

ZK „Lev Ins” AD

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CLAIMS PAYING ABILITY RATING	Initial Rating 6.2006	Non-solicited Rating 11.2007	Non-solicited Rating 11.2008	Update 7.2009
Long-term Rating:	BB+	iBBB-(ns)	iBBB(ns)	iA-
Outlook:		<i>positive</i>	<i>positive</i>	<i>stable</i>
	Update 20.07.2010	Monitoring 07.12.2010	Monitoring 25.05.2011	Update 25.10.2011
Long-term Rating:	iA-	iA-	iBBB+	iBBB+
Outlook:	<i>stable</i>	<i>negative</i>	<i>negative</i>	<i>developing</i>
	Update 29.11.2012	Update 04.11.2013	Update 13.12.2014	Update 10.12.2015
Long-term Rating:	iBBB+	iBBB+	iBBB+	iBBB
Outlook:	<i>positive</i>	<i>stable</i>	<i>stable</i>	<i>negative</i>

BCRA – Credit Rating Agency (BCRA) is the third qualified rating agency in the EU, registered under Regulation (EC) 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 limitations.

BCRA assigns the long-term claims paying ability rating to ZK „Lev Ins” AD: *iBBB* (outlook: *negative*). BCRA uses the officially adopted methodology for assigning a rating of the ability of insurance companies to pay claims¹.

In producing the credit rating report and in deciding the credit rating, BCRA has used information from the insurance company assessed, the Financial Supervision Commission, the National Statistical Institute, BCRA's own database, information from consultants, etc.

The political environment as of the time of preparation of the report could be determined as relatively stable. In October 2015, the held local elections did not lead to any significant changes in the political layers.

For the first quarter of 2015, the country registered a considerably high real GDP growth – 2.2% compared to the same quarter of the previous year (0.2% for Q1 2014), and for the following 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%).

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

A slight improvement was observed in the labour market conditions, represented in the decline 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, the level of the reported deflation fell gradually.

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

¹ http://www.bcra-bg.com/files/file_202.pdf

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electricity prices for the business sector shall lead to the increase of the price level as well.

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

The economy of Bulgaria was characterized by a low economic activity for the previous year (2014) and a weak recovery for the first half of 2015 as the growth levels are foreseen to retain during the remainder of the year.

The 2014 events in the banking system led to the emergence of a potential risk for the banking institutions of deepening the banking crisis and involving a larger number of participants in the sector. Despite the increased risk in the financial system caused by the dropping of one of the main players and a risk of dropping of another, the banks in Bulgaria maintained their stability. For the first half of 2015, the banking environment could be determined as stable, as evidenced by the high capital adequacy and liquidity of assets and growth in the attracted deposits.

During the period of updating, the general insurance sector in Bulgaria operated in an adverse economic environment resulting from the effects of the global crisis on the economy of Bulgaria. However, in 2013 there were signs of recovery: the revenues increased slightly. At the end of 2014, a negative insurance result was reported, and a minimum overall profit for the sector as 10 of the companies reported a negative financial result for the year. An improvement was reported in the middle of 2015, but it was still very low.

The main factors hindering the development of the general insurance companies remained the uncertain recovery of the economy of Bulgaria from the crisis, the weak economic activity, reduced domestic consumption and uncertainty regarding the future income of the households. The sector maintained a high growth potential, with view of the low levels of insurance density and penetration. The market concentration remained high – at the end of 2014 71.5% of GPP in the sector was formed by the seven largest companies (72.2% for 2013). The car insurance continued to dominate the insurance portfolio with a share of ~70%.

During the period of updating, the share capital and ownership structure of ZK „Lev Ins” AD remained

unchanged, as well the Supervisory and Management Boards.

The company’s activity realizes according to the set strategy in compliance with the philosophy of „Active security” – a proactive approach of risk management that gives opportunities to select portfolio so that to provide the respective profitability.

In the short-term term, the purposes of the company are connected to maintenance and increase the market share by main insurances and growth within 10%-15% annually.

The company’s target continues to be directed to the individual approach to customer service and foresees to focus on comprehensive insurance of more solvent customers with the aim of increasing the share of the combined insurances in the insurance portfolio.

The company analyzed the insurance market in Bulgaria in 2014, and the analysis shows that except with competitive rates the company has an extensive range of services in favour of the customers – a non-stop roadside assistance, innovative technical protection products, extended working hours when setting claims and paying off compensations, claims handling centres on the territory of major cities. During the year, two new products were offered for sale („Active care” and „Active road care”) that have been developed in cooperation between „Active security” and the Bulgarian Red Cross, and provide airborne and ground transportation assistance and first aid compliant with the European model.

In 2014, ZK „Lev Ins” registered a drop of 6.6% in Gross Premium Income, while the adjusted sector² realized growth of 1.8% for this period. As a result of the change, the market share of the company decreased by 0.9 p.p. as from 12.8% at the end of 2013 reached 11.9% at the end of 2014. The decrease mainly refers to the leading insurance – „Third Motor Party Liability”. The GPI from this insurance decreased by 12.5% year on year. The decline partially is compensated with the increase in GPI from „Casco” (28.2%) and „Fire and natural disasters” (51.7%). The downtrend in the GPI of ZK „Lev Ins” remained the same in the first half of 2015, as the reported drop year on year is in the amount of 7.0%, whereas an increase was reported of 8.7% for the same period in the sector. The market share of the company decreased to 11.1% at the end of June 2015.

² Adjusted with the data of the rated company.

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In the structure of the insurance portfolio of ZK „Lev Ins“ during the period of updating there were not considerable changes, and it continued to be strongly dominated by „Third Motor Party Liability“. The company has taken actions for increasing the diversification of the insurance portfolio – extra bonus campaigns on different types of insurance, directing products to a certain group of people, etc. During the period of updating, there was growth in the size and shares of the most widespread voluntary insurances.

In 2014 and the first half of 2015, gross and net claims ratios increased. ZK „Lev Ins“ continued to report higher net claims ratio compared to the average for the competitive group.

During the period of observation, the net acquisition ratio continued to be characterized with volatile dynamics as in a comparative aspect, the level of the indicator is lower than the average for the competitive group.

In 2014, the expense ratio of ZK „Lev Ins“ reported a slight decline but it was still higher than the average for the competitive group, while in the first half of 2015, a considerable drop in its level was observed that positioned it below the average of the competitive group.

The Combined expense ratio continued to be higher than 100% (an insurance loss), as well exceeded the average for other leading companies.

During the period of observation, there were not considerable changes in the reinsurance programme. The retention levels of ZK „Lev Ins Инс“ AD remained high.

During the period of updating (June 2014 – June 2015), the volume of the investment assets of ZK „Lev Ins” AD decreased faster compared to other companies in the sector. There are some changes in its structure, as they were caused mainly by the decrease in the size of the bank deposits. The share of the investments in properties exceeded considerably the average for the adjusted sector. The size of the investments in high liquid assets (government securities and bank deposits) decreased significantly, whereas the share of these assets for the adjusted sector reported growth. Comparatively, the trend remains the same – the company reported a lower share of the high liquid assets compared to the average for the adjusted sector.

At the end of 2014 the net revenues from investment activity reported by the company decreased considerably year on year, as they were formed mainly from gain of investment revaluation.

In the first half of 2015, the company generated considerably lower investment income (mainly in line of the revenues from other investments) compared to the realized for the same period of 2014 (generated mainly in line of the net result from revaluations). The achieved profitability of the investment portfolio in 2014 continued to be much higher than the average for other companies in the sector, as after a reported high decline in the first half of 2015 as of its end the level was still higher than this of the adjusted sector but the reported exceeding fell below 1.0 p.p.

At the end of 2014 and June 2015, an increase was reported of the assets covering the technical reserves on an annual basis, as the increase is mainly in line of the growth in receivables to reinsurers and receivables from insured persons. A considerable decline was reported with the bank deposits. The changes led to considerable changes in the structure of the portfolio of assets for covering the technical reserves.

In 2014, ZK „Lev Ins” reported a negative result from an insurance activity, minimum net financial result, low decrease in the level of quick liquidity ratio (remaining below the average level for the general insurance market and other leading companies) and considerable decrease in the return on equity. In the first half of 2015, the rated company registered a negative result from an insurance activity (less negative compared to the same period of the previous year), negative net financial result (positive for the same period of the previous year).

During the period of observation, there were not changes in the registered and paid-in capital. The dynamics of the equity is determined by the generated profit.

The levels of the operating and financial leverages are considerably higher than the average for the group.

The levels of liquidity ratios of the technical reserves and liquidity of the reserve for forthcoming payments decreased in 2014 and the first half year of 2015 keeping lower than the average for the adjusted sector and competitive group.

A negative impact on the assigned rating to ZK „Lev Ins” AD could have the reported trends regarding: generating an insurance loss, reduction in the realized gross premium income, growth in claims, reduction in the liquid assets and deterioration of liquidity, in case they deepen.

The diversification of the insurance portfolio and liquidity of the company continued to be lower compared to these of other general insurance companies. Some improvement in this direction would have a positive impact on the rating.

Main Indicators:

	6.2015	6.2014	2014	2013	2012	2011	2010
Gross Premium Income	85 175	91 597	170 132	182 063	158 632	143 485	135 198
<i>Change on a yearly basis %</i>	-7.0%	-5.9%	-6.6%	14.8%	10.6%	6.1%	-19.6%
Net Premium Income	87 892	91 396	171 812	162 435	159 463	115 683	134 427
<i>Change on a yearly basis %</i>	-3.8%	11.9%	5.8%	1.9%	37.8%	-13.9%	-14.0%
Result from insurance activity	-1 611	-3 488	-11 673	-1 081	3 666	9 621	-26 936
Net Profit	-300	7 424	68	13 704	915	10 601	-25 069
Gross Claims Ratio	66.1%	60.1%	80.3%	59.8%	56.4%	50.5%	50.5%
Net Claims Ratio	61.0%	57.1%	66.8%	58.1%	54.6%	45.1%	49.2%
Combined Expense Ratio	101.8%	103.8%	106.8%	100.7%	97.7%	91.7%	120.0%
Operating Leverage	152%	139%	295%	280%	359%	266%	409%
Financial Leverage	311%	283%	314%	317%	363%	349%	401%
Liquidity Ratio	2.6%	2.9%	2.2%	2.4%	2.8%	2.2%	4.1%
Return on Equity	-13.0%	38.3%	0.1%	28.9%	2.1%	29.2%	-51.0%