Reconstruction Capital II Ltd

(“RC2” or the “Fund”)

Quarterly Report

30 June 2020

neweuropecapital

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Statistics

NAV per share (€)	0.1428
Total NAV (€ m)	19.4
Share price (€)	0.1075
Mk Cap (€ m)	14.6
# of shares (m)	135.9
NAV/share since inception†	-61.44%
12-month NAV/share perfomance	-35.79%

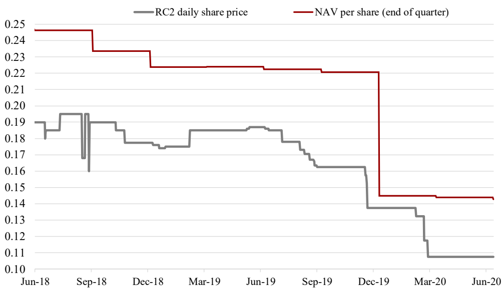
† assumes pro-rata participation in the 2008 share buy-back and the 2017 return of capital

RC2 Quarterly NAV returns

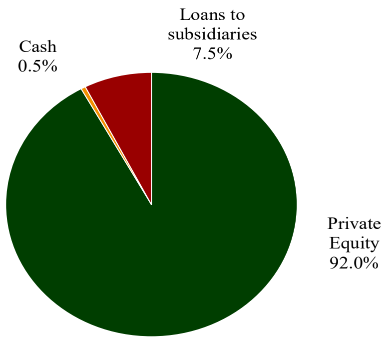
	2017	2018	2019	2020
1Q	-29.08%*	-0.51%	0.12%	-0.77%
2Q	-1.55%	-1.11%	-0.76%	-0.75%
3Q	-1.99%	-5.20%	-0.75%	
4Q	-0.32%	-4.17%	-34.31%	
YTD	-31.79%	-10.61%	-35.22%	-1.51%

** € 17m returned to shareholders in 1Q 2017*

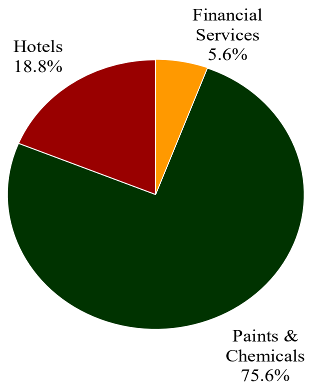
Share price / NAV per share (€)



Portfolio Structure by Asset Class



Equity Portfolio Structure by Sector



Message from the Adviser

Dear Shareholders

During the second quarter, RC2's total NAV fell by € 0.2m, and its NAV per share fell by 0.75% from € 0.1439 to € 0.1428, mainly due to the operating expenses incurred over the quarter.

The Romanian and Bulgarian governments took timely measures to contain the spread of Covid-19 when the numbers of cases and fatalities were still relatively low compared to Western Europe. Although these measures, which were stricter in Romania, seemed to have suppressed the pandemic, once the restrictions in both countries were gradually lifted in mid-May, the number of cases has been rising to worrying levels with Romania and Bulgaria posting two of the highest rates of new cases in South-East Europe. At the end of July, Romania and Bulgaria were reporting 100 and 70 Covid-19 active cases per 100,000 inhabitants, respectively, compared to 22 and 19 active cases at the end of May.

Boosted by a strong first quarter, the Policolor Group's January-June 2020 sales results were up 3.4% year-on-year, albeit 14% below budget. Sales of coatings were badly affected by the Covid pandemic, and related lockdown restrictions, during the month of April, whilst an IT failure in May affected the Group's ability to operate normally, affecting its sales during that month. In June, sales of coatings and resins recovered, making up some of the lost ground. Over the first half of 2020, the Policolor Group generated a recurring EBITDA (excluding revenues and expenses allocated to the real estate division) of € 2.0m, in line with the budget, helped by production efficiencies and operating cost savings.

Both Mamaia and Telecredit's operations have been badly affected by the Covid-19 pandemic, and both management teams have prepared revised budgets to reflect the estimated impact of the pandemic on their respective businesses this year.

Following the finalization of the second phase of the renovation works on its public areas, and due to the Romanian authorities re-allowing open air restaurants to operate, the Mamaia Hotel re-opened at the beginning of June. However, it is still not allowed to use its indoor restaurants, and is forced to restrict its food and beverage service to its outdoor terrace, where social distancing rules limit the number of customers. Management's revised 2020 budget for the Hotel envisages total revenues of € 2.0m instead of an originally planned € 3.2m, and a net loss of € -0.24 instead of an original estimated net profit of € 0.18m. In April, RC2 provided a € 0.3m loan to the Hotel to help finalize its planned renovation works. The loan was fully drawn by the end of May.

Telecredit deployed € 3.7m in financing products to small and medium sized enterprises in the first semester, generating an Operating Loss before Depreciation of € 0.2m due to increased provisions expenses, reflecting the difficulties small and medium-sized companies are currently facing due to the pandemic. Over the quarter, the company reimbursed € 0.3m of the € 1.5m loan RC2 provided to Telecredit in the second half of 2019.

At the end of June, RC2 and RC2 (Cyprus) Ltd had cash and cash equivalents of approximately € 0.1m, loan receivables from Telecredit and Mamaia Resort Hotels of € 1.5m, and short-term liabilities of € 0.1m.

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. All the Group companies are unlisted.

Group Financial results and operations

(EUR '000)	2018*	2019**	2020B***	6M 2019**	6M 2020**	6M 2020B***
Group Consolidated Income statement						
Sales revenues	**64,038**	**59,982**	**72,825**	**30,142**	**31,158**	**36,201**
sales growth year-on-year	*-1.7%*	*-6.3%*	*13.7%*	*-9.3%*	*3.4%*	*20.1%*
Other operating revenues	575	577		69	9	3
Total operating revenues	**64,613**	**60,560**	**72,825**	**30,211**	**31,168**	**36,205**
Gross margin	21,055	18,947	23,687	9,901	10,313	11,981
Gross margin %	*32.6%*	*31.3%*	*32.5%*	*32.8%*	*33.1%*	*33.1%*
Other operating expenses	(22,352)	(22,229)	(21,526)	(10,309)	(9,361)	(11,093)
Operating profit	**(1,297)**	**(3,282)**	**2,161**	**(408)**	**953**	**888**
Operating margin	*-2.0%*	*-5.4%*	*3.0%*	*-1.3%*	*3.1%*	*2.5%*
Recurring EBITDA	**1,884**	**887**	**4,160**	**817**	**2,027**	**1,952**
EBITDA margin	*2.9%*	*1.5%*	*5.7%*	*2.7%*	*6.5%*	*5.4%*
Net extraordinary result - land sale	1,706	2,057		(598)	(13)	-
Nonrecurring items including relocation	(620)	(1,749)	120	(512)	(1)	(100)
Financial Profit/(Loss)	(751)	(879)	(722)	(302)	(329)	(339)
Profit before tax	**(342)**	**(2,103)**	**1,439**	**(1,820)**	**610**	**449**
Income tax	(371)	(319)	(190)	-	-	-
Profit after tax	**(713)**	**(2,423)**	**1,249**	**(1,820)**	**610**	**449**
avg exchange rate (RON/EUR)	*4.65*	*4.75*	*4.75*	*4.74*	*4.82*	*4.75*

*Note: * IFRS audited, ** IFRS unaudited, *** Management's budget*

Following the good sales results in the first quarter, the Group's revenues were significantly below budget in the second quarter, with April sales negatively affected by the impact of the Covid pandemic and related lockdown, and May sales affected by an IT failure which severely affected the Group's ability to operate normally for a number of weeks. June was a much better month in terms of sales, and the Group ended the first half of the year with net sales approximately € 5 million below the budget (-14%).

The sales of coatings during the first half of the year amounted to € 23.3m, 1.8% higher than in the same period last year, but 13.1% below budget. Sales of resins (including sales to Group companies) amounted to € 8.1m, unchanged year-on-year and 5% below budget, whilst sales of anhydrides (including sales to Group companies) reached € 2m, 42% below the budget, due to the anhydrides plant having stopped working at the end of March due to limited availability of the main raw material at commercially viable prices.

In spite of the lower sales, over the first half of 2020, the Policolor Group generated a recurring EBITDA (excluding revenues and expenses allocated to the real estate division) of € 2.0m, in line with the budget, helped by production efficiencies and a favourable mix of products sold and operating cost savings.

Mamaia Resort Hotels

Background

Mamaia Resort Hotels SRL (the "Company") is the owner and operator of the ZENITH – Conference & Spa Hotel (the "Hotel"), located 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)	2019†	2020B*	2020E**	6M 2019***	6M 2020A***	6M 2020E**
Income Statement						
Total Operating Revenues, of which:	**2,964**	**3,212**	**2,033**	**735**	**199**	**172**
Accommodation revenues	1,627	1,854	1,335	366	117	85
Food & beverage revenues	1,127	1,191	635	319	66	76
others	210	167	63	51	16	11
Total Operating Expenses	(2,921)	(2,939)	(2,179)	(1,261)	(871)	(863)
Operating Profit	**43**	**273**	**(146)**	**(526)**	**(672)**	**(692)**
Operating margin	*1.5%*	*8.5%*	*neg.*	*neg.*	*neg.*	*neg.*
EBITDA	**195**	**423**	**1**	**(450)**	**(600)**	**(619)**
EBITDA margin	*6.6%*	*13.2%*	*0.1%*	*neg.*	*neg.*	*neg.*
Profit after Tax	**(55)**	**183**	**(243)**	**(540)**	**(659)**	**(732)**
Net margin	*neg.*	*5.7%*	*neg.*	*neg.*	*neg.*	*neg.*
Avg exchange rate (RON/EUR)	*4.75*	*4.80*	*4.85*	*4.74*	*4.82*	*4.85*

*Note: † RAS audited, * original (pre-Covid19) budget, **revised management's budget, *** RAS management accounts, unaudited*

With the second phase of the renovation works involving the facades, lobby, restaurants and bar area having been finalized in May, the Mamaia Hotel re-opened in the first week of June when the Romanian authorities also allowed open air restaurants to operate. However, since indoor restaurants are still not allowed to operate and are unlikely to open soon due to the worsening Covid-19 situation in Romania, the Hotel is only using its terrace to service its clients. Furthermore, due to restrictions imposed also by the social distancing rules and hygiene conditions, the number of seats on the terrace is limited to only 100, which puts a considerable strain on the Hotel's food & beverage revenues

Given the hugely negative impact of the Covid-19 pandemic on the Hotel's operations, its management produced a revised 2020 budget in May, as shown in the table of this section. The budget reflects a shorter season, lower than initially expected occupancy rates and increased operating complexity resulting in higher costs, all due to the impact of the COVID-19 pandemic. The Hotel is now expected to post a net loss of € -0.24m this year, compared to a previously expected profit of € 0.18m.

Whilst the June revenues and operational KPIs were slightly better than the revised budget, with an actual occupancy rate of 34% compared to 30%, and an average room tariff of € 40 instead of € 34 thee six-month EBITDA loss of € -0.6m is close to the revised budget.

In April, with a planned bank loan evaporating overnight, RC2 had little choice but to provide a bridge loan of € 0.3m to the Hotel in order to help it finalize those renovation works necessary for the Hotel to re-open ahead of the start of the summer season. The Company has now applied for a € 0.5m new bank loan to help it complete its investment plan in the autumn and to meet its working capital needs, under a programme of state-guaranteed loans to support small and medium sized enterprises affected by the Covid-19 pandemic. At the same time, the Hotel's bankers have allowed the Hotel to postpone € 0.15m of principal reimbursements on an investment loan which were due this year in order to alleviate the pressure on the Hotel's cash flow.

The Hotel still needs to undertake various investments to complete the redecoration of the public areas started last year, such as new furniture in the lobby, bar and restaurant areas and a new electrical generator, which are estimated to cost € 0.4m. However, any decision on which, if any, investments can be made will be based on its cash position at the end of the summer season, and the level of bank financing available. Any repayment of the RC2 loan is conditional on the Hotel's bankers' prior approval, and in any event may be constrained by the Hotel's cashflow.

Telecredit

Background

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

Financial Results and operations

(EUR '000)	2019†	2020B*	2020E**	6M 2019***	6M 2020A***	6M 2020E**
Income Statement						
Interest revenues from pay day lending	**824**	**13**	**31**	**580**	**29**	**31**
Interest revenues from SMEs lending, of which:	**340**	**1,330**	**760**	**41**	**448**	**375**
Factoring and Discounting	287	1,144	717	32	381	340
Microloans	53	186	42	10	67	35
Total operating expenses:	**(1,087)**	**(1,015)**	**(963)**	**(664)**	**(666)**	**(444)**
Provisions, of which:	(64)	74	(88)	(122)	(269)	(37)
Pay day lending	(61)	181	139	(122)	77	70
SMEs lending	(3)	(107)	(227)	-	(346)	(108)
Other Operating expenses	(1,024)	(1,089)	(874)	(541)	(397)	(406)
Operating profit before depreciation	**77**	**328**	**(172)**	**(42)**	**(190)**	**(38)**
Depreciation	(81)	(87)	(89)	(23)	(36)	(36)
Operating profit after depreciation	**(4)**	**241**	**(261)**	**(65)**	**(226)**	**(74)**
Operating profit after depreciation margin	*neg.*	*17.9%*	*neg.*	*neg.*	*neg.*	*neg.*
Profit after tax	**(54)**	**63**	**(387)**	**(63)**	**(265)**	**(133)**
net margin	*neg.*	*4.7%*	*neg.*	*neg.*	*neg.*	*neg.*
Avg exchange rate (RON/EUR)	*4.75*	*4.80*	*4.85*	*4.74*	*4.82*	*4.85*

*Note: † RAS audited, * original (pre-Covid19) budget, **revised management's budget, *** RAS management accounts, unaudited*

In May, Telecredit's management produced a revised 2020 budget in order to reflect the negative effect of the Covid-19 pandemic which took a toll on the operations of many of its clients. Both versions of the full year budget are presented in the above table. The revised budget anticipates lower financing volumes, lower interest revenues (€ 0.8m, compared to an initial € 1m), and significantly higher provisions related to SME lending (€ 0.2m, up from an initially estimated € 0.1m).

Over the first semester, Telecredit generated interest revenues from SME financing of € 0.4m, 19.5% above the revised budget. On the other hand, the negative effects of the crisis resulted in higher provisions than anticipated in the revised budget, of € 0.35m, resulting in an operating loss after depreciation over the first semester of € -0.2m, which is worse than the revised target of € -0.07m.

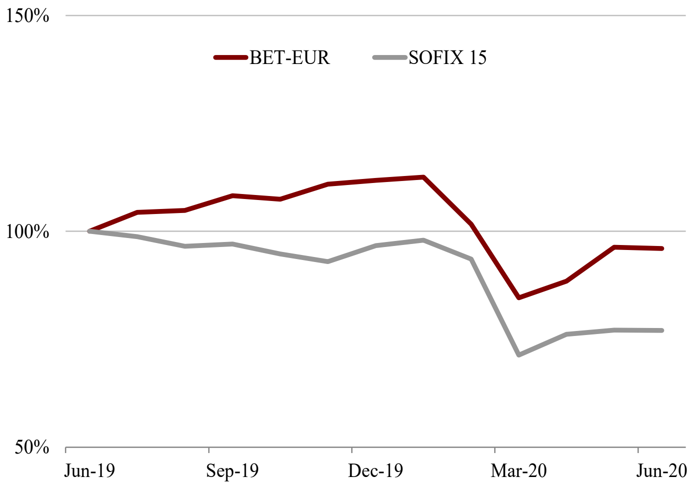
Telecredit deployed € 3.7m in financing products to SMEs in the first half of 2020, € 3.6m of which was factoring and discounting operations, and the balance of € 0.1m being microloans, all of the latter having been granted in the first quarter. At the end of March, Telecredit tightened its lending criteria, being selective in approving new factoring and discounting financing and also temporarily ceasing to grant new microloans, which are deemed the riskiest of its products. At the end of June, the SME loan book was split between € 0.9m of factoring, down from € 1.1m at the end of March, € 0.4m of discounting, down from € 0.6m at the end of the previous quarter, and € 0.3m of micro loans, unchanged quarter-on-quarter.

The pay day activity generated only € 29,000 of interest revenues over the first semester, as the Company continued to wind down its pay day business, limiting itself to only refinancing existing loans. At the end of June, the net value of the pay day loan book was virtually nil.

Over the quarter, the company reimbursed € 0.3m of the loan RC2 had provided it in the second half of 2019, leaving € 1.2m outstanding at the end of June.

Capital Market Developments

BET-EUR and SOFIX-15: 1 year performance



Commentary

Whilst international capital markets suffered severe losses during the first quarter due to the Covid-19 crisis, they recovered some of these losses over the second, when the Romanian BET index and the Bulgarian SOFIX 15 index gained 13.5% and 8.1%, respectively, both in euro terms. Over the second quarter, the MSCI Emerging Market Eastern Europe, the MSCI Emerging Market, and the FTSE100 and S&P indices were also up by 15.2%, 14.4%, 6% and 17.1%, respectively, all in euro terms.

Over the past twelve months, the BET-EUR index has lost 4% while the SOFIX 15 index fell by 22.9%, both in euro terms. By comparison, the MSCI Emerging Market Eastern Europe, the MSCI Emerging Market and the FTSE100 indices lost 19.9%, 4.7% and 18.1%, respectively, whilst the S&P index gained 6.5%, all in euro terms.

Macroeconomic Overview

Overview

	RO	as of:	BG	as of:
GDP Growth (y-o-y)	2.7%	3M20	2.4%	3M20
Inflation (y-o-y)	2.6%	Jun-20	1.6%	Jun-20
Ind. prod. growth (y-o-y)	-28.0%	May-20	-16.1%	May-20
Trade balance (EUR bn)	-7.3	5M20	-0.1	5M20
y-o-y	*11.2%*		*-84.5%*	
FDI (EUR bn)	- 0.3	5M20	0.1	5M20
y-o-y change	*n.a.*		*-66.7%*	
Budget balance/GDP	-4.2%	6M20	1.4%	6M20
Total external debt/GDP	50.2%	May-20	59.9%	May-20
Public sector debt/GDP	39.9%	May-20	20.9%	Jun-20
Loans-to-deposits	70.7%	Jun-20	74.0%	Jun-20

Commentary

Romania

The state of emergency declared by Romania due to the Covid-19 pandemic on 16 March ended on 15 May, with a gradual lifting of restrictions thereafter. Unfortunately, the end of the lockdown has coincided with a worrying increase in the number of new cases, from 120 new cases per day reported at the end of May, to approximately 1,300 daily new cases at the end of July. With the exception of indoor restaurants, cinemas and theatres which remain closed, all other businesses are now operating, whilst obliged to respect strict hygiene and sanitary rules, and all restrictions on domestic travel have been lifted. The Romanian authorities are hoping to contain the spread of the virus by imposing social distancing rules in crowded areas, as well as making the wearing of masks in certain crowded outdoor locations mandatory. So far, they have been met with limited success.

The Romanian National Statistics Institute confirmed the previously reported year-on-year first quarter GDP growth of 2.7%, with the main source of growth being private consumption which increased by 2.8% year-on-year. Investments (especially new construction works) made an important contribution to the first quarter's economic growth, having increased by 13.1%. Meanwhile, industrial production fell 5.9% year-on-year over the first quarter. Information about Romania's second quarter GDP performance is not yet available, but a sharp year-on-year GDP decrease is expected. Although the industrial production in May decreased by 28% year-on-year reflecting the negative effects of the pandemic, on a positive note, it increased by 15.1% compared to the previous month.

Romania's negative fiscal outlook deepened, with the country posting a budget deficit of € -9.4bn over the first six months, the equivalent of -4.2% of GDP, compared to a -1.9% deficit over the same period in 2019. According to the Ministry of Finance, half of the deficit is due to the exceptional measures (such as the postponement of certain taxes, prioritizing VAT reimbursements, and the partial payment of the cost of furloughing employees) taken in the context of the pandemic. Budgetary receipts fell from € 31.2bn to € 30.3bn, mainly due to 7.5% lower corporate tax receipts (the effect of falling economic activity and the postponement of taxes, as explained above), and a 15.8% fall in VAT inflows. On the other hand, total budgetary expenses increased by 13.6% in RON terms, from € 35.3bn to € 39.6bn, with personnel and social expenditures, which accounted for 64% of total expenses, increasing by 14.5%. Public investment amounted to € 1.9bn, up 18.7% year-on-year.

During the first five months of the year, the trade gap increased by 11.2% year-on-year (from € -6.6bn to € -7.3bn), with imports decreasing by € 4.8bn (or -13.5% year-on-year), but exports falling even more, by € 5.6bn (or -19% year-on-year). This large trade deficit was counter-balanced by a € 1.1bn surplus from primary and secondary incomes, and a € 0.4bn surplus from services, resulting in a current account deficit of € 2.9bn in the first five months of 2020, which is an improvement compared to the € 3.4bn deficit recorded over the same period last year. Foreign Direct Investment remained weak, with net flows amounting to € -0.3bn, compared to positive flows of € 2bn over the same period last year.

Romania's total external debt amounted to € 110.8bn at the end of May, which represents a 4.7% year-to-date increase, and now amounts to approximately 50% of GDP. Public debt was € 89bn, or approximately 40% of GDP, at the end of May, up 14.7% year-to-date in nominal RON terms. In May, Romania raised € 3.3bn by means of two eurobond issues, as follows: a € 1.3bn 5-year eurobond at a yield of 2.79% and a € 2bn 10-year eurobond at a yield of 3.62%. These new issues come after Romania borrowed € 3bn in eurobonds in January.

The inflation rate was 2.6% in June, marginally down from 3% in March, with the prices of food and basic need products increasing in spite of low energy prices and decreased overall demand. Due to the negative impact of the pandemic, at the end of May, the National Bank of Romania ("NBR") lowered its monetary policy rate from 2% to 1.75%, after performing another cut (from 2.5% to 2%) at the end of March.

The Romanian leu lost 0.4% against the euro over the second quarter, and has now depreciated by 1.3% against the euro since the beginning of the year. In early June, S&P Global Ratings re-affirmed its BBB Investment grade rating for Romania, although the outlook was changed from "stable" to "negative".

As expected, lending activity slowed down in the second quarter, with total domestic non-governmental credit (which excludes loans to financial institutions) standing at € 56bn at the end of June, down 0.9% from the end of the previous quarter in RON terms. Household loans reached € 30.1bn at the end of June, unchanged from the end of the previous quarter, and accounting for 53% of total loans outstanding. Consumer loans fell by 2.2% quarter-on-quarter and accounted for 41% of household loans, whilst housing loans decreased by 1.8% and accounted for 58% of household loans. Corporate loans reached € 24.5bn at the end of June, a 1.6% decrease since the end of the previous quarter. The NPL ratio was 4.01% at the end of May, marginally down from 4.08% at the end of December 2019. The overall deposit base was € 79.1bn at the end of June, up 1.7% from the end of the previous quarter in RON terms.

Bulgaria

Following a rather "mild" lockdown compared to Romania (with Bulgaria only imposing restrictions on intercity travel whilst allowing shops to remain open and permitting movement within one's locality) Bulgaria gradually loosened these limitations from 13 May, following which, the daily number of coronavirus cases has been on the rise, from 40 daily new cases reported at the end of May up to approximately 300 daily new cases reported at the end of July. The Bulgarian government has announced that it will reinstate certain restrictions if the number of hospitalised persons starts to jeopardize the functioning of the country's health system.

Information about Bulgaria's second quarter GDP performance is not yet available. Bulgaria's May industrial production decreased by 16.1% year-on-year and by 0.1% month-on-month, not showing signs of a rebound yet.

In the first semester, Bulgaria ran a budget surplus of € 0.8bn, or 1.4% of GDP, half of the surplus recorded over the first half of 2019. Tax proceeds fell by 3.8% year-on-year, whilst total budgetary expenses increased by 4.3%, mainly due to personnel and social expenditures increasing by 7.6%, due to the base effect of a July 2019 pensions increase. As the country still runs budgetary surpluses, Bulgaria's public sector debt remains very low at 20.9% of GDP at the end of June, but slightly up from 20.1% at the end of the previous quarter. Gross external debt amounted to € 34bn, or 60% of GDP, at the end of June, a 0.3% year-to-date fall.

Bulgaria's January to May trade deficit of € -0.1bn was better than the € -0.8bn deficit recorded over the same period last year. Exports fell by 7.4% year-on-year, while imports decreased by 12.6%. The trade deficit was counter-balanced by a € 0.3bn surplus from primary and secondary incomes, and a € 0.5bn surplus from services, resulting in a positive current account balance of € 0.7bn, which is a significant improvement on the € 0.04bn surplus recorded over the same period last year. FDI inflows amounted to only € 0.1bn, even lower than the € 0.3bn recorded over the first five months of 2019.

Bulgaria's inflation rate reached 1.6% at the end of June, compared to 3% in March, mainly driven by lower energy prices.

Total domestic non-governmental credit (which excludes loans to financial institutions) fell from € 30.3bn at the end of the previous quarter to € 30.2bn at the end of June, as corporate loans decreased by 1%, whilst household loans increased by 0.8%. The deposit base was € 40.8bn at the end of June, down from € 43.6bn at the end of March. At the end of June, the NPL ratio was 6.4%, unchanged from the end of the previous quarter.

At the beginning of July, Bulgaria was officially asked to join the eurozone waiting room ahead of the euro adoption which is estimated to happen in 2023-2024.

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