BCRA CREDIT RATING AGENCY

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Investbank AD

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FINANCIAL STRENGHT RATING	Update	Monitoring	Update
Rating Committee Date:	18.11.2020	29.03.2021	26.11.2021
Publication Date:	19.11.2020	30.03.2021	29.11.2021
Long-term rating:	B-	B	B
Outlook:	stable	stable	stable
Short-term rating:	C	C	C
Long-term National-scale rating:	B- (BG)	B (BG)	B+ (BG)
Outlook:	stable	stable	stable
Short-term National-scale rating:	C (BG)	C (BG)	C (BG)

1) *Prior to the present publication the credit rating and rating outlook was disclosed to the rated entity or related third party. Following that disclosure amendments in the credit rating and rating outlook have not been executed;*
2) *During the last 2 years, BCRA Credit Rating Agency AD has not provided ancillary services to the rated entity or a related third party.*
3) *To become familiar with the full rating history, please see the table at the bottom of the document.*

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

The officially adopted by BCRA Methodology for assigning a rating to a bank has been used *(https://www.bcra-bg.com/files/bank_methodology_2018_en.pdf)*

The users of the rating can find information on the meaning of each rating category, including definitions of default in the published Global rating scale on the BCRA's website: *(https://www.bcra-bg.com/files/global_scale_en.pdf)*

The report has been prepared and the rating - assigned, based on information made available by the rated bank, Bulgarian National Bank, National Statistical Institute, BCRA' database, consultants and other public information sources.

At a session of the Rating Committee of BCRA, held on **26.11.2021** a report of the review of the credit rating of the Investbank AD has been discussed**.** The session was run by D.Sc. (Econ.) Kiril Grigorov, in his capacity as a Chairman of the Rating Committee. Following a discussion on changes in the factors affecting the rating during the review period, the members of the Rating Committee **took the following decision:**

BCRA – Credit Rating Agency (BCRA) assigns to **Investbank AD** the following ratings:

- **Affirms** long-term financial strength rating **B,** and **affirms** short-term rating **C**
  stable outlook
- **Upgrades long-term** national-scale rating **to B+ (BG)** from B (BG) and **affirms short-term** national-scale rating **C (BG)**
  stable outlook

apprising the stable financial performance of the Bank during the review period. The increase of the capital base and capital adequacy and the improvement of the loan portfolio quality indicators have been observed.

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Operating Environment

Sovereign Risk

The emergence of the COVID-19 pandemic worldwide has turned into a major issue and one of the top priorities both in Bulgaria and in all its political and economic partners. Due to the unprecedented crisis in the country, an 'epidemic emergency' has been introduced and, due to the inability to form a government after two parliamentary elections in 2021, Bulgaria is governed by a caretaker government.

The COVID-19 pandemic and the measures taken to control the infection have adversely affected the economic activity in the country, as the reported decline in GDP in 2020 amounted to 4.2% (3.7% growth achieved a year earlier), but the recovery is already underway. The country's real GDP grew by 3.1% on an annual basis according to preliminary data for the first half of 2021.

Following the slowdown observed in household consumption, lending, external sector indicators, and inflation, in the first half of 2021, the dynamics are reversed, and the achieved real growth averaged 3.1% on an annual basis. The unemployment rate rose to 5.6% by Q2 2021 (5.1% on average for 2020).

Bulgaria has entered the current crisis with a stable fiscal position and a low government debt level. The Consolidated Fiscal Program balance for 2020 was a cash deficit of 3.0% of GDP (1.0% in 2019) after the government-financed fiscal aid to the sectors most affected by the crisis. In the first half of 2021, budget revenues continue to grow at a slower pace than expenditures. General government debt rose to 24.7% of GDP by June 2021 due to financial needs arising from the anti-crisis fiscal measures and the decline in GDP but remained low in comparative terms.

The development of economic processes in the country is analysed in detail by *BCRA - Credit Rating Agency.* A Rating Rationale of the Sovereign Rating assigned by BCRA to the Republic of Bulgaria is available at our official website:

https://www.bcra-bg.com/files/rating_republic_of_bulgaria_oct_2021_bg.pdf

Banking System

One year after Bulgaria became a member of the EU Banking Union, and the Bulgarian lev is officially in the ERM II, in July 2021 the National Plan for the introduction of the euro in Bulgaria was presented with a target date of January 1, 2024.

As of mid-2021, the banking sector remains resilient despite the economic turbulences. The capital ratios and liquidity of banks are at high levels being supported by the steady growth of the deposit base as well as the timely regulatory anti-crisis measures.

Following the slowdown in 2020 (to 4.8%), the credit growth in the non-financial sector remained moderate in the first half of 2021, reaching 6.8% YoY, with higher activity of individual customers. By the middle of 2021, however, there has been a slight acceleration in both enterprises and households. Concurrently, the carrying amount of deferred loans under the Procedure for Deferral and Settlement of Liabilities Payable to Banks and their Subsidiaries – Financial Institutions reached BGN 9.4 billion or 13.3% of the total portfolio at the end of June 2021, after the opportunity to submit applications under this procedure had expired at the end of March.

The profit of BGN 815 million generated in 2020 is 51.4% lower on an annual basis. Net interest income and fees and commissions retain their leading role in its formation, but with an annual decline in both sources. At the same time, the value of the impairments incurred has doubled compared to 2019. In the first half of 2021, there has been a partial recovery of the result of the banking system at opposite movements of the specified parameters, and the BNB decided to fully capitalise the profit for 2020 (as well as the one for 2019) as a measure to further strengthen the capital of banks in the context of the crisis related to COVID-19.

Investbank AD

Ownership and Management

In the first half of 2020, Investbank AD carried out a two-fold rise of its **share capital** related to the Bank's turnaround plan and strengthened capital position. The capital amounts to BGN 155 572 thousand, distributed in the same number of shares, a face value of BGN 1 each. At present, it remains unchanged. There are no significant changes in the shareholding structure - Festa Holding remaining the major shareholder, followed by Mr. Al Shanfari.

In 2021, changes occurred in the management bodies of Investbank, thus the Supervisory Board is composed of:

- Petia Ivanova Barakova-Slavova – Chair;
- Festa Holding AD, represented by Ivailo Stoyanov (replaced Zlatomir Dimitrov);
- Martin Bogdanov – independent member (newly elected).

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Vessela Koleva-Djidjeva and Lyudmila Vassileva were dismissed from the Board and Svetoslav Milanov was appointed as an independent member. Thus the Board is a three-member and includes:

- Zdravka Russeva – Chair and Executive Director;
- Maya Stancheva – member and Executive Director;
- Svetoslav Milanov – member and Executive Director.

Most key indicators in the Bank's plan exceed the rates (including assets, net loans, deposits and interest income). Only the financial result is lower than planned.

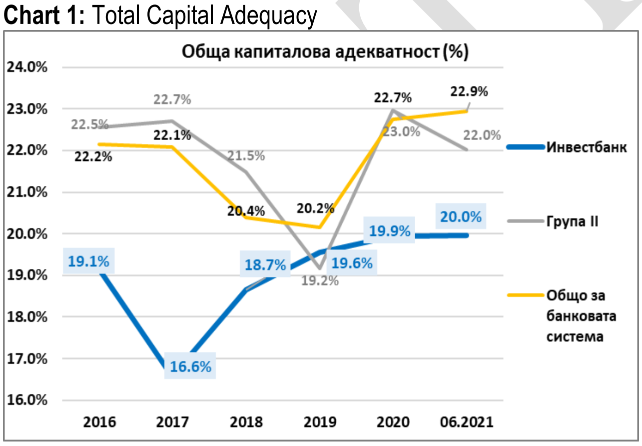
Capital Adequacy

The Bank's **capital base** continued its positive upward trend in 2020, with significant annual growth of 8.4% at year-end, as a result of the aforementioned increase in shareholders' equity. However, in the H1 of 2021, a decrease of 1.9% is posted compared to the end of 2020.

At the end of 2020, **risk-weighted assets (RWAs)** increased more substantially - by 6.3% y-o-y, after a 3.8% decline in the previous year and the stagnation in the past years. Changes in the capital base and RWAs over the review period led to an **increase in the total capital adequacy** to 20.0% in mid-2021.

With the reported increases after 2017, at the end of 2019, the Bank is now positioned very close to the average of total capital adequacy for the banking system (20.2%).

Chart 1: Total Capital Adequacy



As a result of the higher growth in the last year, the negative gap of the indicator exceeded 2 pp of the remaining part of the banks at the end of the review period. This is a result of the BNB's decisions to fully capitalise profits for 2019 and 2020, and the risk treatment of certain exposures that came into force at the end of June 2020 (EU Regulation 2020/873) as measures to further strengthen banks' capital in the context of the COVID-19 crisis. The capital adequacy, however, significantly exceed regulatory requirements, providing both stability against potential shocks and room for additional asset growth in a normal environment.

The level of unadjusted ***leverage***, after a long (3-year) period of decline until the end of 2020, recorded a significant increase in mid-2021 - to 10.3, remaining above the average for the banking system (8.0) and Group II banks (8.1). Adjusted leverage remains significantly above the peer group indicators despite the significant drop in the last period - to 25.2 from 44.8 in the previous year. The leverage ratio "fully phased-in" definition of Tier 1 capital increased again after a two-year upward trend to the highest rate of 11.5% for the prior 2019. The decline at the end of the year 2020 is to 10.7% and continues the downward trend to 9.4%.

In 2020, the Bank recorded a significant decline in the ratio of ***net NPLs to the capital base*** for the third consecutive year, following the increase in the early years of the period. The reduction in the last year was almost 20 p.p. to reach a value of 58.9% - the lowest in all years of the analysis. However, it remains significantly higher than the banking system average of 14.5% at the end of 2020 and 12.5% as of June 2021.

Due to the relatively low net profit for the last 2020, posted amidst increasing equity, the **return on equity** decreased to a relatively low level of less than 1.0% (0.95% for 2020 vs. 1.12% for 2019).

Resources

At the end of 2020, the value of **borrowed funds** marked a significant year-on-year growth of 14.3%, following the only year of the last five-year period with a decline - 2019 (-10.5%). This strong pace continues into the first half of 2021 when the increase is 15.5% and almost BGN 300 mln in just six months.

The strong growth in the last 2020, to a greater extent, is a result of the increase in the value of funds attracted from *corporate customers* - by 58.2%, with much lower growth (3.2%) in deposits of *individuals*. By mid-2021, this growth strengthened, more for corporate deposits (28.4%), but also for individuals (8.9%) on a half-yearly basis.

Structurally, in terms of **source** of deposits, the resource base continues to be dominated by those of individuals and households, but the reported higher growth in corporate deposits over the past year

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resulted in an increase in their share to 37.9% compared to 24.7%.

In the **currency structure** of the Bank's resources, deposits in BGN remain dominant, rising slightly to 62.2% in mid-2021. The stronger share of the Bulgarian Lev in the corporate deposit structure is maintained and even increased further (to over 80%).

The share of guaranteed deposits in the deposit base declined significantly at the end of 2020 - to 65.2%, compared to 75.9% a year earlier, and continued to decline in the first half of 2021, as a result of both strong dynamics in volumes and the structure of the deposit base during the annual review period.

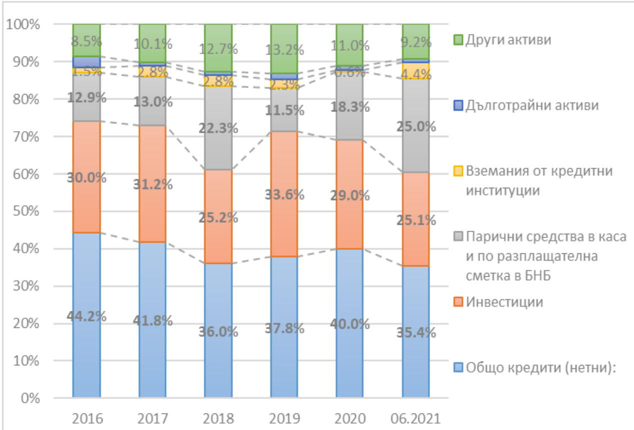
There is no **concentration** in the deposit base but the share of the 15 largest depositors remains relatively high at 21.9% on 30/06/2021 and 21.2% on 31/12/2020 (after 19.3% on 30/06/2020 and 17.6% on 31/12/2019).

Assets Quality

The ***value of Investbank's assets*** grew by a remarkable double-digit annual growth - 15.9% at the end of 2020, following the significant decline of 10.5% in the previous 2019, along with a drop in their value below BGN 2 billion. The increase in assets is also significant in the six months of 2021, amounting to 12.6% compared to the end of 2020 and 25.8% compared to the same period of 2020.
Compared to the national *banking system average*, dynamics in the value of assets are volatile but show signs of recovery. Thus, with the high growth rates for 2020, the Bank exceeds almost twice the system's average (8.6%), characterized by smoothly increasing values that stood at around 8% in the last years.

In the **structure of assets** the downward trend of the *relative share of loans* strengthened, and from an average of about 40.0% for the previous periods, at the end of the last period their share (net loans) was 35.4%. This is significantly lower than the average for the banking system (52.9%) and the Group II banks (51.2%). The share of the *investment portfolio* in the Bank's assets is traditionally higher in comparative terms, at around and above 25%, while the relative share of *Cash on Hand and in current account with the BNB* rose very sharply to 25%, from 11.5% in 2019 and 18.3% at the end of 2020. The total share of this group, together with *Receivables from credit institutions*, exceeded 50% at the end of June 2021. This is viewed positively from a liquidity perspective, but puts pressure on the Bank's return on assets ratio and the financial performance, as well.

Chart 2: Assets Structure in Relative shares (%)



Investbank's gross **loan portfolio** is finally seeing growth, an impressive one of 19.1% year-on-year at the end of 2020. This is a significant change after a series of years of declines and stagnation in lending. The sustained downward trend, which marks the reviewed years ended in the H1 of last year (with six-month growth of 6.9%, accelerating in the H2 of 2020 to the significant BGN 150 million in gross loans). At the end of H1 of 2021, growth has ended, even there is a negligible decline of 0.7% compared to the end of 2020, although year-on-year growth of 10.7%.

In terms of the **structure** of the loan portfolio, the changes confirmed the direction, which started in 2018. These changes are mainly in the two most important groups - loans to corporates and retail exposures. The decrease in loans to corporates both in value (as of the end of 2019) and as a relative share in the structure is strengthened at the expense of the increase in the absolute value and relative weight of retail exposures in the Bank's total loan portfolio for both 2020 and the H1 of 2021. However, the gross structure remains dominated by *loans to corporates*, the decrease in which is due to the decline in the total amount of loans at mid-2020. The turnaround year 2020 saw a 13.2% year-on-year growth in these loans for the first time, but at the end of H1 of 2021, a 2.6% decline was again posted, and their relative share fell to 66.9% (from nearly 80% in the previous years). The term structure of loans has retained the trends from the previous period - a decrease in the average term of corporate loans and an increase in loans to individuals. The structure of the corporate loan portfolio by the *industry* remains well-diversified, with the highest share of loans to the Trade sector (20.9% of loans to enterprises).

Non-performing loans, after a long period of growth, both in absolute value and as a *relative share in the gross loan portfolio*, reversed this trend in the second half of 2019, with their share falling to 30.2%. A real turning point in this respect, however, was 2020, when

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the improvement is more evident and is reflected in a drop of nearly 10 pp., to the lowest value in the 10-year rating history of the rated bank - 20.4%. It should also be noted that the decrease in the relative share of NPLs is also a result of the mentioned strong growth in total loans for 2020 (in contrast to previous years). At the end of the six months of 2021, this share remained close to the result already achieved, with a slight deterioration - an increase by half a percentage point to 20.96%, reflecting both the weak growth of the amount of non-performing loans (by 1.8% for the six months 2021) and the corresponding decrease of gross loans (by 0.7%).

However, the level of these loans remains much higher than the national average for the banking system (7.7% as of June 30, 2021) and the improvement pace needs to resume.

The coverage of the gross loan portfolio by impairments is decreasing. For the last period, after a steady upward trend until 2018, it dropped to 5.2% in mid-2021, compared to an average of 5.0% for the banking system. The coverage of non-performing loans was 24.8% at the end of the period and remained more than twice lower compared to the average for the banking system. This is a result of the continuing decline in impairments in the recent period, despite the positive impact of the declining non-performing loans.

The share of the *15 largest credit exposures* in the gross loan portfolio, despite some decline over the last period, remains high in relative terms and continues to show concentration according to the indicator.

Income Quality

In 2020, the profitability of Investbank AD remains relatively low and close to that reported a year earlier, with a *return on assets* of 0.11% (0.10% in 2019) and only on *interest-bearing assets* of 2.15% (2.50% in 2019). Income generated from *net interest, net fees, and commissions* was in a similar range at just over BGN 24 million, with an annual decline of both main revenue sources. However, together with the corresponding decrease in the achieved operating profit (by 21%), there has been an ongoing optimization of the counter operating expenses (-6.3%) as well as of the Bank's other expenses. As a result, the *net profit* for 2020 increased slightly on an annual basis (by 5.3%), reaching BGN 2.2 million.

At the end of H1 of 2021, the *current financial result* of the bank was a profit of BGN 488 thousand - BGN 5,867 thousand for the corresponding period of the previous year. The significant annual decline is mainly due to the reduction in the operating result (by BGN 4,611 thousand) and the growth in non-operating expenses (by BGN 768 thousand).

During the annual review period, the Bank generally retains its advantages over the system averages of the financial ratios in terms of non-interest income, net fee and commission income, and personnel costs but remains well below average in terms of interest rate spreads and return on assets.

Liquidity

The increase in the amount of shareholders' **equity** in the first half of 2020 (reported in the previous annual review) is reflected in the impressive 31.1% annual growth (by 58.5 million BGN). At the end of the H1 of 2021, the Bank's equity registered a slight decrease, amounting to 2.2% compared to the end of 2020 and 4.5% year-on-year due to the reduced amount of profit for the period. The Bank's **total liabilities** (the sum of Equity and Liabilities) also registered a robust growth of 15.9% for 2020, which is weaker than that of Equity. For the six months of 2021, the increase is again significant at 12.6%, and even higher year-on-year at 25.8%. Thus, with equity growth for 2020 outpacing that of the total liabilities, the level of the *equity-to-total liabilities ratio* confirms a three-year upward trend, reaching 11.2% (9.9% a year earlier). With this increase, the indicator narrows the gap to the average level for the banking system (12.4%). With the reduction of equity and the continuing strong growth of total liabilities for the H1 of 2021, the indicator again fell below 10% (9.7%), and the gap to the average for the banking system reference values again increased above 2 pp. In terms of comparison with previous years over the whole analysed period, the general increase of the indicator **impacts positively the Bank's liquidity position.**

In terms of the ***Total Loans to Total Deposits*** ratio, despite the observed slight increase, the rated bank remains with one of the lowest levels compared to the reference group of banks and much lower levels compared to the average for the system and Group II banks.

The ***Highly Liquid Assets/ (Total Liabilities - Equity)*** ratio, after the decline in 2018 to its lowest value (15.4%), reported a significant improvement - rising to 21.2% at the end of 2020 and peaking at 32.5% at the end of June 2021. This is a result of the robust growth in highly liquid funds in the last period, significantly outpacing that of the attracted funds. On a comparative basis, with the latest increase, the Bank is approaching the average of the reference group of banks, following the significantly lower values of previous periods.

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The Bank maintains a **liquidity coverage ratio (LCR %)** well above the minimum required 100%, including a sufficiently high share of liquid assets. At the end of 2020, there is a significant **increase in net liquidity outflows**, offset to a high extent by the increase in the liquidity buffer. This results in a certain decline of LCR to 286% (444% in the last year). In the H1 of 2021, the LCR rose significantly as a result of the reduction of net liquidity outflows together with the growth of liquidity buffer.

A stable funding structure has been maintained in which the loan portfolio is primarily funded by customer deposits. Net stable funding ratio (NSFR) levels are also positioned above internal and regulatory limits.

Size and Systems

As a result of its strong asset growth over the review period, as well as the consolidation in the sector, Investbank moved up to 10th place in the ranking of banks by **assets held**, regaining the position of Municipal Bank. The position in the ranking by the **size of loans** retained - 11th, while in terms of the size of the **deposit base** (excluding deposits of banking institutions), the Bank gained one position and took 10th place, ahead of Municipal Bank compared to the previous period.

The main banking and additional operational systems used by Investbank AD have sufficient capabilities to service all operational processes. They are maintained following the Bank's approved Development Strategy, and their use is carried out in a secure environment. The Bank's key project to upgrade and extend the functionality of its corporate website was completed in 2021.

In the period under review, Investbank AD maintained a relatively stable financial position, increasing its capital base, retaining the capital adequacy within optimal limits and improving liquidity indicators. The need to accelerate the process of improvement of credit quality by reducing the level of NPLs in the portfolio, which are at a relatively high level for the system, with a low coverage by impairments, is noted.

Positive impact on the Bank's rating could have the following*: steady improvement in the operating result and the generated profit, ensuring high levels of impairment charges, continuation and acceleration of the improvement in the quality of loan portfolio, as well as the successful realisation of the acquired fixed assets (loan collaterals).*

Negative impact on the assigned rating *could have: diminishing or realisation of a negative operating and/or financial result, decrease of profitability, deterioration of the quality of the loan portfolio as a result of adverse effects of the COVID 19 pandemic on the Bank's clients, and the levels of indicators for capital adequacy and liquidity.*

Main Financial Indicators:

(BGN'000)	06.2021	2020	2019	2018	2017	2016
Balance Sum	2 477 588	2 200 670	1 898 475	2 122 039	1 954 129	1 916 189
Gross Loans	924 300	930 668	781 145	850 164	878 351	877 994
Equity	241 151	246 608	188 094	180 266	152 187	181 542
Net Interest Income	10 415	24 346	26 146	30 081	33 144	30 264
Net Financial Result	488	2 200	2 089	22 647	-29 333	1 038
%						
Total Capital Adequacy	19.95%	19.93%	19.55%	18.66%	16.58%	19.14%
Net Interest Margin	1.56%	1.76%	1.90%	2.15%	2.39%	2.07%
Return on Assets	-0.14%	0.11%	0.10%	1.10%	-1.55%	0.05%
Gross classified exposures / Total loans	20.96%	20.44%	30.16%	31.50%	29.28%	28.11%
Net coefficient of overdue generation	0.47%	-8.32%	-5.53%	1.84%	-0.41%	2.28%
Liquidity Ratio	-	-	-	-	37.47	35.90
Liquidity Coverage Ratio	415%	286%	444%	440%	538%	479%

****Rating History:***

FINANCIAL STRENGTH RATING	Rating Committee Date	Publication Date	Long-term Rating	Outlook	Short-term Rating	Long-term National-scale Rating	Outlook	Short-term National-scale Rating
Monitoring	**18.11.2020**	**19.11.2020**	**B**	**stable**	**C**	**B (BG)**	**stable**	**C (BG)**
Update	**18.11.2020**	**19.11.2020**	**B-**	**stable**	**C**	**B- (BG)**	**stable**	**C (BG)**
Update	**29.11.2019**	**3.12.2019**	**B-**	**negative**	**C**	**B- (BG)**	**negative**	**C (BG)**
Update	**28.11.2018**	**30.11.2018**	**B-**	**stable**	**C**	**B- (BG)**	**stable**	**C (BG)**
Update	**22.11.2017**	**23.11.2017**	**B-**	**stable**	**C**	**B (BG)**	**stable**	**C (BG)**
Update	**26.10.2016**	**27.10.2016**	**B-**	**In development**	**C**	**B (BG)**	**In development**	**C (BG)**
Update	**12.10.2015**	**13.10.2015**	**B-**	**stable**	**C**	**B (BG)**	**stable**	**C (BG)**

The ratings in the table below were assigned under the previous Methodology for assigning a financial strength rating to a bank and are not directly comparable to ratings assigned after the effective date of the current Methodology as of September 9, 2015.

FINANCIAL STRENGHT RATING		Long-term Rating	Outlook	Short-term Rating
Monitoring	**8.9.2015**	**B- (under review)**	**-**	**C (under review)**
Update	**13.10.2014**	**B-**	**stable**	**C**
Update	**18.12.2013**	**C**	**stable**	**C**
Monitoring	**10.5.2013**	**B-**	**negative**	**C**
Update	**19.12.2012**	**B+**	**negative**	**C**
Monitoring	**14.9.2011**	**B+**	**negative**	**C**
Update	**25.5.2011**	**BB**	**negative**	**B**
Monitoring	**7.12.2010**	**BBB-**	**negative**	**A-3**
Update	**3.5.2010**	**BBB-**	**stable**	**A-3**
Monitoring	**18.11.2009**	**BBB-**	**negative**	**A-3**
Initial Rating	**1.4.2009**	**BBB-**	**stable**	**A-3**