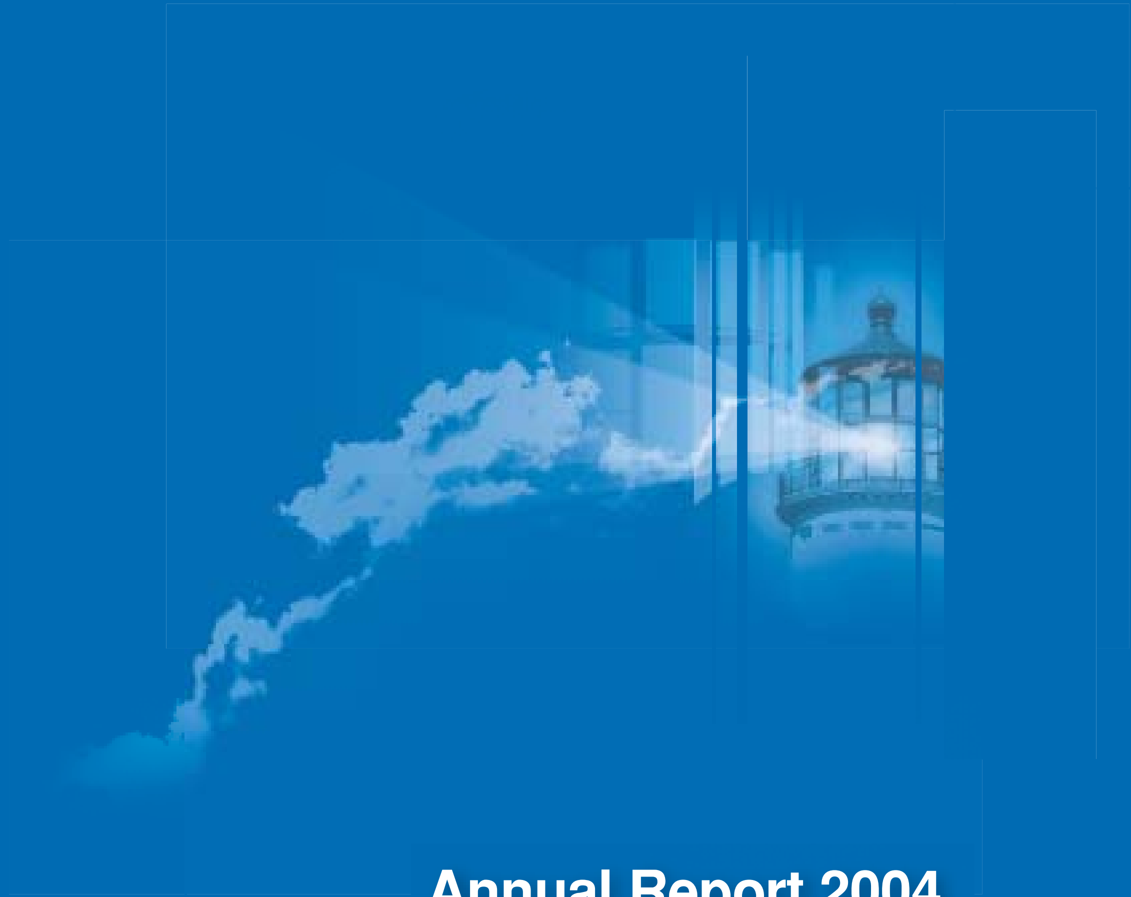

Annual Report 2004

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Black
Sea
Trade &
Development
Bank

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Black Sea Trade & Development Bank

Board of Governors

Republic of Albania
Governor: Ms. Adriana Berberi, Deputy Minister of Finance
Alternate Governor: Mr. Luan Shahollari, Deputy Minister of Economy

Republic of Armenia
Governor: Mr. Vardan Khachatryan, Minister of Finance and Economy
Alternate Governor: Mr. David Avetissian, Deputy Minister of Finance and Economy

Republic of Azerbaijan
Governor: Mr. Farhad Aliyev, Minister of Economic Development
Alternate Governor: Mr. Avaz Alekperov, Minister of Finance

Republic of Bulgaria
Governor: Mr. Ivan Iskrov, Governor, Bulgarian National Bank
Alternate Governor: Mr. Krassimir Katev, Advisor to the Minister of Finance

Georgia
Governor: Mr. Merab Kakulia, Vice President, National Bank of Georgia
Alternate Governor: Mr. David Keresselidze, Director of International Economic Relations Department, Ministry of Foreign Affairs

Hellenic Republic
Governor: Mr. George Mergos, Secretary General, Ministry of Economy and Finance
Alternate Governor: Mr. Ioannis Papadakis, Senior Administrative Advisor, Commercial Bank of Greece

Republic of Moldova
Governor: Ms. Mariana Durlesteanu, Vice Minister of Finance
Alternate Governor: Ms. Tatiana Lapicus, Head of Economic and International Relations Department, State Chancellery

Romania
Governor: Mr. Mihai Nicolae Tanasescu, Minister of Public Finance
Alternate Governor: Mr. Cristian Diaconescu, Minister of Justice

Russian Federation
Governor: Mr. Ivan S. Materov, First Deputy Minister of Economic Development and Trade
Alternate Governor: Mr. Sergey I. Kolotukhin, Deputy Minister of Finance

Republic of Turkey
Governor: Mr. Ibrahim Canakci, Undersecretary of Treasury
Alternate Governor: Mr. Cavit Dagdas, Deputy Undersecretary of Treasury

Ukraine
Governor: Mr. Mikola Derkach, Minister of Economy and European Integration
Alternate Governor: Mr. Sergiy Yaremenko, Board Member, Director of Foreign Exchange Regulations Department, National Bank of Ukraine

Board of Directors

Republic of Albania
Director: Ms. Burbuqe Riba, Director of Financial Supervision Directorate, Ministry of Finance
Alternate Director: Mr. Marian Gjermeni, Director of Monetary Operations Department, Bank of Albania

Republic of Armenia
Director: Mr. Arthur Javadyan, Vice Chairman, Central Bank of Armenia
Alternate Director: Mr. Nerses Mkrtchian, Head of International Economic Cooperation Department, Ministry of Foreign Affairs

Republic of Azerbaijan
Director: Mr. Samir Sarifov, Executive Director, State Oil Fund
Alternate Director: Mr. Adalet N. Aliyev, Division Chief of Foreign Economic Relations, Ministry of Finance

Republic of Bulgaria
Director: Ms. Sophia Kassidova, Deputy Minister of Transport and Communications
Alternate Director: Ms. Nina Stavreva, Head of State Treasury & Debt Department, Ministry of Finance

Georgia
Director: Mr. David Aptsiauri, Deputy Minister of Foreign Affairs
Alternate Director: Mr. George Chikava, Head of Credit Operations Division, National Bank of Georgia

Hellenic Republic
Director: Mr. Vassilios Kanellakis, Director General for Policy Planning and Implementation, Ministry of Economy and Finance
Alternate Director: Mr. Nikolaos Symeonidis, Director for International Organisations and Policies, Ministry of Economy and Finance

Republic of Moldova
Director: Ms. Lilia Razlog, Head of Public Debt Department, Ministry of Finance
Alternate Director: Ms. Elena Matveeva, Deputy Head of External Finance and Debt Divisions, Ministry of Finance

Romania
Director: Ms. Diana Peligrad, Programs Coordinator, General Directorate for External Public Finance, Ministry of Public Finance
Alternate Director: Mr. Stefan Petrescu, General Director, General Directorate for External Public Finance, Ministry of Public Finance

Russian Federation
Director: Mr. Andrei I. Denisov, Deputy Minister of Foreign Affairs

Republic of Turkey
Director: Mr. Memduh Aslan Akcay, Director General of Foreign Economic Relations, Undersecretariat of Treasury
Alternate Director: Mr. Turan Oz, Deputy Director General of Foreign Economic Relations, Undersecretariat of Treasury

Ukraine
Director: Mr. Valeriy Pyatnytskiy, First Deputy Minister of Economy and European Integration
Alternate Director: Mr. Sergiy Manokha, Deputy Minister of Finance

Audit Commitee

As of 31 December 2004

Chairperson:

Ms. Burbuqe Riba, BSTDB Director for the Republic of Albania

Members:

Mr. Arthur Javadyan, BSTDB Director for the Republic of Armenia

Mr. Valeriy Pyatnytskiy, BSTDB Director for Ukraine

Management

As of 31 December 2004

Mr. Mustafa Gürtin
President

Mr. Mikhail Jernov
Vice President Banking

Ms. Valentina Siclovan
Vice President Operations

Mr. Plamen Petrov
Vice President Finance

Mr. Charalampos Tsarouchas
Secretary General

Mr. Mustafa Gürtin
President

Mr. Mikhail Jernov
Vice President Banking

Ms. Valentina Siclovan
Vice President Operations

Mr. Plamen Petrov
Vice President Finance

Mr. Charalampos Tsarouchas
Secretary General

To the Board of Governors

In accordance with Article 35 of the Agreement Establishing the Black Sea Trade and Development Bank and Section 10 of its By-Laws, I submit to the Board of Governors the Bank's Annual Report 2004 as endorsed by the Board of Directors. The Annual Report contains the Bank's financial statements; a separate financial statement for the operations of the Bank's Special Fund has also been issued as prescribed in Section 12 of the Bank's By-Laws.

Mustafa Gürtin
Chairman of the Board of Directors
President
Black Sea Trade and Development Bank

Statement by the President

The Black Sea Region continued its recent record of strong economic growth in 2004 despite the somewhat uneven performance seen globally. The Region at large is now on a path of expansion and development that has as its ultimate aims, elevating living standards, reducing poverty, creating greater economic opportunity, deepening regional cooperation and strengthening intra-regional cross-country links.

Against this background, the BSTDB experienced a most successful year, achieving an increase of 43% in its total of outstanding loans while still maintaining the overall credit quality of its portfolio. The resulting increased revenues coupled with below-budget expenses have seen the Bank return to a near breakeven result while continuing to follow a conservative approach to building general loan loss provisions. This outcome has far-exceeded the expectations that are stated in the current Business Plan.

In March 2004 BSTDB was assigned an investment grade credit rating by Moody's Investors Service and subsequently negotiated its first syndicated loan facility, with a group of leading international commercial banks, for USD 60 million, at favourable terms.

During 2004 our Bank continued to liaise with BSEC and strived to achieve closer coordination as regards the broad direction of the activities in the Region. We will make further progress in this respect, during 2005.

BSTDB continues to develop its relationship with the European Union, with the intention of acting as financial intermediary in the relations between any of our shareholder countries and the European Union. In this vein, negotiations are underway for the BSTDB to be party to a second Memorandum of Understanding, expected to be concluded in the course of 2005,on collaboration of BSTDB shareholder countries with the Union, under the new neighbourhood policy.

Changes to the Bank's senior management team saw the arrival of Mr. Mikhail Jernov (Russia) as Vice President in charge of the Banking Division and Mr. Plamen Petrov (Bulgaria) as Vice President Finance while Mrs. Valentina Siclovan (Romania) moved from Banking to take over control of the Operations Division.

In light of the favourable developments seen in 2004 I strongly believe the firm commitment of BSTDB's management and staff to implementing the Bank's mission and objectives, assisted by our shareholders' confidence and by the continued cooperation of the international financial community; will combine to lead the Black Sea Trade and Development Bank to greater achievements in the period ahead.

Mustafa Gürtin
Chairman of the Board of Directors
President
Black Sea Trade and Development Bank

1 | Highlights of 2004

• The Bank's outstanding loan portfolio increased to SDR 244.3 million (appx. USD 380 million), a 43% increase from the previous year. Despite this strong growth credit quality remained good, with more than 99% of the portfolio performing to expectations.

• Increased revenues from lending coupled with lower expenses than budgeted for resulted in the Bank almost breaking even on the year, while continuing to follow a conservative approach to building general provisions for loan losses.

• In March 2004 the Bank received credit ratings of long term Baa2 and short term P2 from Moody's Investors Service. Investment grade ratings such as these are recognition of the Bank's capital structure, shareholder support and management expertise, as well as staff quality, and will certainly facilitate the achievement of its mandate.

• Following assignment of the long term credit rating, BSTDB launched its first syndicated borrowing, a USD 60 Million Term Loan Facility signed on December 1, 2004. Bayerische Landesbank and SanPaolo IMI S.p.A. acted as Lead Arrangers, while General Bank of Greece SA, Natexis Banques Populaires (London Branch), Raiffeisen Zentralbank Österreich AG, Baden-Württembergische Bank AG, and Commerzbank AG also participated in the facility.

• BSTDB was the first IFI to hold the Annual Meeting of its Board of Governors in Albania. On this occasion, the Bank also hosted its Black Sea Business Day in Tirana attracting 280 officials, international investors, bankers and businessmen, as well as representatives of other IFIs. The event focused on issues of mobilising international financial resources for development in the region and facilitating investments in infrastructure and agri-business. The audience of the Business Day was addressed by H.E. Mr. Fatos Nano, Prime Minister of Albania.

2 Black Sea Region Five years of sustained dynamic growth

The region comprising the member states of the Black Sea Trade and Development Bank (the greater Black Sea Region)[1] continued its recent record of strong real GDP growth in 2004, with rates reaching an estimated 7.3%. This rate of growth exceeded both the 4.9% real GDP growth in 2004 for the new European Union (EU) entrants from Central-Eastern Europe and the Baltics that are considered 'transition' countries[2], and the 1.8% of the 12 Eurozone EU member countries, the most proximate wealthy market for the Black Sea Region. It also follows up on growth of 5.4% in 2002 and 6.4% in 2003 in the greater Black Sea Region, demonstrating that the growth has been sustained at this high level.

Taking a longer term perspective, the greater Black Sea Region grew at an average rate of 5.8% per annum during the five year period between 2000-2004. For the period, this entails a real economic expansion of over 32%. The Black Sea Region's performance is all the more impressive:

- when placed in the context of global growth and measured against growth in other regions,
- when compared to historical trends within the Region since the establishment of the Black Sea Economic Cooperation, and
- when dissected in its own right, examining the factors and structural features behind the performance of the individual countries which comprise the Region.

Prior to examining more closely the nature of this performance, it is important to place it in a general context. For undoubtedly, the Black Sea Region has enjoyed a very encouraging five year stretch, and prospects for 2005 are also favorable. However, this positive period should be seen as part of a process, reaping the initial rewards of sustained efforts at stabilization and reform, and embarking upon a path of growth and development that has as its ultimate aims the raising of living standards, the reduction of poverty, greater economic opportunity, and on a regional level, the deepening of regional cooperation and the strengthening of cross-country links.

Black Sea Region Growth in the Global Context

As Figure 1 shows, the real economic growth observed in the Black Sea Region was more than double the average annual rate of growth of the World Economy during the 2000-2004 period and more than triple the rate of the 12 Eurozone countries. It was also considerably higher than the average annual rate of 3.5% achieved by the Baltic states and the countries of Central and Eastern Europe which collectively comprise the eight so-called 'transition' states which joined the EU in 2004, and which have been most prominently lauded by international institutions and key players in international markets for the success of their transition from centrally planned economies to market oriented economies. While the new EU transition states deserve the accolades for the economic achievements and the successful entry into the EU, their rate of growth has slowed even as the Black Sea states to the east and south have picked up and overtaken them in terms of pace.

In comparison with the rest of the world economy, the greater Black Sea Region was the second fastest growing region between the 2000-2004 period, exceeded only by the 7.0% annual average rate achieved by the developing countries of East Asia and the Pacific, a region which was buoyed by China's tremendous economic expansion.

Moreover, the Black Sea Region achieved this performance despite uneven global growth and in particular, the weak growth of the EU, the Region's most important and proximate market for the development of trade and investment ties, both due to its overall wealth as well as the fact that the EU's influence in setting standards, rules, and trade practices extends beyond its borders. Following the expansion of the EU to 25 members, including Central Europe and the Baltics, the Black Sea Region-including its EU member, EU candidates, and non-candidates-shares a sizeable and soon to grow further common border with the EU, and is affected very much by policy decisions as well as economic developments in the EU- given the latter's overall political and economic weight and its sheer size.

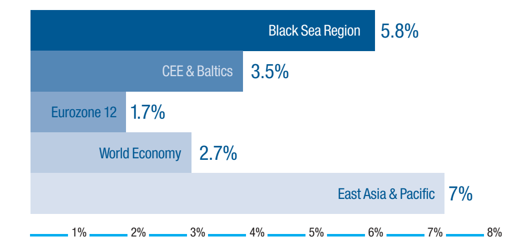


Figure 1: Average Annual GDP Growth 2000-2004

[1] Note on Sources: Black Sea Region data based on BSTDB calculations from National Statistical Agencies of the countries of the Black Sea Region and the International Monetary Fund IFS Database. Additional sources referred to include Global Economic Prospects 2005 of the World Bank (& GEP 2003 & GEP 2004), the OECD Economic Outlook 76 database, and the Economist Intelligence Unit.

[2] Czech Republic, Hungary, Poland, Slovakia, Slovenia, and the Baltics: Estonia, Latvia, Lithuania.

Historical Trends in Black Sea Region Growth

Turning to historical trends within the Black Sea Region, the high regional growth exhibited during the 2000-2004 period comes in marked contrast to the economic performance of much of the Region during the decade of the 1990s. Indeed, Black Sea regional performance can be divided into three stages since the establishment of the Black Sea Economic Cooperation (BSEC) in 1992.

The initial stage lasted until roughly 1995, representing the initial phase of economic transition for nine of the 11 BSTDB members, a situation marked by economic decline including (i) collapse of old systems of production and distribution without the new ones yet in place, (ii) weak or non-existent legal frameworks, (iii) non-functioning financial sectors, (iv) radical but either misunderstood or inconsistently implemented structural reforms, (v) macroeconomic instability highlighted by high inflation (including hyperinflation) and lack of fiscal control, and (vi) in a number of cases the added challenge of needing to construct the apparatus and institutions of newly sovereign states, virtually from scratch. Even for the two non-transition states, Greece and Turkey, the early 1990s was a period of relatively high inflation, fiscal imbalance and uneven growth.

The next stage, roughly during the latter half of the 1990s, was one of stabilization and consolidation during which security and political stability improved, economic decline either slowed down or was reversed, the initial phase of market oriented structural reforms were consolidated and began to have an impact on the economy, and macroeconomic stability was by and large achieved, with improved fiscal discipline and declining inflation rates. In terms of growth, BSTDB member countries in general enjoyed better results and, as Figure 2 shows, real GDP growth during this period averaged approximately 0.6% per annum.

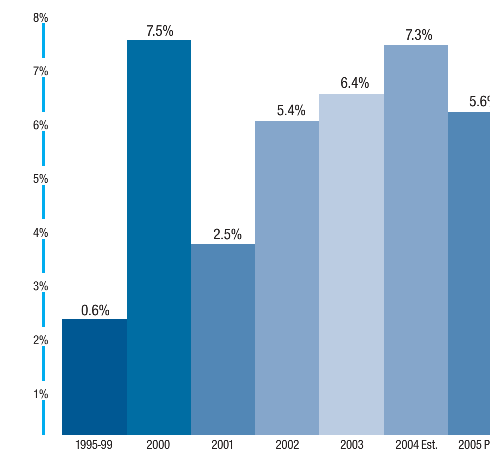


Figure 2: Real GDP Growth in Black Sea Region

Furthermore, Black Sea economies had to contend with shocks which included the increasing volatility in energy prices, the 1998 financial crisis, the devastating 1999 earthquake in Turkey, and the 1999 Kosovo crisis, which mainly affected the Balkans but had negative repercussions for external perceptions of the stability and potential dynamism of the Region. Despite the adverse immediate impacts of these crises, they ultimately proved beneficial because the economies demonstrated their resilience under trying circumstances, and the crises themselves spurred a new round of structural reforms and also helped to consolidate fiscal responsibility in those states that had already made efforts to reduce their deficits, and to bring it about in those that were previously profligate. Two additional factors with roots in this stage, which were to prove significant in bringing about the next period, were (i) the national currency devaluations which improved the price competitiveness in countries affected by the financial crisis and thus helped to spur production, and (ii) the beginning of a declining trend in interest rates, in lower inflation countries, which helped to spur investment.

The third (and current) stage of high and sustained growth can be dated to 2000 (See Figure 2). A series of factors converged to render conditions appropriate for this expansion including:

- Acceptance of, and improved adaptation to, a market oriented system and its requirements by the population at large;
- Improvements in legal frameworks, with the adoption of 'state of the art' market oriented legislation in many sectors (especially for financial matters). The focus shifted from establishing a system to improving its operation, achieving more effective implementation of laws, increasing transparency and clarifying areas where contradictions and confusion existed;
- Previously undertaken reforms- often socially painful or costly- began to pay dividends and have an impact, permitting greater trade and investment activity;
- A strong output response from domestic industries which benefited from the aforementioned devaluations which improved price competitiveness in some countries of the Region, improved financial sectors, and the declining interest rates which spurred higher investment in other countries;
- Greatly improved macroeconomic stability, including the enhanced credibility of governments in the implementation of monetary and fiscal policy, resulting in declining inflation, interest rates, fiscal deficits and external debt and debt-servicing ratios.

The average growth for the period would have been higher if not for the financial crisis in Turkey in 2001. Yet even this adverse event helped to stimulate important and far reaching reforms in the Turkish banking sector and a strong commitment to fiscal and monetary responsibility, including a sustained effort to achieve price stability which resulted in an impressive decline in inflation and the achievement in 2004 of single digit rates for the first time in over 30 years.

Sectoral and Structural Features of Black Sea Region Growth

Looking more closely at the structural features and the sources of the Black Sea Region's growth, initially (e.g. in 2000) a portion of this growth may have been due to recovery from the negative growth of previous years, or the re-activation of idled capacity from the beginnings of the transition process. However, there are strong indications that most of the current growth is the result of new economic activity, reflects fundamental transformations in BSTDB economies, and a re-allocation of capital and resources to more efficient and market-demanded areas.

Perhaps the most important evidence derives from the sectoral shift in the composition of the growth. Industrial growth has been more or less in line with GDP growth in most Black Sea countries, leaving its proportion in the overall economy unchanged except in cases such as Ukraine and Romania, two countries with strong industrial bases which experienced increases in industrial production on the strength of strong external demand for their products. For the Black Sea Region as a whole, the share of the industrial sector in the economy is approximately 30%. The agricultural sector throughout the Region has fared poorly partly due to bad luck, as weather conditions hurt production in certain years, but mainly because of structural inefficiencies which have not permitted the sector to reform and improve productivity. Overall, agricultural growth was very low- negative in real terms in some countries- and as a share of GDP the sector's contribution to GDP formation declined by over 30% to a point where it accounts for less than 10% of GDP formation region-wide.

By way of contrast the services sector, which had been underdeveloped prior to transition, grew rapidly at rates which exceeded the overall rate of GDP growth. Thus the service sector as a share of the economies of the Region grew, and it now accounts for over 60% of GDP formation in the Region. Retailing and sales, financial services, telecommunications, tourism, etc. represent some of the most dynamic sub-sectors of the Region's economy, and have recorded impressive outturns, generating much of the new employment observed in the Region. It is not coincidental that many small and medium sized enterprises (SME's) operate in the services sector, as these have proven the main engines of economic growth globally in many economies (including the so-called 'transition' ones), and have tended to be the most flexible and vibrant portion of the private sector of the Region's economies. This is especially encouraging since healthy SME development, in a context of macroeconomic stability, bodes favorably for maintenance of the high growth rates achieved.

Special mention within services must be made of the construction sector, which has grown particularly strongly, with demand for housing and business construction increasing rapidly across the Black Sea Region, irrespective of country size, structure of economies, or overall national income levels. The rise in income levels, the upsurge in external inflows, declining interest rates, changing tastes and a need to renew housing stocks combined, to varying degrees in individual countries, to generate a housing boom that has impacted every BSTDB member country.

Overall, the Region's economies have transformed steadily as they have grown during this period, with the importance of the role of the private sector increasing and becoming ever more vital for further growth. The share of private expenditure in overall GDP has risen, for while rates of public investment and consumption growth have varied from country to country, private investment and consumption have grown across the board, accounting either for the bulk or the entirety of the incremental growth observed in GDP.

Table 1: Summary of Key Economic Indicators for 2004, BSTDB Member Country[3]

	GDP Growth	Avg. Inflation	Budget/GDP	Cur Acct Bal/GDP
Albania	5.9%	2.9%	-5%	-6.1%
Armenia	10.4%	7.0%	-1.9%	-6.0%
Azerbaijan	10.2%	6.7%	-1.4%	-30.6%
Bulgaria	5.3%	6.2%	0.9%	-7.8%
Georgia	8.4%	5.1%	-1.5%	-13.5%
Greece	3.7%	2.9%	-6.1%	-4.5%
Moldova	8.0%	11.0%	0.2%	-2.5%
Romania	8.3%	11.9%	-1.2%	-6.2%
Russia	7.1%	11.7%	3.5%	7.9%
Turkey	8.9%	10.6%	-10.6%	-4.6%
Ukraine	12.1%	8.6%	-1.7%	7.1%

[3] Sources: National Statistical Agencies and International Monetary Fund IFS Database.

Analysis of Black Sea Region Growth in 2004

Having looked at Black Sea Region growth in the context of global growth, against historical trends, and in terms of sectors of origin and type of expenditure, a better illustration of the trends behind the economic performance may be achieved by focusing briefly on the performance during 2004 of the countries which comprise the Region.

For the third consecutive year, every country in the Black Sea Region recorded positive real GDP growth, ranging from a high of 12.1% for Ukraine, to a low of 3.7% for Greece. Two other countries, Armenia and Azerbaijan, recorded double digit growth in addition to Ukraine, while the rate achieved by Greece, though it represented the lowest growth rate in the Black Sea Region, was still twice the Eurozone average.

Table 1 summarises key macroeconomic indicators by country for 2004, showing that the high growth is occurring in a stable macroeconomic environment characterised by lower fiscal deficits (the Region's weighted average fiscal deficit fell to - 2.1% of GDP, the lowest recorded thus far) and low or diminishing inflation. With the exception of Greece, which incurred large one time expenditures related to the successful organisation and implementation of the 2004 Olympic Games, the other Black Sea countries continued to reduce fiscal imbalances by improving revenue collection and/ or strengthening expenditure controls.

Concerning inflation, most Black Sea countries are stable in the mid to lower single digits, and those that are not are close to single digits- all on a declining trend- something which represents a dramatic improvement relative to the previously chronic high double digits and certain bouts of hyperinflation.

Behind these growth figures, there are two particularly encouraging features. First, the smallest Black Sea countries[4] have generally displayed the highest rates of growth within the Region (See Figure 3). The five smallest economies grew collectively by 48.5% in real terms during 2000-2004, nearly 50% more than the 32.7% achieved by the Black Sea Region overall. Generally, these smaller countries had suffered the greatest turmoil and economic decline during the initial years of transition, as well as some of the greatest obstacles to building the institutions and apparatus of sovereign states. Moreover, they remain among the poorer countries in the Black Sea Region, with higher poverty rates and per capita incomes that are lower, for the most part, relative to other regional countries.

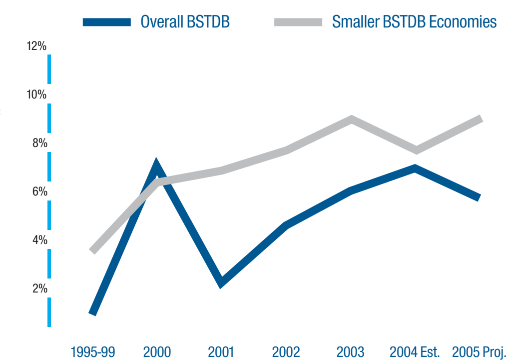


Figure 3: Smaller BSTDB Economies Have Grown Fastest

At a minimum, the relatively higher growth achieved by the smaller economies of the Black Sea Region indicates that the countries which underwent the most trying initial periods of 'transition' are now enjoying growth which includes rapid recovery rates in addition to growth which is attributable to 'new' expansion, with previously underdeveloped sectors such as services and construction representing the fastest growing parts of the economy. That the higher growth has been sustained for a decade now represents a favorable trend, and suggests that they have taken advantage of the 'upside' of the high regional growth and reaped greater benefits. This is important since smaller economies tend to be less diversified than larger economies and thus more vulnerable to adverse events. Moreover, the poorer starting position necessitates higher rates of growth in order to achieve convergence with Black Sea regional averages.

The second encouraging feature of the strong growth is that it has been distributed geographically across the entire Region and observed for all countries, despite the fact that Black Sea countries possess considerably differing economic structures which are increasingly diversifying.

[4] Defined as BSTDB's member countries with annual GDP below US$ 10 billion- Albania, Armenia, Azerbaijan, Georgia, Moldova.

The Region includes energy exporting countries such as Russia and Azerbaijan, a portion of whose growth is related to the increase in global oil prices. Much of Georgia's growth is also energy related, as a transit country for the major oil and gas pipelines from the Caspian Sea to the Mediterranean which are currently under construction. Growth in Albania, Armenia, Moldova, and Greece is the result of strong domestic demand fueled in part by external transfers, with remittances playing a significant role in the case of the first three, while Greek growth is also related to high fixed investment growth and spending for the successfully completed 2004 Olympic Games. Strong consumption has contributed to growth in Romania, Turkey, and Bulgaria, countries which are receiving growing transfers as EU accession countries (or candidates), and benefiting from declining interest rates and an improved investment climate, both associated with progress towards EU membership. Ukraine's growth is also partly due to strong domestic demand, but also to an agricultural recovery and impressive manufacturing growth, with steel exports performing especially well.

The disparities in current account balances (as well as trade balances) in Table 1 underscore the highly and increasingly varied structures of the economies of Black Sea countries, which range from strong exporting countries such as Russia and Ukraine, to countries with high historical trade deficits, such as Albania, Georgia, Moldova, and even Greece. These in turn rely on other sources for external finance, including remittances, external aid, tourism and other exports of services (e.g. shipping). Although some of the current account deficits appear high, the causes behind them suggest that their existence and scope are mainly due to greater investment activity and economic growth, involving increased import of foreign inputs for productive purposes. The case of Azerbaijan is the most telling, as foreign direct investment in the energy sector exceeded 25% of GDP, and this resulted in a surge in imports as virtually all equipment for the development of energy fields and the construction of pipelines was imported.

Evolution of External Perceptions Regarding Prospects in the Black Sea Region

The increasing diversity based on private sector driven, market-oriented growth suggests an emerging complementarity of the economies of the Region, with increased efficiency in the allocation of resources and improved prospects for the expansion and deepening of intra-regional trade and investment linkages- which remain low despite some nascent trends. Coupled with the proximity to the wealthy markets of the EU, and the growing importance of firms from EU countries as trade and investment partners, the Black Sea Region exhibits high potential for continued sustainable growth in coming years.

External perceptions of improvements in the Region have lagged, but certain key external measures are beginning to reflect the observed improvements. Long term sovereign credit ratings represent one such indicator which expresses the confidence of external analysts in the creditworthiness of the countries of the Region. At the beginning of 2004, only one Black Sea country (Greece) enjoyed an investment grade credit rating. During the course of the year Bulgaria, Russia and Romania also achieved investment grade status, while the remaining rated countries of the Region also achieved upgrades and have reached a point where attainment of investment grade credit ratings is not inconceivable in the coming one to three year period if the stability, discipline, and growth of recent record continue. As Table 2 shows, the situation in terms of long term sovereign credit ratings at the end of 2004 represents a significant five year improvement over the sovereign credit ratings observed at the end of 1999.

More tangibly, foreign direct investment (FDI) shows heightened interest and confidence in the Black Sea Region emerging. In the two year period between 2002-2004 Black Sea Region FDI levels tripled in dollar terms, a figure which, given the high growth of the Region's economies and the real appreciation of their exchange rates, represents a near doubling of FDI as a share of GDP to 2.1% from the historic levels of approximately 1-1.2%. The measure of FDI serves as a particularly useful gauge of external perceptions and confidence, since investment figures represent the best available proxy for the translation of external perceptions into economic activity.

While perceptions of the Black Sea Region's prospects have improved and are improving, there is still room for further progress, for even with the impressive growth of the last two years, FDI levels represent a lower share of GDP in the Black Sea Region than they do in the neighboring Central-Eastern Europe and the Baltic new EU entrant states. Thus, whereas on the one hand the argument may be validly made that external perceptions still need additional updating to come around to reflect more accurately the dynamism of the Black Sea Region and its potential, the countries of the Region for their part need to maintain the momentum of political and economic reform which has made possible the achievements of the last few years, to attract further investment, to generate additional wealth creation and employment opportunities, and to raise living standards for their populations.

Table 2: BSTDB Sovereign Credit Ratings Comparison December 1999 vs. December 2004

	December 1999			December 2004		
	Moody's	S&P	Fitch	Moody's	S&P	Fitch
Albania	–	–	–	–	–	–
Armenia	–	–	–	–	–	–
Azerbaijan	–	–	–	–	–	BB
Bulgaria	B2	B+	B+	Ba1	BBB-	BBB-
Georgia	–	–	–	–	–	–
Greece	A2	A-	BBB+	A1	A	A
Moldova	B2	–	B-	Caa1	–	B-
Romania	B3	B-	B-	Ba3	BB+	BBB-
Russia	Ca	SD	CCC	Baa3	BB+	BBB-
Turkey	B1	B	B+	B1	BB-	B+
Ukraine	B3	–	–	B1	B+	B+

3 Countries of Operations Business Environment in 2004

ALBANIA

The Albanian economy has staged a remarkable macroeconomic performance since the slowdown experienced in 2002. Economic growth recovered to 6% annually in 2003-2004, as inflation declined and the current account deficit narrowed, reflecting gains from trade. The principal difference in the growth over the last three years compared to the previous period is that it has occurred against a background of impressive fiscal consolidation, during which government revenues have grown rapidly. This growth has occurred mostly in construction, transport, and services, and less so in industry or agriculture. Given the nature of the growth, as well as the large need for infrastructure development, which requires the importation of goods and equipment from abroad, it is not surprising that Albania has a sizeable structural trade deficit. Substantial volumes of workers' remittances have helped cushion any adverse effects of the latter on the balance of payments. Domestically, the public debt-to-GDP ratio has been reduced considerably and confidence in the national currency has been restored, as reflected in its appreciating trend. Meanwhile, rising incomes have underpinned progress in reducing poverty levels and will be a key factor in achieving job creation and maintaining high rates of economic growth. Improving infrastructure, upgrading industrial and agricultural productive capacity, further encouraging the private sector and improving the business climate further would positively impact investment flows and help bring income up to the potential that exists.

ARMENIA

Armenia's strong macroeconomic performance continued in 2004, fueled by rapid export growth and consumption linked to remittances. As a result, poverty levels have declined and essential social services such as health and education have seen improvements. The growth has been accompanied by the broadening of exports, a reduction in the structural trade deficit, and improvements in the country's current account balance, while key indicators of macroeconomic stability such as inflation and fiscal deficits have remained low and stable. The external debt is decreasing, favorably structured and appears eminently sustainable, as Armenia enjoys access to various sources of external financing- emigrant remittances, grant financing, diaspora investment, concessional financing from international institutions- and is successfully implementing a Poverty Reduction and Growth Facility Program with the IMF. Monetary policy has been tight and prudent, and the financial sector is well regulated, with updated 'best practice' legislation in place. Although financial intermediation in the economy remains low and interest rates are high, bank lending is growing and Armenia is keen to foster further activity in the sector, having taken key measures such as raising capitalisation requirements, enacting legislation to facilitate the registration and enforcement of collateral, requiring the use of international accounting standards for reporting, and the implementing of a deposit insurance scheme in order to boost confidence in the sector. The private sector, which accounts for three quarters of the economy, has led the sustained period of rapid growth. The fastest growth has been in housing construction and services, but also in export oriented industries. Private sector development remains a core part of Armenia's development strategy in order to generate employment opportunities, create wealth, raise living standards and further reduce poverty. Thus, foreign investment is welcomed, and aside from some restrictions on foreign ownership of land, no restrictions exist for foreign investors to invest in existing companies and corporations, and they enjoy equal rights with Armenian citizens.

AZERBAIJAN

Azerbaijan's economic performance in 2004 was strong. Real GDP growth at 10.2% was driven by oil-sector FDI and related spillover effects in the construction, communications and transportation sectors and robust growth in non-oil exports. In addition, non-oil sectors have performed very well. Inflation remained relatively low, as the real effective exchange rate, remained broadly stable. Fiscal policy was tightened in 2004 due to lower-than-budgeted expenditure and strong performance in tax revenues, reflecting the positive impact of tax administration and policy reforms. As a result, the 2004 non-oil fiscal deficit as a share of non-oil GDP materialised at lower than projected levels. Monetary and credit aggregates continued to expand rapidly in 2004, due to the pick up in economic activity outside the oil sector, strong FDI inflows and measures adopted with a view to resist nominal appreciation of the national currency. Balance of payment developments remained positive and non-oil exports continued to grow. Although buoyant growth in bank deposits enabled a significant increase in bank lending, nonperforming loans declined, as did nominal interest rates. Structural reforms accelerated in the second half of 2004.

BULGARIA

Macroeconomic stabilization in Bulgaria has been progressing successfully. The currency board regime that was introduced in July 1997 and is still in place, has made it possible to bring triple-digit inflation in 1996, to single digit figures in 2001 and to maintain them thereafter. Bulgaria's real GDP advanced by 5.3% in 2004. The consolidated government budget also recorded a stronger than anticipated surplus of about 0.9% of GDP. Inflation has accelerated during 2004 at 6.2% compared to only 2.3% in 2003. Strong investment growth, as well as higher consumption demand associated with rising incomes, resulted in high credit growth and a current account deficit of 7,5% of GDP. Nevertheless, FDI inflows are strong and the current account deficit is financed by a combination of FDI inflows and bank borrowing. Furthermore, foreign exchange reserves have accumulated in recent years to a very comfortable level equivalent to 6 months of imports. Ahead of its expected accession to the European Union, Bulgaria's economic policy in 2005-2006 will essentially focus on the implementation of the additional economic stabilization measures required for EU entry.

GEORGIA

Georgia exhibited buoyant growth in 2004, led by manufacturing, telecommunications and construction, and assisted by increased foreign investment and international financial support. Inflation remained low, aided by a tight monetary policy. Thanks to concerted efforts to raise fiscal revenues and reduce the size of unrecorded economic activity, tax receipts increased dramatically in 2004, permitting faster-than-expected clearance of domestic wage and pension arrears, the allocation of resources for capital and social sector spending, and the buildup of government deposits at the Central Bank. The reform agenda of Georgia's new administration aims to improve the economic climate and to implement extensive structural reforms, which will redefine the role of the state in the economy, accelerate privatization and public investment, and improve the business climate at large, in order to attract further domestic and foreign investment. Although the external debt situation remains challenging, Georgia has modified the structure of the debt towards more concessional terms, and during 2004 reached agreement on a new IMF program and with the Paris Club to restructure part of its external debt. The financial sector continued its consolidation against a backdrop of increasing confidence and declining interest rates. As a result, both deposits and the volume of credit extended by banks increased rapidly. Promotion of private sector development represents a strategic objective, and a broad program of accelerated privatization was announced covering energy (extraction, generation and distribution), telecommunications, transportation including the national railway company, and agricultural land and extension, among others. Significantly, the program makes plans for bankruptcy and/or liquidation of insolvent firms and is accompanied by reforms which seek to improve corporate governance, establish a duly regulated competitive environment for firms to operate in and to streamline and simplify the tax code.

GREECE

In 2004, Greece continued to enjoy the sustained economic growth which ranks among the highest in the EU, and has contributed to convergence in income levels towards the EU-15 average. Factors contributing to the growth include strong private consumption and high fixed investment- both public in the form of infrastructure constructed in preparation for the 2004 Olympics and private in the form of a buoyant housing market. The service sector continues to be the largest and most important part of the economy with shipping and tourism playing key roles. Average annual inflation has ranged between 3 - 3.5% and participation in the European Monetary Union (EMU) has helped to entrench macroeconomic stability and supported growth by increasing market confidence, substantially reducing exchange rate risks and permitting a decline in interest rates which spurred investment. Despite impressive improvements in revenue collection, expenditures increased at even greater levels in the run up to the Olympics, and resulted in increased debt and budget deficit levels, beyond the thresholds of EMU's Stability and Growth Pact. Greece has followed a far reaching but gradualist approach to (i) opening up markets and increasing competition in key sectors of the economy, and (ii) implementing a privatization program that has allowed the state to substantially divest itself of holdings in significant sectors such as telecommunications, energy, transport, and banking, and reduced the phenomenon of public sector 'crowding out'. The financial sector is vibrant, and plays an effective intermediation role, and further regulatory reforms are expected in sectors such as energy in order to truly liberalize the electricity market and spur private investor involvement. Additional reforms that have been initiated include a phased reduction in corporate taxation and measures to reduce the transaction costs of establishing and doing business. Entry into the Euro has intensified private sector competition and spurred many Greek firms to expand into BSEC regional markets, especially in the Balkans.

MOLDOVA

Economic growth in Moldova reached 8% in real terms in 2004, on the strength of a favorable external environment and robust consumption growth, fueled in large part by high remittances. Lack of diversification of the economy, with its high reliance on agriculture and food processing, and limited export destinations, remain as structural challenges to be addressed but overall, confidence has continued to grow, as evidenced by remonetization trends in the economy. Tight monetary and fiscal policies have helped entrench macroeconomic stabilization, and a one-off increase in the budget deficit resulted from a favorable debt reduction deal which has reduced external debt levels, and more importantly the debt servicing burden for future years, substantially. Moldova is keen to foster further financial sector growth, having undertaken reforms such as raising capitalization requirements, and improving banking supervision so as to increase confidence. As a result, the sector is well capitalized, and with the enactment of the deposit insurance law in 2004 is poised to play an effective role in enhancing the banking sector's intermediary role. Moldova's current policy priorities focus upon improving social indicators on the one hand, and improving the business environment on the other, in order to stimulate investment and sustained economic growth. To this end, Moldova has adhered to a liberal non-discriminatory foreign investment framework in which foreign investors enjoy equal treatment with domestic investors, they may invest in all sectors of the economy, and they may purchase and trade non-agricultural land. Further reforms mentioned in Moldova's Economic Growth and Poverty Reduction Strategy include reform of the regulatory framework, development and protection of competition, rationalization of corporate management, support and development of Small and Medium Enterprises (SME), promotion of external trade, improvement of investment environment, and creation of a land registry.

ROMANIA

Romania's economy has exhibited a pattern of positive growth and macroeconomic stability in the last three years, on the basis of rising domestic demand and exports expansion, together with buoyant privatization activity, as Romania has engaged on a development path that has proved both solid and sustainable. Over the last three years, GDP expressed in current USD prices grew by over 75 per cent. GDP growth accelerated further in 2004 to some 8.3% on the back of real private consumption growth and gross fixed investment, both of which progressed along an uptrend that had begun in 2003.

A steady improvement in business conditions, as well consumer and investor confidence, resulted from a series of favourable factors. Specifically, the formal recognition of Romania as a "market economy", in addition to the finalization of negotiations with the European Union, aiming for eventual full membership, has resulted in the adoption of EU standards, regulations and practices across all sectors of the economy. In the process, this has intensified economic relations with the EU, which is now Romania's main trading partner.

Against this background, improved fiscal discipline and efficiency gains in fiscal and energy sector revenue collections altogether contributed towards a marked fiscal consolidation. Although net wage growth remained high, helping keep consumption buoyant, disinflation remained on track. Workers' remittances and capital inflows in 2004 were also stronger than expected. The latter reflected higher inward FDI and increased foreign borrowing by banks, which are increasing the size and quality of their credit portfolios, on the back of their financial strength, as well as the improved business sentiment and the still-low indebtedness of households and enterprises.

All together, the favourable outlook of Romania's banking sector is making it easier relative to past years, for the country's corporate sector to gain access to financing under more favourable terms, than was the case in the not-so-distant past. Continuing improvements in Romania's economic competitiveness and business climate, together with further advances with the structural reform agenda in the period ahead, should contribute towards further improving Romania's economic outlook.

RUSSIA

Russia has enjoyed six years of buoyant economic growth averaging 6.7 per cent. Following along this trend, real GDP expanded by 7.1% in 2004, mainly on the back of strong domestic demand. On the supply side, strong growth in services offset a relative moderation in industrial output growth.

Consumption growth, meanwhile, remained buoyant, reflecting rapidly increasing wages, but also making upward pressures on consumer inflation more evident. In addition to solid growth in consumer spending, rising productivity, coupled with strongly-growing wages, falling unemployment, sustained budgetary and balance of payments surpluses, rapid accumulation of gross foreign reserves, declining external debt, in addition to growing inflows of FDI and high volumes of inflows of foreign currency that originated from high energy prices, altogether contributed to a revival of the economy.

Against this background, the trade and current account balances posted record surpluses in 2004. The policy of saving in a stabilization fund, the revenues accruing from high global oil prices, has also benefited the Russian economy at large, to the extent that it has moderated real rouble appreciation, inflation, and interest rates, thereby underpinning steady economic growth.

The Russian government's comprehensive institutional and legal reform program that is currently being implemented, aims to streamline the collection of tax revenues and should ensure that fiscal health remains good in the period ahead. The reform agenda also seeks to help mitigate the risks to the long–term sustainability of growth, and to extend the opportunities arising from the reform process more widely across the population at large.

The ongoing improvement in Russia's external and fiscal balances positions is well-illustrated by the downtrend in Russia's external debt, which has fallen sharply in the course of the last few years to under 30% at present. Accordingly, Russia's external debt is no longer regarded as a prime source of vulnerability, especially as rescheduling agreements have resulted in a favourable maturity structure that stretches through 2030. The rebound in the country's financial markets has also been dramatic.

Russia's federal budget for 2005 targets a surplus of 1.5% of forecast GDP, based on conservative oil price assumptions. As oil prices in 2005 are more likely than not, to tend upwards, the surplus will likely materialize nearer to 2% of GDP.

Provided current global economic trends continue, Russia's GDP is forecast to grow by 6.5% in 2005 and the target of doubling the country's GDP in a decade remains firmly on the country's economic agenda.

TURKEY

Turkey's economic performance in 2004 progressed along the favourable domestic and international trends of the last three years and the economic stabilization program continued to deliver positive results. Output grew by a record 9.9 % in real terms, as inflation fell to its lowest level in a generation and the government debt to GNP ratio declined significantly. GDP growth in 2004 exceeded expectations with a rate of 8.9%, which is a four-decade high. This impressive rate of economic growth is mainly due to the increases in investments and the exports of goods and services.

Gross fixed investment accelerated sharply, the USD 17 billion spent on capital formation being an all time high. Since mid-2002, the nominal exchange rate has remained relatively stable with some nominal appreciation during the last two years, and has appreciated continuously in real terms for three years by about 10% cumulatively. In 2004, the government achieved a primary balance surplus equivalent to 6.5% of GNP.

Thus, against a highly successful policy mix, inflation, as measured by the CPI, declined to 9.3 per cent. Building on this success, the Turkish authorities have slashed six zeroes from the currency and redenominated the latter as the New Turkish Lira. To the extent that the implementation of the current economic program continues successfully into the period ahead, Turkey should be able to create the conditions necessary for sustained long-term growth and employment generation, while reducing inflation further towards European levels.

UKRAINE

An acceleration in the economic growth of Ukraine was evident in 2004. According to the State Statistics Committee of Ukraine, real GDP increased by 12.1% implying the highest growth rate over all previous years.

The dynamic development of economy was supported by sustained high growth of industrial production, which materialized at 12.5 per cent. Export-oriented industries, as well as domestic consumer-oriented industries contributed to the industrial output growth.

Buoyant foreign trade activity and household demand made significant contributions to the evident high economic growth. This, for the most part, was conditioned by extremely favourable external trade conditions and active budgetary, fiscal and social policies of the Government, which were aimed at achieving higher welfare, improved social standards and better labour productivity.

As a result in 2004 exports, imports, nominal wages and real incomes, all recorded high growth rates.

The growth in disposable incomes generated the appropriate conditions for financing consumer demand for high-quality imported consumer durables.

The positive dynamics of both internal and external demand were instrumental in the accelerated growth of incomes which in 2004, exceeded the volumes recorded in 2003 by a high margin that allowed enterprises to use additional revenues for current production expenditures, as well as for increasing inventories.

Despite a loosening of the budgetary policy at the end of the year, fiscal and monetary policies remained on track. This allowed to balance monetary and commodity flows and to maintain macroeconomic and financial stability.

The improvement of the resource base and the high level of banking system liquidity created favourable conditions to stimulate bank lending during the course of the year and the volume of loan-financed investments increased significantly, as did the volume of corporate loans and consumer credit.

The upward dynamics of credit financing was accompanied by a decrease in average weighted monthly interest rates. At the same time, confidence on the part of the population in the banking system increased visibly, as evidenced by a healthy increase in total banking deposits.

In 2004, the Bank moved forward towards achieving its operational goal of mobilizing funds from both within and from outside the region through products tailored to the business needs of regionally active firms and banks and consistent with the development and co-operation objectives of the Member States.

The Bank offers its clients a range of financial products, principally: loans, equity investments and guarantees but also other products tailored to meet specific requirements. The terms of the Bank's financing products are flexible for each client and operation. Adjustments may be made, if so provided in the original documentation, extending to the conversion of one product type to another during the life of an operation. The choice of instrument is, however, determined primarily by client requirements within the framework of the Bank's policies.

The Bank has two main lines of business: Project/Corporate Finance and Trade Finance. In line with its established policies and to most effectively achieve its objectives, the Bank makes two types of operations: direct and through financial intermediaries.

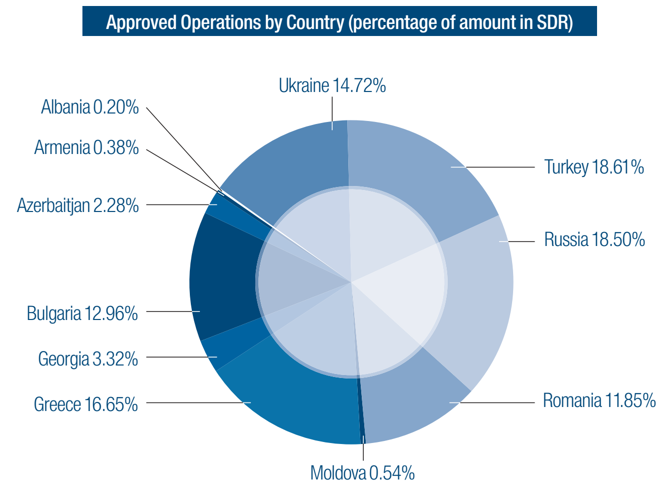
Portfolio Description

The Bank has built up a balanced portfolio mainly comprising short-term revolving facilities and medium to long term project and corporate finance loans, complemented by occasional equity investments and guarantee products. This asset strategy allows a flexible approach to market conditions and generates relatively moderate concentrations of exposure. The Bank maintains its asset quality by following a rigorous due diligence process and by adhering to strict monitoring procedures. As of December 31, 2004, the Bank had only one loan at non-accrual status.

Portfolio Structure by Country

As of end 2004, the Bank's active portfolio consisted of 59[5] approved operations for a total of SDR 426.4 (USD 662.3) million, distributed as follows:

Approved Operations by Country (percentage of amount in SDR)



[5] The total number of approved active operations is 59, but one operation (SEAF – SME equity investment fund) is split among the three beneficiary countries, Albania, Bulgaria and Romania, resulting thus in a total number of operations by country of 61.

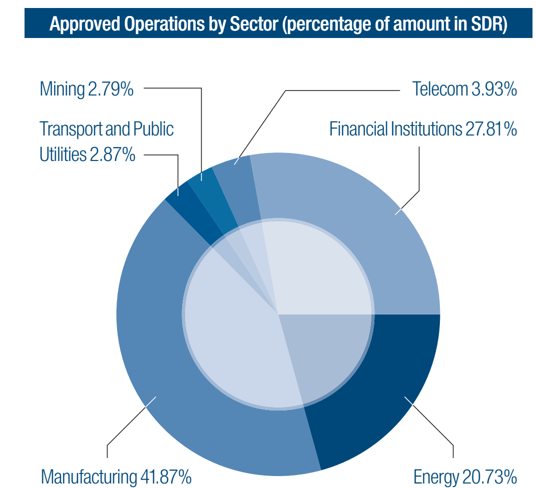
Co-financing

Among the Banks transactions, 11 operations are co-financed with other institutions. The total project cost of these operations is SDR 799.4 (USD 1,241.6) million, of which BSTDB's financing represents 10.25%. Among the co-financiers are international financial institutions - EBRD, IFC and MIGA, official development institutions of developed countries - JBIC (Japan), DEG (Germany), Norfund and Finnfund in Scandinavia, and commercial banks - Citibank, Marubeni, National Bank of Greece, Piraeus Bank, EFG Eurobank, Commercial Bank of Greece and Cyprus Popular Bank.

Portfolio Structure by Sector

By sector, the Bank had at end 2004, 23 approved operations through financial institutions, 23 in manufacturing, 8 in energy, 2 in transport and public utilities, 2 in telecommunications and 1 in mining.

Approved Operations by Sector (percentage of amount in SDR)



Selected BSTDB Financings

Chornomornaftogaz Project, Ukraine

Chornomornaftogaz is a Ukrainian oil-and-gas company whose principle activity is the exploration of reserves and production of primarily gas and gas condensate off the Black and Azov Sea coasts of the Ukraine. The firm possesses more than 25 years of experience in the sector and while its primary activities and assets are on the upstream side, it also operates its own pipelines, delivery systems and storage facilities in Crimea.

BSTDB provided a USD 20 million loan to Chornomornaftogaz, to support the development strategy of the firm, which aims to increase natural gas and gas condensate production and to improve supply to customers in Southern Ukraine and the Crimea. It is anticipated that the Bank's funding will also help to attract additional investors.

The Banks financing will principally support fixed asset investment expenditures- prospecting, drilling of wells, repair programs, constructing of pipelines, etc.- for the development and commissioning of new gas fields and the attainment of increased output from existing fields. The funding will also boost the research and development capacity of the firm for prospecting for new shelf deposits.

The operation is expected to have strong developmental impact, increasing economic activity, creating employment and helping southern Ukraine to improve its energy security, by achieving a stable and continuous supply of gas and energy resources to industries and households. The operation is also expected to have indirect cooperation effects, facilitating the future development of exports to neighboring countries and possibly to western Europe.

Terms and conditions of the operation:

Amount: US$ 20,000,000

Type of Financing: Corporate Loan

Maturity: 7 Years

Neochimiki Project, Greece

BSTDB extended a long-term corporate loan of € 18 million, to Neochimiki L. V. Lavrentiadis S.A. (Neochimiki), the Greek market leader in the production of detergents, for the financing of its capital development plan to be carried out in Greece, Romania and Bulgaria in the years 2003-2009.

In addition to its dominant position in detergent production Neochimiki has made itself the largest trader of chemical products in Greece on behalf of large corporations. As part of its long term strategic development plan, the company is expanding its production base into neighboring Balkan countries and entering local markets dynamically, seeking to expand its customer base against a backdrop of increasing domestic competition and the need to sustain growth.

BSTDB's financing will assist Neochimiki in undertaking this expansion, a key result of which will be employment creation in Romania and Bulgaria as the firm increases its production base. At the same time the expansion of a regional 'blue chip' into the neighboring markets of three of its member countries can only have a favorable impact on regional cooperation.

Terms and conditions of the operation:

Amount: € 18,000,000

Type of Financing: Corporate Loan

Maturity: 7 Years

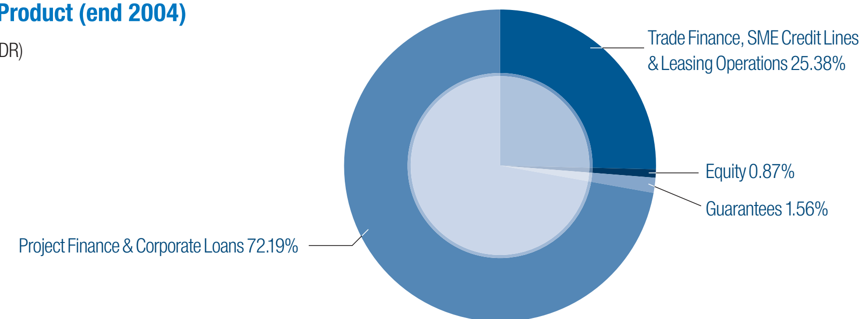
As at the end of 2004 the Bank had 52 operations outstanding, of which 25 (SDR 69.8 million) were in the financial sector, 15 (SDR 117.5 million) in manufacturing, 8 (SDR 50.5 million) in energy, 2 (SDR 7.1million) in transport and public utilities sector, 1 (SDR 3.9 million) in telecommunications, and 1 (SDR 3.5 million) in mining.

Portfolio Structure by Product

Of the 59 operations approved by the Bank's Board of Directors, 36 were in project and corporate finance, 23 in the financial sector, which includes 17 SME credit lines, 2 leasing operations, 2 equity and 2 guarantee operations.

BoD Approvals by Product (end 2004)

(percentage of amount in SDR)



Approved and Signed Operations in 2004

In 2004 the Bank's Board of Directors approved 15 operations for a total amount of SDR 99.1 (USD 154) million. Of these operations 4 were in manufacturing, 2 in energy, 2 in telecommunications and 7 through financial intermediaries. 14 operations were signed for a total amount of SDR 94.2 (USD 146.3) million. By sector, 7 operations were signed with financial institutions, 4 in manufacturing, 2 in energy, and 1 in telecommunications. By product, 7 were project and corporate finance operations and 7 were trade finance operations and SME credit lines.

Selected BSTDB Financings

Teleset Project, Russia

BSTDB extended a USD 10 million loan to Teleset Limited, the second largest private fixed-line communications operator in Kazan; the 8th largest city in Russia with a population of 1.1 million. The firm is the first fully foreign owned 100% digitalised PSTN (Public Switch Telephone Network) operator in the Russian Federation, and currently serves about 70,000 subscribers.

BSTDB financing will support the company's network expansion plan to regions beyond Tatarstan, which include the construction of an intra-city and inter-city fiber optic backbone and Internet infrastructure. This development will help reduce the historically long waiting list of subscribers for fixed-line telephonic services in the Volga Region of Russia, while meeting the demand for quality internet services, at low cost. It is expected that following the completion of the project, at least 10,000 new subscribers per annum will have access to Teleset's telecom services.

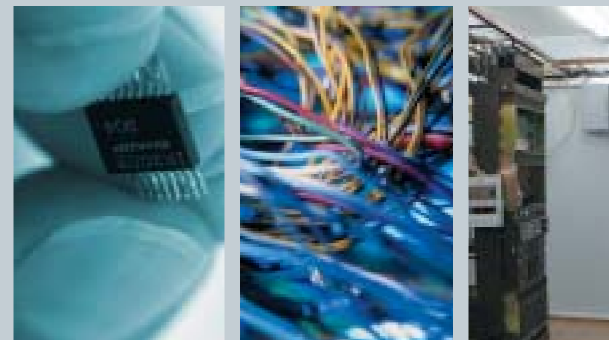
In addition to creating new jobs, as a result of the expansion, and helping to improve consumer choice, the operation will assist the development of telecommunications infrastructure in underserved regions of the country.

Terms and conditions of the operation:

Amount: US$ 10,000,000

Type of Financing: Corporate Finance

Maturity: 7 Years



Pakel Project, Turkey

BSTDB's loan of US$ 13 million to Pakel Kimya Tekstil A.S. will finance the establishment of an acrylic fiber manufacturing plant and entail the construction of a co-generation plant to produce electricity and steam. The project will complement the operations of the "Akteks" Group, a prominent Turkish private textile group engaged primarily in the production and marketing of yarns.

The operation will help Pakel to reduce manufacturing costs, upgrade control of its quality and flow of raw materials, and improve responsiveness and flexibility to customers' requirements, thus enhancing its competitive position.

The Bank financing is part of an overall investment of US$ 39 million, taking place in the Free Trade Zone of Yumurtalik in southern Turkey. The Bank's involvement thus facilitates economic investment which will directly result in the creation of 200 new jobs, while also contributing to further job creation upstream and downstream. In addition, by helping Pakel to develop further its exporting activity the operation will benefit the overall Turkish economy.

Terms and conditions of the operation:

Amount: US$ 13,000,000

Type of Financing: Project Finance

Maturity: 7 Years

Special Fund

The Bank administers one Special Fund (the Hellenic Fund) established with the Contribution Agreement between the Government of the Hellenic Republic and BSTDB in July 2001. The Fund was instituted with an initial amount of Euro 800,000 and was replenished by Euro 500,000 in 2003. The Fund is tied to consulting companies based in Greece. However, up to 25% of an assignment cost may be allocated to consultants who are nationals of the Bank's other member countries.

Altogether, the Hellenic Fund has commited about Euro 543,000 to new consulting assignments since its creation. Out of this amount Euro 441,250 have been disbursed. The sectors benefiting from these funds have included telecoms, oil & gas, manufacturing, transportation, and banking. These funds were distributed among six member states - Albania, Ukraine, Georgia, Russia, Bulgaria, and Greece. In 2004 the Fund spent about Euro 125, 000 on two assignments. The total disbursements from the Fund are expected to reach Euro 700,000 by the end of 2005.

BSTDB Joint Finance Facility with Izmirlian Foundation, Armenia

BSTDB and the Izmirlian Foundation established a joint credit line facility, the Joint Finance Facility, in February 2003 in Yerevan, for direct lending to small and medium sized enterprises in Armenia whereby the Bank and the Izmirlian Foundation jointly finance Armenian SMEs. The Izmirlian Foundation (IF) is a non profit organisation established in 1994 by the Izmirlian family to provide humanitarian assistance in the aftermath of the devastating earthquake in Armenia and to mitigate the economic and social difficulties triggered by the collapse of the Soviet Union. BSTDB and the IF allocated USD 2 million each for joint lending to Armenian SMEs.

- The facility represents a special type of operation and was designed taking into account the structure of the Armenian economy, the characteristics of its industry and the limitations of the Armenian banking and financial environment.
- In 2004, BSTDB and the IF extended long-term corporate loans of $260,000 to Tosp, a manufacturer of knitted and crocheted wear and ready-made garments and $380,000 to Hytex Plastic, Armenia's leading manufacturer of PET pre-forms for plastic bottles and jars.
- This facility will assist Armenian SMEs with new investment in production facilities, thus increasing volumes and supporting export activity. This enhanced activity will foster employment opportunities, improve the business environment in Armenia and generate trade with other Black Sea member countries.

Terms and conditions of the operations:
Amount: Up to $500,000 (each)
Type of Financing: Corporate Loan
Maturity: 5 Years

Financing the Development of Small and Medium Enterprises Working with Procredit Institutions in the Black Sea Region

Small and medium enterprises (SMEs) are among the key driving forces of economic growth in the Black Sea Region. Growth of these firms has expanded rapidly in the Region as the private sector has grown, and they have played a key role in the generation of new employment in member countries, in many cases accounting for well over half of all new job creation and an increasingly important share in gross value added. They have played a key role in the development of the services sectors in the Region, and almost all operate in the private sector. As in the economies of developed countries, turnover in the creation and dissolution of SMEs has been more rapid than for larger enterprises, although their growing share of the economy indicates that there is an overall upward trend. While the progress has been impressive, there is still room for further growth in the Region and potential for them to increase their positive role in fostering private sector growth and employment expansion. BSTDB has emphasized the provision of assistance to SMEs in a number of its operations, offering an array of products mainly through financial intermediaries in the Region.

Among the more prominent financial intermediaries that specialize in SMEs in transition countries are the ProCredit institutions, and BSTDB has actively sought cooperation with branches active in the Black Sea Region. During 2004, the Bank signed/ extended three such operations in Bulgaria, Moldova and Ukraine. Two of the operations involve lending, while the other represents provision of a guarantee.

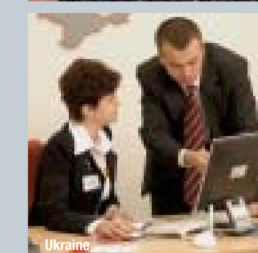
Procredit Bank, Bulgaria
Terms and conditions of the operation:
Increased Amount: € 5,000,000
Type of Financing: Micro and SME Finance Facility
Maturity: 3 years

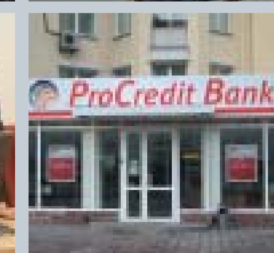
Procredit Moldova
Terms and conditions of the operation:
Guarantee Amount: € 2,300,000
Type of Financing: Guarantee for Micro and SME Finance Facility
Maturity: 3 years

ProCredit Bank, Ukraine
Terms and conditions of the operation:
Increased Amount: $ 2,500,000
Type of Financing: Micro and SME Finance Facility
Maturity: 3 years

Bulgaria

Moldova


Ukraine



Environment Protection

The Bank has a distinctive environmental mandate for the region: protection of the Black Sea against pollution, promoting environmental soundness and sustainable development in all its loan operations. Thus, the Bank seeks to ensure that all the potential environmental risks arising from its operations that are likely to affect the state of environment, human well-being and ultimately the Bank itself, are properly identified, assessed and mitigated. In line with this the Bank undertakes independent environmental assessment of all proposed operations. It analyses all the environmental implications, proposes efficient mitigation measures, and incorporates them into the overall decision-making process before the Bank makes a commitment to finance. For on-going operations the Bank closely monitors the environmental aspects of its financing.

In undertaking its environmental mandate the Bank is guided by its Environmental Policy and Environmental Assessment Procedures document. Assessment of the environmental acceptability of proposed transactions together with the environmental performance of the potential Clients is carried out in line with these procedures, as well as relevant best practices applied by other IFIs. All operations that pass the Banks Concept Clearance stage are subject to Environmental Assessment.

Selected BSTDB Financings Selected BSTDB Financings Selected BSTDB Financings Selected BSTDB Financings Selected BSTDB Financings

Promoting Regional Trade - Banca Transilvania, Romania

A distinguishing aspect of BSTDB's activities is its emphasis on trade promotion and financing. The expansion of trade among Black Sea countries has positive developmental and regional cooperation impact, but is also a necessity for the economies of the Region as they seek to increase output and production, to generate new employment, to diversify and increase sources of foreign exchange generation, and improve the competitive position of the exporting sector. For its part, the Bank seeks to support promising regional financial institutions that are active in trade financing, have a financially sound background, possess a network for the distribution of funds locally, and are interested in expanding their operations internationally. BSTDB provides liquidity, but also the opportunity for financial institutions to enrich their track record of operations and to develop a network and contacts with other regional and international financial institutions. BSTDB and Banca Transilvania signed a EURO 5 million short-term export-import finance facility, enabling Banca Transilvania to advance sub-loans to Romanian exporters and importers to finance contracts with their counterparts from the Black Sea Region. The facility also supports Romanian exports to countries outside the Black Sea Region and allows Romanian companies to propose deferred payment terms under export contracts. Banca Transilvania targets financing the needs of small and medium sized enterprises. It operates as a commercial bank, providing a wide range of products to its corporate clients, with a network of 51 operational units, extending across the entire country.

Terms and conditions of the operation:
Amount: € 5,000,000
Type of Financing: Short-term Revolving Trade Finance Facility
Maturity: 360 days

Resources Management

Human Resources Management

BSTDB recognises that human resources are a key factor in the ultimate success of the institution and strives to maintain its status as a competitive employer by following the best international standards and practices. During 2004 the Bank conducted a comprehensive human resources policy review and implemented a number of changes aimed at increasing the clarity, fairness and transparency of the system.

The Bank's recruitment policies provide for the hiring of employees on a wide geographical basis, preference being given to the citizens of member countries. At the end of 2004, the Bank had 97 employees, from 15 countries, including representatives from all its 11 member states.

The Bank operates a market – oriented staff compensation policy designed to match the employment standards of other IFIs.

The BSTDB Pension Plan, implemented in January 2003, is comprised of a fully funded defined benefit scheme and a matched contribution plan. This combination offers the flexibility crucial to best meet the needs of a multinational work force.

Information Technology

BSTDB has implemented a highly available optical Storage Area Network (SAN) to consolidate and protect its critical data. The connection of the devices attached to the SAN is done through fiber optic switches and wires, increasing the performance of application and data access. The Bank has also put in place a tape library, directly attached to the SAN through fiber switches, allowing for fast and automatic backup of all SAN data.

The Bank has developed disaster recovery plans for its IT systems and data. All critical data is replicated to secondary storage systems using Veritas storage and replication software. Critical IT systems are also replicated on standby hardware and are ready to take over the operation of the primary IT systems.

External Relations and Communications

BSTDB continues to actively develop its corporate relations with member state governments, international institutions and the business community.

In 2004 BSTDB focused on contacts with non-regional governments and institutions with a view to promoting the Bank's recently established observer status.

Relations with the European Commission were further strengthened through participation in the coordination mechanism under the Memorandum of Understanding between the Commission and other IFIs on co-operation for EU accession of some BSTDB member countries (Bulgaria, Romania, and Turkey), which BSTDB joined in 2003. The bank entered negotiations to join another MOU with the Commission and IBRD and EBRD on cooperation in other BSTDB member countries participating in CIS.

In its drive to develop business contacts and to promote investment and cooperation in the region, the Bank hosted its annual Black Sea Business Day in Tirana in June 2004. The event was held under the auspices of the Albanian Government and with the support of local business associations and foreign investors.

Financial Management

Revenues

In this year of operation, the Bank increased the size of its lending portfolio to SDR 244,310 thousand from SDR 170,373 at the end of 2003, an expansion of nearly 43%. As a result total income from Project and Trade financing operations rose to SDR 12,429 thousand during the year from SDR 6,639 thousand in 2003.

Treasury activities in 2004 generated total interest income of SDR 2,033 thousand from placements with other financial institutions and investment in short-term money market instruments.

Total operating income for the year was SDR 13,882 thousand, a substantial increase from the previous year.

Expenses

General administrative expenses, including depreciation, for the year were SDR 9,825 thousand, an increase of SDR 401 thousand on 2003. General administrative expenses include salaries, benefits and other administrative costs.

Salaries and benefits, in the amount of SDR 6,948 thousand, showed a modest increase of SDR 284 thousand from the previous year.

Overall, general administrative expenses were well within the 2004 Budget, reflecting the Bank's effective cost controls.

Capital Base

As specified in the Establishing Agreement, the BSTDB's initial authorised capital stock is one billion (1,000,000,000) Special Drawing Rights (SDR) divided into one million (1,000,000) shares, each with a par value of one thousand (1,000) SDR.

All participating Member States of the Bank had initially fully subscribed to their portion of the initial authorised capital stock. The subscribed capital is composed of:

- ten per cent (10%) fully paid shares
- twenty per cent (20%) paid by promissory notes (eight equal annual instalments, encashment starting from the year 1998) and
- seventy per cent (70%) callable shares.

The aggregate par value of the initial authorised fully paid shares is SDR 100 million and that of the capital paid by promissory notes is SDR 200 million. At the Sixth Annual Meeting of the Board of Governors held in June 2004, Armenia, Georgia and Moldova requested a fifty per cent reduction in their portion of the subscribed capital, which was approved by the Board of Governors.

As of 31 December 2004, 266.75 million SDR's were due to be paid-up by the participating Member States, in accordance with the schedule stipulated in the Agreement. This included the ten per cent fully paid shares and seven of the eight equal annual instalments of the twenty per cent shares payable by promissory notes. The total initial authorised capital stock of the Bank of SDR one billion remained unchanged.

Gearing Ratio

The Establishing Agreement places a number of institutional limitations on the use of the Bank's capital for its ordinary operations. Treasury investments, comprising the Bank's investment of its capital and those assets held for liquidity purposes, are considered auxiliary to the Bank's ordinary operations.

The Bank's institutional gearing ratio, the statutory limit on the total amount of ordinary operations (outstanding loans, equity investments and guarantees) is 150% of the Bank's unimpaired subscribed capital, reserves and surpluses, and as at 31 December 2004 stood at slightly above SDR 1.5 billion.

During the 36th meeting of the Board of Directors held in December 2003, the operational gearing ratio was set at 100% of the Bank's unimpaired paid-up capital, reserves and surpluses and the usable portion of callable capital6. This limit on the total amount of operations stood at about SDR 920 million, as of 31 December 2004, and will amount to approximately SDR 1 billion when all paid-in capital is received by the Bank.

Provisioning

The IAS compliant BSTDB provisioning policy is designed to ensure that the level of general provisions is commensurate with overall portfolio risk levels. While each project contributes to the general provisions, specific provisions are only allocated if and when an operation encounters difficulties. Total provisions at end of 2004 stood at SDR 13,310 thousand equivalent to 5.4% of the outstanding loans and equity investments.

The institutional target to be achieved for total provisions, over time, is set at 10% of disbursed loans and 25% of disbursed equity investments.

Market Risk

Market risk management is conducted within a framework of conservative risk limits and policy documents approved by the Board of Directors. More specific subsidiary documents detailing credit risk parameters, liquidity restrictions, interest rate and foreign exchange risk are approved on an ongoing basis by the appropriate executive committees.

It is the policy of the Bank to take no significant interest rate or foreign exchange exposure. Asset and liability maturities and interest rate tenors are matched wherever possible and the SDR denominated capital, reserves and surpluses are invested in the SDR constituent currencies at weightings intended to keep foreign exchange exposure to a minimum.

Investment / Liquidity

The Bank's surplus funds, totaling SDR 45,907 thousand as at 31 December 2004, were invested in two types of money market instruments:

- Short term deposits with institutions long term rated at a minimum of A2/A by either Moody's or Standard & Poors credit rating agency.
- Euro commercial paper rated at a minimum short term A2/P2 by either Moody's or Standard & Poors credit rating agency.

Investments are denominated in one of the four SDR component currencies and performance is monitored monthly against the Merrill Lynch 3 month Libid index.

The Bank's liquidity ratio calculated as liquid assets over 12 months net cash requirement including signed undisbursed commitments, stood at 146 % on 31 December 2004.

Borrowing

In March 2004, the Bank obtained from Moody's Investor Services initial investment grade ratings of long term Baa2 and short term P2. As the size of the Bank's operations portfolio continued to increase during the latter part of the year and taking into consideration its minimum liquidity requirements, the Bank found it necessary to access sources of long term funds. Two loan agreements were signed in that respect:

- A EUR 15 million 9 year amortizing facility provided by Nordic Investment Bank to enhance co-operation in the financing of projects of mutual interest.
- A USD 60 million 3 year bullet syndicated loan subscribed by 7 major commercial European banks. Proceeds to be drawn for general funding purposes. As at 31 December 2004, USD 10 million had been drawn under this facility.

Similar sources of funding should accommodate the long term funding needs of the Bank in 2005.

Risk Analysis

An independent financial analysis is performed for each of the Banks operations. Corporate entities are initially subject to an assessment of creditworthiness based on historical financial statements. This is followed by cashflow modelling for the life of the proposed operation and stress testing of key assumptions. For financial institutions risk analysis is based on quantitative methodology (i.e. capitalisation, asset quality, liquidity and foreign exchange risk) supported by comparisons of key ratios to industry standards.

Risk Mitigation

The Bank will normally require its operations to benefit from some form of security or risk-sharing in order to mitigate the credit risks involved. When the Bank lends to public or private sector borrowers, it will normally require certain guarantees and, in all cases, will ensure that the parties involved share risks in a reasonable manner.

Evaluation

The Bank conducts assessments of completed and ongoing operations, programs, activities and strategies through rigorous systematic analyses. This evaluation process serves two key objectives: (i) accountability – to reveal the results and impact of the Bank's operations; and (ii) learning – to derive lessons learned from past experience, maintain a corporate memory and enhance future performance.

Preferred Creditor Status

As an international financial institution, the Bank has preferred creditor status. This means that the Bank usually will:

- not reschedule debt payments or participate in debt rescheduling agreements with respect to its loans to, or guaranteed by, its member countries of operations.
- not reschedule its loans to private sector borrower where the borrower's inability or anticipated inability to service its debt is due to a general foreign exchange shortage in the borrower's country.

Corporate Governance

Management structure

The BSTDB is committed to maintaining effective corporate governance through a framework of responsibilities and controls. Transparency and accountability supported by clearly defined reporting systems enable maintenance of an appropriately controlled business environment.

The BSTDB's governing constitution is set out in the Agreement Establishing the Bank. This document requires that the institution be managed by a Board of Governors (BoG), a Board of Directors (BoD), a President, Vice Presidents, a Secretary General and such officers and staff, as may be necessary.

Each of the Bank's Member States is represented on the BoG and BoD. All powers of the Bank are vested in the BoG. With certain exceptions the BoG has delegated the exercise of these powers to the BoD, while still retaining overall authority.

The BoD, chaired by the President of the Bank, is responsible for guiding the general operations of the Bank. Each of the Bank's Member States appoints a Director and an Alternate Director with full powers to act for the Director, when the Director is not present.

The Audit Committee is established by and reports directly to the BoD. The composition of the Audit Committee is three BoD Members, one being appointed as Chairman.

The President, as chief executive of the Bank, is its legal representative. In this capacity, and as Chairman of the Management Committee he conducts the current business of the Bank under the direction of the BoD. The President is appointed by the BoG.

The Management Committee is comprised of the President (as Chairman), the three Vice Presidents and the Secretary General. In the absence of the President, one of the Vice Presidents chairs the meetings of the Management Committee. The Vice Presidents and Secretary General are appointed by the BoD on the recommendation of the President.

Reporting and Disclosure

The BSTDB's corporate governance structure is supported by appropriate financial and management information reporting. Through its reports and disclosures the Bank, in line with its policy of maintaining industry best practice, follows the reporting conventions of other international financial institutions. The Accounting Policies adopted by the Bank are based on International Financial Reporting Standards.

With respect to external financial reporting, the Bank presents financial statements in its quarterly Summary Statements and in the Annual Report. Pursuant to Article 35 of the Agreement, these reports are transmitted to the Governments of the Member States (Annual Report only), members of the Board of Governors and Directors and the BSEC Permanent International Secretary. The Annual Report for 2004 is the sixth report published following the commencement of operations of the Bank.

In its financial reporting, the Bank aims to provide appropriate information on risk and performance. Industry best practice will guide the evolving disclosure practice both in public financial reports and management information reporting, with the ultimate aim of enhancing accountability throughout the organisation.

Financial Statements for the Year Ended 31 December 2004 Together with Auditor's Report

INCOME STATEMENT

For the year ended 31 December 2004

Expressed in thousands of SDR	Note	2004	2003
Interest and similar income			
From loans		10,845	5,816
From placements with financial institutions		454	391
From investment securities		1,579	2,860
Interest expense and similar charges	12	(495)	(130)
Net interest income		12,383	8,937
Net fees and commissions	3	1,584	823
Net income (loss) on foreign exchange		(82)	(93)
Other income (expense)		(3)	1
Operating income		**13,882**	**9,668**
General administrative expenses	4	9,406	9,019
Depreciation	10	419	405
Income before provisions		**4,057**	**244**
Provisions for losses	5	4,256	5,378
Net (loss) for the year		**(199)**	**(5,134)**

The accompanying notes are an integral part of this statement.

BALANCE SHEET

At 31 December 2004

Expressed in thousands of SDR	Note	2004	2003
Assets			
Cash and bank balances	15	2,690	16,890
Placements with financial institutions	15	24,546	30,054
Investment securities	15	18,671	37,659
Total deposits and securities		45,907	84,603
Loans	7	244,310	170,373
Equity investments	8	2,557	2,625
Less: provisions for losses	5	(13,310)	(9,375)
Net loans and equity investments		233,557	163,623
Receivables and accrued interest		1,836	1,566
Paid-in share capital not received	6	3,902	10,926
Property, technology and equipment	10	1,496	1,418
Intangible assets	10	1,060	1,023
Less: accumulated depreciation	10	(1,913)	(1,504)
Net property, technology and equipment		643	937
Other assets	11	1,176	2,285
Total Assets		**287,021**	**263,940**
Liabilities			
Borrowings	12	6,654	0
Payables and accrued interest	13	353	659
Deferred income	3	2,387	2,177
Total liabilities		9,394	2,836
Members' Equity			
Authorised share capital	6	1,000,000	1,000,000
Less: unallocated share capital	6	(30,000)	0
Subscribed share capital	6	970,000	1,000,000
Less: callable share capital	6	(679,000)	(700,000)
Less: payable share capital	6	(24,250)	(50,000)
Advance against future call	6	29	57
Paid in share capital		266,779	250,057
General reserve	14	3,666	3,666
Retained earnings		7,182	7,381
Total member's equity		277,627	261,104
Total Liabilities and Members' Equity		**287,021**	**263,940**
Off-balance-sheet items			
Commitments	9	79,617	100,144

The accompanying notes are an integral part of this statement.

STATEMENT OF CHANGES IN MEMBERS' EQUITY

For the year ended 31 December 2004

	share capital					
Expressed in thousands of SDR	Subscribed	Callable	Payable	General Reserve	Retained Earnings	Total
At 31 December 2002	**1,000,000**	**(700,000)**	**(74,980)**	**3,666**	**12,515**	**241,201**
Paid -in share capital			25,000			25,000
Advance against future call			37			37
Net (loss) for the year					(5,134)	(5,134)
At 31 December 2003	**1,000,000**	**(700,000)**	**(49,943)**	**3,666**	**7,381**	**261,104**
Unallocated share capital	(30,000)	21,000	750			(8,250)
Paid-in share capital			25,000			25,000
Advance against future call			(28)			(28)
Net (loss) for the year					(199)	(199)
At 31 December 2004	**970,000**	**(679,000)**	**(24,221)**	**3,666**	**7,182**	**277,627**

The accompanying notes are an integral part of this statement.

STATEMENT OF CASH FLOWS

For the year ended 31 December 2004

Expressed in thousands of SDR	Note	2004	2003
Cash flows from operating activities			
Net (loss) for the year		(199)	(5,134)
Adjustment for:			
Provisions for losses	5	4,256	5,378
Depreciation	10	419	405
Interest and similar income		(12,878)	(9,067)
Interest expense and similar charges	12	495	130
Foreign exchange adjustments on provisions	5	(321)	(420)
Operating profit before working capital changes		(8,228)	(8,708)
Decrease (increase) in other assets	11	1,109	(2,117)
Increase (decrease) in accounts payable	13	(325)	(2,394)
Increase (decrease) in deferred income	3	210	1,061
Cash generated from (used for) operations		(7,234)	(12,158)
Interest and similar income received		12,608	10,163
Interest and similar charges paid		(476)	(81)
Net cash from (for) operating activities		4,898	(2,076)
Cash flows from investing activities			
Proceeds from repayment of loans	7	93,136	51,102
Proceeds from repayment of equity investments	8	577	328
Proceeds from maturity of investment securities	15	0	58,376
Funds advanced for loans	7	(167,073)	(136,395)
Funds advanced for equity investments	8	(509)	(453)
Purchase of investment securities	15	0	(39,454)
Purchase of property, technology and equipment	10	(125)	(515)
Net cash (used in) from investing activities		(73,994)	(67,011)
Cash flows from financing activities			
Increase in paid-in share capital	6	16,750	25,000
Share capital replenishment portion received		0	854
Decrease (increase) in share capital S.T. receivable	6	7,024	(519)
Increase (decrease) in advance against future call	6	(28)	37
Paid-in share capital received		23,746	25,372
Increase in borrowings	12	36,961	15,334
Repayments of borrowings	12	(30,307)	(15,334)
Net cash provided by financing activities		30,400	25,372
Net increase (decrease) in cash and cash equivalents		**(38,696)**	**(43,715)**
Cash and cash equivalents at beginning of year		84,603	128,318
Cash and cash equivalents at end of year	15	**45,907**	**84,603**

The accompanying notes are an integral part of this statement.

Notes to the Financial Statements

For the year ended 31 December 2004

1. ESTABLISHMENT OF THE BANK

1.1 Agreement Establishing the Bank

The Black Sea Trade and Development Bank ("the Bank"), whose headquarters is located at 1 Komninon Street, Thessaloniki, in the Hellenic Republic, was established as an international financial organisation under the Agreement Establishing the Bank dated 30 June 1994 ("the Agreement"). In accordance with Article 61 of the Agreement, the Bank was established and the Agreement entered into force on 24 January 1997. The Bank commenced operations on 1 June 1999.

As at 31 December 2004 the Bank's shareholders comprised 11 countries: Albania, Armenia, Azerbaijan, Bulgaria, Georgia, Greece, Moldova, Romania, Russian Federation, Turkey and Ukraine.

The financial statements for 2004 have been submitted by the Management Committee to the Board of Directors for approval on 22 April 2005. Pursuant to Article 23 of the Agreement, these financial statements shall be subject to approval by the Board of Governors in their Annual Meeting to be held on 5 June 2005.

1.2 Headquarters Agreement

The status, privileges and immunities of the Bank and persons connected therewith in the Hellenic Republic are defined in the Headquarters Agreement between the Government of the Hellenic Republic and the Bank ("Headquarters Agreement") signed on 22 October 1998.

2. SIGNIFICANT ACCOUNTING POLICIES

2.1 Basis of financial statements

The financial statements have been prepared in accordance with International Financial Reporting Standards (IFRS) as published by the International Accounting Standards Board.

The financial statements have been prepared on a historical cost basis. The Bank has not applied any IFRS before their effective dates.

The Bank's measurement and reporting currency is Special Drawing Rights (SDR), which is the unit of account for the Bank's authorised share capital, pursuant to Article 4 of the Agreement.

2.2 Foreign currencies

Foreign currency transactions are initially recorded in SDR by applying to the foreign currency amount the exchange rate between the SDR and the foreign currency at the rate prevailing on the last day of the month, preceding the date of the transaction, as provided by the IMF. Exchange gains and losses arising from the translation of monetary assets and liabilities at year-end exchange rates are taken to the income statement.

For the purpose of the preparation of the financial statements, the following year-end exchange rates were used for monetary assets and liabilities:

	2004	2003
1 SDR = United States dollar	1.55301	1.48597
Euro	1.13874	1.17897
Japanese yen	159.10600	158.86500
Pound sterling	0.80409	0.83262

2.3 Investments

All investments are initially recognised at cost, being the fair value of the consideration given and including acquisition charges associated with the investment.

Investments intended to be held to maturity are measured at amortised cost, by applying the effective interest rate method, less any provisions for impairment. Gains and losses are recognised in income when the investments are derecognised or impaired as well as through the amortisation process.

Investments in equity instruments that do not have a quoted market price and for which other methods of reasonably estimating fair value are inappropriate, are measured at cost less provision for impairment, where there is objective evidence of impairment. Since the Bank does not prepare consolidated financial statements, investments in associates are measured at cost less provision for impairment. When equity investments are sold the difference between the net proceeds and the carrying value is recognised in the income statement as a gain or loss on sale of equity investments.

2.4 Loans and provisions for losses

Loans providing money directly to a borrower are categorised as loans originated by the Bank and are carried at amortised cost. All loans and advances are recognised when cash is advanced to borrowers. Loans on which either interest or capital is unpaid for 90 days are classified as being at non-accrual status and interest on such loans is not recognised until collected.

A provision for loan impairment is established if there is objective evidence that the Bank will not be able to collect all amounts due. The amount of the impairment is the difference between the carrying amount and the recoverable amount, being the present value of expected cash flows, including amounts recoverable from guarantees and collateral, discounted based on the interest rate at inception.

A specific provision is made for all loans that are individually identified as impaired. If no objective evidence of impairment exists for an individually assessed financial asset, whether significant or not, this is included in a portfolio of financial assets with similar credit risk characteristics. These portfolios are collectively assessed for impairment, using a risk-rated approach, which takes into consideration the country risk and the operations risk applicable by industry segment.

When a loan is deemed uncollectable or there is no possibility of recovery of an equity investment, the principal is written off against the related specific or the general (collective) loss provision. Loans are only written off when the borrower is liquidated or all legal and other avenues for recover or settlement are exhausted. Recoveries of loans previously written off are credited to the income statement.

2.5 Property, technology and equipment

Property, technology and equipment, which include intangible assets, are stated at cost, less accumulated depreciation. Depreciation is provided so as to write off the cost of each asset to their residual values on a straight-line basis over their estimated useful lives. The annual depreciation rates applied are as follows:

• Furniture, furnishings and appliances	20.0%
• Personal computers	33.3%
• Office and telecommunication equipment	20.0%
• Transportation vehicles	20.0%
• Computer software	33.3%

Expenditure on leasehold buildings and improvements are depreciated over the remaining term of the lease.

2.6 Income and expenses

Interest income and expense are recorded on an accrual basis, with the exception of interest on loans overdue by more than 90 days that have been placed on non-accrual status for which interest is recorded when received. Loan commitment and guarantee fees and fees received in respect of services provided over a period of time are recognised as income on an accrual basis matching the period during which the commitment exists or the services are provided. Front-end fees pertaining to loans are amortised through the income statement using the effective interest rate method over the life of the loans, in the case of early repayment, cancellation or acceleration of loans the outstanding deferred income from the related fees are recalculated taking into account the new maturity date. Dividends are recognised when received. General administrative expenses are recorded on an accrual basis.

2.7 Staff retirement plan and termination benefits

The Bank has established a pension plan, where the fund's assets are held separately from the Bank's own assets, for all its permanent employees, consisting of three pillars:

- The first pillar is a defined benefit scheme financed entirely by the Bank. The Bank's contributions are determined on the basis of actuarial valuations using the projected unit credit method, performed annually by qualified, independent actuaries;
- The second pillar is a defined contribution scheme to which both the employee and the Bank contribute equally at a rate of 0-7.5% of basic salary. Each employee determines his/her contribution rate and the mode of investment of the contributions; and
- The third pillar is a defined contribution scheme funded entirely by each employee, up to 40% of basic salary.

Local staff are alternatively entitled to retirement benefits from the Greek State Social Insurance Fund (IKA), which is a defined contribution scheme.

Current service costs in respect of both the pension plan and social insurance contribution schemes (IKA) are recognised as an expense and included in "General administrative expenses".

Employee termination indemnities are charged to the income statement when there is a formal plan to terminate the employment of eligible employees.

2.8 Taxation

In accordance with Article 52 of the Agreement, the Bank, its assets, property, income and its operations and transactions are exempt from all taxation and all customs duties in Greece. The Bank is also exempt from any obligation for payment, withholding or collection of any tax or duty. Also no tax shall be levied on salaries or emoluments paid by the Bank to employees. These tax exemptions are enforced by the Headquarters Agreement of Article 12, and have been implemented by the Greek Government by virtue of the ratification of Law 2380/No.38/7.3.1996.

2.9 Borrowings

Borrowings are stated at costs. Borrowing costs are recognised as expenses and recorded on an accrual basis.

2.10 Derivative financial instruments

In the normal course of business the Bank is a party to spot and forward foreign exchange contracts. These instruments are used to hedge currency exposure associated with the Bank's assets and liabilities and are stated in the balance sheet at fair values, with any revaluation resulting in a gain or loss taken to the income statement. The sum of derivatives is carried as an asset when its fair value is positive and as a liability when its fair value is negative.

2.11 Cash and cash equivalents

For the purpose of the Statement of Cash Flows, cash and cash equivalents consists of cash on hand, placements with other financial institutions and debt securities with maturities of three months or less.

2.12 Use of estimates

The preparation of financial statements involves management estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements, and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates.

3. NET FEES AND COMMISSIONS

Net fees and commissions in the income statement are analysed as follows:

Expressed in SDR (000)	2004	2003
Front-end fees	686	326
Commitment fees	251	276
Guarantee fees	163	65
Management fees	97	70
Appraisal fees	111	71
Prepayment/cancellation fees	244	0
Other	32	15
Net fees and commissions	**1,584**	**823**

The deferred income balance as of 31 December 2004 was SDR 2,387 thousand and as of 31 December 2003 was SDR 2,177 thousand.

4. GENERAL ADMINISTRATIVE EXPENSES

General administrative expenses in the income statement are analysed as follows:

Expressed in SDR (000)	2004	2003
Salaries and benefits	6,058	5,543
Staff retirement plan (note 19)	890	1,121
Other administrative expenses	2,458	2,355
General administrative expenses	**9,406**	**9,019**

The average number of staff employed during the year was 97 (2003: 97). The number of staff at 31 December 2004 was 97 (2003: 97)

5. PROVISIONS FOR LOSSES

Loans and equity investments are stated net of provisions. A summary of the movements in provisions for losses during the year were as follows:

Expressed in SDR (000)	Loans: Collective	Loans: Specific (note 7)	Equity Investments (note 8)	Guarantees	Total
At 1 January	7,674	1,118	291	292	9,375
Charges for the year	3,627	544	23	62	4,256
Foreign exchange adjustments	(378)	74	(17)	0	(321)
At 31 December 2004	**10,923**	**1,736**	**297**	**354**	**13,310**

At 31 December 2004 the Bank categorised one loan and two equity investments as impaired. The total exposure amounts to SDR 4,872 thousand and the provisions on these assets amounted to SDR 2,033 thousand. In addition, interest income of SDR 163 thousand on the impaired loan is suspended and not recognised in the income statement.

6. SHARE CAPITAL

In accordance with Article 4 of the Agreement, the initial authorised share capital of the Bank is one billion SDR divided into one million shares having a par value of one thousand SDR each. All participating members had fully subscribed to their portion of the initial authorised share capital in accordance with Article 5 of the Agreement.

Subsequently, at the Sixth Annual Meeting of the Board of Governors held on 6 June 2004, three Member States, Armenia, Georgia and Moldova requested a fifty per cent reduction of their portion of subscribed capital, from 2% to 1% of total authorised capital. The Board of Governors approved their request, recognising the importance of full commitment of the Member States by way of payment of obligations towards their respective shares. The total initial authorised capital stock of the Bank of SDR one billion remained unchanged.

The issued share capital at end of the year is analysed as follows:

Expressed in SDR (000)	2004	2003
Authorised share capital	1,000,000	1,000,000
Less: unallocated share capital *	(30,000)	0
Subscribed share capital	970,000	1,000,000
Less: shares not yet called	(679,000)	(700,000)
Less: shares called but not yet due	(24,250)	(50,000)
Called-up share capital	266,750	225,000
Advance against future call	29	57
Paid-in share capital	**266,779**	**250,057**

* Shares available to new or existing Member States.

In accordance with paragraph 2 under Article 6 of the Agreement, all Member States were required to pay their share of the first issue of shares of SDR 100 million within 60 days after the date on which they became members of the Bank. In accordance with paragraph 3 under the same Article, a second issue of shares of SDR 200 million was made in 1998 and payment for these shares shall be made by each Member State by promissory notes or other obligation issued by such member in eight equal successive annual instalments in the years 1998 to 2005.

At 31 December 2004 eight Member States had not yet fully settled the called up and due portion of their capital obligations. Three of the eight members had settled more than 99.9%. The balance of share capital due but not received at 31 December 2004 was SDR 3,902 thousand and at 31 December 2003 was SDR 10,926 thousand.

The capital subscription status and voting power, which is based on the paid amount, of each member at 31 December 2004 is analysed as follows:

Member	Shares	Subscribed	Callable	Payable	Paid	Voting Power
		Expressed in SDR (000)				
Albania	20,000	20,000	14,000	6,000	4,999	1.9%
Armenia	10,000	10,000	7,000	3,000	1,999	0.8%
Azerbaijan	20,000	20,000	14,000	6,000	4,422	1.7%
Bulgaria	135,000	135,000	94,500	40,500	37,125	14.1%
Georgia	10,000	10,000	7,000	3,000	2,000	0.8%
Greece	165,000	165,000	115,500	49,500	45,375	17.3%
Moldova	10,000	10,000	7,000	3,000	1,986	0.8%
Romania	135,000	135,000	94,500	40,500	37,125	14.1%
Russian Fed.	165,000	165,000	115,500	49,500	45,327	17.2%
Turkey	165,000	165,000	115,500	49,500	45,375	17.3%
Ukraine	135,000	135,000	94,500	40,500	37,115	14.0%
Total	**970,000**	**970,000**	**679,000**	**291,000**	**262,848**	**100.0%**

7. LOANS

The Bank offers a range of financial instruments for both project and trade financing, tailored to meet an individual operation's requirements. The Bank may also make equity-financing investments and provide guarantees. Loans may be denominated in any convertible currency, or a combination of convertible currencies in which the Bank is able to fund itself.

Expressed in SDR (000)	2004	2003
At 1 January	170,373	85,081
Disbursements	155,330	146,983
Less: repayments	(77,340)	(52,181)
Foreign exchange movements	(4,053)	(9,510)
At 31 December	244,310	170,373
Less: accumulated specific provision (note 5)	(1,736)	(1,118)
Net loans outstanding	**242,574**	**169,255**

Interest is generally based on 3 and 6 months Libor for USD loans and Euribor for EUR loans plus a margin. Margins are dependent on the risk category of each loan and typically range from 1.5% to 4.0%

The fair value of the loan portfolio is approximately equal to book value because the majority of loans bear a variable interest rate and are given at market conditions and terms. Further analysis of the loan portfolio is presented in note 9.

8. EQUITY INVESTMENTS

A primary focus of the Bank is to facilitate access to funding for those small and medium size enterprises with the potential for positive economic developmental impact. With this objective in mind, the Bank, together with a number of other institutions invested in the below entities.

As the Bank does not prepare consolidated financial statements such investments that fall under the definition of associated companies are carried at cost less provisions for impairment, following the option allowed by IAS 28.

Expressed in SDR (000)	2004	2003
At 1 January	2,625	2,499
Disbursements	425	379
Less: repayments	(381)	(13)
Foreign exchange movements	(112)	(240)
At 31 December	2,557	2,625
Less: accumulated specific provision (note 5)	(297)	(109)
Net book value	2,260	2,516

The valuation of such investments has been based on their latest audited accounts as of the 31 December 2003. The investees' details and their net equity as of 31 December 2004 are as follows:

Expressed in SDR (000)	Percentage of Investment	Total net equity
SEAF Trans-Balkan Fund LLC	18.33	5.955
Micro Finance Bank of Azerbaijan	35.00	2,950

Due to the time delay in obtaining audited financial statements from the above investee companies, the loss is based on income statements from the most recent 12-month period for which such information is available.

9. OPERATIONAL ANALYSIS

The analysis of operational activity of the Bank by geographical area, instrument and sector are as follows:

	2004		2003	
Expressed in SDR (000)	Outstanding disbursements	Undrawn commitments	Outstanding disbursements	Undrawn commitments
Analysis by country				
Armenia	391	0	0	0
Azerbaijan	3,240	2,072	3,667	1,885
Bulgaria	30,250	18,741	25,011	27,584
Georgia	5,696	3,035	5,319	4,103
Greece	52,840	6,701	18,957	23,436
Moldova	0	2,020	0	1,957
Romania	17,895	10,275	23,603	9,653
Russia	29,871	12,878	34,090	15,305
Turkey	69,807	1,288	43,800	14,132
Ukraine	35,447	21,700	17,103	857
Regional	1,430	907	1,448	1,232
At 31 December	**246,867**	**79,617**	**172,998**	**100,144**
Analysis by instrument				
Loans	244,310	72,492	170,373	91,899
Equity investments	2,557	907	2,625	1,232
Guarantees	-	6,218	-	7,013
At 31 December	**246,867**	**79,617**	**172,998**	**100,144**
Analysis by sector				
Financial institutions	41,136	18,670	38,682	9,524
Manufacturing	142,480	18,654	91,141	39,034
Infrastructure	63,251	42,293	43,175	51,586
At 31 December	**246,867**	**79,617**	**172,998**	**100,144**

10. NET PROPERTY, TECHNOLOGY AND EQUIPMENT

Property, technology and equipment in the accompanying balance sheet at end of year are analysed as follows:

Expressed in SDR (000)	Buildings (leasehold)	Furniture, office accesories and vehicle	Computers and office equipment	Intagibles	Total
Cost					
At 1 January	129	375	914	1,023	2,441
Additions	0	1	87	37	125
Disposals	0	0	(10)	0	(10)
At 31 December 2004	**129**	**376**	**991**	**1,060**	**2,556**
Accumulated despreciation					
At 1 January	104	285	615	500	1,504
Charges for the year	18	52	143	206	419
Disposals	0	0	(10)	0	(10)
At 31 December 2004	**122**	**337**	**748**	**706**	**1,913**
Net book value					
At 31 December 2004	**7**	**39**	**243**	**354**	**643**
At 31 December 2003	25	90	299	523	937

Intagibles comprises of computer software.

11. OTHER ASSETS

Other assets in the accompanying balance sheet at end of year are analysed as follows:

Expressed in SDR (000)	2004	2003
Advances and prepaid expenses	259	125
Guarantee deposits	54	49
Fair value of forward foreign exchange contracts	863	2,111
Other assets	**1,176**	**2,285**

12. BORROWINGS

Borrowing facilities arranged at end of year were SDR 52,452 of which an amount of SDR 45,798 was not utilised, as analysed below. In addition to medium or long-term borrowings, the Bank utilises short-term financing in the form of borrowings from major commercial banks for cash management purposes.

	2004		2003	
Expressed in SDR (000)	Amount utilised	Borrowings arranged	Amount utilised	Borrowings arranged
Euro	0	13,172	0	0
United States dollar	6,439	39,065	0	0
Other	215	215	0	0
At 31 December	**6,654**	**52,452**	**0**	**0**

13. PAYABLES AND ACCRUED INTEREST

Payables and accrued interest in the accompanying balance sheet at end of year are analysed as follows:

Expressed in SDR (000)	2004	2003
Interest payable	68	49
Social insurance fund (IKA) contributions	8	9
Pension plan obligation (note 19)	24	322
Suppliers and other accrued expenses	253	279
Payables and accrued interest	**353**	**659**

14. GENERAL RESERVE

In accordance with Article 36 of the Agreement, the Board of Governors shall determine annually what part of net income or surplus of the Bank from operations shall be allocated to reserves, provided that no part of the net income or surplus of the Bank shall be distributed to members by way of profit until the general reserves of the Bank shall have attained the level of ten (10%) per cent of the subscribed capital including all paid, unpaid but payable, and unpaid but callable share capital.

15. CASH AND CASH EQUIVALENTS

Cash and cash equivalents include cash on hand, placements with other financial institutions and debt securities with maturities of three months or less. End of year are analysis is as follows:

Expressed in SDR (000)	2004	2003
Cash	1	3
Placements and/or investment securities:		
Up to 1 month	39,621	55,408
From 1 month to 3 months	6,285	29,192
Total deposits and securities	**45,907**	**84,603**

The commercial paper held in the Bank's portfolio is rated A2/P2 and above, in accordance with internal financial policies.

16. CURRENCY RISK

The Bank's policy is to have no significant foreign exchange position, but to invest its SDR denominated capital and reserves in the SDR constituent currencies in proportion to their weight in determining the value of SDR.

The table below provides a currency breakdown of the Bank's assets and liabilities.

Expressed in SDR (000)	United States dollar	Euro	Japanese yen	Pound Sterling	Special Drawing Right	Total
Assets						
Cash and bank balances	24	133	2,506	27		**2,690**
Placements with financial institutions	2,221	7,245		15,080		**24,546**
Investment securities			6,285	12,386		**18,671**
Loans	160,446	83,864				**244,310**
Equity investments	2,557					**2,557**
Provisions for losses	(9,672)	(3,638)				**(13,310)**
Receivables and accrued interest	1,036	572	55	173		**1,836**
Paid-in share capital not received					3,902	**3,902**
Net property, technology and equipment					643	**643**
Other assets					1,176	**1,176**
Total assets	156,612	88,176	8,846	27,666	5,721	**287,021**
Liabilities						
Borrowings	6,654					**6,654**
Payables and accrued interest	23	283	39	8		**353**
Deferred income					2,387	**2,387**
Members' equity					277,627	**277,627**
Total liabilities and members' equity	6,677	283	39	8	280,014	**287,021**
Net assets (liabilities)	149,935	87,893	8,807	27,658	(274,293)	**0**
Derivative financial instruments	(48,102)	14,896	27,655	6,414	(863)	**0**
Net currency balance at 31 December 2004	**101,833**	**102,789**	**36,462**	**34,072**	**(275,156)**	**0**
Correct SDR weights *	102,231	102,935	36,317	33,673	275,156	
Currency position at 31 December 2004	(398)	(146)	145	399	0	
Net currency balance at 31 December 2003	**97,479**	**90,399**	**33,468**	**29,898**	**(251,244)**	**0**

* As per IMF rule (effective as of 1 January 2001)

17. LIQUIDITY RISK

Liquidity is a measure of the extent to which the Bank may be required to raise funds to meet its obligations. The Bank's commitment to maintaining a strong liquidity position is established in policies, approved by the Board of Directors, that require a minimum target liquidity ratio of 50% of the net cash requirements for the next 12 months. Liquid assets are maintained in short-term placements and negotiable securities.

The table below provides an analysis of assets, liabilities and members' equity by relevant maturity groupings based on the remaining period from the balance sheet date to the contractual maturity date. It is presented under the most prudent consideration of maturity dates where options or repayment patterns allow for early repayment possibilities. Therefore, in the case of liabilities the earliest possible repayment date is shown, while for assets it is the latest possible repayment date. Those assets and liabilities that do not have a contractual maturity date are grouped together in the "maturity undefined" category.

Expressed in SDR (000)	Up to 1 month	From 1 month to 3 months	From 3 months to 1 year	From 1 year to 5 years	Over 5 years	Maturity undefined	Total
Assets							
Cash and bank balances	2,690						**2,690**
Placements with financial institutions	24,546						**24,546**
Investment securities	12,386	6,285					**18,671**
Loans	301	21,270	49,018	158,367	15,354		**244,310**
Equity investments						2,557	**2,557**
Provisions for losses						(13,310)	**(13,310)**
Receivables and accrued interest		1,836					**1,836**
Paid-in share capital not received	3,902						**3,902**
Net property, technology and equipment						643	**643**
Other assets	259					863	**1,176**
Total assets	44,084	29,391	49,018	158,421	15,354	(9,247)	**287,021**
Liabilities							
Borrowings				6,439		215	**6,654**
Payables and accrued interest		353					**353**
Deferred income	2,387						**2,387**
Members' equity						277,627	**277,627**
Total liabilities and members' equity	2,387	353	0	6,439	0	277,842	**287,021**
Liquidity position at 31 December 2004	**41,697**	**29,038**	**49,018**	**151,982**	**15,354**	**(287,089)**	**0**
Liquidity position at 31 December 2003	**65,220**	**48,844**	**22,589**	**117,681**	**9,354**	**(263,688)**	**0**

* The fair value of investment securities maturing up to one year approximates the book value.

18. INTEREST RATE RISK

Interest rate risk is the risk that the value of a financial instrument will fluctuate due to changes in market interest rates. The length of time for which the rate of interest is determined on a financial instrument indicates to what extent it is exposed to interest rate risk. The Asset and Liability Unit monitors the interest rate exposure of the Bank.

The table below provides information on the extent of the Bank's interest rate exposure based either on the contractual maturity date of the financial instruments or, in the case of instruments that re-price to a market rate of interest before maturity, the next re-pricing date.

Expressed in SDR (000)	Up to 1 month	From 1 month to 3 months	From 3 months to 1 year	From 1 year to 5 years	Over 5 years	Non-interest bearing	Total
Assets							
Cash and bank balances	2,689					1	**2,690**
Placements with financial institutions	24,546						**24,546**
Investment securities	12,386	6,285					**18,671**
Loans	29,013	108,798	104,778	1,721			**244,310**
Equity investments						2,557	**2,557**
Provisions for losses						(13,310)	**(13,310)**
Receivables and accrued interest						1,836	**1,836**
Paid-in share capital not received						3,902	**3,902**
Net property, technology and equipment						643	**643**
Other assets						1,176	**1,176**
Total assets	68,634	115,083	104,778	1,721	0	(3,195)	287,021
Liabilities							
Borrowings		6,439				215	**6,654**
Payables and accrued interest						353	**353**
Deferred income						2,387	**2,387**
Members' equity						277,627	277,627
Total liabilities and members' equity	0	6,439	0	0	0	280,582	287,021
Interest rate risk at 31 December 2004	**68,634**	**108,644**	**104,778**	**1,721**	**0**	**(283,777)**	**0**
Interest rate risk at 31 December 2003	**59,412**	**148,453**	**47,103**	**0**	**0**	**(254,968)**	**0**

19. STAFF RETIREMENT PLAN

The defined benefit scheme covers all eligible employees of the Bank. At normal retirement age (60 years), a staff member is entitled to a pension equal to 1% of his pensionable salary (ie: average of the last five years of service) multiplied by his/her years of service at the Bank. Also, upon retirement, a staff member will be entitled to receive in cash the full balance standing to the credit of his/her individual account for the second and third pillars.

An actuarial valuation of the defined benefit scheme is performed each year by a qualified actuary taking into consideration the Bank's human resources strategy and policies.

Expressed in SDR (000)	2004	2003
Amounts recognised in the balance sheet		
At 1 January	331	2,726
Current service costs	866	799
Employee contributions	399	431
Past service obligation	24	322
Contributions paid	(1,588)	(3,947)
At 31 December	**32**	**331**
Amounts recognised in the income statement		
Current service costs:		
Define benefits scheme	509	470
Define contributions scheme	309	293
Greek social insurance fund	48	36
Past service obligation	24	322
Total included in general administrative expenses	**890**	**1,121**
Principal actuarial assumptions used		
Discount rate	5.4%	5.0%
Expected return on plan assets	6.0%	6.0%
Future salary increases	3.0%	3.0%
Average remaining working life of employees	21 years	22 years

20. OPERATING LEASES

The Bank has entered into lease contracts for its Headquarters premises. These are operating leases and include renewal options and periodic escalation clauses. There is no commitment at end of year for non-cancellable lease contracts. Rental expenses for the year included in "General administrative expenses" totalled SDR 568 thousand (SDR 521 thousand in 2003).

21. SPECIAL FUNDS ADMINISTERED BY THE BANK

Special funds may be established in accordance with Article 16 of the Agreement and are administered under the terms of rules and regulations adopted by the Bank. At 31 December 2004 the Bank administered one such fund the Technical Cooperation Special Fund. The assets and fund balance are not included in the Bank's balance sheet.

The objective of the fund, which has been funded by the Hellenic Republic, is to contribute to the economic development of the Black Sea Region's Member Countries. The fund extends technical assistance grants for preparation of high quality project documentation including business plans, feasibility studies and financial reporting methods and standards. The movement in the fund for the years 2004 and 2003 is shown below.

Expressed in SDR (000)	2004	2003
Fund statment of movement		
Balance of fund brought forward	802	487
Contribution received	0	424
Interest and other income	16	18
Less: disbursements	(120)	(117)
Less: other operating expenses	(2)	(2)
Foreign exchange movements	27	(8)
Balance of fund available	**723**	**802**
Fund balance sheet		
Assets		
Placements with other financial institutions	723	802
Total Assets	**723**	**802**
Liabilities		
Allocated fund balance	0	0
Unallocated fund balance	723	802
Total Liabilities and contributors resources	**723**	**802**

To the Board of Directors of the
Black Sea Trade and Development Bank

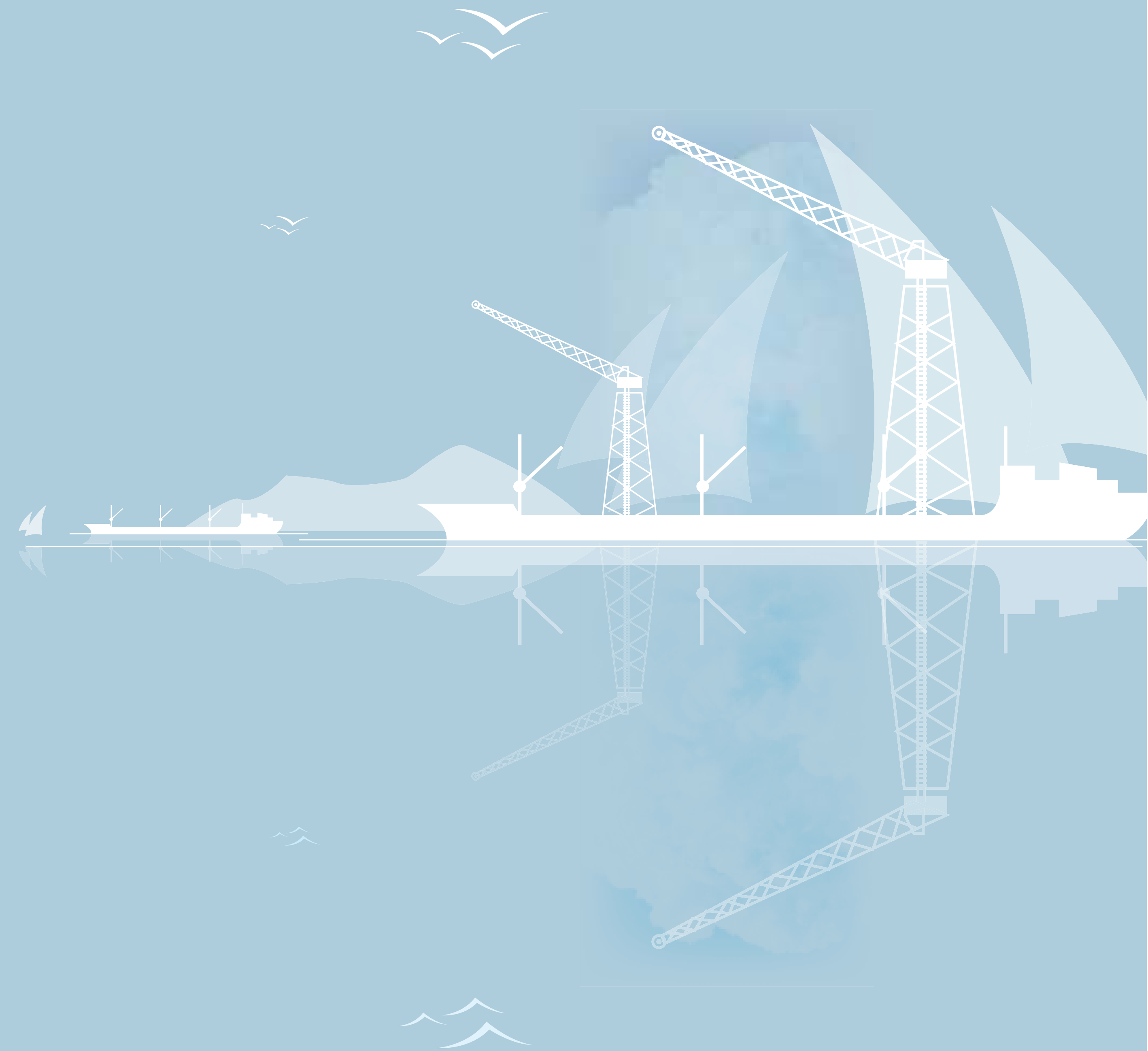
We have audited the accompanying balance sheet of the Black Sea Trade and Development Bank (hereinafter called the Bank) for the year ended 31 December 2004 and the related income statement and statements of changes in members' equity and cash flows for the year then ended. These financial statements are the responsibility of the Bank's management. Our responsibility is to express an opinion on these financial statements based on our audit.

We conducted our audit in accordance with International Standards on Auditing. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audit provides a reasonable basis for our opinion.

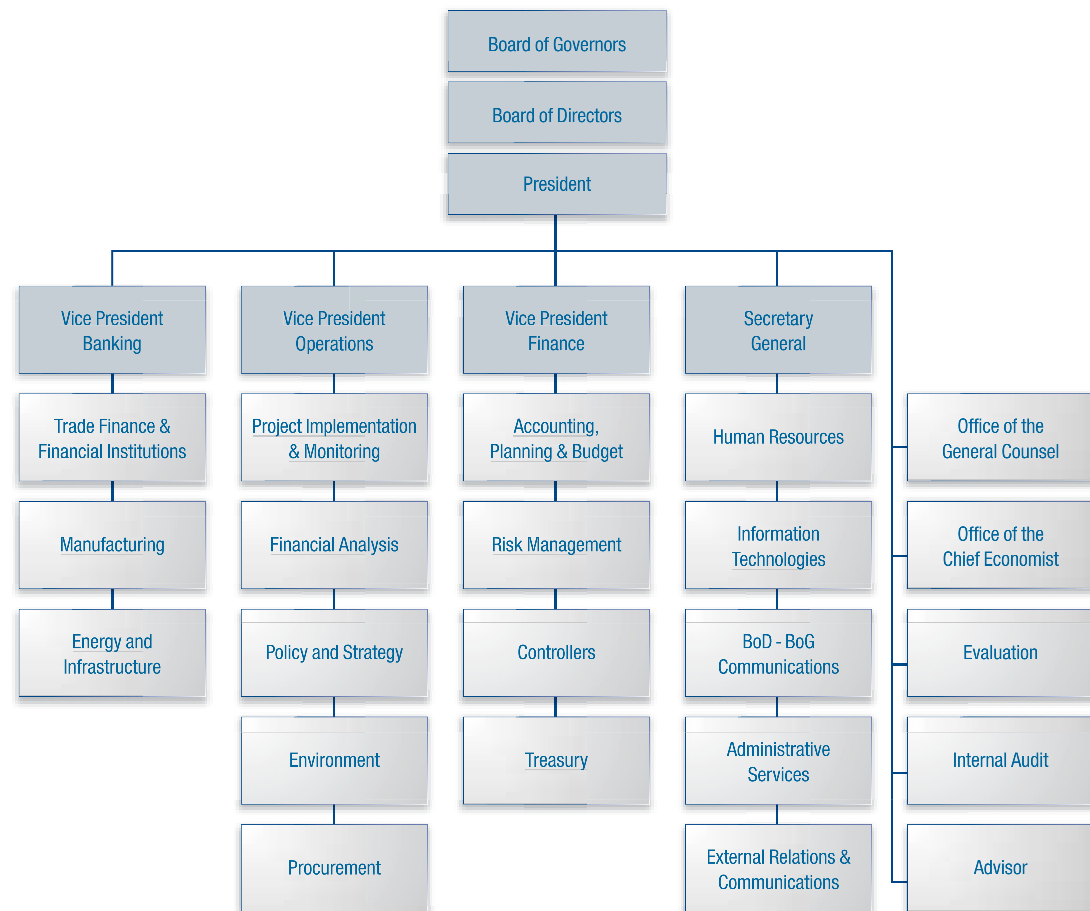
In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of the Bank as of 31 December 2004 and the results of its operations and cash flows for the year then ended, in accordance with International Financial Reporting Standards.

Ernst and Young,

Athens, Greece,
15 March 2005



Annex 1 | Organisational Structure



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