Reconstruction Capital II Ltd

("RC2" or the "Fund")

Quarterly Report

31 December 2016

neweuropecapital

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Statistics

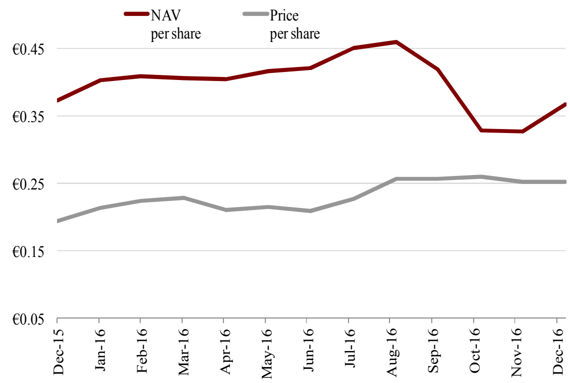
NAV per share (€)	0.3670
Total NAV (€ m)	54.2
Share price (€)	0.2525
Mk Cap (€ m)	37.3
# of shares (m)	147.6
NAV return since inception	-61.63%
12-month NAV CAGR	-1.75%
NAV annualized Return*	-8.34%
NAV annualized Volatility*	20.27%
Best month (NAV)	15.60%
Worst month (NAV)	-33.53%
# of months up (NAV)	70
# of months down (NAV)	62

** since inception*

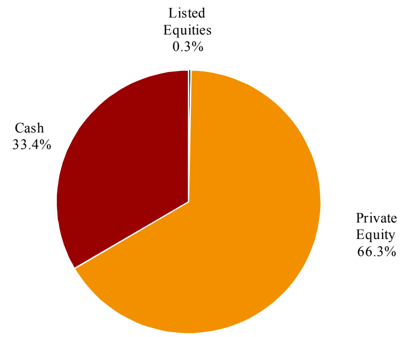
RC2 NAV returns (undiluted basis)

	2012	2013	2014	2015	2016
Jan	0.12%	-31.58%	-0.65%	-0.07%	8.03%
Feb	-9.69%	-0.51%	-0.34%	-0.34%	1.22%
Mar	-0.50%	-0.62%	2.94%	-0.70%	-0.66%
Apr	-0.66%	0.29%	2.73%	0.93%	-0.49%
May	-4.98%	-33.53%	2.70%	3.11%	3.09%
Jun	-1.47%	-0.85%	0.28%	-0.38%	1.18%
Jul	-0.73%	-0.28%	0.44%	3.24%	6.83%
Aug	0.61%	1.27%	3.23%	-0.85%	2.11%
Sep	0.01%	-0.69%	0.01%	0.31%	-8.63%
Oct	-0.82%	-0.72%	1.87%	-0.35%	-21.79%
Nov	-0.36%	0.43%	0.15%	3.17%	-0.24%
Dec	0.29%	-16.44%	0.73%	-8.47%	12.06%
YTD	-17.17%	-62.64%	14.91%	-0.94%	-1.75%

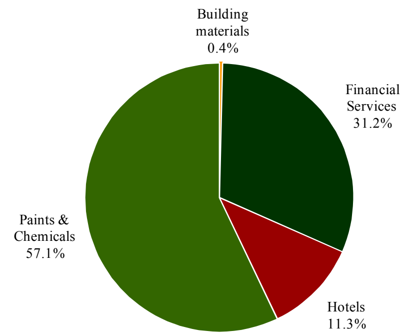
Share price / undiluted NAV per share (€)



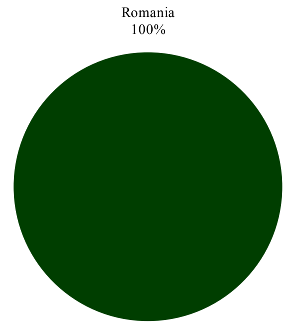
Portfolio Structure by Asset Class



Equity Portfolio Structure by Sector



Portfolio Structure by Geography



Message from the Adviser

Dear Shareholders

During the fourth quarter, RC2's NAV grew from € 41.4m to € 54.2m, mainly due to the annual independent valuation exercise which resulted in the following changes to the valuations of the private equity positions:

	Prior valuations €	Revised valuations €
Policolor S.A.	19,920,000	20,640,000
Top Factoring Group	6,925,544	11,284,423
Mamaia Hotel Resorts SRL	3,194,735	4,079,921
Total	**30,040,279**	**36,004,344**

However, the NAV per share fell from € 0.4198 to € 0.3670, due to the issuance of new shares following a series of conversions of loan notes in October. At the end of December, RC2 had 147.6m shares in issue, compared to 98.5m shares at the end of September.

The Policolor Group's 2016 consolidated sales were slightly higher than in 2015, as all divisions, with the exception of anhydrides, reported improved sales figures, whilst recurring EBITDA fell from € 2.1m to € 1.4m. As the buyers of the Policolor real estate were not able to fulfil their contractual commitments, Policolor has been trying to reach a settlement to enable it to sell its plot to one or more other buyers.

Top Factoring continued its excellent performance, with higher than expected collections on its portfolios, resulting in 2016 EBITDA of € 6.0m, compared to € 5.2m over the prior year.

Mamaia Resort Hotels' EBITDA of € 0.4m was below the budgeted € 0.6m due to lower than expected food and beverage revenues, and poor weather in May, whilst operating costs came in 3% below budget.

At the end of the quarter, the Fund had cash and cash equivalents of approximately € 18.1m and short-term liabilities of € 0.1m.

In November 2016, RC2 issued a Circular to its shareholders proposing that its life be extended by a further two years, and explaining that the Board was studying ways of returning the bulk of the proceeds from the Albalact sale to shareholders. On 22 December 2016, shareholders voted to extend RC2's life by a further two years.

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

(EUR '000)	2014*	2015*	2016B	2016**	2017B
Group Consolidated Income statement					
Sales revenues	**53,655**	**56,935**	**64,937**	**59,141**	**63,869**
sales growth year-on-year	*-2.4%*	*6.1%*		*3.9%*	*8.0%*
Other operating revenues	252	356		88	
Total operating revenues	**53,907**	**57,291**	**64,937**	**59,229**	**63,869**
Gross margin	16,877	19,807	22,796	20,531	24,175
Gross margin %	*31.3%*	*34.6%*	*35.1%*	*34.7%*	*37.9%*
Total operating expenses	**(55,549)**	**(59,378)**	**(65,748)**	**(61,313)**	**(63,387)**
Operating profit	**(1,642)**	**(2,087)**	**(810)**	**(2,085)**	**482**
Operating margin	*-3.0%*	*-3.6%*	*-1.2%*	*-3.5%*	*0.8%*
Recurring EBITDA	2,438	2,089	1,806	1,391	3,452
Non-recurring items	(563)	(286)	(125)	(223)	331
Total EBITDA	**1,875**	**1,803**	**1,681**	**1,168**	**3,782**
EBITDA margin	*3.5%*	*3.1%*	*2.6%*	*2.0%*	*5.9%*
Net extraordinary result - land sale		490		3,754	324
Financial Profit/(Loss)	(958)	(1,147)	(855)	(594)	(1,000)
Profit before tax	**(2,600)**	**(2,744)**	**(1,665)**	**1,075**	**(194)**
Income tax	114	(31)		(368)	(579)
Profit after tax	**(2,486)**	**(2,775)**	**(1,665)**	**707**	**(773)**
Minority interest	48				
Profit for the year	**(2,438)**	**(2,775)**	**(1,665)**	**707**	**(773)**
avg exchange rate (RON/EUR)	*4.45*	*4.44*	*4.50*	*4.49*	*4.50*

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

The Group's 2016 consolidated sales were 3.4% higher than in 2015, but 8.8% below budget, due to lower than expected sales at the automotive and resins divisions, with sales of decorative products and anhydrides coming in on budget.

Overall, the Group generated recurring EBITDA of € 1.4m in 2016, lower than the € 2.1m generated in 2015, and € 0.4m below budget. The 2016 net result has been inflated by € 3.7m of contractual penalties charged to the former buyers of the land, which most likely will be reversed if a settlement takes place in 2017.

Real Estate

Policolor has continued to negotiate to reach a settlement with the former buyers of its main Bucharest site who have filed a claim to have their advance of € 3.0m plus VAT of € 0.7m reimbursed. Whilst Policolor refutes these claims and believes it is entitled to retain the advance as the buyers failed to meet their contractual commitments, a settlement is important to enable Policolor to sell its plot to one or more new buyers.

Prospects

The Group's 2017 budget provides for consolidated revenues of € 64m, up 8% year-on-year, and recurring EBITDA of € 3.5m, significantly above the 2016 result, mainly as a result of eliminating losses at the anhydrides division, and a significantly improved result from the coatings and resins divisions.

The 2017 budget assumes the sale of approximately half of Policolor's main site for € 9.5m and the reversal of penalties charged to the former buyers in 2015 and 2016.

Top Factoring Group

Background

RC2 invests in Romanian non-performing loans through its 100%-owned subsidiary Glasro Holdings Ltd ("Glasro"), and also owns a 93% interest in Top Factoring, a Romanian receivables collection company. Top Factoring and Glasro are together referred to as the "Top Factoring Group" or the "Group".

Group Financial Results

EUR'000	2014*	2015*	2016B	2016**	2017B
Combined Group Income Statement					
Gross revenues	**12,354**	**14,030**	**12,741**	**13,394**	**15,682**
Debt purchase gross collections	11,460	12,855	11,950	12,527	14,993
Mandate agreements and other revenues	894	1,176	791	868	689
Amortization	(6,261)	(7,825)	(6,469)	(7,219)	(7,047)
Fair value adjustments of debt portfolios	2,054	3,936	2,556	4,590	
Net revenues	**8,147**	**10,142**	**8,828**	**10,766**	**8,635**
Operating expenses	**(4,560)**	**(4,901)**	**(4,848)**	**(4,730)**	**(5,415)**
EBITDA	**3,587**	**5,241**	**3,979**	**6,035**	**3,221**
EBITDA margin (%)	*44.0%*	*51.7%*	*45.1%*	*56.1%*	*37.3%*
Depreciation	(135)	(240)	(330)	(313)	(311)
Earnings before taxes	**2,894**	**4,417**	**3,157**	**5,135**	**2,259**
Income tax	(547)	(625)	(410)	(657)	
Net profit	**2,347**	**3,792**	**2,747**	**4,478**	
Net profit margin (%)	*28.8%*	*37.4%*	*31.1%*		
Avg exchange rate (RON/EUR)	*4.44*	*4.44*	*4.45*	*4.49*	*4.50*

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

With higher than budgeted collections on proprietary portfolios, the Group wrote up its portfolios by € 4.6m in 2016, helping to generate an EBITDA of € 6.0m, up 15.2% on last year's € 5.2m, when the Group had booked € 3.9m of portfolio write-ups. The € 4.6m of write-ups booked in 2016 reflect the portfolios' improved future collection curves, which have been written-up to reflect the better than expected collections over 2016.

The agency business generated revenues of € 0.9m, down 26.2% year-on-year, but above the budgeted figure of € 0.8m. The main reason is that Top Factoring stopped working on certain unprofitable contracts in 2016, which helped the operating margin of this business line increase from 25.8% in 2015 to 29.7% in 2016.

Operations

Glasro has invested € 9.0m in new portfolios in 2016, financed by a combination of bank loans and its own equity. At the end of December 2016, the Group owned portfolios with a book value of € 16.8m. Bank debt amounted to € 9.0m, with cash holdings amounting to € 1.1m, resulting in a net debt position of € 7.9m and a net book value of € 8.9m.

Gross collections from proprietary portfolios fell from € 12.9m in 2015 to € 12.5m in 2016, primarily due to the larger portfolios acquired in 2016 only generating collections in the second part of the year.

The share of collections generated by the field and legal departments increased to 16% and 38%, respectively, from 14% and 30%, respectively, in 2015. The balance of 46% was collected by the call centre. The increase in the share of legal collections is explained by Top Factoring's decision to start legal execution procedures earlier on, in order to maximise its recoveries.

Prospects

The 2017 budget is based on € 5.5m of estimated new investments in portfolios, gross collections of € 15m, and an EBITDA of € 3.2m.

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)	2014*	2015*	2016B	2016**	2017B
Income Statement					
Sales Revenues	**1,972**	**2,331**	**2,527**	**2,244**	**2,561**
Total Operating Revenues	**2,045**	**2,349**	**2,527**	**2,336**	**2,751**
Total Operating Expenses	(2,106)	(2,044)	(2,163)	(2,151)	(2,148)
Operating Profit	**(61)**	**305**	**364**	**185**	**603**
Operating margin	*neg.*	*13.0%*	*14.4%*	*7.9%*	*21.9%*
EBITDA	**253**	**484**	**580**	**355**	**783**
EBITDA margin	*12.4%*	*20.6%*	*22.9%*	*15.2%*	*28.5%*
Profit after Tax	**(158)**	**176**	**204**	**89**	**651**
Net margin	*neg.*	*7.5%*	*8.1%*	*3.8%*	*23.7%*
Avg exchange rate (RON/EUR)	*4.44*	*4.44*	*4.45*	*4.49*	*4.50*

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

The Company's 2016 operating revenues were pretty much unchanged compared to the previous year, but were 7.5% below the budget mainly due to bad weather in May and weak food & beverage sales (-9% year-on-year), following a decision by the management to allow customers on a half-board package to choose between having lunch or dinner at the Hotel, resulting in low usage of the restaurant in the evening.

Accommodation revenues accounted for 52% of overall sales and increased by 10% year-on-year, with the occupancy rate reaching 25.9%. In terms of sales channels, 62% of the accommodation revenues were generated through agencies, 16% by "walk-in" clients, 9% by corporate contracts, and the balance of 13% was generated by online booking channels, the latter representing a healthy increase on the 9% achieved in 2015.

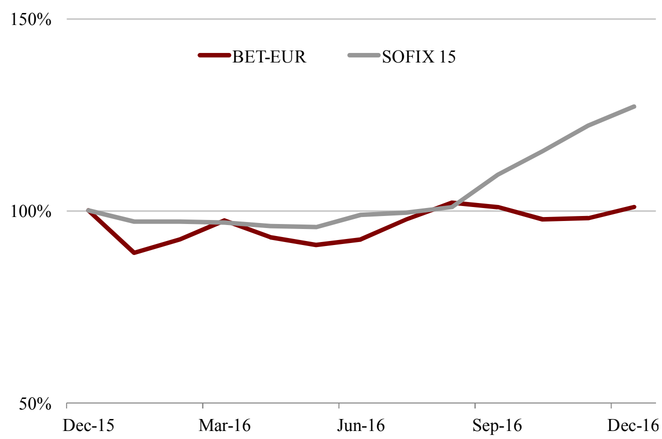
The 2016 EBITDA of € 0.4m was below the budgeted € 0.6m due to the lower than expected revenues, whilst operating costs came in 3% below budget.

Prospects

The 2017 budget is based on accommodation revenues of €1.4m, up 15% year-on-year, the combined effect of a higher occupancy rate (29.2% compared to 25.9% in 2016) and a higher average room tariff (€ 46.8 versus € 45.8 in 2016). Management is aiming to increase the share of online sales and walk-in clients, who are typically charged higher tariffs. In 2016, bookings made directly through the Hotel's own website accounted for 1% of total accommodation revenues, whilst for 2017 management is targeting 5%. Management also intends to focus on increasing *a la carte* revenues as well as redesigning the meal packages. The food & beverage revenues are budgeted to increase from € 1.0m to € 1.1m in 2017. The budgeted EBITDA is € 0.8m.

Capital Market Developments

BET-EUR andSOFIX-15: 1 year performance



Commentary

During the fourth quarter, the Romanian BET index was flat, whilst the Bulgarian SOFIX 15 index increased by 16.2%, all 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 21.0%, 1.6%, 4.9% and 9.9%, respectively, all in euro terms.

Over 2016, the BET-EUR and SOFIX 15 indices were up by 0.8% and 27.2%, respectively, all in euro terms. By comparison, the MSCI Emerging Market Eastern Europe, the MSCI Emerging Market and the S&P indices gained 37.0%, 11.9% and 12.8%, respectively, while the FTSE100 lost 1.2%, all in euro terms.

Macroeconomic Overview

Overview

	RO	as of:	BG	as of:
GDP Growth (y-o-y)	4.8%	FY16	3.4%	FY16
Inflation (y-o-y)	-0.5%	Dec-16	0.1%	Dec-16
Ind. prod. growth (y-o-y)	5.8%	Dec-16	7.0%	Dec-16
Trade balance (EUR bn)	-10.0	FY16	-1.8	FY16
y-o-y	*20.2%*		*-31.7%*	
FDI (EUR bn)	4.1	FY16	0.7	FY16
y-o-y change	*34.5%*		*-59.7%*	
Total external debt/GDP	54.9%	Dec-16	72.7%	Nov-16
Reserves to short-term debt	146.2%	Dec-16	298.8%	Nov-16
Loans-to-deposits	80.3%	Dec-16	75.8%	Dec-16
Public sector debt-to-GDP	37.7%	Dec-16	29.4%	Dec-16

Commentary

Romania

Romania experienced the highest economic growth in the EU during the fourth quarter of 2016, with its GDP's increasing by 4.8% year-on-year, compared to average EU growth of 1.8%. Private consumption, boosted by tax cuts and wage increases, was the main driver of economic growth, having increased by 3.8% in the fourth quarter of 2016 compared to the same quarter of the previous year. In 2016, private consumption increased by 5.8% year-on-year whilst overall GDP grew by 4.8% in 2016. In its latest report published in February 2017, the European Commission is forecasting 4.4% GDP annual growth in 2017, helped by continuing strong domestic demand.

Inflation remained in negative territory as prices fell by 0.5% year-on-year in December 2016. The National Bank of Romania ("NBR") is forecasting an inflation rate of 1.7% by December 2017, mainly driven by robust domestic demand and increasing international commodities prices.

The Romanian leu was down 0.4% against the euro in 2016, and it has continued to lose ground against the euro so far in 2017 (-0.5% year-to-date), due to worries about the expansionary political programme of the ruling Social Democratic Party (PSD), which involves tax cuts and wage increases.

In 2016, the budget deficit came in at € 4.1bn, equivalent to 2.4% of GDP, compared to a deficit of 0.8% in 2015. The deepening of the deficit is no surprise given the pre-electoral fiscal relaxation of 2016 (the standard VAT rate was lowered from 24% to 20% from January 2016, while the minimum wage was increased from € 236 to € 282). Budgetary receipts fell by 4.3% year-on-year in RON terms, mainly due to lower VAT collections, which made up 23.1% of total budgetary receipts and fell by 9.6% year-on-year. This was only partially compensated by improved receipts from corporate profit taxes, which represent 6.9% of total receipts and increased by 11.7% year-on-year. Total budgetary expenses fell by 0.6% year-on-year, with personnel and social expenditures, which account for 57.4% of total expenses, increasing by 8.5%. In 2016, Romania's absorption of EU funds was poor, with the overall absorption of such funds only growing from 74% at the end of 2015 to approximately 78% at the end of 2016.

In December 2015, the left of centre Social Democratic Party (PSD) won the parliamentary elections, and went on to form a new government with the support of the Alliance of Liberals and Democrats (ALDE). The new government's plan for a budget deficit target of -3% hardly looks credible, as it has already adopted populist fiscal measures such as an increase in pensions and salaries for certain categories of state employees, another increase in the minimum wage (+16%), and a further reduction in the standard VAT rate from 20% to 19%.

With domestic demand increasing, the 2016 trade deficit worsened by 20.2% year-on-year (from € -8.4bn to € -10.0bn), with exports increasing by only 6.2% whilst imports grew by 8.0%. The negative evolution of the trade balance was the main reason behind a € 4.1bn current account deficit, which is the equivalent of 2.4% of GDP and compares to a deficit of € 1.9bn in 2015. FDI inflows amounted to € 4.1bn, up from € 3.0bn in 2015. Romania's total external debt was € 92.5bn at the end of December, which represents a 2.3% increase over the year and amounts to approximately 55% of GDP. The increase in external debt is mainly due to Romania successfully placing three eurobond issues worth a combined € 3.25bn in 2016. Total public debt was € 63bn, or 37.7% of GDP, at the end of 2016, virtually unchanged since the end of 2015. At the beginning of March, Romania's Finance Minister announced that Romania plans to sell about € 2.5-3.0bn worth of eurobonds on the international markets and some € 10bn worth of RON-denominated domestic debt in 2017.

Total domestic non-governmental credit (which excludes loans to financial institutions) amounted to € 48.5bn at the end of December, and was up 1.2% over the year in RON terms. Household loans increased by 4.7% year-on-year and accounted for 51.4% of the total loan stock at the end of 2016, compared to 49.6% at the end of 2015. The main trigger for the increase in household lending was housing loans which grew by 12.5% year-on-year in RON terms, or from € 11.5bn to € 12.9bn in euros. The overall deposit base increased by 8.2% in RON terms over the year, and amounted to € 60.4bn at the end of 2016. The NPL ratio was 9.5% at the end of December, down from 13.5% at the end of 2015.

Bulgaria

Bulgaria's fourth quarter GDP grew by 3.4% year-on-year, and by 0.9% compared to the previous quarter. Overall, GDP grew by 3.4% in 2016. In 2016, private consumption increased by 0.7%, whilst exports increased by 3.3% over the same period. In its latest prognosis report, the European Commission forecasts GDP will grow by 2.9% in 2017, mainly due to the positive effect of investments, as a number of big infrastructure projects are to be launched in 2017.

The deflationary trend experienced over the prior fourteen months reversed in December 2016, as domestic demand picked up. Accordingly, Bulgaria recorded a 0.1% year-on-year increase in prices that month, compared to a 0.4% year-on-year fall in December 2015.

In 2016, Bulgaria ran a budget surplus of € 0.8bn, or 1.6% of GDP, which compares to a target deficit of 2% of GDP. The main trigger for the positive budget balance was lower investments, which fell from € 3.5m in 2015 to € 2.0m in 2016, as a series of infrastructure projects were postponed to 2017. For 2017, the government is targeting a budget deficit equal to 1.4% of GDP. Bulgaria's public sector debt was 29.4% of GDP at the end of December, up 3 basis points from the end of 2015. The increase was due to Bulgaria placing € 1.1b of seven-year bonds, and € 0.9bn of 12-year bonds, in March 2016. Debt denominated in euros accounted for 81% of total public debt, with the balance of 19% being denominated in Bulgarian leva.

Bulgaria's trade balance improved from a deficit of € 2.6bn in 2015 to a deficit of € 1.8bn in 2016. Exports experienced 3.3% year-on-year growth, whilst imports fell by 0.4%. Helped by a € 3.4bn surplus from services, the current account balance was € 1.8bn in surplus, or 3.9% of GDP, up from a surplus of 0.4% of GDP the previous year. FDI inflows were only € 0.7bn, 59.7% lower than in 2015. The fall was mainly due to lower equity investments, which were down from € 1.8bn to € 0.8bn, and lower intra-group loans which fell by € 0.1bn.

Total domestic non-governmental credit (which excludes loans to financial institutions) amounted to € 25.1bn at the end of December, and was up 0.7% year-on-year. Whilst corporate loans increased by 1.5%, household loans grew by 2%. NPLs accounted for 14% of the overall loan stock at the end of December. The deposit base increased from € 31.1bn at the end of 2015 to € 33.1bn at the end of 2016 (+6.5%).

Bulgaria's presidential elections which were held in early November were won by a candidate backed by the Bulgarian Socialist Party. Following the results, the centre-right Prime Minister has tendered his resignation, and early parliamentary elections are due to be held at the end of March.

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