95, Evlogi Georgiev Blvd.
Sofia 1142
phone: (+359 2) 9876363
www.bcra-bg.com

„Bulgarian American Credit Bank" AD July 2018	Radoslav Marinov, Lead Financial Analyst r.marinov@bcra-bg.com Ventseslav Petrov, Financial Analyst v.petrov@bcra-bg.com Radostina Stamenova, Economist stamenova@bcra-bg.com

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

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

„BCRA – Credit Rating Agency" (BCRA) updates the assigned credit ratings to „Bulgarian American Credit Bank" AD (BACB):

- Affirms the long-term financial strength rating: to **B+**, changes the outlook from „stable" to **„positive"**, affirms the short-term rating to **B**;
- Upgrades the national-scale long-term rating: from BB- (BG) to **BB (BG),** changes the outlook from „stable" to **„positive"**, affirms the national-scale short-term rating to **B (BG).**

The officially adopted methodology for assignment of a financial strength rating of a bank is used: (https://www.bcra-bg.com/files/bank_methodology_2018_bg.pdf).

The report has been prepared and the rating – assigned based on information, provided by the rated bank, Bulgarian National Bank, National Statistical Institute, BCRA databases, consultants and other public resources.

After the formation of the ruling coalition GERB - United Patriots in April 2017, the political situation in Bulgaria remains stable. The Presidency of the Council of the European Union in the first half of 2018 is the main challenge for the country in its international relations.

In 2017, the **Bulgarian economy** reports a real growth of 3.6% with the main driver for the growth of GDP being the domestic demand.

As at end of 2017 the foreign **reserves of BNB** stand at 23 662 million EUR (46.9% of the GDP), used by the Central bank as a solid buffer to guarantee the stability of the Currency Board. The reserves coverage on the average import of goods and non-factor services in nominal terms for the last twelve months is 8.7 months, high enough to avoid any external shocks.

In 2017, the **foreign direct investment flow** continues the downtrend to 1.9 % (a drop of 12% compared to 2016 in nominal terms).

The labour market data record high employment and economic activity values. Ascending remains the labour income trend.

The price levels in Bulgaria (measured by the average annual HIPC) is gradually raising. In the last six months (September 2017 – March 2018) the inflation reaches 1.4%.

The improvement of the **public finances** is driven by the growing economic activity. Since 2016, when the balance of the Consolidated Fiscal Programme reported surplus, in 2017, the trend is maintained and for a second consecutive year, the budget balance is positive. The balance of CFP for 2017 amounts to BGN 846 million (0.9% of GDP) and forms surplus both in the national budget and in EU funds account.

A deficit in the amount of 1% of GDP is set out as a target for 2018. The government declares its intention to pursue the policy of gradual consolidation and in the updated mid-term budget forecast targets a deficit for 2019 amounting to 0.5% of GDP and achieve a balanced budget in 2020. No significant changes in tax policy are foreseen during the projection horizon.

The government debt, as a "debt-to-GDP" ratio has decreased at the end of December 2017 to 23.9 % (27.4 % as of the end of 2016).

During the first quarter of 2018, 25 banks are operating in the Bulgarian market (incl. 4 foreign branches) and the tendency of consolidation is preserved.

The banking system of the country remains stable, characterized by continuous growth in assets base. The deposit base in the sector continues to grow with the increase in lending and deposit base. The high levels of liquidity and capital adequacy remain with a sustained improvement of assets quality, with a decrease of non-performing exposures down to 10.2 % as of the end of 2017 (12.9 % as of the end of 2016) and to 9.3% as of end of March 2018. The bank sector continues to report stable return. The conducted Asset Quality Review (AQR) and Stress Tests (ST) confirm the favourable situation of the banking system. Main challenges remain, namely, the transformation of the deposit base to the credit base and the decrease in the share of deteriorated loans. The favourable conditions in the system retain in the beginning of 2018.

In the period of updating no changes occurred in the value of the shareholding capital of Bulgarian American Credit Bank, while the changes in the shareholding structure are insignificant (0.12 p.p. in a part of the shares) of the share capital of Bulgarian American Credit Bank, and the changes in the shareholding structure are insignificant:

Shareholder	Capital Share	
	31.03.2018	*22.5.2017*
CIF AD	61.43%	61.43%
LTBI Holdings LLC	35.41%	35.29%
Other shareholders	3.16%	3.27%
Total	**100%**	**100%**

During the period there are no changes in the Bank's participations.

During the analysed period the following changes occurred in the composition of the Supervisory Board (SB) – Mr Jason Lil Kuk is dismissed as a member of the SB, replaced by Mr Serge Lioutyi. The said changes are officially entered in the Commercial Registrar on October 19th, 2017. Serge Lioutyi has a solid background in the restructuring, evaluation, analysis and management of investment portfolios. As of the date of elaboration of the report, the SB consists of the following members:

- Mrs Tzvetelina Borislavova Karagyozova
- Mr Martin Boychev Ganev
- Mr Serge Lioutyi

The mandate of the SB expires on May 10th, 2021.

After March 2017, when Mr Alexander Dimitrov has been appointed as a member of the Management Board, no changes have been carried out and now it has the following members:

- Mr Vassil Simov – Chairman of the MB and Executive Director;
- Mr Ilian Georgiev – member and Chief Executive Director;
- Mrs Loreta Grigorova – member and Executive Director ;
- Mr Alexander Dimitrov – member and Executive Director;
- Mrs Silvia Kirilova – member.

The mandate term expires on June 6th, 2022.

By a resolution of the General Assembly of the shareholders, held on June 5th, 2017 a new position is opened, namely "Chief Executive Director" and with respect to resolutions of the MB and SB (July 3rd, 2017 and July 6th, 2017 respectively) Mr Ilian Georgiev is appointed for this position.

During the analysed period certain changes in the organizational structure have been conducted for the transformation of the bank's business structure from product-oriented to client-oriented. The changes entered into force on November 1st, 2017.

The Bank continues implementing an innovative approach to attract new clients and financial resources, as well to diversify the deposit base. New deposit products are developed and the implementation of plans to attract deposits from abroad continues.

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During the period of the update, the capital base is predominantly formed by Tier 1 capital and the outpacing increase of the assets results in a decrease of the capital adequacy. The level of capital adequacy of BACB is below the average for the banking system and the average of the second group of banks in a comparative aspect, however significantly exceeds the regulatory requirements.

In 2017 and in the first quarter of 2018, a growth is reported in the value of the non-adjusted leverage, as well as in the value of the adjusted one.

In 2017, as a result of the deteriorated exposures (by 13.8%) and a slight increase in the capital base (by 4.8%) the *Net value of the non-performed exposures to capital base ratio* reports decline of 19.26 p.p. on a yearly basis, and for the first time in the last five completed years the value of the indicator drops below 100%. The upward trend retains in the first quarter of 2018. In a comparative aspect, the reported values are substantially higher than the average level for the banking system and for the second group of banks.

The return on equity maintains its upward trend in 2017, as well as in the first quarter of 2018 with rates of 4.69% and 5% as at the end of the periods. The reported indicator continues to be significantly lower than the average for the banking system (9.60% and 9.45%), for the second group of banks (9.36% and 9.00%) and for the reference group (10.65% and 10.44%).

During the period of the update, the uptrend registered as of 2012 of growth in the attracted funds, reported annual growth for 2017 and amounts to 17.6%, while the one for the first quarter of 2018 is 1.9% compared to the reported a year earlier. The raise in the attracted funds in 2017 and in the first quarter of 2018 is in line with the growth in the deposits – by 19.3% and 2.1%, while the values of the other borrowed funds decrease. A favourable dynamics of the rated bank is observed compared to the banking system and the second group of banks.

The resource base structure is dominated by the deposits, which value reports slight increase in 2017 (from 95.2% as of the end of 2016 to 96.5%) and in the first quarter of 2018 (by 0.2 p.p. compared to the end of 2017), up to 96.7%.

In 2017, the growth of deposits base is influenced by the increase of individuals and households deposits, while in the first quarter of 2018 the reported growth is dominated by the deposits of non-financial institutions.

During the period of the update, the deposits base structure is not changed substantially and a relatively high concentration is observed in the share of largest depositors. The reported levels of the resource sustainability and the growth in the term deposits are positively assessed.

During the analysed period the bank is primarily financed by funds attracted from the retail banking segment (micro enterprises and natural persons), with a share in the total resource base retained at approximately ~75%.

For the period under review the total assets report growth, as for 2017 their amount is 15.6%, and for the first quarter of 2018 – 1.9% compared to 2017. In a comparative aspect, the reported growth is higher than the average for the banking system and for the second group of banks, while in the first quarter of 2018 there is a decrease in the average indicators – by 0.2% and 8.5%.

The value of net loans holds a major share in the assets structure, which is dominated by the corporate loans.

With the largest growth in 2017 as an increasing percentage compared to a previous year are the funds in cash and in the current account in BNB – 79.9%. However, the increase as a share of the deposits base (14.4%) is at a comparatively low level to the average for the banking system (~20% of the assets).

For the last completed 2017, the investment portfolio reports decline of 10.6%, while it have registered a substantial growth in the last two years (39.1% for 2016 and 52.0% for 2015). As a result, the investments share in the total assets base decreases to 12.2% (15.8% in 2016), holding third place in the structure. For the first quarter of 2018 the opposite trend is observed and as a result, their share in the assets structure increased by 1.4 p.p. to 13.6% compared to the end of 2017. The increase is due to the decrease in Investment properties.

The receivables from credit institutions have a relatively low share in the assets structure (~5%), and in a comparative aspect are much lower than the average for the banking system (13.5%).

BACB maintains well-diversified credit portfolio by sectors. With respect to the maturity structure of the corporate credit portfolio the trend of gradual increase of the term is confirmed, and as at the end of the period with the largest share are the loans with 5 and 10 years residual term. By the residual term of loans, a stabilization of the ratios is observed compared to the

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ones from the last two years, with a slight increase in the largest loans.

The share of "non-performing" loans continues to decrease, a decline of 7.4 p.p. in 2017 and realizing further drop by 1.1 p.p. in the first quarter of 2018.

An important part of the analysis of the credit portfolio quality of the rated bank is the breakdown by years of lending. It should be noted, however, that much of the deteriorated exposures are the result of bad "inheritance" – as of March 31st, 2018, a share of 87.5% loans are granted in the period by 2011 incl.

Preserved are the downward trends from previous years in the *gross ratio of generated non-performing loans* and in the reported negative value of the *net ratio of generated non-performing loans*.

In 2017, the coverage of the depreciated non-performing loans registers growth for a second consecutive year although by slowing pace. In a comparative aspect, it is lower than the average for the banking system. In the first quarter of 2018, the coverage for the banking system is at outpacing growth compared to BACB.

As of the end of the period the share of 15^{-th} major credit exposures continues to decline, although a relative concentration related to the largest loans is still observed.

In 2017, the operating profit decreases by 19.2 % and amounts to BGN 11 984 thousand as of the end of the year. Should be considered that if we ignore the effect of the lump-sum payment for the acquisition of VISA Europe from VISA Inc. in 2016, there would be an increase of 8.3% (BGN 923 thousand).

The net profit of the bank increases both in relative and nominal terms (by 31.6%, BGN 1 878 thousand) and as of the end of the year, it amounts to BGN 7 830 thousand. During the first quarter of 2018, the operating result and the financial one reports an increase in the amount of BGN 3 677 thousand and BGN 3 181 thousand, respectively.

In 2017 and the first quarter of 2018 significant changes of the values of the gross interest spread and the net interest margin are not observed. For the above-mentioned periods decline is registered in the values of the indicators for the banking system and the second group of banks. The shrinking trend in the differences compared to the average is preserved.

The outpacing growth of the profit compared to the average level of assets is leading to a growth in the return on assets ratio, reaching 0.67% as of the end of 2017. In the first quarter of 2018, the value of the indicator amounts to 0.72% and in a comparative aspect is considerably lower than the average for the banking system and the second group of banks.

The downward trend of the equity share in total liabilities retains, and the value of the indicator amounts to 13.8% as of the end of March 2018. In a comparative aspect, the values are higher than the average.

In 2017 the discontinued descending trend Current assets to (Total liabilities minus Equity) ratio from the year 2016 is reversed and reports growth on an annual basis by 5.8 p.p. up to 23.3%. In the first quarter of 2018, the value of the indicator registers insignificant decline (by 0.1 p.p.)

During the period under review significant changes in the liquidity ratio are observed, and on a comparative basis, the ration is still significantly lower than the average for the banking system and for the second group of banks.

BNB recommends within the meaning of Ordinance 11 the ratio of liquid assets to attracted funds from individuals and households and institutions other than credit ones be at least 20%. BACB continues to position itself above that level.

As of the end of 2017 BACB retains its positions as follows:

- 16th by assets;
- 14th by gross loans;
- 16th by deposits.

During the first quarter of 2018 the bank moves up with one place by the size of assets and the size of deposits – to 15th position, however, the change is not a result of the overtaking a place of another bank, it is due to the merger of CIBank in United Bulgarian Bank.

By the size of the credit portfolio, BACB moved up to 12th position. The move is a result of both the merger of CIBank to UBB and of heading up CB Investbank.

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The rating of Bulgarian American Credit Bank would be negatively affected by a sustainable improvement of the portfolio quality, an increase of the generated profit and income indicators along with a stable capital adequacy and liquidity.

The rating would be negatively affected by deterioration of assets quality, increase in the depreciation costs, significant reduction in business activity, as well by a decrease in the capital adequacy and deterioration of bank's liquid position.

Main Financial Indicators:

(thousand BGN)	*3.2018*	*2017*	*2016*	*2015*	*2014*	*2013*
Balance sum	1 263 499	1 240 099	1 072 892	1 017 537	815 298	777 729
Equity	174 209	176 285	168 171	161 944	155 628	165 656
Total Interest Income	10 248	39 064	38 098	37 117	32 790	33 778
Net Financial Result	3 181	7 830	5 952	814	-9 167	-15 996
Net Interest Margin	3.07%	3.01%	3.03%	2.59%	1.78%	0.84%
Return on Assets	0.72%	0.67%	0.57%	0.09%	-1.19%	-2.00%