Reconstruction Capital II Ltd

("RC2" or the "Fund")

Quarterly Report

31 December 2022

New Europe Capital SRL
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Statistics

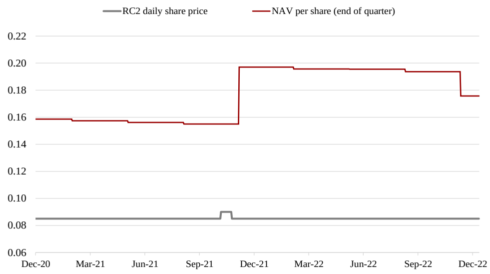
NAV per share (€)	0.1757
Total NAV (€ m)	23.8
Share price (€)	0.0850
Mk Cap (€ m)	11.5
# of shares (m)	135.7
NAV/share since inception†	-57.99%
12-month NAV/share perfomance	-10.88%

† assumes pro-rata participation in the 2008 share buy-back, the 2017 return of capital and subsequent buy-backs

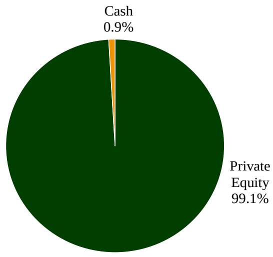
RC2 Quarterly NAV returns

	2019	2020	2021	2022
1Q	0.12%	-0.77%	-0.75%	-0.76%
2Q	-0.76%	-0.75%	-0.78%	-0.07%
3Q	-0.75%	-0.86%	-0.74%	-0.93%
4Q	-34.31%	12.04%	27.16%	-9.29%
YTD	-35.22%	9.40%	24.30%	-10.88%

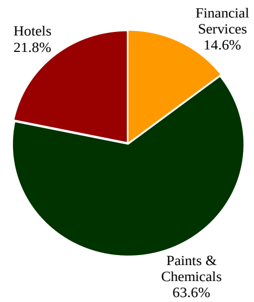
Share price / NAV per share (€)



Portfolio Structure by Asset Class



Equity Portfolio Structure by Sector



Message from the Adviser

Dear Shareholders

During the fourth quarter, RC2's total NAV fell by € 2.4m, with its NAV per share falling by 9.29% from € 0.1937 to € 0.1757, reflecting the new valuations of RC2's investments pursuant to the annual independent valuation exercise. These resulted in the following changes to the valuations of RC2's private equity positions:

	Prior valuations €	Revised valuations €
Policolor SA	17,000,000	14,080,000
Mamaia Resort Hotels SRL	4,076,986	4,814,247
Telecredit IFN SA	1,895,500	3,230,000
Total	**22,972,486**	**22,124,247**

In 2022, the outbreak of war across the border in Ukraine triggered a global energy and food crisis, adding fuel to inflationary pressures which were already building up as the world transited out of Covid-induced economic repression, resulting in rising interest rates, and disrupted supply chains, and the erosion of the purchasing power of households and businesses. Mainly due to these difficult circumstances, Policolor fell short of its budgeted targets, whilst Mamaia and Telecredit were able to shrug off the economic headwinds and beat their budgets. The changes in the valuations above reflect future expectations for these businesses, in the light of their trading performance in 2022.

The Policolor Group managed to generate a 7.4% year-over-year increase in sales, from € 79.4m in 2021 to € 85.3m in 2022, helped by the resins division whose sales were 24.1% above 2021. However, the Group's gross margin shrank from 28.8% in 2021 to 24.5%, mainly due to the Coatings division not having the pricing power to enable it to implement price increases sufficiently quickly to compensate for the steep increase in raw material and energy prices. Mainly due to this, in spite of significant cost savings in administration and logistics costs, the Group's recurring EBITDA of € 2.6m was 37.6% lower year-on-year and 56.2% below budget. Policolor's management believes that the price increases implemented throughout 2022 will result in an improved gross margin in 2023, and the 2023 Group budget targets much higher recurring EBITDA of € 4.7m.

In 2022, Mamaia Resort Hotels achieved record results, with operating revenues of € 4.0m, 29.5% above budget and 32.4% above 2021, driven by a higher occupancy rate as the Hotel managed to secure more group occupancy contracts in the off-season. The Hotel's EBITDA was € 0.7m, 77.3% above budget and 72.1% higher year-on-year. The Hotel's 2023 budget targets operating revenues of € 4.0m, in line with 2022, and an EBITDA of € 0.5m, lower than in 2022 due to strong inflationary pressures on the costs side.

Also, Telecredit had another high-growth year. In 2022, the Company deployed € 28.5m in financing products to small and medium-sized enterprises, generating Operating profit before depreciation and interest expenses of € 0.7m, 78% higher than 2021 and 48% above budget. Telecredit's 2023 budget targets a 31.7% increase in interest revenues, based on € 36.3m of funds deployed. The company's target for 2023 is to reach Operating profit before depreciation and interest expenses of € 0.9m.

During the fourth quarter, RC2 received a € 0.08m dividend from Policolor and the same amount from Mamaia Resort Hotels. In order to meet its operating costs for 2023, RC2 also contracted an € 0.8m loan from Mr. Ion Florescu, a substantial shareholder of the Fund, of which €0.25m was drawn at year-end. At the end of December, RC2 and RC2 (Cyprus) Ltd had cash and cash equivalents of € 0.2m, receivables of € 0.05m, and short-term liabilities of € 0.38m.

Yours truly,

New Europe Capital

Policolor Group

Background

RC2 has a 40.0% shareholding in Policolor, the parent company of the Policolor Group (“Policolor” or the “Group”), which operates along the following business lines: coatings (architectural, automotive and industrial), resins and specialty chemicals. The Romanian company Policolor SA and its 100%-owned Bulgarian subsidiary Orgachim AD produce and sell coatings, primarily in Romania and Bulgaria. The Group also includes Orgachim Resins, a producer of resins, and Ruse Chemicals, a producer of anhydrides, both being located in Bulgaria.

Group Financial results and operations

(EUR '000)	2021*	2022B	2022A**	2023B
Group Consolidated Income statement				
Sales revenues	**79,382**	**90,008**	**85,252**	**92,906**
sales growth year-on-year	*23.8%*	*13.4%*	*7.4%*	*9.0%*
Other operating revenues	210	4	559	-
Total operating revenues	**79,592**	**90,012**	**85,811**	**92,906**
Gross margin	22,954	25,123	20,991	24,570
Gross margin %	*28.8%*	*27.9%*	*24.5%*	*26.4%*
Other operating expenses	(21,350)	(21,409)	(20,614)	(22,888)
Operating profit	**1,604**	**3,714**	**377**	**1,683**
Operating margin	*2.0%*	*4.1%*	*0.4%*	*1.8%*
EBITDA	**4,190**	**5,971**	**2,615**	**4,653**
EBITDA margin	*5.3%*	*6.6%*	*3.0%*	*5.0%*
Nonrecurring items / Extraordinary Items	-	-	(66)	-
Financial Profit/(Loss)	(590)	(397)	(447)	(924)
Profit before tax	**1,014**	**3,317**	**(136)**	**759**
Income tax	(299)	(464)	-	-
Profit after tax	**715**	**2,853**	**(136)**	**759**
avg exchange rate (RON/EUR)	*4.92*	*4.95*	*4.92*	*4.92*

*Note: * IFRS audited, IFRS ** unaudited*

The Policolor Group achieved a 7.4% year-on-year increase in sales in 2022, which at € 85.3m were still 5.3% below budget. Helped mainly by the positive results achieved by the Bulgarian Coatings division, coatings sales increased by 8.1%, whilst the Resins division continued its strong growth trend and generated sales of € 30.7m, 24.1% higher year-over-year and 20.6% above budget. Sales of anhydrides were constrained by difficulties in accessing orthoxylene, the main raw material in anhydrides production, after the EU banned imports from Russia in June, and fell to 9.7m, 16.5% lower than the prior year.

The main reason the group failed to meet its EBITDA target of € 6m for 2022, is that the Coatings division did not have the pricing power to enable it to implement price increases sufficiently quickly to compensate for the steep increase in raw material and energy prices which took place over the year. This resulted in the Group’s gross margin shrinking from 28.8% in 2021 to 24.5% in 2022. Mainly due to this, the Group’s recurring EBITDA came in at € 2.6m, 37.6% lower year-on-year and 56.2% below budget, even though the Resins division outperformed the budget and the prior year in terms of profitability.

Prospects

The 2023 budget targets 9.0% sales growth to reach € 93m and assumes that the coatings division manages to significantly improve its gross margin, helping the Group’s gross margin reach 26.4%, which although two percentage points above 2022, would still be below the historical average. The improvement in the gross margin is expected to help the Group achieve a 78% increase in recurring EBITDA to € 4.7m.

Notwithstanding the difficulties experienced with the gross margin in 2022, the Group has continued to implement its turnaround plan, and over 2022-23 is implementing a new ERP, as well as extending and automatizing its Bucharest factory. The total Group capex envisaged for 2023 amounts to € 6.3m.

Mamaia Resort Hotels

Background

Mamaia Resort Hotels SRL (the “Company”) is the owner and operator of the ZENITH – Conference & Spa Hotel (the “Hotel”) in Mamaia, Romania’s premium seaside resort next to the city of Constanta. RC2 owns 63% of the Company, with the remaining 37% being owned by a Romanian private individual.

Financial results and operations

(EUR '000)	2021*	2022B	2022A**	2023B
Total Operating Revenues, of which:	**2,996**	**3,064**	**3,967**	**3,986**
Accommodation revenues	1,732	1,654	2,433	2,146
Food & beverage revenues	1,084	1,321	1,347	1,710
Other operating revenues	179	89	187	129
Total Operating Expenses	(2,748)	(2,749)	(3,332)	(3,572)
Operating Profit	**248**	**314**	**636**	**413**
Operating margin, %	*8.3%*	*10.3%*	*16.0%*	*10.4%*
EBITDA	**416**	**404**	**716**	**493**
EBITDA margin, %	*13.9%*	*13.2%*	*18.1%*	*12.4%*
Profit after Tax	**90**	**196**	**435**	**271**
Net margin, %	*3.0%*	*6.4%*	*11.0%*	*6.8%*
avg exchange rate (RON/EUR)	*4.92*	*4.95*	*4.92*	*4.92*

*Note: * RAS audited, ** RAS management accounts, unaudited*

Despite the challenging macroeconomic context and a difficult year for Black Sea operators, as some Romanian holidaymakers took the opportunity to travel abroad after two years of Covid related travel restrictions, whilst others avoided the Black Sea area due to the conflict in neighbouring Ukraine, the Hotel’s 2022 operating revenues of € 4.0m were 29.5% above budget and 32.4% above 2021, driven by a 49% occupancy rate, much higher than both the budgeted 28%, and the 40% achieved the prior year. The high occupancy rate was helped by a number of long-term group occupancy contracts which started in the off-season and continued at varying levels into the autumn. Accommodation revenues increased by 40.5% to € 2.4m, while Food & Beverage revenues were € 1.3m, 24.2% higher year-over-year but only 2% above budget, as tourists reduced their spending due to the cost of living crisis.

The full-year EBITDA of € 0.7m was 77.3% above budget and 72.1% higher year-over-year, mainly due to the higher revenues, whilst operating expenses were 21.2% above budget, as a result of cost increases and the higher occupancy rate. The net income of € 0.44m compares to a budgeted € 0.2m and was helped by Covid-related subsidies of € 0.03m received during the year. The Hotel's net debt fell from € 2.1m at the end of 2021 to € 1.8m at year end.

Prospects

The 2023 budget targets revenues of € 4.0m, in line with 2022, the result of a lower occupancy rate but a higher average room tariff, and higher F&B revenues. However, due to inflationary pressures on the costs side, the budget's EBITDA target of € 0.5m is 31% lower than the number achieved in 2022.

Telecredit

Background

Telecredit IFN S.A. ("Telecredit" or the "Company") is a Romanian Non-Banking Financial Institution ("IFN") whose main activity is providing factoring, discounting, and microloans to small and medium-sized companies ("SMEs"). RC2 owns an 85% shareholding, with the balance of 15% being owned by the Company's CEO, Elisa Rusu.

Financial Results and operations

(EUR '000)	2021*	2022B	2022A**	2023B***
Income Statement				
Interest revenues from SMEs lending, of which:	**1,093**	**1,389**	**1,625**	**2,141**
Factoring and Discounting	1,029	1,339	1,606	2,109
Microloans	64	50	19	32
Total operating expenses:	**697**	**(878)**	**(920)**	**(1,234)**
Provisions, of which:	21	(40)	27	(124)
Pay day lending	58	24	32	-
SMEs lending	(37)	(64)	(5)	(124)
Other Operating expenses	(718)	(838)	(948)	(1,110)
Operating profit before depreciation and interest expenses	**396**	**511**	**705**	**907**
Depreciation	(98)	(127)	(93)	(173)
Operating profit before interest expenses (EBIT)	**298**	**384**	**612**	**734**
EBIT margin, %	*27.3%*	*27.7%*	*37.7%*	*34.3%*
Profit after tax	**82**	**60**	**255**	**269**
net margin %	*7.5%*	*4.3%*	*15.7%*	*12.6%*
Avg exchange rate (RON/EUR)	*4.95*	*4.95*	*4.92*	*4.92*

*Note: * RAS audited, ** RAS unaudited management accounts, ***IFRS*

In spite of the difficult macroeconomic conditions, Telecredit had another high-growth year, generating interest revenues of € 1.6m, 17% above budget and 47% higher than the prior year, and an Operating profit before depreciation and interest expenses of € 0.7m, 78% above 2021 and 48% above budget.

The outstanding performance was the result of financing volumes reaching € 28.5m, 50% above the € 19m achieved in 2021, and 14% above budget. The value of the financing book was € 4.1m at the end of 2022, almost all made up of factoring and discounting operations, with only € 0.02m of microloans.

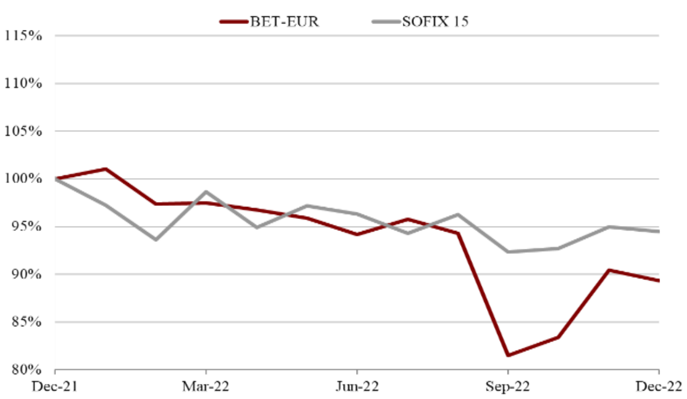
The non-performing loan (NPL) rate (defined as the balance of receivables over 90 days overdue divided by the gross book value of the portfolio) was 6.4% at the end of December 2022, slightly up on 6.1% at the end of 2021. Out of the 6.4% NPL rate, 2.2% was generated in 2022, with the balance of 4.2% having been generated in prior years. At the end of 2022, total debt amounted to € 3.4m, slightly below the € 3.5m recorded at year end 2021.

Prospects

Telecredit's 2023 budget aims for a 31.7% year-on year-increase in interest revenues, based on € 36.3m of funds deployed. Management aims to achieve this by a combination of organic growth and the launch of a new supply chain financing product; both of which to be supported by a 161% increase in marketing expenses. Overall, the Company is targeting an operating profit before depreciation and interest expenses of € 0.9m, compared to € 0.7m in 2022.

Capital Market Developments

BET Index and SOFIX Index 1 year performance



Commentary

During the fourth quarter, the Romanian BET and the Bulgarian SOFIX 15 indices gained 9.7% and 2.3%, respectively, both in euro terms. Over the same quarter, the MSCI Emerging Market and S&P indices were down by 0.2% and 2.1%, respectively, while the MSCI Emerging Market Eastern Europe and the FTSE100 indices were up by 26.3% and 7.4%, respectively. Over 2022, the BET-EUR and SOFIX 15 indices fell by 10.6% and 5.5%, respectively, both in euro terms. By comparison, the MSCI Emerging Market, the MSCI Emerging Market Eastern Europe, the FTSE100, and the S&P indices fell by 17.5%, 81.8%, 4.1%, and 14.4%, respectively, over the same period.

Macroeconomic Overview

Overview

	RO	as of:	BG	as of:
GDP Growth (y-o-y)	4.8%	FY22	3.4%	FY22
Inflation (y-o-y)	16.4%	Dec-22	16.9%	Dec-22
Ind. prod. growth (y-o-y)	-7.1%	Dec-22	2.1%	Dec-22
Trade balance (EUR bn)	-34.1	FY22	-7.4	FY22
y-o-y change	*44%*		*76%*	
FDI (EUR bn)	1.8	FY22	2.4	FY22
y-o-y change	*-60%*		*49%*	
Budget balance/GDP	-5.7%	FY22	-2.9%	FY22
Total external debt/GDP	49.8%	Dec-22	52.1%	Dec-22
Public sector debt/GDP	47.2%	Dec-22	22.9%	Dec-22
Loans-to-deposits	70.5%	Dec-22	69.3%	Dec-22

Commentary

Romania

In spite of the war in Ukraine which added fuel to the already high inflationary pressures, rising interest rates and supply chain disruptions, Romania's economic output grew by 4.8% year-on-year in 2022 according to the National Institute of Statistics, making it the fourth fastest growing economy in the EU. During the fourth quarter, Romania's GDP grew by 4.9% year-on-year, which follows revised year-on-year growth of 4.6% over the third quarter. Among the aggregates that contributed to Romania's positive GDP evolution in 2022, are household consumption which grew by 6.6%, services (+13.2%), and the construction sector whose output grew by 8.8%, whilst the agriculture and industrial sectors fell by 11.6% and 2.3%, respectively. For 2023, the EU Commission expects Romania's GDP growth to slow down to 2.5% in the context of ongoing macroeconomic headwinds.

The war in Ukraine triggered an energy and food crisis which brought inflationary pressures to levels last seen in Europe decades ago. At the end of December, Romania's inflation rate reached 16.4%, having remained in double-digits throughout the year. Due to rapidly rising European gas and electricity prices, in order to protect the most vulnerable consumers, the Romanian government capped the price of electricity for low-consumption households at € 0.16/KWh. and at € 0.20/KWh for SMEs, whilst the price of gas was capped at € 0.06/KWh for households, and at € 0.08/KWh for SMEs with an annual consumption of under 50,000 MWh.

In response to the high inflation, the National Bank of Romania increased its monetary policy rate from 1.75% and the end of 2021 to 6.75% at the end of 2022. Helped by the strong hikes in interest rates, the Romanian leu appreciated by 0.54% against the euro over the year.

The concerns about a possible energy blackout in Europe eased as the winter progressed, as European countries managed to boost their reserves by replacing much of Russian gas supplies with alternative suppliers, and the weather turned out to be milder than the seasonal norm. Romania also started the exploitation of a new offshore gas field in 2022, with an estimated annual production capacity of 1bn cubic meters, equivalent to 10% of Romania's consumption.

In 2022, the trade gap increased by 44% (from € -23.7bn to € -34.1bn), with exports growing by 23.1%, while imports grew by 28.1% from an already larger base. FDI inflows over 2022 amounted to € 1.8bn, 60% lower than the € 4.2bn recorded in 2021, with total equity investment amounting to € 7.9bn, and intra-group loans amounting to € 2.8bn.

Romania posted a budget deficit of € -16.4bn over the year, or 5.7% of GDP, compared to 6.7% over 2021. At € 93bn, budgetary receipts were 21.2% higher, mainly due to a 25.0% increase in revenues generated by taxes on income and salaries, an 18.6% increase in VAT proceeds, and a 14.8% increase in revenues generated by excise duties. The budgetary receipts were helped by inflation which increased the taxable base. Total budgetary expenses increased by 17.5% in EUR terms, from € 93.4bn to € 109.7bn, with personnel and social expenditures, which accounted for 20.5% of total expenses, growing by 12.7%. As a result of the tightening monetary policy, interest expenses increased by 61.8% to € 5.9bn. The average yield of a 10-year Romanian Government Bond increased from 5.06% at the end of December 2021 to 7.75% at the end of December 2022. Of the budgetary expenses, € 3.6bn was agricultural subsidies and compensations for higher energy prices.

In 2022, Romania received € 6.3bn from the EU under its EU-approved € 29bn Recovery and Resilience Plan. For 2023, the Romanian government expects to receive a further € 6.1bn to support the development of key sectors such as public infrastructure, agriculture, digital transformation, and green energy. As the Romanian Government has not managed to implement on time certain commitments it made under the plan, especially those related to pensions reform and a new "whistle-blower" law, its second payment request of € 3bn is at risk of being postponed.

Romania's total external debt amounted to € 142.7bn at the end of 2022, approximately 49.8% of GDP, which represents a 6.5% year-on-year increase. Public debt has also continued to grow, having reached € 135bn, or 47.2% of GDP, at the end of December, up 15.2% over the year in nominal EUR terms.

After several years of continuous expansion, lending activity contracted during the fourth quarter, with total domestic non-governmental credit (which excludes loans to financial institutions), amounting to € 73.9bn at year end, down 0.3% in

RON terms over the quarter. Household loans reached € 34.8bn at the end of December, having fallen by 0.8% over the quarter, and accounted for 47.2% of total loans outstanding at year-end. Consumer loans, which account for 38.1% of household loans, fell by 2.2% over the quarter. Housing loans were almost unchanged over the quarter and accounted for 61.9% of household loans. At the same time, corporate loans reached € 35.9bn at the end of December, down 0.4% over the quarter. The NPL ratio was 2.7% at the end of December, down from 2.8% at the end of September. On the other hand, the overall deposit base has continued to expand, reaching € 104.3bn at the end of December, which is 4.4% higher than at the end of September.

Bulgaria

In spite of internal political instability and its greater dependence on Russian energy, Bulgaria's economy grew by 3.4% year-on-year (compared to 4.2% in 2021), underpinned by strong private consumption and robust exports growths. For 2023, the European Commission is estimating 1.4% GDP growth, almost double the expected EU average of 0.8%.

Over the year, the Bulgarian economy faced soaring energy and food prices, supply difficulties for certain raw materials, and growing uncertainties given the country's dependence on Russian gas. On 27 April, when Bulgaria was still nearly 90% dependent on Russian gas, Russia suspended its supplies to Bulgaria. In order to mitigate the shortage, a new pipeline connection with Greece, allowing greater imports from Azerbaijan, became operational in October.

In order to protect low-income households from rising energy prices, the Bulgarian government capped the price of electricity for households at the level of July 2021. The Government also decided to support companies by compensating 80% of the costs of electricity above € 100 per MWh until December 2023. On the other hand, its compensation for the increase in natural gas prices was stopped at the end of June 2022.

Bulgaria's inflation rate reached 16.8% at the end of December 2022, compared with 18.7% at the end of the previous quarter, when it peaked.

At the end of 2022, Bulgaria posted a budget deficit of approximately € 2.9bn, or 2.9% of GDP, compared to a 3.9% deficit over the prior year. Total budgetary revenues increased by 13% over 2022, with tax and social security contributions growing by 15.9%. On the other hand, total budgetary expenses grew by 15.7%, mainly due to a 10% increase in salaries and social expenditures, a 47% increase in goods and services, and a 200% increase in public investments. In spite of pressures from businesses to receive greater compensation for the sharp increase in energy prices, the value of subsidies fell by 9% in 2022.

Bulgaria's public sector debt increased from € 18.3bn at the end of September to € 18.9bn at the end of December and is now approximately 22.9% of GDP. Gross external debt amounted to € 43.9bn, or 52.1% of GDP, at the end of December, having increased by 5.9% over the year.

Bulgaria's 2022 trade deficit of € -7.4bn was significantly worse than the € -4.4bn recorded over the prior year. Exports increased by 36.6%, and imports by 40.8%. The trade deficit was counter-balanced by a € 4.3bn surplus from services, and primary and secondary incomes, resulting in a current account deficit of € 0.6bn, lower than the € 1.3bn deficit of 2021. FDI inflows amounted to € 2.4bn during the year, compared to € 1.3bn in 2021.

Total domestic non-governmental credit (which excludes loans to financial institutions) increased from € 40.3bn at the end of September to € 41.2bn at the end of December, with corporate loans growing by 1.9%, whilst household loans grew by 2.3%. The deposit base was € 59.4bn at the end of December, up 4.3% from € 56.9bn at the end of the previous quarter. The NPL rate was 3.2% at the end of December, down from 3.4% at the end of September.

Bulgaria continues to suffer from political instability. After the collapse of the coalition government led by the pro-EU anti-corruption reformist Kiril Petkov in June, a new round of elections was scheduled for 2 October. The results of the 4th parliamentary vote in two years were again unconclusive, and a new round of elections was held on 2 April 2023.

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