this at a time when demand has become increasingly sluggish in multiple property markets globally.

Analytical Considerations And Assumptions

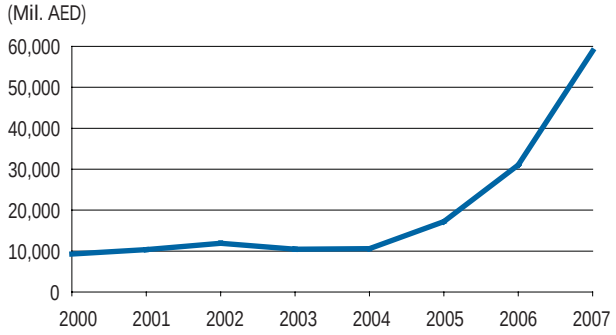
Most elements of the underlying process by which we rate the notes of transactions backed by residential and consumer receivables across multiple jurisdictions can generally be applied to transactions in GCC/MENA. This approach can be summarized as follows:

- *Market environment:* We undertake a review of the environment of the transaction, which includes macroeconomic factors, the housing market (for residential mortgage-backed securities, or RMBS, transactions), and consumer credit trends (for asset-backed securities, or ABS, transactions).
- *Sovereign:* We make an assessment of the extent to which sovereign or jurisdictional factors relating to the domicile of the assets may affect the ratings process.
- *Credit:* We seek to understand the characteristics and quality of the collateral, and apply default and recovery assumptions to this collateral to determine expected losses on a static basis.
- *Cash flow:* We model the cash flows expected to be generated by the assets over time under an assumed environment that is appropriate to the rating level being sought, and form a view on whether these flows are sufficient to pay timely interest and ultimate principal (or otherwise) under the terms and conditions of the notes.
- *Legal:* We assess and may seek comfort in the form of legal opinions on the relevant aspects of the structure of the transaction in order to form a view on how the applicable legal regime affects our credit and cash flow

Chart 4

Real Estate Mortgage Loans In The UAE

Aggregated Balance Sheet Of Banks, Total Credit To Residents



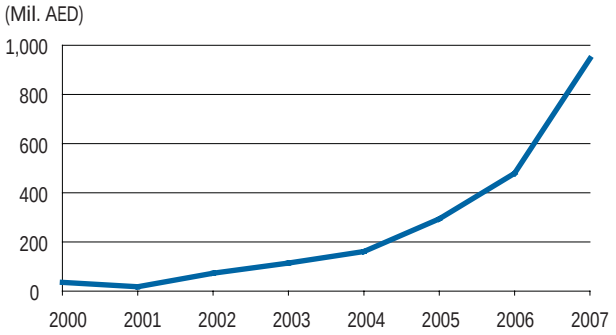
Source: Central Bank of the UAE.

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Chart 5

Real Estate Mortgage Loans In UAE

Aggregated Balance Sheet Of Banks, Total Credit To Non-Residents



Source: Central Bank of the UAE.

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assumptions and ultimately the ability of the issuer to service the rated instruments.

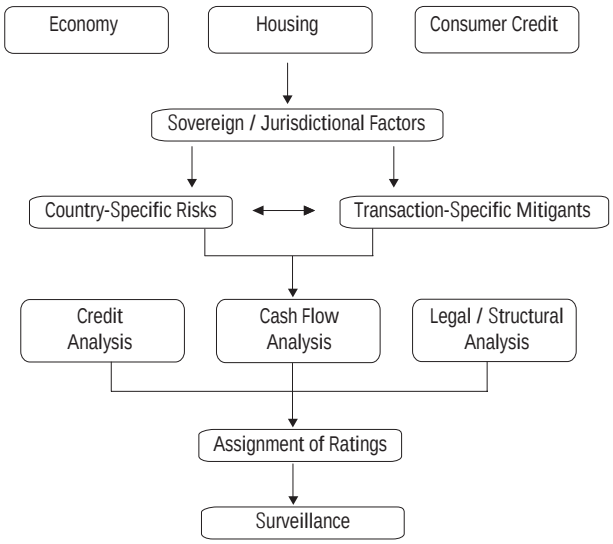
- *Surveillance:* After we assign ratings in the transaction, our surveillance process continually reassesses any changes in our opinion of default risk, which may then be expressed via corresponding changes in the ratings on the notes.

This rating process can also be applied to transactions in the GCC/MENA region. However, there are certain additional considerations that we would take into account to address attributes of the collateral and structure that may pertain specifically to these markets. Where such specific attributes amount to additional risks that could have an impact on our rating, we would also seek to understand any available mitigants in the specific transaction. In analyzing the key issues and potential challenges that face securitization in this region, however, it must be noted that it is possible that a confluence of unmitigated credit, cash flow, legal, and sovereign risks or uncertainties could render it impossible to rate a transaction at any rating level. Likewise, the quantity and granularity of data captured may vary by market, product, and lender, but to undertake adequate credit and cash flow analysis—and ultimately also to rate a transaction—there must be sufficient data captured to permit an adequate degree of analysis on the underlying receivables.

In the following sections we provide a more detailed overview of our usual rating approach in a typical RMBS/ABS transaction and some considerations on how certain aspects specific to the GCC/MENA region could affect this. Specific circumstances sometimes warrant a departure from these general guidelines, and this is especially true for ratings in new jurisdictions or for new structure types.

Chart 6

Rating And Surveillance Approach For RMBS Transactions



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Credit Considerations

General approach

Before addressing those additional considerations for transactions in the GCC/MENA region, it is initially worth briefly recapping our methodology for rating ABS and RMBS transactions across multiple jurisdictions.

Residential mortgages

For each mortgage loan in the pool we estimate the likelihood that the borrower will default on his mortgage payments (called the foreclosure frequency), and the amount of loss on the subsequent sale of the property (the loss severity, expressed as a percentage of the outstanding loan). This credit analysis is based on the characteristics of the loans and the associated borrowers.

In relation to foreclosure frequency, we assign a base default rate to each loan in the portfolio at each rating level, and subsequently adjust up or down this assigned probability of default according to the underlying borrower, loan, and property characteristics. Hence, each loan in the portfolio is associated with a unique assigned default rate, based on its underlying attributes. The penalties applied reflect the higher foreclosure frequency likely to occur due to specific loan or

"The principal driver behind this growth in residential lending has been the fast growth in residential construction, which has accelerated rapidly throughout the region in recent years. We expect this trend to continue unabated, at least in the immediate future."

borrower attributes; for instance, loans with higher loan-to-value (LTV) ratios compared with the market standard, with low seasoning, with a high outstanding principal balance, and with geographic concentration.

In relation to loss severity, we apply an assumed market value decline to the property, and subtract assumed recovery costs from the proceeds of the sale.

As a result, the total mortgage balance assumed to default, and the total amount of this defaulted balance that is not recovered for the entire pool, are determined by calculating the weighted-average foreclosure frequency (WAFF) and the weighted-average loss severity (WALS). The WAFF and WALS estimates increase as the required rating level increases, because the higher the rating required on the notes, the higher the level of mortgage default and loss severity they should be capable of withstanding.

Consumer loans

For automobile loans and similar consumer finance transactions, our rating analysis also involves an assessment of the credit risk inherent in the transaction by sizing credit enhancement—or support—for each class of notes after analyzing the impact that various stress scenarios would have on the collateral. We expect to be provided with quarterly static net loss data starting from the earliest point in time available. For instance, for automobile loans this data may be subdivided both by vehicle type (new, used) and loan type (amortizing, balloon), and we would assess whether certain categories of loan and vehicle perform substantially better than others. Base case loss levels are then derived, including potential base cases for the sub-categories referenced above. This static net loss data indicates the actual write-offs—or losses—after recoveries, including vehicle sale proceeds and other recovery sources. If we are provided with separate recovery and prepayment data, we do a more granular analysis that includes default levels, prepayment rates, and recovery expectations. The final result of the analysis, in either case, will be expected losses for the portfolio.

In the case of residential and consumer loans in the GCC/MENA region, we would likely use the approaches outlined above to the extent that they apply to the assets and receivables, which we anticipate would often be the case. However, there may be a number of additional considerations to ensure that the approach we take is appropriate to both the nature of the assets and the jurisdiction. The following six primary additional credit considerations are discussed in more detail below:

- Historical collateral performance data
- Ownership of underlying assets
- Recovery process
- Geographic concentration
- Occupancy status
- Residential house price trends

Historical collateral performance data

Broad and deep historical data on delinquency and default rates is sometimes not available for residential and consumer asset classes in certain countries in these regions. Where such data is available, it often reflects the relatively benign economic environment that has been prevalent in the recent past. Consequently, this data may not demonstrate the collateral performance through a number of different economic cycles, including adverse points in these cycles. However, such a paucity of data can also be encountered in other countries also.

Therefore, in setting default and recovery rates for residential mortgages, we would place emphasis primarily on adjusting our assumptions by making these more conservative both in absolute terms and in comparative terms (i.e., compared with other countries that have longer and broader performance data available). Similarly, when deriving default rates for auto loan transactions, we assess the quality of the loss data provided by the lender, take into account the extent to which it reflects benign or recessionary periods, and derive base loss cases.

Ownership of underlying assets

The financing of residential lending in countries in this region can sometimes take the form of sharia-compliant products. In such products, ownership title of the underlying property frequently does not pass to the borrower until such time as the balance payable has been extinguished in full. A typical example of this is a "ljarah," which is a home financing tool that essentially resembles a lease-to-buy method of financing a

home purchase. As a result, the lender holds title to the actual property and a lease agreement upon that property; this is different to non-sharia mortgage loan products where the lender has rights to the loan receivables, but does not hold title to the actual property.

We would take the above product features into account in our ratings analysis because when the sale of the assets to the SPE happens it may be both the lease receivable and title to the actual underlying property that passes to the SPE—especially if the aim is to structure an SPE that is itself sharia-compliant. This differs from a traditional securitization with non-sharia products, in which it is only when foreclosure occurs and the property becomes real-estate-owned (REO) that ownership of the actual property may be ceded to the SPE.

We have framed this issue of sharia-compliance in the context of residential lending, but it may apply equally to the financing of other consumer receivables. For instance, the financing of an auto purchase typically also takes the form of a lease, in which ownership of the underlying automobile is maintained by the SPE until such time as lease term has ended, at which point ownership of the automobile transfers to the lessee.

In the case of residential lending, where the SPE (not the borrower) actually owns the property, it may also be liable for ancillary expenses and maintenance responsibilities in relation to these properties, as well as being exposed to potential undeterminable one-off liabilities regarding the property. Furthermore, in some countries (for instance, Dubai) lessees can set off property maintenance charges against lease installments.

The same scenario could potentially apply also to auto loans, in which the automobile is still actually owned by the SPE, and so the issuer may continue to have expenses, responsibilities, and potential liabilities in relation to this ownership.

From a credit perspective, when rating a transaction secured on such products, we would seek to assess, quantify, and model the potential expenses to the SPE that could arise from its ownership of these underlying assets, in order to form an opinion as to whether to consider the SPE bankruptcy remote to the relevant rating level or not. These expenses could, for instance, take the form of fees paid to a third-party property management or auto maintenance company to ensure that the quality of the assets is maintained at a viable level. However, there may be cases where there are potential liabilities that cannot be easily predicted or quantified—for instance, the risk of a claim against the property owner by a third party. We would seek to understand whether such risks are mitigated, for example, through an insurance policy or indemnification from an appropriately rated third party. Should there be the risk of contingent expenses or claims that cannot be quantified and/or are not adequately mitigated either internally or externally, this would affect our view of the SPE's bankruptcy remoteness. We deal with this in more detail in the section on legal considerations below.

Recovery process

As stated above, the nature of sharia-compliant products is often such that outright ownership of the underlying asset (be it a property, automobile, etc.) does not pass to the obligor until the term of the financing has ended. Until then, it is the obligee that maintains ownership of the underlying asset. As such, the equivalent of enforcement or foreclosure proceedings against the obligor in a manner typical of receivables secured by non-sharia mortgage products would not appear as pertinent to expected recoveries. Rather, it is the legal ability to remove a non-current obligor from a property, or the ability to reclaim a vehicle from a non-current obligor, that becomes more important.

Under certain circumstances and in certain jurisdictions, it may be the case that because the issuer holds the actual title to the property or automobile, it is easier to remove a noncurrent obligor than is the case for a traditional mortgage or auto loan (as in the latter case the defaulted borrower holds the title). However, it can also be the case in other jurisdictions that the ability to take action against an obligor that is not current on payments is very limited, in particular in the case where the asset is a property (as opposed to an automobile) that is the primary occupancy of the obligor. We would assess the extent to which the latter is a risk, and assume a lower recovery rate should the process for removal of a non-current obligor be ill-defined, cumbersome, or untested. Likewise, we would assess the potential cost of such a process, and factor this into our loss estimate.

A final consideration that relates to the recovery process is the arrears management function of the servicer. In many jurisdictions there has not necessarily been a substantial

downturn in the asset class being securitized, and as a result there may not yet be any significant experience servicing delinquent residential and consumer loans in substantial volume. In such circumstances, we would assess the extent to which the servicer has the capacity, flexibility, and planning in place to handle any sudden increase in arrears management activities and requirements. Likewise, if there is not a broad and liquid market for servicing the specific residential or consumer asset class being securitized, our analysis may include whether there is standby servicing in place from the outset of the transaction to avoid disruption in the servicing and arrears management procedures.

Geographic concentration

In our analysis of residential and consumer receivables in any jurisdiction, we typically take account of the geographic concentration of the receivables within a country, as well as the level of diversification of the economy of that specific country. The aim is to capture the additional risk that is posed by a pool of receivables that is geographically concentrated in an undiversified economy compared with the lesser risk of a pool of receivables that is geographically diversified across a number of more economically diversified regions. In our credit analysis of such receivables in the GCC/MENA region, we would give credit to the latter and make more conservative assumptions in our analysis of the former. In particular, we would focus on any exposure to a specific segment of an economy (for instance, residential homes primarily occupied by expatriate employees working mostly in one sector of an undiversified economy).

Occupancy status

In relation to residential receivables, an additional consideration is the occupancy and ownership status not just of such specific properties, but also of the market as a whole. In certain real estate markets in this region—for instance, that of Dubai—a sizeable proportion of demand is derived from expatriates, second-home buyers, and private or institutional investors. Such demand is generally more volatile than a source of demand that arises from owner-occupiers. Likewise, the type of real estate development that is undertaken to satisfy such demand can create a supply of properties that might not meet owner-occupied requirements outside of this specific buyer segment.

As such, we would assume an appropriate increase in the foreclosure frequency associated with such loans (given the possibly more speculative or discretionary nature of such residential house purchases), as well as a potential increase in the loss severity assumed (given the risk in a stressed environment of a number of such properties on the market depressing pricing in that specific market segment). This is in line with our rating assumptions used in other developed and developing markets. Also, we would take into account the property type—for instance, there might be more risk in luxury apartments than in residential villas, if demand for the latter proves to be more stable and domestically oriented, while demand for the former proves to be less stable and more expatriate-derived.

Residential house price trends

We outlined above that a challenge in setting default assumptions for new markets in this region is the lack of historical data on the performance of collateral through a number of different economic cycles, including adverse points in these cycles. Those comments pertained to the probability of default of an obligor, which is the basis for the WAFF that we assume. However, these same observations apply to the quantification of loss upon default, which is the basis for the WALS that we assume. Loss severity for a property or vehicle is driven by the assumed appreciation or deprecation in the value of the asset when repossessed or reclaimed. Should the financing product be one in which the obligee owns the underlying property until the outstanding balance has been repaid in full, then an alternative approach might be to assess the extent to which the repossessed property or vehicle (which was already, in any case, owned by the SPE before a default of the obligor) could be leased under similar terms to another obligor.

In the case of residential properties, we would assume a recessionary market value decline in the value of the property. This is typically an estimate of potential house price volatility, and we generally take into account the specific nature of the property market of the jurisdiction in question, as well as the severity and duration of previous housing market declines in that same jurisdiction (or comparable jurisdictions). However, there appear to be few reliable time series of house price data available for the GCC/MENA regions, and where data does

exist it is generally for a short period in which economic conditions were benign. Indeed, the extent of house price increases in recent years in such emirates as Dubai and Abu Dhabi presents a challenge in assessing what a potential market value decline of such properties would be during a recession. As a result, the approach we would expect to take would be to analyze comparative house price movements in other developed and developing countries with more extensive data availability, and to apply a suitably conservative assessment of the potential magnitude of recessionary house price declines on this basis.

In the case of auto lending, on the other hand, we would expect to receive static net loss data that indicates the actual write-offs after recoveries, with the latter including vehicle sale proceeds and other recovery sources. As with our default assumptions for auto lending, when establishing recovery assumptions, we would assess the quality of the data provided by the lender, take into account the extent to which it reflects benign or recessionary periods, and derive recovery expectations accordingly.

Cash Flow Considerations

General approach

When assigning ratings to residential mortgage loans, we run a cash flow model simulating the performance of the specific portfolio of loans—using the transaction's actual priority of payments (the so-called "waterfall")—under certain scenarios to test the ability of the assets (loans or leases) to generate sufficient cash flows to pay the notes and other obligations. Prepayment levels, interest rates, delinquency timing, and expenses payable by the issuer are the most important parameters stressed in such scenarios. Should there be potential credit losses resulting from the insolvency of the seller or servicer of the assets (for instance, commingling and set-off risk), we would also quantify these in the cash flow model when sizing the required levels of credit enhancement.

Similarly, for automobile loans (and certain other consumer finance transactions) we make assumptions on the timing of defaults, delinquencies, and prepayment levels. These are based on the standard assumptions that we apply to consumer finance transactions with similar types of assets across securitizations, which may nonetheless be modified to ensure relevance by jurisdiction and product type. We test different scenarios of the cash flows throughout the life of the transaction under different stress scenarios and corresponding to different rating levels.

In the case of residential and consumer loans from the GCC/MENA region, we would assume the approach outlined above to the extent that it applies to both the assets and the priority of payments, which would often be the case. However, we would take into account a number of additional considerations to ensure that the approach we take is suitable. The following four additional considerations are outlined in more detail below.

- Interest rate risk
- Currency risk
- Recovery timing
- Expenses

Interest rate risk

In any transaction in which there is a rating-relevant potential mismatch between the interest rate referenced by the assets and the liabilities, we take account of this during our cash flow analysis. Such a potential mismatch or basis risk generally relates to the nature of the rate or index (fixed, floating, etc.), the reference index itself (London interbank offered rate, or LIBOR, European interbank offered rate, or EURIBOR, etc.), the periodicity of the index (one-month, three-month, etc.), and the actual date on which the index is referenced for calculations. The risk of such mismatches can be mitigated, e.g., through a swap. Where no mitigants are presented to us, we would usually stress the potential risk of rate and basis widening in our cash flow analysis of the respective transaction.

An additional consideration that may apply to transactions in certain GCC/MENA jurisdictions is the presence of government-imposed caps on rental increases. These exist in certain countries in the region, for instance in Dubai. In a rising interest rate environment, such a cap would prevent the floating rate on the assets from rising, while the floating rate on the liabilities would nonetheless continue to rise. However, such a risk could be mitigated by an appropriately rated

counterparty assuming the risk—for instance, in the form of a swap that specifically makes whole on income shortfalls.

Furthermore, it should be noted that such caps on rental increases often apply only to existing tenants. Consequently, should a new occupier be sought for a property, the cap does not prevent an increase in the rent for such a new occupier. We would also take this into account when assessing any potential cash flow risk due to rental increase caps.

Currency risk

In any transaction in which there is a potential mismatch between the currency of the assets and the liabilities, we also take account of this during our cash flow analysis. However, such a risk could be mitigated by an appropriately rated counterparty assuming the risk—typically in the form of a balance guaranteed swap referencing the underlying receivables.

An additional consideration that may apply to transactions in certain GCC/MENA jurisdictions is the existence of currency pegs to other currencies, for instance the UAE dirham, which is pegged to the U.S. dollar. While on a superficial level this may seem to mitigate currency risk in certain circumstances (for instance, if liabilities are in the foreign currency unit to which the domestic currency unit is pegged), it cannot necessarily be relied on completely to mitigate currency risk. The possibility remains that the currency peg could be broken, in which case the value of the assets (in domestic currency) could depreciate in value versus the value of the liabilities (in foreign currency). This previously happened with the Kuwaiti dinar, which in 2007 had its peg switched from the dollar to a basket of currencies. We understand that the UAE is also currently underway regarding the possibility of breaking the peg between the dirham and the dollar, although the outcome of this still appears uncertain. As a result of such potential uncertainties, if the risk of such a currency peg being broken is not mitigated by, for instance, currency options, we would expect to appropriately stress it in our cash flow analysis.

Recovery timing

Should an underlying obligor default, it is the ability to recover the underlying asset (property, auto, etc.) that is important for credit purposes, but it is also the timing of this recovery that is important for cash flow purposes. For instance, in a developed mortgage market with typical secured mortgage loan products, should it become necessary to foreclose upon a borrower, we assume the time it could potentially take to recover the property—under benign to stressed market conditions—would be between 18 months and seven years (depending on the jurisdiction).

In many GCC/MENA jurisdictions, an assessment of potential recovery timing can be complicated by two factors. First, there is generally very little aggregate history of recovery timing against which to benchmark what is probable in benign and stressed market conditions. Second, if the products are sharia-compliant it may often be the case that the underlying asset (property, auto, etc.) is actually owned by the seller, SPE, or lessor—in which case the actual ownership of the asset does not have to be changed, rather the existing occupier or user of the asset must be removed and the asset repossessed. In such instances, recovery timing may essentially become comparable to the ability to act against a defaulted lessee. In certain countries (for instance, Saudi Arabia) it may be quite difficult to do so, whereas in others (for instance, Dubai) there appears to be a broader capacity to do so. In each case, we would assess for the product and jurisdiction in question what are reasonable expectations in terms of not just the ability but also the time it takes to recover, and we would then apply suitable assumptions when rating transactions.

Expenses

In any transaction there are generally certain expenses that we would model, which involve servicing of the assets—with the latter being defined as the receivables (for instance, auto or mortgages loans), rather than the underlying security (for instance, actual automobiles and properties). However, in circumstances where the SPE actually owns the underlying property during the tenor of the loan, lease, or other obligation (which could be the case in GCC/MENA transactions) there could be additional ongoing expenses that relate to the maintenance and repair of the assets themselves, as well as unexpected expenses that also relate thereto. The extent to which these expenses are covered by the obligor or obligee may vary by contract type, product, and jurisdiction.

Depending upon the exact circumstances relevant to a specific product, transaction, or jurisdiction, we would assess potential expenses and liabilities to be paid by the obligee in our cash flow analysis, and also assess whether we can rely on

a suitably rated third party that has assumed part of this risk, if this is the case.

Legal Considerations

General approach

Securitization structures are usually aimed at isolating the underlying assets (receivable and collateral) from the originator's bankruptcy risk so that the likelihood of payment on the issued securities (and thus the rating thereon) is not affected by the originator's creditworthiness. Besides an assessment of credit risk and cash flow modeling, our rating involves an analysis of whether the underlying legal regimes support this. The following is meant as a brief overview of some of the aspects of our legal analysis that are likely to be relevant in transactions involving residential and consumer receivables in the GCC and MENA regions. For a more detailed description of the most pertinent elements of our approach to analyzing legal risks in structured finance transactions, reference can be made to "Criteria|Structured Finance|Legal: European Legal Criteria for Structured Finance Transactions" (see "Related Articles" below). We have also recently published an analysis of the bankruptcy regime of one particular jurisdiction, the UAE, in the article "Debt Recovery For Creditors And The Law Of Bankruptcy In The United Arab Emirates" (see page 16 of this publication).

The following four additional considerations are outlined in more detail below:

- Key principles
- Assets
- Asset isolation
- SPE bankruptcy remoteness
- GCC / MENA legal environment

Key principles

Part of our legal analysis is to understand the rating-relevant legal risks in the transaction that could affect the availability of the assets or related cash flows on which the rating on the structured securities relies, or otherwise cause disruption to the timely servicing of the securities. If we come to the view that a risk is not remote enough, or not adequately mitigated, to be commensurate with the relevant rating level, we would factor it into our rating decision. Depending on the type of risk, this could mean, for example, that we adjust our credit or cash flow assumptions or that our rating is linked to the creditworthiness of the originator or other relevant parties.

Structured finance transactions often involve multiple jurisdictions and legal regimes, such as the jurisdiction of incorporation of the originator, the law governing the assets, the law governing the transfer thereof, and the jurisdiction of incorporation of the SPE to name a few. For each transaction rated by us, we generally expect to see legal opinions dealing with the relevant issues under the relevant legal regimes. These opinions are usually issued by external counsel to the arranger, originator, or issuer. Whilst we may in certain cases choose to seek the (additional) view of our own external counsel—e.g., to help us identify the relevant questions—the opinions and memoranda provided to us by the lawyers to the transaction parties, and our discussions with them, usually constitute the primary source of legal comfort on a specific transaction. These experts thus play a key role in helping us understand the relevant legal risks to the structure. We encourage legal counsels to the transaction to approach us early on in the rating process with their opinions in order to identify relevant issues as early as possible.

Our ratings do not address the compliance of a transaction with sharia law. Accordingly, our legal analysis does not entail anything that would support this.

Assets

The existence of the securitized assets can be influenced by several legal factors which we deal with differently in our rating analysis. For instance, we generally expect the originator, who has been involved most closely in the documentation process, to provide a representation that the assets are valid and in existence. If such a representation is given, we would usually not expect to be provided with an additional legal opinion addressing the risk that the underlying contract (loan agreement) is unenforceable for whatever reason. Legal opinions do, however, usually deal with the risks of set-off and dilution by explaining whether and how the assets could extinguish or become unenforceable as a result of set-off rights of the debtor and whether and how the borrower could be entitled to refuse payment as a result of defective

goods or services. If such a possibility exists, legally and practically, we would take it into account in our credit and cash flow analysis in absence of adequate mitigants.

When rating a new type of asset in a new jurisdiction for the first time, we may seek to understand more generally the relevant legal environment, and ask for pertinent information from transaction counsel. For instance, in the context of a first RMBS transaction, we may ask for information about the kind of security; how it is evidenced; how this interest is protected upon personal bankruptcy of the debtor; whether property titles exist; remedies of the lender; details, experience, and lengths of the foreclosure procedures and parties involved; whether the lender is entitled to full recovery; and so forth. This will help us form a view on the assumptions we would make in terms of extent and timing of recoveries. Both practical as well as legal aspects can play a role in this. In parts of the GCC/MENA region, both the relative lack of enforcement experience and the influence of sharia principles on enforcement steps taken against individuals could potentially affect our recovery assumptions. Sometimes, the involvement of bodies other than courts in disputes between originator and debtor can add an additional layer of uncertainty (e.g., in Dubai the Rent Committee has jurisdiction to hear disputes between landlords and tenants). The feature seen in the lease-like, sharia-based lending products whereby the financed asset (property, vehicle, etc.) is legally owned not by the borrower but by the lender/SPE could on the other hand have a positive effect on recovery prospects, compared with the commonly known non-sharia products where the asset is "merely" subject to a security interest (e.g., mortgage).

Asset isolation

The isolation of the assets from the originator's bankruptcy risk is often to be achieved through a sale and transfer of the assets from the originator to the SPE. Among other things, the transaction's legal opinion would usually deal with two aspects of this: That the sale and transfer is enforceable and effective under all applicable laws to transfer the assets to the SPE, and that it will be recognized in and not affected by a subsequent bankruptcy of the originator.

The first aspect relates to issues such as the transferability of the assets, registration requirements, requirements to notify the debtor or obtain his consent, contractual restrictions on assignment, the influence of data protection and bank secrecy rules, whether the transfer is effective against third parties, etc. Many jurisdictions in the GCC region generally seem to recognize the concept of assigning rights under a contract, either through explicit statutes (e.g., Kuwait, Bahrain, Qatar) or court practice (e.g., UAE and Oman). However, the practical experience with assignments would often appear limited, and the details with respect to the governing rules sometimes uncertain. In Dubai, for instance, there seems to be some uncertainty as to whether a "silent consent" would be sufficient where the underlying asset agreement stipulates that consent to the asset's transfer is needed. The assignment of receivables is to be distinguished from the transfer of any collateral, or collateral enforcement proceeds that may be securing the loan, lease, etc. That transfer is usually governed by separate rules depending on the type of collateral (e.g., mortgage over land, title to vehicle). Its relevance in our analysis is in the context of factoring collateral enforcement proceeds into our credit and cash flow assumptions. Here, the sharia-based products mentioned above show certain particularities because the collateral securing the debt owed by the debtor is not, in legal terms, a security interest but full legal title to the financed asset (e.g., real estate or vehicle). A transfer of legal title to the financed asset to the SPE can have certain implication on our SPE bankruptcy remoteness analysis (see below). It is also sometimes subject to stricter rules than a transfer of security. For instance, in Dubai the rules regarding foreign ownership of land would seem to restrict the transfer of financed properties in the context of an RMBS transaction to either a transfer to a Dubai or GCC resident SPE or to a transfer of properties in certain designated areas.

The second aspect is primarily a question of the bankruptcy regime that would govern a bankruptcy of the originator. From our experience, there are two points to consider in particular. The first one, often referred to as "re-characterization risk," is the question whether, upon bankruptcy, the sale of the assets will continue to be recognized as such, i.e., constitute a "true sale," or whether it could be re-characterized by the bankruptcy official or court as a loan from the SPE to the originator collateralized by a security interest over the assets. In some jurisdictions this could have an adverse impact on the SPE's

rights regarding the assets, e.g. because such a security interest would have had to be registered in a special register or because its enforcement would be subject to delays, haircuts, and other restrictions in case of the originator's bankruptcy. The second point is often referred to as "preference" or "claw-back risk" and relates to the principle incorporated in many bankruptcy regimes by which certain transactions (e.g., a sale of assets) can be set aside by the bankruptcy official or court under certain conditions. To date, many of the GCC/MENA countries' bankruptcy regimes are still relatively untested, which can influence the degree of comfort the relevant legal opinions may be able to provide on these points.

SPE BANKRUPTCY REMOTENESS

Securitization usually also involves a transfer to a "bankruptcy remote" SPE. That entity is to serve as a "safe haven" for the assets and may either issue the asset-backed notes itself or enter into a financing arrangement with another bankruptcy-remote SPE that acts as note issuer. Many SPEs in transactions we rate are not "bankruptcy proof" by law, i.e., they are corporate entities, or partnerships, which could by law be subject to bankruptcy proceedings in their jurisdiction just like any other operating company. In the process of forming our opinion on whether to consider a bankruptcy of such an SPE remote to the rating on the relevant security, we would consider whether the SPE in the given transaction satisfies certain features, which would reduce the likelihood of a voluntary or involuntary bankruptcy, in our view. These criteria—which are explained in detail, for instance in our European legal criteria (see "Related Articles")—can broadly be divided into the following categories: Restrictions on objects and powers, debt limitations, independent directors, no merger or reorganization, separateness covenants, and security interests over assets. Each of these is in principle significant in our overall bankruptcy remoteness analysis.

SPEs incorporated in offshore jurisdictions (e.g., Jersey, Ireland, Cayman Islands) are likely to be less affected by the relative lack of practical experience with bankruptcy regimes in the GCC/MENA region (although this could still play a role in our analysis where the domestic regime allows local bankruptcy). The lack of experience is likely to be more relevant for transactions involving domestic SPEs, such as a Dubai-incorporated SPE used to hold title to the securitized assets because of the restriction on foreign ownership of assets in the UAE. We already mentioned above that certain securitizations of sharia-based assets may involve a transfer of legal title to the financed real estate or vehicle to the SPE. Where this is the case, we would seek to understand from transaction counsel which liabilities may arise to the SPE as a result of owning the property. Often, the ownership of real estate can entail several potential liabilities, ranging from fees and taxes to unexpected types such as environmental liabilities or accident-related personal injury claims. Whilst fees and taxes can be sized for, the unexpected type of liabilities presents a much greater challenge to the SPE's bankruptcy remoteness. Features such as insurance policies can to some extent mitigate that risk, but might not be able cover the risk fully, or bear in themselves certain risks. Another consideration in the bankruptcy remoteness analysis of SPEs used in the GCC/MENA region is likely to be the lack of certainty that seems to exist in many parts of the region as to the effectiveness of security granted over local bank accounts. As part of our analysis, we generally seek to understand whether the SPE owns significant assets that are not effectively secured in favor of, for instance, the trustee. We do this to take a view on how this may increase third parties' incentive to seek a bankruptcy of the SPE.

GCC/MENA LEGAL ENVIRONMENT

The GCC/MENA region consists of many different jurisdictions, each of which has its legal framework and some, like the UAE, even more than one. We have dealt above with some specific challenges that some transactions in the region could face compared with transactions in more established securitization markets. There are other potential challenges of a more general nature. One of these is the influence of sharia principles on the enforceability of the underlying transaction and asset documentation, and the unpredictability that may follow from that. In certain countries, commercial and civil codes restrict the influence of sharia law to such domestic matters as probate and family law. In others, however, sharia plays a more significant role in that its principles still override local laws, or that the entire legal regime is based on sharia (e.g., Saudi Arabia). Another potential challenge is that many of the legal regimes remain untested to date in many aspects. The general lack of jurisprudence often makes it more difficult for the lawyers to opine on specific untested matters of laws by,

for instance, applying known principles of interpretation followed by the courts. Other areas of uncertainty expected in some of the GCC/MENA jurisdictions include the recognition and enforceability of foreign law as the governing law of transactions. An additional layer of complexity or legal uncertainty is added to transactions in certain countries where there exists a continuum between the judicial branch of government, the executive branch of government, and the ultimate ruling authorities or family.

Given the diversity of the region, we have not tried in this article to anticipate all rating-relevant legal challenges that a securitization transaction may face, let alone for each jurisdiction. Our experience in other securitizations markets at times when these markets were still nascent has shown that the creativity of arrangers and lawyers has often managed to address some of the challenges initially posed. Sometimes, of course, challenges are of a type that cannot be overcome structurally, and may ultimately affect the rating we are able to assign. Overall, we think that the recent legislative developments in the region show that the legal environment is getting more favorable to complex financial products, such as securitization. The ambitions of many of the countries to create Western-style financial centers also seems to increase an awareness of the need to create the stable legal environments that investors and other market participants usually associate with global financial centers. The development of Dubai International Financial Centre (DIFC) and the Qatar Financial Center (QFC), together with their separate legal regimes, are both noteworthy in this context. Similarly, the desire to foster local consumer finance markets has also brought various positive developments, such as the newly established property registration system in Dubai that ensures title can be effectively registered or the anticipated new mortgage law in Saudi Arabia.

Sovereign Considerations

While the sovereign rating on the country of domicile of the assets that underlie a transaction does not "cap" our structured finance ratings, many country-specific risks can affect the performance of a transaction. Therefore, we examine sovereign and country-specific risks when sizing stresses and possible mitigants in a structured finance transaction. Among the factors we commonly consider, and that we discuss below, are:

- Underlying sovereign ratings
- Performance of assets under sovereign debt default scenario
- Currency transfer and convertibility restrictions
- Exchange rate risk
- Government interference affecting transaction or cash flows
- Domestic financial system risk

Underlying sovereign ratings

The sovereign ratings in the GCC region are supported mainly by governments' balance-sheet strengths and external liquidity. The transformation of GCC economies to more-diversified, private-sector-led economies is thus a long-term aspiration that has only a marginal immediate effect on the sovereign's credit ratings. More significant in the near-term is the effect of geopolitical risk, which remains the principal constraint on GCC sovereign ratings.

The sovereign ratings perspective in the region will depend largely on the evolution of key geopolitical risks, including for example the situation in Iraq and tensions between the West and Iran. The balance-sheet strength of the rated GCC states means that the possibility of these risks materially affecting the sovereign's creditworthiness, even were they to materialize, is in practice small. Nevertheless, these risks differentiate the GCC states from higher-rated sovereigns, and the positive ratings prospects for most will continue to be tempered by the higher-risk political environment that prevails in the region.

The table on the next page provides the global scale local currency and foreign currency ratings on a number of sovereigns in the GCC/MENA region *(Editor's note: the table has been updated as of May 13, 2009. For the most recent ratings information see RatingsDirect).*

Performance of assets under sovereign debt default scenario

A sovereign default scenario often entails a major general economic stress situation, with rising defaults across a range of residential and consumer asset classes, including mortgages, automobile loans, etc. Rating a structured finance transaction

Table 1: Global Scale LC And FC Ratings On Certain Sovereigns In GCC / MENA Region

Country	Sovereign LC ratings (long-term/outlook/short-term)	Sovereign FC ratings (long-term/outlook/short-term)
Abu Dhabi	AA/Stable/A-1+	AA/Stable/A-1+
Bahrain	A/Stable/A-1	A/Stable/A-1
Egypt	BBB-/Stable/A-3	BB+/Stable/B
Jordan	BBB/Stable/A-3	BB/Stable/B
Kuwait	AA-/Stable/A-1+	AA-/Stable/A-1+
Lebanon	B-/Stable/C	B-/Stable/C
Morocco	BBB/Stable/A-3	BB+/Stable/B
Oman	A/Stable/A-1	A/Stable/A-1
Qatar	AA-/Stable/A-1+	AA-/Stable/A-1+
Ras Al Khaimah	A/Stable/A-1	A/Stable/A-1
Saudi Arabia	AA-/Stable/A-1+	AA-/Stable/A-1+
Tunisia	A-/Stable/A-2	BBB/Stable/A-3

**All ratings correct at May 13, 2009. LC—Local currency. FC—Foreign currency.*

higher than the rating on the jurisdiction in which the securitized assets are located implies a measurable probability that the transaction would continue to meet its debt service obligations even when the sovereign does not. The same factors that underlie a government default would likely lead to deteriorating performance of mortgage receivables, since borrowers are subject to the same political, social, and economic infrastructure. This may affect default rates, as well as recovery values.

The likelihood that the sovereign will default on its foreign currency debt is reflected in the sovereign foreign currency rating *(see table 1 above)*. Hence, we would typically assess the extent to which a sovereign default on its foreign currency debt is accompanied by a general economic stress scenario. If the transaction's notes are rated above the level of the sovereign foreign currency rating, we would form a view on whether those notes could withstand a specifically harsh economic stress scenario, reflected for instance in high asset default rates and lower recoveries.

Currency transfer and convertibility restrictions

Our transfer and convertibility assessment relates to the probability of a sovereign restricting nonsovereign access to foreign exchange it needs to service its debt. We generally base our assessment on a review of the sovereign's foreign exchange regime and economic policy orientation, as well as its external management flexibility *(see "Ratings Associated With Risk Of Foreign Exchange Controls Raised In 27 Countries" in "Related Articles")*.

For transactions that depend on the conversion and transfer of local currency (generally, cross-border transactions whose rated securities are denominated in foreign currency), restrictions on access to foreign exchange needed for debt service can cause a default on the securities. Consequently, for notes of such transactions to achieve a foreign currency rating above the transfer and convertibility assessment of the country in which the assets are domiciled, we would typically expect this risk to be mitigated. We have seen this risk addressed in the form of an adequately rated counterparty to the transaction

(for instance, the swap counterparty) assuming the risk of disrupted payments, or by a third-party guarantee, or political risk insurance covering debt service on these notes. In such instances, it is possible for a transaction's notes to be rated higher than the transfer and convertibility assessment of the country in which its assets are domiciled.

We regularly publish updated tables of all global transfer and convertibility assessments. The most recent the assessments for countries in the GCC/MENA region are provided in table 2 (updated as at May 13, 2009).

Exchange rate risk

Notes denominated in foreign currency that are secured by domestic assets may be directly or indirectly exposed to exchange rate risk. Exchange rate volatility is present at all rating levels, although typically, under a sovereign default scenario, the probability of major currency fluctuations would increase significantly.

If the payment streams of the underlying borrowers are in local currency, while the notes are payable in foreign currency, exchange rate risk is borne directly by the issuer. Currency depreciation could therefore affect:

- *Solvency:* The adequacy of cash flows generated by the assets to pay the transaction's notes could deteriorate, as the SPE seeks to pay its interest, principal, and expenses in an appreciated nondomestic currency, while the inflows generated by its assets to meet these payments have been reduced through local currency depreciation.
- *Leverage:* The leverage of the transaction would increase, as the SPE's domestic-currency assets would have depreciated compared with its non-domestic-currency liabilities.

Exchange rate risk can potentially be mitigated, for example, by a swap with an adequately rated counterparty. If the payment streams from the underlying borrowers are in (or linked to) a foreign currency, so that there is no direct exchange rate risk at the issuer level, then the borrowers themselves may be exposed to exchange rate risk. When rating transactions in which the underlying assets comprise nondomestic-currency loans, we generally assume that the borrower is paid in domestic currency, or—if his income is indexed to a foreign currency—that the borrower may potentially have their income de-indexed from this foreign currency back to the domestic currency.

The extent and duration of currency depreciation we assume when analyzing a transaction depends on, and is appropriate to, the rating on the specific note.

Government interference affecting the transaction or cash flows

Direct government interference in a transaction may take many forms, and we assess on a transaction-by-transaction basis whether we believe that such a risk applies. Such government action may include—but is not limited to—expropriation or invalidation of the transaction contracts, if a government ceases to recognize the issuer's ownership of (or security over) the underlying assets, and as a result also ceases to recognize its entitlement to the current and future flows generated by these assets.

While this risk is in many cases not the one that most constrains a transaction's rating, it is a risk that can usually be mitigated by external support from third parties, e.g., by political risk insurance. The possibility of this risk crystallizing would be assessed even in the absence of prior events of

Table 2: Global T&C Assessments*

Country	Transfer and covertibility assessment
Abu Dhabi	AA+
Bahrain	AA-
Egypt	BBB-
Jordan	BBB
Kuwait	AA+
Lebanon	B+
Morocco	BBB
Oman	AA-
Qatar	AA+
Ras Al Khaimah	AA+
Saudi Arabia	AA+
Tunisia	A-

**Updated as of May 13, 2009.*

interference in receivables in the specific jurisdiction in which the assets are domiciled, in which case the approach adopted may potentially be informed by interference that has occurred in other jurisdictions.

Government action can also affect the cash flows generated from the underlying assets. This interference is not limited to, but may be likely to occur in, the context of a general economic stress situation. In our view, the likelihood of such interference may, for instance, depend on the nature of the underlying assets. If the government considers housing to be a politically sensitive topic, for example, then government action in the mortgage market—hence affecting a transaction—may be more likely than action in other consumer asset classes. Such sovereign interference can take manifold forms, and we assess to what extent the structure of a given transaction might be exposed to such actions.

Domestic financial system risk

In a financial sector crisis, the functioning of the banking system may be limited temporarily for several reasons, and could thereby jeopardize debt service payments on the rated notes. To prevent bank runs or capital flight, for instance, governments may temporarily close down the banking system, limit cash withdrawals, freeze accounts, or restrict bank transfers. Under such a scenario, the underlying borrowers' ability to pay their obligations may be limited. In addition, it may be likely that a large segment of the banking system will itself become insolvent and default. This may create individual or systemic risks that threaten the safety of onshore reserve and liquidity accounts, as well as risk interrupting transfers of funds through the domestic financial system.

Potential mitigants to the risk of a temporary unavailability of the domestic banking system include the existence of a liquidity facility or an offshore reserve account. We review the flow of funds and payment mechanics for each specific transaction, and simultaneously assess the domestic and overseas accounts, reserves, and liquidity facilities available to the issuer—in both cases, in light of the rating level being sought for the notes to be issued. On this basis, we would form an opinion on the extent to which this risk crystallizes, and then also review the extent to which structural mitigants may be in place.

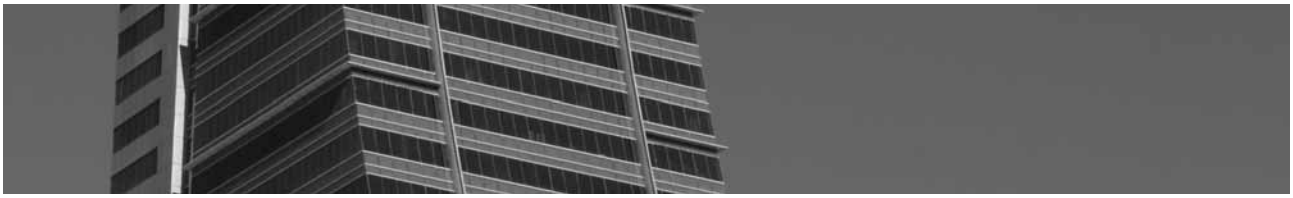
Table 3 summarizes the different types of sovereign risk with examples of sizing or potential mitigants thereof.

Concluding Remarks

The securitization of residential and consumer receivables in the GCC/MENA region provides a number of potential challenges in terms of certain aspects of our credit, cash flow, structural, and legal analysis. In analyzing and taking these into account in our rating decisions, we will be using our broad experience from other emerging markets and other new jurisdictions, combined with our understanding of local market practices already gained from collateral reviewed and/or transactions rated in the GCC/MENA region. As residential and consumer lending volumes continue to expand in this region, the balancing of such risks and the mitigation thereof will become an increasingly key opportunity for lenders and capital market participants in the region.

Table 3: Sovereign-Related Risk

Type of country-related risk	Sizing or examples of possible mitigants
Asset performance affected by circumstances of sovereign stress	Risk is stressed in credit/cash flow analysis
Transfer and convertibility restrictions	Structural/third-party mitigation (e.g., political risk insurance or an appropriately structured swap)
Currency depreciation	Risk is stressed in credit/cash flow analysis if unmitigated
Domestic bank freeze	Structural/third-party mitigation (e.g., offshore reserve account)
Government interference	Risk is stressed in credit/cash flow analysis; structural/third party mitigation for forms of direct interference may be required (e.g., political risk insurance)



Related Articles Available On RatingsDirect

Sovereign Ratings And Country T&C Assessments, Aug. 19, 2008.

Debt Recovery For Creditors And The Law Of Insolvency In The United Arab Emirates, Aug. 19, 2008.

Ratings Definitions, Sept. 21, 2007.

Corporate And Counterparty Credit Ratings That Exceed The Sovereign's Rating, Sept. 10, 2007.

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All criteria and related articles are available on RatingsDirect, the real-time Web-based source for Standard & Poor's credit ratings, research, and risk analysis, at www.ratingsdirect.com. The criteria can also be found on Standard & Poor's Web site at www.standardandpoors.com.

Glossary Of Islamic Finance Terms

The Five Pillars Of Islamic Finance

THE BAN ON INTEREST
Interest must not be charged or paid on any financial transaction, as interest (or the intrinsic value of the money) is deemed unlawful by Sharia.

THE BAN ON UNCERTAINTY OR SPECULATION
Uncertainty in contractual terms and conditions is forbidden. However, risk taking is allowed when all the terms and conditions are clear and known to all parties.

THE BAN ON FINANCING CERTAIN ECONOMIC SECTORS
Financing of industries deemed unlawful by Sharia—such as weapons, pork, and gambling—is forbidden.

THE PROFIT- AND LOSS-SHARING PRINCIPLE
Parties to a financial transaction must share in the risks and rewards attached to it.

THE ASSET-BACKING PRINCIPLE
Each financial transaction must refer to a tangible, identifiable underlying asset.

Vocabulary Of Islamic Finance

BAY SALAM
A sales contract where the price is paid in advance and the goods are delivered in the future, provided that the characteristics of the goods are fully defined and the date of delivery is fixed.

DIMINISHING MUSHARAKA
A form of partnership in which one of the partners undertakes to buy the equity share of the other partner gradually until ownership is completely transferred to the buying partner.

GHARAR
An exchange transaction in which one or both parties remain ignorant of an essential element of the transaction.

HALAL
Lawful; permitted by Sharia.

HARAM
Unlawful; prohibited by Sharia.

IFI
Islamic financial institution.

IJARA
Lease financing. The purchase of the leased asset at the end of the rental period is optional.

IJARA MUNTAHIA BITTAMLEEK
A form of lease contract that offers the lessee the option to own the asset at the end of the lease period, either by purchase of the asset through a token consideration or payment of the market value, or by means of a gift contract.

IJARA WA IQTINA
Lease purchasing, where the lessee is committed to buying the leased equipment at the end of or during the rental period.

INVESTMENT RISK RESERVE
The amount appropriated by an IFI from the income of PSIA holders, after allocating the mudarib's share of the profit or mudarib fee (mudarib refers to the IFI as a manager of the PSIA), in order to create a cushion against future investment losses for account holders.

ISTISNA
A contract that refers to an agreement to sell to a customer a nonexistent asset, which is to be manufactured or built according to the buyer's specifications and is to be delivered on a specified date at a predetermined selling price.

MUDARABA
A contract between a capital provider and a mudarib (skilled entrepreneur or managing partner) whereby the IFI provides capital to an enterprise or activity to be managed by the mudarib. Profits generated by that enterprise or activity are shared in accordance with the terms of the mudaraba agreement while losses are borne solely by the capital provider, unless the losses are due to the mudarib's misconduct, negligence, or breach of contractual terms.

Murabaha
The financing of a sale at a determined markup (cost plus profit margin).

Musharaka
A contract between an IFI and a customer to provide capital to an enterprise, or for ownership of real estate or a moveable asset, either on a temporary or permanent basis.
Profits generated by the enterprise or real estate/asset are shared in accordance with the terms of the musharaka agreement, while losses are shared in proportion to each partner's share of capital.

Profit equalization reserve
The amount appropriated by an IFI from mudaraba income before allocating the mudarib share (fee; mudarib refers to the IFI as a manager of the PSIA), in order to maintain a certain level of return on investment for PSIA holders.

PSIA (profit-sharing investment account)
A financial instrument relatively similar to time deposits of conventional banks. According to the terms and conditions of PSIAs, depositors are entitled to receive a share of a bank's profits, but also obliged to bear potential losses pertaining to their investment in the bank. PSIAs can be restricted (whereby the depositor authorizes an IFI to invest his funds based on a mudaraba or wakala, with certain restrictions as to where, how, and for what purpose these funds are to be invested); or unrestricted (whereby the depositor authorizes the IFI to invest his funds based on mudaraba or wakala contracts without laying down any restrictions).

Qard hasan
A loan granted for welfare purposes or to bridge short-term funding requirements; it could also take the form of a nonremunerated deposit account. The borrower is required to repay only the principal.

Retakaful
A form of Islamic reinsurance that operates on the takaful model.

Riba
Usury.

Sharia (or Shari'ah)
Islamic law.

Stability rating
A rating that represents Standard & Poor's current opinion about the prospective relative stability of cash flow distributable to PSIA holders.

Sukuk
Sharia-compliant financial certificates similar to bonds.

Takaful
A form of Islamic mutual insurance based on the principle of mutual assistance.

Wadia
An amount deposited whereby the depositor is guaranteed his funds in full on demand.

Wakala
An agency contract where the investment account holder (principal) appoints an IFI (agent) to carry out an investment on his behalf either for or without a fee.

Sources: Islamic Financial Services Board and Standard & Poor's.

Key Contacts

Standard & Poor's Middle East Regional Office

Jan Willem Plantagie
Managing Director
Regional Manager Middle East
jan_plantagie@standardandpoors.com

Raeda Kassab
Office Manager
raeda_kassab@standardandpoors.com

Standard & Poor's
The Gate Village, Building 5
Dubai International Financial Centre
PO Box 506650
Dubai, UAE
Tel: (971) 4 709 6800
Fax: (971) 4 709 6888
www.gcc.standardandpoors.com

Sovereigns/Supranational Entities/ Public Finance

Farouk Soussa
Director
Dubai (917) 4 709 6820
farouk_soussa@standardandpoors.com

Moritz Kraemer
Managing Director
Frankfurt (49) 69 33 999 249
moritz_kraemer@standardandpoors.com

Group E-mail Address:
SovereignLondon@standardandpoors.com

Financial Institutions

Emmanuel Volland
Senior Director
Paris (33) 1 4420 6696
emmanuel_volland@standardandpoors.com

Mohamed Damak
Associate
Paris (33) 1 4420 7322
mohamed_damak@standardandpoors.com

Group E-mail Address:
FIG_Europe@standardandpoors.com

Insurance

Kevin Willis
Director and Takaful Specialist
London (44) 20 7176 7085
kevin_willis@standardandpoors.com

David Anthony
Director
London (44) 20 7176 7010
david_anthony@standardandpoors.com

Group E-mail Address:
InsuranceInteractive_Europe@standardandpoors.com

Project Finance/Utilities/Corporates

Jon Manley
Senior Director
London (44) 20 7176 3952
jon_manley@standardandpoors.com

Peter Tuving
Managing Director
Stockholm (46) 8 440 5913
peter_tuving@standardandpoors.com

Mohammed Fayek
Rating Specialist, Islamic Finance
London (44) 20 7176 3408
mohammed_fayek@standardandpoors.com

Karim Nassif
Associate Director
London (44) 20 7176 3677

Group E-mail Addresses:
InfrastructureEurope@standardandpoors.com
CorporateFinanceEurope@standardandpoors.com

Structured Finance

Zeynep Adalan
Director
London (44) 20 7176 3703
zeynep_adalan@standardandpoors.com

Group E-mail Address:
StructuredFinanceEurope@standardandpoors.com

Legal

James Penrose
Managing Director and Senior European Counsel
London (44) 20 7176 3960
james_penrose@standardandpoors.com

Marketing

Claude Chaubet
Director
Corporate & Governments
London (44) 20 7176 3689
claude_chaubet@standardandpoors.com

Isobel McCalman
Senior Marketing Manager
Financial Institutions and Insurance
London (44) 20 7176 7233
isobel_mccalman@standardandpoors.com

Fleur Hollis
Marketing Executive
Financial Institutions and Insurance
London (44) 20 7176 7212
fleur_hollis@standardandpoors.com

Raeda Kassab
Office Manager
Dubai, (971) 4 709 6830
raeda_kassab@standardandpoors.com

Media

Matthew McAdam
Communications Officer
London
(44) 20 7176 3541

Group E-Mail Address:
media_europe@standardandpoors.com

Credit and Risk Training

Robin Burnett
Director,
Standard & Poor's European Risk Learning Institute
London (44) 20 7176 7019
robin_burnett@standardandpoors.com

Group E-mail Address:
CreditRiskTraining@standardandpoors.com
Group Website:
www.risksolutions.standardandpoors.com

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Vice President, Editor-in-Chief Bob Arnold

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Subscription Information

Hong Kong (852) 2533-3535, London (44) 20-7176-7425

Melbourne (61) 1300-792-553, New York (1) 212-438-7280, Singapore (65) 6239-6316, Tokyo (81) 3-4550-8711

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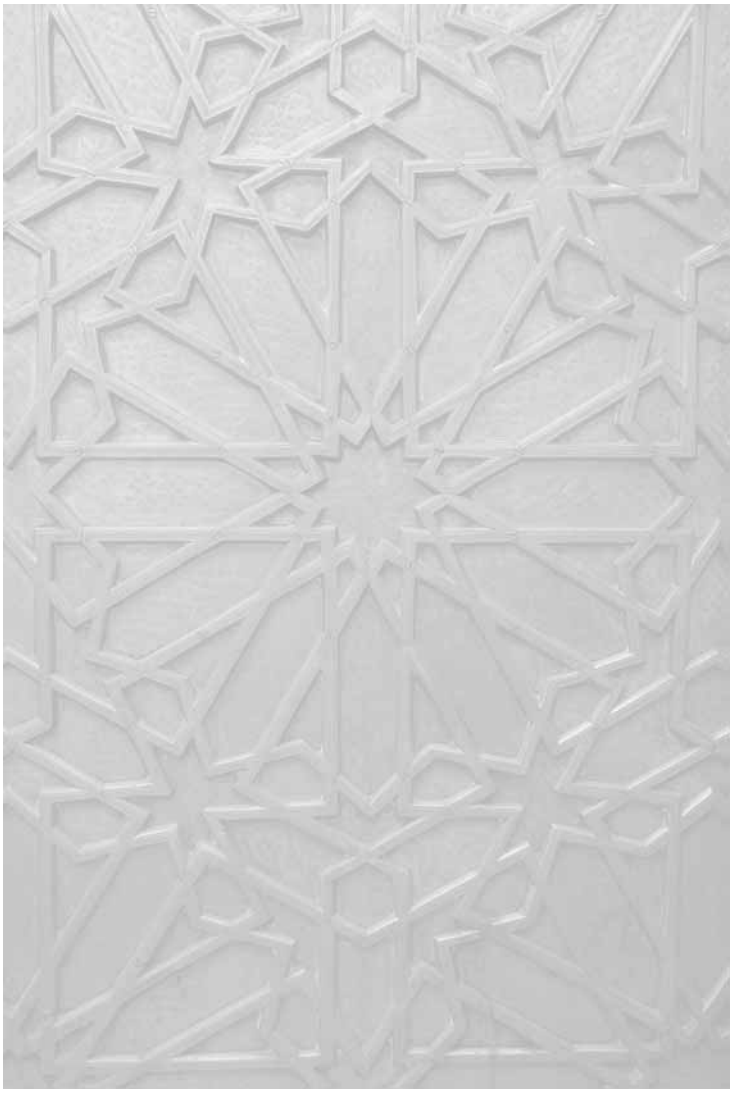
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STANDARD
&POOR'S

20 Canada Square
Canary Wharf
London E14 5LH, U.K.

Dubai International Financial Centre (DIFC)
The Gate Village, Building 5, Level 2
PO Box 506650, Dubai, UAE
www.gcc.standardandpoors.com

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