

„Bulgarian American Credit Bank” AD

July 2017

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

- Upgrades the long-term financial strength rating from B to **B+**, retains the **stable** outlook and the national-scale short-term rating **B**;
- Upgrades the national-scale long-term rating from B+ (BG) to **BB- (BG)**, retains **stable** outlook, retains the national-scale short-term rating **B (BG)**.

BCRA uses the methodology, which is officially adopted for assigning bank financial strength ratings http://www.bcra-bg.com/files/file_377.pdf.

The report has been prepared and the rating – assigned based on information, provided by the rated bank, BNB, NSI, BCRA`s database, consultants and other sources of public information.

With full EU membership in 2007, Bulgarian

governments lose their main incentive to pursue a reform policy. The country continues to be in a monitoring regime, with no significant progress in any of Bulgaria's problematic areas in the last years, which are mainly about fighting corruption and improving the functioning of judiciary.

The political situation at the time of writing the report can be defined as relatively stable.

During 2016, the growth rate of economy slows down slightly (3.4%), but remains close to the reported a year earlier (3.6% in 2015). Among the groups with the largest contribution remain the exports, while household consumption and imports of goods and services slow down to half of the growth rates a year earlier.

During 2016, there is some reduction in Direct investment flows (up to 1.5% of GDP), as the investments in share instruments amount to barely 37.3% of the reported a year ago, and the debt instruments continue to report a low-tide which triples compared to a year earlier.

The positive changes in the labor market observed after 2013 remain the same. With the downtrend in unemployment rate over the last 3 years, at the end of 2016, the official registered unemployment rate by the Employment Agency reaches 8.0%.

Despite some slowdown in the fall of prices in early 2016, in the second half and the first two months of 2017, the deflation remains at levels of about 1.1-1.4% on average per year as measured by the HICP.

The slight improvement observed in the state budget of the country in 2015 remains the same in 2016.

The state budget balance for 2016 is negative – a deficit of 1.2% of GDP at the end of the year is reported, which is lower than envisaged in the Law on the State Budget of the Republic of Bulgaria (1.9% of GDP).

The state debt level continues to be a positive factor in Bulgaria in comparison with the EU indicators. The average leverage in the EU is about 83.3% of GDP as of September 2016, and in the Eurozone it comes to 90.1% of GDP.

The banking sector can be defined as stable – with high levels of liquidity and capital adequacy. The deposit base in the sector continues to grow and lending shows slowdown in the negative trends. During 2016, the conducted Asset Quality Review (AQR) and Stress Tests (ST) confirm the stability in the system, although some adjustments are required for individual participants.

During the period of updating, changes have been made in the shareholding capital of „Bulgarian American Credit Bank“ (BACB), while in the shareholding structure insignificant changes are observed:

Shareholder	% of the capital	
	22.05.2017	2015
CSIF	61.43%	61.43%
LTBI Holdings LLC	35.04%	35.04%
Other shareholders	3.53%	3.53%
Total	100.00%	100.00%

During the period of updating, there haven't been any changes in the bank participations.

Bulgarian American Credit Bank has a two-tier management system. During the analyzed period, there haven't been any changes in the composition of the Supervisory Board, while in the composition of the Management Board Mr. Alexander Dimitrov joined. The General Meeting of Shareholders took a decision on 05.06.2017 to add a new post „Chief Executive

Director“. Together with this new change, the members and posts of the Management Board are the following:

- Vasil Simov – Chair of the Management Board and Executive Director;
- Ilian Georgiev – Member of the Management Board and Chief Executive Director;
- Loreta Grigorova – Member of the Management Board and Executive Director;
- Alexander Dimitrov – Member of the Management Board and Executive Director;
- Silvia Kirilova – Member of the Management Board.

The changes in the bank's organizational structure result from the entry of a new member and executive director in the Management Board.

During 2016, the overtaking increase of risk-weighted assets compared to the capital base leads to a decrease in capital adequacy (total adequacy and the adequacy of Tier 1 capital) by 2.27 p. p., while in the first quarter of 2017, the trend is reversed and capital adequacy rises by 0.47 p. p. In a comparative aspect, Bank's capital adequacy is lower than the average for the banking system and for the second group of banks but it continues to exceed considerably the regulatory requirements.

During 2016, the upward trend of the previous year's growth in the value of non-adjusted leverage of the bank. Adjusted leverage shows an opposite trend (decline). In the first quarter of 2017, the levels of both indicators are rising. At the end of 2016 and March 2017, the realized by the bank levels of non-adjusted leverage continue to be lower than the average indicators for the banking system, second group of banks and the reference group of banks¹. Regarding the adjusted leverage levels in the mentioned periods the started bank's trend in 2014 to report higher levels than the average for the banking system and the first group of banks, and lower than the banks in the reference group remains.

In 2016, as a result of a decrease in the deteriorated exposures and a slight increase in the capital base, the ratio net classified exposures to capital base reports a decline by 11.41 p.p. annually. In the first quarter of 2017, there is a faster increase in the capital base compared to the deteriorated exposures,

¹ It includes two banks before and after the rated bank – determined by balance sum (Municipal bank, International bank, D Commerce Bank and TBI Bank)

 <p>BCRA CREDIT RATING AGENCY</p>	<p>FINANCIAL STRENGTH RATING Bulgarian American Credit Bank Long-term /short-term rating: B+ / B (stable) National-scale rating: BB- (BG) / B (BG) (stable) July 2017</p>
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as a result of which the value of the indicator decreases by another 2.74 p. p. In a comparative aspect, the bank's reported values at the end of 2016 and March 2017 continue to be considerably higher than the average for the banking system and for the second group of banks.

The return on equity of the bank continues to rise in 2016 (by 3.03 p.p.) and in the first quarter of 2017 (by 2.05 p.p. compared to the same period of the previous year). The Bank's reported values move to the average for the banking system, the second group of banks and the banks from the reference group, but they continue to be at considerably lower levels.

During 2016 and in the first quarter of 2017, the ascending trend in attracted funds by the bank, as the reported growths come to 6.0% (compared to the end of 2015) and 6.3% (compared to the previous year). The structure of the resource base of the rated bank continues to be dominated by the deposits as individuals and households have the largest share in them.

There are no considerable changes in the deposit structure during the period of updating. The Bank continues to account for a larger share of deposits of individuals than for the banking system and second group of banks, while the shares of deposits from non-credit and credit institutions are lower as the Bank continues to be characterized by a very low share of deposits of credit institutions (~ 1.5%).

During the period, there are not considerable changes in currency and debt structure of the deposit base.

During the period of updating, there is relatively high concentration in resource and deposit base of the bank.

During the period of updating, the bank continues to be financed mainly with attracted funds from retail banking segment, as its share in total resource decreases by 5.5 p.p. in 2016, amounting to 74.9% at the end of the period.

For the period of updating, the total amount of assets of BACB reports stable growth of over 5%, after the end of the previous periods the highest growth of 24.8% is reported in 2015. At the end of the next calendar year, 2016, the increase in assets amounts to 5.3% on a yearly basis, and at the end of the last reporting period – March 2017 the growth only for the three months is 5.4% /and 11.1% on a yearly basis, compared to the first quarter of 2015/.

With the largest share in asset structure (during the 5-year period and the update) are the loans (63% – net), as dominant are corporate loans (93.6%). BACB has a

well-diversified credit portfolio by sectors. With regard to debt structure of bank's credit portfolio in prevailing corporate sector the trend for gradual increase in maturity of loans confirms, but with improved group diversification. In the structure of credit portfolio by residual of loans there are slight changes and confirmation of characteristics of a typical corporate portfolio as diversification is very good during the whole period. The most considerable of characteristics of the loans portfolio with a bad quality is that at the end of March 2017 the share of loans granted in the period by 2011 incl., remains high – 88.8% /compared to 96.1% a year earlier/. In a comparative aspect, the share of bank deteriorated loans exceeds considerably the banking system and the second group of banks, but during the period of updating, the trend of gradual improvement is confirmed with rates higher than the average for the system. Thus, the difference also decreases to the average indicators for the banking system, nevertheless there is still a big lag. At the end of the period, the share of the 15th largest credit exposures decreases slightly, as positive fact is the more sensitive decline of the share of non-performing exposures in the group. The depreciation coverage of gross loans continues to be higher than the average for the system /average by about 6%, though its gradual decrease with regard to faster growth in loans/. The coverage of non-performing loans from depreciation increases but remains lower on average by about 10 p.p. compared to the average for the banking system.

The investments register considerable growth which lead to enhancement of their share in asset structure. For the last period of updating, the largest growth is reported by investment properties as this is due to reclassification of 27 million leva from assets for resale /acquired from realization of securities on non-performed loans in the period before 2015/ to investment properties due to expiration of a two-year period after their acquisition. Since 2014, the major share of investments is taken by Debt instruments (56%), as they are composed entirely by investments in state securities. The capital instruments and investments in associate, subsidiary and joint enterprises take an inconsiderable share during the period of updating as well.

At the end of 2016, funds in cash and current account in the BNB decrease considerably, as their share in the asset structure decrease to below 10%. The process of considerable growth of the cash (reported

by the banking system in 2015), brought to an increase of their share to over 20% of the banks' assets and the introduced by the BNB negative interest rates for the excess reserves held by central bank. The rated bank is in considerably more narrow and acceptable boundaries. During 2016, considerably lower than the average ratios for the system of these funds in the bank's assets are maintained.

In the bank's asset structure the receivables from credit institutions continue to decrease, which result in a decrease in their share in assets, as in a comparative aspect it is lower than the average for the banking system.

During 2016, the indicator for return on interest-bearing assets of the bank reports a decline of 0.81 p.p. to 4.34%. The gained value is lower than the average for the banking system (4.51%), but higher than the second group of banks (4.24%), whose values also decrease (by 0.43 p.p. and 0.70 p. p.). The downward trend for the bank (by 0.08 p. p.) and the sector (by 0.15 p. p.) and for the the second group of banks (0.11 p. p.) continue in the first quarter of 2017. In a comparative aspect, the level of the bank indicator (4.27%) continues to be lower than the sector (4.36%) and higher than the second group of banks (4.13%).

With regard to the price of interest payables of the bank, sector and second group of banks, during the period of updating the downward trend in the indicator levels remains. The indicator level of the bank continues to be considerably higher than the average for the banking system and the second group of banks. The reported indicator value at the end of the period indicates a possibility for additional optimization in the price of interest payables.

During the period of updating, the increase in gross interest spread slows down considerably, as its value continues to be lower than the average for the sector and the second group of banks. Similar dynamics is observed in net interest margin.

In 2016, the started trend in 2015 the bank to report a positive financial result is confirmed, as also a

significant increase is reported in its value (616.3% growth year on year), reaching BGN 5 831 thousand at the end of the year. The growth of assets is considerably lower (11.8%), which reflects to a considerable increase in the value of return on assets (by 0.47 p. p.), from 0.09% at the end of 2015 it reaches 0.56% at the end of 2016. In the first quarter of 2017, a positive trend remains, as the value of the indicator increases by 0.16 p. p. compared to the end of the previous year and reach 0.72%. In a comparative aspect, the return on assets of BACB is lower than the banking system and the banks in the second group, as during the period of updating the smallest differences are reported compared to the previous years (0.86 p. p. and 0.47 p. p. 2016, and 0.66% and 0.35% for March 2017).

In a comparative aspect, the return on assets of BACB is lower than the banking system and the second group of banks as during the period of updating the smallest differences are reported compared to the previous years (0.86 p.p. and 0.47 p.p. for 2016, and 0.66% and 0.35% for March 2017).

During the period of updating, the liquidity ratio is characterized by volatility (a decrease in 2016 and a partial recovery in the first quarter of 2017), as in a comparative aspect its value is significantly lower than the average for the banking system and second group of banks.

The BNB recommends that the ratio of liquid assets within the meaning of Ordinance No. 11 to attracted funds from individuals and households and institutions other than credit ones should be at least 20%. BACB continues to position itself above that level.

During the period of updating, BACB keeps its positions:

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

**FINANCIAL STRENGTH RATING****Bulgarian American Credit Bank**Long-term /short-term ratingинг: **B+ / B** (stable)National-scale rating: **BB-** (BG) / **B** (BG) (stable)**July 2017****95, Evlogi Georgiev Blvd., fl. 1**
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*The rating of **Bulgarian American Credit Bank** would be positively affected by a sustainable improvement in portfolio quality, an increase in generated profit and income indicators keeping stable capital adequacy and liquidity.*

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

Main Indicators

<i>(thousand BGN)</i>	3.2017	2016	2015	2014	2013	2012
Balance Sum	1 128 841	1 071 101	1 017 537	815 298	777 729	827 222
Equity	168 323	166 471	161 944	155 628	165 656	177 059
Total Interest Income	9 486	38 098	37 117	32 790	33 778	35 119
Net Financial Result	2 350	5 831	814	-9 167	-15 996	-19 807
Net Interest Margin	3.07%	3.05%	2.60%	1.78%	0.84%	0.28%
Return on assets	0.72%	0.56%	0.09%	-1.19%	-2.00%	-2.45%