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March 2020

„DZI – General Insurance" EAD

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CLAIMS PAYING ABILITY RATING *	Review	Review
Date of Rating Committee:	08.03.2019	10.03.2020
Date of Publication:	12.03.2019	12.03.2020
Long-term Rating:	BBB+	BBB+
Outlook:	Stable	Positive
Long-term National-scale Rating:	AA+ (BG)	AA+ (BG)
Outlook:	Stable	Stable

** To become familiar with the full rating history, please, see the chart at the bottom of the document*

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 the Council. The credit ratings, assigned by BCRA, are recognized throughout the EU and are entirely equal with other ratings, recognized by the European Securities and Markets Authority (ESMA), without any territorial or other restrictions.

BCRA assigns the following ratings to **DZI – General Insurance EAD**:

- Long-term claims-paying ability rating: **BBB+** and changes the outlook from "stable" to "**positive**"
- Long-term national-scale rating: **AA+ (BG)** and outlook **„stable"**.

The officially adopted methodology of BCRA for assignment of the ability of insurance companies to pay claims is used: *https://www.bcra-bg.com/files/cpaic_methodology_2018_en.pdf*

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

Operating Environment

Sovereign Risk

The economic development of the country in the context of the expected accession of the Bulgarian Lev to the ERM II exchange rate mechanism has been thoroughly analysed by BACR - Credit Rating Agency and thus was assigned the unsolicited sovereign rating of the Republic of Bulgaria. The growth of GDP and GVA by components as well as the dynamics of the external sector indicators were studied. The level and structure of government debt are positively assessed, taking into account the parameters of new debt issued in 2019. The banking sector is assessed as stable.

The Rationale related to the assigned rating of the Republic of Bulgaria can be viewed on the BCRA's official website:

https://www.bcra-bg.com/files/rating_republic_of_bulgaria_oct_2019_en.pdf

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General Insurance Market in Bulgaria

In the period of the update, the Bulgarian insurance market maintains the features of:

- **An upward trend in the income** of written gross premiums by 19.4 % in 2018 (the same trend is in 2019), resulting from the growing price of motor insurance (above 30% for the period November 2017 – July 2019 according to NSI) and the penetration in the foreign markets of some of the Bulgarian insurers benefiting from the principle for free movement of goods and services in the EU;
- **High development potential**, as a result of the relatively low levels of insurance density and penetration, improved in the period from the increase of generated gross premium income;
- **A high degree of market concentration** – the seven biggest companies are retaining a share of above 70% of the gross premium income in the sector (70.9% at the end of September 2019, 70.7% at the end of 2018 and 70.1% at the end of 2017);
- **Leading share of the motor insurance** in the structure of the aggregated insurance portfolio – at about and over 70.0%, affected to a high degree from the compulsory nature of the "Motor Third-Party Liability" insurance.

In the period under review, the **regulatory framework** continues being affected by the solvency requirements for insurers, reinsurers and groups of insurers and reinsurers as well as reporting requirements, evaluation of assets and liabilities and the technical reserves in compliance with the "**Solvency II**" Directive (Directive 2009/138 of the EP and the EU). The implementation of **IFRS 9** "Financial Instruments" as from 01.01.2018, affects further the accounts and financial reports.

The general factors hindering the development of the general insurance market include slow economic growth, relatively low economic activity and uncertainties about future households' income.

„DZI – General Insurance“ EAD

In the period under review, no changes occurred in the **share capital** of DZI – General Insurance EAD, amounting at BGN 66 586 779, distributed in 9 512 397 shares with a nominal value of BGN 7. The sole owner of the capital is DZI – Life Insurance EAD and ultimate shareholder is KBC Group NV.

In the period, there were no changes in the **management** and the compositions of the Management and Supervisory Board.

No significant **changes** are observed in the activity and the systems for management and risk profile of the insurance portfolio. The insurer has implemented and applies all management principles of the Directive 2009/138 of the EP and EC (Solvency II) and in the period under review improves the level of the solvency capital requirement. The management declares its intention to keep the company' position in the top ranking according to market share.

A further increase in the volume of gross premium income is planned for 2020 and 2021 with a set high amount of net financial result.

In 2018, the GPI increases for a fifth consecutive year. The reported growth amounts at 24.3% (11.5% for 2017) due to the increased prices of the Motor Third Party Liability insurance. The increase exceeds the reported by the adjusted sector of 18.8%, which results in the growth of company market share to 11.2% at the end of 2018. Thus, the company holds the second position in terms of volume of GPI, after Lev Ins (13.5% market share) and equals to the position of Bulstrad VIG (11.3%). In the nine months of 2019, the trend of the aforementioned dynamics is maintained, with a growth of 12.8% on an annual basis, while the company loses slightly part of its market share (declining to 10.5%). This results from the slowdown of the business of Auto Casco and Motor Third Party Liability insurance.

The active reinsurance preserves a negligible share in GPI having minimal volumes, mainly under fire and natural disaster insurance. In terms of the structure of the insurance portfolio, there are no significant changes. Dominating is the auto Casco insurance (over 40% share), followed by the Motor Third Party Liability insurance (over 30% during the review period) and fire and natural disasters. Comparatively, the company continues to report higher shares for Casco and property insurance, and a lower share of Motor Third Party Liability insurance than the average levels of the competitive group of insurers[1].

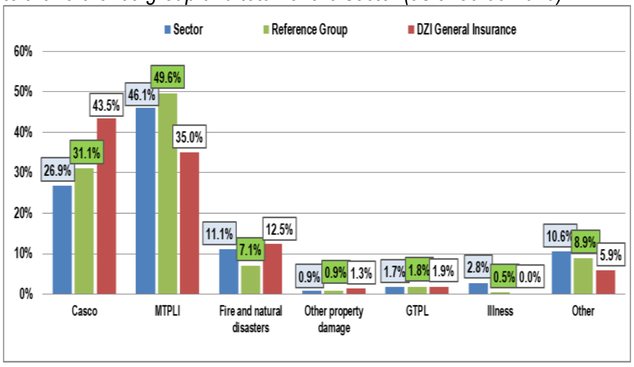
The company reports an increase of 13.9% in GPI of the **Auto Casco** insurance and by 5.3% for the nine months of 2019 thus maintaining a market share of the product at about 17%.

Second in portfolio by GPI remains the **Motor Third Party Liability insurance**. In 2018, it registered an increase of 57.7% and for the nine months of 2019, a growth of 20.6% is reported.

[1] „IC Lev Ins" AD; „IC Euroins" AD; „IC Bulstrad VIG" AD; „IC Armeec" AD; „IC Allianc Bulgaria" AD; „IC Bul Ins" AD

Third in the portfolio by GPI is the **Fire and natural disasters** insurance. In 2018, the insurance recorded a growth of 7.3%, while for the nine months of 2019, the growth was 17.6%.

Insurance portfolio structure of DZI – General Insurance EAD compared to the reference group and total for the sector (as of 30.09.2019)



In 2018, the insurer reported substantial improvement of the gross and net claims, decreasing to 46.3% (71.5% for 2017) and 49.4% of the net (55.0% for 2017) respectively due to the decline in the values of incurred claims (gross and net) and the significant increase in GPI. The volume of the net claims is close to the average of the other companies in the group.

Net Claims	*09.2019*	*2018*	*2017*	*2016*
DZI General Insurance	**48.3%**	**49.4%**	**55.3%**	**54.0%**
"IC Lev Ins" AD	59.4%	43.0%	39.5%	45.6%
"IC Euroins" AD	43.5%	50.6%	46.8%	49.8%
"IC Bulstrad VIG"	56.0%	51.2%	43.2%	55.9%
„IC Armeec" AD	45.6%	43.1%	55.2%	50.3%
"IC Allianz Bulgaria" AD	52.5%	46.8%	56.1%	57.3%
" IC "Bul Ins" " AD	60.3%	55.7%	58.1%	43.9%
Average of the Reference Group:	**53.1%**	**47.7%**	**49.2%**	**51.2%**

In the period under review, the positive downward trend of the **acquisition ratio** remains, and in 2018 the ratio registered the lowest value for the past five years. A specific feature of the review period is the reported increase in the value of acquisition costs for 2018 (by 4.7%) while the net earned income grew highly (20.0%). For the nine months of 2019, the value of the indicator (26.9%) maintains a positive downward trend (compared to 28.5% in the corresponding period of 2018). In a comparative aspect, the levels of the indicator of DZI – General Insurance are slightly higher than the average for the reference group and almost similar to those of the main competitors.

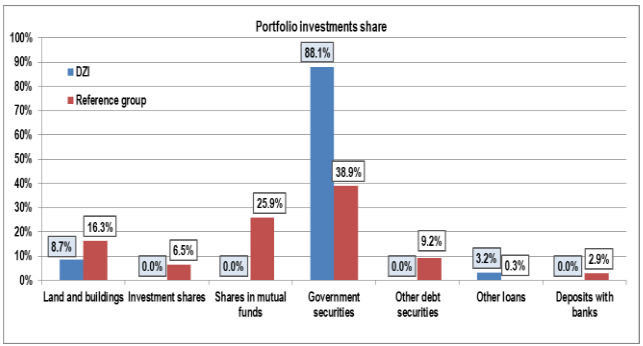
The ***cost ratio*** increased by 6.6 pp, reaching a rate of 20.7% in 2018, due to a change in the methodology for allocation of costs and the higher increase of the administrative and other technical costs. For the nine months of 2019, while applying the same methodology, the value of the ratio declined to 13.9% (14.6% for the corresponding period of 2018). The result is related to the increase in expenses (by 16.7%), lagging behind the increase in net earned income (22.2%). The level is below the average compared to the levels reported by the reference group of insurers (23.7%) and is the lowest for the group.

In 2018 and the nine months of 2019, the rated company maintains a downward trend of the ***combined cost ratio,*** a trend that has been already started in 2017 and with the registered rates of 95.2% (2018) and 89.1% (the nine months of 2019) it positions the insurer below the average for the group (97.2% and 93.3% respectively).

In the review period, the company maintains a high and relatively unchanged ***self-retention level***, the highest compared to the competitors in the reference group and substantially above its average levels. The reinsurance policy complies with that of the majority shareholder. The company cooperates with reinsurers having an excellent reputation and assigned with high credit ratings. The amendments in the reinsurance programmes for the period 2019-2020 are mainly related to the increase of the coverages.

The share of the reinsurers in the technical reserves of the company remains low (the lowest compared to the companies in the competitive group). At the end of 2018, the company reported a decline by 5 pp, down to 10.5%, while as of September 2019 there is a twofold decrease on an annual basis, with a registered value of 5.6%.

In the period under review, the company retains its policy for maintaining high-liquidity and secured **investment portfolio** having high profitability. In 2018, the investment portfolio reduced by 13.1% determined by the remit of a significant part of the deposit resource (being transferred to cash and acquisition of non-investment property). The defining element in the investment portfolio are the government securities (mainly Bulgarian), which are gradually holding an increasing share in the portfolio structure, reaching 89.1% at the end of 2018 and an even higher rate of 92.9% at the end of September 2019.



The restructuring of the portfolio results in a slight increase of the **profitability**, however, the company remains positioned below the average compared to the adjusted sector at the end of 2018 (3.09%) and at the end of September 2019 (2.83%).

The **net financial result** for 2018 is a profit of BGN 13 969 thousand, a twofold increase compared to the result in the previous year (BGN 6 375 thousand). The profit for 2018 has been left at the disposal of the insurer to achieve a sufficiently high level of Solvency Capital Requirement (SCR) which, according to KBC Group requirements, is at least 175%.

The current profit for the nine months of 2019 amounts at BGN 21 618 thousand, an increase by the significant rate of 43.5%, compared to the corresponding period of the previous year.

In 2018, the ***liquidity ratio*** of technical reserves decreased by 10.6 pp. compared to 2017, but is yet, significantly higher than the average for the adjusted sector and other leading insurers.

The liquidity ratio of the reserve for upcoming claims payments reports a slight decline (1.1 pp) in 2018, changing the upward trend from the previous five years. There was a three-year downward trend of the averages for the adjusted sector and declining volatile values of the average for the reference group at the end of 2018.

At the end of 2018, the ***operating leverage*** (*ratio of net earned income to equity*) of DZI increased to 193%, reducing the difference in the average for the reference group (203%). In the nine months of 2019, no significant changes in the levels of the indicator are observed annually. The Company continues to maintain higher levels of ***Insurance Leverage*** (ratio of technical reserves to equity) compared to the average for the reference group, with the difference increasing to 55 pp in 2018 (39 pp as of the end of 2017), and 25 pp as of 09.2019.

The capital adequacy in the period under review, while applying Directive 2009/138 of the EU Parliament and EC (**Solvency II**) is presented in the table below:

Indicator / Year:	***09.2019***	***2018***	***2017***
Excess of assets over liabilities	161 251	129 242	121 385
Eligible own funds MCR	139 916	129 242	115 333
Eligible own funds SCR	139 916	129 242	115 333
Minimum Capital Requirement (MCR)	79 952	69 883	71 741
Solvency Capital Requirement (SCR)	35 978	31 447	27 765
Coverage of MCR *	**175%**	**185%**	**161%**
Coverage of SCR *	**389%**	**411%**	**415%**

The analysed period is marked by the relatively high levels of coverage for the local insurance market on the ***Solvency Capital Requirement (SCR)***. The company reported a level of 185% for 2018 and 175% at the end of September 2019 (and as of December 2019 according to preliminary FS), while the value of MCR is retained at a steady level of 400% (145% in 2017). The indicator registered better value than the achieved by two of the insurance companies in the reference group but remains around 20 pp below the average (143%).

Again, in the review, the Company's SCR coverage levels remained significantly higher than the average level of competitors. For 2018 and by the end of September 2019, they are already the highest in the group (for 2017, the highest value of the indicator was that of Bulstrad with a rate of 170%).

The company does not report liabilities net of insurance reserves.

The main indicators related to the evaluation of the business in the last five years are shown in the table below:

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Main Financial Indicators

Indicator / Year:	*09.2019*	*09.2018*	*12.2018*	*12.2017*	*12.2016*	*12.2015*
Gross Premium Income (хил.лв.):	**189 156**	**167 694**	**234 534**	**189 054**	**164 618**	**158 067**
Change on an yearly basis	*12.8%*	*21.2%*	*24.1%*	*14.8%*	*4.1%*	*10.6%*
Net Earned Income (хил.лв.):	**176 836**	**144 673**	**196 890**	**164 077**	**147 452**	**141 904**
Change on an yearly basis	*22.2%*	*5.3%*	*20.0%*	*11.3%*	*3.9%*	*9.6%*
Self-retention Level	**95.3%**	**95.7%**	**95.7%**	**94.6%**	**93.9%**	**94.1%**
Net Financial Result (хил.лв.)	**21 618**	**15 069**	**13 969**	**6 375**	**8 585**	**8 823**
Result from Insurance Activity	**19 209**	**11 504**	**9 510**	**3 468**	**-6 930**	**935**
Gross Claims	46.3%	44.9%	46.3%	71.5%	63.0%	49.8%
Net Claims	48.3%	48.9%	49.4%	55.0%	54.0%	50.3%
Costs Ratio	13.9%	14.6%	20.7%	14.1%	12.1%	11.2%
Acquisition Ratio	26.9%	28.5%	25.1%	28.7%	38.6%	37.8%
Combined Ratio	**89.1%**	**92.0%**	**95.2%**	**97.9%**	**104.7%**	**99.3%**
Net Earned Income / Equity (Operating Leverage)	137%	139%	193%	168%	164%	187%
Technical Reserves / Equity (Insurance Leverage)	217%	233%	255%	229%	233%	267%
Debt Net of Insurance Reserves / Equity (Financial Leverage)	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%
Total Equity	**129 259**	**101 940**	**97 382**	**90 132**	**74 358**	**129 259**
Return on Equity	18.0%	5.0%	13.9%	6.6%	10.4%	12.1%
Total Investment Portfolio	**300 559**	**235 225**	**230 432**	**265 074**	**252 951**	**237 415**
Change on an yearly basis	*27.8%*	*-11.8%*	*-13.1%*	*4.8%*	*6.5%*	*5.2%*
Share of High Liquidity Assets in the Investment Portfolio	92.9%	90.6%	90.8%	94.3%	93.9%	93.5%
Investment Portfolio Yield TTM	2.6%	2.4%	2.6%	2.5%	3.2%	3.9%
SCR Coverage	**175.0%**	**177.7%**	**184.9%**	**0.0%**	**0.0%**	**0.0%**
MCR Coverage	**388.9%**	**394.9%**	**411.0%**	**0.0%**	**0.0%**	**0.0%**
Technical Provisions Liquidity Ratio	**115.3%**	**106.8%**	**106.3%**	**116.9%**	**117.5%**	**112.9%**
Liquidity Ratio of the Reserve for Upcoming Claims	197.0%	183.1%	188.0%	189.1%	176.6%	172.7%

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Rating History:

Claims paying ability rating	Initial rating 25.05.2015	Update 19.05.2016	Monitoring 05.07.2016
Long-term rating:	iA	iA+	iA+ (under review)*
Outlook:	stable	stable	-

** The rating is placed "under review" following the requirements of Regulation 1060/2009 due to the procedure for changes in the methodology for assignment of a rating upon expiration of the one month for public consultations and the review of the ratings under the new methodology.*

Claims Paying Ability Rating	Monitoring	Update	Update	Monitoring	Monitoring
Date of Rating Committee:	06.01.2017	21.02.2017	21.02.2018	15.05.2018	20.06.2018
Long-term Rating:	BBB-	BBB-	BBB-	BBB	BBB (under review)*
Outlook:	Negative	Stable	Stable	Stable	-
Long-term National-scale Rating:	AA+ (BG)	AA+(BG)	AA+(BG)	AA+(BG)	AA+ (BG) (under review)*
Outlook:	Stable	Stable	Stable	Stable	-

** The outlook is changed due to a review of the rating placed "under review", given the changes in the used by BCRA "Methodology for the ability of the insurance company to pay claims" (**https://www.bcra-bg.com/files/cpaic_methodology_2018_en.pdf**) and concerns all valid ratings of the insurers and is not related to the business of the rated company.*

The ratings in the charts above are assigned according to the previous versions of "Methodology for an insurance company to pay claims" and are not comparable with ratings assigned according to the new Methodology entered into force on June 21, 2018.

Claims Paying Ability Rating	Monitoring	Update	Update
Date of Rating Committee:	18.12.2018	08.03.2019	10.03.2020
Long-term Rating:	BBB	BBB+	BBB+
Outlook:	Positive*	Stable	Positive
Long-term National-scale Rating:	AA+ (BG)	AA+ (BG)	AA+ (BG)
Outlook:	Positive*	Stable	Stable

** The outlook is changed due to a review of the rating of the insurer given the changes in the used by BCRA "Methodology for the ability of the insurance company to pay claims" entered into force on June 21, 2018.*