CREDIT RATING AGENCY

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„ZK Lev Ins" AD

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CLIAMS PAYING ABILITY RATING*	Initial Rating ** 09.02.2017
Long-term rating:	BB+
Outlook:	Positive
National-scale long-term rating:	A- (BG)
Outlook:	Positive

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

*** An initial rating is assigned because on a meeting held on 06.01.2017 the Rating Committee of BCRA took a decision to withdraw the assigned long-term claims paying ability rating to the insurance company. The withdrawal was dictated due to a delay in submitting part of the needed information, therefore the process of updating of the assigned rating was not completed as of the time of expiry.*

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 to „ZK Lev Ins" AD the following ratings:

- ***Long-term claims paying ability rating: BB+, outlook: „positive";***
- ***National-scale long-term claims paying ability rating: A- (BG), outlook: „positive".***

The officially adopted methodology by BCRA for assigning rating of the ability of insurance companies to pay claims is in use*: http://www.bcra-bg.com/files/file_202.pdf.*

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.

During 2015, the economy of the country reported a 3.6% real growth – the highest value after the financial crisis, as the major growth factors are export of commodities and services and growth in final consumption. The marked growth in GDP was twice higher than the achieved for the past two years (1.6% in 2014, 1.3% in 2013). In the first half of 2016, there was an increase in importance of the domestic consumption for economic growth.

The FIF (foreign investments flow) reached 3.7% of GDP after hesitations of about 3.1%-3.3% over the past three years. A significant increase in the reinvested profit after the past year, and in investments in the share capital. The investors, however, remained cautious as the levels of the investments remained considerably lower compared to the years before the crisis. For the first half of 2016, the foreign investments reduced slightly compared to the same period of the past year – declined to 2.0% of GDI (2.2% of GDI as of Q2 2015).

The favourable changes in the labour market remained the same – unemployment rate (as well as continuous unemployment rate as a percent of the active population) maintained their downtrend after 2013. In 2015, the average unemployment rate was 9.2% (11.5% in 2014).

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Since early 2014, deflationary processes have been detected and reached their peak in early 2015 and remained the same at the end of the year. According to the EC spring forecast, there will be deflation in 2016 as well, as the expected price level change is about -0.7% at the end of the year. EC foresees the factors causing a decline in the price level to be removed, and in 2017 the country to switch to a situation of low inflation.

The 2014 banking system events led to the emergence of a potential threat to banking institutions to deepen the banking crisis and involvement of a larger number of participants in the sector. Despite the increased risk in the financial system raised by the removal of one of the main players and the risk of dropping the second, the banks in Bulgaria maintained its stability. The announced on 13.08.2016 results from the assets quality review and stress tests for stability of the banks in Bulgaria show that the banking sector is stable, well capitalized and public support to the banks with funds given by the public budget is not needed.

The general insurance market in Bulgaria during the period of updating is characterized by:

- Strengthening the uptrend in written gross premiums income over the past three years;
- High level of market concentration - 72.7% of GPI in the sector (as of 09.2016) is formed by the seven largest companies (71.5% in 2014);
- High share of car insurances in the structure of the aggregate insurance portfolio (69.7% as of 09.2016).

The major factors hindering the development of the general insurance companies continued to be uncertain recovery of the Bulgaria's economy from the crisis and low economic activity, decreased domestic consumption and uncertainty concerning future revenues of the households. The sector keeps high growth potential, having in mind low levels of insurance density and penetration.

The published results (on 03.02.2017) from the led assets review and stress-tests of the insurance companies in the country are evidentiary for the stability of the rated company.

During the period of updating, the shareholding capital of ZK „Lev Ins“ AD remained unchangeable. The share of the majority shareholder rose in the shareholding structure. The Supervisory Board did not change after June 2015. During 2016, Mrs. Vera Lyubenova Pavlova and Mrs. Spaska Petrova Shtereva from the Management Board were replaced by Mrs. Marusiya Georgieva Stoyanova-Ivanova and Mr. Galabin Nikolov Galabov, as Mr. Galabov is employed as Executive Director as well.

During 2015, ZK „Lev Ins“ AD reported a decline of 4.3% in gross premium income (GPI), while for the given period the adjusted sector realized growth of 9.5 p.p. As a result of the change, the market share of the company decreased by 1.5 p.p., as from 11.9% at the end of 2014 declinea to 10.4% at the end of 2015. During the first nine months of 2016, the trend of decreasing GPI has been overcome and as of the end of September 2016 an increase of 20.6% was reported on a yearly basis. The reported growth by the company increased faster than the adjusted sector which amounted to 6.2% in the period under review. This is reflected in the increase in the market share of the company to 12.1% as of the end of September 2016.

There were not any significant changes in the the insurance portfolio structure of ZK „Lev Ins“ AD during the period of updating, and it continued to be highly dominated by „Motor Third Party Liability“. Regardless of the activities taken by the company to improve the diversification of the insurance portfolio in the structure of the portfolio, there were not any considerable changes.

During 2015 and the nine-month of 2016 there was a downtrend in the gross and net claims ratios. With this, the company has overcome the trend in the past period in reporting higher net claims ratios compared to the average in the competitive group and at the end of 2015 and in September 2016 it reported by 8.3 p.p. and 13.2 p.p. lower values compared to the group.

The analysis of the expense structure of ZK „Lev Ins“ shows that in 2015 the combined expense ratio overcame the uptrend in the past three years, as on a yearly basis its value decreased by 12.0 p.p. and for the first time after 2012 reported a growth below 100% (94.8%) which is an indicator for realizing insurance profit. As of 30.09.2016, the ratio value was 93.2%. With the reported values as of the end of 2015 and the end of September 2016, the company had an average position in the competitive group.

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During the period of updating, there were not considerable changes in the company reinsurance programme. A start of a downtrend was watched in the retention level, continuing in the nine-month of 2016, as a result of which the held higher retention level by the company compared to the average for the adjusted sector considerably reduced.

The started downtrend in 2014 of the investment assets volume of ZK „Lev Ins” AD continued, as the same was opposite in the sector which increased during the period of updating. The structure changes in the investment portfolio are determined mainly by a considerable decrease in the bank deposits which contributes for increasing the share on other positions. The investments share in real estates considerably exceeded the average in the adjusted sector (7.5% in both reporting periods). The size of the investments in high liquid assets (government securities and bank deposits) decreased considerably, while the share of those assets in the adjusted sector reported growth.

The achieved as of the end of 2015 profitability of the investment portfolio of ZK „Lev Ins“ AD decreased considerably compared to 2014, for the first time after 2012 it is lower than the average in the sector. The trend is maintained as of the nine-month period of 2016 as well.

As of the end of 2015, the assets for covering the technical reserves reported an insignificant increase (0.2%) but with considerable structure changes on positions assets. The receivables to reinsurers increased considerably compared to significant reductions of the receivables from insurance persons and mediators and bank deposits. As a result there were considerable changes in the structure of the assets portfolio for covering the technical reserves. The assets are structured according to the diversification requirements determined in the Insurance Code.

During 2015, ZK „Lev Ins” AD continued the uptrend in net earned income which together with the decline of the operating expenses led to reporting of a positive result from insurance activity (negative in the past two years) and a net financial result of 10 667 thousand BGN.

During 2015, the value of the quick liquidity ratio increased (to 3.8%), as in a comparative aspect remained below the average for the adjusted general insurance market (6.0%), but higher compared to the other leading companies (3.2%). As a result of the realized profit, the return on equity increased considerably.

During the first nine months of 2016, the rated company reported a decline in net earned income yoy, but achieved a positive result from insurance activity, a total minimum positive financial result. The value of quick liquidity ratio amounted to 2.9%, being below the average for adjusted general insurance market (8.2%) and the average for other leading companies (4.0%). Return on equity (16.9%) is significantly better compared to the same period of the past year and higher than the average for the other companies in the sector (8.4%).

During the period under review, the company has not distributed dividends, as the dynamics of equity is determined only by the generated profit.

During 2015, the value of the operating leverage remained above the average for the other leading insurance companies, despite the reported decrease during the period under review. The financial leverage reported a greater decline in value, for which except the increase in equity, also the reduction in the technical reserves contributes. As of 30.09.2016 the operating and financial leverage declined, and they come closer to the average in the competitive group, but continued to be higher than the adjusted sector.

The levels of liquidity ratios of technical reserves and liquidity of the reserve for forthcoming payments declined in 2015 and the first nine months of 2016 remaining lower than the average in the adjusted sector and competitive group.

During the period of updating, ZK „Lev Ins” AD maintained a relatively stable financial condition. During 2015 and the nine-month period of 2016 realized a positive result from insurance activity and from the realized incomes from the investment portfolio.

A decline in realized gross premium income, increase in claims, significant negative re-evaluations from the owned investment portfolio, deepened decline in liquid assets and additional deterioration of the liquidity can influence negatively on the assigned company rating.

The diversification of the insurance portfolio and liquidity of ZK „Lev Ins” AD continue to be lower compared to the other general insurance companies. Some improvement in those directions could *influence positively on the rating.*

Main Financial Indicators:

Indicator / Year:	*09.2016*	*09.2015*	*2015*	*2014*	*2013*	*2012*	*2011*
Gross Premium Income (thousand BGN):	**145 203**	**120 362**	**162 876**	**170 132**	**182 063**	**158 632**	**143 485**
Change on a yearly basis	*20.6%*	*-7.7%*	*-4.26%*	*-6.6%*	*14.8%*	*10.6%*	*6.1%*
Net Earned Income (thousand BGN):	**107 026**	**124 662**	**184 449**	**171 812**	**162 435**	**159 463**	**115 683**
Change on a yearly basis	*-14.1%*	*-3.7%*	*7.4%*	*5.8%*	*1.9%*	*37.8%*	*-13.9%*
Net Profit (thousand BGN)	**69**	**-526**	**10 667**	**68**	**13 704**	**915**	**10 601**
Result from insurance activity	7 276	-1 979	9 602	-11 673	-1 081	3 666	9 621
Gross Claims Ratios	56.1%	66.7%	70.3%	80.3%	59.8%	56.40%	50.47%
Net Claims Ratios	42.6%	61.6%	42.8%	66.8%	58.1%	54.60%	45.06%
Expense Ratio	27.1%	17.9%	32.6%	19.5%	20.9%	22.94%	22.02%
Acquisition Ratio	23.5%	22.1%	19.3%	20.5%	21.7%	20.17%	24.60%
Combined Ratio	93.2%	101.6%	94.8%	106.8%	100.7%	97.70%	91.68%
Operating Leverage	156%	216%	268%	295%	280%	359%	266%
Financial Leverage	205%	306%	185%	314%	317%	363%	349%
Quick Liquidity Ratio	2.9%	1.8%	3.8%	2.2%	2.4%	2.83%	2.18%
Return on equity	16.9%	3.9%	17.8%	0.1%	28.9%	2.1%	29.2%

***Rating history:**
The ratings in the chart are assigned under the previously used Methodology for rating of the ability of insurance companies to pay claims, respectively with the applied rating scale, are not directly comparable with the ratings assigned after the entry into force of the current methodology (as of July 2016).

Claims paying ability rating	**Initial Rating 6.2006**	**Non-solicited update 11.2007**	**Non-solicited update 11.2008**	**Update 7.2009**	**Update 20.07.2010**	**Monitoring 07.12.2010**
Long-term rating:	**BB+**	**iBBB-(ns)**	**iBBB(ns)**	**iA-**	**iA-**	**iA-**
Outlook:		*positive*	*positive*	*stable*	*Stable*	*negative*
Claims paying ability rating	**Monitoring 25.05.2011**	**Update 25.10.2011**	**Update 29.11.2012**	**Update 04.11.2013**	**Update 13.12.2014**	**Update 10.12.2015**
Long-term rating:	**iBBB+**	**iBBB+**	**iBBB+**	**iBBB+**	**iBBB+**	**iBBB**
Outlook:	*negative*	*developing*	*positive*	*stable*	*stable*	*negative*
Claims paying ability rating	**Monitoring 05.07.2016**	**Update 06.01.2017**				
Long-term rating:	**iBBB (under review)**	**iBBB (w)***				
Outlook:	**-**					

(w) stands for withdrawn rating. The rating was withdrawn keeping the internal rules and procedures for withdrawal, due to impossible update of the rating within the deadline;

***** A requirement of internal rules and procedures after withdrawal for assigning initial rating***