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„Bulgarian-American Credit Bank” AD

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FINANCIAL STRENGHT RATING	Initial Rating	Update	Update	Update
Date of Rating Committee:	26.07.2016	25.07.2017	26.07.2018	15.04.2019
Date of Publication:	27.07.2016	26.07.2017	30.07.2018	17.04.2019
Long-term rating:	B	B+	B+	BB-
Outlook:	Stable	Stable	Positive	Stable
Short-term rating:	B	B	B	B
National-scale long-term rating:	B+ (BG)	BB- (BG)	BB (BG)	BB+ (BG)
Outlook:	Stable	Stable	Positive	Stable
National-scale short-term rating:	B (BG)	B (BG)	B (BG)	B (BG)

BCRA – CREDIT RATING AGENCY (BCRA) is the third qualified rating agency in the EU, registered under Regulation (EC) No. 1060/2009 of the European Parliament and of the Council. The credit ratings, assigned by BCRA, are recognized throughout the EU and are equal with the other ratings, recognized by the European Securities and Markets Authority (ESMA), without any territorial or other restrictions.

During the analysis of all data (audited annual report and annual statements) of the Bulgarian-American Credit Bank AD for 2018, BCRA confirmed the sustainable improvement in observed indicators. On April 15, 2019, the Rating Committee of BCRA examined in detail the situation of the bank and decided to update the Bank’ ratings as follows:

- Upgrades the long-term financial strength rating from B+ **to BB-**, changes the outlook from „positive” to **„stable“**, maintains the short-term rating at **B**;
- Upgrades the long-term national-scale rating from BB (BG) to **BB+ (BG),** changes the outlook from „positive” to **„stable“**, maintains the short-term national-scale rating at **B (BG).**

The officially adopted by BCRA methodology for assigning financial strength ratings to banks is used (https://www.bcra-bg.com/files/bank_methodology_2018_en.pdf).

The report has been prepared and the rating assigned based on the information, provided by the rated bank, the Bulgarian National Bank, the National Statistical Institute, BCRA`s database, consultants and other sources of public information.

The Government of the Republic of Bulgaria is committed to speeding up the process of joining the euro area by officially submitting a letter of intent. In August 2018, the Council of Ministers approved an Action Plan including measures for realizing Bulgaria’s intentions to join the Exchange Rate Mechanism II and the Banking Union by July 2019.

In 2018, the country's economic growth slowed down to 3.1% (3.6% in 2017). Domestic demand (consumption and investment) contributed positively to GDP dynamics. On the other hand, net exports had a negative contribution to the GDP growth in the first half of 2018.

In 2018, the current account balance reported a surplus of EUR 2 539 million (4.6% of GDP) compared to a surplus of EUR 3 368 (6.5% of GDP) in 2017.

The inflow of foreign direct investment remains weak. According to preliminary data, direct investments in Bulgaria, in 2018 amounted to € 703 million or 2.8% of projected GDP, recording a nominal decrease of 34.5% compared to the previous year.

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At the end of December 2018, the country's gross external debt amounted to EUR 32 716 million or 59.3% of the projected GDP. In nominal terms, the debt decreased by EUR 682 million compared to the end of 2017. The relative share of the public sector's external debt fell to 18.7%, while that of the private sector rose to 81.3% of the total external debt.

As of the end of 2018, the BNB's international reserves amounted to EUR 25 072 million and provided 150.5% coverage of the monetary base, a solid buffer used by the central bank to ensure the stability of the currency board.

In 2018, the labour market conditions are tightening along with the growth of the general economic activity. The number of unemployed persons decreased in all age groups, determining the unemployment rate for the population over 15 years from 5.2% on average in 2018 and 6.2% in 2017.

Labour incomes in the economy retain their upward trend. In the first half of 2018, the average gross wage in Bulgaria reached BGN 1 135 in 2018, nominally increasing by 9.5% on a yearly basis.

The average annual inflation rate (measured by HIPC) accelerates to 2.6% in 2018. This value exceeds the Maastricht convergence criterion, which could slow down the country's entry into the Eurozone waiting room by mid-2019.

At the end of 2018, the budget balance was expected to be positive at 0.1% of the projected GDP or lower compared to the previous year (0.8% of GDP). The budget framework for 2019 envisages a deficit under the CFP amounting to 1.0% of GDP based on the budget execution so far we expect 2018 to be the third consecutive year with a deficit projected by law but an actual budget surplus achieved.

The budget framework for 2019 envisages a deficit under the CFP amounting to 0.5% of GDP, and the updated mid-term forecast reaffirms the balanced budget objectives in 2020 and 2021.

The low government debt level is assessed as a positive factor in comparison with the other EU countries. As of the end of Q3 2018, the consolidated debt of "General Government" sector amounted to 23.8% of GDP. The country has a significantly lower level of government debt than the Maastricht convergence criterion of 60% and is among the three EU countries with the lowest government debt level, being outpaced only by Estonia and Luxembourg.

In the period under review, the banking system remains stable, marked by a decrease of the non-performing exposures and retained high levels of capital adequacy.

At the end of 2018, 25 banks were operating in the Bulgarian banking market. The consolidation trend of the system continues. At the beginning of the third quarter of 2018, Commercial Bank "Victoria" EAD merged into Investbank AD and the process of the merger of DSK Bank and Societe Generale Expressbank (under the management of the Hungarian ORP Group) has been commenced. The same is the situation of the ownership change of Piraeus Bank Bulgaria, which is to be merged in Eurobank Bulgaria AD in the current year following the decision taken by BNB for preliminary approval of the deal at the end of March 2019.

In 2018, the profit of the banking system increased considerably. It reached BGN 1 678 million in nominal terms and the net revenues from interests, taxes and commissions retained their leading share. The generated profit in the banking system ensures confidence to some extent, as these available funds are a potential source for a capital increase and maintenance the stability in the sector.

During the period of the update, the share capital of Bulgarian-American Credit Bank remains unchanged and the changes in the shareholding structure are insignificant.

Shareholder	Share of capital	
	31.12.2018	31.03.2018
CISF AD	61.43%	61.43%
LTBI Holdings LLC	35.49%	35.41%
Other shareholders	3.08%	3.16%
Total:	**100%**	**100%**

There are no changes occurred in the participation of the bank, as well in the compositions of the Supervisory and Management Boards. The mandate of the SB expires on May 10th 2021 and that of the Management Board on June 6th 2022.

During the review period, no changes occurred in the organisational structure of the bank.

The management of the bank declares its intention to reach a sustainable growth rate of business and to maintain the diversification of the loan portfolio by increasing the share of individuals and SMEs.

During the period (2018), there is faster growth in risk-

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weighted assets compared to the capital base (CB), resulting in a decrease in the levels of total capital adequacy ratio and adequacy of Tier 1 capital. The capital adequacy levels of the rated bank remain lower than the average of the banking system and for the Second group of banks in a comparative aspect, while significantly exceed the regulatory requirements.

In 2018, the indicator Net classified exposures to Capital base has been decreasing for a sixth consecutive year. It is a result of both the shrinkage of the non-performed exposures and the increase in Capital base.

At the end of 2018, the Bank reported a lower value of the non-adjusted leverage compared to the Second Group of banks, while exceeded the banking system. In terms of the adjusted leverage, the bank continues to report higher values compared to the average of the banking system and the Second group of banks, and lower to the banks of the reference group[1].

The return on equity ratio continued to grow for a fourth consecutive year, up to 6.84% in 2018. It is a result of the outpaced growth of the net profit (55.8%) compared to that of the equity (3.8%).

In the last three years, the level of the leverage registers a decline, while during the entire period the ratio exceeds considerably the minimum required.

In the period of the update, the upward trend in the levels of attracted funds remained in the last two years. In 2018, the total attracted funds (deposits and others) have grown by 16.1% (17.8% in 2017). With these growth rates, the Bank remains well above the average increase in attracted funds in the banking system for the second consecutive year (7.2% in 2018 and 6.5% in 2017 respectively).

Deposits dominate the resource structure, where no substantial changes occurred in both their currency and term structure.

During the review period, relatively high concentration is observed in the resource and deposit base.

The reported levels of retention (sustainability) of the resources and the growth in term deposits are positively assessed.

In the period, the total assets of BACB registered stable growth in 2018 amounting to 14.5% (15.6% in 2017). The growth in assets continues to be higher compared to the average of the banking system (7.9%).

The increase of the assets is due to the growth rates of *Net loans*, which remain dominating in the assets structure, followed by the *Cash in cash account*, and *cash in BNB current account*. *Investments* also registered growth, albeit lower – 7.2% (BGN 10.8 million), contributing 6% to the increase in total assets.

The size of the ***Gross Loan portfolio*** increases for a fifth consecutive year. In 2018, there was an accelerating growth pace (13.9% in 2018, 10.0% in 2017). The identified growth substantially exceeds the average of the banking system (8.6%).

In structural terms, the major characteristic of the bank that marks it as corporate one is not changed – it keeps a considerable share of *Loans to enterprises* in the loan structure.

BACB maintains a well-diversified credit portfolio by sectors.

The share of "non-performing" loans continues to decrease for a sixth consecutive year. In 2018, the improvement of this key asset quality indicator was due both to the decline in non-performing loans and to the relatively high growth rate in gross loans. Structurally, most of the "inherited" loans continue to stand out - 83.5% of non-performing loans were granted until 2011.

At the end of 2018, the coverage of the gross loan portfolio from impairments remained higher compared to the average of the banking system and one of the Second group of banks.

The coverage of classified credits by the total impairments is lower compared to the system and Second group of banks.

The share of the 15th biggest credit exposures rose slightly, continuing to evidence for a certain concentration according to the indicator.

In 2018, the income from interest has been increasing for a fourth consecutive year and is noted an accelerating pace compared to both 2016 and 2017.

Interest expenses have been declining for a sixth consecutive year, and in 2018, the registered decrease was of 26.4% (11.3% in 2017).

The relative annual growth of fee and commission income in 2018 is higher than in 2017 and 2016 but close to half of the levels observed in 2014 and 2015.

[1] Municipal Bank, International Asset Bank, Commercial Bank D and TBI Bank

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In 2018, the upward trend in the income of fees and commissions was resumed.

Net interest income and Net fee and commission income are rising for the sixth consecutive year. The relative changes reported in 2017 and 2018 were lower than those in the previous three years, whereas on an annual basis in 2018, there was an accelerated pace compared to the previous year.

In 2018, the operating profit of the bank increased by 27.9% on an annual basis (down from 18.5% in 2017) to BGN 17 085 thousand at the end of the year, which is the highest value registered in the past 5 years.

The growth of the financial result for 2018 is about 2 times higher than that of the operating profit (55.8% against 31.6% for 2017). The nominal value amounted to BGN 12 202 thousand at the end of the year, which is also the highest registered value in the last five years.

In 2018, for a third consecutive year, the bank reported a decrease in the Return of interest-bearing assets (by 0.09 p.p.).

Regarding the *price of interest-bearing liabilities*, the bank also reports a decline but for seventh consecutive year – by 0.35 p.p. The higher decrease in the ratio *Price of interest-bearing liabilities to Rerun on interest-bearing assets* is positively assessed from a rating viewpoint and is resulting in an increase in the level of *Gross interest spread* (by 0.26 p.p. in 2018), increase for a sixth consecutive year.

After 2017, the slight annual decrease of the *Net Interest Margin* (by 0.02 p.p.) in 2018, its value increased by 0.26 p.p.)

The outpacing growth of the profit compared to the average level of assets led to additional growth in the *Return on Assets* value (by 0.26 p.p. on a yearly basis), reaching 0.93% at the end of the year. The value of the indicator continues to be lower to the average of the banking system (1.66%) and to the average of the Second group of banks (1.21%) in a comparative aspect.

The value of the ratio Operating Profit to the average size of the Assets (1.28%) reported by the bank at the end of 2018 is also lower than the average for the banking system (2.46%) and for the Second group banks (1.76%).

In 2018, the downward trend in the ratio *Equity to Total liabilities* to 12.9% continue. In a comparative aspect, the ratio level is close to and slightly lower to the average of the banking system, while excesses (by 1.0 p.p.) the level of the Second group of banks.

In 2018, for the second consecutive year, there was an increase in the current assets, in line with the growth of Cash and cash balances with the central banks. The current asset value reported at the end of the year is the highest for the past five years.

The reported liquidity coverage level for supervisory purposes registered a slight decrease over the last two years but significantly exceeded the minimum requirements throughout the period (2016-2018).

As of the end of 2018, BACB moved up one position in terms of assets and deposits to 15th place and two positions up in terms of gross loans to 12th place. The move with one position up is a result of the merger of CIBank in United Bulgarian Bank, while the move up by two positions in terms of gross credits is due to the outpace of TB Investbank.

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Bulgarian-American Credit Bank AD *continues to report an improvement in its activities and the reported result, while to a part of the results in addition to the affirmation of the positive trends acceleration is also witnessed.*

An additional ***positive impact on the rating*** *of Bulgarian-American Credit Bank AD could have the sustained improvement in the portfolio quality, the retention and increase of the generated profit and the profitability indicators, while at the same time maintaining stable levels of capital adequacy and liquidity.*

In negative direction of the rating *could affect the deterioration in assets quality, the increase of the depreciation costs, the significant contraction of the activity (its profitability), as well as a decrease in the capital adequacy and deterioration of the liquidity position of the bank.*

Main Indicators

BGN ('000)	2018	2017	2016	2015	2014
Balance Sum	1 420 303	1 240 099	1 072 892	1 017 537	815 298
Equity	182 960	176 285	168 171	161 944	155 628
Total Interest Income	42 803	39 064	38 098	37 117	32 790
Net Financial Result	12 202	7 830	5 952	814	-9 167
Net Interest Margin	3.27%	3.01%	3.03%	2.59%	1.78%
Return on Assets	0.93%	0.67%	0.57%	0.09%	-1.19%