CREDIT RATING AGENCY

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„Investbank” AD

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FINANCIAL STRENGHT RATING *	Update	Update	Update	Update
Date of Rating Committee:	12.10.2015	26.10.2016	22.11.2017	28.11.2018
Date of Publication:	13.10.2015	27.10.2016	23.11.2017	30.11.2018
Long-term Rating:	B-	B-	B-	B-
Outlook:	stable	в развитие	stable	stable
Short-term Rating:	C	C	C	C
Long-term National-scale Rating:	B (BG)	B (BG)	B (BG)	B- (BG)
Outlook:	stable	в развитие	stable	stable
Short-term National-scale Rating:	C (BG)	C (BG)	C (BG)	C (BG)

** За да се запознаете с пълната рейтингова история вижте таблицата в края на документа.*

„BCRA – CREDIT RATING AGENCY” (BCRA) is the third qualified rating agency in the EU, registered under Regulation (EC) 1060/2009 of the European Parliament and of the Council. BCRA assigns credit ratings 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 limitations.

„BCRA – Credit Rating Agency“ (BCRA) assigns to „Investbank” AD the following ratings:

- *Long-term financial strength rating **B-, stable** outlook**,** short-term rating **C;***
- *National-scale long-term rating **B (BG), stable** outlook**,** national-scale short-term rating **C (BG).***

BCRA‘s officially adopted Bank Financial Strength Rating Methodology has been applied (https://www.bcra-bg.com/files/bank_methodology_2018_bg.pdf).

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

The political situation in Bulgaria remains stable and the government is committed to speeding up the process of joining the Eurozone by officially submitting a letter of intent. In August 2018, the Council of Ministers approved an appropriate Action Plan including measures aimed at Bulgaria's accession to ERM II and the Banking Union by July 2019. A number of legislative changes are foreseen to improve financial sector supervision, the bankruptcy framework, the fight against money laundering and the modernization in the management of state enterprises. Measures will be implemented in a coordinated manner by national and international institutions, and progress in all these areas will, when achieved, pave the way for the country to join simultaneously the ERM II and the Banking Union

In the first half of 2018, the **Bulgarian economy** expanded by 3.4%[1] in real terms. Domestic demand (consumption and investment) contributed positively to GDP dynamics. Household consumption increased by 7.9% on an annual basis, boosted by the favourable labour market developments and credit acceleration. Investments' trend is also in an upward direction. Gross fixed capital formation accelerated considerably, reaching an annual growth of 8.5% (compared to 3.3% in the same period of 2017). Both public (mainly EU programs) and private investment drove enhanced investment activity.

At the end of August 2018, country's **gross external debt** amounted to EUR 33 805 million (61.1% of projected GDP). In nominal terms, the debt increased by EUR 408 million compared to the end of 2017. The relative share of the public sector's external debt fell to

[1] *Unadjusted data.*

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18.2%, while that of the private sector rose to 81.8% of the total external debt.

As of the end of August 2018, the BNB's **international reserves** amounted to EUR 23 960 million (43.3% of projected GDP) and provided 160.7% coverage of the monetary base, a solid buffer used by the central bank to ensure the stability of the currency board.

The inflow of **foreign direct investment** to the country is decreasing. According to preliminary data, foreign direct investments in Bulgaria for the first eight months of 2018, reported according to the principle of the initial direction of the investment, amounted to EUR 231 million or 0.4% of projected GDP, which represents a nominal decrease of 71.6% compared to the same period of the previous year.

The **labour market** marks a favourable development, with record-high indicators for economic activity and employment of the population. Labour incomes in the economy retain their upward trend. In the first half of 2018, the **average gross wage** in Bulgaria reached BGN 1 101 per month (~EUR 563 per month), nominally increasing by 7.6% compared to the same period in 2017. Annual minimum wage hikes in the country continued to be a major factor for the wage growth in some economic activities. Gross base remuneration was raised by 11% to BGN 510 per month from the beginning of 2018, also has an analogous impact on labour costs.

The price level in Bulgaria continues to be on a rise. In September 2018, the annual inflation rate (measured by the HICP) reached 3.6%, while the average rate for the last 12 months accelerated to 2.3%. The price level was impacted jointly by internal and external factors. The rise was mainly driven by services inflation accelerating in line with the strengthened domestic demand. Hikes in some of the administered goods and services' prices generated additional pro-inflationary pressure. The external factor of significant contribution was the increase of international prices of oil and other major commodities, exerting both direct effects, as well as indirect effects on other HICP components.

Public finance indicators are improving, backed by the robust economic activity in recent years. In the period January - August 2018, total budget revenues under the Consolidated Fiscal Programme (CFP) increased by 11.6% compared to the same period of the previous year, with the tax revenues being the main driver. Tax revenues (including social security contributions) grew by 10.0% on an annual basis summing up to 82.3% of total CFP revenues for the period. The budget balance as of August 2018 posted a surplus for BGN 2 388 million or 2.2% of projected GDP, compared to a surplus of BGN 2 151 million or 2.1% of GDP in the same period of 2017. The CFP for 2018 set a budget deficit target at 1.0% of GDP but 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 government plans 10% increase in the funds for wages and contributions in the budget sector as from 2019, while the wage hike in the education sector would be 20% in line with the existing government commitment. The minimum wage in the country is scheduled to reach BGN 560 per month. Pensions are set to increase by 5.7% from July 1, 2019, and their maximum amount would reach BGN 1 200. Other measures with an impact on the insurance policy include an increase in the maximum insurable income to BGN 3 000 and an increase of the minimum insurable income for the self-insured persons to BGN 560.

The **government debt** follows a positive downward trend both in nominal terms and as a share of GDP. At the end of August 2018, government debt amounted to BGN 22 320 million (20.6% of projected GDP). The debt decreased nominally by BGN 1 215 million compared to the end of 2017 due to regular repayments and absence of new obligations during the year.
The low government debt level is assessed as a positive factor also in comparison with the other EU countries. As of the end of Q2 2018, the consolidated debt of "General Government" sector amounted to BGN 24 815 million or 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.

Bulgarian government securities achieve relatively low **yield** for the region. The yield on the long-term benchmark issue (with a maturity of 10Y and 6M), based on actual concluded deals on the secondary market, fell beneath 1% for the first time in January 2018 and reached 0.81% in August, which is the lowest monthly value of the long-term interest rate for convergence assessment purposes reported so far.

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The banking system of the country remains stable, characterized by a growth in the assets, maintained in the last two years by the savings from households and non-financial corporations and the increase in lending. By the end of June 2018, gross credit portfolio of the banking system annually increased by 6.1% - a record high value for the past five years. The quality of bank portfolios continues to improve, which is evidenced by the decreasing ratio of the gross non-performing exposures to the gross value of loans, which, however, remains relatively high (9.1%). There have been some structural changes concerning ownership in some banks, a further outflow of the Greek capital and the ongoing consolidation in the system.

The European Central Bank plans to execute asset quality review and stress tests of Bulgarian banks[2] in 2019 in order to ensure a smooth transition to the Banking Union.

At the end of the update period, June 19, 2018, a resolution is taken for an increase of the **shareholders capital of “Investbank” AD** by BGN 10 million and all shares are recorded by the main shareholder “Festa Holding” AD and has not changed significantly the banking structure.

On July 12, 2018, is completed the final deal for the acquisition of “Victoria EAD Commercial Bank” (Affiliate of “Corporate Commercial Bank” AD (in …) by Investbank AD. With a contract for a reorganisation, dated August 6, 2018, is finalized the official legal merger of the “Victoria” Commercial Bank (Transformative Company) into the “Investbank” AD (Receiving company). The latter becomes the universal legal successor of all rights and obligations, arising from the ownership of Victoria Commercial Bank EAD, which is terminated without liquidation. As a result of the merger, an increase of the capital of Investbank will not be carried out as the latter holds all shares of the transforming company. The BNB Governing Council approves the merger with a Decision 116 354 / 01.11.2018.

In the period under analysis, there are no changes in the **Supervisory Board** and by November 2018, its members are as follows:

- Petia Ivanova Barakova-Slavova – Chair;
- „Festa Holding“ AD, ЕИК 103123984, represented by Zlatomir Dimitrov;
- Dimitrijka Lazarova Andreeva.

In 2017, the composition of the **Management Board** is unchanged, while in 2018 the following members are dismissed: Emilia Traykova (March 23, 2018) and Plamen Milkov (October 2, 2018), replaced by Ivaylo Vassilev Sotirov (September 4, 2018) and Ivan Tsvetkov Bachovski (October 29, 2018). By November 2018, the members are namely:

- Zdravka Rumenova Russeva – Chair of MB and Executive Director;
- Vesela Ivanova Koleva-Djidjeva – member and Executive Director;
- Ivaylo Vassilev Sotirov - member and Executive Director;
- Ivan Tsvetkov Bachovski - member.

In 2017, the bank reports a considerable decrease in the **capital base** of 14.4 % (BGN 32.5 million), followed by 1.8 % as of the H1 2018. The decrease is in the line of Tier-1 capital, while the decrease in Tier-2 relates to the decrease in value of the subordinated term debt. The main reason for the reported decline is the implementation of the recommendations under the approved by BNB Action Plan as a result of the Assets Review and Evaluation carried out in 2016. Following its commitment, the Bank covered in full the rest of the additional buffer, calculated as additional provisions for impairment loss at the amount of BGN 29 295 thousand.

By the end of 2017, the total amount of **risk exposures** decreased by 1.2% (following a rate of 1.9% in 2016) for a second consecutive year, while in the first half of 2018 there is a growth of 5.5% (3.0%) compared to the end of the past year.

The outpaced decrease of the capital base compared to the decrease of the risk-weighted assets in 2017 and the continuous decrease of the capital base and the increase of the risk exposures in the first half of 2018 led to a decrease in the **total capital adequacy** by the significant 2.56 p.p., reaching 19.14% at the end of 2017. There is a further decline of 1.15 p.p. to 15.43% at the end of June 2018, which is the lowest recorded in a retrospective aspect following the end of 2012. With the capital adequacy levels thus reached, the bank is already positioning itself significantly below the average levels of the banking system (22.08% at the end of 2017 and 20.82% as of 30 June 2018) and the banks in the second group (22.72% at the end of 2017 and 22.30 % as of 30 June 2018), but still remains above the required minimum (13.5%).

[2] In a press release published on 12.11.2018 by the ECB, six banks will be subject to evaluation: UniCredit Bulbank AD; DSK Bank EAD; United Bulgarian Bank AD; First Investment Bank; Central Cooperative Bank AD and Investbank AD

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In the update period, the bank continues to increase and retains higher levels of unadjusted (12.8-13.3) and adjusted (31.5-31.8) **leverage** compared to the average of the banking system and the banks in the second group. The significantly higher rates of the adjusted leverage compared to the average levels in the banking system (9-10) and the banks in the second group (10) are due to the significantly higher share of long-term assets in total assets.

During the review period, due to the significant fall in the capital base, a decline in the net exposures of the classified exposures declined in 2017, and the increase in the latter in the first half of 2018, led to a continuing deterioration in the ratio of **net exposures to capital base** by 5.8 pp. and by 9.2 pp. In a comparative aspect, the level of the indicator remains significantly higher than the average for the banking system and for the banks in the second group, which reported a steady downward trend.

As a result of the significant loss reported in the fourth quarter of 2017, and the inability to be compensated by profits attained in the next two quarters, the value of the **return on equity** ratio is severely deteriorated. It is negative, loose analytical value, and cannot be compared with the average levels for the banking system (9.6% in 2017) and banks in the second group (9.4% in 2017).

In past two completed financial years (2015 and 2016), the downward trend of the **resource base** has been changed during the current review period. The total attracted funds increase in 2017 by 4.1 % and in the six months of 2018, the trend retains with a growth rate of 3.7%. The increase is mainly driven by the corporate deposit portfolio, with a growth of 18.5% in 2017, followed by another 12.2% for the first half of 2018. This process runs against the backdrop of the repaid debt under a credit line provided by the Bulgarian Development Bank AD, which led to an annulment of the attracted funds from credit institutions. The growth rates for the bank in 2017 are lower than those for the banking system (6.5%) and the banks in the second group (10.5%). While, in the first half of 2018, these rates exceed the reported growth rate of 2.9 % for the banking system and the decline of 4.7% for the Second Group of Banks.

There are no significant changes in the structure of the deposit base over the review period. Deposits of natural persons dominate; while in a comparative aspect the share of these deposits in the total resources of the bank exceed the average for the banking system and for the banks in the second group.

The dominant role of term deposits in the attracted funds from households and non-credit institutions is preserved. The concentration in the resource base remains moderate, with rising shares of the 15 largest depositors by the end of 2017 and by the end of June 2018.

At the end of 2017, Investbank AD reports annual growth of 2.0% of the **value of assets** after a decline in 2016 of 2.0% compared to the previous year. For the same period, the assets of the banking system increase by 6.2 % (5.2% in 2016) and those of the banks in the second group by 9.9 % (9.2%). These trends continue in the first half of 2018 when the bank assets grew by 2.8 % compared to the past year and compared to the achieved growth of 2.4 % for the banking system and decline of 5.4% for the banks in the second group.

The size of the investment portfolio rose at the end of 2017, decreased in the first half of 2018 (considerably less compared to the growth), and maintains a stable relative share of about and slightly below 30% since 2013 in a retrospective aspect. The share exceeds considerably the average level of the banking system (14.3% as of end of 2017 and 13.6% as of June 2018) and of the banks in the second group (14.0% in 2017 and 13.3% in June 2018). The registered growth in 2017 is mainly a result of the increased size of the debt instruments (7.6%), which are the leading type of investment (share of 86.6%), consisting almost entirely of Government Securities. Investment property (maintained after 2016 at around 12%) retains the second largest share in the portfolio, by a growth of 5.4% in 2017 and 0.5% in the first half of 2018.

In 2016, after a two-year trend of growth of the **gross loan portfolio** and a reported decline of 11.3%, the bank registered almost zero growth in 2017 (0.04%). In a comparative aspect, after the year of the Review of the Assets Quality of Bulgarian banks, the gross loans in the banking system started to increase gradually and after the minimum growth of 0.6% in 2016, the increase in the year 2017 is 3.0%. Merely, for the six months of 2018, the growth is 5.0% compared to 2017, while Investbank reports again decline of 5.2% for the same period. By the share of gross and net loans in total assets, the Bank remains well below the system's average and of the banks in the second group.

The **structure** of gross portfolio is almost unchanged in the period of the update and is dominated by loans to corporates (slightly below 80%). The terms structure is characterised by a decrease in the leading group of exposures of corporate loans – those with a repayment

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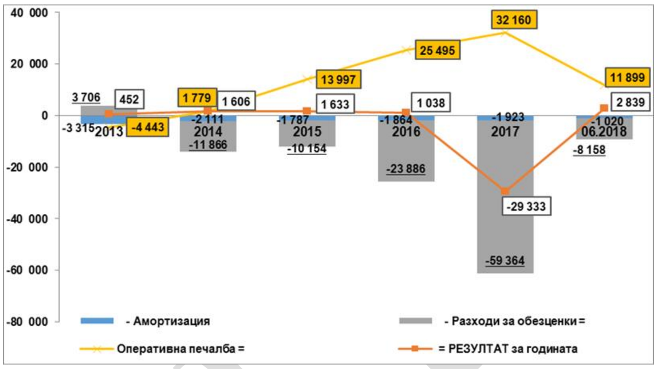
period of up to 5 years, at the expense of those with a period between 5 and 10 years. For the individuals, the change is characterised by an increase of exposures of the group with a residual repayment period of over 20 years. In the structure of the corporate loan portfolio, some concentration by industries remains.

In 2016, following the reported significant increase of the **deteriorated loans** to a level of 28.1% (by 5.7 p.p.) in the gross loan portfolio, in 2017 there is another increase (by 4.2%), thus reaching a share of 29.3% compared to the gross ones. The quality deterioration of loan portfolio is evident also from the marked in 2017 almost double amount of newly classified loans in the non-performing ones. During the review period, the imbalance towards the banking system is eliminated, and Investbank maintains much lower coverage levels for gross classified loans. At the end of 2017 and at the end of June 2018, they are already slightly below the system average, and over a period are above the average for the banks in the second group.

In the period under review, in 2017, Investbank reports an increase in operating profit by 26.1% compared to the previous financial year, while for the first half of 2018 there is a negative change of 19.7% compared to the first half of 2017. The positive change in 2017 is due to the one-off effects of the 9.5% increase in net interest income (influenced by a significant decrease in interest expense) and to the decrease in administrative expenses by 7.7%. Non-interest income has a relatively minor change over the period of + 1.8%.

The negative tendency in the first half of 2018 is mainly influenced by the significant decrease in profits from operations with financial assets.

The net financial result for 2017 is an excessive amount of loss of BGN 29.3 million, after the reported in the past three years similar net profits at the range of BGN 1.0 million – 1.6 million. In view of the reported improvement in the operating results, the registered loss results from the high amount of the impairment for the year - a net value of BGN 59.4 million. The significant increase compared to previous reporting period is a result of the activities implemented in compliance with the approved by BNB Plan related to the findings from the independent review and assessment of bank's assets as of December 31, 2016. As a result, the residue of the calculated additional impairments are incorporated in full for the financial 2017 year, and the formed additional capital buffer as of December 31, 2017, is reset, thus the recommendations are fulfilled.



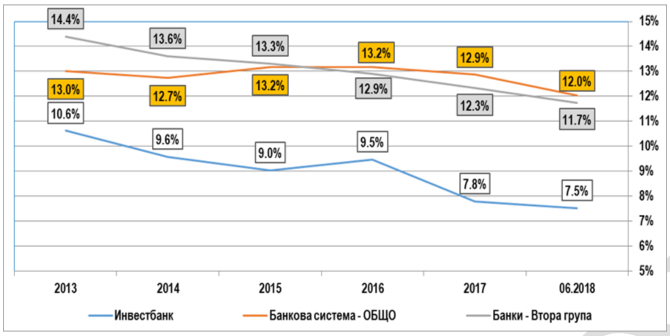
In the average amount of income-bearing assets is observed a decline more visible in the interest income leading to a decrease in the indicator **return on interest-bearing assets**, which value decreases by 0.50 p.p. as of the end of 2017 (down to 3.87% and goes down in the same direction reaching the level of 3.52 % as of 30 June 2018. The levels reached by the rated bank are lower than the average of the banking system (3.95% и 3.83% at the end of the two periods respectively), while the levels of the banks from the reference group are lower than the levels of the rated bank as of end of 2017 (3.82%) and higher as of end of June 2018 (3.72%).

The descending trend in the **price of interest liabilities** is retained in the period and its level (1.19 as of the end of 2017 and 0.94 as of the end of June 2018) remains considerably higher compared to the average of the banking system (0.45% at the end of 2017 and 0.38% as of June 2018) and of the banks in the second group (0.49% at the end of 2017 and 0.42% as of June 2018).

The rising trend in the **gross interest spread** is retained and its value is 2.68% as of the end of 2017 (2.45% a year earlier) and 2.58% in the middle of 2018. The Group and the banks in the second group are characterized by decreases in the indicator's figures, but at levels (3.3% -3.5%) continuing to exceed significantly those reported by the Bank. Similar dynamics and positioning of the bank are observed in relation to the **net interest margin** indicator.

Non-interest income of the rated bank remains high and rises compared to the average value of the assets, while at the end of 2017, it covers a large part of the operating expenses (92.7%), thus exceeding the average level of the banking system (72.6%) and much more of the banks in the second group (59.6%).

In the period of rating review, the equity declines by the considerable rate of 16.2% in 2017 (as a direct result from the high value of the reported loss in 2017) and by the additional 0.8% in the first half of 2018, while in total liabilities a growth is observed in each of the past five years, except in 2016. These one-way changes led to a decrease in the share of equity in total liabilities by 1.7 p.p. in 2017, reaching a rate of 7.8%, which is significantly lower than the average of the banking system (12.9%) and of banks in the second group (12.3%). By the first half of 2018, the ratio continued to decline, reaching a level of 7.5% of the banking system, which had a similar change of direction, but at a higher range.



In the review period, the liquidity indicators of Investbank alter as follows:

- **Current Assets to attracted funds -** since the previous two years (2015 and 2016) the indicator decreased, reaching a level of 14.4%. In 2017 there is an increase in value to 15.9%, which trend continued in the first half of 2018, while the level of the ratio is far below the average retained by the banking system and the banks in the second group with levels at about 36%;
- **Liquidity ratio -** the indicator is characterized by slight fluctuations in relatively constant level during the last three financial years prior to the review period, while in 2017, it rises by 1.6 p.p. up to 37.5%, reaching the average of the banking system (39.0%) and of the banks in the second group (38.9%), but below their levels.
- **Total amount of credits to total amount of deposits3 -** the decline in the value of the indicator from the previous year retains and reaches 52.4% at the end of 2017 and moves down to 47.9% in the first half of 2018. This fact shows the outpaced increase in the value of the attracted deposits to the value of the loans. The banking system has a similar downward dynamics for the period, but at significantly higher levels of the indicator (at the end of 2017 average 71.5% of the total of the system and 73.2% of the second group banks).

According to Ordinance 11, the Bulgarian National Bank recommends the **ratio of liquidity assets to attracted funds from institutions**, different from credit institutions, citizens and households of at least 20%, which requirement was fulfilled by the bank. By the end of 2017 the value of the indicator continues to exceed significantly the required level and is 40.2% (the highest value for the last 5 years), following the level of 38.9% at the end of 2016.

The maintained values of liquidity ratios under Regulation 575 (LCR, NSFR) position the bank significantly above the regulatory levels and are as follows:

- **LCR (Liquidity coverage ratio) –** under the requirement ≥ 100%, the reported values by the bank are 479% by December 2016, 506% by June 2017 and 538% by December 2017 (at the average level for the banking system at the end of 2017 of 347.6%);
- **NSFR** (Net stable funding ratio) – under the requirement ≥ 100%, the reported values by the bank are 211%, 190% и 214% at the same reporting periods.

In the review period, Investbank retains its position by the size of assets – 12th at the end of 2017 and 11th at the end of first half of 2018 (the move is a result of the merger of CIBANK and UBB). According to the size of gross credits the bank moves downwards with one position in 2018 (13th), outpaced by BACB, and also moves downwards with regard to the attracted deposits (12th position, left behind by CIBANK in 2017 and positioned conditionally at the same place in 2018, as a result of the merger of the latter in UBB).

After the implementation and the launch of the newly introduced accounting system, Internet banking and card system, the development of information systems in 2017 are subject to additional upgrade and optimization of their various functions. A significant part of the Bank's IT department is engaged in the implementation of a system responding to the requirements of the standards IFRS 9 entered into force as from 01.01.2018. In 2018, a platform / software for assessment of the credit quality of borrowers (a rating system for legal entities and a scoring system for individuals) is developed and implemented in compliance with the requirements of the standard. The work on implementing a system for

[3] The calculation excludes loans and deposits of credit institutions

independent authentication when using electronic channels for services of the bank and deployment of IP telephony in all bank branches continues.

Main Indicators:

(Thousand BGN.)	**6.2018**	**12.2017**	**12.2016**	**12.2015**	**12.2014**	**12.2013**
Balance Sum	2 009 465	1 954 129	1 916 189	1 955 963	1 913 558	1 676 365
Gross Credits	832 913	878 351	877 994	989 726	877 063	728 977
Equity	150 908	152 187	181 542	176 474	183 287	177 989
Total Interest Income	22 883	53 558	63 963	70 559	67 053	59 331
Net Financial Result	2 839	-29 333	1 038	1 633	1 606	452
Total Capital Adequacy	15.43%	16.58%	19.14%	18.70%	21.41%	15.50%
Net Interest Margin	2.32%	2.39%	2.07%	1.32%	0.48%	0.29%
Return on Assets	-1.40%	-1.55%	0.05%	0.08%	0.09%	0.03%
Gross Non-performing Exposures / Total Loans	32.91%	29.28%	28.11%	22.41%	25.79%	38.68%
Net Ratio of Impairments	2.94%	1.68%	3.29%	-0.67%	-12.48%	0.00%
Liquidity Ratio	-	37.47	35.90	34.47	35.17	33.35

***The rating might be positively** affected by sustained improvement in the quality of the portfolio, increase in generated profits and profitability indicators, with further decrease of the share of non-performing exposures, increase of their coverage from depreciation, successful realization of the acquired fixed assets (collateral on loans), maintaining stable capital adequacy and liquidity.*

Rating History:

The ratings displayed in the chart are assigned under the previous Methodology for assigning ratings of the ability of insurance companies to pay claims and are not directly comparable with the ratings assigned after the entry into force of the current methodology in September 2015.

FINANCIAL STRENGTH RATING	**Initial Rating 4.2009**	**Monitoring 18.11.2009**	**Update 03.5.2010**	**Monitoring 07.12.2010**	**Update 25.5.2011**
Long-term Rating:	**BBB-**	**BBB-**	**BBB-**	**BBB-**	**BB**
Outlook:	***Stable***	***Negative***	***Stable***	***Negative***	***Negative***
Short-term Rating:	**A-3**	**A-3**	**A-3**	**A-3**	**B**
FINANCIAL STRENGTH RATING	**Monitoring 14.09.2011**	**Update 19.12.2012**	**Monitoring 10.05.2013**	**Update 18.12.2013**	**Update 13.10.2014**
Short-term Rating:	**B+**	**B+**	**B-**	**C**	**B-**
Outlook:	***Negative***	***Negative***	***Negative***	***Stable***	***Stable***
Short-term Rating:	**C**	**C**	**C**	**C**	**C**