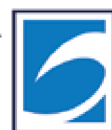
Black Sea Region:
The Quest for Economic Growth and Financial Stability

Annual Report 2011



Black Sea Trade & Development Bank

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Contact BSTDB

Board of Governors

As of 31 December 2011

Republic of Albania

Governor: Mr. Nezir HALDEDA, Deputy Minister of Finance
Alternate Governor: position vacant

Republic of Armenia

Governor: Mr. Arthur JAVADYAN, Chairman, Central Bank of Armenia
Alternate Governor: Mr. Vahe VARDANYAN, Director, Financial Sector Policy & Analysis Department, Central Bank of Armenia

Republic of Azerbaijan

Governor: Mr. Samir SHARIFOV, Minister of Finance
Alternate Governor: Mr. Shahin MUSTAFAYEV, Minister of Economic Development

Republic of Bulgaria

Governor: Ms. Boryana PENCHEVA, Deputy Minister of Finance
Alternate Governor: Mr. Stefan SOTIROV, Head, European Financial Institutions Division, External Finance and International Cooperation Directorate, Ministry of Finance

Georgia

Governor: Mr. George KADAGIDZE, President, National Bank of Georgia
Alternate Governor: Mr. Dimitri GVINDADZE, Minister of Finance

Hellenic Republic

Governor: Mr. Ioannis DRYMOUSSIS, Secretary General Ministry of Economy, Competitiveness & Shipping
Alternate Governor: Prof. Panagiotis KORLIRAS, Chairman, Board of Directors & Scientific Director, Centre of Planning & Economic Research (CPER)

Republic of Moldova

Governor: Mr. Veaceslav NEGRUTA, Minister of Finance
Alternate Governor: position vacant

Romania

Governor: Mr. Gheorghe IALOMITIANU, Minister of Public Finance
Alternate Governor: Mr. Bogdan Alexandru DRAGOI, Secretary of State, Ministry of Public Finance

Russian Federation

Governor: Mr. Sergey STORCHAK, Deputy Minister of Finance
Alternate Governor: Mr. Sergey BELYAKOV, Director, Investment Policy & Public-Private Partnership Development Department, Ministry of Economic Development

Republic of Turkey

Governor: Mr. Ibrahim H. CANAKCI, Undersecretary of Treasury Undersecretariat of Treasury
Alternate Governor: Mr. Cavit DAGDAS, Deputy Undersecretary of Treasury Undersecretariat of Treasury

Ukraine

Governor: Mr. Vadym KOPYLOV, First Deputy Minister of Economic Development & Trade
Alternate Governor: position vacant

Board of Directors

As of 31 December 2011

Republic of Albania

Director: Mr. Xhentil DEMIRAJ, General Director, General Debt Management Directorate, Ministry of Finance

Alternate Director: Mr. Resmi HIBRAJ, Director of Borrowing, General Debt Management Directorate, Ministry of Finance

Republic of Armenia

Director: Mr. Vardan ARAMYAN, Deputy Minister of Finance

Alternate Director: Mr. Nerses MKRTCHIAN, Director, Multilateral & Bilateral Economic Cooperation Department, Ministry of Foreign Affairs

Republic of Azerbaijan

Director: Mr. Mikayil JABBAROV, Director, Administration of State Historical Architectural Reserve “Icherisheher”, Cabinet of Ministers of the Republic of Azerbaijan

Alternate Director: Mr. Famil ISMAYILOV, Deputy Head, International Relations Department, Ministry of Finance

Republic of Bulgaria

Director: Ms. Milena BOIKOVA, Director, Government Debt & Financial Markets Directorate, Ministry of Finance

Alternate Director: Mr. Nikola SHERLETOV, Parliamentary Secretary, Ministry of Finance

Georgia

Director: Mr. Konstantine KINTSURASHVILI, Deputy Minister of Finance

Alternate Director: Mr. Giorgi BARBAKADZE, Head, Macroeconomics & Statistics Department, National Bank of Georgia

Hellenic Republic

Director: Mr. Petros KONTOS, Director, International Economic Organizations Directorate, Ministry of Economy, Competitiveness & Shipping

Alternate Director: Ms. Zoe DRIVA EVANGELOPOULOU, Director for Quality & Efficiency, Ministry of Economy, Competitiveness & Shipping

Republic of Moldova

Director: Ms. Elena MATVEEVA, Director, Public Debt Department, Ministry of Finance

Alternate Director: Ms. Ina GOREA, Deputy Chief, On-Lending Directorate, Public Debt Department, Ministry of Finance

Romania

Director: Ms. Diana PELIGRAD BLINDU, Head Operations I, General Directorate for Treasury & Public Debt, Ministry of Public Finance

Alternate Director: Mr. Stefan PETRESCU, Head of Operation Division, External Public Finance, Ministry of Public Finance

Russian Federation

Director: Mr. Alexander GORBAN, Director, Economic Cooperation Department, Ministry of Foreign Affairs

Alternate Director: position vacant

Republic of Turkey

Director: Mr. Evren DILEKLI, Acting Director General, General Directorate for Foreign Economic Relations, Undersecretariat of Treasury

Alternate Director: position vacant

Ukraine

Director: Mr. Valeriy PYATNYTSKIY, Deputy Minister of Economy

Alternate Director: Mr. Serhiy RYBAK, Deputy Minister of Finance

Audit Committee

As of 31 December 2011

Ms. Milena Boikova, Director for the Republic of Bulgaria and AC Chairperson
Mr. Mikail Jabbarov, Director for the Republic of Azerbaijan, AC member
Mr. Konstantine Kintsurashvili, Director for Georgia, AC member
Ms. Elena Matveeva, Director for the Republic of Moldova, AC member

Management

As of 31 December 2011

Vitalii Mygashko	**Valentina Siclovan**	**Andrey Kondakov**	**Orsalia Kalantzopoulos**	**Mustafa Boran**
Vice President Operations	Vice President Finance	President Chairman of the Board of Directors	Secretary General	Vice President Banking

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 for 2011 as endorsed by the Board of Directors. The Thirteenth Annual Report also contains the Bank's financial statements; separate financial statements for the operations of the Bank's Special Funds have also been issued, as prescribed in Section 12 of the Bank's By-Laws.

Andrey Kondakov

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

Statement by the President

Despite a challenging and unpredictable global background, the Black Sea region posted healthy economic growth that in real terms reached approximately 4.1% of GDP in 2011. Recovery continued and many of the countries exceeded pre-crisis levels of economic activity. Post-crisis growth rates were generally lower. However, they still more than doubled the average growth rates in the Eurozone, being in a range which is likely to prove more sustainable than the impressive rates achieved in the previous decades. Unfortunately, those rates ultimately led to overheating and greater vulnerability when the global financial crisis broke out in late 2008.

At the macroeconomic level, there were many positive developments beyond the overall growth rate. A few of the more notable developments included, high export growth, a modest but noteworthy rise in investment, including foreign direct investment, progress in fiscal consolidation, and abating price pressures. Similarly, at the 'micro' level there were many significant improvements in the business environment in which firms operate. This was underscored by the fact that no fewer than five Black Sea states figured in the top 30 'most improved' reported in the World Bank's annual Doing Business Report, with two in the top 10: Armenia, which was second overall globally, and Moldova, which placed ninth.

On the ground, the Black Sea Trade and Development Bank observed these improvements first hand, as strong client demand resulted in a record year for new operational activity. For 2011, the first year of implementation of the Bank's Medium Term Strategy and Business Plan (MTSBP) for the 2011–14 period, approvals of new operations by the Bank's Board of Directors reached EUR 359.3 million, an increase of 67.7% over the previous year, and signing of new operations grew 50.5% over 2010, to EUR 298.2 million. Both these figures represent single year record achievements, and are close to the high case scenario of the MTSBP. They highlight the Bank's attractiveness as a development partner for banks, firms and investors active in the Black Sea region.

Many of these operations were finalized either in the latter part of the year or have longer development and implementation periods, and are due to disburse over the next 12 to 18 months. Therefore in 2011, disbursements (including rollovers and renewals) declined slightly to EUR 204.3 million. By way of contrast, the active portfolio of operations grew by 7.0% compared to 2010, and by the end of 2011 it stood at EUR 720.4 million.

There was an increase in the level of problem projects to 6.8%, as well as charges against some bond purchases that declined in value, which were fully covered by provisions. That allowed BSTDB to maintain the quality of its portfolio. Overall, the Bank registered positive net income for the seventh consecutive year. Income before provisions increased by 7.4% relative to 2010 to EUR 20.2 million, while net income declined slightly by 2.4% to EUR 10.1 million.

There were other important developments in 2011 as well. As a follow up to the MTSBP for the period 2011–14, which was approved by the Board of Governors in December 2010, the Bank successfully elaborated, prepared and approved Country Strategies for all eleven Member Countries in the first half of 2011. These Country Strategies took the key strategic objectives and operational goals laid out in the MTSBP and individualized them for each Member, breaking down operational directions and targets in each Country within the overall operating context.

Perhaps the most significant development during 2011 was that the Bank attained a long term issuer credit rating of A and a short term issuer credit rating of A-1 from Standard & Poor's Ratings Services in June. Together with the long term issuer credit rating of A3, to which BSTDB was upgraded by Moody's in September 2010, the Bank's ratings are higher than the individual sovereign rating of any of the Bank's shareholders and approximately six notches higher than the average credit rating for the Black Sea region. These ratings make the Bank the best rated institution in the Black Sea area.

The Bank further extended its links with development partners active and interested in the Black Sea region. BSTDB welcomed two new observers with extensive presence and experience in the region during 2011, the European Bank for Reconstruction and Development and Vnesheconombank, the development bank of Russia. In addition, it became a founding member of the International Development Finance Club (IDFC), a global group of leading national and sub-regional development banks that established a network in order to collaborate on agenda setting and issues of similar interest, to identify joint business opportunities, and to share know-how and best practice experiences. IDFC successfully launched the Smart Partnership Proposal for the UN Green Climate Fund at the United Nations' Climate Financing Conference in Durban, South Africa in December 2011, and aims to generate synergies on additional issues of mutual interest in the future.

As 2011 established a good foundation for implementation of the BSTDB's business and operational strategies in the coming years, the Bank expects to continue its track record into 2012, the second year of the Bank's MTSBP. It will pursue an approach which combines cautious expansion with conservative policies and cost consciousness. The Bank will also make concerted efforts to diversify its sources of funding along with the capital contributions from Member States. This would allow the BSTDB to increase its outreach and seek new opportunities to support the Black Sea region and generate value for the shareholders.

Andrey Kondakov

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

Highlights of 2011

- 2011 was the second best year in the BSTDB history, in terms of its operational and financial results.

The Board of Directors approved 30 new operations of a total amount of EUR 359.3 million – a 67.7% increase over 2010; The Bank signed 29 operations totaling EUR 298.2 million, representing a 50.5% increase over 2010; Disbursements reached EUR 204.3 million, with the total outstanding portfolio reaching EUR 720.4 million.

The Bank's portfolio remained sound, with problem loans accounting for 6.8% of the outstanding. Provisions, reserves, and retained earnings stood at 289.1% of problem loans.

The Bank scrutinized its administrative expenses to achieve greater efficiency, which resulted in a 3% reduction of the ratio of administrative expense to operating income.

By year-end, operating income reached EUR 35.9 million, representing a 7.9% growth from its 2010 level. The Bank's income before provisions in 2011 amounted to EUR 20.2 million, a 7.4% increase over 2010. This is the highest income before provisions achieved since the Bank started operations in 1999.

- The Bank advanced towards meeting the goals and objectives established under the BSTDB Medium-Term Strategy and Business Plan for 2011–2014. In particular, the Bank has already achieved the 20% target lending to small shareholders, which reached 23% of the operational portfolio. Lending to SME sector amounted to 76.5% of intermediated operations, compared to a 55–65% target. The Bank is close to meeting its 5% target for equity investment, with exposure to equities at 4.3% of the portfolio by the end of 2011.

- Between February and April 2011, the Bank completed consultations with Governments of the member states in order to finalize individual country strategies aligned to the corporate operational directions and targets set forth in the BSTDB Medium Term Strategy and Business Plan for 2011–2014. The 11 new country strategies have been approved by the Board of Directors and have become operational.

- In June 2011, the Bank obtained an "A" long term credit risk rating from Standard and Poor's, which is one notch higher than the "A3" rating the Bank has from Moody's. Currently, BSTDB is the best-rated institution in the Black Sea region and one of the top-rated in Central and Eastern Europe.

- The Bank granted its Observer Status to EBRD in June, and to Vnesheconombank of Russia, which became the first national development bank from a member country to obtain Observer Status in September 2011. Observer Status strengthens synergies and developmental effectiveness of BSTDB operations, as well as enhancing its funding opportunities.

- BSTDB became a founding member of the International Development Finance Club (IDFC), a global group of leading national and sub-regional development banks that established a network in order to collaborate on agenda setting and issues of similar interest, to identify joint business opportunities, and to share know-how and best practice experiences.

- BSTDB continued to expand its cooperation with other partners in development to attract additional resources for projects in the member countries. In 2011, the Bank signed three loan agreements with its Observer institutions – KfW, Nordic Investment Bank and Proparco (France) in the total amount of EUR 100 million aimed at investing in the BSTDB member countries to support projects in renewable energy and energy efficiency, social infrastructure, agribusiness and small business development.

Economic Developments in the Black Sea Region during 2011[1]

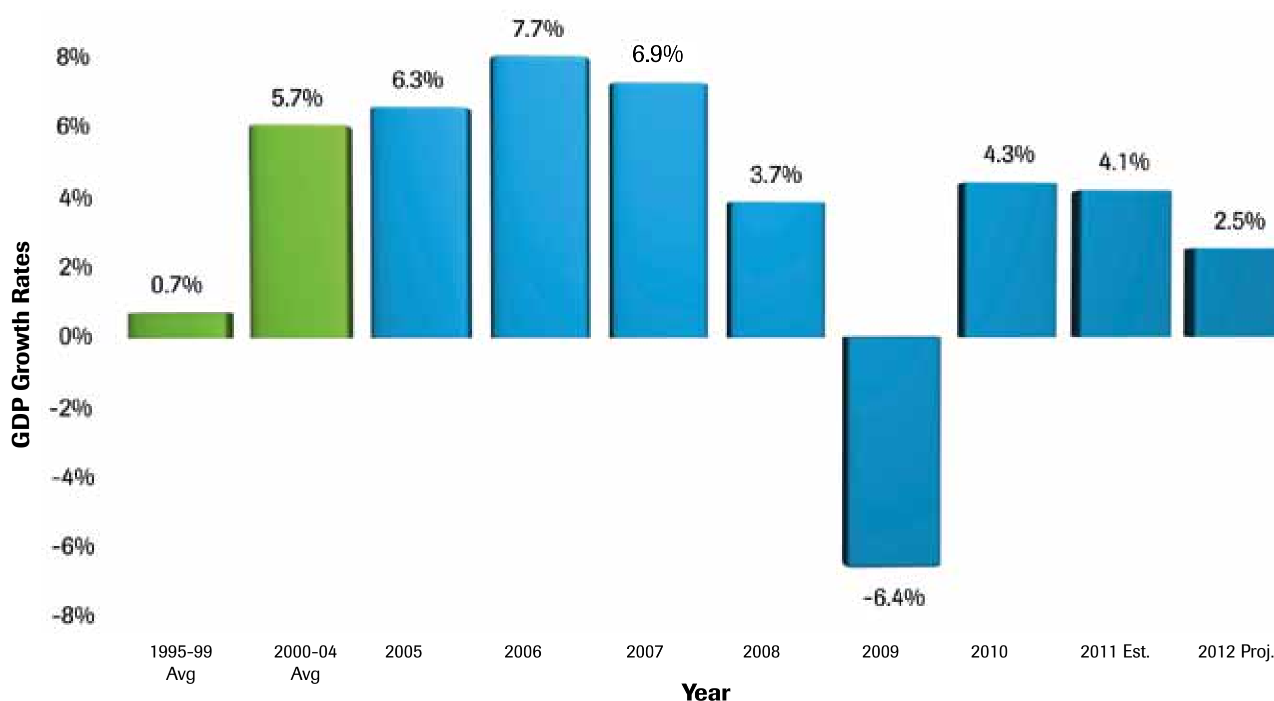
Economic Overview of 2011 in the Black Sea Region

As Figure 1 shows, the average real GDP growth rate for the Black Sea region in 2011 reached an estimated 4.1%. This is similar to, albeit slightly below, the real GDP growth rate of 4.3% achieved in 2010, and indicates that as a whole the region has reached and surpassed the levels of economic output until mid-2008, just prior to the sharp economic downturn that resulted in the aftermath of the global financial crisis of September 2008.

The first part of 2011 was a continuation of the strengthening growth recorded in the latter part of 2010, with both domestic and external demand increasing at the fastest pace since the 2008–09 downturn. However, global growth prospects were affected negatively by a series of shocks including the Japanese earthquake and tsunami, which disrupted global supply chains, the Arab Spring which fueled upward volatility in energy prices, and most importantly, the continuing turmoil of the Eurozone crisis. These exogenous shocks took their toll on the Black Sea region, and as a result, growth in the second part of 2011 slowed, with the weakening of key indicators of manufacturing and industrial production.

For the Black Sea region, the Eurozone crisis is by far the most significant in terms of impact on economic activity and prospects. The European Union (EU) is the most significant trade partner of most of the greater Black Sea states, and is the main source of financing and investment that takes place in the Black Sea region. Thus, the Eurozone's difficulties create problems not only

Figure 1: Black Sea Region Average Annual Real GDP Growth



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 2012* of the World Bank (plus GEPs 2010 & 2011), the IMF's W*orld Economic Outlook* publications (and their updates) and the Economist Intelligence Unit. As many figures represent estimates for 2011, actual final figures may differ in detail, but the overall trends discussed in this section will not be altered.

for Eurozone and EU members, but also for other Black Sea states more remote from the EU with lesser forms of association and fewer institutional links. The most direct impact was the slowdown of economic growth in the EU, which resulted in a reduction of export growth for many Black Sea states, particularly in the second half of the year as the Eurozone crisis worsened. A second way is via contagion from the turmoil in financial markets. As spreads in the Eurozone rose in the latter half of 2011, the general rise in risk aversion impacted the Black Sea region. This resulted in: higher spreads for a number of states, investment plans held up, consumption precluded by rising uncertainty, as well as more difficult, and unsure, access to financing for corporates.

Rising uncertainties and worsening growth prospects in the EU also resulted in reduced investment interest on the part of EU firms, leading to weaker than anticipated foreign direct investment (FDI). In the financial sector, the reduction in cross-border financial flows was particularly marked, as private capital flows from EU based firms to states from the Black Sea region slowed sharply and even reversed in the second half of the year. The situation was further exacerbated by proposed regulatory changes in the financial sector in the EU, and the adoption of austerity policies by many EU states. (See *In Focus: Banking Sector in the Black Sea region* – pages 19–24).

From a structural perspective, private domestic consumption was the main 'engine' driving growth. Already, the single largest structural component in the region's economies, private consumption grew at a pace faster than that of a country's economic growth. External demand was also strong and contributed to regional GDP growth. Regional exports grew impressively 25% in 2011 over 2010 levels and reached record levels but they represent a much smaller component of regional economies so they had less overall impact upon growth (see section on External Trade). Notwithstanding exceptions in countries with high revenue growth, government consumption growth was generally lower as most countries continued an ongoing process of fiscal consolidation that they began in response to the fiscal deterioration caused by the economic downturn in 2009. Investment growth, both public and private, was more mixed but in countries experiencing positive growth its rate of increase was generally above the overall growth rate.

Turning to the supply side and looking at economic sectors of origin, an interesting feature in 2011 was that the agricultural sector generally grew most robustly, with production in the industrial sector also growing at rates above those in the economy as a whole. With the exception of the highest growth countries in the region, services – including construction- grew more sluggishly as a rule. However, since agriculture is the smallest sector of the economy in most countries, generally contributing around 5–10% of GDP, its stronger growth had less of an impact on overall economic growth. The industrial sector typically contributes around 20–40% of GDP to the economies of the region, while services are the single biggest sector, contributing anywhere from 50–70% of GDP. In past years, services and construction had posted the greatest rate of expansion and thus reached their predominant position in the economy. Financial sector uncertainties contributed to this sluggishness, and impacted other sectors such as construction activity, where lower and more uncertain availability of financing resulted in reduced growth.

Table 1 on page 11 shows a detailed summary of key macroeconomic indicators for 2011, broken down by country. It shows that outturns from country to country were varied, although only one experienced negative growth. Greece, caught up in the ongoing Eurozone crisis, experienced a serious economic contraction. Other countries in the Western part of the Black Sea region achieved modest, positive growth, with the other Balkan countries clustered in the 1.5–2.5% real GDP growth range. Growth rates were generally higher in the Eastern part of the Black Sea region. Armenia and Russia achieved growth above 4%; Georgia, Moldova and Ukraine posted growth in excess of 5%, while Turkey realized the highest growth in the region above 8%. Azerbaijan represented an exception of sorts, achieving virtually zero growth after several years of impressive expansion. However, even this hides the fact that this slowdown was due to declines in oil and gas production, which over the past decade have been the principal drivers of the country's rapid economic growth. And this slowdown in turn was fully offset by growth in the non-energy sectors of the economy, which posted real growth of about 9%.

Table 1: Summary of Key Economic Indicators for 2011, by BSEC Member Country

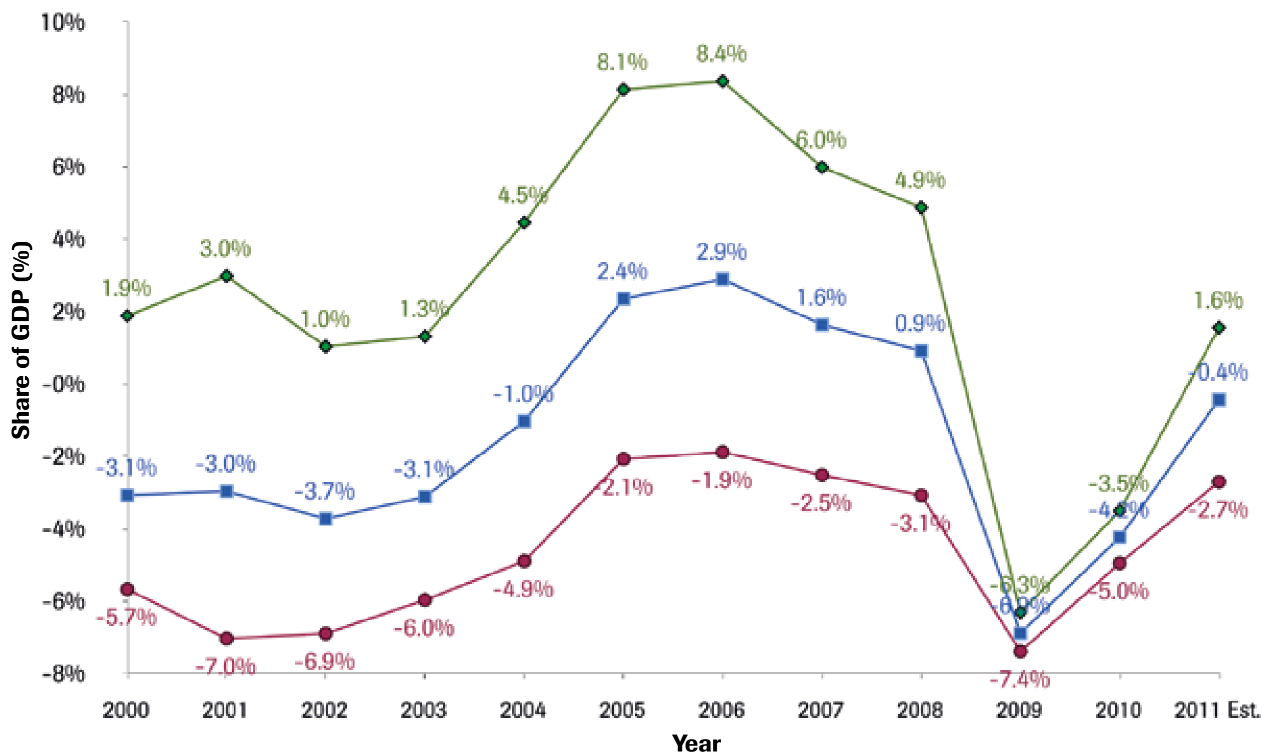
	GDP Growth	Inflation	Current Acct Bal / GDP	Budget / GDP	Public Debt / GDP	FDI / GDP	Industrial Output Growth
Albania	1.6%	3.5%	-12.2%	-3.4%	59.4%	7.0%	1.6%
Armenia	4.6%	7.7%	-10.9%	-2.9%	49.0%	6.5%	4.6%
Azerbaijan	0.1%	7.9%	27%	0.6%	11.7%	1.4%	5.0%
Bulgaria	1.7%	4.2%	0.9%	-2.1%	16.3%	3.1%	6.6%
Georgia	7.0%	8.5%	-12.5%	-3.2%	43.6%	6.8%	7.0%
Greece	-6.9%	3.3%	-9.8%	-9.1%	162.5%	0.6%	-6.9%
Moldova	5.8%	7.6%	-8.4%	-2.4%	23.7%	3.7%	7.4%
Romania	2.5%	5.8%	-4.5%	-4.1%	34.5%	1.4%	2.5%
Russia	4.3%	8.4%	5.3%	1.6%	8.2%	2.8%	4.3%
Serbia	1.6%	11.0%	-9.7%	-5.1%	44.1%	6.4%	1.6%
Turkey	8.5%	6.5%	-10.0%	-1.3%	42.4%	2.1%	8.5%
Ukraine	5.2%	8.0%	-5.5%	-1.4%	38.0%	4.4%	5.2%

Inflation in the Black Sea region was generally benign and stable. All but one country posted single digit inflation figures for the year. The trend in inflation was similar to that of economic growth - higher in the first part of the year but more subdued in the latter part. The diminishing growth prospects in the second half of the year influenced inflation, and expectations of inflation in a downward direction. The decline in inflation was further supported by weaker global commodity prices as well as the strong growth in agricultural output, which resulted in lower food prices in many countries.

Black Sea countries exhibited broad variation on their current accounts in 2011. The energy exporting countries, Azerbaijan and Russia, continued to post high structural surpluses. Bulgaria, recorded its first surplus in over a decade due to its strong record of export growth, and the tight fiscal and monetary policies that constrain domestic demand. The remaining countries posted deficits on their current account, roughly split between those showing improvement relative to 2010, and those showing some deterioration. More importantly, most of the deficits are fairly high, with five countries experiencing double digit deficits (as a share of GDP) and two just below ten percent. In the uncertain current global environment, this raises concerns about ability to access external financing and sustainability, and begs the question whether the deficit results from structural inefficiencies and low competitiveness, or if it is the result of transient factors such as the fact that in Ukraine, spending in preparation for the 2012 European football championship led to a surge in imports, while pre-electoral government spending contributed to increases in Serbia.

Growth in foreign direct investment (FDI) to the region was a contributing factor, since it normally leads to greater importation of intermediate goods, and more generally the region's collective growth in imports of 26% slightly outpaced the 25% growth in exports. Nevertheless, the increasing current account deficits appear paradoxical since most countries are curbing government spending and have experienced moderate credit growth, which when unrestrained are two key factors behind rising domestic consumption and increasing imports. Upon closer inspection, however, one of the reasons for the subdued credit growth was a marked decline in financing flows from Western Europe. While FDI was up, portfolio investment declined and lending slowed substantially. Uncertainty and rising risk aversion in the EU resulted not only in a slowdown in financing and investment from Western Europe, but also to greater profit taking from investments already made, as well as net outflows of capital as Eurozone based financial institutions with holdings in the Black Sea region deleveraged in response to tightening domestic conditions and regulatory pressures in their home countries.

Figure 2: Trends in Average Fiscal Deficit of BSEC Region as a Share of GDP



Note: Black Sea Region Average – Blue, Russia Alone – Green, Black Sea Region Minus Russia – Red

As Figure 2 shows, for the second consecutive year, the countries of the Black Sea region realized considerable progress in their fiscal consolidation efforts. Government finances deteriorated sharply in late 2008 and throughout 2009 as the onset of the economic slowdown resulted in both a decline in revenues due to lower economic activity, and in many cases increased spending due to automatic stabilizers such as unemployment benefits 'kicking in', support to stabilize financial systems, and in some cases fiscal stimulus measures to mitigate the negative impact of the decline in private consumption and investment. Moreover, while revenues are sensitive to changes in overall economic activity, government spending is more difficult to curtail in the short term since most expenditures are for non-discretionary purposes such as repayment of loans and salaries of public sector personnel, while it is often difficult (and more costly) to stop capital expenditures for public investments already initiated, than it is to continue.

With the return to growth in most Black Sea economies in the latter part of 2009, and then through 2010 and 2011, all countries undertook measures to reduce or limit expenditures on the one hand, and to enhance revenues on the other. The revenue picture improved with the rising receipts that accompany increased economic activity, but countries were particularly assiduous in their efforts to contain spending. Within two years, BSEC governments have reduced their budget deficits by an impressive 6.5% of GDP, about 2.7% in 2010 and a further 3.8% in 2011. Figure 2 shows fiscal trends averaged for the entire Black Sea region, but also for the region minus Russia, and Russia individually, since Russia has traditionally posted significant fiscal surpluses due to burgeoning energy receipts, while most of the rest of the region runs fiscal deficits, something which the weighted regional average hides thus rendering it somewhat misleading on a stand alone basis. The Black Sea region ex-Russia reduced

its budget deficit by 2.3% in 2011, and 4.7% total between 2009 and 2011. As a result, its deficit of –2.7% of GDP is roughly on par with pre-crisis levels. Interestingly, Russia's post-crisis fiscal balance converged with that of the rest of the region in 2009 and 2010, but in 2011 it improved by around 5.1% of GDP and returned to the pre-crisis fiscal surpluses it achieved with regularity.

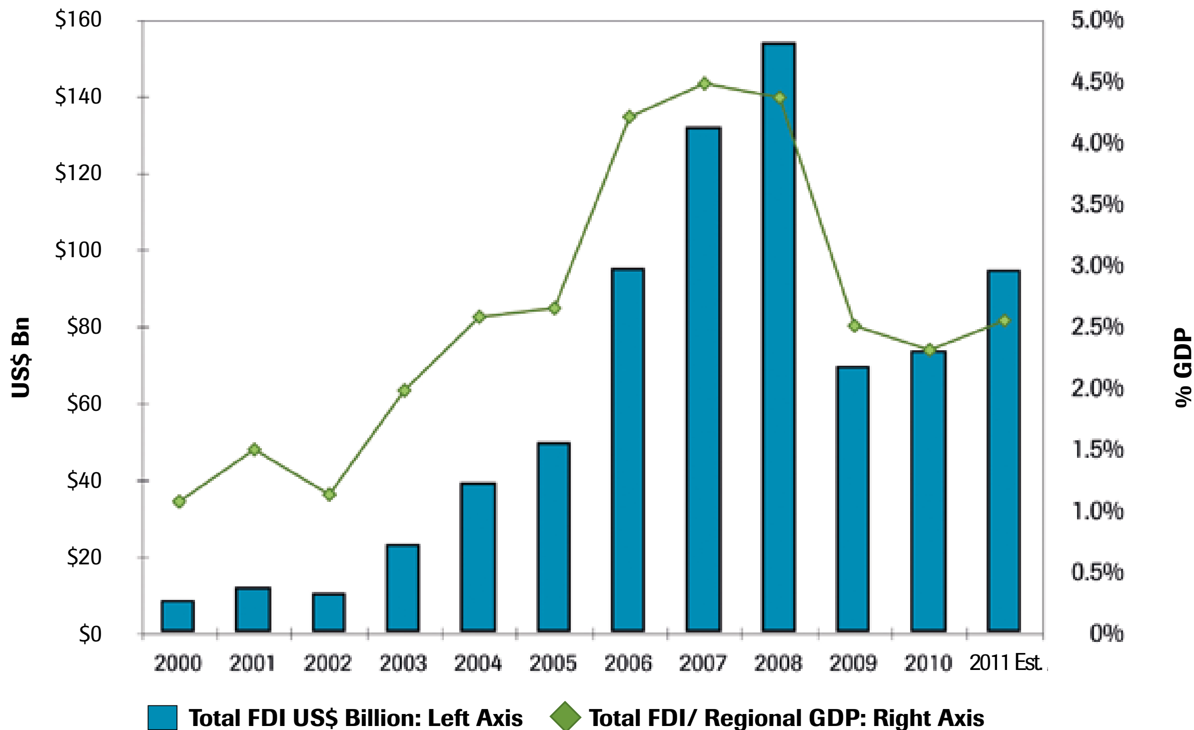
With the exception of Greece, public debt in most Black Sea countries remains at very manageable levels, with little movement of particular significance during the course of 2011. Azerbaijan, Bulgaria, and Russia have public debt levels below 20% of GDP, while most of the remaining countries have debt between 30–50% of GDP. There is some variation as concerns the breakdown of external and domestic public debt, with countries with larger and deeper financial sectors having lower levels of external debt since they are better able to access resources from the domestic market. Moreover, much of the external debt is owed to official bodies, chiefly the International Monetary Fund with which a number of countries continue to have lending programs, but also other international financial institutions and official lenders.

Privately incurred external debt levels in many countries are significantly higher than public external debt, and this represents a potential vulnerability for these countries that requires careful monitoring. One of the key lessons of the September 2008 global financial crisis, was that high reliance on continued external financing by private firms and banks in a country represented a key vulnerability even if that country's public external debt levels were low and comfortably manageable. With the freezing up of global financial markets and the sudden unavailability of additional funding, firms and banks found themselves in acute liquidity (and in some cases solvency) crises, unable to access funds in order to meet obligations and conduct their business.

Facing such stress and crises of confidence, a substantial portion of the private debts ended up nationalized, directly and indirectly. Most evidently, governments in every country were forced, to a greater or lesser degree, to undertake costly measures to support domestic financial systems that suddenly faced crises of confidence. These included direct measures such as share purchases of banks, takeover of teetering financial institutions, and cheap liquidity provision, as well as indirect measures such as banking guarantees and contingent financing. Although ultimately successful, the measures were politically unpopular and financially expensive adding to public deficits and debts. Increased deficit spending to mitigate the economic downturn also effectively nationalized some of the private debt.

Private external debt in the Black Sea region is now off its 2009–10 peaks, as firms and banks have become more cautious, and those highly exposed have been forced to reduce their external borrowing in many cases (due to higher costs and more limited availability). On the one hand, this means that the region is less vulnerable now than it was in 2008. On the other hand, the region is exposed to changes in sentiment, possibly for reasons that have little or nothing to do with fundamental factors in the countries themselves, as was the case by and large in September 2008. Moreover, with regional firms and banks growing in sophistication and contacts, the situation always bears monitoring since trends can emerge rather quickly resulting in changes in underlying system risk levels and overall susceptibility to shocks.

Figure 3: Foreign Direct Investment in the Black Sea Region 2000-2011



As Figure 3 shows, foreign direct investment (FDI) in the Black Sea region picked up in 2011 relative to 2010, rising by nearly 29% to USD 88.9 billion, from USD 69.1 billion. Because of the overall economic growth in the region, the increase as a share of the economy was more modest, with FDI reaching 2.5% of GDP in 2011, up from 2.3% in 2010. This puts regional FDI on a par with the amounts attracted in the earlier part of the previous decade when the economic boom was in its early stages, and falls short of the levels achieved from 2006–2008. Relative to the peak year of 2008, regional FDI in 2011 was approximately 39% lower. Nonetheless, the upswing was a positive development, and an indication that after a couple of 'slow' years, foreign investor interest in the Black Sea region is returning. The 29% increase observed for the Black Sea region is higher than the 17% increase in global FDI into Emerging Markets[2].

This is not surprising, since in contrast to other forms of financing from abroad, such as lending or portfolio investment, direct investment is much slower, given that it takes a long time to plan and implement. Thus if new investment plans were shelved or otherwise cancelled at the peak of the crisis, there would be a time lag before investment levels recover. Lingering post-crisis global uncertainties have dampened investment appetite further, while the Black Sea region is also impacted negatively by the fact that most FDI comes from Eurozone countries. These countries have been primarily focused on the continuing Euro crisis through 2010 and 2011, and as a consequence of the unique uncertainties that their banks and firms have faced, their relative sluggishness to undertake new investments is understandable. Indeed, this puts the increase achieved in 2011 Black Sea region FDI levels in a particularly positive light.

As with other indicators, the overall regional average hides considerable variation from country to country. Relative to the size of the economy, the highest levels of FDI for 2011 attracted in the greater Black Sea region were in Albania (7.0% of GDP), Georgia (6.8%), Armenia (6.5%), and Serbia (6.4%).

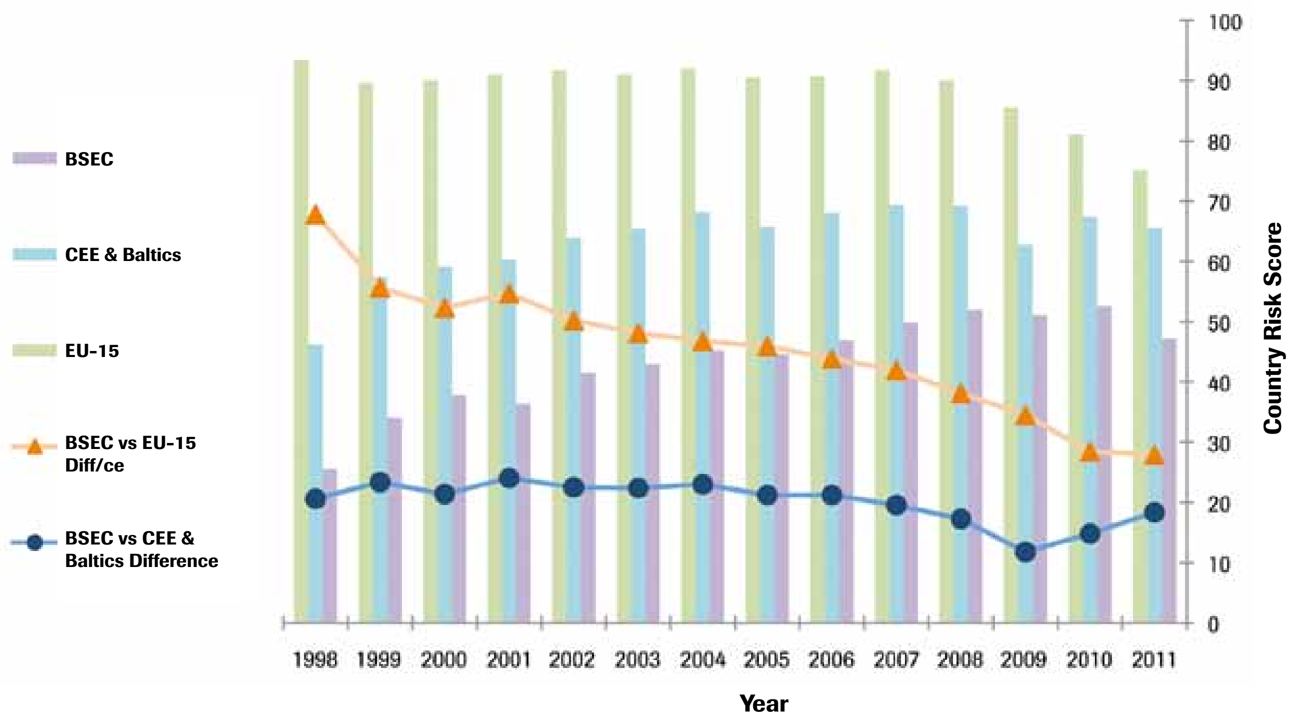
FDI levels are also a useful proxy for assessing the evolution of the business environment in a country (or group of countries), as it represents

2 International Institute of Finance, *Capital Flows to Emerging Market Economies*, 24 January 2012

an easily measurable indicator of (i) attractiveness of a country or region for foreign firms and (ii) how well the investment environment of a country or region is perceived. There is a clear link between ease of doing business on the one hand and attractiveness to external investors on the other hand. The favorable trend implied by FDI is confirmed more directly by other qualitative analyses of the business environment such as Transparency International's *Corruption Perceptions Index,* EBRD's *Transition Indicator Scores*, and the World Economic Forum's *Financial Development Report* and *Global Competitiveness Report.* The various measures of these reports show a number of countries with favorable business environments. For example, Bloomberg's rankings in *Best Countries for Business* puts five Black Sea Countries in its top 50: Romania at 32, Turkey at 41, Bulgaria at 43, Ukraine at 45, and Russia at 48.

More importantly, there is an improving trend over time in the quality of the business environment of the Black Sea region – collectively and the countries individually – even if progress from year to year is sometimes uneven as countries undertaking intensive reforms improve abruptly in relative terms to other countries. A highly systematic analysis of evolution of the business environment is the World Bank's annual *Doing Business Report,* the 2012 edition, which[3] shows significant improvements and positive trends among the countries of the Black Sea region. No fewer than five regional economies are listed among the top 30 economies which improved the most in the ease of doing business during 2010/11. These include Armenia, which was second overall globally, and Moldova, which placed ninth, along with Georgia, Russia, and Ukraine. All Black Sea economies have enacted measures and reforms over the 2005–2011 period that have led to improvements in their overall business environment score, and five have made sustained progress which ranks them in the top quartile of reforming and improving states. Most exceptional is the case of Georgia, which ranks first globally as a reformer over this period, and which has made the biggest improvement of any single country in its overall scores. It is followed by Azerbaijan, which ranks 13th globally, Russia (23rd), Albania (42nd) and Armenia (44th).

Figure 4: Trends in Regional Euromoney Country Risk Scores & Relative Differences



Source: Euromoney Magazine

3 The current version of Doing Business, *Doing Business 2012: Doing Business in a More Transparent World* was issued in October 2011 and covered the 2010-11 period.

Another measure of the business environment is to look at country risk, which assesses the likelihood of a non-business event occurring, or a non-business related situation transpiring, which would threaten (i) the normal operation of a company (ii) the value of assets, and/or (iii) the profitability of loans and investments. The better (e.g. lower) that the level of country risk is in a country, the better the business environment tends to be. Figure 4 on page 15 shows collective country risk developments for the Black Sea region ('BSEC') as well as how it fares relative to two common comparators: (i) the fifteen countries that comprised the European Union prior to its 2004 expansion (the 'EU-15'), and (ii) the eight Central European and Baltic countries[4] that joined the EU in 2004 (the 'CEE & Baltics'). The figure collates country risk scores as measured by Euromoney Magazine in its periodic *Country Risk surveys*[5].

The chart shows that from 1998–2008, the Black Sea region steadily improved its measures of country risk. In 2009, in the aftermath of the crisis, it suffered a decline in its score – in other words, an increase in country risk. It resumed its pattern of improvement in 2010 but experienced another setback in 2011. The 2009 decline may be explained by the economic downturn suffered across the region, while the 2010 improvement coincides with the resumption of growth. The drop in 2011 is at first puzzling, since the region posted economic growth nearly on par with 2010, and the key macroeconomic indicators in Table 1 are by and large stable or even favorable. However, viewed against the much more significant decline of the EU-15, most of whom are Eurozone members, it suggests that contagion from the Eurozone crisis has affected the Black Sea region, and that perhaps the region is viewed as more vulnerable to contagion from the Eurozone than the CEE & Baltic states. Thus, the Black Sea region, despite the slippage in 2011, has continued to narrow the difference in country risk with the EU-15, as shown by the declining line comparing BSEC to the EU-15. By contrast, risk perceptions relative to the CEE & Baltic states – which suffered a sharp decline in 2009, followed by a bigger improvement in 2010 and a smaller decline in 2011, relative to the Black Sea region – have grown. These are all EU countries, that are more institutionally linked to the EU-15 politically and economically, of which three are Eurozone members already. Nevertheless, the long term trend is clearly positive for the Black Sea region, demonstrating considerable improvement over time in relative and absolute terms consistent with the favorable trends in other quantitative assessments of business environment and key macroeconomic indicators.

The positive trends in the business environment extend to the region's sovereign credit ratings, although the global financial crisis has muddled the picture somewhat. (See Table 2)[6]. Every Black Sea country receives at least one sovereign rating from one of the three largest credit rating agencies, something which denotes growing maturity and economic progress since these ratings are prerequisites for entering international capital markets in order to borrow funds. Domestically, they also help to set key benchmarks, which in turn permit local financial markets to grow. Many countries received downgrades during the 2008–09 period as they experienced the impact of the global crisis and the attendant economic downturn, and while aggregate ratings are below those at end 2007 – the last year prior to the global crisis- a number of countries have subsequently been upgraded. As at end-2011, the Black Sea region had four countries rated investment grade, while at the end of 1999 it only had one.

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4 Czech Republic, Estonia, Hungary, Latvia, Lithuania, Poland, Slovakia, Slovenia.

5 Euromoney's Country Risk survey is a comprehensive index, covering nine categories. Figure 4 provides simplified regional representations based only on arithmetic averages. They are not weighted to account for the relative size of economies' other factors. The figure was prepared for illustrative purposes, and shows the evolution of country risk scores over time. For the bars, an increase in score means an improvement (e.g. lowering) of country risk, with 100 representing the maximum (e.g. lowest risk) score. For the lines, a declining trend indicates decreasing differences in country risk scores between the regions being compared (e.g. convergence of scores and country risk levels).

6 Long term sovereign credit ratings, which measure creditworthiness, have certain flaws and limitations, but they are often a useful proxy for business environment. They are easy to recognize and compare, and measure elements relating to country risk which correlates directly to the quality of the business environment. Investment grade refers to a sovereign credit rating of Baa3 or better according to Moody's, and BBB- or better according to Standard & Poor's and Fitch.

Table 2: BSTDB Sovereign Credit Ratings Comparison 1999 vs. 2011

	December 1999			December 2011		
	Moody's	S&P	Fitch	Moody's	S&P	Fitch
Albania	—	—	—	B1	B+	—
Armenia	—	—	—	Ba2	—	BB-
Azerbaijan	—	—	—	Ba1	BB+	BBB-
Bulgaria	B2	B	B+	Baa2	BBB	BBB-
Georgia	—	—	—	Ba3	B+	B+
Greece	A2	A-	BBB+	Ca	CC	B+
Moldova	B2	—	B-	B3	—	—
Romania	B3	B-	B-	Baa3	BB+	BB+
Russia	Ca	SD	CCC	Baa1	BBB	BBB
Turkey	B1	B	B+	Ba2	BB	BB+
Ukraine	B3	—	—	B2	B+	B

External Trade

External trade was a second (behind private domestic consumption), but important contributor to economic growth in the Black Sea region in 2011. As with the overall pattern of economic growth, export growth was more robust in the first half of 2011 and slower in the second half of the year, influenced by the unfavorable environment in Western Europe and growing global uncertainties. Despite the relative slowdown in the latter part of 2011, the momentum from the external trade growth was such that regional exports grew by an estimated 25.4% relative to 2010. This follows up on the 25.3% growth in exports achieved in 2010 and indicates a full recovery from the precipitous decline in external trade of 31.7% during the 2009 recession. Indeed, aggregate regional exports (across all BSEC countries) for 2011 reached USD 890 billion, a record figure that exceeded the previous peak achieved in 2008. Exports were equivalent to 25.7% of regional GDP, also a record figure which was better than the 2008 level and underscored the rapid recovery of external trade flows after the temporary collapse caused by the financial crisis of late 2008 and its subsequent economic crisis.

Moreover, the strong export performance was spread across the region geographically and structurally. Small relatively closed economies such as Albania, Armenia, Georgia, and Moldova were among the countries achieving record export performance. Among larger economies, Russia, primarily an energy and commodity exporter, posted record exports, as did Bulgaria and Romania, which rely mainly on manufactured goods. Import growth for 2011 relative to 2010 was even higher at 26.1%, following up on a 22.6% growth in 2010 and in sharp contrast to the decline of 34.2% during the downturn in 2009. Aggregate regional imports reached an estimated 24.3% of regional GDP (USD 841 billion), another record figure which exceeded the 2008 peak.

Turning to intra-regional trade within the Black Sea, figures over the last few years show similar trends to overall external trade flows, but to a more amplified degree[7]. As with the external trade flows, intra-regional trade among BSEC member countries peaked in 2008. Intra-regional trade declined by 39% in 2009 (against an overall decline of 33%), but reversed this trend and rose 36% in 2010 (against an overall increase in external trade of 23%).

7 Overall export and import estimates for 2011 were available at the time of publication for BSEC countries, but due to measurement lags, full figures for 2011 were not available for the individual country breakdown. Therefore only figures up to 2010 are discussed for the Region, and shown in the figure.

Figure 5: Intra-Regional Trade Flows in the Black Sea Region 1999 – 2010

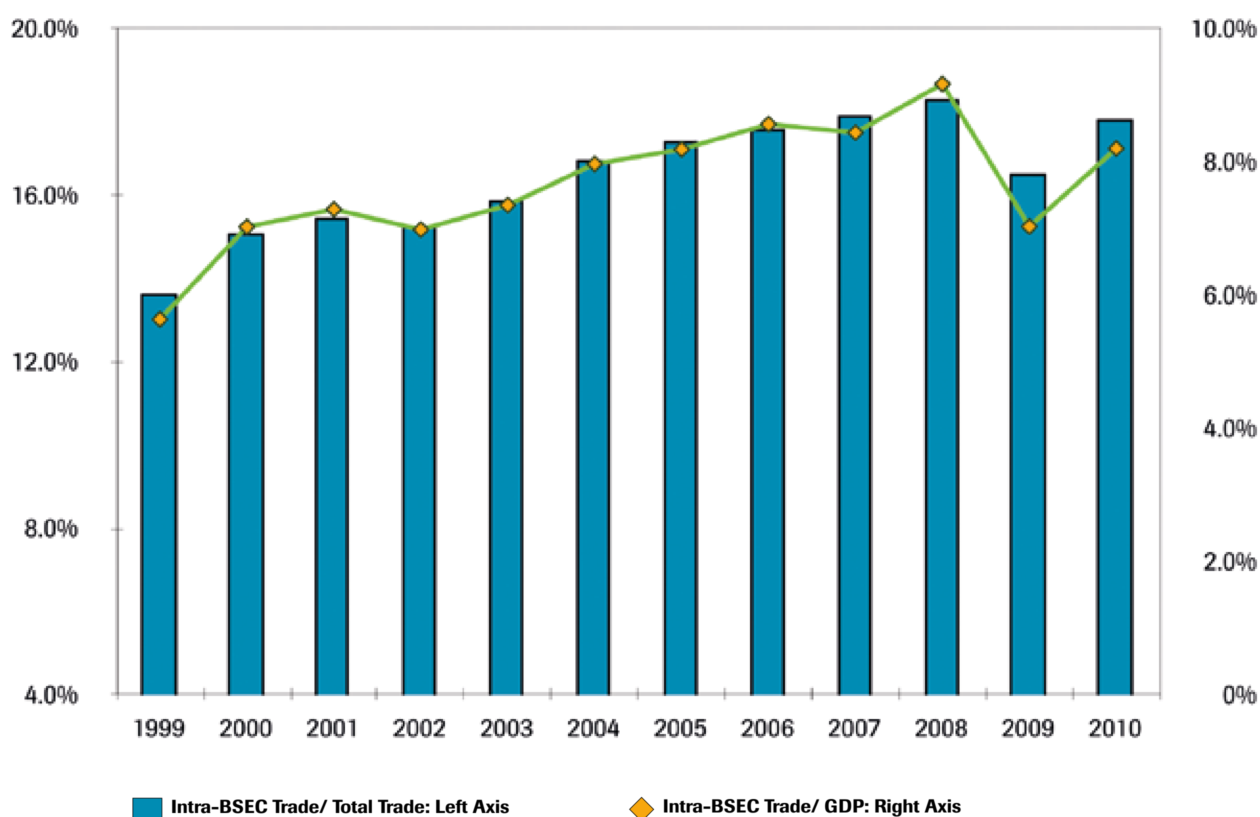


Figure 5 shows the evolution of intra-regional trade flows. As a share of GDP, intra-BSEC trade slipped from a peak of 9.2% of GDP in 2008 to 7.0% in 2009, before rising to 8.2% of GDP for 2010, slightly off the peak level, but on par with the outcomes from 2005–2007. Given its faster growth rate, intra-BSEC trade has also grown as a share of total external trade of the Black Sea region. For 2010, intra-BSEC trade was 17.8% of total external regional trade, a level slightly below the peak of 18.3% achieved in 2008, and a substantial recovery from the dip to 16.5% suffered in 2009. Early evidence from provisional data indicates that this trend continued in 2011, and that regional trade advanced at a faster pace than overall trade volume, providing further evidence of rising regional economic cooperation and the continuing integration of the region in the global economy. However, while these trends are favorable, they fall short of the levels of trade observed in more highly integrated regions such as the Baltic Sea, where intra-regional trade is over 40% of total trade.

The Baltic Sea region has a number of particular characteristics, such as many small states sharing significant institutional structures, since all are EU members, and are highly extroverted and integrated into the global economy, with strong cultural affinities and traditions of commerce.

The Black Sea region's much lower figure of trade among neighboring (or proximate) states, together with the greater year to year volatility of these flows, suggests that intra-regional trade ties remain less fully developed or institutionalized than those observed elsewhere, or even of those which some BSEC counties have with trade partners outside the Black Sea region. This in turn underscores once again the degree to which there exists potential for further development of regional trade and investment, for countries to pursue higher growth on a more sustainable basis, to achieve considerable mutual gains, and to improve their economic competitiveness.

In Focus: Banking Sector in the Black Sea region

The Economic Transformation of the Black Sea Region 1999–2008

The Black Sea region is now very different from what it was in 1999, when the Bank came into existence. During this period per capita incomes have risen dramatically. Between 1999 and 2008 they increased nearly five times in dollar terms, from about USD 2,100 in 1999 to an estimated USD 10,300 in 2008. Apart from the increased prosperity resulting from the 2000–2008 period of high growth, the economies of the region are now more open, interact with each other and are more in touch with the global economy in general.

The robust growth in the decade leading up to 2008 resulted in declining poverty rates in all of the countries in the region. Other key indicators such as health and education have also reflected the improvements in living standards.

During the period the banking sector increased rapidly, with double digit annual growth rates in credit to the private sector. Such growth was supported in some instances, with funding provided by parent banks in Western countries, and in other instances, it was facilitated by easy access by banks to cheap borrowing in the international credit market.

Implications of the Global Crisis for the Black Sea Region – 2009

Since the global financial crisis erupted in September 2008, risk aversion reached panic proportions and access to financing was severely restricted. There was no 'decoupling' between the developed economies and the rest of the transitioning, emerging, developing world; in Central, Eastern and South-Eastern Europe contagion from the global crisis threatened to reverse years of economic progress.

The impact of the crisis on the Black Sea region has been negative. As global financial markets were on the verge of collapse, bank lending to businesses and consumers dried up, thus reducing liquidity and demand and creating uncertainties that severely impeded investment. There was a drop in international trade flows, and the ensuing economic contraction in key Western European markets led to a reduced demand for goods and resources from the region. An additional factor for certain countries was a decline in remittances from migrants and co-nationals living abroad, which also contributed to the reduction in domestic demand. The situation was exacerbated by a slump in commodity prices.

Consequent to the above, regional currencies came under terrible pressure and some countries experienced massive depreciation of their currencies in 2009. Such depreciation however helped exporters, and favored the adjustment of the external balance.

However, the financial systems have not collapsed, and they have managed to avoid the bank insolvencies that marked previous crises and led to panic in places like Bulgaria in 1997, Russia in 1998 and Turkey in 2001.

The nature of the crisis, and the difficulties encountered in agreeing to appropriate response measures, points to the possibility of a lengthy and slow recovery. Furthermore, the global financial crisis reaffirmed that there is a hierarchy of access to financing based on perceptions of country risk which are determined by a combination of credit ratings, levels of development, and overall economic size. Thus, the restoration of credit flows to the Black Sea countries represents a critical element in the recovery from the crisis.

Challenges for Black Sea Economies in 2009–2011

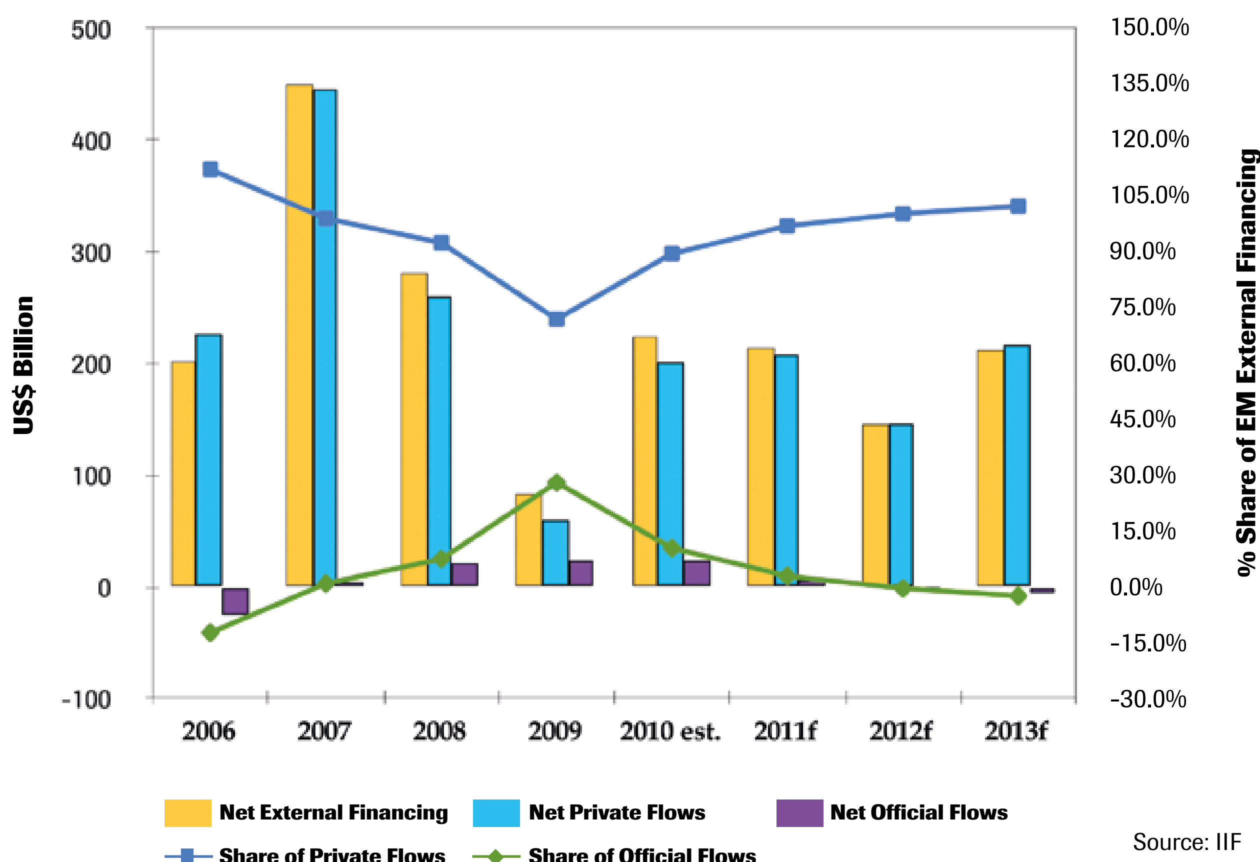
Deleveraging and Capital Flows

The main risk for the region was that deleveraging and balance sheet adjustments in advanced economies weighed heavily on capital flows. In many countries large-scale official financing was needed to offset the contraction in private cross-border funding.

The deleveraging process was mostly driven by high liquidity and, in some instances, write-offs in the financial sector, and in certain cases was accelerated by the reversal of spending decisions of governments and of households who had accumulated record-levels of debt.

Emerging Europe was hit particularly hard. Cross-border bank funding was disrupted and currencies came under pressure, especially in those countries with floating exchange rate systems and large domestic and external imbalances.

Overall, net private flows to emerging markets show a sharp drop in 2009, some recovery in 2010, higher uncertainty in 2011, and again an expected decline in 2012. However, remittances appear to have been generally more resilient to external shocks than private capital flows.



Source: IIF

Protectionism and Trade Finance

Further to decline in economic activity, deterioration of public finances, and increased unemployment in developed economies, there was a contraction of international trade.

The financial crisis also brought about changes in the pricing and availability of trade finance. Thus, trade was inhibited by difficulties in obtaining financing for imports and exports.

Declines in global trade and harsh economic conditions in developed economies induced a growing fear of a resurgence of protectionism. Such protectionist measures include increases in the number of anti-dumping investigations, introduction of potentially trade-distorting subsidies, and implementation of various programs in support of financial services industries.

Response to the Crisis – Black Sea Region 2009–2011

Governments took significant policy steps to address the crisis, but further progress in implementation of adopted policies and additional structural reforms is still needed. Moreover, to the extent that financial market strains are global and interconnected, international policy cooperation is crucial for restoring market trust.

Macroeconomic policies

Central banks reduced policy rates and reserve requirements, thus making additional liquidity available to banks. Central banks also explored unconventional measures to stimulate economic activity, while anchoring expectations of future inflation.

Fiscal stimulus was critical in preventing the regional economy from going into a deep recession in 2009. However, starting with 2010, measures aimed at fiscal consolidation and debt stabilization had been implemented, in order to regain internal balance.

In cases of countries with floating, managed, or adjustable exchange rate regimes, there was also some scope for exchange rate adjustment. This policy action was used diligently to a limited extent, due to inflation risk considerations and because the prevalence of foreign currency-denominated contracts could cause negative balance sheet effects.

Following the success of the initial response to the risks posed by contagion effects from the global financial crisis, countries, in support of their fiscal consolidation efforts, applied increases in indirect and wealth taxes, income policies, and legal and institutional reform of social security systems. Therefore, fiscal deficits in most Black Sea countries contracted significantly in 2010 and 2011 (relative to the crisis levels of 2008 and 2009), and medium-term fiscal and legislative frameworks were strengthened.

Vienna Initiative

When the global financial crisis struck, many countries in emerging Europe were thought vulnerable because of high levels of private debt owed to foreign banks and foreign-currency exposure in their domestic lending activities. Significantly, in many Black Sea countries much of the banking system was foreign-owned (mainly by European Union based entities), and there were fears that the parent banks might withdraw support for their local branches or subsidiaries.

Policymakers in the region became concerned that foreign-owned banks, despite their declared long-term interest in the region, would seek to cut their lending, or worse, might be forced to do so due to pressures in their home country, even if that would have meant writing-off loans and making losses, and closing operations.

At the start of 2009, the foreign owners of banks in many countries of Central and Eastern Europe found themselves in a scenario where cooperation was the best strategy; however, there existed a game theory situation where much trust was needed for cooperation to occur, but lingering uncertainties mitigated against trust and risked forcing actors into unilateral action to safeguard short term interests. In a possible multiple equilibrium situation, incentives to be the first mover were strong, with likely sub-optimal non-cooperation and chaos scenarios resulting. In other words, without coordination, the most likely outcome was that foreign-owned banks would start pulling out.

Previous crises had demonstrated that the unwillingness of foreign banks to maintain trade and other credits precipitated sovereign defaults and currency runs. A sudden outflow of capital therefore, could potentially escalate into a fully-fledged currency and balance of payments crisis with potential devastating consequences especially for countries already hit by recession and running large current account deficits.

A series of meetings resulted, involving the IMF, international financial institutions such as the World Bank, EIB, and EBRD, the European Commission, regional and parent bank country authorities, the European Central Bank, other interested parties and many Western banks with large operations in the Central, Eastern, and South-Eastern Europe region. The aim of these meetings was to prevent foreign-owned banks (those based in the EU) from pulling out of emerging Europe. The result was the European Bank Coordination Initiative, also known as the 'Vienna Initiative' – which played a vital role in helping avert a systemic crisis. With the cautious return of investor appetite for risk in the second quarter of 2009, parent banks have continued to support their local holdings or pledged to do so, thus maintaining their exposure and in certain instances recapitalizing subsidiaries as needed.

The Vienna Initiative proved to be an effective instrument for preventing massive deleveraging, through the provision of incentives and subsidies to Western parents of banks in emerging Europe.

However, for some governments the added burden on public finances of the cost of such incentives proved destabilizing. In the case of Greece, fiscal stimulus extended to avert an abrupt decline in economic activity in 2009 and participation in the Vienna initiative added over 20% of GDP to an already large public debt.

Banking Sector in the Black Sea Region – 2011

Whilst the global crisis has certainly created dysfunctions in the financial systems of the Black Sea region, it has not manifested itself as a full-scale financial crisis. The financial systems however remain under stress, lending to private companies is still limited, and in some countries there has been a painful process of deleveraging that has dampened economic activity.

To a larger degree than in other parts of the world, lending in the countries of Central, Eastern and South-Eastern Europe is dominated by foreign-owned banks. In the 1990s and through much of the 2000s, that arrangement allowed for more rapid credit growth than would otherwise have been possible, as the Western European parents provided cheap funds to those subsidiaries. In 2011, with their own balance sheets under stress and under regulatory pressure to strengthen capital, those banks were unable to fund credit growth in their regional subsidiaries, and in some instances have reversed the flow of funds. Persisting uncertainties and limited access to international credit markets for funding have further limited the ability of regional banks to maintain availability of credit to the private sector.

Moreover, credit to government increased both in relative and absolute terms, although not to excessive levels, in some countries probably crowding-out the private sector in the process, and fiscal consolidation measures taken by governments have depressed domestic demand. Consequently, a large number of SMEs have been closed and unemployment has increased. Faced with an uncertain future and the specter of increased unemployment during a likely protracted and slow recovery, households have increased savings and private enterprises have cut off investment. Thus, while banks have increased their deposit base, demand for credit has also declined. The stable deposit growth, along with low demand for credit on domestic markets, lead to excess liquidity in the banking sector and enabled local banks to repay some of the loans from their parent companies.

Nevertheless, this sequence of events has resulted in higher levels of "precautionary" savings, lower loans to deposit ratios, and lower asset to GDP ratios. On the negative side, the fiscal consolidation and its induced reduction in domestic demand, and economic activity more generally, has also been a driving force behind the rapid increase in NPLs.

While the portrayed situation affected mostly Bulgaria, Romania and Ukraine, it is evident now, that Russia and Turkey were notable exceptions. Russia and Turkey are notable for the small degree of foreign presence in their banking system, something that used to be criticized as protectionism and fostering inefficiency. Economic growth and demand went beyond their own large and dynamic internal markets and have also buoyed growth in neighboring states via capital flows, increased trade, and remittances.

Greece, on the other hand, has been affected by an excessive expansion of its banking sector in South-Eastern Europe and in its domestic financial market as well as by its exposure to Greek Bonds funded by large borrowings from the international capital market, including accessing liquidity from ECB against the collateral of Greek sovereign bonds. The fiscal crisis, the uncertainty and the deep recession that followed, significantly worsened the financial conditions. The "haircut" applied to Greek bonds impaired the asset value of the banking sector. The liquidity position of most Greek banks was further weakened by a significant decline in their deposit base. However, banks will be recapitalized to the tune of about EUR 50 billion. This amount is available according to the new loan agreement and as estimated by the Bank of Greece is quite sufficient to cover the capital requirements of the banks with respect to the impairment of the value of Greek government bonds which they hold in their portfolios, the expected losses in loan portfolios, and the provisions charged already for the above losses and business plans submitted by the banks themselves.

Main Financial Indicators for 2011

Country	Bank Assets/ GDP (%)	Credit Growth (%)	Loans to Assets (%)	Loans to Deposits (%)	Non-Performing Loans (%)	Solvency Ratio (%)
Albania	84.6	12.2	47.4	60.3	18.6	15.6
Armenia	54.6	42.6	62.3	130.9	3.4	18.3
Azerbaijan	28.5	2.3	69.8	105.3	6.4	16.1
Bulgaria	102.1	3.3	68.2	105.1	14.9	17.5
Georgia	52.3	19.6	61.0	136.8	8.6	17.0
Greece	221.4	-4.1	55.0	112.7	14.7	10.1
Moldova	58.1	21.5	62.1	90.7	10.7	30.4
Romania	68.5	8.2	66.8	73.5	14.1	14.5
Russia	76.6	27.1	49.8	174.6	6.6	14.7
Turkey	94.0	29.5	56.1	98.2	2.1	16.6
Ukraine	80.8	12.3	76.1	163.0	14.7	18.9

Source: national central banks

The banking sectors in the countries of the Black Sea region are relatively simple in their structure and operating mode, and the product range they offer is straightforward, without complicated derivative products. With the exception of Greece, banking sector assets to GDP ratios are comfortable, and generally, with the exception of Russia and Ukraine, loans are covered to a safe extent by deposits. Therefore, even though the ratio of non-performing loans to total loans has increased, the solvency ratio is still comfortably high and the ability of regional banks to withstand future shocks coming from the economy is adequate. However, external shocks induced by faster and deeper deleveraging of parent banks in Western Europe, or an increase in the cost of funds, may create significant problems to regional banks.

Indeed, the recent crisis has shown that what was generally considered a weakness – the small size and simple structure of the bank dominated financial sector – in this instance proved to be a strength, and what was considered to be a strength – foreign ownership of financial institutions, highly concentrated lending at the top 5–6 banks in the system, and easy access to cheap liquidity provided by parent institutions making funding and lending decisions on a consolidated basis – proved to be a weakness.

Furthermore, although integration in the global economy provides opportunities for faster growth, there are channels of contagion through which global shocks are easily passed to the domestic economies, which most likely are not well equipped to withstand such shocks. It appears therefore, that locally capitalized and relatively large domestic banks, focused on the domestic market, are better suited than subsidiaries of foreign banks, to understand local conditions, pursue increases in lending based on the available increases in domestic deposits, and perform effectively the intermediation function to the benefit of all parties involved, as these financial institutions are intrinsically linked to, and see their fortunes in, the successful operation of the domestic economy and the growth of the domestic market.

This “history” demonstrates that solid financial systems need not be large, but should be liquid, well regulated and supervised, and should only expand credit to the extent it meets two conditions: (i) there is a credit demand for viable operations; and (ii) credit growth is mainly supported by the growth in the domestic deposit base, with external sources limited to long-term funds from international capital markets. Reliance on funding provided by foreign shareholders should be limited to various forms of capital and subordinated debt.

Financial intermediation is a necessary pre-requisite for efficient use of available capital and economic growth, but supply driven rapid credit growth creates conditions for potentially huge financial and economic problems down the road.

Future of International Cooperation and Coordination from 2012 onwards

Despite fears about larger losses in the future as the effect of renewed recessionary pressures which may hit companies and consumers, most of the banks in the Black Sea region seem to be well positioned to weather moderate shocks, unless the economic downturn results in a sharp rise in non-performing loans.

However, as the sovereign crisis affecting Eurozone countries and the new regulatory requirements imposed on Western European banks under Basel III limit the ability of those banks to raise funds, their dominant presence in CEE and SEE markets through subsidiaries has become a source of economic weakness for the region. The Western European banks that dominate lending in many CEE countries through their subsidiaries face more severe and durable funding problems than they did in early 2009, as well as intense regulatory and political pressure to meet tough new capital-adequacy targets. In this sense, the region is vulnerable to contagion from the Eurozone crisis.

As these concerns have become more pronounced, on 12/13 March 2012 the fourth Full Forum of the Vienna Initiative was held in order to boost coordination between host and home countries on cross-border banking activities. Named 'Vienna 2' and hosted by the European Commission, the meeting raised the specter that cut backs or even withdrawal by Eurozone based banks represents an imminent threat to the region.

If Vienna 1 was concerned with finding solutions to preserve the exposure of Western banks to the region, Vienna 2 may have to deal with finding solutions to mitigate the negative effects of not only a reduction in exposure, but of significant downsizing of operations in the region, which now appears unavoidable. Indeed, policy makers involved in Vienna 2 have conceded that lending to businesses and households in many CEE countries will be held back by the problems facing Western European banks, damaging their growth prospects in 2012, and possibly beyond 2012.

The best they can hope for is to limit the scale of the credit slowdown and ensure any withdrawal of Western European banks from the region is orderly and doesn't generate panic among other investors.

The stability of the financial sector and orderly credit conditions in emerging Europe are in the shared interest of the private sector and home and host countries. Thus, principles to avoid disorderly deleveraging in emerging Europe by officials and private sector banks are necessary. The meeting therefore sought to better coordinate banking sector regulation and supervision, find new and consistent definition for NPLs and effective joint solutions for their resolution, and to contain negative spill-overs between the Euro area and emerging Europe. It also emphasized the central role of European institutions and the international financial institutions in facilitating this coordination.

Under Vienna 2, banking groups active in the region, along with national and European authorities, will try to cooperate closely in efforts to maintain credit conditions consistent with sustainable economic growth. Banks also pledged to maintain lending levels in countries that are receiving help from the International Monetary Fund, including Romania, Serbia, and Ukraine.

Under the principles agreed in this context, an important role lies on the international financial institutions and international organizations which can assist through policy dialogue, knowledge sharing, and of course, financial support functions. In this context, it is particularly important that over the next few years, Multilateral Development Banks increase export credit and related investment facilities.

BSTDB in the Black Sea Region

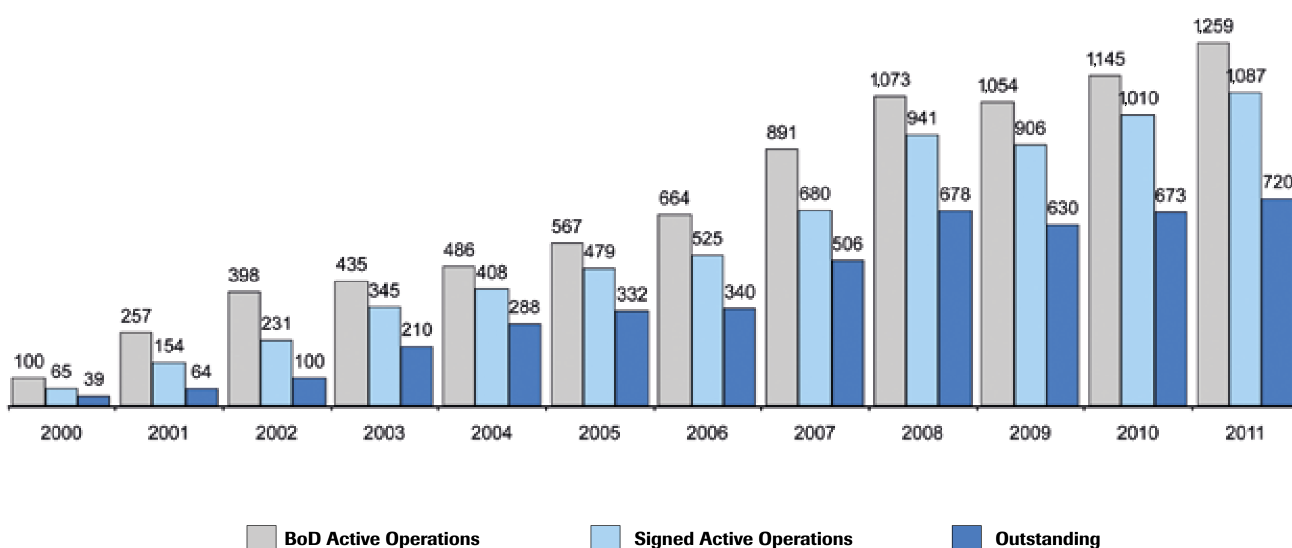
Portfolio Description

Since the beginning of operations in June 1999, the Bank has approved 242 operations amounting to about EUR 2.3 billion.

Throughout this period, there were 227 signed operations for a total outstanding amount of EUR 2.1 billion. A total of 157 operations for about EUR 1.5 billion were repaid.

At end-2011, there were 121 operations in the active outstanding portfolio for EUR 720 million, a 7% increase from the end of 2010. At end-2011, there were 4 problem loans, duly provisioned, representing 6.8% of the value of the outstanding portfolio.

Evolution of Portfolio of Operations 1999–2011



Portfolio Developments During 2011

In 2011, the Board of Directors approved 30 new operations for a total of EUR 359.3 million. This was the result of an intensive business generation effort, which resulted in the signing of 29 new operations for a total of EUR 298.2 million. At end-2011, the Bank had a total of 92 active borrowers.

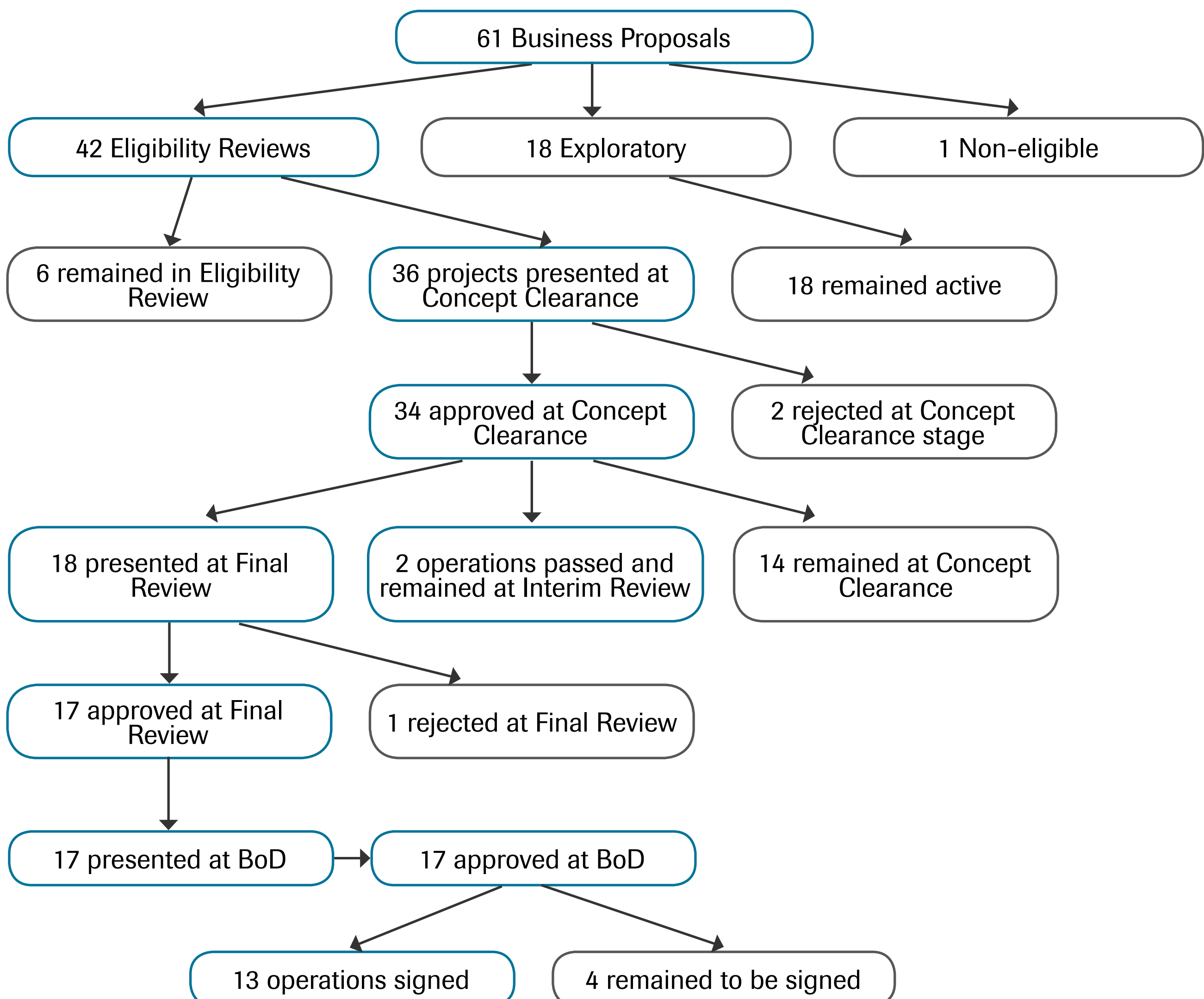
During 2011, the Bank evaluated 61 business proposals, which went through different phases of the operations' cycle. Of these, 17 went through the entire operations cycle and received BoD approval, along with 13 other operations which were identified and went through various phases of the operations cycle in 2010. 16 operations continued the appraisal process. Of the operations identified in 2011, 3 operations completed the internal appraisal and approval cycle and were expected to be submitted for BoD approval, while 4 already approved operations were expected to be signed in 2012.

In terms of concentration, the top 10 exposures represent 41% of the total outstanding amount, and the next 10 largest exposures account for an additional 24% of the total outstanding amount.

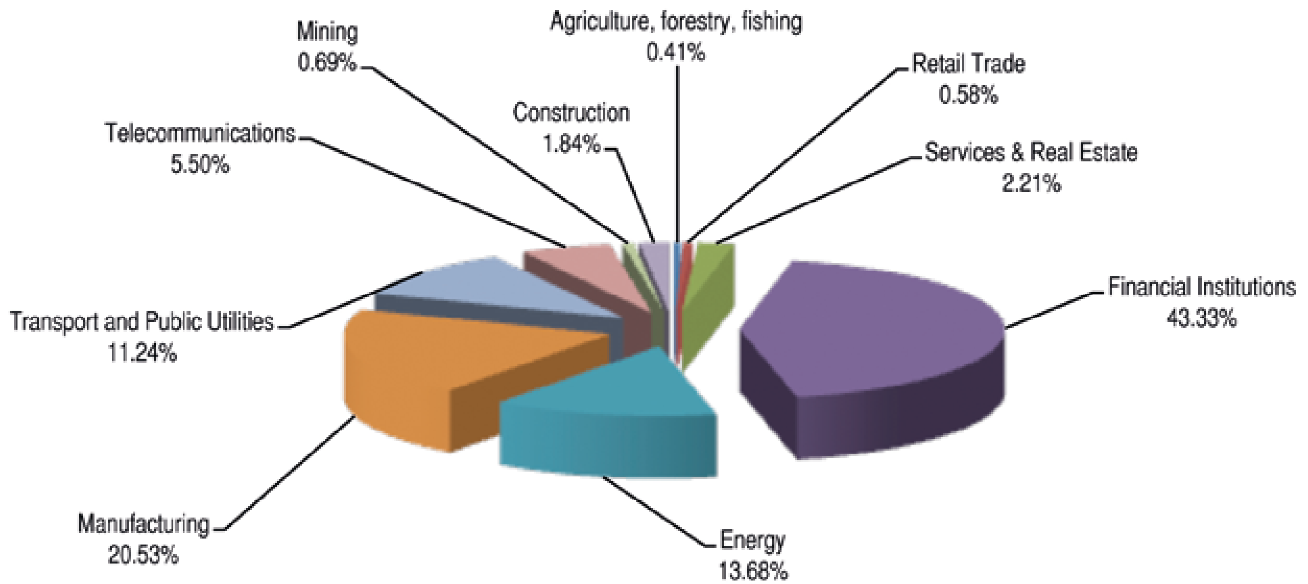
Exposure to the Financial Institutions sector comprised 43% of total loans outstanding. Exposure has historically been high due to the fact that BSTDB used financial institutions for a variety of purposes, including direct lending, SME and mortgage lines of credit and trade finance. The other major sectoral exposure in the outstanding portfolio was for transport and public utilities with 17.3%, energy accounting for 12.4%, and manufacturing with 11.8% of total outstanding amounts.

Developments are graphically exemplified by the following structure:

Pipeline Evolution for Projects Registered in the year of 2011



Signed operations by sector 1999–2011



Selected BSTDB Financings in 2011

Köprübaşi Hydroelectric Power Plant, Turkey

BSTDB provided a long term loan to Yüksel Enerji Elektrik Üretim ve Ticaret A.Ş. to finance the construction and operation of the 74MW Köprübaşi Hydroelectric Power Plant in the province of Bolu in Turkey. The project represents a total investment of USD 51 million, co-financed by BSTDB and DEG.

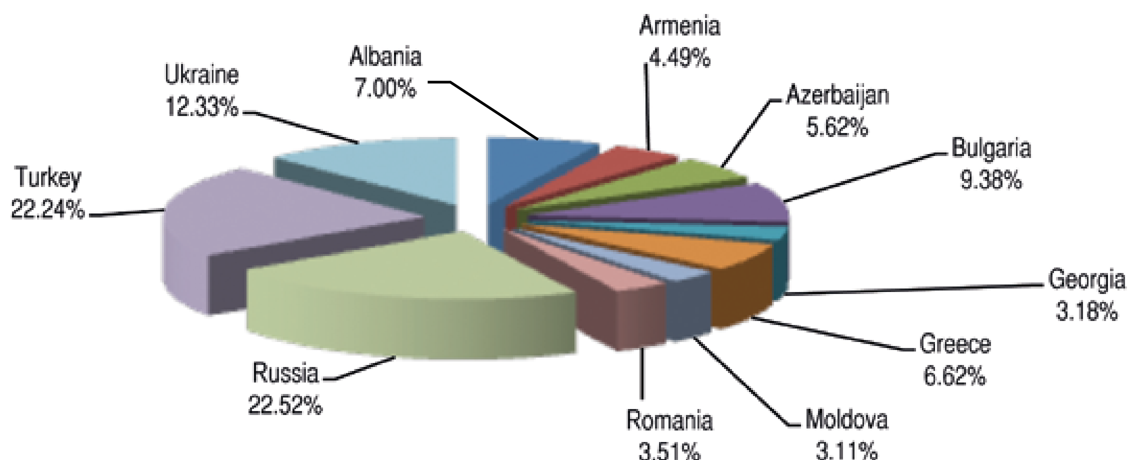
The operation has a high developmental impact as it facilitates development of the energy sector in Turkey and creates new employment in the country. The project mobilizes funding from outside the Black Sea region and exploits co-financing opportunities between BSTDB and DEG.

BSTDB Amount	USD 14 million
Total operation cost	USD 51 million
Type of financing	Project finance loan
Maturity	6 years

The structure of the Bank's active portfolio[8] by country and by sector is as follows:

Outstanding Operations by Country

As of end-2011, the outstanding operations of the Bank (cumulative disbursements less repayments for active operations) represented EUR 720 million, distributed by country as depicted in the following graph:



Source: BSTDB

Selected BSTDB Financings in 2011

Euphoria Mountain Resort Complex, Bulgaria

BSTDB provided a long-term secured loan of EUR 7.5 million to Icon Euphoria EOOD, owned by Icon EOOD, Bulgaria, which is a wholly owned subsidiary of GEK Terna Group, Greece.

GEK Terna Group is a conglomerate of companies with diversified commercial activities. Major business segments of the Group's operations include: construction, production of electricity from renewable sources of energy, real estate development, manufacturing industry, concessions, etc.

Icon Euphoria EOOD, Bulgaria, is a special purpose company established for developing the Borovets Euphoria Club, a mountain resort complex comprising a hotel, an apartment-hotel and villas. The project is located in the renowned Borovets ski resort, one of the most popular mountain resorts, situated approximately 70 km southeast of Sofia.

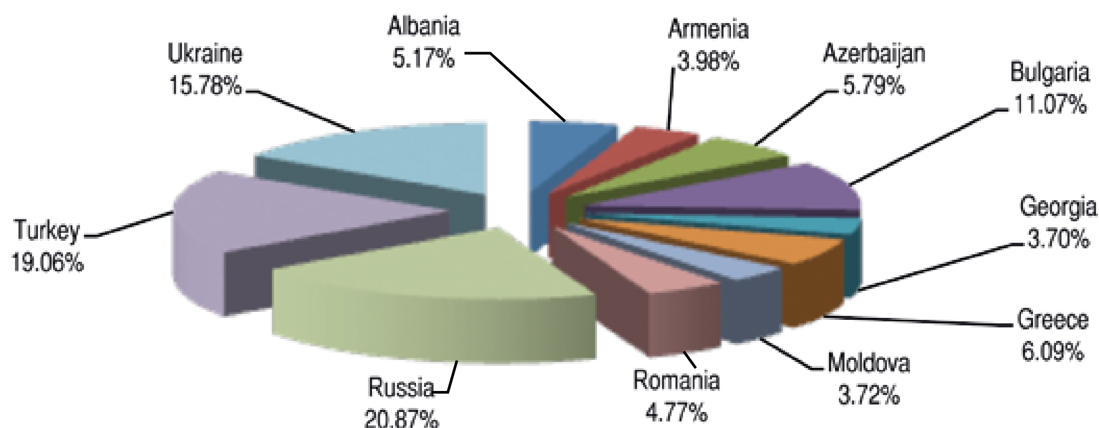
The Borovets Euphoria Club is being constructed on a total land plot area of approximately 15,000 sq.m. The hotel will be managed by Aegis S.A., a Greek company specialized in hotel development and management.

The project will contribute to the upgrading of the tourism infrastructure in Bulgaria and is expected to have a positive employment effect.

BSTDB Amount	EUR 7.5 million
Total operation cost	EUR 24 million
Type of financing	Secured project finance loan
Maturity	5.5 years

8 The active operations in the Bank's portfolio are those currently in any of the phases from Board approval to full repayment (approved, signed, disbursed and in repayment).

Signed Operations by Country



Source: BSTDB

Selected BSTDB Financings in 2011

Kürüm International – Corporate Loan Facility II, Albania

In 2011, BSTDB provided a second medium-term corporate loan to Kürüm International, following up on the existing positive business relationship of the Bank with Kürüm Holding. Kürüm International was established in 1999 to expand the activities of Kürüm Group in Albania.

Kürüm International has the largest steel production facility in Albania with an annual production capacity of 550,000 tones of steel bars, manufacturing and selling a variety of hot-rolled construction iron products to clients in Albania, the EU and the Balkan region.

The repeat loan extended by BSTDB will finance the increased working capital needs of the company, after the completion of the investment program for modernization and maintenance of existing production facilities in Albania.

As planned, the completed investment program financed by DEG and Reiffeisen together with BSTDB back in 2008, led to improved production capacity, modernization and automation of existing facilities in Albania, and increased quality for higher value-added products and cost reduction.

Amount	EUR 20 million
Type of financing	Secured corporate loan
Maturity	3 years

Outstanding Operations by Sector

As of end-2011, the outstanding operations by sector were comprised of: 59 operations through financial institutions for EUR 322.3 million, 11 operations in energy for EUR 89.5 million, 8 operations in manufacturing for EUR 84.8 million, 8 operations in transport and public utilities for EUR 124.3 million, 4 operations in telecommunications for EUR 40 million, 4 operations in construction for EUR 32.7 million, 4 operations in services and real estate for EUR 20.4 million, and 3 operations in the retail trade for EUR 6.4 million.

The portfolio structure by sector shows good diversification. The number of operations in sectors with high development impact has increased. A large share of total portfolio in the financial sector is represented by trade finance and SME credit lines extended through financial intermediaries.

Selected BSTDB Financings in 2011

Abrau Durso, Russia

A EUR 25 million secured senior corporate loan was provided by BSTDB to OAO Abrau Durso, Russia for financing the capital expenditures program of the company. The investments will include the upgrade and extension of the borrower-controlled sparkling wine production facilities in Abrau Durso as well as construction and operation of an all-season 4-star high standard hotel located in the vicinity of Lake Abrau (Krasnodar Region, South of Russia).

Abrau Durso is a famous Russian sparkling wine producer.

BSTDB's financing will contribute to the economic growth in Russia via the development of regional tourism and extensive job creation.

BSTDB Amount	EUR 25 million
Total operation cost	EUR 75.9 million
Type of financing	Secured corporate loan
Maturity	7 years

Co-Financing

The Bank values its cooperation with other financiers which enables it to mobilize investment in the Black Sea region and to realize cross-country operations. Such operations possess high shareholder value for the Bank and are therefore priority activities.

In the course of 2011, 19.54% of signed portfolio was co-financing. In terms of total signed active portfolio in the amount of EUR 1.1 billion, 40.40% of operations are co-financing. The share of co-financed active operations to total active outstanding portfolio is 46.00%.

In 2011 the Bank co-financed the following operations:

1. Koprubasi Hydroelectric Power Plant in Turkey with EUR 11 million for a total amount of EUR 39 million with DEG and equity holders

2. Galnaftogaz III in Ukraine with EUR 23 million for a total amount of EUR 162 million with EBRD and IFC.

3. Equity to ADM CEECAT Recovery Fund in Albania, Armenia, Azerbaijan, Bulgaria, Georgia, Moldova, Romania, Russia, Turkey and Ukraine with EUR 15 million for a total amount of EUR 186 million with EBRD, IFC, commercial banks and equity funds.

4. Europe Virgin Fund in Moldova and Ukraine with EUR 9 million for a total amount of EUR 56 million with EBRD, Dragon Capital, SIFEM, and others.

Selected BSTDB Financings in 2011

ADM CEECAT Recovery Fund, Regional

BSTDB has committed EUR 15 million to ADM CEECAT Recovery fund, a EUR 265,375,000 private equity fund which covers, among others, all BSTDB member countries except Greece, with initial focus on Bulgaria, Russia, Turkey and Ukraine.

The Fund's investments focus on rehabilitating operationally strong but financially distressed companies via debt restructuring, rescheduling, refinancing and debt-equity swaps. It will also fund growth opportunities where alternative sources of capital are not available, with loans and equity investments in the range of EUR 10–30 million. Other investors in the Fund include EBRD, IFC, EIF and FMO.

The Fund is expected to have high developmental impact by investing mainly in distressed companies with the aim to achieve corporate recovery, giving them the opportunity to de-leverage or restructure their balance sheets and by inducing managerial and operational improvements.

The recent financial crisis in the region has created an environment where the Fund can bring significant value to a growing number of companies, including SMEs, facing difficult access to finance.

BSTDB Amount	EUR 15 million
Total operation cost	EUR 265 million
Type of financing	Equity participation
Maturity	5 years with possible extensions for up to two years

Special Funds

The Bank administers a Special Fund (the Hellenic Fund) established in July 2001 by a Contribution Agreement between the Government of the Hellenic Republic and BSTDB. The Fund was instituted with an initial amount of EUR 800,000 and was replenished with EUR 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 allocated around EUR 1,045,000 to consulting assignments since inception and out of this amount EUR 950,684 were in fact disbursed. The sectors benefiting from these funds have included manufacturing, telecoms, oil & gas, transportation, agribusiness, renewable energy, tourism and banking. These funds were distributed among nine Member States – Albania, Armenia, Bulgaria, Georgia, Greece, Moldova, Romania, Russia and Ukraine. In 2011, the Fund has financed due diligence in the tourism and renewable energy sectors for a total amount of EUR 63,788 in Bulgaria and Greece.

Selected BSTDB Financings in 2011

Galnaftogaz Corporate Loan, Ukraine

BSTDB extended a long-term loan to Public Joint Stock Company "Concern Galnaftogaz" (Galnaftogaz) to finance the expansion of its retail network. The project represents a total investment of USD 210 million, co-financed by BSTDB, IFC and EBRD. Galnaftogaz is an independent petroleum product distribution company that operates one of the largest networks of gas filling stations in Ukraine.

The project facilitates the development of the energy sector in Ukraine and contributes to the creation of new jobs. It also demonstrates synergies of development institutions in providing much needed long-term financing in Ukraine.

BSTDB Amount	USD 30 million
Total Operation cost	USD 210 million
Type of financing	Secured corporate loan
Maturity	9 years

The Bank also administers a Technical Cooperation Special Fund (the "Fund") established with the Development Bank of Austria (the "OeEB"). The OeEB contributed to the Fund an initial amount of EUR 500,000 provided by the Government of Austria as Official Development Assistance (ODA). The Fund is an untied facility offering financing for a wide range of technical assistance services related to project preparation and training needs of BSTDB clients in the countries of the Black Sea region. The Fund represents the first financial facility of this kind provided to BSTDB by a non-regional institution. All BSTDB member countries are eligible, except for Bulgaria, Greece, Romania and Russia. In 2011, the Fund has financed due diligence in the energy sector for a total amount of EUR 58,000 in Georgia.

Selected BSTDB Financings in 2011

Rehabilitation of Communal Infrastructure in the City of Batumi, Georgia

BSTDB provided an unfunded risk participation under the loan facility of EUR 20 million extended by Kreditanstalt für Wiederaufbau (KfW) to the Finance Ministry of Georgia for rehabilitation of the municipal infrastructure in Batumi and the surrounding villages. The project involves rehabilitation of the water distribution network and the wastewater system including installation of a wastewater treatment plant.

The project will contribute to the Georgian socio-economic development. It will ensure a 24-hour supply of hygienically sound water to the people and treatment of wastewater. It reflects the BSTDB development objectives in the region and the successful joint efforts between BSTDB, KfW and the Government aimed at improving living standards for the people of Georgia.

BSTDB Amount	EUR 16 million
Total Operation cost	EUR 44 million
Type of financing	Unfunded risk participation
Maturity	15 years

SME Finance in 2011

BSTDB gives strong emphasis to supporting the small and medium sized enterprises (SMEs). This sector is crucial for developing a vibrant private economy and for employment creation. BSTDB makes financing available to SMEs by selecting appropriate financial intermediaries for delivering financing products to SMEs in the countries of operation. These financial intermediaries can be commercial banks, non-bank financial institutions such as leasing companies, as well as SME-focused private equity funds.

The Bank simultaneously aims to be additional and complementary to other financiers, in order to maximize the development impact of its operations.

Below is a list of financial intermediaries who received financing for SMEs development during 2011:

ACBA, Armenia

Amount: USD 10 million w
Type of financing: SME finance credit line
Maturity: 5 years

Armeconombank, Armenia

Amount: USD 5 million
Type of financing: SME finance credit line
Maturity: 5 years

BM Leasing, Bulgaria

Amount: EUR 3 million
Type of financing: Credit line for SME leasing
Maturity: 5 years

Bulgarian Development Bank, Bulgaria

Amount: EUR 31 million
Type of financing: SME finance credit line
Maturity: 5 years

Credit Bank of Moscow, Russia

Amount: USD 30 million
Type of financing: SME finance credit line
Maturity: 6 years

Demirbank, Azerbaijan

Amount: USD 15 million
Type of financing: SME finance credit line
Maturity: 5 years

Europe Virgin Fund, Regional

Amount: up to USD 12 million
Type of financing: Equity participation
Maturity: 8 years

Europlan, Russia

Amount: USD 20 million
Type of financing: Credit line for SME leasing
Maturity: 5 years

MAIB Leasing, Moldova

Amount: EUR 4 million
Type of financing: Credit line for SME leasing
Maturity: 5 years

Moldindconbank, Moldova

Amount: USD 10 million
Type of financing: SME finance credit line
Maturity: 5 years

NBD Bank, Russia

Amount: USD 5 million
Type of financing: SME finance credit line
Maturity: 5 years

Rosevrobank, Russia

Amount: USD 20 million
Type of financing: SME finance credit line
Maturity: 4 years

TBC Bank, Georgia

Amount: USD 10 million
Type of financing: SME finance credit line
Maturity: 3 years

Trade Finance Program for the Region in 2011

Cartu Bank, Georgia

Amount: USD 3 million
Type of financing: Revolving trade finance facility
Maturity: 360 days

TBC Bank, Georgia

Amount: USD 5 million
Type of financing: Revolving trade finance facility
Maturity: 360 days

Turan Bank, Azerbaijan

Amount: USD 4 million
Type of financing: Revolving trade finance facility
Maturity: 360 days

Environment Protection

In 2011 BSTDB continued to play an important role in promoting environmentally sound and sustainable development in all its financing activities in the Black Sea region. The Bank favored operations with a strong environmental impact, which apply cleaner technologies and energy efficiency, use of renewable resources, waste reduction and resource recovery and recycling.

One such operation was co-financing the 74 MW Koprubashi Hydroelectric Power Plant (HEPP) in Turkey, where specific attention was paid to such issues as pollution prevention and abatement, labor and working conditions of the workforce involved, local communities' health, safety and security, land acquisition and involuntary resettlement, biodiversity conservation, and sustainable natural resources management. As a result in addition to such obvious positive impacts as generation of energy from non-polluting and renewable source, the project also increased the flood security of the downstream communities, as well as offered employment opportunities for the local communities during the construction and operation stage of Koprubasi HEPP.

Another important operation was repeat financing of Kurum Metallurgical Complex in Albania where significant efforts were made in order to further reduce the negative environmental and social impacts that historically were associated with the industry in the town of Elbasan. These efforts were aimed specifically at increasing the environmental performance of the Plant's metal scrap processing, the Meltshop, the rolling mills, the lime calcination plant, as well as the general environmental management of the plant.

Financing of Galnaftogaz – one of Ukraine's leading players in distribution of oil products is just another example where BSTDB and the Borrower jointly managed to work closely in implementing efficient pollution control, including preventive and mitigation measures. Altogether this led to a further reduction in environmental, health and safety impacts resulting from its gas stations and distribution networks.

BSTDB's unfunded risk participation in the rehabilitation of the Batumi water supply and wastewater infrastructure project in Georgia will also result in significant positive impacts on public health, quality of water supply and sewer service. Further, it is expected to reduce water losses in the network, reduce energy use, decrease the pollution load on the Black Sea coastal environment, as well as benefit tourism, fishing and general socio-economic development of the region.

The year 2011 was also notable for the Bank in terms of cooperation with its counterparts in the area of development finance and the common efforts these institutions put together in order to harmonize their environmental requirements. To emphasize its commitment to this harmonization process, the Bank hosted the Multilateral Financial Institutions (MFI) Working Group on Environment, in Thessaloniki, which proved to be a very lucrative platform for fostering cooperation among the MFIs and addressed such issues as policy developments, ecosystem services, climate change and harmonization, challenges in small-scale hydropower projects, sustainability reporting, risk management and climate change adaptation.

Use of Resources

Resources Management

Human Resources

BSTDB recognizes that human resources are a key factor in the success of the institution and strives to maintain its status as a competitive employer by following the best international standards and practices.

HR development

In 2011, the BSTDB continued implementing the HR Reform, supporting the achievement of the institutional goals as set out in the BSTDB Strategy. The development of HR policies has improved, for example, recruitment and appointment, and benefits and allowances. New systems were introduced which benefited the management of human resources.

Staffing and recruitment

The BSTDB conducts recruitment on a wide geographical basis, with preference given to the citizens of the Member States. At the end of 2011, the BSTDB had a total of 101 employees, from 14 member and non-member countries.

Staff Development

The BSTDB offers learning opportunities in addressing the development needs of its staff within the context of the organization's business requirements. In 2011, the majority of these opportunities focused on the further development of professional and technical skills of the staff. Emphasis was placed on reflecting the organization's business needs in staff development. Efforts and resources were especially concentrated on the development of new processes, and the streamlining of existing ones.

Staff Benefit System

The BSTDB operates a market-oriented staff compensation and benefits system designed to match the employment standards of other International Financial Institutions.

The BSTDB medical, life and temporary incapacity/ long-term disability insurance plan provides adequate coverage emphasizing preventive medical care. The BSTDB also offers an optional post-separation medical coverage.

The BSTDB pension plan, launched in January 2003, is comprised of a fully funded defined benefit scheme and a matched defined contribution component. This combination offers the flexibility crucial for best meeting the needs of a multi-national work force. In 2011, an increase of the maximum contribution rate to the defined contribution component was approved.

Information Technologies

The IT work program for year 2011 was well aligned with the institutions strategic plan. The mission of the IT department is to efficiently manage IT costs and ensure budgeting discipline, while contributing to staff productivity by introducing innovative IT solutions which could add value to the organization. The IT Department has carried out the following initiatives in 2011:

- Upgraded its whole network infrastructure with new network switches and a 10 Gigabit Ethernet, fiber optic network backbone.
- Improved its Data Center infrastructure to be more compliant with the industry standards.
- Upgraded its backup, restore and vaulting software with the latest version of it and also implemented the Veeam backup and replication technology for its virtual environment.
- Upgraded its communication link with its Disaster Recovery Site (DRS) to a higher bandwidth to accommodate the replication of its systems and data, and installed a new dual path, fiber optic Internet feed, giving a higher bandwidth for accessing the Internet and allowing its staff to remotely access its systems.
- Upgraded the IT security systems to allow a more secure and reliable access for mobile users.
- Successfully carried out the currency changeover project in SAP.
- Upgraded its Enterprise Content Management (ECM) system to the Open Text's Extended ECM (xECM) for SAP, to better manage content in the Bank.
- Installed an archiving system based on the NetApp SnapLock solution, allowing the Bank to archive its content in a secure environment.
- Upgraded its SWIFT system and installed SWIFT in its DRS location.

External Relations and Communications

In 2011, the Bank's external relations and communications activities focused on supporting the implementation of the new BSTDB Medium-Term Strategy and Business Plan for 2011–2014.

Between February and April 2011, the Bank completed missions to the member countries in order to prepare individual country strategies aligned to the corporate operational directions and targets, while taking into account needs and priorities of the shareholders. Constructive meetings held with national economic and investment policy makers, as well as with business communities and media, considerably increased the awareness of the Bank's development activities and strategy in the member countries. The Bank's country strategies for all member states for the period 2011–2014, prepared as a result of those missions, have been approved and have become operational.

With a view to enhancing its operational coverage to all countries of the Black Sea region, BSTDB maintained a dialogue with the Government of the Republic of Serbia on the prospects of its membership in BSTDB.

Institutional relations with other international financial institutions and other development banks active in the region have been strengthened, with the aim of improving synergies, as well as attracting additional resources for projects in the member countries against a background of lingering economic uncertainties and limited access to financing in the region. In 2011, the Bank signed three loan agreements with its Observer institutions – KfW, Nordic Investment Bank and Proparco (France) in the total amount of EUR 100 million aimed at investing in the BSTDB member countries to support projects in renewable energy and energy efficiency, social infrastructure, agribusiness and small business development.

While maintaining the established institutional relations with Observer institutions, the Bank continued to attract other IFIs to coordinate and develop joint business activities in the Black Sea region. In June 2011, BSTDB granted the Observer Status to the European Bank for Reconstruction and Development. In September, Vnesheconombank of Russia became the first national development bank from a member country to obtain Observer Status, thus bringing the number of BSTDB Observer institutions to ten.

On the occasion of its Annual Meeting in Tirana in June 2011, the Bank organized a Business Forum "Albania: Working together to Promote Development Opportunities". The discussion focused on the national economic policy priorities and challenges and the role of the financial sector in the country's development. Representatives of EIB, EBRD, the World Bank Group, KfW, the Austrian Development Bank and Proparco presented their strategies for Albania and explored opportunities for coordinated investment activities in the country.

In September, BSTDB co-hosted a Roundtable Discussion titled "Development Banks: Their Role in the Growth Agenda" with the Greek Ministry for Development on the occasion of the Thessaloniki International Fair. BSTDB, EIB, Austrian Development Bank, Bulgarian Development Bank, Croatian Bank for Reconstruction and Development, China Development Bank and KfW of Germany exchanged views on policy approaches to development finance and debated how multilateral and national development institutions can improve synergies. The discussion gathered over 100 participants, including Greek government officials, members of parliament, bankers and businessmen, as well as diplomatic corps and the media.

In May, the Bank sponsored the South-Eastern Europe and the Mediterranean Public Private Partnership (PPP) Forum jointly organized by the Greek Ministry of Regional Development and Competitiveness and the World Bank Institute. The event highlighted the opportunities for development and growth presented by well designed PPP programs, underlined the importance of a sound legal and regulatory environment as a pre-condition for transparency and competition, and offered useful insights on current developments in structuring and financing PPP projects.

The Bank cooperated with Ubifrance, a French business promotion organization, in arranging for a presentation of investment and trade opportunities in the region for the interested French companies in Thessaloniki.

BSTDB maintained contacts and information exchange with European bilateral development finance institutions in the framework of EDFI Interact Group.

BSTDB participated in the preparation of a report on "International Finance Institutions and Development through the Private Sector",

which was launched by 31 international finance institutions (IFIs) during the World Bank–IMF Annual Meetings in Washington in September 2011. The report finds that international finance institutions play a key role in catalyzing job creation and growth through the private sector in emerging markets, particularly as governments face increased pressure on public resources. Joining forces with other IFIs, the Bank is diversifying its support for private sector development, particularly for small and medium-sized businesses in the countries of the Black Sea region.

BSTDB was among 25 development finance institutions which adopted the Corporate Governance Development Framework, a common set of guidelines to support sustainable economic development in emerging markets, in September 2011. Good corporate governance helps businesses operate more efficiently, attract capital, and safeguard against corruption and mismanagement. It makes businesses more accountable and transparent and builds investor confidence in public and private companies in developing countries. BSTDB is among the nine members of the DFI Corporate Governance Working Group.

In the framework of cooperation and harmonization initiatives with other Multilateral Development Banks (MDBs), BSTDB participated actively in the consultations of the Heads of Procurement Group (HOP) of the MDBs, under whose auspices BSTDB and the World Bank co-chaired the HOP PPP working group and co-authored a harmonized note on "Procurement and PPP Transactions Guidance for MDB Public Sector Engagements".

Enhanced cooperation with the Organization of the Black Sea Economic Cooperation (BSEC) and its family institutions remained an important priority. The Bank intensified its collaboration with BSEC Business Council and Parliamentary Assembly of BSEC. The Bank maintained its involvement in the activities of BSEC working groups dealing with the preparation of the Black Sea Ring Highway and Motorways of the Sea projects initiated by BSEC.

The Bank continued cooperation with the International Road Transport Union (IRU) on the promotion of its Model Highway Initiative for the Black Sea region, which involves several BSTDB member-countries, with a view of upgrading the infrastructure along key motorways of regional importance, including border crossing facilities, gas-filling stations, etc. The Bank is exploring opportunities for its involvement in financing a pre-feasibility study for the project, while promoting the initiative with other IFIs and potential international investors.

BSTDB cooperation with the European Commission and EU institutions was continued on a regular basis in the framework of the MOUs signed with the EC and IFIs on cooperation in the new EU member states, candidate and potential candidate, as well as EU accession countries.

In 2011, BSTDB renewed its membership of the Institute of International Finance (Washington).

Financial Management

Business Volume

In 2011, the Bank's total assets stood at EUR 836,831 thousand at the end of the year against EUR 808,100 thousand at end 2010. The size of the Bank's outstanding loan and equity portfolios were EUR 720,391 thousand compared to EUR 672,900 thousand in the previous year. Funds committed but not yet disbursed stood at EUR 171,967 thousand.

Revenues

Total income from lending activities increased to EUR 35,584 thousand for the year, from EUR 33,946 thousand in 2010. Treasury activities in 2011 generated total income of EUR 5,256 thousand from its available for sale and held to maturity portfolios. Operating income for the year was EUR 35,911 thousand compared to EUR 33,287 thousand in 2010, an increase of almost 8%. This increase derived from an increase in the Bank's business volume as indicated above.

Expenses

Interest and similar expense for the year was EUR 12,110 thousand compared to EUR 12,417 thousand in 2010. This reduction was due principally to the lower borrowing requirements as the Bank used more internal generated funds for its lending activities.

Administrative expenses, including depreciation, in 2011 were EUR 15,664 thousand, an increase of EUR 1,234 thousand over the previous year. Administrative expenses include salaries, benefits and other administrative costs.

Salaries and benefits, in the amount of EUR 10,867 thousand showed an increase of EUR 673 thousand from the previous year. This included a supplementary amount recognized in the actuarial valuation of the Bank's staff retirement plan so that the plan would be fully funded. Other administrative costs had an increase from the previous year in an amount of EUR 511 thousand.

Overall, administrative expenses were well within the 2011 Budget, reflecting the Bank's focus on budgetary discipline and effective cost controls.

Net Income

Income before impairment during the year was EUR 20,247 thousand compared to EUR 18,857 thousand in 2010, or an increase of over 7%. Total impairment losses in an amount of EUR 10,188 thousand were due to specific provision charges on a few operations, in addition to provision charges on debt investment securities held by the Bank.

The Bank posted net income of EUR 10,059 thousand for the year. The quality of the lending portfolio remained sound, experiencing only two additional loans and two equity investments impaired operations.

Capital Base

Initial Share Capital

The initial authorized share capital of the Bank was SDR 1 billion divided into one million shares having a par value of SDR 1,000 each. Member States subscribed to all of the initial authorized share capital. Each of Armenia, Georgia and Moldova voluntarily agreed to reduce its share from 2% to 1% in June 2004 leaving SDR 30 million unsubscribed. At the Board of Governors meeting in October 2008, it was decided that Azerbaijan would take up this 3% of unsubscribed shares. The additional subscription amount was fully paid in 2009.

New Share Capital

The Board of Governors decided in December 2007 to approve an increase to the Bank's authorized capital from SDR 1 billion to SDR 3 billion. They further approved an SDR 1 billion increase in the subscribed capital to be subscribed by the existing Member States, thereby increasing subscribed capital to SDR 2 billion. An announcement that this additional SDR 1 billion was fully subscribed was made after the Board of Governors meeting in October 2008. Georgia declined to take up its 1% allocation and this was taken up by Romania. Upon completion of the subscription, Greece, Russia and Turkey remained the largest shareholders of the Bank with 16.5% stake each, followed by Romania with 14%, Bulgaria and Ukraine with 13.5% each, Azerbaijan with 5%, Albania with 2%, Armenia and Moldova with 1% each, and Georgia with 0.5% stake. In October 2011, Moldova reduced its portion of the subscribed capital, from 1% to 0.5%, to which those shares were released to unallocated.

The new subscribed capital will be paid according to the following schedule:

- Payment of the paid-in portion of the new subscribed capital, equivalent to 10% of the subscribed number of shares (totalling SDR 99 million), will be paid in cash by the Member States in 2010.
- Payment of the paid-in portion of the new subscribed capital, equivalent to 20% of the subscribed number of shares (totalling SDR 198 million), will be made by each Member State in eight equal successive annual instalments between 2011 and 2018.
- Payment for the remaining callable portion of the new subscribed capital, equivalent to 70% of the shares (totalling 693 million), represents a firm commitment on the part of the Member States to pay such amount when due in conformity with the relevant provisions of the Establishing Agreement.

As of 31 December 2011, the paid in share capital was EUR 467.2 million.

The Board of Governors may also authorize additional subscriptions from the remaining SDR 1 billion of authorized capital in three instances:

- To satisfy demand for shares expressed by Member States.
- If in conformity with the provisions of Article 3 (Membership) of the Establishing Agreement, any BSEC Member State not yet member of the Bank (currently Serbia) wishes to subscribe for BSTDB shares.
- If in conformity with the provisions of Article 3 (Membership) of the Establishing Agreement, a multilateral bank or financial institution expresses a desire to become a member.

Gearing Ratio

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, which at the end of 2011 stood at about EUR 3.7 billion.

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 capital, which limits the total amount of operations at approximately EUR 2.2 billion.

Provisioning

Provisions are recorded in two ways:

- General provisioning rate applied to the entire portfolio
- Specific provisions applied against certain assets and are determined following an impairment test if evidence of credit deterioration is found during regular monitoring

Starting with 2011, BSTDB has moved to a Basel II approach to include Loss Given Default and Discount Factors for security.

At the end of 2011, total provisions for loans stood at EUR 39,843 thousand, equivalent to 5.8% of the outstanding loan portfolio. Total provisions for equity investments stood at EUR 608 thousand, equivalent to 1.9% of the outstanding equity investment portfolio. The institutional target to be achieved for general provisions and reserves, over time, is set at 10% of total outstanding exposures, less the gross value of non-performing operations.

Furthermore, total provisions for debt investment securities stood at EUR 14,171 thousand, equivalent to 9.1% of the investment securities portfolio that was held by the Bank.

Reserves and Surplus

Reserves represent the internal generation of capital through the retention of earnings. Pursuant to the Bank's financial policies, reserves are the ultimate protection of the Bank's share capital against impairment resulting from credit losses, in excess of provisions, or losses due to market, operational and compliance risks. The Bank targets a level of profitability guided by the desire to build an appropriate cushion of reserves against the risks inherent to its normal operations and subsequently to grow its capital base consistent with its financial and growth objectives.

In addition to building up a cushion of reserves, the Bank also sets aside retained income to enable it to maintain the real value of its share capital funds, and increase its investment headroom through internally generated funds.

Market Risks

Market risk management is conducted within a framework of conservative risk limits and policy documents approved by the Board of Directors.

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.

Operational Risks

The Bank, like all financial institutions, is exposed to operational risks, defined as the risk of loss resulting from inadequate or failed internal processes, people and systems, or from external events, which are risks other than those falling within the scope of credit and market risk. The definition includes legal risk but excludes strategic and reputational risk.

Appropriate measures are taken to achieve a high level of operational risk awareness and to enhance the operational risk management system. The Bank adopts market best practices and methods to manage and coordinate its operational risks. Key processes for the management of operational risk include, amongst others: (i) internal controls (e.g. the 'four eyes principle', proper segregation of duties) within its offices and departments, (ii) the establishment of disaster recovery and business continuity plans that take into account different types of plausible scenarios to which the Bank may be vulnerable, (iii) the purchase of corporate and property insurance policies to confront potential losses which may occur as a result of various events and natural disasters and (iv) the approval process of New Products to identify and assess the operational risk related to each new product, activity, process and system.

The Bank utilizes the Standardized Approach (SA) as issued by the Basel Committee to monitor operational risk incurred[1] and the adequacy of its operational risk-related capital charges (Reserves).

Should the Bank quantify the operational risk embedded in its operations, it would, with the use of SA amount to EUR 7.4 million for 2011 and EUR 7.9 million for 2010, constituting a fraction of the Bank's total reserves amount, which represents the ultimate protection of the Bank's capital against impairment resulting from credit losses in excess of provisions, or losses due to market, operational and compliance risks. There is no general accepted methodology for calculating risks associated with compliance and other "black swan" type of events.

Based on the above quantified operational risk, it is deemed that the Reserves of the Bank are adequate to cover all potential losses arising from events of an operational risk nature and because the Establishing Agreement requires the Bank to maintain reserves at a relatively high percentage of its portfolio,[2] there is no need to make supplementary allocations.

Short Term Liquidity

As indicated in the statement of cash flows, the Bank's short term liquidity totalling EUR 126,209 thousand as of 31 December 2011 was invested in two types of money market instruments:

- Short-term deposits with institutions long term rated at a minimum of A2/A either Moody's or Standard & Poor's credit rating agency.
- Euro commercial paper rated at a minimum short term A1/P1 by either Moody's or Standard & Poor's credit rating agency.

Investments are primarily denominated in EUR or USD currencies and performance is monitored monthly against the Merrill Lynch 3 month Libid index.

The Banks liquidity ratio calculated as liquid assets over 12 months net cash requirements including signed undisbursed commitments, stood at 93% on 31 December 2011.

[1] International Convergence of Capital Measurement and Capital Standards, a Revised Framework, June 2004.

[2] 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%) percent of the subscribed capital including all paid, unpaid but payable, unpaid but callable capital. (Art. 36 – Allocation of Net Income).

Borrowings

As of end 2011, the Bank had issued a bond for USD 125,000 thousand and had signed loan agreements equivalent to EUR 148,923 thousand and USD 146,926 thousand. As the size of the Bank's operation portfolios continue to increase, and taking into consideration its minimum liquidity requirements, the Bank will access sources of long term funds in 2012.

The Bank has a long term investment grade credit rating from Standard and Poor's Investor Service of A and a short term rating of A1. The Bank also has a long term rating of A3 and a short term rating of P2, from Moody's Investor Service.

Risk Analysis

An independent financial analysis is performed for each of the Bank's operations. Corporate entities are initially subject to an assessment of creditworthiness based on historical financial statements. This is followed by cash flow 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 either public or private sector borrowers, it normally requires certain guarantees and, in all cases, ensures that the parties involved share risks in a reasonable manner.

Evaluation

The Bank conducts assessments of completed and current 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, a Board of Directors, a President, Vice Presidents, a Secretary General and such officers and staff, as may be necessary.

Each of the Member States of the Bank is represented on the Board of Governors. All powers of the Bank are vested in the Board of Governors. With certain exceptions the Board of Governors has delegated the exercise of these powers to the Board of Directors, while still retaining overall authority.

The Board of Directors, 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 Board of Directors. The composition of the Audit Committee is three Board of Director 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 Board of Directors. The President is appointed by the Board of Governors.

The Management Committee comprises of the President (as Chairman), 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 Board of Directors on the recommendation of the President.

Compliance

The Compliance function of the Compliance and Operational Risk Management Office of the Bank assists Management in managing effectively the compliance risks faced by the Bank. To this end, it identifies, assesses, advises on, monitors and reports accordingly on the Bank's compliance risk.

With regard to the financing operations, anti-fraud, corruption, money laundering and terrorism financing due diligence is – among other types of due diligence – integrated into the Bank's normal approval of new business and into the monitoring of existing activity. The Bank screens all transactions to ensure that they do not represent such risks. The Head of the Compliance function advised the business groups, upon their request, inter alia, on the Customer Due Diligence process and integrity issues.

Within 2011 the Bank's Anti-Fraud, Corruption, Money Laundering and Terrorism Financing Policy together with the Know-Your-Customer Procedures were revised, reflecting international and International Financial Institutions' standards.

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 in compliance with 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 Establishing 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.

In its financial reporting, the Bank aims to provide appropriate information on risk and performance. Industry best practice guides the evolving disclosure practice both in public financial reports and management information reporting.

Internal Audit

Internal Audit is an independent, objective, assurance, and consulting activity that examines and evaluates the activities of the Bank as a service to management and the Board of Directors (primarily through its Audit Committee). The Audit Committee has the responsibility, inter alia, of satisfying itself that the internal audit process is adequate and efficient through reviewing the policy, the scope, the work program and the reporting relating to the Bank's internal audit.

According to the Bank's Internal Audit Charter, the internal Audit Department's main objective is to help Management and the Board of Directors discharge their responsibilities and accomplish the objectives of the Bank by bringing a systematic, disciplined approach to evaluate and improve effectiveness of risk management, control, and governance processes. The Internal Audit's mission is to foster an environment of continuous improvement in controls and risk awareness.

Enterprise Risk Management

Recognizing the need for effective internal controls and acknowledging that Enterprise Risk Management (ERM), including internal controls over financial reporting, is a fundamental approach for the management of an organization, the Bank has established a functioning, consolidated and on-going Enterprise Risk Management system. This system includes certification in the Annual Report as to the effectiveness of internal controls over external financial reporting, using the standards and practices prescribed by the Committee of Sponsoring Organizations of the Treadway Commission (COSO), Internal Control Framework and Enterprise Risk Management.

Upon the overall assessment of the effectiveness of internal controls over financial reporting, coordinated by the Internal Audit Department and a Working Group with representatives of all the Divisions of the Bank, an annual certification statement is issued, signed by the President and the Vice President Finance and subject to review and an attestation of the Bank's external auditors.

The external auditors review and offer their opinion on Management's assertion as to the effectiveness of internal controls over financial reporting.

External Auditors

The External Auditors are appointed by the Board of Governors upon the recommendation of the Board of Directors. They are qualified outside auditors of international reputation and appointed for a term of one year, renewable further on such terms and conditions as approved by the Board of Directors.

The External Auditors' services are limited only to audit related services, but may be subject to certain exceptions that are in the interest of the Bank. The performances and independence of the External Auditors are assessed by the Audit Committee.

In addition, the External Auditors review and offer their opinion on management's assertion as to the effectiveness of internal controls over financial reporting. This opinion is given as a separate report to the audit opinion. At the conclusion of their annual audit, the External Auditors prepare a management letter for the Board of Directors, which is reviewed in detail and discussed with the Audit Committee, setting out the External Auditor's views and Management's response on the effectiveness and efficiency of internal controls and other matters.

Management's Attestation and Independent Auditor's Report

Internal Control over External Financial Reporting

Responsibility for external financial reporting

Management's responsibility

Management's report regarding the effectiveness of internal control over external financial reporting.

The management of the Black Sea Trade and Development Bank ("the Bank") is responsible for the preparation, integrity, and fair presentation of its published financial statements and all other information presented in this report. The financial statements have been prepared in accordance with International Financial Reporting Standards (IFRS) issued by the International Accounting Standards Board.

The financial statements have been audited by an independent accounting firm, which has been given unrestricted access to all financial records and related data, including minutes of all meetings of the Board of Directors and committees of the Board. Management believes that all representations made to the external auditors during their audit were valid and appropriate. The external auditors' report accompanies the audited financial statements.

Management is responsible for establishing and maintaining effective internal controls over external financial reporting for financial presentations in conformity with IFRS. The system of internal control contains monitoring mechanisms, and actions are taken to correct deficiencies identified. Management believes that internal controls for external financial reporting, which are subject to scrutiny and testing by management and internal audit, and are revised as considered necessary, support the integrity and reliability of the financial statements.

There are inherent limitations in the effectiveness of any system of internal controls, including the possibility of human error and the circumvention of overriding controls. Accordingly, even an effective internal controls system can provide only reasonable assurance with respect to financial statements. Furthermore, the effectiveness of an internal controls system can change with circumstances.

The Bank's Board of Directors has appointed an Audit Committee, which assists the Board in its responsibility to ensure the soundness of the Bank's accounting practices and the effective implementation of the internal controls that management has established relating to finance and accounting matters. The Audit Committee is comprised entirely of members of the Board of Directors. The Audit Committee meets periodically with management in order to review and monitor the financial, accounting and auditing procedures of the Bank and related financial reports. The external auditors and the internal auditors regularly meet with the Audit Committee, with and without other members of management being present, to discuss the adequacy of internal control over financial reporting and any other matters which they believe should be brought to the attention of the Audit Committee.

The Bank has assessed its internal control over external financial reporting for 2011. The Bank's assessment was based on the criteria for effective internal controls over financial reporting described in the "Internal Control – Integrated Framework" issued by the Committee of Sponsoring Organisations of the Treadway Commission (COSO). Based upon this assessment, management asserts that, on 31 December 2011, the Bank maintained effective internal control over its financial reporting as contained in the Financial Statements for 2011.

The Bank's external auditors have provided an audit opinion on the fairness of the financial statements presented within this report. In addition, they have issued an attestation report on management's assessment of the Bank's internal control over financial reporting, as set out on page 46.

Andrey Kondakov
President

Valentina Siclovan
Vice President Finance

Black Sea Trade and Development Bank
Thessaloniki, Greece
27 April 2012

Report of the Independent Auditors

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

We have audited Black Sea Trade and Development Bank ("the Bank") internal control over financial reporting as of 31 December 2011 based on criteria established in "Internal Control – Integrated Framework" issued by the Committee of Sponsoring Organisations of the Treadway Commission (the COSO criteria).

The Bank's Management is responsible for maintaining effective internal controls over financial reporting, and for its assessment of the effectiveness of internal control over financial reporting included in the accompanying management's report. Our responsibility is to express an opinion on the Bank's internal control over financial reporting based on our audit.

We conducted our audit in accordance with the International Standard on Assurance Engagements (ISAE) 3000. Our audit included obtaining an understanding of internal controls over financial reporting, evaluating the management's assessment and performing such other procedures as we considered necessary in the circumstances. We believe that our work provides a reasonable basis for our opinion.

A bank's internal control over financial reporting is a process designed to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles. A bank's internal control over financial reporting include those policies and procedures that: (1) pertain to the maintenance of records that, in reasonable detail, accurately and fairly reflect the transactions and dispositions of the assets of the bank; (2) provide reasonable assurance that the transactions are recorded as necessary to permit preparation of financial statements in accordance with International Financial Reporting Standards, and that receipts and expenditures of the bank are being made only in accordance with authorisations of management and directors of the Bank; and (3) provide reasonable assurance regarding prevention or timely detection of unauthorized acquisition, use, or disposition of the bank's assets that could have a material effect on the financial statements.

Because of its inherent limitations, internal control over financial reporting may not prevent or detect misstatements. Also, projections of any evaluation of effectiveness to future periods are subject to the risk that controls may become inadequate because of changes in conditions, or that the degree of compliance with the policies and procedures may deteriorate.

In our opinion, Black Sea Trade and Development Bank maintained, in all material respects, effective internal control over financial reporting, as of 31 December 2011, based on the COSO criteria.

We have also audited, in accordance with International Standards on Auditing, the financial statements as of 31 December 2011 and the related statement of comprehensive income, statement of changes in equity and cash flow statement for the year then ended of Black Sea Trade and Development Bank and, in our report dated 16 March 2012, we have expressed an unqualified opinion.

27 April 2012

ERNST & YOUNG (HELLAS)
CERTIFIED AUDITORS ACCOUNTANTS SA
11th Km National Rd. Athens – Lamia
GR – 144 51 Metamorphosis
Athens,
Greece

Financial Statements and Notes

Financial Statements for the Year Ended
31 December 2011
Together with Auditor's Reports

INCOME STATEMENT

For the year ended 31 December 2011

Presented in thousands of EUR	Note	2011	2010
Interest and similar income	3	39,706	37,209
Interest and similar expense	4	(12,110)	(12,417)
Net interest income		**27,596**	**24,792**
Net fees and commissions	5	433	799
Dividend income	14	1,250	958
Net profit on sale of equity investments		25	2,563
Net gains from available-for-sale investments	14	4,693	3,932
Net income on foreign exchange		1,033	245
Other income (expense)	6	881	(2)
Operating income		**35,911**	**33,287**
Administrative expenses	7,24	15,266	14,082
Depreciation and amortisation	17,18	398	348
Income before impairment		**20,247**	**18,857**
Impairment (gains) losses on loans	8	(4,591)	8,550
Impairment losses on equity investments	9	608	0
Impairment losses on available-for-sale-debt securities	10	14,171	0
Net income for the year		**10,059**	**10,307**
Earnings per share basic and diluted	21	0.022	0.027

The accompanying notes are an integral part of these financial statements.

STATEMENT OF COMPREHENSIVE INCOME

For the year ended 31 December 2011

Presented in thousands of EUR	Note	2011	2010
Net income for the year		10,059	10,307
Net gains (losses) from available-for-sale financial assets	22	2,761	(5,550)
Exchange rate difference on conversion	22	(200)	0
Total comprehensive income for the year		**12,620**	**4,757**

The accompanying notes are an integral part of these financial statements.

STATEMENT OF FINANCIAL POSITION

At 31 December 2011

Presented in thousands of EUR	Note	2011	2010
Assets			
Cash and bank balances	23	11,888	85,134
Placements with financial institutions	23	0	4,528
Debt investment securities:			
Available-for-sale	10,11	26,528	57,029
Held-to-maturity	11,23	114,321	29,122
Total deposits and securities		152,737	175,813
Loans	13,15	688,218	654,746
Less: deferred income	13	(6,913)	(6,305)
Less: impairment losses on loans	8	(39,843)	(43,334)
Loans net of impairment		641,462	605,107
Equity investments: available-for-sale	9,14,15	31,565	18,154
Other assets	16	9,588	7,966
Property and equipment	17	555	288
Intangible assets	18	924	772
Total Assets		**836,831**	**808,100**
Liabilities			
Borrowings	19	268,084	298,254
Derivatives financial instruments	12	8,746	202
Payables and accrued interest	20	3,051	3,579
Total liabilities		279,881	302,035
Members' Equity			
Authorised share capital	21	3,547,897	3,486,870
Less: unallocated share capital	21	(1,198,597)	(1,162,290)
Subscribed share capital	21	2,349,300	2,324,580
Less: callable share capital	21	(1,653,115)	(1,627,206)
Less: payable share capital	21	(228,767)	(268,452)
Cumulative translation adjustment	21	(216)	0
Advance against future call	21	15	30
Paid-in share capital		467,217	428,952
Reserves	22	40,103	30,996
Retained earnings		49,630	46,117
Total members' equity		556,950	506,065
Total Liabilities and Members' Equity		**836,831**	**808,100**
Off-balance-sheet items			
Commitments	15	171,967	82,334

The accompanying notes are an integral part of these financial statements.

STATEMENT OF CHANGES IN MEMBERS' EQUITY

For the year ended 31 December 2011

Presented in thousands of EUR	Share capital			Reserves	Retained earnings	Total
	Subscribed	Callable	Payable			
At 31 December 2009	**2,177,500**	**(1,524,250)**	**(324,958)**	**29,980**	**37,417**	**395,689**
Paid-in share capital	0	0	100,665	2,198	2,761	105,624
Total comprehensive income	0	0	0	(5,550)	10,307	4,757
Cumulative translation adjustment	147,080	(102,956)	(44,124)	0	0	0
Advance against future call	0	0	(5)	0	0	(5)
General reserve	0	0	0	4,368	(4,368)	0
At 31 December 2010	**2,324,580**	**(1,627,206)**	**(268,422)**	**30,996**	**46,117**	**506,065**
Paid-in share capital	0	0	38,496	0	0	38,496
Total comprehensive income	0	0	0	2,761	9,859	12,620
Cumulative translation adjustment	24,720	(25,909)	973	0	0	(216)
Advance against future call	0	0	(15)	0	0	(15)
General reserve	0	0	0	6,346	(6,346)	0
At 31 December 2011	**2,349,300**	**(1,653,115)**	**(228,968)**	**40,103**	**49,630**	**556,950**

The accompanying notes are an integral part of these financial statements.

STATEMENT OF CASH FLOWS

For the year ended 31 December 2011

Presented in thousands of EUR	Note	2011	2010
Cash flows from operating activities			
Net income for the year		10,059	10,307
Adjustment for:			
Impairment losses		10,188	8,550
Depreciation and amortisation		398	348
Interest and similar income		(7,258)	(6,851)
Interest and similar expense		1,167	1,905
Realized gains on equity investments	14	(4,740)	(6,538)
Foreign exchange differences		(9,670)	172
Exchange rate difference on conversion		(1,041)	0
Operating income before changes in operating assets		(897)	7,893
Derivative movements		8,544	(1,110)
Increase in other assets		(1,215)	1,662
Decrease in accounts payable		210	32
Increase in deferred income		608	649
Interest and similar income received		6,851	8,746
Interest and similar expense paid		(1,905)	(1,640)
Fair value movements		(11,410)	(5,550)
Cash generated from operations		786	10,682
Proceeds from repayment of loans		246,175	384,563
Proceeds from repayment of equity investments		8,252	7,162
Proceeds from sale of equity investments		25	2,172
Funds advanced for loans		(275,387)	(378,446)
Funds advanced for equity investments		(13,563)	(5,466)
Net cash (used in) from operating activities		(33,712)	20,667
Cash flows from investing activities			
Proceeds from available-for-sale investment securities		34,312	43,475
Purchase of available-for-sale investment securities		(3,894)	(29,798)
Purchase of property, technology and equipment		(832)	(423)
Net cash from investing activities		29,586	13,254
Cash flows from financing activities			
Payments received from share capital		38,496	78,491
Decrease in advance against future call		(15)	(5)
Paid-in share capital received		38,481	78,486
Proceeds from borrowings		86,572	172,055
Repayments of borrowings		(116,742)	(292,632)
Net cash from (used in) financing activities		8,311	(42,091)
Net increase (decrease) in cash and cash equivalents		**4,185**	**(8,170)**
Cash and cash equivalents at beginning of year		122,024	130,194
Cash and cash equivalents at end of year	23	**126,209**	**122,024**

The accompanying notes are an integral part of these financial statements.

Accounting Policies

Summaries of the Bank's significant accounting policies applied in the preparation of these financial statements are presented in this section. These policies have been consistently applied to all the financial periods being presented, unless otherwise indicated.

Basis of Preparation of Financial Statements

The accompanying financial statements are a complete set of financial statements and are 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 except for those financial assets that have been measured at fair value. The Bank has not adopted any IFRS before their effective dates.

Change in Functional and Presentation Currency

The Bank changed its functional and presentation currency from the Special Drawing Right ("SDR"), as defined by the International Monetary Fund ("IMF"), component currencies to the Euro ("EUR"), as defined by the European Central Bank ("ECB"), as of 1 January 2011 under the directions of the Board of Governors decision on 5 December 2010. It was concluded that the Euro is more representative of the Bank's operations and environment as the Bank's lending operations are increasing in Euro, and the administrative expenses and capital expenditures shall be primarily denominated and settled in this currency.

Subject to this decision the Bank applied the translation procedures in accordance with IAS 21, and translated all items into the new functional currency prospectively using the exchange rate at the above date of change. The resulting translated amounts for non-monetary items are treated as their historical cost.

For comparative purposes the year ended 31 December 2010 financial statements were translated in accordance with IAS 21 using the official exchange rate published for the SDR by the IMF. As such, assets and liabilities were translated at the closing rate at the date of that financial position, and income and expenses were translated at rates that approximated the exchange rates at the dates of the transactions.

The Bank continues to denominate its share capital in SDR, the Bank's unit of account for its authorized capital, in accordance with Article 4 of the Establishing Agreement. The value of the SDR is based on the weighted average of the values of a basket of major international currencies. Share capital which is paid is converted into the Bank's functional currency.

Reclassified Accounts

For comparative purposes the amounts presented in the 2010 financial statements in respect of front-end fees and commitment fees are reclassified from "fees and commission income" to "interest and similar income" in the income statement using the effective interest method and the deferred income under "loans" in the statement of financial position in accordance with IAS 18. As such the prior year amounts in interest and similar income was EUR 2,932 thousand, and under loans was EUR 6,305 thousand, respectively. There was no impact on the net income of the Bank as a result of reclassification.

Foreign Currencies

Foreign currency transactions are initially recorded in EUR by applying to the foreign currency amount the exchange rate between the EUR and the foreign currency at the rate prevailing on the date of transaction. Exchange gains and losses arising from the translation of monetary assets and liabilities at the end of year exchange rates are recorded in the income statement.

As of 1 January 2011 the Bank uses the official exchange rates published for the EUR by the ECB, and uses the official exchange rate published for the SDR by the IMF for share capital instalment obligations. Exchange rates used by the Bank at the financial position date were as follows.

			31 December 2011	31 December 2010
1 EUR	=	United States dollar	1.29390	-
	=	Japanese yen	100.20000	-
	=	Pound sterling	0.83530	-
	=	Azerbaijan manta	1.01739	-
	=	Romanian lei	4.32330	-
	=	Special drawing right	0.84265	0.86037

Recognition and Derecognition of Financial Instruments

The Bank recognizes a financial asset or financial liability in its statement of financial position when, and only when, it becomes a party to the contractual rights or obligations.

The Bank derecognizes a financial asset or a portion of financial asset when, and only when, it loses control of the contractual rights that comprise the financial asset or a portion of the financial asset. The Bank derecognizes a financial liability when, and only when, a liability is extinguished, that is when the obligation specified in the contract is discharged, cancelled or expires. The evaluation of the transfer of risks and rewards of ownership precedes the evaluation of the transfer of control for derecognition transactions.

Cash and Cash Equivalents

For the purposes of the statement of cash flows, cash and cash equivalents consist of cash on hand, placements with other financial institutions and debt securities with original maturities of three months or less. These are highly liquid assets that are readily convertible to a known amount of cash and are subject to insignificant risk in value.

Financial Assets

The Bank classifies financial assets in the following categories; loans and receivables, held-to-maturity investments and available-for-sale financial assets. Their classification is determined at the time of initial recognition.

Held-to-maturity investments and available-for-sale financial assets are recognized on a trade date basis, which is the date the Bank commits to purchase or sell the asset. All loans are recognized when cash is advanced to borrowers at settlement date.

The Bank did not reclassify any non-derivative financial assets out of the fair value through profit or loss category in any particular circumstance. Nor did the Bank transfer any financial assets from the available-for-sale category to the loans and receivables category.

Loans and Receivables

Loans and receivables are non-derivative financial assets with fixed or determinable payments that are not quoted in an active market. Third party expenses, such as legal fees, incurred in securing a loan are treated as part of the cost of the transaction. Subsequently, loans are measured at amortized cost using the effective interest rate method less any provision for impairment or uncollectability. All revenues generated are reported in income.

Held-to-Maturity

Financial assets with fixed or determinable payments, and fixed maturity dates are classified as held-to-maturity when the Bank has the positive intention and ability to hold to maturity. These financial assets are measured at amortized cost using the effective interest rate method, less any impairment in value. Amortized cost is computed as the amount initially recognized including the premium or discount that may arise on the date of acquisition, as well as transaction costs. Interest arising from these investments is reported in income.

Available-for-Sale

Financial assets such as the Bank's equity investments or held bonds are classified as available-for-sale are intended to be held for an indefinite period of time, and may or may not be sold in the future. After initial recognition at cost, these financial assets are measured at fair value. The fair value of the available for sale securities that are traded in organized financial markets is determined by reference to quoted market bid prices. For those where there is no active market the fair value is determined using accepted valuation techniques.

The unrealized gains and losses that arise from fluctuations in fair value are recognized as a separate component of equity until the financial asset is sold or derecognized for any other reason or until the investment is determined to be impaired, at which time, the cumulative gain or loss previously reported in equity is included in income. Foreign exchange gains or losses and any income accrued, by using the effective interest rate method, for these assets are recognized directly in income. Dividends received are included in income.

Financial Liabilities

Financial liabilities include borrowings and other liabilities.

Borrowings

Borrowing transactions are recognized in the statement of financial position at the time the funds are transferred to the Bank. They are initially stated at cost, which comprises the fair value of the funds transferred, less any transaction costs. In instances where the Bank uses derivative instruments to hedge the fair value of borrowing transactions, such borrowings are subsequently carried in the statement of financial position at fair value where the amortized cost value is adjusted to fair value by the hedged risks, with any changes in value recognized in income. Relevant interest expenses are reported in income using the effective interest rate method.

Other Liabilities

All other liabilities that are not derivatives or designated at fair value through profit or loss are recorded at amortized cost. The amounts include accrued finance charges on borrowings and other accounts payable.

Derivatives

In the ordinary course of business, the Bank enters into various types of transactions that involve derivative financial instruments. A derivative financial instrument is a financial contract between two parties where payments are dependent upon movements in price in one or more underlying financial instruments, reference rates or indices.

Derivatives can include interest rate and cross currency swaps, forward foreign exchange contracts, interest rate future contracts, and options on interest rates and foreign currencies. Such financial instruments are initially recognized in the statement of financial position at cost and are carried as assets when fair value is positive and as liabilities when fair value is negative. Changes in fair value of derivatives are included in income. Fair values are obtained from quoted market prices, to the extent publicly available, discounted cash flows and options pricing models as appropriate.

Currently, given the market sensitivity, the Bank is only involved with foreign exchange forwards.

Impairment

An impairment loss for the Bank is the amount by which an asset's recorded carrying amount exceeds its expected recoverable amount.

Financial Assets Carried at Amortized Cost

For amounts due from loan and receivable portfolios, losses under guarantees, commitments, held-to-maturity and other investments carried at amortized cost, the Bank first assesses whether objective evidence of impairment exists individually for those that are individually significant, or collectively for those that are not individually significant. If the Bank determines that no objective evidence of impairment exists for an individually assessed asset, whether significant or not, it includes the asset in a group of assets with similar credit risk characteristics and collectively assesses them for impairment. Assets that are individually assessed for impairment and for which an impairment loss is, or continues to be, recognized are not included in a collective assessment of impairment.

The criteria that the Bank uses to determine that there is objective evidence of an impairment loss include:

- Delinquency in contractual payments of principal or interest,
- Cash flow difficulties experienced by the borrower,
- Breach of loan covenants or conditions,
- Initiation of bankruptcy proceedings,
- Deterioration in the borrower's competitive position, and
- Deterioration in the value of collateral.

If there is objective evidence that an impairment loss has been incurred, that the Bank will not be able to collect all amounts due (principal and interest) according to original contractual terms, such assets are considered and classified as "non-performing". The amount of the loss is measured as the difference between the asset's carrying amount and the present value of expected future cash flows (excluding future credit losses that have not yet been incurred). The carrying amount of such an asset is reduced to its estimated recoverable amount through the use of an allowance for impairment account and the amount of loss is recognized in income. Interest income continues to be accrued based on the original effective interest rate of the asset. The Bank ceases to accrue interest on those assets classified as non-performing for more than 90 days, or earlier when there is reasonable doubt as to actual collection, and for which the recoverable amount is determined primarily in reference to fair value of collateral.

An asset together with the associated allowance is written off when all or part of it is deemed uncollectible, liquidation or all legal and other avenues for recover or settlement are exhausted, or in the case of debt forgiveness. Write-offs are charged against previously established allowances

and reduce the principal amount of an asset. Whenever an amount of the estimated impairment loss increases because of an event occurring after the impairment was recognized, the previously recognized impairment loss is increased by adjusting the allowance account. Recoveries of such assets written off in earlier periods are included in income.

The present value of the estimated future cash flows is discounted at the asset's original effective interest rate as determined under the contract. If an asset has a variable interest rate, the discount rate for measuring any impairment loss is the current effective interest rate. The calculation of the present value of the estimated future cash flows of a collateralized asset reflects the cash flows that may result from foreclosure less costs for obtaining and selling the collateral, whether or not foreclosure is probable.

For the purpose of a collective evaluation of impairment, assets are grouped on the basis of the Bank's internal credit grading methodology that considers credit risk characteristics such as asset type, industry and geographical location. As of 31 December 2011, the Bank adopted a new basis for the purposes of collective evaluation of impairment, which was approved internally by the Credit Committee. The Bank's analysis, which was previously based on the banking systems in the BSEC countries, is currently based on the Global Emerging Markets (the "GEM") credit monitoring system. The GEM risk database standardized the data collection process and also has a common methodology adopted by many International Financial Institutions. The standardisation process used by the Bank was also reviewed independently by Moody's rating agency. The methodology and assumptions used for estimating future cash flows are reviewed regularly to reduce any difference between loss estimates and actual loss experience.

If the amount of impairment subsequently decreases due to an event occurring after a write-down, the release of the provision is credited to the provision for asset losses expense. Unwinding of the discount is treated as income and remaining provision is then reassessed.

Available-for-Sale Financial Assets

At each financial position date the Bank assesses whether there is objective evidence that a financial asset or a group of financial assets is impaired. For equity investments carried at fair value, a significant or prolong decline in the fair value below its cost is considered in determining whether the assets are impaired. If any such evidence exists, the cumulative impairment loss, which is measured as the difference between the acquisition cost and the current fair value, net of any impairment loss previously recognized in net income, is removed from reserves and included in income. Impairment losses once recognized and included in income on these equity investments carried at cost, are not reversed.

For debt securities the Bank assesses at each financial position date whether there is objective evidence of impairment. The criteria that the Bank uses to determine that there is objective evidence of an impairment loss include:

- Downgrading of the issuer below minimum eligibility levels for Treasury exposures,
- Issuer failure to pay amounts contracted under the security,
- Covenant breaches, default events and trigger level failures,
- Deterioration of credit enhancement including diminution of collateral value, and
- Legal proceedings such as bankruptcy, regulatory action or similar.

If any such evidence exists, the cumulative impairment loss measured as the difference between the acquisition cost and the current fair value is removed from reserves and included in income. If in a subsequent period the impairment indications of such securities cease to exist, related to an event after the impairment loss was recognized, that loss is reversed through income.

Non-Financial Assets

At each financial position date the Bank reviews the carrying value of the non-financial assets and assesses whether there is any indication of impairment. If such indications exist an analysis is performed to assess whether the book value of the specific assets can be recovered. The recoverable amount is the

higher amount between the net value of sale (value of sale reduced by sale expenses) and of the value in use (as calculated from the net cash flows). If the carrying value of an intangible asset exceeds its recoverable value, then an impairment loss is recorded in income.

Renegotiated Loans

When necessary, the Bank seeks to restructure loans that may involve extending the payment arrangements and the agreement of new loan conditions. Once the terms have been renegotiated, the loan is no longer considered past due.

Risk Management continuously reviews renegotiated loans to ensure that all criteria are met and that future payments are likely to occur. These loans continue to be subject to an individual or collective impairment assessment, calculated using the loan's original effective interest rate.

Financial Guarantees

Issued financial guarantees are initially recognized at their fair value, being the premium (fee) received and subsequently measured at the higher of the unamortized balance of the related fees received and deferred, and the expenditure required to settle the commitment at the financial position date. The latter is recognized when it is both probable that the guarantee will require to be settled and that the settlement amount can be reliably estimated. Financial guarantees are recognized within other financial assets and other financial liabilities.

Property and Equipment

Property and equipment 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 were as follows:

- Expenditure on leasehold buildings and improvements are depreciated over the remaining term of the lease -
- Transportation vehicles 20.0%
- Furniture and office accessories 20.0%
- Personal computers 33.3%
- Office and telecommunication equipment 20.0%

Intangible Assets

Intangible assets comprise software expenditures and other intangible assets. These assets are amortized on a straight-line basis over the best estimate of their useful lives, which is normally five years. Their carrying values are reviewed for impairment when events or changes in circumstances indicate that the carrying value may not be recoverable.

Taxation

In accordance with Article 52 of the Establishing 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.

Other Provisions

The Bank raises provisions for potential obligations and risks when the following circumstances exist (a) there is an existing legal or constructive obligation as a result of past events (b) for the obligation to be settled an outflow of resources embodying economic benefits is possible and (c) a reliable estimate of the amount of the obligation can be made.

Share Capital and Dividends

In accordance with Article 36 of the Establishing 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.

Reserves

In accordance with the Establishing Agreement of the Bank the general reserve is created from the profits of the Bank, as mentioned above for meeting any unforeseeable risks or contingencies.

The revaluation reserve represents the accumulated change in fair value of available-for-sale investments of the Bank, which have not been impaired.

Retained earnings is the accumulated undistributed and unallocated net income.

Netting of Financial Assets and Liabilities

The netting off of assets and liabilities in the financial statements is permitted if, and only if, there is a currently enforceable legal right to offset the recognized amounts and there is an intention to settle on a net basis, or to realise the asset and settle the liability simultaneously.

Revenues and Expenses

Interest income and expense are recorded in income for all interest bearing instruments on an accrual basis using the effective interest rate method based on actual contractual terms, with the exception being those assets that are individually identified as impaired for which interest is recognized through unwinding the discount arising from the present value calculations applied to the expected future cash flows. The effective interest rate method is a method of calculating the amortized cost of a financial asset or a financial liability and of allocating the interest income or interest expense over the relevant period. The effective interest rate is the rate that exactly discounts estimated future cash flows (inflows and outflows) through the expected life of the financial instrument, or when appropriate, a shorter period to the carrying amount of a financial asset or financial liability.

In accordance with IAS 18, front-end fees and where applicable commitment fees pertaining to loans are amortized through income using the effective interest rate method over the life of the loans. This calculation however, does not include costs that any other party is directly responsible for as: taxes, notary fees, insurance, registration, etc. In the case of early repayment, cancellation or acceleration the outstanding deferred income from the related fees is recalculated taking into account the new maturity date. If the commitment expires without a loan being drawn down, the related fee is recognized as income on expiry.

Other commitment and guarantee fees and fees received in respect of services provided over a period of time are recognized as income on an accrual basis matching the period during which the commitment

exists or the services are provided. Additionally, fees from negotiation, cancellation, arrangement, etc. are recognized on completion of the related transaction. Dividends are recognized when received. Administrative expenses are recorded on an accrual basis.

Staff Retirement 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. Actuarial gains and losses are recognized as income or expense when the net cumulative unrecognized actuarial gains and losses at the end of the previous reporting year exceed 10% of the higher of the defined benefit obligation and the fair value of plan assets at that date. These gains or losses are recognized over the expected average remaining working lives of the employees participating in the plan.
- 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.
- The third pillar is a defined contribution scheme funded entirely by each employee, up to 40% of basic salary.

As an alternative, local staff are 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 IKA are recognized as an expense and included in "Administrative expenses".

The Bank may offer termination benefits to employees that are terminated before the normal retirement age. These indemnities, including any related retirement benefits, are recognized in income as an expense in the same period which they are incurred.

Government Grants

Government grants are recognised where there is reasonable assurance that the grant will be received and all attaching conditions will be complied with. Grants relating to fixed asset expenditures are recognized in income on a straight-line basis over the same period as that applied for depreciation purposes. Those relating to administrative expenses are recognized in income matching with the expense incurred. The balance of grants received or receivable that has not been taken to income is carried in the statement of financial position within "Other liabilities".

Operating Leases – The Bank as a Lessee

For the Bank, an operating lease is a lease other than a finance lease. Under such agreements, all the risks and benefits of ownership are effectively retained by the lessor. The Bank has entered into this type of lease for its Headquarters building. Payments made under operating leases are charged to income on a straight-line basis over the period of the lease term. Any benefits received or that are receivable are also recognized on a straight-line basis over the lease term. When an operating lease is terminated before the lease period has expired, any payment required to be made to the lessor, by way of penalty, is recognized as an expense in the period which the termination takes place.

Use of Judgement and 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. Estimates and judgements are continually evaluated and are based on historical experience and other factors, including expectations of future events that are believed to be reasonable under the circumstances.

Consequently, the specific considerations regarding the use of management judgement in each area of estimate have been outlined in the respective accounting policy and disclosure note. The Bank's critical accounting judgements and estimates are as follows:

- Provisions for the impairment of loan operations. The Bank's method for determining the level of impairment of loan operations is described in the "impairment" accounting policy on page 56 and further explained under credit risk on page 66. Portfolio provisions for loans not individually assessed as impaired amounted to EUR 11,388 thousand as at 31 December 2011.

In determining the probabilities of default the Bank applies a collective provisioning rate on the entire loan portfolio from the GEM's database, maintained by the European Investment Bank and the International Financial Corporation. This constitutes a change from the previous year's methodology as indicated in the "impairment" accounting policy on page 56. The new calculation formula of the GEM database takes into account Basel II criteria such as loss-given default and discount factor multipliers, which resulted in a decrease of collective provisions of EUR 9,962 thousand.

On the other hand, an increase on specific provisions during the year was made for the identified impairment of EUR 5,371 thousand. Specific Provisions are assigned according to the degree of potential impairment resulting from the impairment test that is conducted on the basis of objective evidence obtained through a risk asset review process. An impairment test includes projected cash in-flows and out-flows, available for debt service until maturity, which are discounted at the effective rate to reach a net present value for a particular operation, less any collateral that can be realized. Impairment losses incurred from specific provisions are recognized to the income statement.

- Provisions for the impairment of equity investments. The Bank's method for determining impairment of equity operations is described in the "impairment" accounting policy on page 57 and further explained under credit risk on page 66. The amount of such impairment is indicated in note 10.

- Provision for impairment on debt investment securities. The Bank has impaired bonds issued by the Greek government as indicated in note 11. The Bank, as a multilateral development institution enjoys and should benefit from "preferred creditor status" in all its Member States. Accordingly, the Bank expects that in respect of the bonds issued by the Member States, the latter should meet its obligations thereunder to the Bank at maturity in full.

- Staff retirement benefits. The Bank has established a pension plan for its staff which is described in "staff retirement and termination benefits" accounting policy on page 60 and is detailed under staff retirement plan on page 90. The present value of retirement benefit obligations is sensitive to the actuarial and financial assumptions used, including the discount rate applied. At the end of each year, the Bank determines the appropriate discount rate and other assumptions to be used to determine the present value of estimated future pension obligations, based on interest rates of suitable long-term bonds and on currencies as the EUR and USD. The Bank's liability to the staff retirement plan at 31 December 2011 was EUR 841 thousand.

Actual results could differ from those estimates mentioned above, although such differences are believed not material and do not affect these financial statements.

New Accounting Standards and Interpretations of IASB

A) Changes in accounting policies and disclosures.

The accounting policies adopted are consistent with those of the previous financial year except as follows. The Bank has adopted the following new and amended IFRS and IFRIC interpretations as of 1 January 2011:

- IAS 24: Related Party Disclosures (Revised).
- IAS 32: Classification on Rights Issues (Amended).
- IFRIC 14: Prepayments of a Minimum Funding Requirement (Amended).
- IFRIC 19: Extinguishing Financial Liabilities with Equity Instruments.
- Improvements to IFRSs (May 2010).

When the adoption of the standard or interpretation had an impact on the financial statements or performance of the Bank, this impact is described below.

IAS 24: Related Party Transactions (Amendment).
The IASB issued an amendment to IAS 24 that clarifies the definitions of a related party. The new definitions emphasize a symmetrical view of related party relationships and clarifies the circumstances in which persons and key management personnel affect related party relationships of an entity. In addition, the amendment introduces an exemption from the general related party disclosure requirements for transactions with government and entities that are controlled, jointly controlled or significantly influenced by the same government as the reporting entity. The amendment is applied retrospectively.

IAS 32: Financial Instruments: Presentation (Amendment).
The IASB issued an amendment that alters the definition of a financial liability in IAS 32 to enable entities to classify rights issues and certain options or warrants as equity instruments. The amendment is applicable if the rights are given pro rata to all of the existing owners of the same class of an entity's non-derivative equity instruments, to acquire a fixed number of the entity's own equity instruments for a fixed amount in any currency. The amendment is applied retrospectively.

IFRIC 14: Prepayments of a Minimum Funding Requirement (Amendment).
The amendment removes an unintended consequence when an entity is subject to minimum funding requirements and makes an early payment of contributions to cover such requirements. The amendment permits a prepayment of future service cost by the entity to be recognized as a pension asset. The amendment is applied retrospectively. The Bank was not obligated to a minimum funding requirement from any country it operates for post-employee defined benefits and other long-term employee defined benefits. The Bank's defined benefit schemes are currently in deficit, consequently this interpretation had no impact on the financial position or performance of the Bank.

IFRIC 19: Extinguishing Financial Liabilities with Equity Instruments.
The interpretation clarifies that equity instruments issued to a creditor to extinguish a financial liability qualify as consideration paid. The equity instruments issued are measured at their fair value. In case that this cannot be reliably measured, the instruments are measured at the fair value of the liability extinguished. Any gain or loss is recognized immediately in profit or loss.

In May 2010 the IASB issued its third omnibus of amendments to its standards, primarily with a view to removing inconsistencies and clarifying wording.

- **IFRS 3:** Business Combinations. The measurement options available for non-controlling interest (NCI) were amended. Only components of NCI that constitute a present ownership interest that entitles their holder to a proportionate share of the entity's net assets in the event of liquidation should be measured at

either fair value or at the present ownership instruments' proportionate share of the acquirees' identifiable net assets. All other components are to be measured at their acquisition date fair value.
This improvement clarifies that the amendments to IFRS 7 Financial Instruments: Disclosures, IAS 32 Financial Instruments: Presentation and IAS 39 Financial Instruments: Recognition and Measurement, that eliminate the exemption for contingent consideration, do not apply to contingent consideration that arose from business combinations whose acquisition dates precede the application of IFRS 3 (as revised in 2008).
Finally, it requires an entity (in a business combination) to account for the replacement of the acquirees' share-based payment transactions (whether obliged or voluntarily), i.e., split between consideration and post combination expenses.

- **IFRS 7:** Financial Instruments: Disclosures. The amendment was intended to simplify the disclosures provided by reducing the volume of disclosures around collateral held and improving disclosures by requiring qualitative information to put the quantitative information in context.

- **IAS 1:** Presentation of Financial Statements. The amendment clarifies that an entity may present an analysis of each component of other comprehensive income either in the statement of changes in equity or in the notes to the financial statements.

- **IAS 27:** Consolidated and Separate Financial Statements. This improvement clarifies that the consequential amendments from IAS 27 made to IAS 21 The Effect of Changes in Foreign Exchange Rates, IAS 28 Investments in Associates and IAS 31 Interests in Joint Ventures apply prospectively for annual periods beginning on or after 1 July 2009 or earlier when IAS 27 is applied earlier.

- **IAS 34:** Interim Financial Reporting.This improvement requires additional disclosures for fair values and changes in classification of financial assets, as well as changes to contingent assets and liabilities in interim condensed financial statements.

- **IFRIC 13:** Customer Loyalty Programmes. This improvement clarifies that when the fair value of award credits is measured based on the value of the awards for which they could be redeemed, the amount of discounts or incentives otherwise granted to customers not participating in the award credit scheme, is to be taken into account.

B) Standards issued but not yet effective and not early adopted.

- **IFRS 7:** Financial Instruments: Disclosures (Amended) – Enhanced Derecognition Disclosure Requirements. The amendment is effective for annual periods beginning on or after 1 July 2011. The amendment requires additional disclosure about financial assets that have been transferred but not derecognized to enable the user of the financial statements to understand the relationship with those assets that have not been derecognized and their associated liabilities. In addition, the amendment requires disclosures about continuing involvement in derecognized assets to enable the user to evaluate the nature of, and risks associated with, the entity's continuing involvement in those derecognized assets. The amendment has only disclosure effects. The Bank does not expect that this amendment will have an impact on the financial position or performance of the Bank.

- **IFRS 7:** Financial Instruments: Disclosures (Amended) – Offsetting Financial Assets and Financial Liabilities. The amendment is effective for annual periods beginning on or after 1 January 2013. The amendment introduces common disclosure requirements. These disclosures would provide users with information that is useful in evaluating the effect or potential effect of netting arrangements on an entity's financial position. The amendments to IFRS 7 are to be retrospectively applied. This amendment has not yet been endorsed by the EU. The Bank is in the process of assessing the impact of the new standard on the financial position or performance of the Bank.

- **IFRS 9:** Financial Instruments – Classification and Measurement. The new standard is effective for annual periods beginning on or after 1 January 2015. IFRS 9 as issued reflects the first phase of the IASBs work on the replacement of IAS 39 and applies to classification and measurement of financial assets and financial liabilities as defined in IAS 39. Phase 1 of IFRS 9 will have a significant impact on (i) the classification and measurement of financial assets and (ii) a change in reporting for those entities that have designated financial liabilities using the FVO. In subsequent phases, the IASB will address hedge accounting and impairment of financial assets. The completion of this project is expected over the first half of 2012. Early application is permitted. This amendment has not yet been endorsed by the EU. The Bank is in the process of assessing the impact of the new standard on the financial position or performance of the Bank.

- **IFRS 10:** Consolidated Financial Statements. The new standard is effective for annual periods beginning on or after 1 January 2013. IFRS 10 replaces the portion of IAS 27 Consolidated and Separate Financial Statements that addresses the accounting for consolidated financial statements. It also includes the issues raised in SIC-12 Consolidation – Special Purpose Entities. IFRS 10 establishes a single control model that applies to all entities including special purpose entities. The changes introduced by IFRS 10 will require management to exercise significant judgment to determine which entities are controlled, and therefore, are required to be consolidated by a parent, compared with the requirements that were in IAS 27. This standard has not yet been endorsed by the EU. The Bank is in the process of assessing the impact of the new standard on the financial position or performance of the Bank.

- **IFRS 11:** Joint Arrangements. The new standard is effective for annual periods beginning on or after 1 January 2013. IFRS 11 replaces IAS 31 Interests in Joint Ventures and SIC-13 Jointly-controlled Entities – Non-monetary Contributions by Venturers. IFRS 11 removes the option to account for jointly controlled entities (JCEs) using proportionate consolidation. Instead, JCEs that meet the definition of a joint venture must be accounted for using the equity method. This standard has not yet been endorsed by the EU. The Bank is in the process of assessing the impact of the new standard on the financial position or performance of the Bank.

- **IFRS 12:** Disclosures of Involvement with Other Entities. The new standard is effective for annual periods beginning on or after 1 January 2013. IFRS 12 includes all of the disclosures that were previously in IAS 27 related to consolidated financial statements, as well as all of the disclosures that were previously included in IAS 31 and IAS 28. These disclosures relate to an entity's interests in subsidiaries, joint arrangements, associates and structured entities. A number of new disclosures are also required. This standard has not yet been endorsed by the EU. The Bank is in the process of assessing the impact of the new standard on the financial position or performance of the Bank.

- **IFRS 13:** Fair Value Measurement. The new standard is effective for annual periods beginning on or after 1 January 2013. IFRS 13 establishes a single source of guidance under IFRS for all fair value measurements. IFRS 13 does not change when an entity is required to use fair value, but rather provides guidance on how to measure fair value under IFRS when fair value is required or permitted. This standard should be applied prospectively and early adoption is permitted. This standard has not yet been endorsed by the EU. The Bank is in the process of assessing the impact of the new standard on the financial position or performance of the Bank.

- **IAS 1:** Financial Statement Presentation (Amended) – Presentation of Items of Other Comprehensive Income. The amendment is effective for annual periods beginning on or after 1 July 2012. The amendments to IAS 1 change the grouping of items presented in OCI. Items that could be reclassified (or 'recycled') to profit or loss at a future point in time (for example, upon derecognition or settlement) would be presented separately from items that will never be reclassified. The amendment affects presentation only and has no impact on the Group's financial position or performance. This standard has not yet been endorsed by the EU. The Bank is in the process of assessing the impact of the new standard on the financial position or performance of the Bank.

- **IAS 12:** Income Taxes (Amended) – Recovery of Underlying Assets. The amendment is effective for annual periods beginning on or after 1 January 2012. The amendment clarified the determination of deferred tax on investment property measured at fair value. The amendment introduces a rebuttable presumption that deferred tax on investment property measured using the fair value model in IAS 40 should be determined on the basis that its carrying amount will be recovered through sale. Furthermore, it introduces the requirement that deferred tax on non-depreciable assets that are measured using the revaluation model in IAS 16 should always be measured on a sale basis of the asset. This amendment has not yet been endorsed by the EU. The Bank does not expect that this amendment will have an impact on the financial position or performance of the Bank.

- **IAS 19:** Employee Benefits (Amended). The amendment is effective for annual periods beginning on or after 1 January 2013. The IASB has issued numerous amendments to IAS 19. These range from fundamental changes such as removing the corridor mechanism and the concept of expected returns on plan assets to simple clarifications and re-wording. Early application is permitted. This amendment has not yet been endorsed by the EU. The Bank is in the process of assessing the impact of this amendment on the financial position or performance of the Bank.

- **IAS 27:** Separate Financial Statements (Revised). The Standard is effective for annual periods beginning on or after 1 January 2013. As a consequence of the new IFRS 10 and IFRS 12, what remains of IAS 27 is limited to accounting for subsidiaries, jointly controlled entities, and associates in separate financial statements. Early application is permitted. This amendment has not yet been endorsed by the EU. The Bank is in the process of assessing the impact of this amendment on the financial position or performance of the Bank.

- **IAS 28:** Investments in Associates and Joint Ventures (Revised). The Standard is effective for annual periods beginning on or after 1 January 2013. As a consequence of the new IFRS 11 and IFRS 12, IAS 28 has been renamed IAS 28 Investments in Associates and Joint Ventures, and describes the application of the equity method to investments in joint ventures in addition to associates. Early application is permitted. This amendment has not yet been endorsed by the EU. The Bank is in the process of assessing the impact of this amendment on the financial position or performance of the Bank.

- **IAS 32:** Financial Instruments: Presentation (Amended) – Offsetting Financial Assets and Financial Liabilities. The amendment is effective for annual periods beginning on or after 1 January 2014.This amendment clarifies the meaning of "currently has a legally enforceable right to set-off" and also clarifies the application of the IAS 32 offsetting criteria to settlement systems (such as central clearing house systems) which apply gross settlement mechanisms that are not simultaneous. The amendments to IAS 32 are to be retrospectively applied. Early application is permitted. However, if an entity chooses to early adopt, it must disclose that fact and also make the disclosures required by the IFRS 7 Offsetting Financial Assets and Financial Liabilities amendments. This amendment has not yet been endorsed by the EU. The Bank is in the process of assessing the impact of this amendment on the financial position or performance of the Bank.

- **IFRIC 20:** Stripping Costs in the Production Phase of a Surface Mine. The interpretation is effective for annual periods beginning on or after 1 January 2013.This interpretation only applies to stripping costs incurred in surface mining activity during the production phase of the mine ('production stripping costs'). Costs incurred in undertaking stripping activities are considered to create two possible benefits (a) the production of inventory in the current period and/or (b) improved access to ore to be mined in a future period (stripping activity asset). Where cost cannot be specifically allocated between the inventory produced during the period and the stripping activity asset, IFRIC 20 requires an entity to use an allocation basis that is based on a relevant production measure. Early application is permitted. This interpretation has not yet been endorsed by the EU. The Bank does not expect that this interpretation will have an impact on the financial position or performance of the Bank.

Risk Management

Risk is inherent in the Bank's activities but is managed through a continuous process of identification, measurement and monitoring, and is subject to risk limits and controls. A conservative approach to risk taking together with effective risk management, are critical to the Bank's continuing operations and profitability. The Board of Directors has approved risk management policies and guidelines that are delegated to the Management of the Bank for the identification and control of risk.

The Bank's lending risk management policy documents describe the procedures for approval, management and review of lending activity exposures. The Bank's Treasury investment policy documents define the risk parameters to be observed by the Treasury in managing its exposures. The Bank is exposed to risks identified in this section.

Financial Risk

The Bank exposure to financial risk is through its financial assets and liabilities including any receivables from these financial assets. Two key aspects of financial risk are (i) credit risk and (ii) liquidity risk.

Credit Risk

The Bank is subject to credit risk, which is the risk that customers or counterparties will be unable to meet their obligations as they fall due. Credit risk arises principally from the Bank's lending activities. Regular reviews are conducted of all exposures within the lending portfolios, typically on a semi-annual basis, though exposures that are perceived to be more vulnerable to possible default are reviewed more frequently.

At each review there is (i) an assessment of whether there has been any change in the risk profile of the exposure, (ii) recommendations of actions to mitigate risk and (iii) reconfirming or adjusting the risk ratings, and for equity investments, reviewing of fair value. Where relevant, the level of collective impairment or specific provision is evaluated and reconfirmed or adjusted. Responsibility for operations considered to be in jeopardy may be transferred from the original lending department to a corporate recovery team in order to most effectively manage the restructuring and recovery process.

Provision and reserve amounts are calculated each month using the Bank's IFRS compliant methodology, which as of 31 December 2011 uses a different source of information, the GEM risk database (see section: "Impairment" of the accounting policies). The loan loss data is updated semi-annually and provides objective evidence of impairment, using separately each sector's risk profile adjusting it for current circumstances when necessary, upon which to estimate provisions for losses.

For credit risks incurred by the Bank's Treasury in its investment and hedging activities, the Board of Directors has approved policies and guidelines for the determination of counterparty and investment exposure limits. The Bank's Risk Management assigns and monitors these counterparty and issuer credit risk limits. Treasury credit risks are also reviewed on a monthly basis by the Bank's Asset and Liability Committee.

Presented in EUR (000)	At 31 December 2011	At 31 December 2010
Cash and bank balances	11,888	85,134
Placements with financial institutions	-	4,528
Investment securities	155,020	86,151
Loans	688,218	654,746
Equity investments	32,173	18,154
Other assets	9,588	7,966
On-balance-sheet	**896,887**	**856,679**
Undrawn commitments	171,967	82,334
Total	**1,068,854**	**939,013**

The table above summarizes the maximum exposure to credit risk and indicates the worst-case scenario, without taking into consideration collateral, other credit enhancements or impairment provisions.

Analysis by Rating Agency

The tables below provide an analysis of financial investments in accordance with their Moody's rating as follows:

Presented in EUR (000)	2011					
	Aaa –Aa3	A1–A3	Baa1–Baa3	Caa1–Caa3	Unrated	Total
Analysis by Moody's rating						
Cash and bank balances	11,888	-	-	-	-	11,888
Investment securities	-	114,321	21,229	19,470	-	155,020
Equity investments	-	-	-	-	32,173	32,173
At 31 December	**11,888**	**114,321**	**21,229**	**19,470**	**32,173**	**199,081**
Of which issued by						
Governments	-	-	8,680	19,470	-	28,150
Corporates	-	114,321	12,549	-	32,173	159,043
Deposits at banks	11,888	-	-	-	-	11,888
At 31 December	**11,888**	**114,321**	**21,229**	**19,470**	**32,173**	**199,081**
Of which classified as						
Available-for-sale	-	-	21,229	19,470	32,173	72,872
Held-to-maturity	-	114,321	-	-	-	114,321
Amortized cost	11,888	-	-	-	-	11,888
At 31 December	**11,888**	**114,321**	**21,229**	**19,470**	**32,173**	**199,081**

Presented in EUR (000)	2010					
	Aaa –Aa3	A1–A3	Baa1–Baa3	Caa1–Caa3	Unrated	Total
Analysis by Moody's rating						
Cash and bank balances	89,662	-	-	-	-	89,662
Investment securities	15,992	29,122	41,037	-	-	86,151
Equity investments	-	-	-	-	18,154	18,154
At 31 December	**105,654**	**29,122**	**41,037**	**0**	**18,154**	**193,967**
Of which issued by						
Governments	-	-	25,182	-	-	25,182
Corporates	15,992	29,122	15,855	-	18,154	79,123
Deposits at banks	89,662	-	-	-	-	89,662
At 31 December	**105,654**	**29,122**	**41,037**	**0**	**18,154**	**193,967**
Of which classified as						
Available-for-sale	15,992	-	41,037	-	18,154	75,183
Held-to-maturity	-	29,122	-	-	-	29,122
Amortized cost	89,662	-	-	-	-	89,662
At 31 December	**105,654**	**29,122**	**41,037**	**0**	**18,154**	**193,967**

Collateral and Credit Enhancements

The Bank mitigates credit risk by holding collateral and other credit enhancements against exposure to customers and counterparties where it believes such security is necessary. The Bank defines security as mechanisms, procedures and assets negotiated in transactions that are meant to protect it against loss in case of non-performance. Security includes, but is not limited to, material assets, financial instruments, covenants and comfort letters.

- Loans and advances. The Board of Directors' approved guidelines for taking security under lending operations sets the amounts and types of collateral and other credit enhancements. The main types of collateral that may be obtained by the Bank are: mortgages on properties and equipment, pledges of equity shares and investment instruments, assignment of rights on certain contracts, cash or blocked deposits and other third party guarantees. When needed the Bank reassesses the change in the market value of collateral and, if necessary, requests the pledging of additional collateral in accordance with the relevant agreement.

- Other financial instruments. Collateral held as security for financial assets other than loans and advances is determined by the nature of the instrument. Investment securities, treasury bills and other eligible bills are generally unsecured.

Liquidity Risk

Liquidity risk concerns the ability of the Bank to fulfil its financial obligations as they become due, and is a measure of the extent to which the Bank may require funds to meet those obligations. The Bank's liquidity management is concentrated on the timing of cash in-flows and out-flows, as well as the adequacy of available cash and liquid securities. For this, the Bank estimates and relates all expected cash flows from assets and liabilities.

The Bank's commitment to maintaining a strong liquidity position is established in policies, approved by the Board of Directors, including a minimum liquidity ratio of 50% liquid assets to the next twelve months net cash requirements. The Bank's liquid assets are maintained in short-term placements and negotiable securities.

The table below presents the cash flows payable on financial liabilities placed into relevant maturity groups, based on the remaining period from the financial position date to the contractual maturity date. It indicates the earliest maturity dates that the Bank's counterparties have the ability to demand repayment. The figures represent undiscounted cash flows and therefore do not match to the statement of financial position.

Presented in EUR (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	Total
Borrowings	-	122	173,343	99,529	11,467	284,461
Derivative financial instruments	-	8,746	-	-	-	8,746
Payables and accrued interest	-	2,210	841	-	-	3,051
Financial Liabilities at 31 December 2011	**0**	**11,078**	**174,184**	**99,529**	**11,467**	**296,258**
Borrowings	-	78	95,292	199,894	18,763	314,027
Derivative financial instruments	-	202	-	-	-	202
Payables and accrued interest	-	2,670	909	-	-	3,579
Financial liabilities at 31 December 2010	**0**	**2,950**	**96,201**	**199,894**	**18,763**	**317,808**

For the Bank's financial assets, the majority mature from one year and over taking into consideration the latest possible repayment date.

Market Risk

Market risk refers to the probability of losses due to changes in the market prices of financial instruments, interest rates and exchange rates. The Bank funds its operations by using its capital and by borrowing in the international capital markets. The Bank aims to match, wherever possible, the currencies, tenors and interest rate characteristics of its borrowings with those of its lending portfolios. When necessary, the Bank uses derivative instruments to reduce its exposure to exchange rate and interest rate risk.

Foreign Exchange Risk

Exchange rate risk is the impact of unanticipated changes in foreign exchange rates on the Bank's assets and liabilities, and any impact that could reflect on the income statement. The Bank monitors its assets and liabilities in order to ensure the Bank takes no significant foreign exchange risks. In doing so the Bank matches, to the extent practicable, the lending obligations in any one currency, after swap activities, with liabilities in the same currency.

Furthermore, to avoid currency mismatches, borrowers are required to service their loans in the currencies disbursed by the Bank.

The effect of any currency fluctuations to the net exposure of the Bank is minimal. The tables below provide a currency breakdown of the Bank's assets and liabilities.

Presented in EUR (000)	Euro	United States dollar	Japanese yen	Pound Sterling	Other	Special drawing right	Total
Assets							
Cash and bank balances	8,277	3,590	-	13	8	-	11,888
Investment securities	123,150	31,870	-	-	-	-	155,020
Impairment losses on invest. securities	(14,171)	-	-	-	-	-	(14,171)
Loans	278,730	409,488	-	-	-	-	688,218
Deferred income	(3,779)	(3,134)	-	-	-	-	(6,913)
Impairment losses on loans	(4,961)	(34,882)	-	-	-	-	(39,843)
Equity investments	12,245	2,587	-	-	17,341	-	32,173
Impairment losses on equity investments	(183)	(425)	-	-	-	-	(608)
Other assets	5,260	4,328	-	-	-	-	9,588
Property and equipment	555	-	-	-	-	-	555
Intangible assets	924	-	-	-	-	-	924
Total assets	406,047	413,422	0	13	17,349	0	836,831
Liabilities							
Borrowings	57,923	210,161	-	-	-	-	268,084
Derivative financial instruments	8,746	-	-	-	-	-	8,746
Payables and accrued interest	2,155	785	-	111	-	-	3,051
Members' equity	89,733	-	-	-	-	467,217	556,950
Total liabilities and members' equity	158,557	210,946	0	111	0	467,217	836,831
Net assets (liabilities)	247,490	202,476	0	(98)	17,349	(467,217)	0
Derivative financial instruments	211,021	(210,743)	-	-	(278)	-	0
Net currency balance at 31 December 2011	**458,511**	**(8,267)**	**0**	**(98)**	**17,071**	**(467,217)**	**0**

Presented in EUR (000)	Euro	United States dollar	Japanese yen	Pound Sterling	Other	Special drawing right	Total
Assets							
Cash and bank balances	3,181	7,212	74,077	542	122	-	85,134
Placements with financial institutions	-	4,528	-	-	-	-	4,528
Investment securities	37,934	15,854	-	32,363	-	-	86,151
Loans	263,260	391,486	-	-	-	-	654,746
Deferred income	(4,381)	(1,924)	-	-	-	-	(6,305)
Impairment losses on loans	(4,119)	(39,215)	-	-	-	-	(43,334)
Equity investments	6,742	170	-	-	11,242	-	18,154
Other assets	3,337	4,503	-	126	-	-	7,966
Property and equipment	288	-	-	-	-	-	288
Intangible assets	772	-	-	-	-	-	772
Total assets	307,014	382,614	74,077	33,031	11,364	0	808,100
Liabilities							
Borrowings	98,461	199,793	-	-	-	-	298,254
Derivative financial instruments	202	-	-	-	-	-	202
Payables and accrued interest	2,225	1,348	-	6	-	-	3,579
Members' equity	77,113	-	-	-	-	428,952	506,065
Total liabilities and members' equity	178,001	201,141	0	6	0	428,952	808,100
Net assets (liabilities)	129,013	181,473	74,077	33,025	11,364	(428,952)	0
Derivative financial instruments	(28,838)	16,958	-	12,814	(934)	-	0
Net currency balance at 31 December 2010	**100,175**	**198,431**	**74,077**	**45,839**	**10,430**	**(428,952)**	**0**

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 Management Unit monitors the interest rate exposure of the Bank.

The tables below provide 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 reprice to a market rate of interest before maturity, the next re-pricing date as at the financial position date.

Presented in EUR (000)	Interest bearing				Non-interest bearing	Total
	Up to 1 month	From 1 month to 3 months	From 3 months to 1 year	From 1 year to 5 years		
Assets						
Cash and bank balances	11,884	-	-	-	4	11,888
Investment securities	114,321	-	-	40,699	-	155,020
Impairment losses on invest. securities	-	-	-	-	(14,171)	(14,171)
Loans	118,383	257,533	297,042	15,260	-	688,218
Deferred income	-	-	-	-	(6,913)	(6,913)
Impairment losses on loans	-	-	-	-	(39,843)	(39,843)
Equity investments	-	-	-	-	32,173	32,173
Impairment losses on equity investments	-	-	-	-	(608)	(608)
Other assets	-	-	-	-	9,588	9,588
Property and equipment	-	-	-	-	555	555
Intangible assets	-	-	-	-	924	924
Total assets	244,588	257,533	297,042	55,959	(18,291)	836,831
Liabilities		-	-	-	-	
Borrowings	-	57,908	210,176	-	-	268,084
Derivative financial instruments	-	-	-	-	8,746	8,746
Payables and accrued interest	-	-	-	-	3,051	3,051
Members' equity	-	-	-	-	556,950	556,950
Total liabilities and members' equity	0	57,908	210,176	0	568,747	836,831
Interest rate risk at 31 December 2011	**244,588**	**199,625**	**86,866**	**55,959**	**(587,038)**	**0**

Presented in EUR (000)	Interest bearing				Non-interest bearing	Total
	Up to 1 month	From 1 month to 3 months	From 3 months to 1 year	From 1 year to 5 years		
Assets						
Cash and bank balances	85,132	-	-	-	2	85,134
Placements with financial institutions	4,528	-	-	-	-	4,528
Investment securities	29,122	3,239	11,572	42,218	-	86,151
Loans	135,710	184,890	284,109	50,037	-	654,746
Deferred income	-	-	-	-	(6,305)	(6,305)
Impairment losses on loans	-	-	-	-	(43,334)	(43,334)
Equity investments	-	-	-	-	18,154	18,154
Other assets	-	-	-	-	7,966	7,966
Property and equipment	-	-	-	-	288	288
Intangible assets	-	-	-	-	772	772
Total assets	254,492	188,129	295,681	92,255	(22,457)	808,100
Liabilities and Equity	-	-	-			
Borrowings	-	56,603	147,518	94,133	-	298,254
Derivative financial instruments	-	-	-	-	202	202
Payables and accrued interest	-	-	-	-	3,579	3,579
Members' equity	-	-	-	-	506,065	506,065
Total liabilities and members' equity	0	56,603	147,518	94,133	509,846	808,100
Interest rate risk at 31 December 2010	**254,492**	**131,526**	**148,163**	**(1,878)**	**(532,303)**	**0**

Sensitivity Analysis

The Bank interest rate sensitivity analysis comprises of two elements. Firstly, there is the differential between the interest rate the Bank earns on its assets and the cost of borrowing to fund these assets. For this element the Bank does, as closely as possible, match interest rate periods, thus minimising sensitivity. Secondly, there is the absolute rate earned on assets that are funded by the Bank's equity resources. The majority of these equity resources are currently invested in the Bank's loan portfolio at floating rates; therefore, subjecting earnings on equity resources to some degree of fluctuation. As the Bank matures and its financial position grows it is the intention that earnings on equity resources be stabilized by an increased investment in fixed rate instruments.

The table below details the re-pricing gap by currency. A parallel upward or downward shift in the EUR curve of 50 basis points would have generated the maximum loss or gain respectively.

Presented in EUR (000)	At 31 December 2011	At 31 December 2010
Euro	162,900	180,600
United states dollar	28,700	(13,200)
Pound sterling	-	1,600
Romanian lei	(100)	-
Total re-pricing gap	191,500	169,000
Shift of 50 basis points in the EUR curve	**958**	**845**

Operational Risk

The Bank defines operational risk as all aspects of risk related exposure other than those falling within the scope of financial and market risk. This includes the risk of loss resulting from inadequate or failed internal processes, people and systems or from external events and legal risk. The Bank has a low tolerance for losses arising from the operational risks it is exposed to.

Where any such risks are identified, appropriate mitigation and control measures are put in place. The Bank's operational risk management focuses on proactive measures to mitigate the operational risk.

Classification and Fair Value

The tables below identify the Bank's financial assets and liabilities in accordance with IAS 39 categories.

	At 31 December 2011					
Presented in EUR (000)	**Held-to-maturity**	**Derivatives held for hedging**	**Loans and receivables**	**Available-for-sale**	**At amortized Cost**	**Carrying Amount**
Assets						
Cash and bank balances	-	-	-	-	11,888	11,888
Investment securities	114,321	-	-	40,699	-	155,020
Impairment losses on treasury assets	-	-	-	(14,171)	-	(14,171)
Loans	-	-	688,218	-	-	688,218
Deferred income	-	-	-	-	(6,913)	(6,913)
Impairment losses on loans	-	-	(39,843)	-	-	(39,843)
Equity investments	-	-	-	32,173	-	32,173
Impairment losses on equity investments	-	-	-	(608)	-	(608)
Other assets	-	-	9,588	-	-	9,588
Total financial assets	114,321	0	657,963	58,093	4,975	835,352
Liabilities						
Borrowings	-	-	-	-	268,084	268,084
Derivative financial instruments	-	8,746	-	-	-	8,746
Payables and accrued interest	-	-	-	-	3,051	3,051
Total financial liabilities	**0**	**8,746**	**0**	**0**	**271,135**	**279,881**

Presented in EUR (000)	At 31 December 2010					
	Held-to-maturity	Derivatives held for hedging	Loans and receivables	Available-for-sale	At amortized Cost	Carrying Amount
Assets						
Cash and bank balances	-	-	-	-	85,134	85,134
Placements with financial institutions	-	-	-	-	4,528	4,528
Investment securities	29,122	-	-	57,029	-	86,151
Loans	-	-	654,746	-	-	654,746
Deferred income	-	-	-	-	(6,305)	(6,305)
Impairment losses on loans	-	-	(43,334)	-	-	(43,334)
Equity investments	-	-	-	18,154	-	18,154
Other assets	-	-	7,966	-	-	7,966
Total financial assets	29,122	0	619,378	75,183	83,357	807,040
Liabilities						
Borrowings	-	-	-	-	298,254	298,254
Derivative financial instruments	-	202	-	-	-	202
Payables and accrued interest	-	-	-	-	3,579	3,579
Total financial liabilities	**0**	**202**	**0**	**0**	**301,833**	**302,035**

Fair Value Hierarchy

The Bank held the below financial instruments measured at fair value, and uses the following hierarchy for determining and disclosing the fair value of financial instruments by valuation technique:

- Level 1: Quoted market prices in active markets for identical assets or liabilities,
- Level 2: Other techniques for which all inputs that have a significant effect on the recorded fair value are observable, either directly or indirectly, and
- Level 3: Techniques which use inputs that have a significant effect on the recorded fair value that are not based on observable market data.

The tables below identify the Bank's financial instruments measured at fair value.

Presented in EUR (000)	Level 1	Level 2	Level 3	Carrying Amount
Available-for-sale:				
Investment securities	40,699	-	-	40,699
Equity investments	517	-	31,656	32,173
Derivative financial instruments	-	(8,746)	-	(8,746)
At 31 December 2011	**41,216**	**(8,746)**	**31,656**	**64,126**

Presented in EUR (000)	Level 1	Level 2	Level 3	Carrying Amount
Available-for-sale:				
Investment securities	57,029	-	-	57,029
Equity investments	1,186	-	16,968	18,154
Derivative financial instruments	-	(202)	-	(202)
At 31 December 2010	**58,215**	**(202)**	**16,968**	**74,981**

Classification

Investment securities classified as "available for sale" include government and corporate bonds and their fair value has been determined using quoted prices.

Investment securities classified as "held to maturity" include European commercial papers and notes with an initial maturity lower than 12 months; they are carried amortized which is estimated to be their fair value due to their short term nature. No market prices are available.

Equity investments classified as "available for sale" include investments that are not quoted on an exchange (i.e. private equity), the fair value of which has been estimated with techniques that use inputs not based on observable market data.

Capital Management

The Bank's initial authorized share capital was SDR 1 billion, which is fully subscribed by the shareholding states. In December 2007 the Board of Governors approved a tripling of the Bank's authorized share capital to SDR 3 billion and authorized the offering of SDR 1 billion to the existing Member States for subscription, with the objective of increasing subscribed capital to a total of SDR 2 billion. This increase will allow the Bank to implement its operational strategy to a substantial degree. The Bank does not have any other classes of capital.

In October 2008 the above new shares in the amount of SDR 1 billion that were offered for subscription to the Bank's shareholding states were fully subscribed and allocated. Accordingly, the Bank's paid-in share capital was doubled from SDR 300 million to SDR 600 million. The remaining SDR 1 billion of authorized share capital has not yet been allocated.

The capital usage of the Bank is guided by statutory and financial policy parameters. Article 15 of the Establishing Agreement limits the total amount of outstanding loans, equity investments and guarantees made for ordinary operations to 150% of the Bank's unimpaired subscribed capital, reserves and surpluses, establishing a 1.5:1 institutional gearing ratio. Additionally, disbursed equity investments shall not at any time exceed an amount corresponding to the Bank's total unimpaired paid-in capital, surpluses and general reserve. At the 36th meeting of the Board of Directors in 2008, the operational gearing ratio was set at 100% of the Bank's unimpaired paid-up capital, reserves and surpluses, and the usable portion of the callable capital. As of the financial position date, this limit on the total amount of operations is approximately SDR 1.9 billion (EUR 2.2 billion).

The Bank preserves an actively managed capital to prudently cover risks in its activities. As a multilateral financial institution, the Bank is not subject to regulatory capital requirements. However, the Bank uses standards proposed by the Basel II Capital Accord as a benchmark for its risk management and capital framework. Pursuant to Article 5 of the Establishing Agreement, the Board of Governors shall at intervals of not more than five years review the capital stock of the Bank. In substance, the primary objective of the Bank's capital management is to ensure adequate capital is available to support the Bank's operations.

Notes to the Financial Statements

1. Establishment of the Bank

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 "Establishing Agreement"). In accordance with Article 61 of the Establishing Agreement, following establishment of the Bank the Establishing Agreement entered into force on 24 January 1997. The Bank commenced operations on 1 June 1999.

The purpose of the Bank is to accelerate development and promote cooperation among its shareholder countries. As a regional development institution it is well placed to mobilize financial resources and to improve access to financing for businesses in the whole region as well as for those active only in its individual Member Countries. The Bank offers project and trade financing facilities, equity participations and guarantees. Bank financing of projects and programs is available directly or in cooperation with other national and international development institutions. The Bank may also, where appropriate, provide technical assistance to potential clients.

As at 31 December 2011 the Bank's shareholders comprised 11 countries: Albania, Armenia, Azerbaijan, Bulgaria, Georgia, Greece, Moldova, Romania, Russian Federation, Turkey and Ukraine.

Headquarters Agreement

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

Approval of Financial Statements

The financial statements for 2011 were submitted by the Management Committee to the Board of Directors for approval on 16 March 2012, and were approved on that date. Pursuant to Article 23 of the Establishing Agreement, these financial statements shall be subject to approval by the Board of Governors in their Annual Meeting to be held on 24 June 2012.

2. Segment Reporting

The Bank is a multilateral financial institution dedicated to accelerating development and promoting cooperation among its shareholder countries. The Bank operates in a specific geographical area and the primary reporting format for business segments includes Lending and Treasury operations. Lending activities represent investments in projects such as loans, equity investments and guarantees, which in accordance with the Establishing Agreement, are made to accelerate development and promote co-operation among the Bank's shareholder countries. Treasury activities include raising debt finance, investing surplus liquidity, and managing the Bank's foreign exchange and interest rate risks.

Presented in EUR (000)	2011			2010		
	Lending	Treasury	Total	Lending	Treasury	Total
Income statement						
Interest and similar income	34,452	5,254	39,706	32,802	4,407	37,209
Fees and commission income	1,132	2	1,134	1,144	-	1,144
Total segment revenues	35,584	5,256	40,840	33,946	4,407	38,353
Less: interest and similar expense	(11,924)	(186)	(12,110)	(12,094)	(323)	(12,417)
Less: fees and commission expense	(701)	-	(701)	(345)	-	(345)
Net fair value, foreign exchange and other	6,871	1,011	7,882	7,494	202	7,696
Less: administrative expenses	(14,219)	(1,047)	(15,266)	(13,404)	(678)	(14,082)
Less: depreciation and amortisation	(330)	(68)	(398)	(274)	(74)	(348)
Segment income before impairment	15,281	4,966	20,247	15,323	3,534	18,857
Less: impairment losses	3,983	(14,171)	(10,188)	(8,550)	-	(8,550)
Net income for the year	**19,264**	**(9,205)**	**10,059**	**6,773**	**3,534**	**10,307**
Financial position						
Segment assets	684,094	152,737	836,831	632,287	175,813	808,100
At end of year			**836,831**			**808,100**
Segment liabilities	271,135	8,746	279,881	301,833	202	302,035
Members' equity	-	-	556,950	-	-	506,065
At end of year			**836,831**			**808,100**

The geographical segment reporting of the Bank is presented in the following note "Operational analysis".

3. Interest and Similar Income

Interest and similar income are analysed as follows:

Presented in EUR (000)	Year to 31 December 2011	Year to 31 December 2010
From loans	31,633	29,870
From placements with financial institutions	25	23
From investment securities available-for-sale	1,436	3,584
From investment securities held-to-maturity	3,009	794
From derivative financial assets at fair value	784	6
From front-end fees and commitment fees	2,819	2,932
Interest and similar income	**39,706**	**37,209**

4. Interest and Similar Expense

Interest and similar expense are analysed as follows:

Presented in EUR (000)	Year to 31 December 2011	Year to 31 December 2010
From borrowed funds	5,254	4,521
From issued debt	6,105	6,067
From derivative financial liabilities at fair value	71	255
From amortized issuance and arrangement costs	596	1,496
From other charges	84	78
Interest and similar expense	**12,110**	**12,417**

5. Net Fees and Commissions

Net fees and commissions are analysed as follows:

Presented in EUR (000)	Year to 31 December 2011	Year to 31 December 2010
Management fees	187	271
Appraisal fees	11	27
Prepayment/cancellation fees	153	501
Participation fees	(74)	-
Other	156	-
Net Fees and commissions	**433**	**799**

6.Other Income (Expense)

Other income (expense) is analysed as follows:

Presented in EUR (000)	Year to 31 December 2011	Year to 31 December 2010
Host country reimbursement	875	-
Other	6	(2)
Other income (expense)	**881**	**(2)**

The amount of EUR 875 thousand is granted by the HellenicRepublic for the prior year rental expense.

7. Administrative Expenses

Administrative expenses are analysed as follows:

Presented in EUR (000)	Year to 31 December 2011	Year to 31 December 2010
Salaries and benefits	9,277	8,761
Staff retirement plan	1,590	1,433
Professional fees and related expenses	1,229	747
Utilities and maintenance	1,303	1,360
Other administrative	1,867	1,781
Administrative expenses	**15,266**	**14,082**

8. Impairment Losses on Loans

Loans are stated net of provisions. A summary of the movements in provisions for impairment is as follows:

Presented in EUR (000)	Collective	Specific	Total
At 31 December 2009	27,773	8,385	36,158
Charge for the year	-	8,550	8,550
Release for the year	(5,643)	-	(5,643)
Foreign exchange adjustments	(865)	5,134	4,269
At 31 December 2010	21,265	22,069	43,334
Charge for the year	-	5,371	5,371
Release for the year	(9,962)	-	(9,962)
Foreign exchange adjustments	85	1,015	1,100
At 31 December 2011	**11,388**	**28,455**	**39,843**

As of 31 December 2011 the Bank adopted a new basis for the purpose of collective evaluation of impairment, which was approved internally by the Credit Committee. The Bank's analysis, which was previously based on the banking systems in the BSEC countries, is currently based on the Global Emerging Markets (the "GEM") credit monitoring system. The GEM risk database standardized the data collection process and also has a common methodology adopted by many International Financial Institutions. The standardisation process used by the Bank was also reviewed independently by Moody's credit rating agency. As a result of the revised methodology adopted, there was a release in collective impairment of EUR 9,962 thousand.

At 31 December 2011 the Bank categorized three non-performing and one sub-standard loan as impaired with an exposure amount of EUR 48,415 thousand (2010: EUR 35,841 thousand) and the provision on these assets amounted to EUR 28,455 thousand (2010: EUR 22,069 thousand), as collateral held is estimated not to have significant value.

At 31 December 2011 an amount of EUR 3,409 thousand is included in foreign exchange adjustments due to conversion.

9. Impairment Losses on Equity Investments

A summary of the movements for impairment losses of Available-for-Sale equity investments is as follows:

Presented in EUR (000)	Total
At 31 December 2010	-
Charge for the year	608
At 31 December 2011	**608**

At 31 December 2011 the Bank categorized two equity investments as impaired with an exposure amount of EUR 2,567 thousand (2010: nil) and the provision on these assets amounted to EUR 608 thousand.

10. Impairment Losses on Debt Investment Securities

A summary of the movements for impairment losses of Available-for-Sale debt investments is as follows:

Presented in EUR (000)	Total
At 31 December 2010	-
Charge for the year	14,171
At 31 December 2011	**14,171**

11. Debt Investment Securities

Debt investment securities are analysed as follows:

Presented in EUR (000)	At 31 December 2011	At 31 December 2010
Government bonds	28,150	25,182
Corporate bonds	12,549	31,847
Commercial papers	114,321	29,122
Debt investment securities	155,020	86,151
Less: impairment losses	(14,171)	-
Debt investment securities net of impairment	**140,849**	**86,151**

The Bank's bonds are classified within the available-for-sale portfolio and commercial papers are classified within the held-to-maturity portfolio.

The above government bonds are further analysed as follows:

Presented in EUR (000)	Nominal value	Acquisition cost	Cumulative fair value gain (loss)		Fair Value
			Income statement	Other comprehensive income	
HellenicRepublic	20,000	19,470	(14,171)	-	5,299
Republic of Albania	10,000	9,950	-	(1,270)	8,680
At 31 December 2011	**30,000**	**29,420**	**(14,171)**	**(1,270)**	**13,979**

The Bank, as a multilateral development institution and based, in addition to accepted customary international practices, on certain provisions of the constitutive international treaty of the Bank (inter alia Articles 46 and 48, in conjunction with Articles 38 and 39 thereof of the Establishing Agreement), enjoys and should benefit from "preferred creditor status" in all its Member States. Accordingly, the Bank expects that in respect of any bonds held by it that have been issued by the Member States, the latter should meet their obligations thereunder to the Bank at maturity in full.

12. Derivative Financial Instruments

The table below shows outstanding forward foreign exchange contracts the Bank has engaged. The first column shows the sum of notional amounts, which is the amount of a derivative's underlying asset, and is the basis upon which changes in the value is measured.

Presented in EUR (000)	At 31 December 2011		At 31 December 2010	
	Notional Amount	**Fair Value**	**Notional amount**	**Fair value**
Currency swap purchases	202,275	202,275	37,822	37,748
Currency swap sales	211,808	211,021	37,816	37,950
Derivative financial instruments	**(9,533)**	**(8,746)**	**6**	**(202)**

13. Loans

The Bank offers a range of loan facilities directed to investments for both project and trade financing, tailored to meet an individual operation's requirements. Loans may be denominated in any convertible currency, or a combination of convertible currencies in which the Bank is able to fund itself.

Presented in EUR (000)	At 31 December 2011	At 31 December 2010
At 1 January	654,746	619,049
Disbursements	214,132	249,694
Less: repayments	(190,062)	(252,286)
Foreign exchange movements	9,402	38,289
Loans total	688,218	654,746
Less: deferred income	(6,913)	(6,305)
Less: impairment losses	(39,843)	(43,334)
Loans net of impairment	**641,462**	**605,107**

The Bank classifies loan facilities as either standard, overdue, doubtful or non-performing. Non-performing are those that are primarily impaired and which associated interest is not being accrued. As of 31 December 2011 all loan facilities are classified as standard and there were four that were impaired.

Renegotiated loans that are included in the total above and were made in 2011 were nil (2010: EUR 35,237 thousand).

At 31 December 2011 an amount of EUR 1,701 thousand is included in foreign exchange movements due to conversion.

Interest is generally based on 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 8.0%. The fair value of the loan portfolio is approximately equal to carrying value plus accrued interest as all loans bear a variable interest rate and are given at market terms and conditions. Further analysis of the loan portfolio is presented in note 15 "Operational analysis".

14. 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 entities as detailed below.

		At 31 December 2011		At 31 December 2010	
Presented in EUR (000)	**% of Investment**	**Cost**	**Fair Value**	**Cost**	**Fair Value**
SEAF Trans-Balkan Fund LLC	18.33	-	-	-	169
Access Bank, Azerbaijan	19.99	13,328	16,824	7,888	10,056
TransgazRomania	0.72	419	517	859	1,186
Balkan Accession Fund	9.09	7,226	6,792	6,402	5,859
A-Park Kaluga, Russia	19.99	1,714	1,467	800	800
Emerging Europe Accession Fund	6.93	188	188	84	84
Rusal	0.01	4	208	-	-
ADM Ceecat Recovery Fund	5.65	4,106	3,798	-	-
European Virgin Fund	21.05	2,379	2,379	-	-
Available-for-sale total		29,364	32,173	16,033	18,154
Less: impairment losses		-	(608)	-	-
Equity investments net of impairment			**31,565**		**18,154**

The valuation of such investments, which are unlisted, has been estimated using the most recent management accounts or the latest audited accounts as of 31 December 2010, as management considers that is the best available estimate of the investments fair value as of 31 December 2011.

The increase of EUR 2,809 thousand since the acquisition of the investments was due to an unrealized gain in fair value, attributable to the Bank's participation.

During the year the Bank received dividend income of EUR 1,250 thousand. Furthermore, the Bank realized a net gain of EUR 4,711 thousand from its investment in the Access Bank by way of increase in share value.

The Bank has a committed amount of EUR 25,955 thousand towards the above entities share capital, which as of 31 December 2011 has not been called-up. Further analysis of the equity investment portfolio is presented in note 15 "Operational analysis".

As at 31 December 2011 the Bank has only one equity investment where it holds 21 per cent of the investee share capital, but does not exert significant influence, hence the investment is not accounted for as an investment in an associate under IAS 28.

15. Operational Analysis

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

Presented in EUR (000)	At 31 December 2011		At 31 December 2010	
	Outstanding disburse-ments	Undrawn commitments	Outstanding disburse-ments	Undrawn commitments
Analysis by instrument				
Loans	688,218	130,012	654,746	73,238
Equity investments	32,173	25,955	18,154	9,096
Guarantees	-	16,000	-	-
At end of year	**720,391**	**171,967**	**672,900**	**82,334**
Analysis by country				
Albania	50,250	3,478	29,937	12,264
Armenia	32,332	-	39,456	1,132
Azerbaijan	40,499	22,184	44,406	7,705
Bulgaria	66,121	21,000	52,244	2,590
Georgia	22,877	17,082	15,095	2,264
Greece	47,724	-	59,400	-
Moldova	21,064	4,000	8,135	-
Romania	20,517	20,000	26,185	20,000
Russia	162,241	35,082	120,835	27,283
Turkey	158,051	-	159,409	-
Ukraine	85,558	23,186	111,686	-
Regional	13,157	25,955	6,112	9,096
At end of year	**720,391**	**171,967**	**672,900**	**82,334**
Analysis by sector				
Financial institutions	292,211	62,805	222,911	25,103
General industries*	298,701	49,977	294,708	34,642
Energy and infrastructure	129,479	59,185	155,281	22,589
At end of year	**720,391**	**171,967**	**672,900**	**82,334**

* Also includes transport and tourism.

The Bank is restricted to operating in its 11 Member States and individual country limits are set at a maximum of 30% of approved commitments. This limit is calculated on the basis of the Board of Directors approved operations, minus repayments and cancellations. Individual operations are further constrained by the Single Obligor Limit and by monitoring of Sectoral Exposure.

Operations are monitored according to a schedule prepared by the Bank's Risk Management in conjunction with the originating Banking Teams. Monitoring reports are completed by the Bank's Project Implementation and Monitoring on an individual basis and risk asset reviews are performed which may result in a downgrade or upgrade of an operation's status and, if a significant deterioration is noted, trigger an impairment test.

16. Other Assets

Other assets are analysed as follows:

Presented in EUR (000)	At 31 December 2011	At 31 December 2010
Accrued interest	7,258	6,851
Paid-in share capital not received	-	2
Advances and prepaid expenses	1,149	810
Other prepayments	236	233
Rental reimbursement receivable *	875	-
Guarantee deposits	70	70
Other assets	**9,588**	**7,966**

* The HellenicRepublic has granted the rental expense of prior year in September 2011.

17. Property and Equipment

Property and equipment are analysed as follows:

Presented in EUR (000)	Buildings (leasehold)	Vehicle	Furniture and office accessories	Computers and office equipment	Total
Cost					
At 31 December 2009	191	68	486	1,435	2,180
Additions	3	-	12	33	48
Disposals	-	-	(1)	(35)	(36)
At 31 December 2010	194	68	497	1,433	2,192
Additions	3	95	57	287	442
Disposals	-	(68)	-	(11)	(79)
At 31 December 2011	**197**	**95**	**554**	**1,709**	**2,555**
Accumulated depreciation					
At 31 December 2009	186	35	422	1,190	1,833
Charges	4	14	30	59	107
Disposals	-	-	(1)	(35)	(36)
At 31 December 2010	190	49	451	1,214	1,904
Charges	3	33	24	115	175
Disposals	-	(68)	-	(11)	(79)
At 31 December 2011	**193**	**14**	**475**	**1,318**	**2,000**
Net book value					
At 31 December 2011	**4**	**81**	**79**	**391**	**555**
At 31 December 2010	4	19	46	219	288
At 31 December 2009	5	33	64	245	347

18. Intangible Assets

Intangible assets comprising computer software are analysed as follows:

Presented in EUR (000)	Total
Cost	
At 31 December 2009	2,390
Additions	219
At 31 December 2010	2,609
Additions	390
At 31 December 2011	**2,999**
Accumulated amortisation	
At 31 December 2009	1,653
Charges	184
At 31 December 2010	1,837
Charges	238
At 31 December 2011	**2,075**
Net book value	
At 31 December 2011	**924**
At 31 December 2010	772
At 31 December 2009	737

19. Borrowings

Borrowing facilities arranged at end of the year are analysed below. In addition to medium or long-term borrowings, the Bank utilizes short-term financing in the form of borrowings from commercial banks for cash management purposes. At 31 December 2011 the Bank has one issued debt security in the amount of EUR 96,551 thousand.

	At 31 December 2011		At 31 December 2010	
Presented in EUR (000)	**Amount used**	**Borrowings arranged**	**Amount used**	**Borrowings Arranged**
Euro	57,923	148,923	98,461	139,461
United States dollar	210,161	210,161	199,793	199,793
Total	**268,084**	**359,084**	**298,254**	**339,254**

The Interest rate on borrowings falls within a range of Euribor or USD Libor of +0 to +250 points. There is no collateral against the above borrowed funds. The fair value of the borrowings is approximately equal to their carrying value.

20. Payables and Accrued Interest

Payables and accrued interest are analysed as follows:

Presented in EUR (000)	At 31 December 2011	At 31 December 2010
Accrued interest	1,167	1,905
Social insurance fund (IKA) contributions	31	27
Pension plan obligation	841	910
Suppliers and other accrued expenses	1,012	737
Payables and accrued interest	**3,051**	**3,579**

21. Share Capital

In accordance with Article 4 of the Establishing Agreement, the initial authorized share capital of the Bank is one billion SDR divided into one million shares having a par value of one thousand SDR each. The authorized capital stock of the Bank may be increased at such time and under such terms as may seem advisable.

The Bank's capital stock is divided into paid-in shares and callable shares. Payment for the paid-in shares subscribed to by members is made over a period of years in accordance with Article 6 of the Establishing Agreement or as determined in advance by the Bank. The same Article states that payment of the amount subscribed to the callable shares is subject to call only as and when required by the Bank to meet its obligations.

Under Article 37 of the Establishing Agreement any member may withdraw from the Bank by transmitting in writing to the Bank at its Headquarters. Withdrawal by a member shall become effective and its membership shall cease on the date specified in its notice, but in no event less than six months after such notice is received by the Bank. However, at any time before the withdrawal becomes finally effective, the member may notify the Bank in writing of the cancellation of its notice of intention to withdraw. Under Article 39 of the Establishing Agreement after the date on which a member ceases membership, it shall remain liable for its direct obligations to the Bank, and also remain responsible for its contingent liabilities to the Bank, incurred as of that date. No member has ever withdrawn its membership, nor has any ever indicated to the Bank it might do so. Were a member to withdraw from the Bank, at the time a member ceases membership, the Bank shall arrange for the repurchase of such a member's shares by the Bank as part of the settlement of accounts with such a member, and be able to impose conditions and set dates pursuant to the same Article 39 of the Establishing Agreement. Any amount due to the member for its shares shall be withheld so long as the member, including its central bank or any of its agencies, has outstanding obligations to the Bank, which may, at the option of the Bank, be applied to any such liability as it matures. If losses are sustained by the Bank on any guarantees or loans which were outstanding on the date when a member ceased membership and the amount of such losses exceeds the amount of the reserves provided against losses on the date, the member concerned shall repay, upon demand, the amount by which the repurchase price of its shares would have been reduced if the losses had been taken into account when the repurchase price was determined.

Under Article 42 of the Establishing Agreement in the event of termination of the operations of the Bank, the liability of members for the unpaid portion of the subscribed capital of the Bank shall continue until all claims of creditors, including all contingent claims, have been discharged.

All participating members had fully subscribed to the initial authorized share capital in accordance with Article 5 of the Establishing 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 the initial authorized capital and the Board of Governors approved their request. On 5 October 2008 the new shares offered in the same structure as the initial authorized share capital, in the amount of SDR 1 billion were fully

subscribed by the Member States. Furthermore, Azerbaijan also subscribed to the 3% of the initial authorized share capital that remained unallocated, while Romania subscribed both to their allocation of new shares and to those of Georgia. This subscription process followed a decision taken by the Board of Governors in December 2007 to triple the Bank's authorized capital to SDR 3 billion and to double the subscribed capital to SDR 2 billion, while leaving authorized capital of SDR 1 billion unallocated. On October 2011 the Board of Governors approved the request from Moldova to a fifty per cent reduction of its portion of subscribed capital, from 1% to 0.5%, and those shares were released to unallocated.

The above share capital both in SDR and EUR equivalent is analysed as follows:

Presented in (000)	At 31 December 2011		At 31 December 2010	
	SDR	EUR	SDR	EUR
Authorized share capital	3,000,000	3,547,897	3,000,000	3,486,870
Less: unallocated share capital*	(1,010,000)	(1,198,597)	(1,000,000)	(1,162,290)
Subscribed share capital	1,990,000	2,349,300	2,000,000	2,324,580
Less: shares not yet called	(1,393,000)	(1,653,115)	(1,400,000)	(1,627,206)
Less: shares called but not yet due	(177,269)	(210,371)	(200,000)	(232,458)
Less: shares called and past due	(15,502)	(18,396)	(30,968)	(35,994)
Called-up share capital	404,229	467,418	369,032	428,922
Cumulative translation adjustment	-	(216)	-	-
Advance against future call	12	15	26	30
Paid-in share capital	**404,241**	**467,217**	**369,058**	**428,952**

* Shares available to new or existing Member States.

The translation gains or losses on share capital which is callable and payable are credited or debited to the "Cumulative translation adjustment" to duly reflect the fluctuations of the SDR value of the members' equity.

Initial Capital

In accordance with paragraph 2 under Article 5 of the Establishing Agreement, the initially authorized capital stock was subscribed by and issued to each Member as follows: 10% (SDR 100 million) fully paid and 20% (SDR 200 million) payable by promissory notes or other obligations which are not negotiable and non-interest bearing in eight equal successive annual instalments in the years 1998–2005.

Capital Increase

The capital increase of SDR 1 billion is divided into SDR 300 million paid in capital and SDR 700 million callable capital. Pursuant to the Board of Governors decision in October 2008, the SDR 300 million paid in portion is divided into 10% (SDR 100 million) fully paid shares in 2010 and 20% (SDR 200 million) payable shares by promissory notes or other obligation issued by such member in eight equal successive annual instalments in the years 2011 to 2018. As of October 2011, the capital increase was reduced by SDR 10 million of the subscribed share capital.

The initial and capital increase that was issued is analysed as follows:

Presented in SDR (000)	At 31 December 2011		
	Initial Capital	Capital Increase	Total
Authorized share capital	1,000,000	2,000,000	**3,000,000**
Less: unallocated share capital	(30,000)	(980,000)	**(1,010,000)**
Subscribed share capital	970,000	1,020,000	**1,990,000**
Less: shares not yet called	(679,000)	(714,000)	**(1,393,000)**
Less: shares called but not yet due	-	(177,269)	**(177,269)**
Less: shares called and past due	-	(15,502)	**(15,502)**
Called-up share capital	291,000	113,229	**404,229**
Advance against future call	35	(23)	**12**
Paid-in share capital	**291,035**	**113,206**	**404,241**

Statement of Subscriptions

A statement of capital subscriptions illustrating the number of shares and the amount subscribed by each member is shown below, including their respective callable, payable and the amount paid. The capital subscription status at 31 December 2011 is analysed as follows:

		Subscribed	Callable	Payable	Paid
Member	Shares	Presented in SDR (000)			
Albania	40,000	40,000	28,000	6,000	6,000
Armenia	20,000	20,000	14,000	1,750	4,250
Azerbaijan	100,000	100,000	70,000	8,750	21,250
Bulgaria	270,000	270,000	189,000	23,625	57,375
Georgia	10,000	10,000	7,000	-	3,000
Greece	330,000	330,000	231,000	28,970	70,030
Moldova	10,000	10,000	7,000	-	3,000
Romania	280,000	280,000	196,000	25,426	58,574
Russian Fed.	330,000	330,000	231,000	28,875	70,125
Turkey	330,000	330,000	231,000	28,875	70,125
Ukraine	270,000	270,000	189,000	40,500	40,500
Total	**1,990,000**	**1,990,000**	**1,393,000**	**192,771**	**404,229**

Basic Earnings per Share

Basic earnings per share is calculated by dividing the net income for the year attributable to ordinary shareholders of the Bank by the weighted average number of ordinary shares outstanding during the year.

Presented in EUR (000)	At 31 December 2011	At 31 December 2010
Net income attributable to ordinary shareholders of the Bank	10,059	10,307
Weighted average number of ordinary shares for basic earnings per share	448,085	378,600
Basic earnings per share in EUR	**0.022**	**0.027**

22. Reserves

Reserves are analysed as follows:

Presented in EUR (000)	General	Available-for-sale	Total
At 1 January 2010	25,209	4,771	29,980
Gains (losses) on revaluation of available-for-sale	-	(5,550)	(5,550)
Transferred from retained earnings	4,368	-	4,368
Foreign exchange adjustments	1,874	324	2,198
At 31 December 2010	31,451	(455)	30,996
Gains (losses) on revaluation of available-for-sale	-	(11,410)	(11,410)
Transferred to income statement due to impairment	-	14,171	14,171
Transferred from retained earnings	6,346	-	6,346
Exchange rate difference due to conversion	200	(200)	-
Foreign exchange adjustments	(338)	338	-
At 31 December 2011	**37,659**	**2,444**	**40,103**

23. Cash and Cash Equivalents

Cash and cash equivalents are analysed as follows:

Presented in EUR (000)	At 31 December 2011	At 31 December 2010
Cash on hand	4	2
Investments maturing up to 1 month:		
Bank balances	11,884	85,132
Placements with financial institutions	-	4,528
Held-to-maturity portfolio	114,321	29,123
Investments maturing from 1 month to 3 months:		
Available-for-sale portfolio	-	3,239
Cash and cash equivalents	**126,209**	**122,024**

The commercial papers held in the Bank's portfolio and issued by other financial institutions were rated at a minimum of A1 by Standard and Poor's or P1 by Moody's, in accordance with internal financial policies.

24. Staff Retirement Plan

At normal retirement age (60 years), a staff member is entitled to a pension equal to 1% of his pensionable salary (i.e. average of the two best out of the last five years) multiplied by his/her years of service at the Bank, under the defined benefit scheme. 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.

Defined Benefit Scheme

The defined benefit scheme covers all eligible employees of the Bank. A qualified actuary performs an actuarial valuation of this scheme at each end of year using the projected unit method, which is rolled forward to the following year accounts. The most recent valuation date was 31 December 2011. The present value of the defined benefit obligation and current service cost was calculated using the projected unit credit method.

Presented in EUR (000)	**At 31 December 2011**	**At 31 December 2010**
Amounts recognized in the statement of financial position		
Present value of the defined benefit obligations	7,935	7,095
Fair value of plan assets	(7,788)	(6,860)
	147	235
Unrecognized actuarial gains	694	675
Net liability	841	910
Expenses for the year	970	875
Past service obligation	69	(10)
Contributions paid	(1,039)	(865)
At end of year	**841**	**910**
Amounts recognised in the income statement		
Current service cost	826	715
Interest cost	354	313
Expected return on plan assets	(374)	(295)
Amortisation of unrecognized gain	-	(11)
Past service obligation	164	153
Total included in administrative expenses	**970**	**875**
Principal actuarial assumptions used		
Discount rate	5.00%	5.00%
Expected return on plan assets	5.11%	5.14%
Future salary increase	2.50%	3.50%
Future pension increase	2.00%	2.00%
Average remaining working life of employees	12 years	13 years

The following table presents the major categories and reconciliation of the plan assets:

Presented in EUR (000)	**At 31 December 2011**	**At 31 December 2010**
Major categories of plan assets		
Cash instruments	20.80%	26.50%
Fixed interest	54.70%	43.70%
Equities	18.60%	23.50%
Other	5.90%	6.30%
Reconciliation of plan assets		
Market value at 1 January	6,860	5,851
Expected return	374	295
Contributions paid	1,039	865
Fund benefits	(137)	(144)
Expenses	(93)	(87)
Asset (loss) gain	(255)	80
Fair value of plan assets	**7,788**	**6,860**

The actual investment return on assets of the Fund was 1.60%. The expected return on plan assets has been based on asset structure allowed by the Fund as well as the yield of high quality corporate bonds. The Bank estimate of contributions to be paid in 2012 will not materially differ from those paid in the current year.

The funding status at year end and at the end of the last four years was as follows:

Presented in EUR (000)	**2011**	**2010**	**2009**	**2008**	**2007**
Defined benefit obligations	7,935	7,095	5,967	4,431	3,899
Plan assets	(7,788)	(6,860)	(5,851)	(4,835)	(4,582)
Plan deficit (surplus)	147	235	116	(404)	(683)
Net experience adjustments on plan liabilities (assets)	**(275)**	**177**	**677**	**(295)**	**(1,244)**

Defined Contribution Scheme

The pension expense under this scheme was EUR 487 thousand (2010: EUR 437 thousand) and is included in "Administrative expenses".

Greek State Social Insurance Fund

The pension expense of staff that is alternatively entitled to retirement benefits from this fund was EUR 133 thousand (2010: EUR 121 thousand) and is included in "Administrative expenses".

25. Operating Leases

The Bank has entered into lease contracts for its Headquarters and other 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 "Administrative expenses" totalled EUR 882 thousand (2010: EUR 919 thousand).

The HellenicRepublic has granted the rental amounting to EUR 875 thousand for 2010, which is included in "Other income".

26. Related Parties

The Bank has the below related parties.

Key Management Personnel

Key management personnel comprise: the President, Vice Presidents and Secretary General. They are entitled to a staff compensation package that includes a salary, medical insurance, inclusion in the Bank's retirement schemes and eligibilityfor other short term benefits. The amounts paid to key management personnel during the year were EUR 1,200 thousand (2010: EUR 1,102 thousand). Key management personnel do not receive post-employment benefits, other long term benefits, termination benefits nor any share based payments.

The members of the Board of Directors are not personnel of the Bank and do not receive any fixed term salaries nor any staff benefits.

Special Funds

Special funds are established in accordance with Article 16 of the Establishing Agreement and are administered under the terms of rules and regulations adopted by the Bank. Special Funds are audited on an annual basis and their assets and fund balances are not included in the Bank's statement of financial position. During 2011 the Bank administered two special funds. Extracts from the audited financial statements are included under the "Summary of special funds".

27. Events after the Reporting Year

The European Virgin Fund, of which the Bank owned 21.05% of the investee share capital, has decided to extend its share capital contributions into 2012. As such, the Bank estimates that its equity share will be diluted to about 16.7% of the total investee share capital.

There are no other material events after the reporting year that would require disclosure or adjustment to these financial statements.

28. Summary of Special Funds

With the Hellenic Government

The Technical Cooperation Special Fund's objective 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 is shown below.

Presented in EUR (000)	At 31 December 2011	At 31 December 2010
Statement of movements		
Balance brought forward	406	405
Net income for the year	3	1
Less: disbursements	(64)	-
Balance of available funds	**345**	**406**
Financial position		
Placements with other financial institutions	345	406
Total Assets	**345**	**406**
Unallocated fund balance	345	406
Total Liabilities and Contributor Resources	**345**	**406**

With the Development Bank of Austria

The Technical Cooperation Special Fund's objective is to cover reasonable technical cooperation activities in the Bank's member countries, with a strong potential to generate an opportunity for the Development Bank of Austria to co-finance a project in the private sector in connection with a technical cooperation activity. The movement in the Fund is shown below.

Presented in EUR (000)	At 31 December 2011	At 31 December 2010
Statement of movements		
Balance brought forward	354	479
Net income for the year	1	-
Less: disbursements	(23)	(125)
Balance of available funds	**332**	**354**
Financial position		
Placements with other financial institutions	332	389
Total Assets	**332**	**389**
Allocated fund balance	-	35
Unallocated fund balance	332	354
Total Liabilities and Contributor Resources	**332**	**389**

Independent Auditor's Report

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

Report on the Financial Statements

We have audited the accompanying financial statements of the Black Sea Trade and Development Bank (the "Bank"), which comprise the statement of financial position as at 31 December 2011, the income statement and the statement of comprehensive income, statement of changes in equity and cash flow statement for the year then ended, and a summary of significant accounting policies and other explanatory information.

Management's Responsibility for the Financial Statements

Management is responsible for the preparation and fair presentation of these financial statements in accordance with International Financial Reporting Standards as adopted by the European Union and for such internal controls as management determines is necessary to enable the preparation of financial statements that are free from material misstatement, whether due to fraud or error.

Auditor's Responsibility

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 comply with ethical requirements and plan and perform the audit to obtain reasonable assurance whether the financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation and fair presentation of the financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of accounting estimates made by management, as well as evaluating the overall presentation of the financial statements.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinion.

Opinion

In our opinion, the accompanying financial statements present fairly, in all material respects, the financial position of the Black Sea Trade and Development Bank as at 31 December 2011 and of its financial performance and its cash flows for the year then ended in accordance with International Financial Reporting Standards as adopted by the European Union.

16 March 2012

ERNST & YOUNG (HELLAS) CERTIFIED
AUDITORS ACCOUNTANTS SA
11thKm National Rd.Athens – Lamia
GR – 144 51 Metamorphosis
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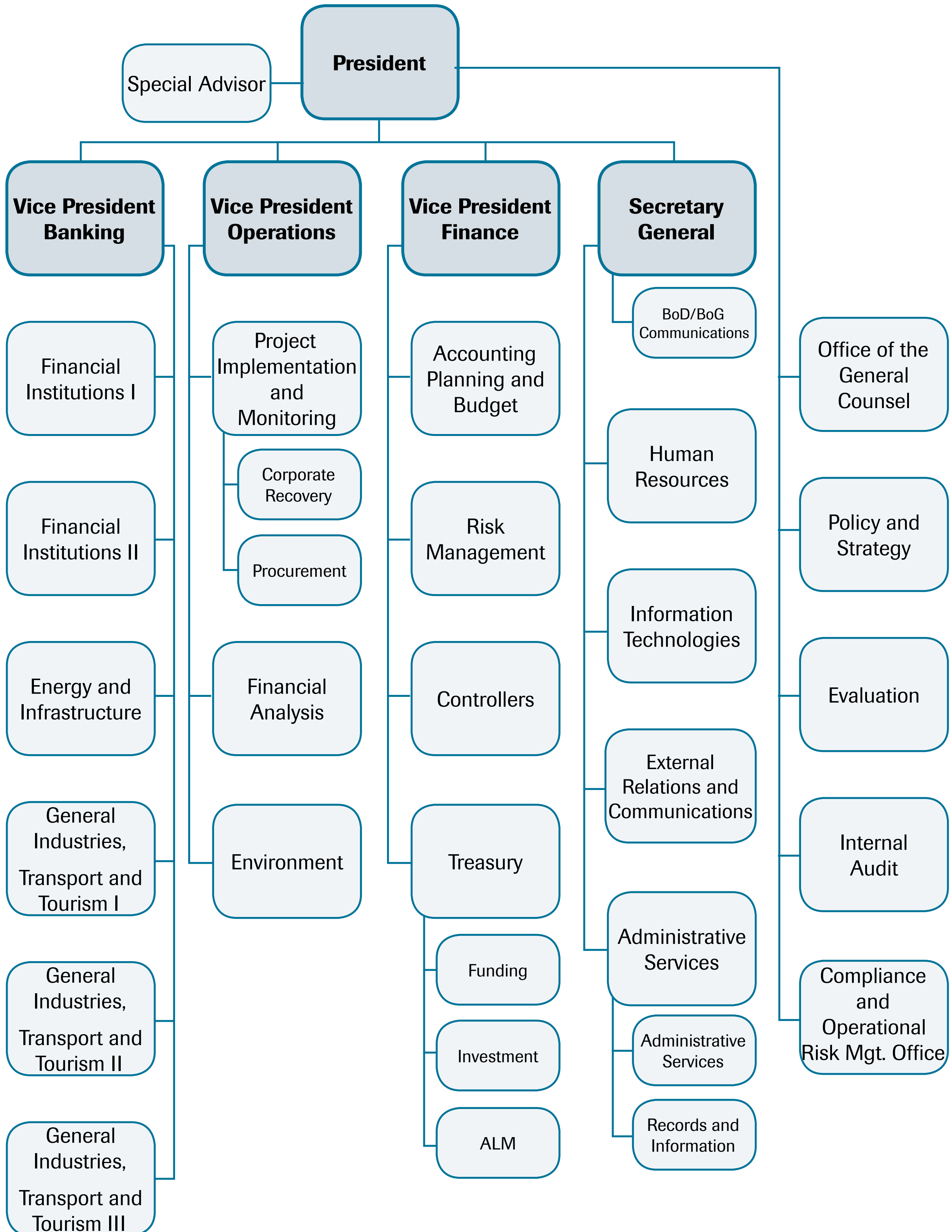
Annex A

ORGANIZATIONAL CHART



As of 31 December 2011

Annex B

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