

<p>August 2012</p> <p>ZAD „Armeets” AD</p>	<p>Delyan Pehlivanov, lead financial analyst d.pehlivanov@bcra-bg.com</p> <hr/> <p>Vesela Velichkova, financial analyst v.velichkova@bcra-bg.com</p>
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Claims Paying Ability Rating	Initial rating 6.2006	Update 11.2007	Update 12.2008	Update 10.2009	Update 30.08.2010	Update 10.08.2011	Update 10.08.2012
Long-term Rating:	BB+	iBBB-	iBBB-	iBBB	iBBB	iBBB	iBBB
Outlook:		stable	stable	stable	stable	stable	stable
Short-term Rating:		A-3	A-3	A-3	A-3	A-3	A-3

BCRA – CREDIT RATING AGENCY (BCRA) is the third qualified rating agency in EU, registered under Regulation 1060/2009 of the European Parliament and of the European 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. The rating scale of BCRA coincides with the scale of Standard & Poor's.

BCRA retains the long-term claims paying ability rating of ZAD „Armeets” AD iBBB and short-term rating ia-3 (outlook: stable). The officially adopted methodology for assignment of claims paying ability rating to insurance companies is used by BCRA (http://www.bcra-bg.com/files/file_202.pdf). To elaborate the credit report and to award the credit rating, BCRA uses information from the rated insurance company, FSC, National Statistical Institute, BCRA's database, consultants and other sources of public information.

The features of Bulgarian general insurance market during the period under review (03.2011– 03.2012) are as follows:

- Maintain the descending trend in the realized gross premium income (GPI), as the decrease year on year as of the end of the first quarter of 2012 (3.7%) was higher compared to the period 3.2010-3.2011 (2.6%). GPI in direct insurance decreased by 3.4% yoy;
- The potential for growth of the insurance market remained high with view of the low levels of insurance density and penetration;
- Despite the decline in GPI as a result of the taken measures by the general insurance companies

to optimize the costs and to optimize also the expenses of the overall activity at the end of 2011 the financial results improved abruptly: the sector closed up the year with a negative result from insurance activity, but the loss was considerably less in absolute value than the previous year. Despite the reported decline of investment income by 14.5%, net financial result of general insurance companies was positive;

- At the end of the first quarter of 2012 a minimum loss from insurance activity was registered and total positive financial result in the amount of EUR 9,721 thousand.

- The trend of ceding of a market share of leading insurance companies was retained;

- The motor insurances continued playing a leading role on the market of general insurance in Bulgaria with a total share of 75.5% (compared to 77.2% to 3.2011).

During the rating update no change has occurred in the shareholding structure of ZAD "Armeets" AD. The number and the team of members of Management and Supervisory Boards remained the same as in the previous period. The strategic directions of development of the company remained unchanged, and the management activities are focused on achieving the set targets in the programme of ZAD "Armeets" AD.

In 2011 ZAD "Armeets" AD registered a growth of 3.6% in GPI in direct insurance in the conditions of a shrinking market (a decline of 2.3% for the adjusted sector¹), as a result of which the company increased its market share to 11.71% (11.10% year back). The

¹ The data from the sector are adjusted with the data from the rated company.

increase is mainly in line of “Third Party Liability for motors” (annual growth of 21.2% compared to 6.9% on average for the other companies), while „Autocasco” insurance reported a decrease of 1.5% (a 12.8% decline for the adjusted sector). As a result of this dynamics the rated company increased its market share by 0.98 % with “Third Party Liability for motors” and by 1.69 % with „Autocasco” insurance. On the insurances „Fire and natural disasters” the company realized lower GPI by 9.3% compared to 2010 (and a slight decline of the market share), while with „Other claims of the property” there was an increase of 20.3% in GPI in direct insurance. In the first quarter of 2012 the upturn trend with GPI was retained and ZAD Armeets AD registered a growth of 6.1% (a decline of 4.5% for the adjusted sector) and increased its market share by 1.01 % to 11.41% year on year. During this period the increase was in line of „Third Party Liability for vehicles” (5.1%), as well as of „Autocasco” (8.8%). The trend with the two insurances on average for the other companies from the sector is negative, which led to improvement of the market position of ZAD “Armeets” in these directions. Regarding the portfolio structure of the company in 2011 the main changes are related to a slight decline in the share of Autocasco insurance year on year (2.56 % to 49.59%) and growth of the share of “Third Party Liability for motors” (4.59 % to 31.68%). The share of the insurance „Fire and natural disasters” decreased (from 6.59% for 2010 to 5.77% for 2011). In the first half year of 2012 the downturn trend with „Autocasco” was retained; „Third Party Liability” also registered a decline. The insurance share of „Accident” insurance, as well as „Aircrafts” reported an increase.

After its decline in 2010, in 2011 net claims ratios increased and reached to the level of 2009 (53%), which is slightly above the level of the other leading companies. As of 03.2012 the company occupied a more favorable position by this indicator. Over the last two years net commission ratio of the company is about the average for the other leading companies. In 2011 it was lower, while in the first three months of 2012 it was slightly higher compared to the competitive group. In 2011 combined expense ratio retained almost without any change on an annual basis and a little bit higher compared to the average for the other leading companies. As of 03.2012, however, an increase was registered as the gained value exceeded 100%, which is an indicator for a loss from insurance activity.

ZAD "Armeets" AD continues keeping contracts for reinsurance coverage on its main insurance groups. For the update period no considerable changes from rating point of view under the reinsurance contracts.

On part of the contracts the insurance limits are slightly increased, as well as the coverage is expanded. The rates of premiums and organized stakes were updated on a little part of reinsurance contracts. The Company keeps working with reinsurers with high credit ratings.

As of the end of 2011 the size of the investment portfolio of the company increased by 4.9% compared to the previous year, as the increase was ahead strongly from the average for other companies in the sector (2.5%). The increase of the portfolio of ZAD "Armeets" is in line of a 30 % growth of investments in bank deposits, which increased the total relative share of highly liquid assets (government securities + bank deposits) to 37.8% (32.7% at the end of 2010). However, this share remained significantly lower than the average for the other general insurance companies (70.9%). In its bigger part the incomes from investment activity in 2011 are formed by interests of bank deposits and coupon payments on government securities. As a result of losses from reevaluation of the stocks the profitability of the investment portfolio of ZAD "Armeets" dropped considerably - up to 0.52% at the end of the year (6.11% in 2010.) and it is considerably lower than the average for other companies in the sector (4.60%). At the end of the first quarter of 2012 the company increased the size of its investment assets by 3.8% yoy, while the other companies in the sector reported an average increase of 1.1%. The achieved profitability as of 31.03.2012 (0.88%) is lower compared to the achieved by ZAD „Armeets” AD during the same period of the previous year (1.21%), as well as by the realized average profitability of the other general insurance companies in the first quarter of 2011 (4.39%). As 30.06.2012 the increase in the investment portfolio of ZAD "Armeets" AD achieved 4.0% yoy. The structure of the portfolio did not report considerable changes. Profitability as of the end of the second quarter of 2012 was -0.59% (3.79% for the same period of 2011). Forming the portfolio of assets for covering the technical reserves the diversification requirements set out in the Insurance Code were followed.

In 2011 ZAD "Armeets" registered a growth of 4.2% in realized total GPI in the conditions of shrinking market (a decline of 2.2 % for the adjusted sector) and a 10.0% growth in net earned income (with an average decline for the other companies of 4.6%). Net financial result is positive (BGN 899 thousand), but significantly lower than the previous year (BGN 6,718 thousand) as the result from insurance remained relatively unchanged compared to 2010 but there is a decline in investment income. There is an increase in the values of both gross and net claims ratio, but they remain close to the average for the group of leading

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companies. The values of combined expense ratio remained relatively favorable. As a result of a decline in the profit the return on equity decreased to 2% (16% in 2010). Liquidity ratio decreased its cost, but remained higher than the average for the competitive group. In the first half year of 2012 ZAD "Armeets" registered a growth of 10.1% in GPI and 10.9% in net earned income. Also gross and net claims ratios grew up in comparison with the first half of the previous year, and to the end of 2011, too. As a result of increased claims the company reported a loss from insurance activity and negative net financial result in the amount of BGN 1,650 thousand. In comparison with the first half of 2011 expense ratio improved to some extent, and the value of commission ratio did not register considerable changes. In the period 6.2011-6.2012 ZAD "Armeets" haven't distributed dividends and capitalize its profit, due to which the dynamics of equity is entirely determined by the registered financial result. As a result of the reported negative net financial result, as of the end of the first half year of 2012, the equity decreased by 10.7% yoy. Due to a decline in their own funds, decreased with intangible assets and a slight increase in the solvency margin, the coverage ratio decreased its value to 1.27 (1.50 as of 06.2011). During the period of surveillance liquidity ratio of technical provisions retained its value relatively stable,

and that of the reserve for upcoming payments decreased slightly due to anticipating increase of the reserves to the liquid assets. The values of both indicators remained lower than the average for the group of leading companies.

During the period under review ZAD „Armeets” AD is featured with a relatively fair financial condition.

Main financial indicators of ZAD 'Armeets" AD	6.2012	6.2011	2011	2010	2009
Gross Premium Income	83 471	75 836	161 733	155 269	148 239
<i>Change rate yoy</i>	10.1%	6.3%	4.2%	5.0%	2.0%
Net earned Income	73 150	65 989	138 622	126 030	138 567
<i>Change rate yoy</i>	10.9%	1.8%	10.0%	-9.0%	30.0%
Result from insurance activity	-1 290	791	577	614	224
<i>Change rate yoy</i>	-	63.0%	-6.0%	174.0%	-
Net profit	-1 650	1 687	899	6 718	2 975
<i>Change rate yoy</i>	-	-52.0%	-86.6%	126.0%	54.0%
Gross Claims Ratio	53.7%	46.8%	51.4%	44.1%	50.1%
Net Claims Ratio	56.2%	50.9%	53.4%	47.9%	53.1%
Combined Expense Ratio	101.8%	98.8%	99.6%	99.5%	99.8%
Operating Leverage	-	-	335%	306%	394%
Financial Leverage	-	-	323%	283%	299%
Liquidity Ratio	3.3%	3.5%	3.4%	4.4%	4.4%
Return on equity	-4.2%	11.8%	2.2%	17.2%	9.0%