BCRA CREDIT RATING AGENCY

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„Eurolease Auto“ EAD

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Credit Rating	Initial Rating	Monitoring	Review	Review
Date of rating Committee:	20.12.2016	16.05.2017	05.02.2018	21.02.2019
Date of Publication:	23.12.2016	18.05.2017	06.02.2018	22.02.2019
Long-term Rating :	BBB-	BBB-	BBB-	BBB-
Outlook :	negative*	stable	stable	stable
Short-term Rating :	A-3	A-3	A-3	A-3
National-scale Long-term Rating:	A (BG)	A (BG)	A (BG)	A (BG)
Outlook:	stable	stable	stable	stable
National-scale Short-term Rating:	A-1 (BG)	A-1 (BG)	A-1 (BG)	A-1 (BG)

** The assigned „negative“ outlook is a result from the applied ceiling of the rating, which is determined by the sovereign rating and outlook (as of the time of reconsideration the rating assigned to the Republic of Bulgaria by BCRA is long-term rating: BBB-(ns), outlook: „negative“, short-term rating: A-3 (ns)*

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

BCRA ***affirms*** the assigned ratings of “Eurolease Auto” EAD as follows:

- Long-term rating: **BBB-** , short-term rating: **A-3;**
- National-scale long-term rating **A (BG)** , National-scale short-term rating: **A-1 (BG) ;**
- and ***maintains*** **the „stable“** outlook;

BCRA uses the officially adopted methodology for assignment of a credit rating of a leasing company ***(https://www.bcra-bg.com/files/Leasing_Company_Methodology_2016_bg.pdf).***

To elaborate the credit report and to assign the credit rating, BCRA uses information from the rated company, the National Statistical Institute, the BNB its own database, consultants and other public information sources.

The political situation in Bulgaria remains stable. The Government of the Republic of Bulgaria is committed to speeding up the process of joining the euro area by officially submitting a letter of intent. In August 2018, the Council of Ministers approved an Action Plan including measures for realizing Bulgaria’s intentions to join the Exchange Rate Mechanism II and the Banking Union by July 2019. A number of legislative changes related to financial sector supervision, insolvency framework, anti-money laundering framework and modernisation of the management of state-owned enterprises are envisaged. The measures will be implemented by national and international institutions in coordination. Progress in all these areas, when achieved, should pave the way for the country to join both the ERM II and the Banking Union.

In the first half of 2018, the **Bulgarian economy** expanded by 3.4% in real terms (3.6% in 2017). 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. On the other hand, net exports had a negative contribution to the GDP growth in the first half of 2018.

At the end of August 2018, the 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 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

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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 data** marks a favourable development with record high indicators for economic activity and employment rates. 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 wage growth in some economic activities. Gross base remuneration was raised by 11% to BGN 510 per month from the beginning of 2018. From the beginning of 2019, the gross base remuneration is raised to BGN 560 per month, which also has an analogous impact on labour costs.

The price level in Bulgaria continues to raise. Over the first eight months of 2018, inflation followed an upward trend. 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. в

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 in the amount of 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. As a result, the relative share of domestic debt dropped to 25.3% while the share of external debt rose to 74.7% of total government debt. 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

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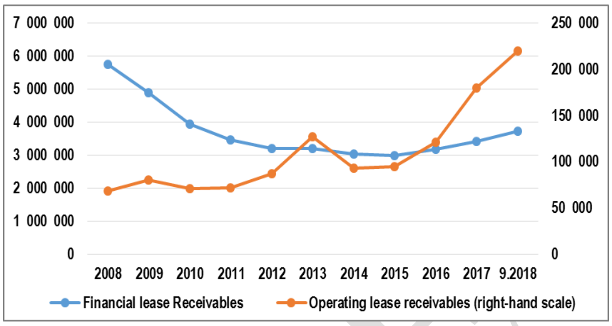
secondary market, fell beneath 1% for the first time in January 2018 and reached 0.81% in August, which is the lowest monthly value of the long-term interest rate for convergence assessment purposes reported so far.

The **banking system** remains stable characterized by a gradual increase in assets base, as well as raise in deposit base from savings from households and non-financial corporations and lending.

By the end of September 2018, gross credit portfolio of the banking system annually increased by 7.6% - 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 (8.5%). 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 in 2019 in order to ensure a smooth transition to the Banking Union[1].

The leasing sector in Bulgaria to a high extent retains its dependency from the development of cars' sales, which account for more than 70% share of the total leasing sales. The registered new vehicles in Bulgaria report a growth of 11.6% in 2018 (14.6% in 2017), which preserves the positive development perspective before the leasing companies.

The portfolio of financial and operating lease receivables of the companies in the sector grew for the second consecutive year with a growth of 8.8% (reaching BGN 3 605 million) after the increase of 7.3% in 2016. As of the end of September 2018, the portfolio reached BGN 3,950 million, further increasing by 9.6% in the first nine months of the year. The observed positive trends came after a long period of delays in investment intentions by the business and the final constraint in household consumption, reflecting to a high extent the influence of the stable macroeconomic indicators and political stability of the country.



The largest share in the lease receivables structure takes those financing the purchase of **passenger cars** - 39.3% at the end of September 2018, with a total increase of 6.6 p.p. compared to the 32.7% at the end of 2016 and a sustained steady upward trend from 2012 to present. The second largest share of leased assets held **heavy-freight and light commercial vehicles** - 31.4% at the end of September 2018, down from 33.5% at the end of 2016. As a third share of the receivables are those for the purchase of **Plant and Equipment** – 19.3% as of the end of September 2018 (compared to 18.3% as of the end of 2017), resulting from the constant downward trend since 2014 (a share of 25.2% as of December 31, 2014). The decrease in the volume and share of the financing of the **purchase of immovable property** (other than plant and equipment) remains permanent and reached a share of 6.6% (BGN 124.9 million) as of September 30, 2018, at 10.3 % (BGN 342.6 million) at the end of 2016.

In the period of analysis, the overall downward trend of the amount of **non-performing receivables** remains, which at the end of September 2018 reached 7.6% of the financial lease receivables (BGN 282.8 million in absolute value), declining significantly compared to the highest registered value of BGN 859.0 million (and a share of 26.8%) at the end of 2013. The reported decrease in 2017 is 12.7% (from 17.8% in 2016 to the significant 44.7% in 2015), followed by a slight increase of 1.4% in the nine months of 2018 (it should be noted that in the last quarter of the year, significant parts of the receivables of the leasing companies are written off / sold.

Non-financial companies remain the main type of **lessee;** however, there is a visible increase in the share of households and Non-profit institutions serving households (including political parties over the last three years (2016-2018). The latter remains at still low levels (13.5% at the end of

[1] In published by ECB press release, dated November 12, 2018, 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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September 2018 and 11.9% at the end of 2017), with high growth prospects and, respectively, the share of corporate clients in leasing portfolios declining slightly (from 91.1% end of 2016 at 86.0% at the end of September 2018).

Since in the last four years, the level of **leasing penetration** has maintained a general trend of growth (from 0.34% in 2012 to 0.49% in 2016), in 2017 the rate decreases by a little to a level of 0.47%, under the influence of the higher GDP growth compared to the increase in the total amount of lease receivables. The value of the indicator remains very low and highlights the high market perspectives in the background of an increase in the purchasing power of the participants.

After significant volatility in the sector, the last three years of activity are characterized by much greater stability, reflecting in minor changes in the structure of assets and liabilities, as well as in improved financial performance in the past year. Against this background, for the same period, there is a slight increase in the number of leasing companies registered in the domestic market, from 42 at the end of 2016 to 47 at the end of September 2018.

The development trends in the sector could be identified as rather favourable while taking into account the lower values of market interest rates and the overall positive signs for country-supported economic developments that are expected to stimulate the economy and leasing activity. An important factor is a growth in household purchases, which continues to show growth compared with the continued positive development of the market for new cars (the most leased asset at the moment), the low levels of purchase of new cars and leased penetration, are expected to push the business forward.

In the reverse, negative direction, the highest level of influence preserves the insufficient household incomes – respectively, the low purchasing power.

„Eurolease Auto“ EAD

In the period of the update, there are no changes in the value and distribution of the **shareholder capital**, which remains at the amount of BGN 20 million, solely owned by “Eurolease Group”, a part of “Eurohold Bulgaria” AD. The management of the company is unchanged as well.

The rated company is specialized in providing of **leasing services**, connected mainly with the purchase of cars and light consumer vehicles (total share of 98.9% in company’s portfolio as of the end of 2017, 61.7% - passenger cars and 37.2% light consumer vehicles. The credits provided for the purchase of vehicles (interest rates and taxes for the management of the financial leasing) have a major share at 60% of the income. The balance is realized through loans provided by the company (21% -23%), commissions from insurance services and other smaller revenues.

The complex **product** offered by Eurolease Auto EAD combines delivery, lending, insurance package and the possibility of buying back the object of leasing. The leasing product is determined by the market demand, which is why the average class of vehicles are mainly offered, namely passenger cars and commercial vans. Without being limited to certain brands or class of vehicles, among vehicles given on lease by the company prevail the brands offered by dealers and agencies of the Auto Union group (part of the Eurohold Group), namely: Dacia, Renault, Nissan, Fiat, Alfa Romeo, Maserati, Mazda, Opel. The company offers vehicles on lease and in partnership with many other vehicle dealers.

Main competitors of “Eurolease Auto” EAD are companies, specialized in leasing activities with new passenger cars: Interlease Auto (at present, UBB Interlease), “DSK Leasing” AD, “Raiffeisen Leasing Bulgaria” EOOD, “Unicredit Leasing” EAD, “Allianz Leasing Bulgaria” AD, “ERB Leasing” EAD, “Porsche Bulgaria” EOOD and other companies.

The market share of “Euolease Auto” AD moves with slight fluctuations, at an average of 1.5% over the last four years (from 2015 to the present), remaining below the direct competitors' level of the reference group[2].

	Eurolease Auto	*ERB Leasing*	*Interlease Auto*	*Porsche Leasing BG*
2017	1.59%	3.31%	2.99%	3.98%
2016	1.48%	4.69%	2.88%	3.35%
2015	1.63%	6.11%	4.23%	3.16%
2014	1.96%	6.01%	3.83%	2.46%
2013	1.65%	6.15%	3.61%	2.19%

The analysed data shows that by the end of 2017, the company retains the downward trend in the

[2] „Eurolease Auto” EAD „ERB Leasing” EAD, „Porsche Leasing BG“ EOOD

revenues from financial leasing as well as in total revenues. In 2017, the decrease was less (7.2%) than the one in 2016 (25.7%). The reported revenues for the nine months of 2018, however, increase compared to the same period of the past year by 6.9% and these changes are the first signs of overcoming the negative trends in past two years. Interest income on loans granted by the company is in a relatively constant annual rate over the last four years.

Net profit in 2017 is at the amount of BGN 747 thousand, or 29.0% higher than the one reported in the past year (BGN 579 thousand in 2016). As at the end of September 2018, the company registered a net current profit of BGN 555,000, which is 6.9% higher than the one for the corresponding period (as of 30.09.2017) and provides additional increase of the equity by another 2.5% for the nine months of the year, after a growth of 3.5% in 2017. As of the date of publication of the present Rationale, the company published preliminary data of the annual net profit for 2018 at the amount of BGN 1,834 thousand).

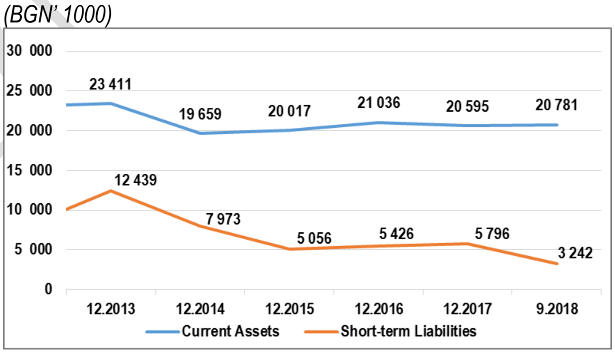
In 2017, the amount of **non-current assets** of the rated company increased by 20.9% after a registered decline in two consecutive years, reaching BGN 66.4 million at the end of the year and after growth of another 3.9% in the next nine months reaching BGN 68.9 million as of September 30, 2018. The Company continues to maintain minimum tangible fixed assets available so that the dynamics of non-current assets is determined entirely by changes in the values of trade and other receivables. In the latter, financial lease receivables (above 74% in the review period), which increased by 19.7% in 2017 and by another 3.3% in the first nine months of 2018, retained the largest share. High growth (more than twice in the period from 01.2017 to 09.2018), a majority share of the receivables being from the majority shareholder “Eurolease Group” and its owner “Eurohold Group” AD, respectively characterize the long-term receivables from related companies). Without any significant change, the remaining part of receivables on the financing provided by the company remain.

Alongside the increase in long-term receivables, in 2017, the company reported a significant increase of 20.3% in **long-term liabilities** (to 58.8 million BGN), followed by another one by 8.1% (up to 63.5 million BGN) for the nine months in 2018. The growth is entirely due to an increase in the amount of resources attracted by banks - by 46.5% on an annual basis as of 31.12.2017 and by 16.2% in the first nine months of 2018, the conditions for the new loans being improved, preserved major lending banks and low level of creditor concentration. All bank loans are collateralized by receivables under leasing contracts and leased assets.

The changes in **current assets** of the company vary in a slight range, and in 2017, their value decreases by 2.1%, while in the next nine months increases by 0.9%. There is a steady upward trend of the free cash and in 2018; there is a significant decrease in the amount of the court and awarded receivables.

In 2017, the value of **current liabilities** increased by 6.8%, while the structure remained relatively stable but by the end of September 2018, it declined significantly (44.1%, largely influenced by a decline in liabilities to related companies), resulting in significant increase in the coverage of current liabilities with such assets, and a general improvement in **the liquidity** of the company.

Coverage of current liabilities from current assets and size dynamics (BGN' 1000)



The increase of company's profits in 2017 and as of the end of September 2018 led to an improvement in the level of **profitability** indicators that already reached values above the reported by competitors in the reference group.

The increased credit exposure of the company has led to a slight increase in total **leverage** and financial leverage, as well as to a decrease of the solvency ratio. The comparative analysis of the leverage shows that the reached values are still lower compared to the average for the competitive group.

In the period under review, the company formed a positive change in most of the **efficiency** indicators (decreasing collection period of receivables and

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inventory turnover) and reported an increase in the repayment period of its liabilities to suppliers. By all indicators, however, competitors reached better levels at the end of the review period.

Eurolease Auto EAD remains the company with the smallest leasing portfolio compared to the competitors in the competitive group. Since the reduction of the company's portfolio in 2016, (a year marked by declines for all leasing companies, after high growth rates for many in 2015), in 2017 and in the nine months of 2018, is reported a stable growth of 19.7% and a slight of 3.3% for the first nine months. The latter corresponds to the changes in the group, where the data for "ERB Leasing" (with a decline in the portfolio of 23.2% in 2017) are more volatile.

The sole owner of the rated company, namely **“Eurolease Group” EAD** reported a net **profit** in 2017 at the amount of BGN 112 thousand compared to a loss of BGN 482 thousand in 2016, given a reported increase of the **total revenues** by the significant rate of 15.7% (after the fall of 2.6% in 2016). In the part of interest income, the change remains negative (a decline of 7.6%, after a decrease of 18.0% in the previous year) and already reflected on the value of net interest income, which decreased by 19.5%. Given the overall negative effect from lower net interest income, the improved earnings from net sales in the other business lines appear to be the company's constructive changeover in the review period.

The **liquidity** indicators are improved, while the total **leverage** (relatively slightly) and the **financial leverage** (considerably) increase.

Conclusion:

*In the review period, **“Eurolease Auto” EAD** reported a growth in the leasing portfolio structure after two consecutive years of decline. Despite the continued decrease in interest income (and their general market movement), the interest spread remains higher than that of competitors. The net financial result increased by 29.0% in 2017 and by 6.9% in the nine months of 2018 (and by 146% as shown in preliminary data for 2018), improve the profitability levels. In the performance indicators, the changes are rather positive, with the main positive feature being the significant decrease in the repayment period of receivables. Despite the general increase in loan liabilities (increasing the leverage ratios), interest coverage remains stable at a moderate improvement in values. As a positive factor, the improvement in liquidity at the end of the review period (September 2018) should also be noted.*

BCRA will continue to monitor the future changes in the financial situation of the company and all the indicators that characterize it by downgrading the rating in case of adverse changes such as a significant shrinking of market share, a decrease in revenues, deterioration of the financial result, an excessive decrease in liquidity or increase of leverage. Accordingly, improvement in the indicators may lead to an increase in the company's national-scale rating (the global rating is limited by the sovereign rating).

Main Financial Data „Eurolease Auto“ EAD

Financial Indicators, BGN Thousand	*09.2018*	*09.2017*	*2017*	*2016*	*2015*	*2014*	*2013*
Total Income	4 334	4 106	5 899	6 274	7 763	7 563	9 862
Total Expenses	3 779	3 587	5 152	5 722	6 527	7 684	9 405
Net Financial Result	**555**	**519**	**747**	**579**	**1 220**	**-111**	**428**
Income from Interests	3 782	3 589	4 818	4 955	6 254	6 458	6 543
Interest Expenses	1 988	1 957	2 605	2 762	3 808	4 091	4 308
Net Interest Income	**1 794**	**1 632**	**2 213**	**2 193**	**2 446**	**2 367**	**2 235**
Assets	89 726	-	86 987	75 952	80 414	87 368	88 872
Net investments in financial lease	56 626	-	57 439	48 964	50 248	61 111	55 040
Cash	2 319	-	1 700	988	5 565	1 134	656
Receivables on loans to related parties and other receivables	30 781	-	27 848	26 000	24 601	25 123	33 176
Equity	22 937	-	22 382	21 635	21 056	19 836	19 947
Liabilities on Bank Loans and Bond Obligations	63 547	-	58 807	48 887	54 296	59 548	56 486
Payables to Suppliers and Others	3 242	-	5 798	5 430	5 062	7 984	12 439