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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:	<i>Stable</i>	<i>Stable</i>	<i>Stable</i>	<i>Stable</i>	<i>Stable</i>	<i>Stable</i>	<i>Stable</i>
	Update 14.10.2013	Update 07.11.2014	Update 06.11.2015				
Long-term Rating:	iBBB	iBBB	iBBB-				
Outlook:	<i>Stable</i>	<i>Stable</i>	<i>Stable</i>				

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**BCRA assigns the long-term claims paying ability rating to ZAD „Armeets” AD: iBBB- (outlook: stable). The officially adopted methodology by BCRA for assigning a claims paying ability rating is used ([http://www.bcra-bg.com/files/file\\_202.pdf](http://www.bcra-bg.com/files/file_202.pdf)).**

The report has been prepared and the rating – assigned, based on information, made available by the rated insurance company, the FSC, the National Statistical Institute, BCRA’s database, consultants and other sources of public information.

The political environment as of the time of preparation of the report could be determined with a relative stability.

During October 2015, there were local elections in Bulgaria that did not lead to any significant changes in the political layers.

For the first quarter of 2015, the country registered a considerably high real growth in GDP – 2.2% compared to the same quarter of the previous year (compared to 0.2% for Q1 2014), and for the next quarter (Q2 2015) the rate remained almost unchangeable – 2.3%, as the reported value was slightly under this of the same (second) quarter of the previous year (2.6%).

During the first half of 2015, the investments in the country remained at similar levels compared to the reported during the same period of the previous year, despite the observed drop in the investment flows during the second half of 2014 (compared to the reported values for 2013).

A slight improvement was observed in the labour market conditions, manifested through a drop of the unemployment rate as the levels remained high.

The price level in the country reported drops over the months since the beginning of 2014, that led to intensification of the deflation processes. After February 2015, a gradual decline was observed in the level of the reported deflation.

The forecast says that the country shall be in a situation of low deflation by the end of 2015 – within 0.5%, measured through Harmonised Indices of Consumer Prices (HICP). The increase in the

electricity prices for business sector also led to an increase of the price level.

As a result of the political and economic instability of the country observed during 2014, at the end of the year a significant increase was reported in the budgetary deficit, as well as an increase in the leverage level of Bulgaria. The increase of the debt continued also in 2015, while there was an improvement in the budget.

The economy of Bulgaria can be determined with a low economic activity for the previous year (2014) and a weak recovery for the first half of 2015 which was expected to persist through the remainder of the year.

The events in the banking system during 2014 led to a potential risk for the banking institutions to deepen the banking crisis and involvement of a larger number of participants in this sector. Despite the increased risk, the banks in Bulgaria maintained its stability. For the first half of 2015, the banking environment could be described as stable, as evidenced by the high capital adequacy and liquidity of assets and growth in the deposits. There was reduction in the negative rate of the change of loans, and the share of the classified loans marked a decrease.

During the period of updating, the general insurance sector operated in an adverse economic environment resulting from the effects of the global crisis on the economy of Bulgaria. There were reported weak signs of recovery in 2013 as a slight revenue growth was reported. As a result from the catastrophic events during 2014, at the end of 2014, a negative result from an insurance activity was reported and a minimum total profit for the sector; 10 companies reported a negative financial result for the year. For the first half of 2015, a weak recovery was reported.

The main factors hindering the development of general insurance companies remained the uncertain recovery of the Bulgarian economy from the crisis, the weak economic activity, reduced domestic consumption and uncertainty in regard to future income of the households. The sector maintained a high growth potential, with view of the low levels of insurance density and penetration.

At the time of preparing the report a new Insurance Code (that has being prepared for a long time) was adopted at first reading. One of the most important changes is related to the introduction of the EU Directive "Solvency II", that brings in new guidelines – of the capital requirements, for determining the reserves, for determining the solvency margin, for the

financial stability of the insurance and reinsurance companies.

A requirement is introduced - solvency to be calculated in such a way to ensure that the risk of insolvency shall be reduced to 0.5% within a year.

Many other changes are proposed as a result from the implementation of the requirements of the European legislation. Improvements of the entire regulatory framework with the aim at providing a better protection of the interests of the users of insurance services are forthcoming.

During the period of updating, there were not changes in the shareholding structure of ZAD „Armeets” AD, nor in its structure, as a major shareholder remains „CCB Group” EAD.

In 2014, the Gross premium income (GPI) of ZAD "Armeets" AD increased by 11.0% with growth of 0.8% for the adjusted sector<sup>1</sup>, that led to an increase in the market share by 1.3 p.p. to 13.7% p.p. The increase is mainly due to the increase in the registered revenue on "Casco" (12.7%, 11,928 thousand leva yoy) and "Third Motor Party Liability" (7.2%, 4 066 thousand leva yoy). As a result of the reported increase in GPI on these insurances, the market shares of the insurance company for them recorded an increase of 1.7 p.p. and 1.3 p.p. reaching 24.5% and 10.9%. The Company also performs an active reinsurance activity, as the registered income for 2014 is 2142 thousand leva, with 100.9% (1 076 thousand leva) higher than the previous year.

For the first half of 2015, ZAD "Armeets" AD increased its market share to 13.8% (13.2% as of 06.2014) due to an increase in GPI by 11.0% yoy, strongly outpacing the sector (6.0%). An improvement was observed with both motor insurances, GPI increased by 10.9% with "Motor Casco", but the market share decreased by 0.4 p.p. to 23.8%; with "Third Motor Party Liability", after an increase of 7.4% in the realized GPI, the market share reported an increase to 10.0% (9.6% to 06.2014). Regarding the active reinsurance during this period, the amount of written premiums was 12.2% higher compared to the same period of the previous year.

The main insurance for the company during the period of updating remains "Motor Casco", its share in the 2014 portfolio continued to increase and reached 53.7% (52.9% for 2013.). A slight decrease was observed with another car insurance ("Third Party Motor Liability"), which is next by importance for the

<sup>1</sup> The sector data are adjusted with data of the rated company.

	<b>CLAIMS PAYING ABILITY RATING</b> <b>ZAD „Armeets” AD</b> <b>iBBB- (outlook: stable)</b> <b>November 2015</b>
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company: in 2014 its share (30.6%) was lower by 1.0 p.p. than the previous year. Both property insurances had an unchanged share during the year (6.6% at end of 2013 and 2014).

During the first half of 2015, the structure of the portfolio did not report significant changes and it was characterized with a slight decrease in the shares of "Autocasco" and "Third Motor Party Liability" and an insignificant increase of the property insurance. In comparative aspect during the analyzed period, there were not significant changes. ZAD "Armeets" AD maintained a significantly lower share of "Third Motor Party Liability" and property insurance, and higher of "Autocasco" compared to the average for the competitive group.

During 2014, there was a growth in both Gross and Net claims ratio, as their values reached 71.7% and 59.5%. During the first six months of 2015, the values of gross and net claims ratio decreased on an annual basis, and as of the end of June 2015 amounted to 50.6% and 51.5%. The realized levels at the end of first half were more favorable than the average for other leading companies in the sector.

The Net acquisition ratio decreased in 2014, and reported a drop for the first six months of 2015, as its value for both periods was lower than the average for the competitive group.

The level of the expense ratio of ZAD "Armeets" AD reported a significant drop in 2014 (compared to a growth in the previous two years) and an increase for the first half of 2015. Following those amendments since 2011 up to now the indicator has had less favorable values compared to the average for the competitive group.

During 2014, ZAD "Armeets" AD generated an insurance loss for third consecutive year, as the combined expense ratio reached its highest value at the end of 2014 within the last five years. The trend the company to realize an insurance loss kept in the first half of 2015, but the value of the indicator improved and was over 100.0%. At the end of 2014, the company's position in a comparative perspective was unfavorable compared to the average for its direct competitors. At the end of June 2015, the value reported by the company was slightly better than the average for the competitive group.

The reinsurance programme of ZAD "Armeets" AD is designed to ensure stability of the portfolio of the company and meet the customer needs in unfavourable events. In 2014, the level of retention did not change in comparison with the previous year. For

the first half of 2015, a slight increase of 2.9 p.p. was observed in comparison with the middle of 2014, as the level of the indicator reached 92.4%.

In 2014, the size of the investment portfolio of the company increased in comparison with the end of the previous year by 17.3%, while the size of the investment portfolio for the adjusted sector decreased by 1.9%. The increase is mainly due to the increased investments in subsidiaries, as a result of the acquisition of Russian insurance company "Itil" and increased bank deposits. A lower absolute growth was observed with other positions – the shares and participations in IF, land and buildings, other debt securities and government securities. These changes did not lead to significant changes in the structure of the investment portfolio, and the shares and participations in IF continued to have the largest share at the end of 2014, followed by bank deposits. The share of the quick liquid assets (government securities and bank deposits) at the end of 2014 was approximately at the same level as in 2013, remaining below the average for other companies in the sector, while the part of the shares continued to be much higher than the average for the adjusted sector.

In the first half of 2015, the investment assets of ZAD "Armeets" AD decreased by 2.2% compared to the end of 2014. During this period, the adjusted sector reported an insignificant increase (0.4%). The share of highly liquid assets remained unchanged and continued to be lower than the average for the adjusted sector, while the part of the shares was still much higher than the average for the adjusted sector. During this period, no significant changes were observed in the structure of the investment portfolio of the rated entity.

The income from investing activities in 2014 amounted to 6 268 thousand leva, and was higher by 41.5% than the realized in 2013. In 2014, the trend - the income from revaluation of the investment assets to have the largest share in the structure of investment income, was maintained. The achieved profitability<sup>2</sup> of the investment portfolio of ZAD "Armeets" (3.84%) in 2014 was close to the average for other companies in the sector (3.78%).

During the first half of 2015, as a result of the realized negative revaluations of investment assets, the company reported a loss from investment activities. The reported profitability by TTM as of 30.06.2015 (2.13%) continues to be close to the average for the sector (2.20%).

<sup>2</sup> Using TTM Method

At the end of 2014, the assets serving to cover the technical reserves of the company increased by 16.7% yoy. The receivables increased significantly from insured persons and intermediaries, bank deposits and government securities. The increase in the bank deposits and government securities led to an increase in the share of quick liquid assets (bank deposits, government securities, cash in hand and current accounts) to 28.1% (25.5% at end of 2013.).

At the end of the first half of 2015, the size of the portfolio covering the technical reserves decreased by 3.8% compared to the end of 2014., as the relative share of highly liquid assets rose to 28.6%.

During the update period, the investment portfolio of ZAD "Armeets" continued to be structured with a relatively high risk.

In 2014, ZAD "Armeets" AD reported an increase in Net earned income - 19.5% (3.2% for other leading companies), while the sector realized a decline of 1.2%. The company generated a loss of EUR 10 879 thousand leva. The continuous decline in immediate liquidity ratio placed the company more unfavorably compared to the average for the competitive group and the adjusted sector. The return on equity decreased significantly and at the end of the year had negative values, remaining significantly below the average for other companies in the sector.

In the first half of 2015, the following was observed:

- outpacing growth in the net earned income (14.3%) compared with the average change for the adjusted sector (0.7%) and for the competitive group (1.2%);

- loss from insurance activity in the amount of 494 thousand leva that is significantly less negative than in the reported for the same period of the previous year (8 523 thousand);

- negative result from investment activity, while for the same period of 2014 a profit was reported;

- Net financial result was negative, in the amount of 2 456 thousand leva, because of which the return on equity was also negative. In comparative aspect, the reported values of the return were also negative but less negative than the reported one from the company.

In 2014, the actual solvency of the company decreased, as a result the coverage ratio also decreased and amounted to 1.23 at the end of the year. In the first half of 2015, an additional decline was reported to 1.07.

The leverage levels increased during the update period, maintaining considerably higher levels compared to the average for other leading companies.

The liquidity ratios of the technical reserves and reserve for upcoming payments continued to decrease in 2014, also during the first six months of 2015. Their values were lower than the average for the comparative group and sector.

*When preparing the credit rating, BCRA has taken into consideration the positive changes occurred in the indicators of ZAD "Armeets" AD during the period of updating – the main is the increased Gross Premium Income, the adverse factors for the financial condition of the company; the trend to generate a loss from insurance activity is becoming consolidated; the continuous decrease in the levels of the liquidity indicators; the growth in claims (gross and net) in 2014; the loss from insurance and investment activity for the first half of 2015; the risk profile of the investment portfolio.*

<b>Main Financial Indicators (thousand leva)</b>	<b>6.2015</b>	<b>6.2014</b>	<b>2014</b>	<b>2013</b>	<b>2012</b>	<b>2011</b>
Gross Premium Income	105 871	95 384	196 896	177 412	170 891	161 733
<i>Change rate year on year (%)</i>	11.0%	19.4%	11.0%	3.8%	5.7%	4.2%
Net Earned Income	95 960	83 927	175 698	147 066	146 338	138 622
<i>Change rate year on year (%)</i>	14.3%	13.4%	19.5%	0.5%	5.6%	10.0%
Result from Insurance Activity	-494	-8 523	-15 747	-5 395	-10 237	577
<i>Change rate year on year (%)</i>	-94.2%	435.4%	191.9%	-47.3%	-1874.2%	-6.0%
Net Profit	-2 456	-8 048	-10 879	443	205	899
<i>Change rate year on year (%)</i>	-69.5%	7421.5%	-2555.8%	116.1%	-77.2%	-86.6%
Gross Claims Ratio	50.6%	51.3%	71.7%	51.3%	56.1%	51.37%
Net Claims Ratio	51.5%	57.4%	59.5%	53.2%	58.8%	53.38%
Combined Expense Ratio	100.5%	110.2%	109.0%	103.7%	107.0%	99.58%
Operating Leverage	203%	161%	351%	242%	250%	335%
Financial Leverage	459%	368%	438%	298%	270%	323%
Liquidity Ratio	2.1%	2.2%	2.1%	2.5%	2.9%	3.43%
Return on Equity	-10.7%	-12.8%	-19.8%	0.8%	0.5%	2.1%