

REPORT ON THE INSURANCE MARKET SITUATION IN 2007

Podgorica, 30 June 2008

I Introduction

Main features of the Insurance market in 2007 and at the beginning of 2008 were the:

- Establishment of the Insurance Supervision Agency, as an independent regulatory body;
- Finalization of legislation governing the field of insurance;
- Establishment of new insurance companies and alignment of existing ones to the new legislation.

The institution competent for supervision and control of the insurance is the Insurance Supervision Agency, which is independent in performing tasks from within its scope of authority. The Agency was established in accordance with the Insurance Law (*Official Gazette of the Republic of Montenegro*, No 78/06 and 19/06). The founder of the Agency is Montenegro, and the Council of the Agency exercises the founders' rights on its behalf, in accordance with the Law. The Insurance Supervision Agency carries out the supervision of activities in the insurance industry having as the objective to spur the development of the insurance market and provide for adequate protection of the insured parties.

The Parliament of Montenegro appointed the Council of the Agency on 3 July 2007 (*Official Gazette of Montenegro*, No 42/07 of 12 July 2007). The Statute, Financial Plan, and Work Program for 2008 were adopted at the end of December 2007, therefore the Agency operates in its full institutional capacity since January 2008.

The Report on the State of the Insurance Market in 2007 is based on preliminary data, given that insurance companies are obliged to submit financial reports with the auditor's opinion and adopted by the General Shareholders' Meeting by no later than 30 June 2008.

II Legislation

The passing of the Insurance Law (*Official Gazette of the Republic of Montenegro*, No 78/06) in December 2006, the Law on Compulsory Transportation Insurance (*Official Gazette of Montenegro*, No 46/07) in July 2007, and the Law on Bankruptcy and Liquidation of Insurance Companies (*Official Gazette Montenegro*, No 11/07) in December 2007 has completed the legislative framework.

The Insurance Law governs the conditions and the manner of performing insurance activity, as well as supervision of insurance activities in Montenegro. The Insurance Law prescribes the method of founding and rules for operation of insurance companies. The following are particularly prescribed: a manner of risk assessment and determining the classes of insurance based on risk coverage principle; insurance company type; as well as method and rules on insurance risk management (capital adequacy, liquidity maintenance, determination of technical reserves in property insurance, and depositing and investment of technical reserves funds, as well as other risk management measures). Beside the abovementioned, the Law defines reinsurance, manner of performing actuarial and audit activities, manner and types of financial reporting, rules on internal audit enforcement, as well as forms and manner of performing insurance brokerage, insurance agency and rendering of ancillary insurance services.

Law on Compulsory Transportation Insurance governs the compulsory transportation insurance and defines classes of compulsory insurance, compulsory insurance contract, sum insured, insurance conditions and insurance tariffs, amount, deadlines and rights to indemnity, international identification on existence of Automobile Liability Insurance (Green Card), Border Insurance. The Law especially defines that it should be obligatory to establish the Association of Insurers of Montenegro – the National Bureau and a manner of its establishment of, which performs its activities through separate organizational parts: Green Card Bureau, Guaranty Fund and Information Centre.

The Law on Bankruptcy and Liquidation of Insurance Companies stipulates the bankruptcy and liquidation proceedings with reference to the application of the Law on Business Organization Insolvency.

During 2007, two enabling regulations were adopted, and so as follows:

- Rulebook on Detailed Requirements for Licensing Insurance, Brokerage and Agency Activities and Provision of Ancillary Insurance Services and the Manner of Proving the Fulfillment of such Requirements (*Official Gazette of the Republic of Montenegro* No 08/07 of 9 February 2007);
- Instructions on the Manner of Determining the Solvency Margin Level (*Official Gazette of the Republic of Montenegro*, No 24/07 of 4 May 2007).

Plans in the field of developing legislation aimed at creating the market attractive for further foreign and domestic investments, relate to implementation of current legal infrastructure and their elaboration through drafting of enabling regulations, in order for those to be further harmonized with the European Union legislation. Drafting of 12 enabling regulations, which shall elaborate in details the procedure for control of operations, reporting and manner of calculating basic indicators of insurance market development, is currently in progress¹, and so as follows:

1. Rulebook on Statistical Reports of Insurance Companies;
2. Rulebook on Detailed Criteria and Manner of Calculating Unearned Premiums;
3. Rulebook on Detailed Criteria and Manner of Calculating Risk Equalization Reserves;
4. Rulebook on Detailed Criteria and Method of Calculating Outstanding Claims;
5. Rulebook on Detailed Criteria and Manner of Calculating Mathematical Reserve and Bonus Reserve;
6. Rulebook on Manner of Determining and Monitoring of the Insurance Companies Liquidity;
7. Rulebook on Restrictions related to Certain Types of Depositing and Investing Technical Reserves and on Maximum Amounts of Certain Deposits and Investing Guarantee Funds of Insurance Companies;
8. Rulebook on the Content and Manner of Taking Professional Examination for Conducting Insurance Brokerage or Agency Activities, and Manner of Proving the Fulfillment of other Requirements for Obtaining Authorization for Conducting such Activities;
9. Rulebook on the Content and Manner of Keeping Registers on Insurance Companies Data and other Entities Subject to the Control of the Insurance Supervision Agency;

¹ Drafts of enabling regulations were submitted to insurance companies, in order for them to be able to give their suggestions and comments, all with the purpose to attain to their higher quality,

10. Rulebook on the Content of Reports, Notifications and Other Data submitted by the Insurance Company to the Insurance Supervision Agency and the Manner and Deadlines for Submission Thereof;
11. Rulebook on the Content of Certified Actuary's Opinion; and
12. Rulebook on Requirements for Acquiring the Title of Certified Actuary.

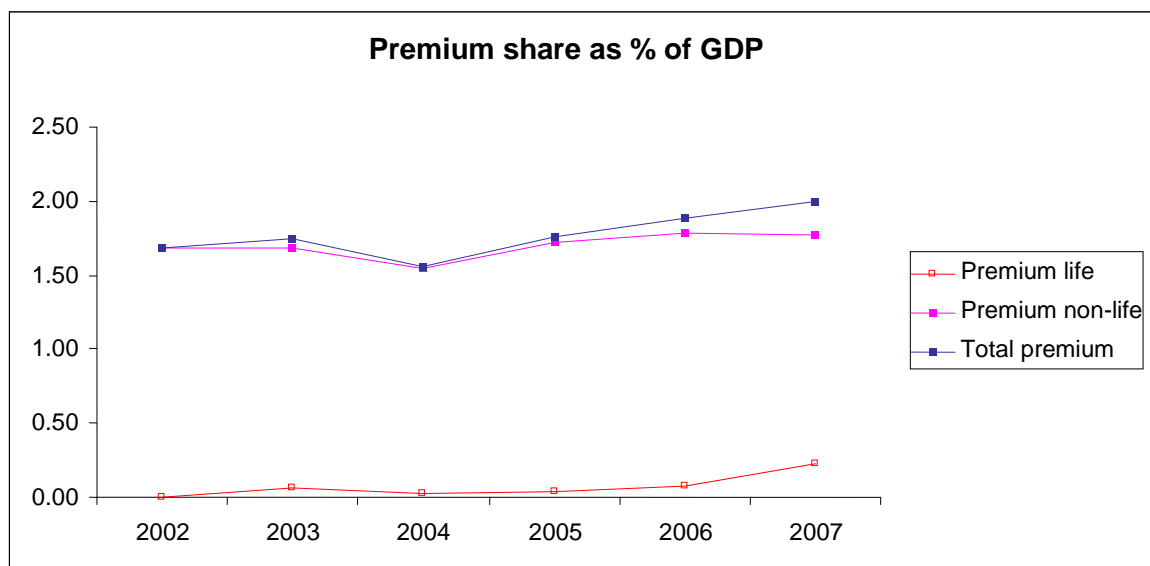
III Market Description

3.1. Market Situation

Data on the share of gross written premiums in the gross domestic product (GDP) and data on insurance density (ratio of gross premium to total population) are present as important indicators for situation on the insurance market in certain countries.

The share of gross premium in GDP has shown slight rise in the period from 2002 to 2007.² Therefore, the share of gross premium in GDP in 2002 was 1.68%, while in 2007 it was 2.0%. The share of non-life insurance premium in GDP has shown slight decrease if compared to the previous period, therefore in 2006 it was 1.79%, while in 2007 was reduced to 1.77 %. At the same time, the share of life insurance premium in GDP showed slight rise from 0.08% as it was in 2006, to 0.23 % in 2007.

Graph1: Premiums share as % of GDP



² Gross Domestic Product in 2007 was 2.541 billion EUR

The following table shows premiums share as % of GDP in neighboring countries, as well as in European Union in 2006, whilst the amount of gross premiums per capita is also shown.

Table 1: Gross premium share in GDP and gross premium per capita in neighboring countries and in EU 25 in 2006

Country	Gross premium/GDP	Gross premium per capita (€)
Neighboring countries		
Slovenia	5.7%	978
Croatia	3%	274
Serbia	2.1%	64
EU 25	8.8%	2,174

Source: www.fren.org.yu and www.cea.eu

The amount of gross premium per capita³ (insurance density), which in 2007 was 82.27€ and which is way below the average of the European Union countries, where it was 2,174 €⁴ in 2006, is often used as an indicator of the insurance market development.

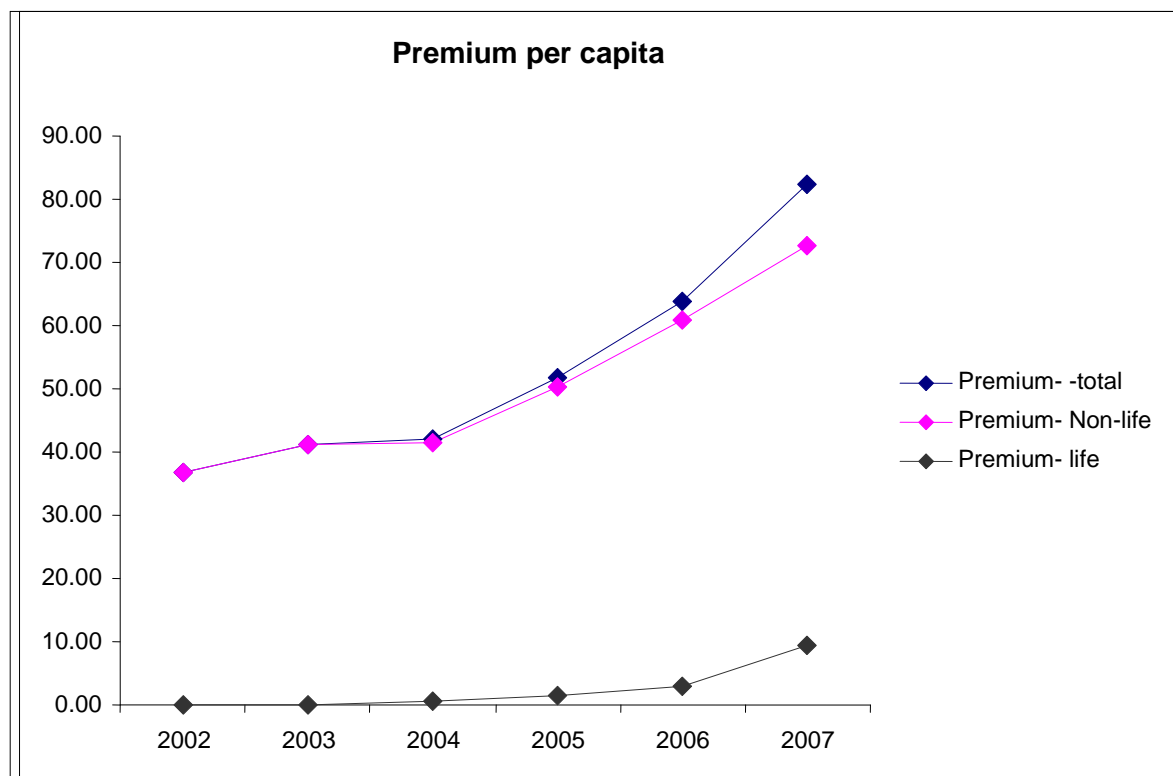
Table 2: Premium per capita

PREMIUM	2002	2003	2004	2005	2006	2007
Life	0.00	0.15	0.72	1.32	2.95	9.53
Non-life	36.83	41.14	41.41	50.33	60.95	72.76
Total	36.83	41.29	42.12	51.65	63.91	82.29

³ Data on population is official as per the 2003 Census, and downloaded from the MONSTAT website

⁴ Data source www.cea.eu

Graph 2: Premium per capita in the period 2002 – 2007



3.2. Insurance Market Participants

Six insurance companies and one reinsurance company have carried out insurance activities on the insurance market in Montenegro during 2007. One of insurance companies was engaged only in life insurance activities, three companies were engaged in non-life insurances and two companies were engaged in both life and non-life insurances. In November 2007, the license for conducting life insurance activities was granted to the Atlas Life JSC insurance company, but it started operations in 2008. The following table contains an overview of insurance companies that operated during 2007 in Montenegro:

Table 3: List of insurance companies

No	Insurance company	Class of insurance
1	<i>Lovćen osiguranje</i> JSC	Life/ Non-life
2	<i>Montenegro osiguranje</i> JSC	Non-life
3	<i>SWISS osiguranje</i> JSC	Non-life
4	<i>Grawe osiguranje</i> JSC	Life/ Non-life
5	<i>Zepter osiguranje</i> JSC	Life
6	<i>Magnat osiguranje</i> JSC	Non-life

An important characteristic of the insurance market is that profitable European companies show an increasing interest for expanding their business activities in Montenegro. The ownership structure in the company *Montenegro osiguranje* changed in 2007, thus the Slovenian reinsurance company *SAVA RE* became the majority shareholder with package of 99.92%. The *UNIQA International Beteiligungs*, beside being the major shareholder of *Zepter osiguranje* with the package of 53% of shares, together with *Uniqa International Versicherungs - Holding GmbH* established a new insurance company - *Uniqa Non-life Insurance* at the beginning of 2008. Furthermore, at the beginning of 2008, insurance companies *Delta Life* JSC and *Delta osiguranje* JSC were granted operating licenses, founded by the *DC Holding* LLC having 99.9% of the initial capital.

3.3. Ownership Structure in Insurance Companies

Ownership structure of Montenegrin insurance industry is based on approximately equal share of domestic and foreign capital. As of 31 December 2007, the total share capital was 22.44 million euro, of which 11.83 million euro or 52.74% was foreign capital, and 10.6 million euro or 47.25% was domestic capital (Table 4). *Montenegro*, *Grawe* and *Zepter osiguranje* are 100% foreign-owned, while the share of domestic capital in *Lovćen osiguranje* is 49.23%, in *Magnat osiguranje* is 100% and in *Swiss osiguranje* is 98.32%. Private ownership prevails in the insurance sector in Montenegro, while the State owns shares in only one insurance company which is *Lovćen osiguranje*, of 41.14%. Until the end of 2008, full privatization of insurance sector is expected.

Table 4: Total share capital (2007)

Name of the company	Domestic capital		Foreign capital		Total
	<i>Amount</i>	%	<i>Amount</i>	%	<i>Amount</i>
<i>Montenegro osiguranje</i>	0	0	4,499,863.29	100	4,499,863
<i>Lovćen osiguranje</i>	5,184,816	49.23	5,347,940	50.77	10,532,756
<i>Swiss osiguranje</i>	3,082,885.26	98.32	52,766.74	1.68	3,135,652
<i>Grawe osiguranje</i>	0	0	1,177,446.19	100	1,177,448
<i>Magnat osiguranje</i>	830,000	100.00	0	0	830,000
<i>Zepter osiguranje</i>	0	0	750,760.65	100	750,761
<i>Lovćen reosiguranje</i>	1,506,666.61	99.45	7,391.87	0.49	1,515,058
TOTAL	10,604,367.87	47.25	11,836,168.74	52.74	22,441,538.19

IV Gross Premium Structure

Gross written premium, as revenues of insurance and reinsurance companies, for non-life insurances includes all amounts of premiums contracted in current accounting period, for a period not exceeding one year, irrespective whether those amounts relate partially or fully to subsequent accounting period, while for life insurances it includes all amounts of premiums collected until the end of the accounting period. Following Table contains a comparative overview of gross written premiums by company:

Table 5: Gross written premium of insurance companies

No.	Name of the company	2007		2006		Index 2007 / 2006
		Premium	Share (%)	Premium	Share (%)	
1.	<i>Lovćen osiguranje</i>	33,949,502	66.54	29,082,747	73.4	116.73
2.	<i>Montenegro osiguranje</i>	10,171,027.64	19.93	8,150,010.86	20.57	124.8
3.	<i>Grawe osiguranje</i>	4,065,002	7.97	1,233,109	3.11	329.65
4.	<i>Zepter osiguranje</i>	44,680	0.09	61,273	0.15	72.92
5.	<i>Magnat osiguranje</i>	1,576,364.64	3.09	0	0	0
6.	<i>Swiss osiguranje</i>	1,210,535.14	2.37	1,094,160	2.76	110.63
	TOTAL	51,017,112.03	100	39,621,299.9	100	128.76

Total gross premium realized on the insurance market of Montenegro in 2006 amounted 39.62 million euro, while in 2007 growth rate of 28.76% was achieved, and gross premium reached 51.017 million euro. Like previous years, *Lovćen osiguranje* has a dominant position on the insurance market, whose premium represented 66.5% of the total premium. If compared to 2006 when *Lovćen osiguranje* generated premium of 73.7% of the total premium, in 2007 its market share declined by 7.2 percentage points. First three ranked insurance companies, in terms of gross written premiums, are: *Lovćen*, *Montenegro* and *Grawe osiguranje* and their market share was 86.6% in 2007, representing a decrease if compared to 2006, when it was 97.8%. The *Zepter osiguranje* had the lowest market share on the insurance market in 2007 with share of 0.09%.

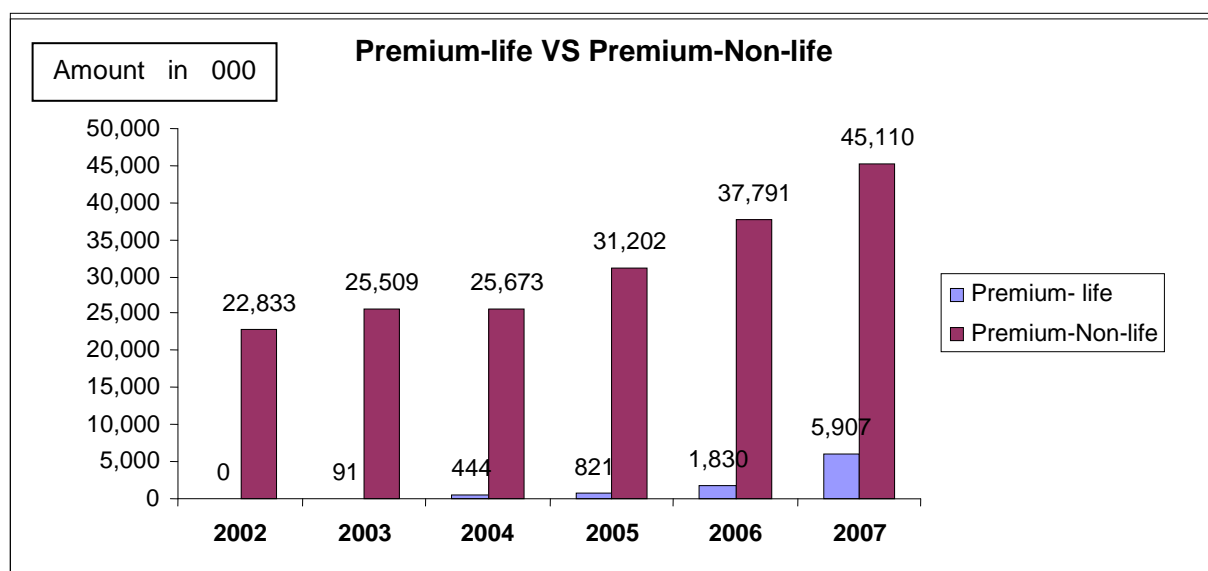
A low level of life insurances and very high level of compulsory insurances was the characteristic of the insurance market in Montenegro in 2007. However, if we compare 2007 with the previous year, it could be concluded that life insurance has had positive trend and that its share in total premium is approximately 11.58%. Considering that generated gross premium of life insurances in 2007 was 5.907 million euro, it can be concluded that life insurance premium has increased by 322.78% if compared to 2006, when it was 1.83 million euro.

If observing the period from 2005 it may be concluded that non-life insurance premium has an annual growth at average rate of 20.7%, while life insurance has expanded and continued growing at average rate of 143.53%.

Non-life insurance premium had a growth at the rate of 16.95% if compared to 2006, and has reached the amount of 45.11 million euro in 2007. Non-life insurance per capita amounted to €72.74 in 2007, precisely the density ratio of non-life insurance in 2007 has increased by €10.5 if compared to the previous year, when non-life insurance premium per capita was €62.12. In 2007, the share of non-life insurance premium in GDP of Montenegro was 1.77%.

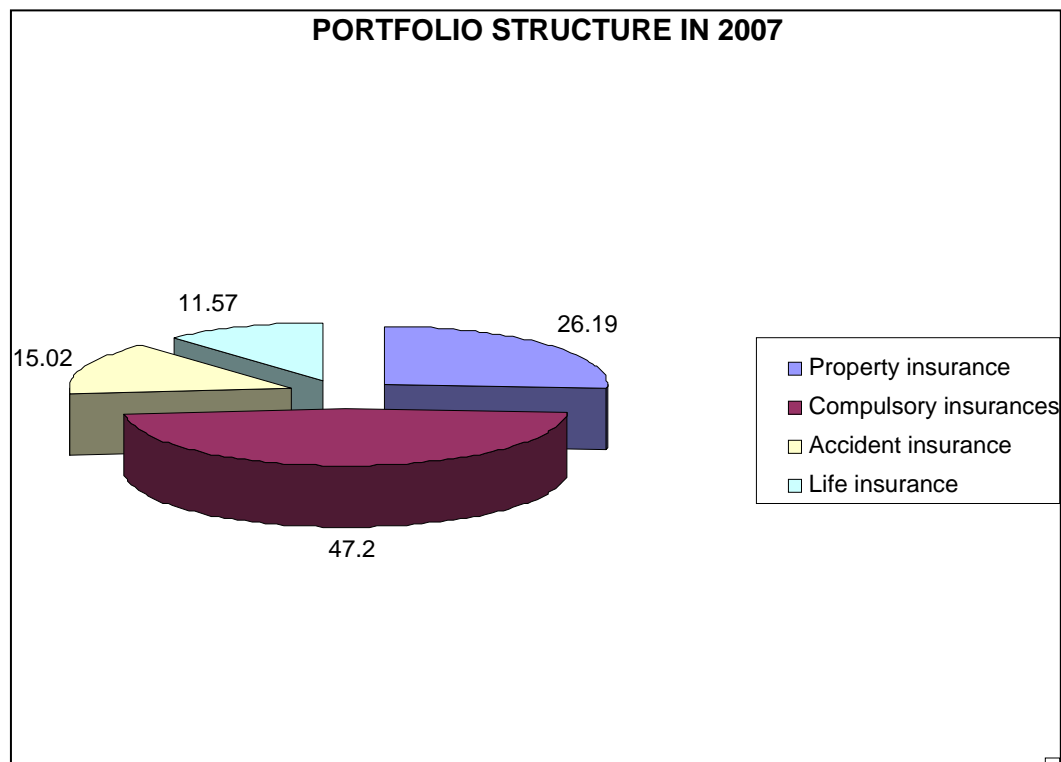
Relation of life and non-life insurances is shown on the following graph:

Graph 3: Premium relation: Life VS Non-life



Structure of insurance portfolio on the Montenegrin market can be presented by the following graph:

Graph 4: Insurance portfolio



Compulsory insurances have had the greatest share in insurance portfolio of Montenegro in 2007 with 47.2%, followed by property insurances, which made 26.19% of total insurance portfolio.

Table 6: Compulsory insurance by the company

Compulsory Insurances	Premium
<i>Lovćen osiguranje JSC</i>	15,090,124
<i>Montenegro osiguranje JSC</i>	7,416,107.84
<i>SWISS osiguranje JSC</i>	628.35
<i>Magnat osiguranje</i>	1,576,364.61
TOTAL	24,083,224.80

Lovćen osiguranje JSC had the greatest share in compulsory insurances of 15.09 million euro, or 62.65%, followed by *Montenegro osiguranje* of 7.41 million euro or 30.8% and *Magnat osiguranje* of 1.57 million euro or 6.54%.

V Assets Structure

Total assets value for all insurance and reinsurance companies according to balance sheet as of 31 December 2007 was 77.85 million euro and it was higher by 28.1% than the total assets value in 2006. Short-term financial placements and cash equivalents and cash make 35.58% of the total asset value, 30.09% relates to tangible and intangible assets, 21.35% to investments and 12.9% relates to receivables.

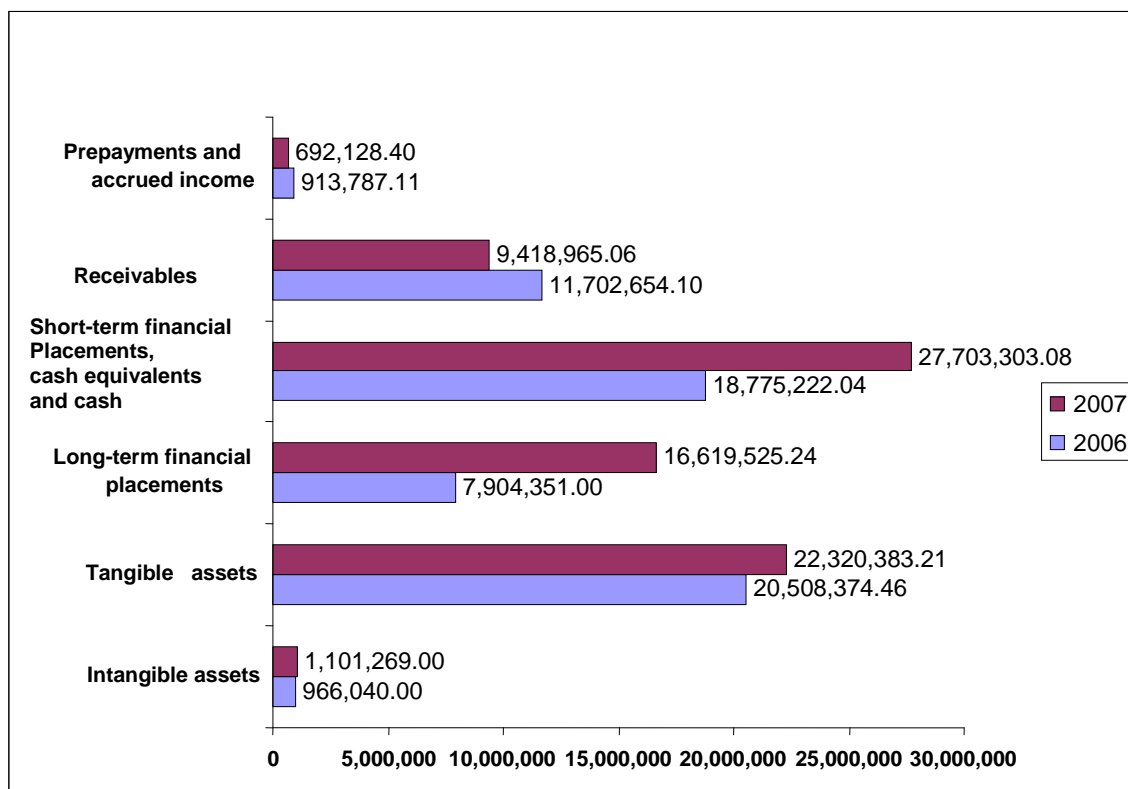
Table 7: Assets structure of insurance companies in 2006 and 2007

	2006		2007		INDEX 2007 / 2006
	<i>Amount</i>	<i>Share</i>	<i>Amount</i>	<i>Share</i>	
Intangible assets	966,040	1.59	1,101,269.00	1.42	113.99
Tangible assets	20,508,374.46	33.75	22,320,383.21	28.67	108.83
Long-term financial placements	7,904,351	13.01	16,619,525.24	21.35	210.25
Long-term financial placements and cash equivalents and cash	18,775,222.04	30.90	27,703,303.08	35.58	147.55
Receivables	11,702,654.10	19.26	9,418,965.06	12.09	80.48
Prepayments and accrued income	913,787.11	1.50	692,128.40	0.89	75.74
TOTAL:	60,770,428.71	100.00	77,855,573.99	100	128.11

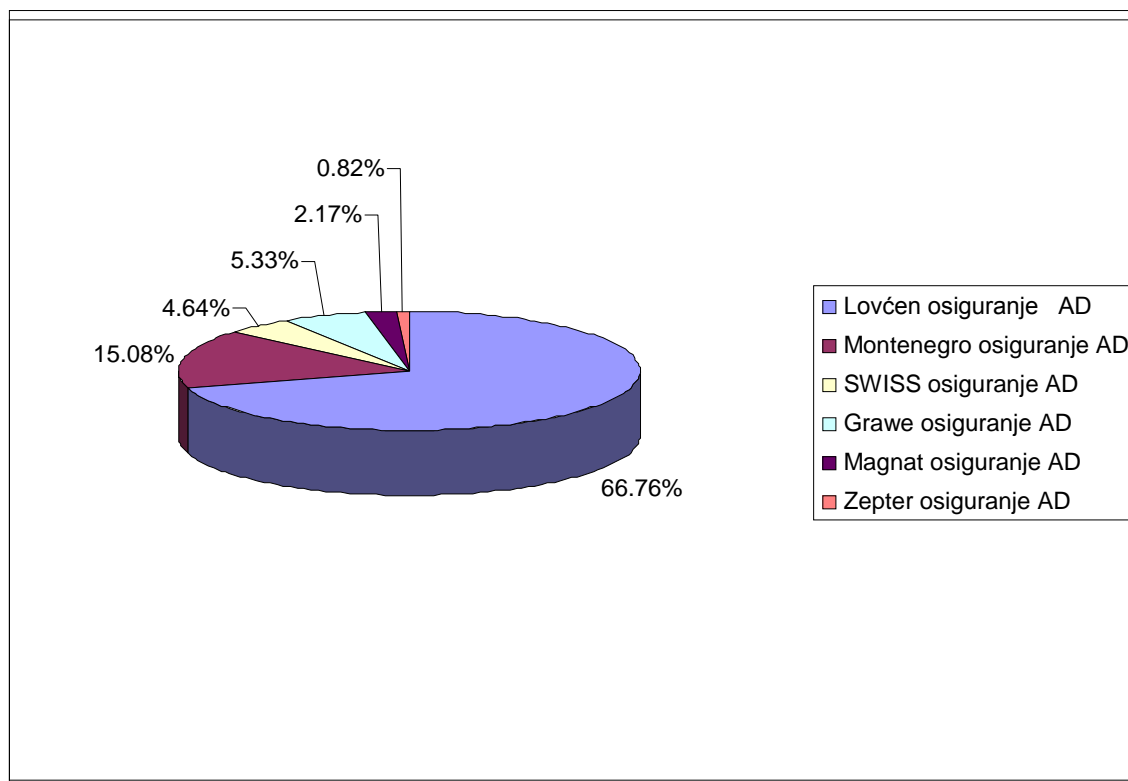
Long-term financial placements in 2007 in the amount of 16.62 million euro have evidenced growth of over 100% if compared to 2006, which led to a growth of its share in total assets of companies from 13.01% in 2006 to 21.35% in 2007.

Likewise, the total short-term financial placements and cash equivalents and cash amounting to 27.7 million euro have recorded a growth of 47.55% if compared to 2006, which led to an increase of their share in total assets of companies from 31% in 2006 to 36% in 2007. The growth of total assets (tangible and intangible) of 9.06% was also recorded, if compared to 2006.

Graph 5: Assets structure of insurance companies



Graph 5: Share of assets of insurance companies in total assets in 2007 (%)



In respect of representation of certain companies in total insurance and reinsurance companies' assets, *Lovćen osiguranje* has the greatest share of 66.76%, which was reduced by 3 percentage points if compared to 2006, when it was 69.33%. It is followed by *Montenegro osiguranje* JSC with 15.08%, *Grawe osiguranje* JSC with 5.33%, *Swiss osiguranje* with 4.64%, *Magnat osiguranje* with 2.17%, while *Zepter* share was only 0.82%.

VI Liabilities and Capital Structure

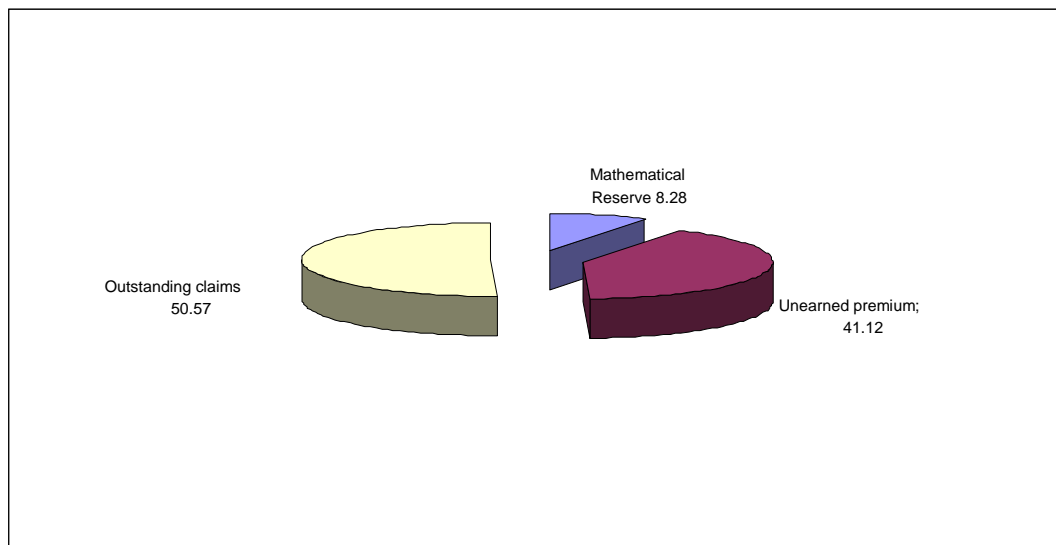
Out of the total value of liabilities and capital of insurance companies in 2007, 45.85% relates to technical provisions, 44.65% to the capital and reserves and 9.45% relates to other obligations.

Table 8: Structure liabilities and capital of insurance companies:

TOTAL LIABILITIES AND CAPITAL	2007		2006		index 2007 / 2006
	Amount	Share	Amount	Share	
Capital	34,765,388.00	44.65	26,103,341.22	42.95	133.18
Technical reserves	35,697,846.97	45.85	25,048,131.70	41.21	142.51
Others	7,392,339.02	9.49	9,618,955.79	15.82	23.14
TOTAL:	77,855,573.99	100	60,770,428.71	100	128.11

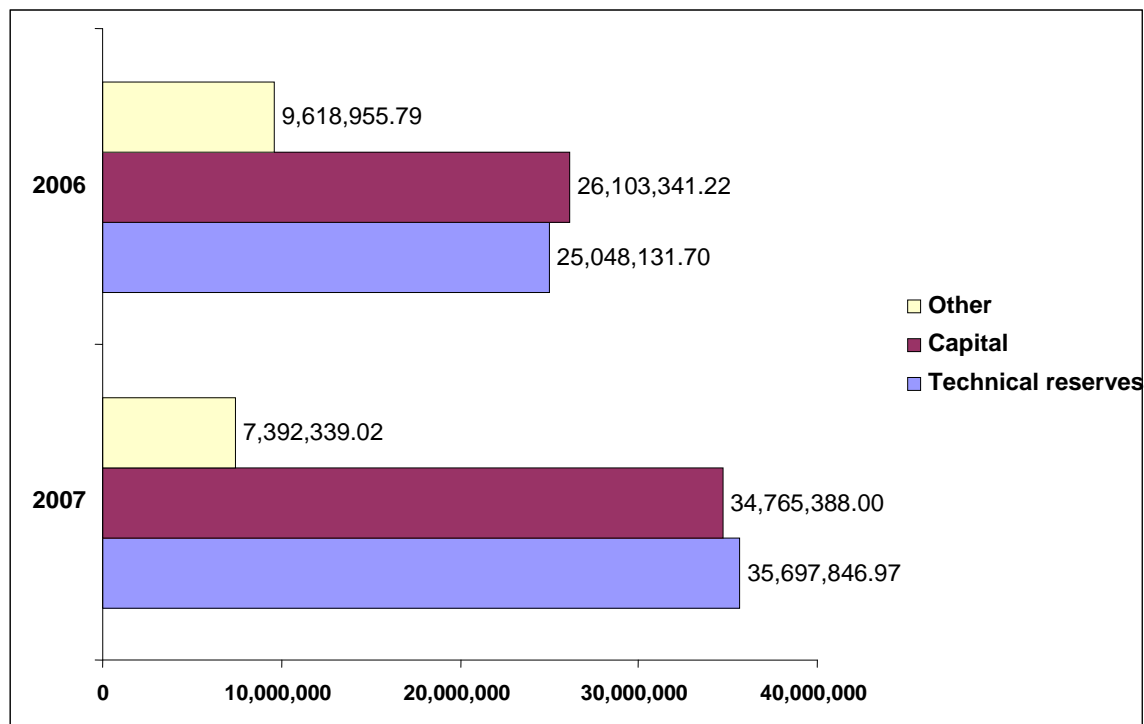
Technical reserves of 35.69 million euro, which rose by 42.52% if compared to 2006, have the greatest share in structure of liabilities and capital, which was primarily influenced by allocation of outstanding claims in the amount of 18.05 million euro, having a growth rate of 44.68%, if compared to 2006. Allocations for mathematical reserve in 2007 amounted to 2.95 million euro, having a growth of 95.77% if compared to 2006, when those were 1.51 million euro.

Graph 6: Structure of technical reserves of insurance companies



In 2007, the capital and reserves have increased by 33.18% and amounted to 34.76 million euro, which makes 44.65% of total liabilities and capital. Other obligations of insurance companies have share of 9.49% and their amount was reduced if compared to 2006, when they amounted 9.61 million euro and made 15.82% of total liabilities and capital.

Graph 7: Structure of Companies' liabilities and capital



VII Technical Reserves

According to provisions of the Insurance Law, insurance companies, in the course of their regular activity of performing insurance business, are obliged to form certain technical reserves from the pure premium funds which are used for coverage insurance-based liabilities. An insurance company, engaged in one or more classes of life insurances, determines technical reserve for unearned premiums, outstanding claims, bonuses and mathematical reserves. An insurance company, engaged in non-life insurances, determines technical reserve for unearned premiums, outstanding claims and risk equalization.

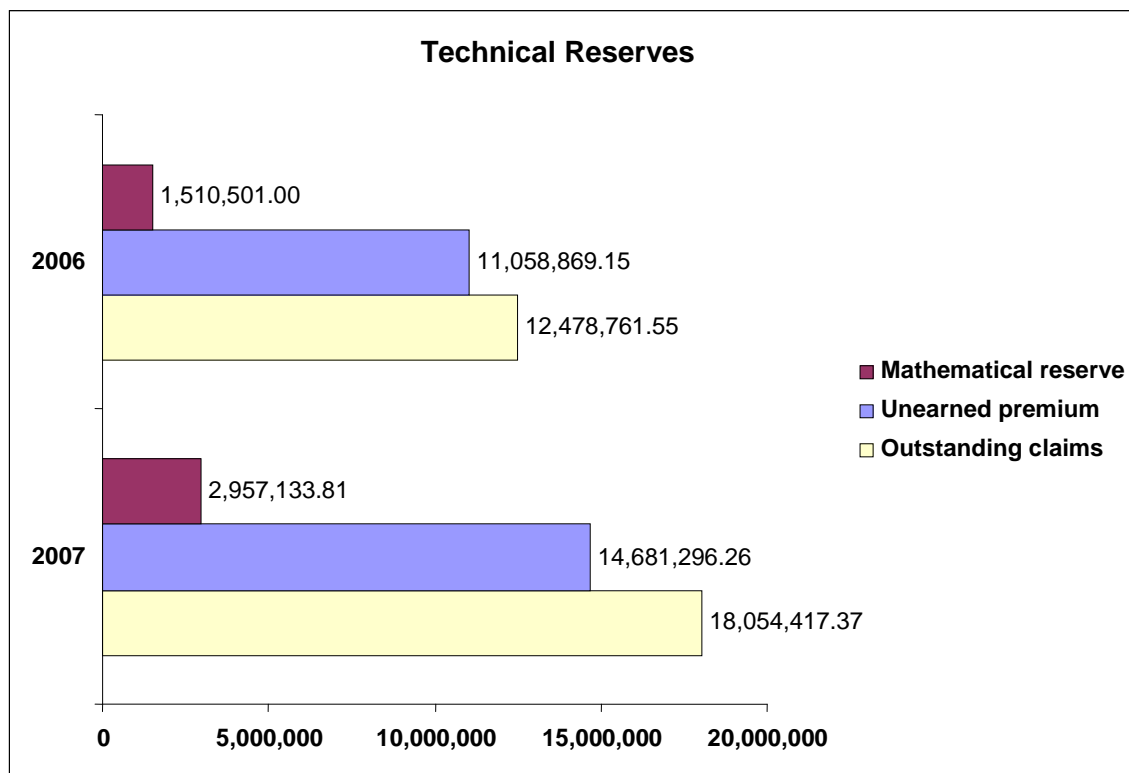
Unearned premium are formed from the total insurance premium, separately for each class of insurance in proportion to the insurance period, and serve to cover obligations arising during the forward accounting period.

Outstanding claims are formed at the level of estimated obligations for incurred, reported but unprocessed claims and incurred but unreported claims in the current period.

Mathematical reserve is formed at the level of present value of future obligations of the company reduced by present value of future obligations of the insurers (insurance premium) and is calculated for each separate contract.

Companies are obliged to keep life insurance funds on the separate account and those funds can be used, precisely can be the subject of enforced execution, only for covering of company's obligations arising from a life insurance contract.

Graph 8: Allocation of technical reserves in 2007, if compared to 2006



As of 31 December 2007, the technical reserves at the level of insurance activity, amounted 35.69 million euro, which represents 45.85% of total liabilities and capital. In 2007, the level of technical reserves was increased by 42.5%, if compared to 2006. Like in the previous year, companies have allocated the majority of funds for outstanding claims, which make approximately 50% of total technical reserves. Allocations for outstanding claims had a growth of 44.7% in relation to 2006. Unearned premiums made 41.13% of total technical reserves in 2007. The lowest allocation was for mathematical reserves, in the amount of 2.95 million euro, however the growth generated was of 95.77% if compared to 2006.

VIII Financial Operating Results

Profit and Loss Statement (Income Statement) is one of the basic financial reports prepared by insurance companies. Insurance companies, according to the Law, are obliged to classify profit and loss by classes of insurance (separately for all classes of life and all classes of non-life insurances) and separately for reinsurance operations.

In 2007, insurance activity generated a profit of 819 thousand euro, as opposed to previous year when it operated at a loss of 1.38 million euro. Five out of six insurance companies which operated in 2007, generated profit and one operated at a loss. Five insurance companies generated profit of 906 thousand euro, and one company operated at a loss of 87 thousand euro. *Lovćen osiguranje* generated the largest profit in the amount of 684 thousand euro, which makes 83.5% of the total net profit.

IX Licensing

The characteristic of the Insurance Market in 2007 was implementation and harmonization of overall operations of insurance companies, reinsurance companies, insurance brokerage companies and insurance agency companies, as well as insurance agents and brokers, with the provisions of the Insurance Law and the Law on Compulsory Transportation Insurance.

During 2007, one of the insurance companies, *Montenegro osiguranje*, harmonized its organization, business activity and business policy acts with the Insurance Law. Three of the companies (*Swiss osiguranje*, *Magnat osiguranje* and *Zepter*) are in final phase of harmonization with the Law, while *Lovćen* and *Grawe osiguranje*, engaged in both life and non-life insurances, will harmonize their organization, business activity, and acts until the end of 2010, when the period defined under Article 202 of the Law expires. According to the new Insurance Law, the following companies were granted operating license:

1. *Atlas Life* JSC, No.02-5834/2 of 12 November 2007;
2. *Delta Life* JSC, No. 32-1/08 of 22 February 2008;
3. *Delta osiguranje* JSC, No. 33-1/08 of 22 February 2008;
4. *Uniqa neživotno osiguranje* JSC, No.09-5/08 of 24 April 2008.

There are nine insurance agency companies in Montenegro, out of which three have harmonized their operations with the new Law, while six newly established companies were granted operating license for insurance agency. Two out of three insurance agency companies have harmonized their operations, and one newly established was granted operating license for agency operations.

Additionally, authorizations for performing insurance agency activities were granted to 180 natural persons and one person was granted the authorization for insurance brokerage activities.