Reconstruction Capital II Ltd

("RC2" or the "Fund")

Quarterly Report

30 September 2017

neweuropecapital

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Statistics

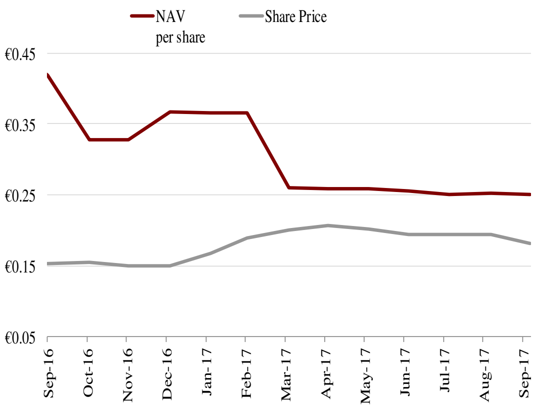
NAV per share (€)	0.2512
Total NAV (€ m)	36.8
Share price (€)	0.1813
Mk Cap (€ m)	26.6
# of shares (m)	146.5
NAV/share since inception†	-50.11%
12-month NAV/share perfomance	-40.17%
NAV/share annualized Return*†	-5.75%
NAV/share annualized Volatility*†	17.71%
Best month (NAV/share)*†	13.98%
Worst month (NAV/share)*†	-28.27%
# of months up (NAV/share)*†	73
# of months down (NAV/share)*†	68

** since inception † assumes pro-rata participation in the 2008 share buy-back and the 2017 return of capital*
Note: € 17m returned to shareholders in 2017

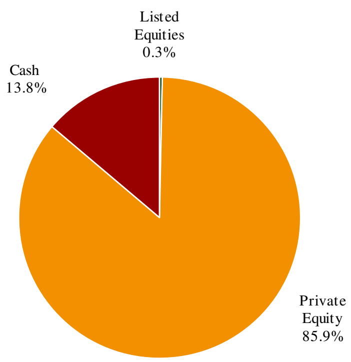
RC2 NAV returns

	2014	2015	2016	2017
Jan	-0.65%	-0.07%	8.03%	-0.26%
Feb	-0.34%	-0.34%	1.22%	-0.21%
Mar	2.94%	-0.70%	-0.66%	-28.75%
Apr	2.73%	0.93%	-0.49%	-0.31%
May	2.70%	3.11%	3.09%	-0.23%
Jun	0.28%	-0.38%	1.18%	-1.02%
Jul	0.44%	3.24%	6.83%	-1.84%
Aug	3.23%	-0.85%	2.11%	0.10%
Sep	0.01%	0.31%	-8.63%	-0.26%
Oct	1.87%	-0.35%	-21.79%	
Nov	0.15%	3.17%	-0.24%	
Dec	0.73%	-8.47%	12.06%	
YTD	14.91%	-0.94%	-1.75%	-31.57%

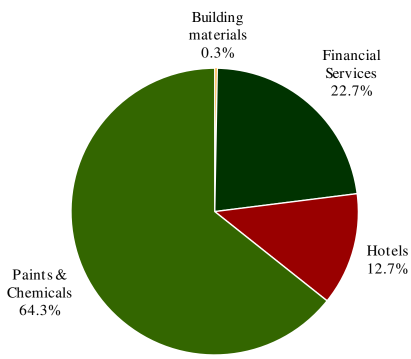
Share price / NAV per share (€)



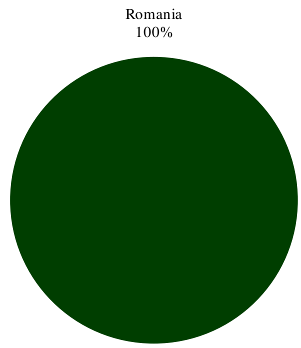
Portfolio Structure by Asset Class



Equity Portfolio Structure by Sector



Portfolio Structure by Geography



Message from the Adviser

Dear Shareholders

During the third quarter, RC2's total NAV fell by € 0.7m, and its NAV per share by 2.0% from € 0.2563 to € 0.2512, mainly due to various closing adjustments related to the exit process from the Top Factoring Group.

Policolor's paints and coatings sales grew by over 5% during the first nine months of 2017, with its EBITDA coming in 21.1% below budget at € 3.6m, mainly due to underperformance at the Resins division which was particularly badly affected by raw material price increases.

Mamaia Resort Hotels achieved a good occupancy rate of 77% over the summer months, compared to a budgeted 75%, but increasing competition from AIRBNB-type short-term holiday lets has had a downward effect on the average net tariff, which, combined with an increase in salary costs, has resulted in the nine-month EBITDA coming in approximately € 0.3m below budget at € 0.64m.

As provided in the acquisition contract signed in March 2017, Glasro effected a € 0.15m capital increase in Telecredit in August, thereby bringing its shareholding in the Company at 80% for a total investment of € 2.85m. Telecredit has granted 25,100 loans with a total value of € 3.7m over the first nine months of 2017, and the net value of its loan book amounted to € 0.53m at the end of the September.

At the end of the quarter, the Fund had cash and cash equivalents of approximately € 5m, a further € 4.5m of cash in Glasro, and liabilities of € 0.5m, of which € 0.15m represents outstanding B Class share redemptions, and € 0.19m represents sundry liabilities related to the exit from Top Factoring.

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 form the largest producer of coatings in Romania and Bulgaria. The Group also includes Orgachim Resins, the leading supplier of resins in South East Europe, and Ruse Chemicals, a producer of anhydrides. All the Group companies are unlisted.

Group Financial results and operations

(EUR '000)	2015*	2016**	2017B	9M 16	9M 17	9M 17B
Group Consolidated Income statement						
Sales revenues	**56,935**	**58,722**	**63,869**	**47,839**	**50,779**	**53,907**
sales growth year-on-year	*6.1%*	*3.1%*	*8.0%*	*3.0%*	*6.1%*	*12.7%*
Other operating revenues	356	160		1,041	657	(303)
Total operating revenues	**57,291**	**58,882**	**63,869**	**48,879**	**51,436**	**53,604**
Gross margin	19,807	20,577	24,175	17,315	18,129	20,255
Gross margin %	*34.6%*	*34.9%*	*37.9%*	*35.4%*	*35.2%*	*37.8%*
Total operating expenses	**(59,092)**	**(60,923)**	**(63,717)**	**(48,312)**	**(50,193)**	**(51,590)**
Operating profit	**(1,801)**	**(2,041)**	**152**	**567**	**1,243**	**2,014**
Operating margin	*-3.6%*	*-3.5%*	*0.8%*	*1.2%*	*2.4%*	*3.8%*
EBITDA	**2,089**	**1,219**	**3,452**	**2,989**	**3,624**	**4,592**
EBITDA margin	*3.6%*	*2.1%*	*5.4%*	*6.1%*	*7.0%*	*8.6%*
Net extraordinary result - land sale	204	(668)	655	3,643	5,320	(63)
Financial Profit/(Loss)	(1,147)	(1,023)	(1,000)	(1,043)	(1,660)	(776)
Profit before tax	**(2,744)**	**(3,732)**	**(194)**	**3,167**	**4,903**	**1,176**
Income tax	(31)	(279)	(579)	(368)	(494)	-
Profit after tax	**(2,775)**	**(4,011)**	**(773)**	**2,799**	**4,409**	**1,176**
avg exchange rate (RON/EUR)	*4.44*	*4.49*	*4.50*	*4.49*	*4.55*	*4.50*

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

The Group generated consolidated operating revenues of € 51.4m in the first nine months of 2017, 4% below budget but 5.2% above the same period of 2016. The Group's consolidated results reflect a good performance by the paints and coatings business, and lower than expected sales of resins by volume due to price increases triggered by increased raw materials costs. The anhydrides division prioritized the Group's internal needs and only made opportunistic sales to third parties. Overall, sales of paints and coatings grew by 5.6% year-on-year, and sales of resins were up 13.3% year-on-year, but 7.4% below the budget.

The Group generated EBITDA of € 3.6m, up 21.2% compared to the previous year, but 21.1% below budget, mainly due to the negative impact of raw material cost increases at the resins division.

Real Estate

In May, Policolor signed a pre-contract for the sale of its main Bucharest site where its current Romanian production plant is located to a Romanian real estate development company for a total price of € 22m, of which € 4.5m was received at signing. A further € 6.9m was received in June, when Policolor sold approximately half the site. Policolor is due to further receive € 0.7m in the summer of 2018 and € 9.9m in June 2019, when it is due to deliver the remaining land.

Net Debt

The Group's total net debt amounted to € 15.7m at the end of September, slightly up on € 15.3m at the end of June.

Mamaia Resort Hotels

Background

Mamaia Resort Hotels SRL (the "Company") is the owner and operator of the now re-branded ZENITH – Conference & Spa Hotel (the "Hotel"), which is located in Mamaia, Romania's premium seaside resort next to the city of Constanta. In March 2008, RC2 acquired 63% of the Company, with the remaining 37% being owned by a Romanian private individual.

Financial results and operations

(EUR '000)	2015*	2016*	2017B	9M16**	9M17**	9M17B
Income Statement						
Total Operating Revenues	**2,349**	**2,337**	**2,751**	**2,242**	**2,336**	**2,571**
Total Operating Expenses	(2,044)	(2,200)	(2,148)	(1,738)	(1,818)	(1,707)
Operating Profit	**305**	**137**	**603**	**504**	**518**	**864**
Operating margin	*13.0%*	*5.9%*	*21.9%*	*22.5%*	*22.2%*	*33.6%*
EBITDA	**484**	**353**	**783**	**631**	**637**	**909**
EBITDA margin	*20.6%*	*15.1%*	*28.5%*	*28.2%*	*27.3%*	*35.4%*
Profit after Tax	**176**	**40**	**651**	**376**	**442**	**829**
Net margin	*7.5%*	*1.7%*	*23.7%*	*16.8%*	*18.9%*	*32.2%*
Avg exchange rate (RON/EUR)	*4.44*	*4.49*	*4.50*	*4.49*	*4.55*	*4.50*

*Note: *RAS (audited), **RAS (management accounts)*

The Hotel generated operating revenues of € 2.3m over the first nine months of 2017, up 4.2% year-on-year, but 9.1% below budget, mainly due to lower than budgeted sales in May and August.

Although the 35.4% occupancy rate over the first nine months of 2017 was higher than the 33.2% achieved over the same period of 2016, and the occupancy rate over the summer months reached 77%, compared to a budgeted 75%, the hotel suffered a downward pressure on room tariffs, with the average tariff falling from € 36 to € 34. This is mainly the result of the Romanian seaside hotel industry facing stiff and increasing competition from AIRBNB-type short term holiday lets, with many new flats having been developed which are cheaper to rent than the conventional accommodation packages offered by hotels. Over the past few years there has been a construction boom in the northern Mamaia area, with some 6,000 new accommodation units having been finalized over the past year alone.

Accommodation revenues amounted to € 1.2m over January-September 2017, and accounted for 50% of total revenues, whilst the food & beverage department generated revenues of € 1.0m, or 43% of overall revenues over the period.

The nine-month EBITDA of € 0.64m was well below the budgeted € 0.91m, and virtually unchanged compared to the same period last year. Apart from the pressure on tariffs, the Hotel is facing continued upward pressure on the salaries side due to a chronic shortage of labour of all types, compounded by the Romanian government's policy of increasing the minimum wage.

Telecredit

Background

RC2's wholly-owned subsidiary Glasro Holdings Ltd owns an 80% shareholding in Telecredit IFN S.A. ("Telecredit" or the "Company"), a Romanian non-banking financial institution that provides consumer loans to individuals. The balance of 20% is owned by RC2's former partner in Top Factoring and his family.

Financial Results

EUR'000	2015*	2016*	2017B	9M16**	9M17**	9M17B
Income Statement						
Total interest revenues	**441**	**1,020**	**1,799**	**716**	**1,170**	**1,279**
Total operating expenses	**(233)**	**(550)**	**(1,085)**	**(557)**	**(1,038)**	**(1,058)**
Operating profit (before depreciation)	48	220	309	159	132	220
Operating profit (after depreciation)	**43**	**211**	**291**	**153**	**118**	**207**
Operating profit (after depreciation) margin	*9.8%*	*20.6%*	*16.2%*	*21.4%*	*10.1%*	*16.2%*
Financial result	(4)	(4)		(3)	(2)	
Profit before tax	39	207		150	116	
Profit after tax	**36**	**175**		**126**	**92**	
Avg exchange rate (RON/EUR)	*4.445*	*4.491*		*4.485*	*4.551*	

*Note: * RAS (audited), ** RAS (unaudited)*

Telecredit generated revenues of € 1.2m over the first nine months of 2017, up 63.4% year-on-year, but 8.5% below budget. The Company operating profit over the first nine months of 2017 amounted to € 0.12m compared to € 0.15m over the same period of 2016, mainly due to increased promotion and marketing expenses generated by a TV campaign with a limited run which was launched in February 2017 to improve the general awareness of the Company.

As at 30 September, the net value of Telecredit's loan book was € 0.53m, including accrued interest of € 0.08m. 74% of the loan stock was represented by standard loans (with days past due between 0-15), whilst 1% of the loan stock was represented by non-performing loans ("NPLs"). Telecredit sells its NPLs to a debt collection company on a monthly basis.

Operations

Over January-September 2017, the Company granted 25,100 loans with a total value of € 3.7m.

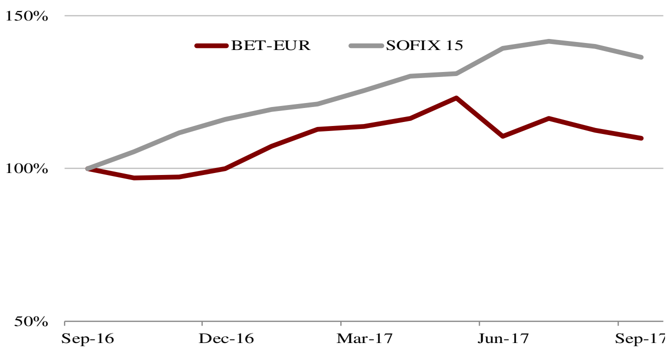
As provided in the acquisition contract signed in March 2017, Glasro made a € 0.15m capital increase in Telecredit in August, thereby bringing its shareholding in the Company to 80%.

The National Bank of Romania has passed a new regulation which came into force on 1 October, which requires non-banking financial institutions ("NFIs") such as Telecredit which make loans above a certain interest rate threshold to a have minimum regulatory capital equal to 66% of loans granted over a specific month.

Currently, Telecredit's equity amounts to € 0.9m (including the recent € 0.15m capital increase), and its current value of loans granted per month amounts to approximately € 0.4m, so it has sufficient capital to easily support its current lending activities. However, the new regulation could limit its future growth. Based on its current capital, the maximum amount of loans it can grant in a given month is capped at € 1.3m.

Capital Market Developments

BET-EUR and SOFIX-15: 1 year performance



Commentary

During the third quarter, the Romanian BET-EUR and the Bulgarian SOFIX 15 indices fell by 0.6% and 2.2%, respectively, both in euro terms. Over the same quarter, the MSCI Emerging Market Eastern Europe, the MSCI Emerging Market, the FTSE100 and the S&P indices were up by 8.9%, 3.5%, 0.4% and 0.5%, respectively, all in euro terms.

Over the past year, the BET-EUR and SOFIX 15 indices were up by 9.9% and 36.4%, respectively, all in euro terms. By comparison, the MSCI Emerging Market Eastern Europe, the MSCI Emerging Market, the FTSE100 and the S&P indices gained 17.0%, 13.9%, 5.0% and 10.5%, respectively, all in euro terms.

Macroeconomic Overview

Overview

	RO	as of:	BG	as of:
GDP Growth (y-o-y)	5.8%	6M17	3.7%	6M17
Inflation (y-o-y)	1.8%	Sep-17	2.1%	Sep-17
Ind. prod. growth (y-o-y)	10.3%	Aug-17	4.9%	Aug-17
Trade balance (EUR bn)	-7.9	8M17	-1.4	8M17
y-o-y	*28.2%*		*107.0%*	
FDI (EUR bn)	2.5	8M17	0.5	8M17
y-o-y change	*-18.6%*		*-54.1%*	
Budget balance/GDP	-0.8%	9M17	2.4%	9M17
Total external debt/GDP	52.5%	Aug-17	66.1%	Aug-17
Public sector debt-to-GDP	41.7%	Aug-17	24.8%	Sep-17
Loans-to-deposits	81.3%	Sep-17	75.4%	Sep-17

Commentary

Romania

Romania's GDP grew by 5.9% in the second quarter compared to the same quarter of the previous year. Overall, GDP grew by 5.8% year-on-year during the first six months of 2016. With net exports having made a negative contribution to GDP growth, private consumption was the main growth driver having increased by 5.2% year-on-year in the first semester, while industry had a lower growth dynamic, having increased by 1.8% over the same period. In its latest report, the IMF has forecast Romania's overall 2017 GDP growth to come in at 5.5%.

Romania's inflation rate has continued its upward trend, coming in at 1.8% in September, up from -0.5% in December 2016. The higher inflation rate in September was the consequence of mounting inflationary pressures generated by increasing domestic demand and higher energy and oil prices.

The Romanian leu fell by 1% against the euro over the third quarter, and by 1.3% year-to-date. At the end of September, the leu hit its lowest point against the euro of the past five years. The forex rate has been affected by the mounting current account and budget deficits worries, and ongoing concerns about the government's attempts to restrict the independence of the judicial system and decriminalize certain corruption offences.

The budget deficit over the first nine months of 2017 came in at € 1.5bn, equivalent to -0.8% of GDP, compared to a deficit of -0.5% over the same period in 2016. Budgetary receipts increased by 8.8% year-on-year, triggered by higher social contributions and personal income taxes which grew by 13.9%, whilst VAT collections were 0.3% lower year-on-year. The receipts from corporate profit taxes fell by 6.2% year-on-year. On the other hand, total budgetary expenses increased by 10.5% year-on-year, from € 37.7bn to € 41.2bn, with personnel and social expenditures, which account for 63% of total expenses, increasing by 15.7% year-on-year. With most of the budgetary revenues being directed towards personnel and social expenditures due to a series of public sector salary and pensions increases, public investments have not been a priority for the Romanian government and amounted to only € 1.6bn over the first nine months of 2017, 20% below the same period of the prior year, and equivalent to only 0.9% of GDP.

Over the first eight months of 2017, the trade gap widened by 28.2% year-on-year (from € -6.1bn to € -7.9bn), as imports grew by 12.2%, driven by higher internal private consumption, while exports increased by 9.6%. The negative evolution of the trade balance was the main reason behind the € -4.0bn current account deficit, which is the equivalent to 2.2% of GDP and compares to a € -2.7bn deficit over the same period of 2016. Over the first eight months of 2017, FDI flows amounted to € 2.5bn, of which € 2.9bn were equity investments, whilst net intra-group loans amounted to a negative € -0.4bn. Overall, FDI flows were 18.6% lower year-on-year and covered only 62% of the current account deficit, compared to a 116% coverage ratio over the same period last year. Romania's total external debt was € 94.1bn at the end of August, which represents a 1.3% year-to-date increase and amounts to approximately 53% of GDP. Total public debt was € 76.6bn, or 41.7% of GDP, at the end of August, up 2.7% year-to-date in RON terms, driven by the growing budget deficit.

Total domestic non-governmental credit (which excludes loans to financial institutions) amounted to € 50.6bn at the end of September, and was up 5.7% year-to-date in RON terms. Corporate loans increased by 4.5% year-to-date, triggered by a 9% increase in corporate RON-denominated loans, whilst corporate euro-denominated loans fell by 0.4%. Corporate loans accounted for 46% of the total loan stock at the end of September, unchanged since the end of 2016. Household loans increased by 6.1% year-to-date in September, with housing loans growing by 9.3% while consumer loans increased by 3.4% since the beginning of the year, both in RON terms. The overall deposit base was € 62.3bn at the end of September, having increased by 4.4% year-to-date in RON terms. The NPL ratio was 8.3% at the end of June, down on the 9.6% recorded at the end of December 2016, as banks continued to clean their balance sheet through sales of NPLs.

Bulgaria

Bulgaria's second quarter GDP grew by 3.9% year-on-year, helped by individual consumption which increased by 5.7%, whilst exports increased by 13.7%. Overall, GDP grew by 3.7% year-on-year during the first six months of 2017. According to its latest report issued in October, the IMF is forecasting 3.6% overall GDP growth in 2017.

Bulgaria's inflation rate has been increasing over the quarter and reached 2.1% in September, compared to an inflation rate of 1.9% recorded in June.

Over the first nine months of 2017, Bulgaria achieved a budget surplus of € 1.2bn, or 2.4% of GDP, which compares to a 3.7% GDP surplus achieved over the same period of 2016. Tax revenues increased by 2%, from € 13.1bn to € 13.4bn, whilst total budgetary expenses increased by 6.4% from € 11.1bn to € 11.8bn, mainly triggered by higher personnel and social expenditures following an increase in pensions in July. Public sector investments fell by 9% year-on-year, from € 0.8m to € 0.7m, while gross external debt amounted to 66.1% of GDP as at the end of August, down from 73.1% at the end of 2016. Bulgaria's public sector debt fell by 8.3% year-to-date, from € 13.8bn to € 12.6bn, and amounted to 24.8% of GDP at the end of September, down from 29.1% at the end of 2016. The decrease was mainly due to the repayment of € 1bn of 5-year Eurobonds which matured in July.

Bulgaria's trade balance worsened from a € -0.7bn deficit over the first eight months of 2016 to a € -1.4bn deficit over the same period in 2017. While exports grew by an impressive 14.3%, the year-on-year increase in imports was even higher at 18.4%. Helped by a € 2.7bn surplus from services, the current account balance was € 2.3bn in surplus over the first eight months of 2017, slightly higher than the € 2.2bn surplus achieved in 2016 ago. FDI inflows amounted to € 0.5bn, 54.1% lower than over the same period of 2016.

Total domestic non-governmental credit (which excludes loans to financial institutions) amounted to € 26bn at the end of September, up 3.7% year-to-date. Total corporate and household loans increased by 2.6% and 5.4%, respectively. NPLs accounted for 11.5% of the overall loan stock at the end of September, which compares to 12.1% at the end of the previous quarter. The deposit base amounted to € 34.5bn at the end of September, up 4.3% year-to-date.

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