Promoting Regional Prosperity

Annual Report 2018

Black Sea Trade & Development Bank

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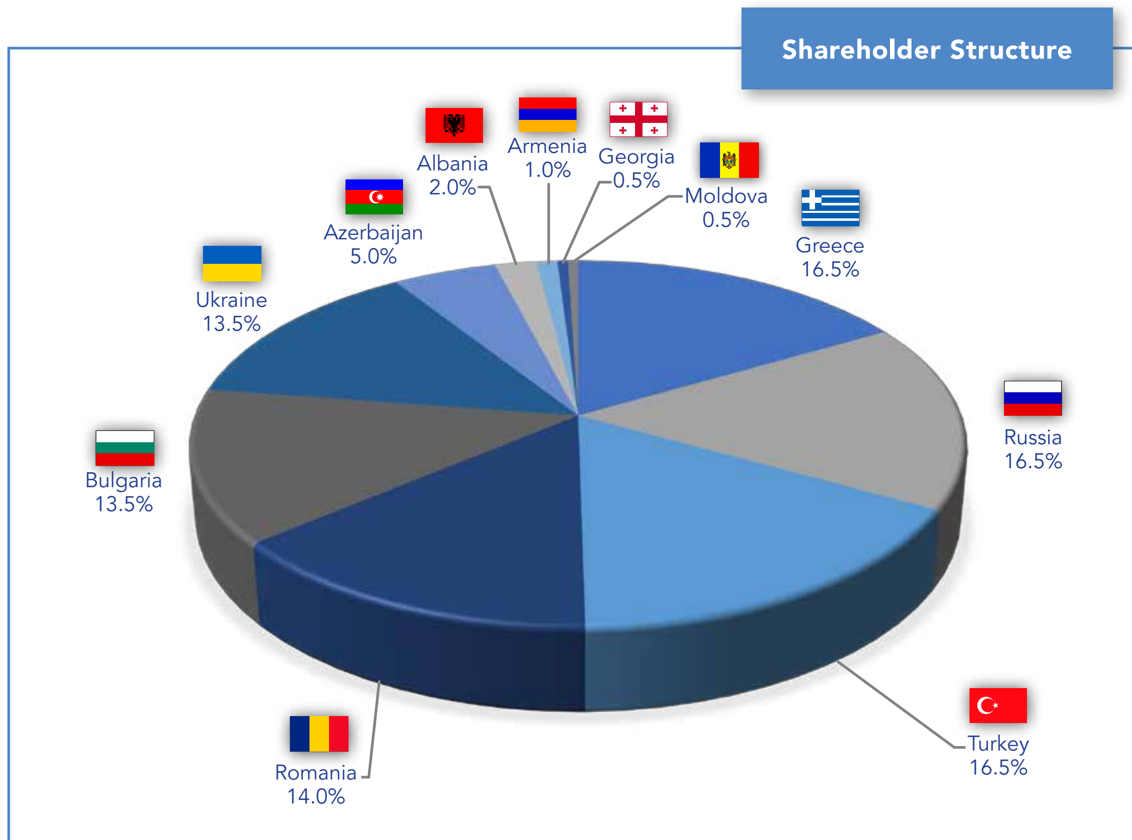
Introduction

Who We Are

The Black Sea Trade and Development Bank (BSTDB or 'the Bank'), an international financial institution with headquarters in Thessaloniki, Greece, was established by Albania, Armenia, Azerbaijan, Bulgaria, Georgia, Greece, Moldova, Romania, Russia, Turkey, and Ukraine. BSTDB started operations in June 1999 and has an authorized capital of EUR 3.45 billion and a subscribed capital of EUR 2.3 billion.



BSTDB supports economic development and regional cooperation in the Black Sea Region through loans, guarantees, and equity participations in private enterprises and public entities in member countries.

As an international financial institution, the Bank has preferred creditor status. This means that the Bank will usually (i) not reschedule debt payments with respect to its loans to, or guaranteed by, its member countries and (ii) not reschedule its loans to a private sector borrower due to a general foreign exchange unavailability in the borrower's country.

Corporate Governance

Management Structure

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.

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

Each of the Member States of the Bank is represented on the Board of Governors. All powers of the Bank are vested in the BoG. With certain exceptions, the BoG 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 BoD. The composition of the Audit Committee is four BoD members, one being appointed as Chairman.

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

The Management Committee 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 BoD on the recommendation of the President.

Compliance

The compliance function of the Compliance and Operational Risk Management Office (DCR) of the Bank assists management in effectively managing 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 internal integrity issues, DCR monitors, administers and advises on Code of Conduct-related issues for the Bank Officials and staff.

With regard to financing operations, anti-fraud, corruption, money laundering, terrorism financing and sanctions, 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 advises the business groups, as needed, inter alia, on the Customer Due Diligence process and integrity issues.

Reporting and Disclosure

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 to the Board of Directors, and both the interim financial statements and the Annual Report are published on the Bank's website. Pursuant to Article 35 of the Establishing Agreement, published reports are accessible [transmitted to] the Governments of the Member States, 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, scope, work program, and 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 ongoing 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 BoD.

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 BoD, 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.

Board of Governors

Republic of Albania

Governor: Mr. Erjon LUCI, Deputy Minister of Finance
Alternate Governor: position vacant

Republic of Armenia

Governor: Mr. Arthur JAVADYAN, Chairman, Central Bank of Armenia
Alternate Governor: Mr. Andranik GRIGORYAN, Head, Financial System Stability & Development Department, Central Bank of Armenia

Republic of Azerbaijan

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

Republic of Bulgaria

Governor: Ms. Marinela PETROVA, Deputy Minister of Finance
Alternate Governor: Ms. Gergana BEREMSKA, Director, International Financial Insitutions & Cooperation Directorate, Ministry of Finance

Georgia

Governor: Mr. Koba GVENETADZE, Governor, National Bank of Georgia
Alternate Governor: Mr. Ivane MATCHAVARIANI, Minister of Finance

Hellenic Republic

Governor: Mr. Yannis DRAGASAKIS, Deputy Prime Minister & Minister of Economy & Development
Alternate Governor: position vacant

Republic of Moldova

Governor: Mr. Octavian ARMASU, Minister of Finance
Alternate Governor: position vacant

Romania

Governor: Mr. Eugen Orlando TEODOROVICI, Minister of Public Finance
Alternate Governor: Mr. Gyorgy ATTILA, Secretary of State, Ministry of Public Finance

Russian Federation

Governor: Mr. Sergey STORCHAK, Deputy Minister of Finance
Alternate Governor: position vacant

Republic of Turkey

Governor: Mr. Bulent AKSU, Deputy Minister of Treasury & Finance
Alternate Governor: position vacant

Ukraine

Governor: Mr. Stepan KUBIV, First Vice-Prime Minister of Ukraine
Alternate Governor: Mr. Volodymyr KUCHYN, Head of Office for European Integration & International Programs, National Bank of Ukraine

As of 31 December 2018

Board of Directors

Republic of Albania

Director: Ms. Gelardina PRODANI, General Secretary, Ministry of Finance
Alternate Director: position vacant

Republic of Armenia

Director: Mr. Davit ANANYAN, Chairman of the State Revenue Committee
Alternate Director: Mr. Argam ARAMYAN, Head, International Cooperation Department, Ministry of Finance

Republic of Azerbaijan

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

Republic of Bulgaria

Director: Mrs. Petya KUZEVA, Director, Govenrment Debt Directorate, Ministry of Finance
Alternate Director: Mr. Nikola SHERLETOV, Parliamentary Secretary, Ministry of Finance

Georgia

Director: Mr. Nikoloz GAGUA, Deputy Minister of Finance
Alternate Director: Mr. Lasha KHUTSISHVILI, Deputy Minister of Finance

Hellenic Republic

Director: Mr. Ilias XANTHAKOS, Secretary General, Ministry of Economy & Development
Alternate Director: position vacant

Republic of Moldova

Director: Ms. Elena MATVEEVA, Head, Public Debt Department, Ministry of Finance
Alternate Director: position vacant

Romania

Director: Ms. Diana BLINDU, Senior Advisor, General Directorate for International Financial Relations, Ministry of Public Finance
Alternate Director: Mr. Stefan PETRESCU, Deputy Director General, General Directorate for International Financial Relations, External Public Finance, Ministry of Public Finance

Russian Federation

Director: Mr. Evgeny STANISLAVOV, Director, Department of Economic Cooperation, Ministry of Foreign Affairs
Alternate Director: position vacant

Republic of Turkey

Director: Mr. Kemal Cagatay IMIGRI, Acting Director General, Foreign Economic Relations, Ministry of Treasury & Finance
Alternate Director: position vacant

Ukraine

Director: position vacant
Alternate Director: Mr. Vitaliy LISOVENKO, Government Envoy for Public Debt Management, Ministry of Finance

Audit Committee

Ms. Diana BLINDU	Director for Romania and Chairperson of the Audit Committee
Mr. Davit ANANYAN	Director for the Republic of Armenia and Audit Committee member
Mr. Famil ISMAYILOV	Director for the Republic of Azerbaijan and Audit Committee member
Mr. Nikoloz GAGUA	Director for Georgia and Audit Committee member

Management

On 16 July 2018, Mr. Dmitry Pankin assumed his duties as President of the Black Sea Trade and Development Bank for a four-year period, as appointed by the Board of Governors. Mr. Pankin (Russia) replaced Mr. Ihsan Ugur Delikanli (Turkey), who had run the Bank since July 2014.

On 17 July 2018, Mr. Hasan Demirhan assumed his duties as Vice President Banking for a four-year period, as appointed by the BoD. Mr. Demirhan (Turkey) replaced Mr. Igor Leshukov (Russia).

On 16 September 2018, Mr. Valeriy Piatnytskyi assumed his duties as Vice President Finance for a four-year period, as appointed by the Board of Directors. Mr. Piatnytskyi (Ukraine) replaced Ms. Valentina Siclovan (Romania).

On 17 December 2018, Mr. Ivaylo Moskovski assumed his duties as Vice President Operations for a four-year period, as appointed by the Board of Directors. Mr. Moskovski (Bulgaria) replaced Ms. Nina Stavreva (Bulgaria).

On 16 March 2019, Mr. Aristotelis Spiliotis assumed his duties as Secretary General for a four-year period, as appointed by the Board of Directors. Mr. Spiliotis (Greece) replaced Mr. Serafeim Tsokas (Greece).

Present Management Team

Dmitry Pankin
President
Chairman of the Board of Directors

Hasan Demirhan
Vice President Banking

Ivaylo Moskovski
Vice President Operations

Valeriy Piatnytskyi
Vice President Finance

Aristotelis Spiliotis
Secretary General

Management Team 2014-2018

Ihsan Ugur Delikanli
President
Chairman of the Board of Directors

Igor Leshukov
Vice President Banking

Nina Stavreva
Vice President Operations

Valentina Siclovan
Vice President Finance

Serafeim Tsokas
Secretary General

To the Board of Governors

In accordance with Article 35 of the Agreement Establishing the Black Sea Trade and Development Bank and Section 10 of its By-Laws, I submit to the Board of Governors the Bank's Annual Report for 2018 as endorsed by the Board of Directors. The Twentieth Annual Report 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.

Dmitry Pankin
President
Chairman of the Board of Directors

Statement by the President

Beneath the turmoil that affected many emerging markets in 2018, the Black Sea Region achieved steady growth. Real GDP growth in the Region reached 2.7% for the year. While this number lagged overall global growth for 2018 and was down from the 3.7% regional growth posted in 2017, it contained a number of positive features. First and foremost, every member country of the Black Sea Economic Cooperation (BSEC) posted real positive GDP growth for the second consecutive year, something which had not occurred in over a decade. Second, the growth occurred against the backdrop of uncertainty and volatility that impacted emerging markets disproportionately and raised concerns about their ability to withstand such headwinds. Third, and relatedly, this turmoil underscored the sound basis of growth in the economies of the Black Sea Region. The continued dedication to the maintenance of balance of key macroeconomic indicators has boosted the credibility and the resilience of these economies, allowing them to weather turbulence by suffering contained setbacks, and recovering quickly and resiliently.

The Region faces its share of challenges to increase levels of investment in order to support current growth and to improve future prospects, and it still faces perception problems despite its sustained commitment to economic stability and improving the business environment. However, it enjoys a very solid foundation upon which to grow in a balanced and viable manner.

Operating in this vibrant and at times challenging environment, the Black Sea Trade and Development Bank accelerated its growth over the course of 2018. Operational activity expanded as the Bank's Board of Directors approved 28 new projects for EUR 569.7 million, up 8.6% from 2017. Commitments grew even more robustly, increasing 54% over 2017, as 30 operations amounting to EUR 617.9 million were signed. Disbursements were up nearly 46% over 2017 levels to EUR 573.8 million, with net disbursements growing EUR 191.1 million. The levels of operational activity achieved established new annual highs for the Bank.

As a result, the operational portfolio grew to EUR 1.36 billion at year end, more than fulfilling the targets outlined in the high case scenario of the Bank's Medium-Term Strategy and Business Plan for the 2015-2018 period. The Bank achieved greater diversification of its portfolio in both geographical and sectoral terms; in most Member States the high case targets that were set were exceeded, with high demand in certain countries resulting in significant levels of assistance being directed to fast growing banks and firms. The Bank also achieved improved sector distribution, with a greater share of operations taking place in the so-called 'real sectors' of the economy. Vigorous demand in the area of renewable energy generation led to a sharp jump in such activities, helping countries towards meeting their climate change commitments and to diversify and improve their sources of energy generation. Local currency lending grew further in scope and size as the Bank increased its support to efforts to develop and deepen local financial systems; to help regional banks and firms to access a diversified array of financial resources; and to contribute to the priority effort of countries to increase confidence in the use of local currencies while reducing dollarization.

These operational achievements occurred even as non-performing loans declined to one operation accounting for less than 1% of the portfolio, while credit-impaired operations were reduced from seven to four, accounting for less than 3.5% of the portfolio. The Bank's mobilization of external resources grew at a steady but prudent rate, as by year end 2018 the ratio of own to borrowed funds had risen to nearly 1:1.25 and capitalization stood at 43%. This is consistent with the importance that the Bank attaches to stable managed growth that increases the institution's activities and role in the Region while safeguarding its extremely strong financial profile. Net income for the year reached EUR 5.2 million, the 14th consecutive year that the Bank has achieved a net profit.

As important as the operational achievements were, they were backed by other institutional achievements which helped the Bank advance its central purpose and lay the ground for continued development. In July, the Bank's Annual Meeting of the Board of Governors was held in Sochi, Russia, accompanied by a successful Business Forum that was well attended. Over the second half of 2018, the Bank executed a smooth rotation of upper Management, with new Vice Presidents of Banking, Finance and Operations joining the new Presidency for the coming four-year period. The new Management, with the input of the Bank's staff, and following extensive consultation with the Bank's Member State shareholders, prepared and received for a new Medium-Term Strategy and Business Plan (MTSBP) for the 2019-2022 period. The new MTSBP, approved by the Board of Governors in February 2019, intends to build upon the excellent financial profile of the Bank to expand operational activity and to achieve higher development and regional cooperation impact in its operations.

Ten years removed from the global financial crisis, the Black Sea Region has settled upon a stable economic model of growth that seeks to minimize economic vulnerabilities, even if the effort to do so comes at the expense of growth. The countries have succeeded in achieving stability and have greatly expanded their capacity to withstand shocks and sudden turns in market sentiment. However, in doing so there is an ever-growing gap in investment needs in order to increase future potential economic growth and to sustain the effort to converge towards the living standards of the most developed countries.

Development institutions have an important role, and indeed a responsibility, to work towards filling this gap. Perceptions of regional risk play a key part in sustaining the observed under-investment, and in this respect, the Black Sea Trade and Development Bank and the other development finance institutions active in the Region have an ever-relevant task, as well as a growing duty to fulfill, to use the connections, the experiences, the tools, and the privileges they possess to mobilize more financial resources for the benefit of the Region's economies while also introducing risk mitigation solutions and innovative ideas and products.

Dmitry Pankin
President
Chairman of the Board of Directors

Highlights of 2018

- In 2018, the last year of the implementation of the Medium-Term Strategy and Business Plan for the period of 2015-2018, BSTDB outperformed the lending target with total loans outstanding amounted to EUR 1.36 billion (the target was EUR 1.29 billion). Over the strategy period, direct lending has increased, signifying a focus on value-added project lending. The Bank's portfolio has become more diversified and balanced by sector and geography. Although financial institutions continued to be the Bank's largest single sector exposure, the level of the real sector financing increased to over 60% of the portfolio, most significantly to the sectors with clear relevance for economic growth, such as industrials (13%), public utilities (12%), energy (11%), materials (8%), and consumer staples (8%).

- In 2018, the Board of Directors approved a record EUR 569.7 million in new operations, which represents a 61% increase over the Strategy period since end-2014. During the year, the Bank signed 30 loan agreements for EUR 617.9 million, an increase of close to 300% compared to 2014. Disbursements to business clients in member countries reached EUR 573.8 million in 2018, close to 90% increase over the period. These operational achievements occurred as non-performing loans declined to one operation accounting for around 0.32% of the portfolio. The Bank registered a positive net income for the fourteenth consecutive year.

- The targeted more balanced geographical portfolio distribution has been achieved most notably with a dramatic increase in the Bank's financing in Greece, which came in response to the country's particularly difficult years of economic and financial crises. In 2018, Greece became the second largest BSTDB client to account for nearly 15% of the outstanding portfolio, up from under 5% at end-2014. BSTDB's participation in the project to modernize 14 Greek regional airports by Fraport Greece received the 'Deal of the Year' European Award by the Project Finance and Infrastructure Journal. The Bank's participation of over EUR 62 million in the project was its largest single investment to date.

- BSTDB expanded its lending facilities in national currencies of Member States through issuing local currency bonds. In 2018, the Bank issued a GEL 120 million bond in Georgia, the largest public corporate bond issued in the country that year.

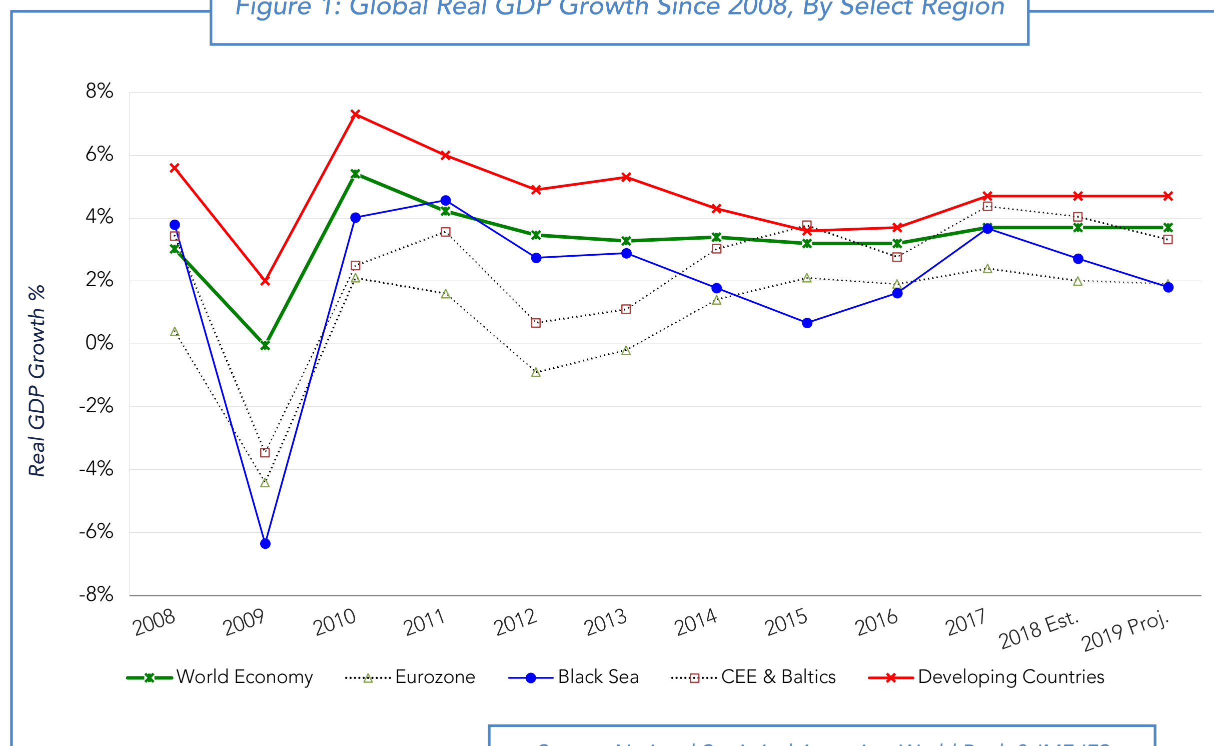
- In 2018, the Bank led the effort by a group of international lenders resulting in the restructuring of a major healthcare provider in Albania and the creation of an integrated healthcare company with over 2,300 employees.

- In 2018, the Bank made a major breakthrough with its social media presence. The number of BSTDB's followers across Facebook, Twitter and LinkedIn surged almost two-fold during the year, while the Bank's content received over 3.2 million impressions, thus becoming an increasingly important 'voice' in the Black Sea Region.

Economic Overview of the Black Sea Region in 2018[1]

Economic growth in the Black Sea Region[2] in 2018 was positive, but relatively modest compared to other regions globally and the overall world economy. It also marked a slowdown relative to its performance in 2017. Real GDP growth in the Region slipped to an estimated 2.7%, down from 3.7% the year before. While this represents a year-on-year slowdown, it was better than the rates achieved during the regional slowdown of 2014-2016 and suggests that the Region remains on a path of growth, albeit with fluctuations from year to year that highlight the impact of various negative, and for the most part, exogenous factors.

Figure 1: Global Real GDP Growth Since 2008, By Select Region



Source: National Statistical Agencies, World Bank & IMF-IFS

Figure 1 shows how the Black Sea Region compares to the world economy and select comparator regional groupings. The 2.7% outturn was well below the global economy's growth of 3.7%, as well as the 4.7% growth achieved by developing economies which were the principal drivers of global growth. In this respect, the Region was much closer to the 2.4% growth outturn for advanced economies. The European Union, and more specifically the Eurozone common currency area, experienced a slowing in economic activity in 2018 relative to 2017. Given the close economic ties with the Eurozone, which represents the Black Sea Region's principal source of financing and investment as well as its largest trading partner, the observed slowdown in the Black Sea is unsurprising.

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* reports of the World Bank, and the IMF's *World Economic Outlook* publications (and their updates) and the Economist Intelligence Unit. As many figures at the time of writing represent estimates for 2018, actual final figures may differ in detail, but the overall trends discussed in this section will not be altered.

2 Comprised of the 12 member countries of the Black Sea Economic Cooperation (BSEC): Albania, Armenia, Azerbaijan, Bulgaria, Georgia, Greece, Moldova, Romania, Russia, Serbia, Turkey, Ukraine.

Regional economic activity was further hurt by other external factors. Increases in interest rates by the US Federal Reserve created turbulence in emerging markets, with already edgy financial markets concerned that firms with large levels of external debt and in countries with current account deficits might face difficulties meeting their debt obligations. This created self-fulfilling turmoil. Investors, fearing economic prospects, were thus taking money out of markets perceived as vulnerable; currencies in those countries were coming under depreciation pressure; anti-growth measures such as interest rate hikes were being undertaken (to mitigate depreciation pressures); many firms were left with increased burdens and reduced access to financing; and investors feared rising defaults and sharply declining economic prospects.

Another factor hurting growth was the imposition of sanctions, and in some cases, the mere threat of the imposition of sanctions, mainly as an outgrowth of various geopolitical disputes. This greatly increased global uncertainties and had a detrimental effect on trade flows as well as foreign direct investment and other forms of cross-border financing. It was further exacerbated by the increasing tendency of the US to take advantage of the ubiquitous reach of the dollar as a global reserve currency, threatening banks, firms and countries with severe penalties if they did not comply with US policy priorities.

Global turbulence thus impacted the Black Sea Region negatively, and put a brake on the two-year upswing in economic growth that peaked in 2017. Moreover, the 2.7% real GDP growth rate fell short of the 4.0% growth rate posted by the Central and Eastern European and Baltic states ('CEE & Baltics')[3], most of whom joined the European Union in 2004 and, as former 'transition' countries, represent a source of comparison to the countries of the greater Black Sea Region. For the fifth year running, the CEE & Baltics achieved higher growth than the countries of the Black Sea Region. Out of all emerging market regions globally, only Latin America and the Caribbean (1.7%), still recovering slowly from its protracted 2015-2016 recession, posted lower growth outturns.

While the Black Sea Region's outturn appears unexceptional, it contained a number of positive aspects. The growth was balanced in terms of geography, sector of origin, and type of expenditure. In contrast to the previous five years, in which the western part of the BSEC Region enjoyed substantially higher GDP growth than the eastern part of the BSEC Region, in 2018 the growth rates converged substantially, with the western part growing at 3.2% and the eastern part at 2.4%. Furthermore, Table 1 shows that all BSEC countries posted positive real GDP growth rates for 2018. This across-the-board positive growth was achieved for the second consecutive year, the first such two-year sequence since 2006-2007, just before the onset of the 2008 financial crisis. As the table shows, only two countries achieved relatively high GDP growth in excess of 5.0%, and most country outturns were fairly close to the regional average.

3 EU members since 2004: Czech Republic, Estonia, Hungary, Latvia, Lithuania, Poland, Slovakia, Slovenia; and Croatia, which joined the EU in 2014.

Table 1: Summary of Key Economic Indicators for 2018, by BSEC Member Country

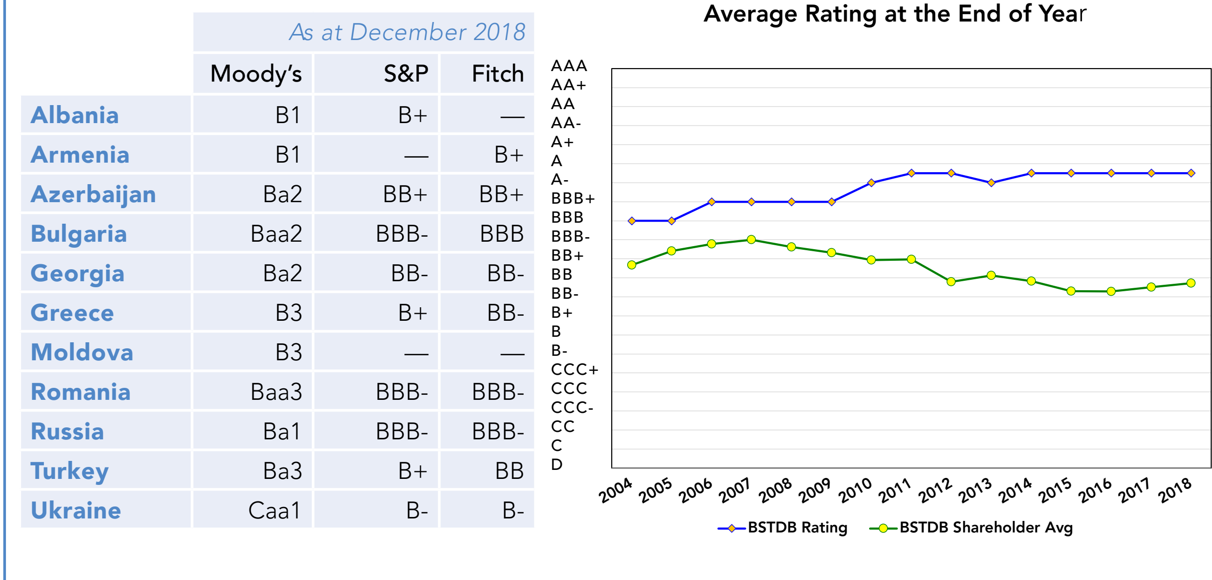
	Real GDP Growth	Inflation	Cur Acct Bal / GDP	Budget/ GDP	Public Debt/ GDP	FDI/ GDP
Albania	4.3%	2.0%	-6.2%	-1.6%	71.0%	7.5%
Armenia	5.3%	3.2%	-5.4%	-2.8%	52.5%	2.3%
Azerbaijan	1.4%	2.3%	12.9%	5.6%	20.7%	14.9%
Bulgaria	3.3%	2.8%	4.5%	0.5%	23.3%	3.1%
Georgia	5.2%	2.6%	-11.0%	-2.8%	45.7%	10.8%
Greece	2.1%	0.6%	-1.9%	-0.1%	188.1%	2.0%
Moldova	4.0%	3.0%	-10.5%	-0.85%	30.5%	2.1%
Romania	4.3%	4.6%	-4.5%	-3.0%	37.2%	2.9%
Russia	2.3%	2.9%	6.5%	2.7%	15.3%	0.9%
Serbia	4.4%	2.0%	-5.1%	0.4%	58.8%	5.9%
Turkey	3.1%	16.3%	-4.5%	-2.0%	32.3%	1.2%
Ukraine	2.9%	10.9%	-4.3%	-1.9%	70.5%	2.4%
BSEC Region	2.7%	6.3%	1.7%	0.7%	36.8%	1.7%

In terms of sector of origin, services -which account for around 60% of GDP- grew at an estimated 2.8% for the year; industry -which accounts for 34% of GDP- increased by a slightly lower 2.2%; and agricultural -which accounts for the remaining 6% and is generally more volatile from year to year- grew at a more modest 1.0%. On the demand side, one key positive contribution was that exports grew by an estimated 17.6%, while imports increased 6.6%. Interestingly, this strong growth in international trade defied the slowing overall global trend.

Private consumption remained the largest and most consistent source of expenditure. Making up 58% of total outlays, it increased by 2.9% in 2018. By contrast, gross fixed investment, which accounts for 22% of expenditure, grew by a disappointing 2.4%, down from nearly 6% in 2017 and continuing a post-2008 crisis pattern of generally lackluster investment. Government consumption, which makes up 16% of GDP, also grew more slowly at 1.4% for the year, although this highlights the ongoing fiscal consolidation in the Region and the fact that most countries have been restraining expenditures while seeking to bring down both general government budget deficits and public debt levels.

Table 1 summarizes how BSEC Member States on the whole have remained dedicated to the achievement of stable, healthy macroeconomic indicators, quite likely to the detriment of higher growth, especially in the short term. In spite of the occasional outlier, on the whole, countries have worked hard to achieve and sustain low, single-digit inflation, stable or declining current account and fiscal balances, as well as moderating public debt levels. As the next section of this chapter analyzes, this represents a legacy of the 2008 financial crisis. One decade removed from that traumatic event, key lessons observed by all countries include (i) reducing external dependence and potential vulnerability, and (ii) the overriding importance of not just achieving stability, but demonstrating that the economy is positioned to ride out potential turmoil on its own, without needing to resort to external sources of financing.

Figure 2 shows another reason for this lingering emphasis on continued macroeconomic discipline, even if it is to the detriment of growth. While key macroeconomic indicators have improved and remained strong even during the frequent periods of global economic turmoil, regional credit ratings, as perceived by the three main credit rating agencies, have remained at low levels in the post-crisis period.



	As at December 2018		
	Moody's	S&P	Fitch
Albania	B1	B+	—
Armenia	B1	—	B+
Azerbaijan	Ba2	BB+	BB+
Bulgaria	Baa2	BBB-	BBB
Georgia	Ba2	BB-	BB-
Greece	B3	B+	BB-
Moldova	B3	—	—
Romania	Baa3	BBB-	BBB-
Russia	Ba1	BBB-	BBB-
Turkey	Ba3	B+	BB
Ukraine	Caa1	B-	B-

Figure 2: Regional Credit Ratings at end 2018 & Average Evolution Over Time

The right-hand chart shows the course of the average weighted credit rating of Black Sea countries since 2004, and compares it to the evolution of the average credit rating of the Black Sea Trade and Development Bank. These ratings compare especially poorly with many western European countries that are wealthier on a per capita basis, but which possess much higher debt levels, fiscal and/ or current account deficits and other indicators of potential concern. The upward trend in the chart does show that upgrades exceeded downgrades in 2017 and 2018, but even so the Region's average credit rating remains more than two notches below the BBB- average reached in 2007. Rating agencies have continued to place sub-investment grade credit ratings to all but three Black Sea economies and have been slow to recognize the improved resilience of the Region's economies and the sustained consistency of macroeconomic policies. Downgrades during periods of turmoil have come quickly, whereas upgrades have been much slower, even during periods of sustained positive performance.

Such caution entails real costs for the economies, in terms of access to, and cost of financing, and the overall perception that exists about the health of the economies. Rating downgrades also often set off, or aggravate, economic turmoil such as capital outflows, increased risk premiums, depreciation pressure on the domestic currency, greater dollarization of the economy, etc.

Excessive concern about the impact of potential downturns, lingering risk aversion, and a general edginess and sense of uncertainty are relics of the 2008 global crisis, and have proven difficult to overcome despite the considerable achievements of the Region over the past decade. This merits an examination of how the Black Sea Region has changed - and has been changed - during this period.

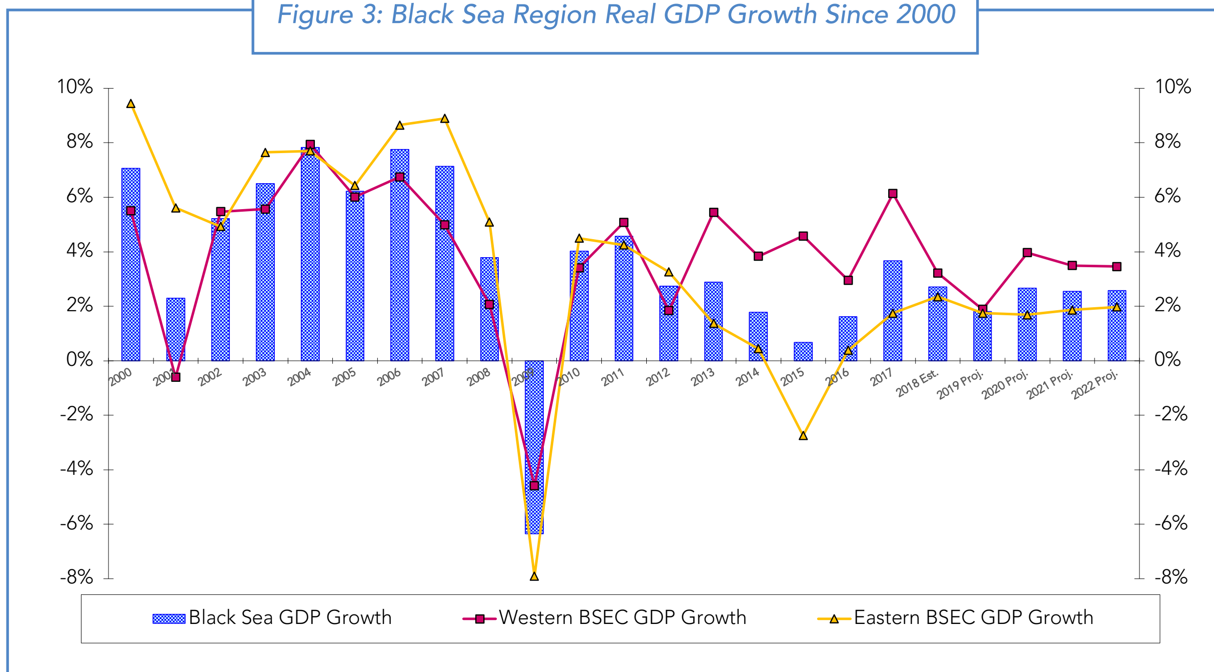
The Black Sea Region One Decade Removed from the Crisis

September 2018 marked the tenth anniversary of the global financial crisis that broke out in the aftermath of the bankruptcy of the investment bank Lehman Brothers in September 2008. The global financial system suffered a near meltdown as markets panicked and lending seized up. To prevent total collapse, governments were forced to undertake large scale interventions in support of their respective financial systems. The type of intervention varied from country to country, but all involved the use of public financing in order to support or bail out financial institutions that normally were deemed to operate in a commercial environment. The aid provided was expensive, politically unpopular, perceived as rewarding irresponsibility, and viewed as favourable to the wealthy as opposed to the poor; however, these interventions by and large succeeded in stemming the panic and preventing the collapse of financial systems.

Figure 3 shows the negative impact of the financial crisis on economic activity. Beginning in the last quarter of 2008 and extending through most of 2009, the global economy went into recession, with global GDP contracting by -0.1% in real terms. For the most part, the growth outturns were much worse in the developed world than in the developing world, and emerging markets as a whole remained in positive territory, with real GDP growth slowing to 2.0%. An important exception to this was Emerging Europe, and even more specifically the Black Sea Region, which experienced a real GDP contraction of -6.3%, the worst performance of any region globally.

This severe reversal brought to a sudden end a lengthy stretch of impressive economic growth dating back to 2000. Black Sea countries experienced a prolonged period of robust growth from 2000-2008, with regional GDP growth rates averaging 6.0% on an annual basis. Every country posted positive growth rates in every year from 2002 to 2008, and during this period, incomes and living standards rose while poverty rates declined substantially. In the early part of this growth cycle, productivity gains and rising investment levels contributed primarily to the growth, whereas in the latter part, consumption dependence grew, with rapid credit growth driving a good portion of the increase. As a result, many regional economies reached a stage where they were overheating, having (i) pursued pro-cyclical fiscal policies, (ii) experienced rising wages, asset prices, and consumer price pressures, and (iii) increased private sector borrowing levels from abroad, which in turn fed rising current account deficits.

Figure 3: Black Sea Region Real GDP Growth Since 2000



With the freezing of global financial markets in September 2008, the flow of financing to the Black Sea Region stopped. Private firms and banks, but also governments, suddenly found themselves unable to refinance their external exposures and faced the prospect of default. In other words, many entities were dependent upon continued foreign flows in order to finance accrued deficits and debts, but were unable to access financing.

This inability first affected the more globally integrated countries. These countries tended to rely more on foreign financing, as well as tended to have stronger commercial and investment links externally, particularly with the countries of the European Union (EU). The economic contraction in the EU sharply reduced foreign demand for exports from the Black Sea, a situation further exacerbated by the decline in commodity prices which struck resource-rich and commodity-dependent countries, deteriorating their terms of trade. In these countries, economic recession took hold quickly.

The less globally integrated economies soon followed. These were smaller and more isolated economies, with lower levels of international trade and less contact with global financial markets. As they were also poorer, they had large emigrant populations working abroad - in neighboring countries as well as other EU countries - upon whose remittances they depended. When the more integrated economies suffered recessions and an increase in unemployment, remittance flows fell, forcing the economies of labor-exporting countries deeper into recession.

Another reason for the -6.3% contraction was the limited availability of policy responses in most countries. In most of the EU, public spending increased in order to reduce the impact of the reduction in credit availability and the resulting decline in private consumption and investment. The increase occurred via discretionary spending as well as the onset of automatic stabilizers (e.g. unemployment benefits) in order to offset, to some degree, the decline in private activity.

The institution of such counter-cyclical policies presumes access to the necessary additional resources, normally either the drawdown of reserves, or increased borrowing. For the most part, Black Sea countries had limited recourse to these options, and were thus left with fiscal cutbacks as the principal available policy. Government spending was constrained by the lack of access to additional resources, and thus public spending cuts exacerbated the recession caused by reduced private spending. Ironically, fiscal deficits also rose, mainly due to lower tax receipts from the reduced economic activity.

Fortunately, the recession in most countries was short-lived, and by the second half of 2009, a robust bounce-back had begun. As the global economy recuperated, so did most Black Sea economies, in certain cases very dynamically through 2010 and 2011. External trade flows were boosted by a general rise in commodity prices, while private domestic demand also recovered strongly. Regional GDP grew 4.0% in 2010 and 4.6% in 2011 in real terms. However, an emerging series of destabilizing events impacted the global economy and enhanced risk aversion towards emerging markets. These included lingering financial market uncertainties, as well as the natural disasters in Japan; the Arab Spring and its aftermath; and most importantly, the Eurozone crisis which led to a downswing in the Eurozone region and significant turmoil in financial markets.

The Eurozone's recession quickly translated into slowing economic activity in Black Sea countries, as regional GDP growth fell to 2.7% in 2012, with a much more pronounced decline in western BSEC countries - those that are either EU members already or which have developed close institutional and economic ties as a result of the prospect of potential membership - than in eastern BSEC countries, which continued to enjoy favorable conditions due to high commodity prices. Figure 3 shows how western BSEC countries grew only 1.8% while eastern BSEC states grew by 3.3%.

By 2013, however, this situation had reversed. On the one hand, a recovery in EU markets, together with the European Central Bank's programs of quantitative easing, led to a resurgence of economic activity that lifted western BSEC as well. On the other hand, eastern BSEC experienced slowing due to weakening commodity prices, particularly for energy, and uncertainties in financial markets created by expectations for US monetary policy shifts and the sharp appreciation of the US dollar, which in turn put downward pressure on most domestic currencies, increased the value of foreign denominated debt (whether publicly or privately held), and exacerbated the high degree of dollarization of the economies. Thus, while overall regional growth rose slightly to

2.9%, the western BSEC states posted vigorous growth of 5.4% while the eastern BSEC countries slowed to 1.4%.

This pattern of divergent growth continued in 2014 and 2015, with overall real GDP growth rates of 1.8% and 0.7% hiding the wide gap within the Region which saw western BSEC growing 3.8% and 4.6% respectively, while eastern BSEC slipped to 0.4% GDP growth in 2014 and experienced a -2.7% contraction in 2015.

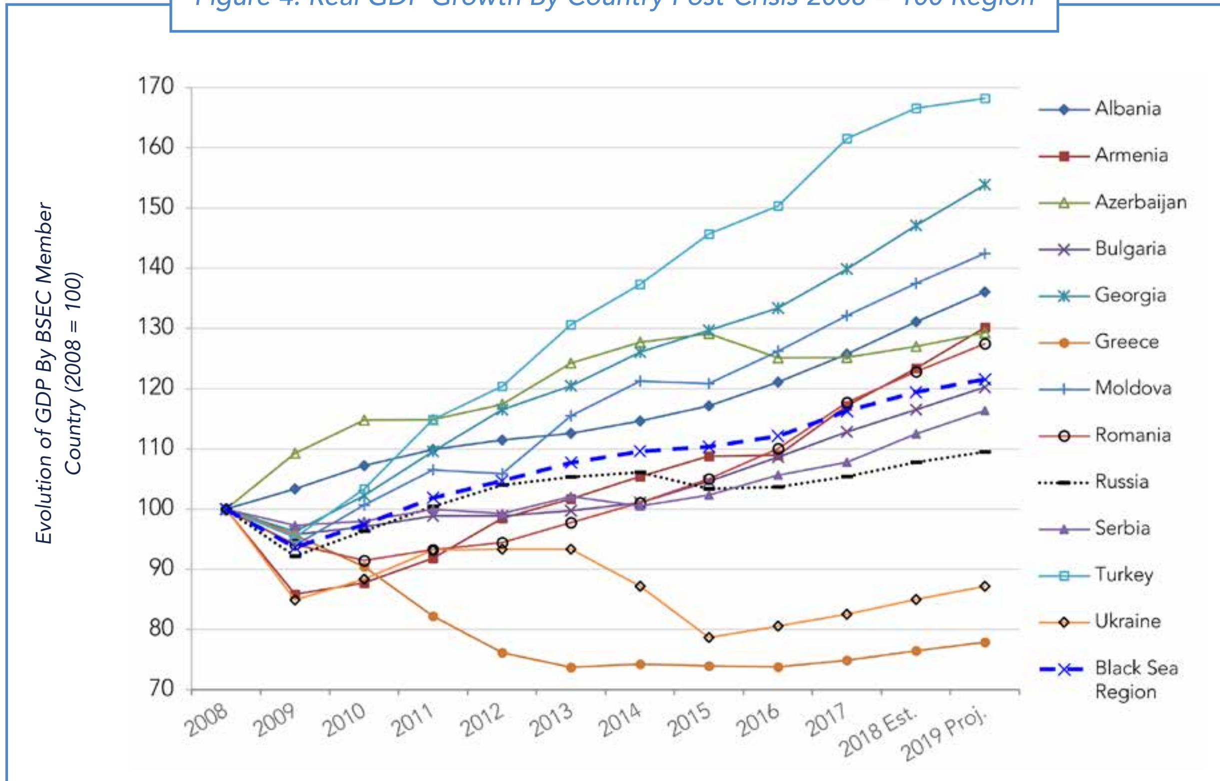
Regional performance improved in 2016, mainly as a result of an upswing in eastern BSEC countries, which posted modest, but positive real growth of 0.4%. The western BSEC states slowed to 3.0% and overall regional growth reached 1.6%. The recovery gathered speed in 2017 and continued, albeit at a more moderate pace, in 2018. For 2017, regional GDP jumped to 3.7% and growth distributed across the board. All BSEC countries posted positive growth rates for the first time since 2007, with the western countries leading with 6.1% growth and the eastern countries posting 1.7%. The Black Sea Region overall grew 2.7% in 2018, with the western part growing at 3.2% and the eastern part at 2.4%. Alongside this increased convergence in performance, all countries posted positive growth rates for the second consecutive year.

Taking stock of the ten years since the 2008 crisis, a more complex and nuanced picture emerges. One obvious conclusion is that economic growth has been much lower post-crisis than it was pre-crisis. Real GDP growth in the Black Sea Region averaged 2.7% per annum between 2010-2018, a number which is less than half the 6.0% average annual real GDP growth that the Region experienced from 2000-2008. On a compound basis, this means that the Region's economies grew only 27.5% post-crisis, whereas they grew 68.5% during the pre-crisis boom. With the sole exception of Turkey, which has enjoyed robust growth post-crisis as well, all Black Sea countries have posted lower average rates of growth post-crisis than they did pre-crisis.

This means that regional convergence with the income levels and standards of living of advanced global economies slowed considerably. Similarly, unemployment rates and poverty rates rose and have remained stubbornly high in certain countries, while the rate of poverty reduction also slowed and in certain countries poverty rates have increased significantly. Economic decline - and uncertainty - have had a negative impact on demographic trends as well, which were already challenging in a number of countries, with emigration and the continued 'brain drain' phenomenon particularly problematic.

While there has been growth, it has been very unevenly distributed. Figure 4 shows how each BSEC member country has fared post-crisis, taking 2008 as the base year. Two countries have yet to return to pre-crisis levels of economic activity. All the others have exhibited growth, but with broad variance from case to case. Moreover, as already discussed, there has been a divergence in the growth trend of western BSEC members versus eastern BSEC members, particularly between 2012-2017, as they appear to follow different business cycles. However, this is not absolute, and there have been notable exceptions like Georgia, which has posted some of the highest post-crisis growth rates (although they are still lower than the boom-period rates achieved). Uniquely, Albania is the only country to not experience an economic contraction in any single year during this period, as it has posted positive GDP growth every year since 1997.

Figure 4: Real GDP Growth By Country Post-Crisis-2008 = 100 Region



With all BSEC countries having posted positive GDP growth in 2017 and 2018, and projected to continue doing so in 2019, it appears that the Member States have put the crisis behind, and that a new 'normal' seems to be emerging. This unfolding situation appears to be one of slower but steady growth, based upon a solid economic foundation.

Closely correlated to the lower post-crisis growth, investment rates in the Black Sea Region have lagged during 2010-2018. Gross fixed investment (GFI), which accounted for around 22% of GDP expenditure in 2018, is perhaps the most significant indicator of current and future economic activity. GFI contributes to current economic output but is also a key lead indicator of future activity, the prospects for creation of wealth and potential rates of growth in coming years, and confidence in future economic prospects. Investment is a necessary precondition for further growth, and during the 2000-2008 period, it grew at an average annual rate of 12% across the Black Sea Region, exactly double the overall average rate of regional GDP growth during that period. During the sharp recession of 2009, regional GFI contracted drastically by -19%. GFI did bounce back subsequently, and during the 2011 bounce-back grew at a pre-crisis like 15%, but Region-wide it has grown at appreciably lower rates between 2010-2018. Average annual investment growth fell to 3.8% during this period; investment has been volatile and uncertain, with considerable fluctuation from year to year, and has remained very low, at levels less than one third from those reached during the boom period.

Another important legacy effect of the crisis is the determination of countries not to leave themselves vulnerable to the causes of the 2008 crisis, and in particular to those factors which exacerbated the economic downturn. Since countries that were deemed to be overheating suffered bigger downturns than those which were not, those indicators which directly or indirectly gauge degrees of overheating are those which have received the most attention. These include indicators of external balance such as the current account - and more specifically, whether and how much it is in deficit, levels of foreign exchange reserves, and extent of foreign currency borrowing (both public and private). They include indicators of fiscal health such as the central government budget deficit, and public debt levels - further sub-divided into foreign versus local currency debt; questions about who owns the debt (domestic or foreign actors, private or official sector creditors); the average term of the debt; spikes in repayments, etc. Debt in particular is parsed and scrutinized more than ever. The indicators also include monetary markers such as nominal and real

interest rates, inflation, as well as financial measures related to size of the financial sector, growth of lending, and loan impairment.

This extensive list is not exhaustive and merely highlights the post-crisis sensitivity to ensuring that key indicators are steady, stable or at worst trending in the direction of improved balance. By and large, it has successfully been implemented. In other words, Black Sea countries have implemented prudent fiscal, monetary and other policies that have aimed to enhance their economic standing and mitigate fears of potential weaknesses. As a matter of policy, they have been committed for years to eliminating imbalances, reducing vulnerabilities, increasing hardiness and establishing a solid basis for growth, exercising sensible and pragmatic policies over the elements of economic policy that they control. The dedication to maintaining a solid macroeconomic foundation also reinforces their demonstrated ability to undertake difficult measures and politically unpopular reforms in order to restore and maintain economic health.

Ten years removed from the crisis, in 2018 the risk of endogenous shocks to the Region's economies stands at a historically low level. While the Region's resilience is greatly improved, and it currently, by and large, is growing upon solid, stable foundations, the risk of externally generated shocks remains. If anything, exogenous risks have increased in scope and complexity, and there is a growing array of financial and geopolitical risks that could affect the global economy, and consequently filter down to advanced and developing economies including the Black Sea Region.

Reduced vulnerability and lower rates of investment and growth seem to be the new emerging state of affairs in the Black Sea Region. Investment flows have been among the biggest casualties of the crisis, despite the resilience which regional economies demonstrated, as well as their demonstrated dedication to the exercise of prudent fiscal and monetary policies and the implementation of reforms to improve the business environment and consolidate stability.

These characteristics may not be universally applicable to all countries, but they do hint at the type of economic model of growth which has evolved in the post-crisis period. There has been much debate in recent years about what sort of economic model the countries of Central and Eastern Europe - BSEC countries but also the Central European and Baltic States that joined the EU in 2004 and western Balkan states neither in the EU nor BSEC - would follow in order to pursue growth in the post-crisis period. During the 2000-2008 boom period there was clearly a predominant economic model in which growth was fueled by plentiful external financing, which was used both for investment and consumption. As previously discussed, over the course of this period there was a shift from investment towards greater consumption, and this contributed to the eventual overheating that left economies exposed.

Characterizing the post-crisis period is more difficult as there is no universal model that is applicable across the board, but there does appear to be an emerging strategy of economic growth that possesses common characteristics across countries. Reducing external vulnerability while seeking to enhance domestic capacity to fuel growth is one such pattern. The emphasis on achieving and maintaining solid macroeconomic indicators is one consequence of this. It appears often to have taken priority over pushing for greater growth - in other words, the lower growth is in many ways a consequence of the priority given to reducing vulnerability. Since factors such as current account deficits and external lending were viewed as sources of vulnerability, the imperative to reduce these necessarily meant utilizing less external financing to finance domestic growth. Instead, much was made about increasing domestic sources of financing.

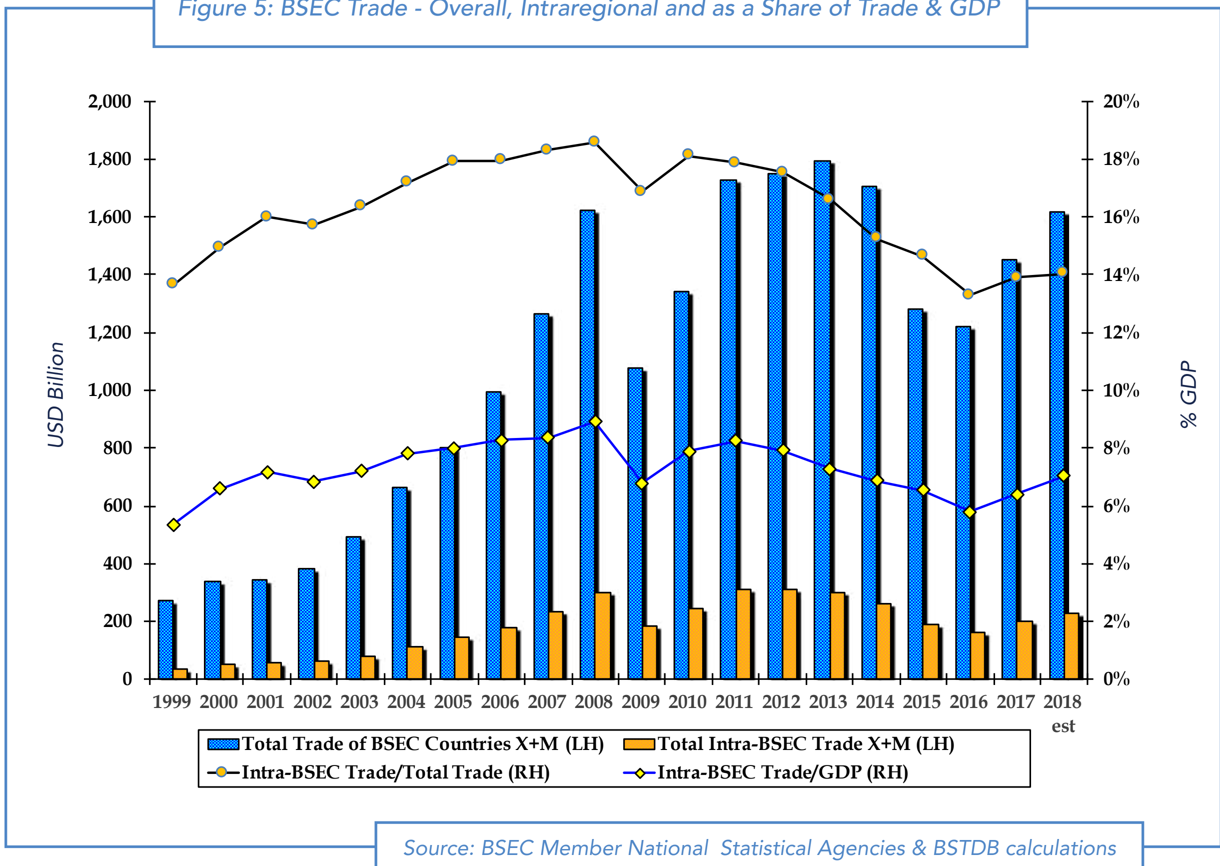
The financial systems of Black Sea economies have grown substantially over the last two decades in terms of sophistication, depth, and size. Furthermore, governments have strengthened these systems, to make them more resilient to external shocks, and ultimately to enable them to play a greater and more stable role in financing investment. The efforts have generally been successful, and most financial systems are on far more solid ground than they were a decade ago, having achieved consolidation, higher capital requirements for banks, and more rigorous and effective regulation. Challenges remain, however, including legacy effects of the crisis such as high lingering levels of non-performing loans, and a continued sense of uncertainty that translates into risk aversion and reduced lending. In addition, regional financial systems remain small relative to the size of the economies in which they operate, implying that domestically mobilized financial resources remain insufficient to support

the required levels of investment to achieve high and sustained growth. Consequently, if Black Sea Region economies are to achieve high rates of growth, they will need to rely upon external financing.

While development of the domestic financial sector is desirable, it is necessarily a slow process that must evolve gradually in order to build capacity as well as credibility. Without confidence, no financial sector can develop effectively, and while it can be lost easily, it can only be built step by step over time with measures and policies which demonstrate to the private sector that the system is well and fairly regulated, stable, and with promising prospects.

In the meantime, reducing external exposure risks by reducing external financing flows translates into lower growth. Greater resilience and stability have been achieved at the expense of investment and growth. Reliance on external financing has declined, but at the cost of economic activity foregone. Exceptions to this emerging model persist, but interestingly they serve to underscore the issue of opportunity costs from sacrificed growth. The two countries which have experienced the highest post-crisis growth, Turkey and Georgia, are also the two countries which have been most open to continued receipt of external financing and which have posted the highest average investment rates over the 2010-2018 period. Lost investment, and hence current and future potential growth, is a significant 'cost' of the greater 'safety' offered by lower vulnerability and less exposure to external financing.

Figure 5: BSEC Trade - Overall, Intraregional and as a Share of Trade & GDP



Source: BSEC Member National Statistical Agencies & BSTDB calculations

An additional consequence of the reduced reliance on external financing is, unsurprisingly, lower levels of cross-border activity and cooperation. Not only are financing and investment lower, so is international trade, and more generally the interest and willingness in international cooperation and multilateral participation. As countries have looked inward, and sought to increase their degree of self-reliance, the international dimension of their activity has inevitably suffered.

From 1999 to 2008, BSEC international trade increased sixfold from USD 270 billion to over USD 1.6 trillion, as Figure 5 shows. The financial crisis induced collapse in international trade in 2009 brought a 34% drop to under USD 1.1 trillion. With the subsequent economic recovery, trade picked up fairly rapidly, and peaked at USD 1.8 trillion in 2013, on the back of high commodity prices - particularly those for energy. When commodity prices then softened, trade began to trend downwards and was aggravated by the emergence of geopolitical conflicts that led to the imposition of sanctions and countersanctions directly affecting the BSEC Region which hindered trade flows from 2014-2016. This downtrend reversed in 2017, as the global economic growth accelerated and the Region recovered from its downswing.

Interestingly, up to 2017, regional external trade followed general trends in global commerce, particularly those with respect to emerging markets. Initial indications are that the BSEC Region, despite its slower overall economic growth in 2018, bucked the slowdown observed in global trade in 2018, and has continued a second post-crisis recovery back above the USD 1.6 trillion level.

Trade within and among the BSEC Member States was, and remains, fairly low compared to other regions of Europe, e.g. the Baltics or the Mediterranean EU states, both in absolute terms and as a share of overall economic output. Figure 5 shows that from a very low base, intra-regional trade in the BSEC region has mirrored the general trend in international trade of BSEC Member States, but at somewhat higher rates. Thus, as international trade grew from 1999-2008, so did intra-BSEC trade, and in fact at a rate that exceeded overall international trade growth of Black Sea countries and GDP growth, as shown by the rising lines for intra-BSEC trade as a share of overall trade and as a share of GDP respectively. At -40%, the decline in intra-regional trade in 2009 was bigger than the -34% in overall trade. Moreover, intra-regional trade, both relative to GDP and to overall trade has generally followed a declining trend in the post-crisis period up through 2017.

In other words, even as overall international trade activity of BSEC Member States has generally declined (with the exception of 2017-2018), trade among the BSEC countries has dropped at an even faster rate. This disappointing drift represents unrealized economic activity and another significant opportunity cost for the Black Sea Region, since regional trade benefits neighboring economies in many ways, creating win-win prospects for their firms and for consumers. The proximity of countries reduces transport costs and increases familiarity and local knowledge of a market. This has the benefit of creating closer economic links among neighboring countries, increasing familiarity and creating greater interdependence and trust. Furthermore, past crises have demonstrated that relations among neighbors tend to be more stable and less susceptible to sudden changes in global risk perceptions, as proximity breeds greater familiarity and closeness, reducing shifts in risk aversion.

In addition, the small and medium size of the vast majority of regionally based firms allows for quick and flexible decision-making to adapt to changing circumstances as well as considerable room for promising firms to develop the necessary economies of scale that can dramatically improve their competitiveness and allow them to expand beyond the BSEC Region into new export markets. In short, with international commerce affected by unpredictable exogenous factors such as commodity prices, reserve currency monetary regimes, tendencies towards sanctions and other trade restrictions, and overall economic conditions, increasing the level of regional trade among neighboring states offers a significant opportunity to buffer against downturns, develop closer ties, improve competitiveness, and stabilize economic activity.

Taking advantage of this regional effect will require containing, if not reversing, the post-crisis mindset that emphasizes maintaining stability, even if it comes at the high cost of foregone growth. At its core, international cooperation is about opening up and putting greater trust in working with external partners. When successful, it creates a self-propagating virtuous cycle that benefits all parties, generating new wealth and conferring improved living standards. When, in 2008, international markets seized up and many countries - along with their agencies - banks, firms and agencies- found themselves frozen out of markets and without any access to continued financing that had been plentifully provided under benign conditions, the trust required to maintain such relationships dissipated and everyone felt as though they were left to fend for themselves. The subsequent situation of cheap and vast levels of liquidity provided by central banks on the one hand, but lenders unwilling to extend financing to many parties on the other hand (unless they were low-risk highly-rated sovereigns or blue chips) generated an understandable reaction on the part of previous borrowing parties about not wishing to put themselves in such a position.

Hence the new growth model putting a premium on vulnerability reduction appears to have emerged. It has not completely supplanted the externally financed fuel growth of the previous decade, but it has certainly taken hold in a number of countries. Even in countries which have continued to rely to a large degree on externally financed growth, greater attention is paid to reducing, limiting, or if possible eliminating vulnerabilities to avoid a repeat of the overheating and subsequent sharp contraction observed in late 2008 and 2009. It is a model that requires less trust among parties, and while it may have brought greater resistance and resilience, it has reduced the level of trust and the risk appetite that are required for increased international cooperation and faster economic growth.

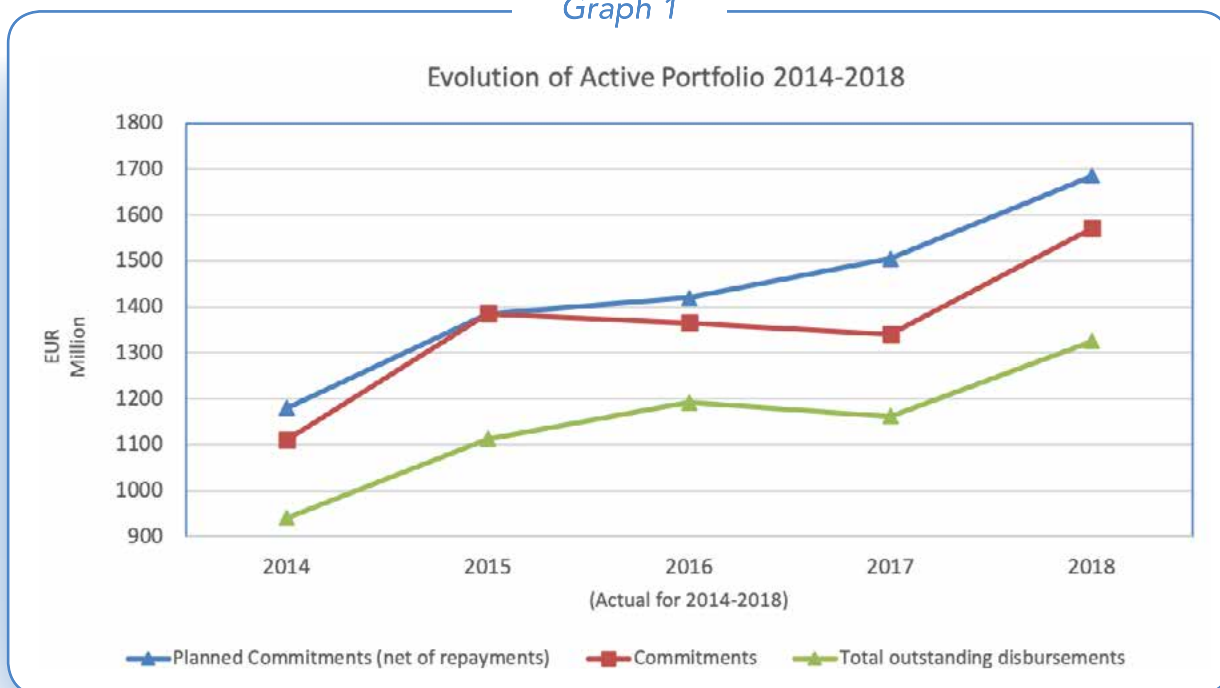
BSTDB in the Black Sea Region

In Focus: Performance Summary of the Mid-Term Strategy and Business Plan 2015-2018

During the 2015-2018 period, BSTDB took advantage of a benign market environment, and growing demand for its products in spite of geopolitical vulnerabilities and proximity drawbacks. Consequently, the Bank's portfolio of operations expanded in terms of signed operations (a.k.a. 'Commitments') in line with the high case scenario forecast of its Board approved Mid-Term Strategy and Business Plan (MTSBT) and medium-term update.

After a robust beginning in 2015 and 2016, the overall level of the outstanding portfolio lagged relative to targets and even declined in 2017, before picking up strongly, in particular in the second half of 2018. Ultimately, the value of the Bank's portfolio of outstanding operations exceeded by a comfortable margin the medium-term strategic target, as shown in the following graph:

Graph 1



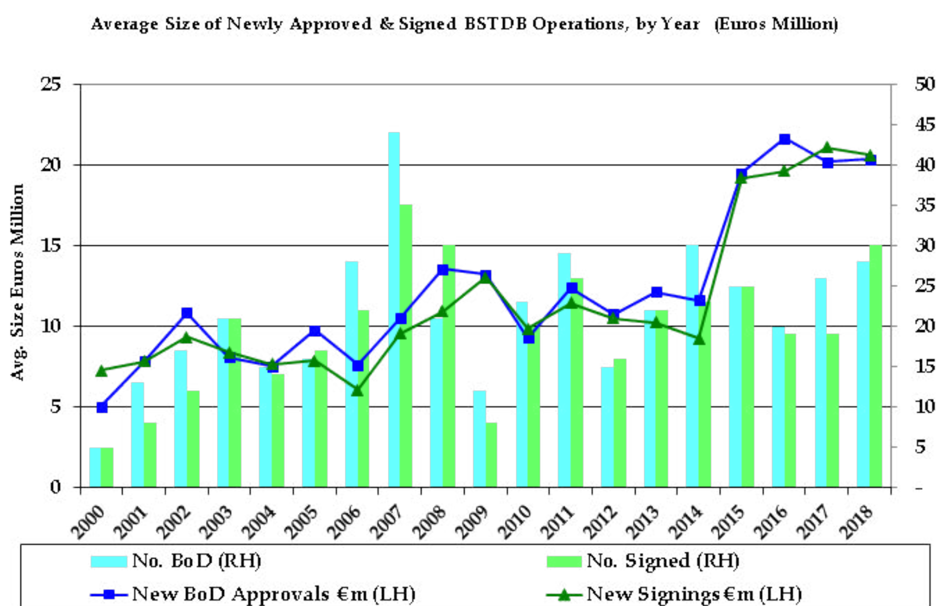
Financial institutions accounted for one third of signings during this period, with the remainder of new operational activity divided fairly evenly among consumer staples, energy, industrials, materials, and utilities.

Private sector operations comprise 89.5% of the outstanding portfolio (versus 94.5% at end 2014), while the share of public sector operations increased to 10.5% (up from 5.5% at end 2014); with sovereign guaranteed operations comprising 10.2% of the overall portfolio.

The average life of the active portfolio stood at 3.54 years at end December 2018, slightly longer than the 3.34 years at end December 2014; even during the intervening years, this figure has remained very stable.

The average size of operations, as seen in the following graph, grew significantly in the 2015-2018 period. New signed operations averaged €19.3 million, about 86% larger than the average signing size of €10.4 million between 2011-2014; new operations approved by the Board of Directors (BoD) averaged €19.1 million, approximately 62% higher than the average BoD approval size of €11.8 million between 2011-2014.

Graph 2



As Table 1 below shows, operational activity was constantly strong and the target amounts projected by the Bank's 2015-2018 MTSBP was exceeded for all approvals, signings and outstanding, with targets reached or exceeded for all but two of our member countries.

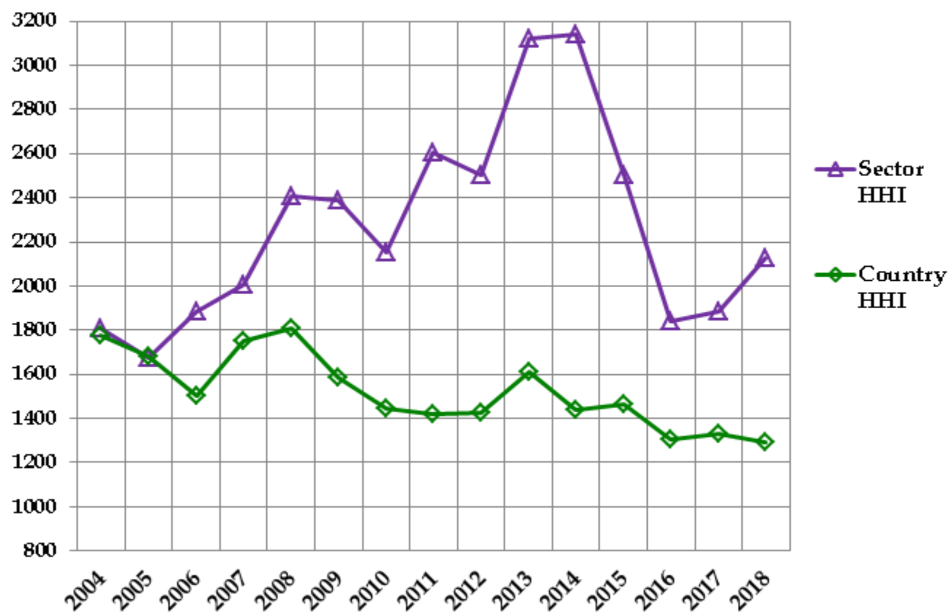
Table 1: Summary of Key BSTDB Indicators 1 January 2015 - 31 December 2018[4]

INDICATOR	2015	2016	2017	2018
Outstanding portfolio (EUR million)	1,113.4	1,191.7	1,166.2	1,358
Share of NPLs (%)[a b]	1.2%	3.4%	2.1%	1.0%
Capital Adequacy Ratio (%)[d]	55.4%	44.9%	49.3%	48.6%
Efficiency (%)[c d]	43.0%	60.0%	50.2%	57.1%
Operating Income (EUR million)[b]	41.4	30.8	38.4	34.0
Net Income (EUR million)[b]	15.2	1.8	8.7	5.2
Return on Equity (%)[b]	2.1%	0.2%	1.1%	0.6%

4 Notes to Table: (a) NPLs to Total Loans; (b) Figure is estimate for 2018; (c) Defined as administrative expenses relative to revenues (lower value means higher efficiency) (d) Figure is for first half of 2018.

As a result, the concentration index improved both for country and sector distribution of operations, as can be seen in Graph 3 below.

Graph 3: Geographical & Sector Concentration



For the period covered by the MTSBP 2015-2018 the Bank's financial performance was overall strong as demonstrated by the values presented in the following table:

Table 2: BSTDB Summary of Performance Indicators

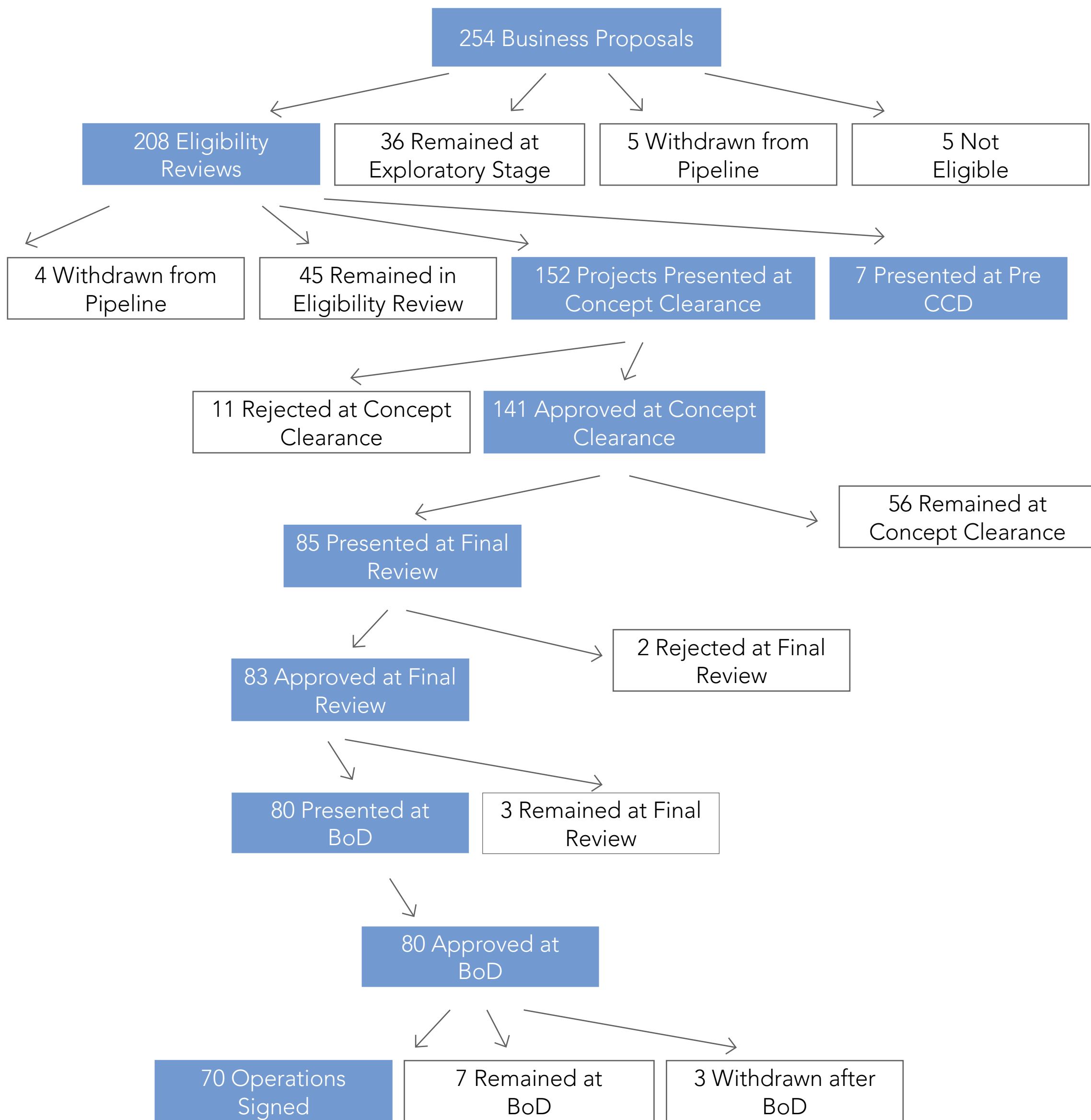
INDICATORS EUR million	**2015**	**2016**	**2017**	**2018**
Ratios				
Capital	709	735	759	807
ROAE	2.17%	0.24%	1.14%	1.55%
ROAA	1.31%	0.12%	0.54%	0.76%
Cost/Income Ratio (before provisioning)	44.88%	61.71%	51.44%	58.40%
Equity/Total Assets	55.27%	45.19%	50.08%	48.21%
Loan loss provisions/total loans (end of year)	3.08%	2.65%	4.68%	4.00%
Revenues after opex/revenues before opex	39.78%	17.10%	22.63%	18.46%

This positive performance was both supported by and further underpinned the strong credit rating of BSTDB, the highest rated entity in the Black Sea region.

As visible from the following graphic presentation, the Bank had identified during the past Medium-Term Strategy and Business Plan period 254 business proposals, of which 141, or 55%, past Concept Clearance. Of these, 83 were approved by the Credit Committee at the Final Review phase, with 56 proposals still under review. From the 83 Credit Committee approved projects, 80 were approved by the Board of Directors, but 3 projects were withdrawn after approval. A total of 70 operations were signed with clients and started disbursing. About 10 operations are waiting for potential signing in 2019, while about 33 operations from those that already passed Concept Clearance may be presented to the BoD for approval at some point.

The fact that only about 40% of operations will end up signing, from those identified as new business proposals, is proof of the rigorous appraisal and due diligence process and the conservative risk management the Bank applies in order to secure the highest quality at entry of operations. The high quality of this selection process is testified by both the high percentage of operations rated as having relevant mandate fulfillment and the very low level of NPLs.

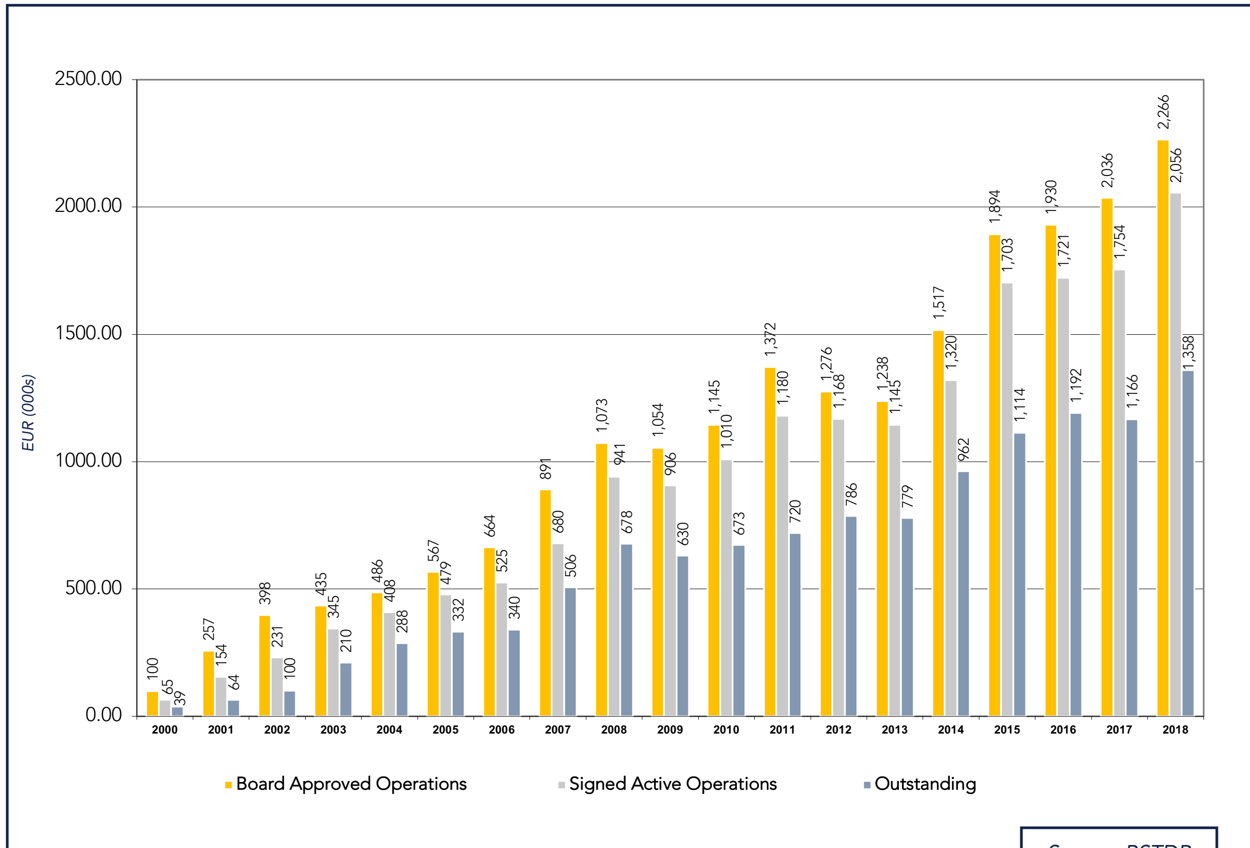
Graph 4:



Portfolio Description

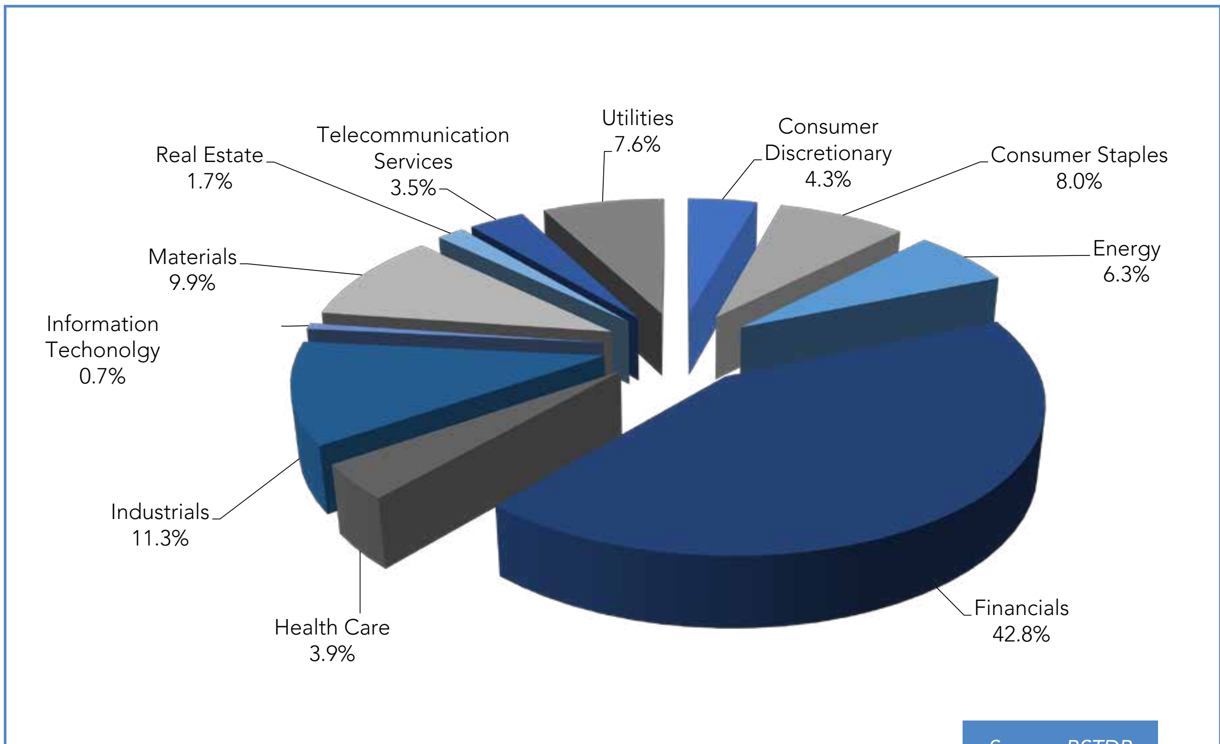
Since the beginning of operations in June 1999, the Bank has approved 391 operations amounting to about EUR 5.7 billion. Throughout this period, there were 341 signed operations for a total signing amount of EUR 4.7 billion. A total of 281 operations for about EUR 3.6 billion were repaid. At end-2018, there were 112 operations in the total portfolio outstanding balance for EUR 1.358 billion.

BSTDB Portfolio Development 2000-2018



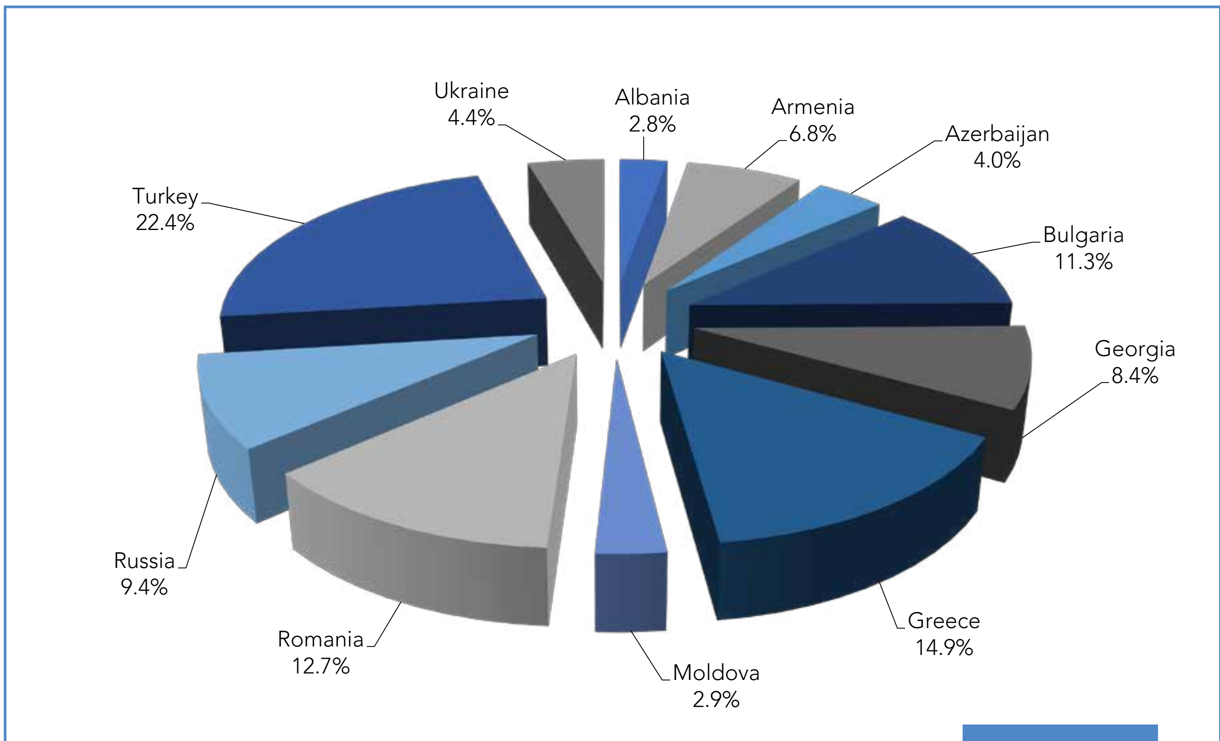
Source: BSTDB

Cumulative Signed Operations by Sector

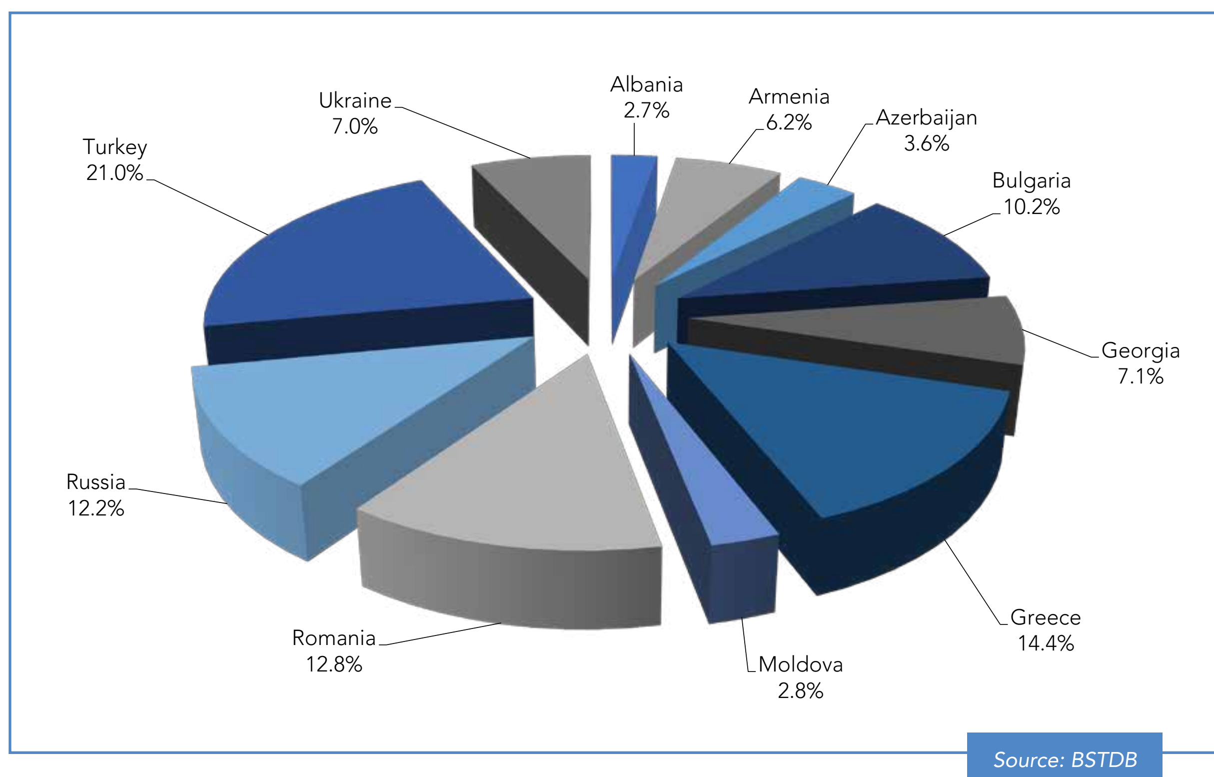


As of end-2018 the outstanding operations of the Bank (cumulative disbursements less repayments for active operations) represented EUR 1.358 billion, distributed by country as per the following graph:

Oustanding Operations by Country



Active Signed Operations by Country



Source: BSTDB

2018 Portfolio Developments

In 2018, the Board of Directors approved 28 new operations for a total of EUR 569.7 million. Thirty new operations were signed for a total of EUR 617.9 million. As a result, the Bank had 112 outstanding operations to 89 clients at the end of 2018.

Portfolio structure by sector remained broadly in line with the Bank's historical trends. As in previous years, the most significant exposures were in financial institutions, industrials, energy, utilities, materials and consumers staples. Significant exposure to financial institutions reflects BSTDB's strategic focus on the SME sector development, trade finance, leasing and mortgage lines of credit extended through financial intermediaries in member countries. The Bank's participation in regional SME equity funds represented a further 2.0% of the outstanding portfolio.

Enhanced effort was put into increasing the share of the real (i.e. non-financial) sector, which reached 60.5% of outstanding portfolio at year-end. One third of the new approvals in 2018 went to the real sector. The sectorial structure was well diversified, with projects originating from various industries and economy sectors: manufacturing, agribusiness, healthcare, energy, IT, financing small and medium enterprises, leasing, trade finance, etc.

Co-Financing

The Bank values its cooperation with other financiers in mobilizing investment in the Black Sea Region and realizing cross-country operations. Such operations possess high shareholder value for the Bank and are therefore priority activities.

In the course of 2018, 37.1% of signed portfolio was co-financing. In terms of total signed active portfolio in the amount of EUR 2.0 billion, 52.5% of operations are co-financing. The share of co-financed active operations to total portfolio outstanding balance is 51.4%.

SELECTED BSTDB FINANCING IN 2018

BSTDB amount	EUR 50 million
Total operation cost	EUR 600 million
Type of financing	bond
Maturity	7 years

Bulgarian Energy Holding bond (Bulgaria)

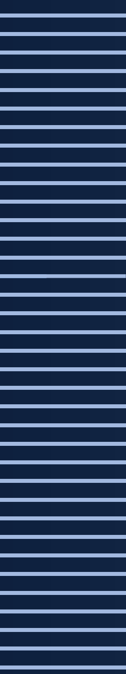
BSTDB invested EUR 50 million in a bond issue of the Bulgarian Energy Holding EAD (BEH), the incumbent 100% state-owned electricity and gas utility in Bulgaria and a major electricity exporter in the Balkans.

The BSTDB funding helped in implementing the BEH's priority investment projects in Bulgaria, such as the modernization of the electricity and gas transmission infrastructure, in particular the interconnectors between Bulgaria and its neighbouring countries, which is crucial for energy security and integration in the region.

The total volume of the BEH bond was EUR 600 million issued in several tranches, with BSTDB subscribing to the last tranche of EUR 50 million.

SELECTED BSTDB FINANCING IN 2018

BSTDB amount:	EUR 52.5 million
Total operation cost:	EUR 520.2 million
Type of financing:	loan
Maturity:	5 years & 4 months

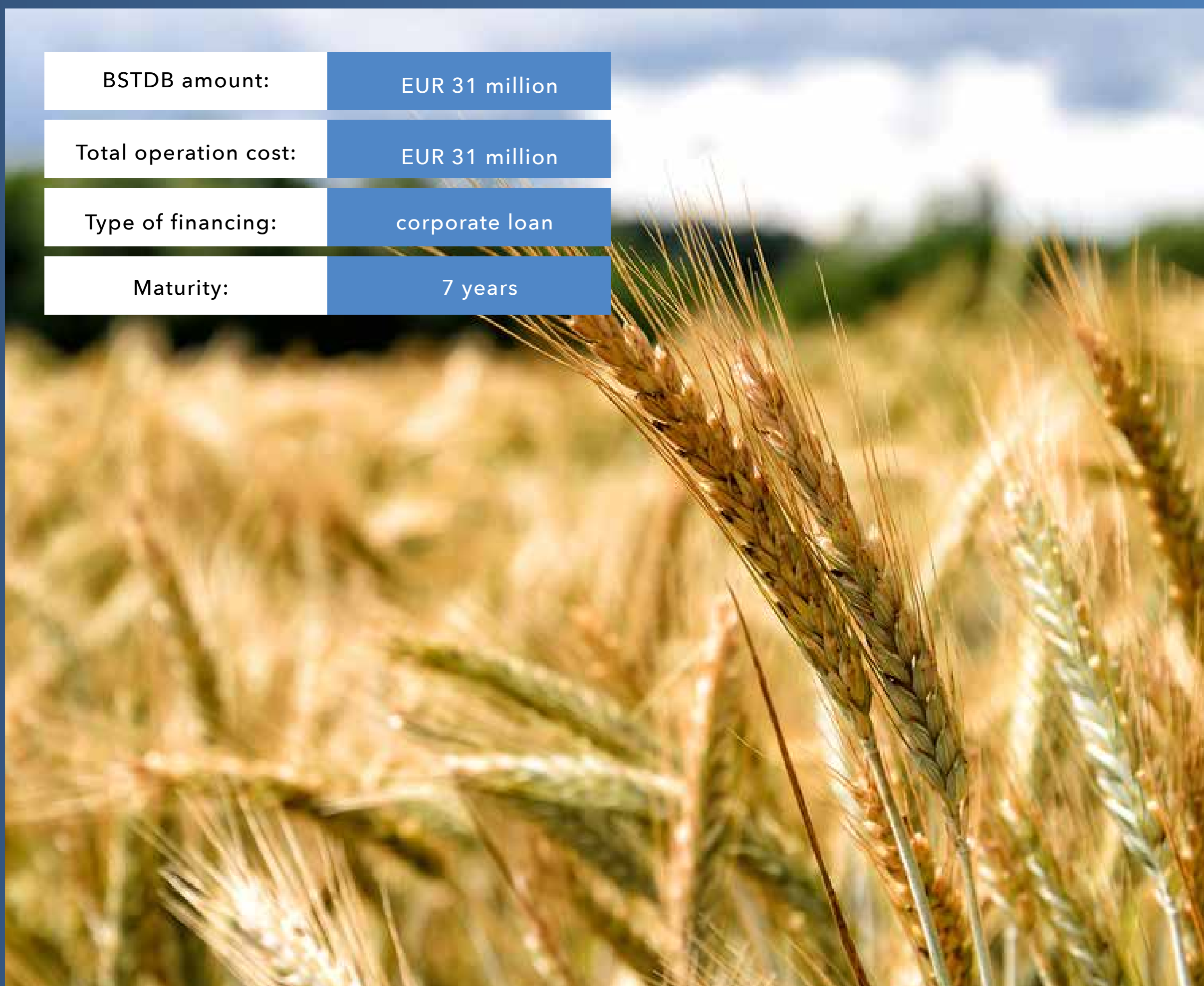


Energean Oil and Gas reserves-based loan (Greece)

BSTDB provided a reserves-based loan facility in the amount of USD 52.5 million to Energean Oil & Gas, a Greek exploration and production company, to accelerate the development of Greece's hydrocarbon sector.

The facility will help the company's existing oil development program to access additional oil reserves in the Prinos, Prinos North and Epsilon operating oil fields, located offshore Greece (Prinos-Kavala Basin). In particular, the financing will cover capital expenditures for drilling and additional well platforms and consolidation of the company's existing debt.

The loan is part of a senior reserves-based facility amounting to USD 180 million, jointly provided by BSTDB, the European Bank for Reconstruction and Development (EBRD), and a Romanian Club facility, arranged by the Export-Import Bank of Romania.



BSTDB amount:	EUR 31 million
Total operation cost:	EUR 31 million
Type of financing:	corporate loan
Maturity:	7 years

Orexim grain terminal investment (Ukraine)

Orexim Group invited the Bank to provide a loan of EUR 31 million to finance the company's investment in a new grain terminal in Mykolaiv Port in Ukraine. The BSTDB loan was used for the modernization of the port terminal and to increase its capacity from 60,000 mts to over 142,000 mts.

Orexim Group was founded in 2004 as a trading house and in 2010 it started to expand its activities into port operations, with a brand-new vegetable oil terminal. The Group now operates in three main segments: port operations (bulk and liquid cargoes and grains trans-shipment), trading (sunflower oil and grain export) and other services (forwarding, logistics). It employs about 1500 people.

The expansion of Orexim Group's grain terminal is expected to facilitate the exports of grains from Ukraine by providing better access to the international markets for Ukrainian agribusiness companies. The investment is expected to contribute to an increase in hard currency revenues of the Ukrainian agribusiness, transport and stevedoring companies, with a positive effect on strengthening the balance of payments of the country and ensuring stability of the local currency.

Given the considerable volumes of grain exports to the countries of the Black Sea region, the operation is expected to have a favourable impact on the trade and maritime transport services in the region.

SELECTED BSTDB FINANCING IN 2018

TBC Bank local currency loan for SMEs (Georgia)

BSTDB provided a loan of GEL 120 million (equivalent of USD 50 million) to TBC Bank to finance the investments and working capital needs of Georgian small- and medium-sized enterprises (SMEs).

This is the second local currency SME facility extended by BSTDB to TBC Bank since 2015, bringing the total amount to the equivalent of USD 70 million.

By financing in local currency for Georgian SMEs, BSTDB helps to overcome the foreign exchange rate fluctuation risk, a challenge faced often by businesses, and it contributes to the program of the Georgian Government to de-dollarize the banking sector.

BSTDB has cooperated with TBC Group since 2003, providing over USD 162 million in revolving trade finance, SME finance and leasing facilities.

The new loan to TBC Bank will support the development of SMEs in Georgia and will have a positive impact on poverty alleviation by stimulating self-employment, creating new jobs and generating income.

Being a local currency loan backed by the issuance of a Georgian Lari-denominated bond, the operation is innovative and has a positive demonstration effect.

BSTDB amount:	GEL 120 million
Type of financing:	loan for SMEs
Maturity:	3 years

Trade finance facility to Türk Eximbank (Turkey)

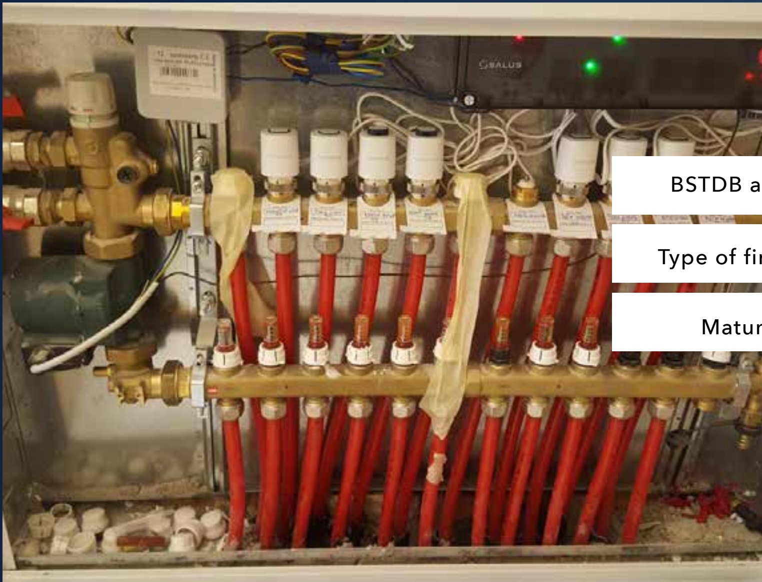
BSTDB helps promote Turkey's export potential with a two-year EUR 50 million trade finance facility extended to Türk Eximbank, the country's state export credit agency. The loan will be used to finance Turkish exporting companies, in particular, manufacturers of goods and equipment.

BSTDB started its cooperation with Türk Eximbank in the year 2000 and since has disbursed over USD 400 million for pre-export finance facilities.

The loan is expected to contribute to regional cooperation, given that around 10% of Turkish exports are to BSTDB member countries, and in support of the strong presence of Turkish contractors in the region.

BSTDB amount:	EUR 50 million
Type of financing:	trade finance facility
Maturity:	2 years

SELECTED BSTDB FINANCING IN 2018



BSTDB amount:	EUR 7 million
Type of financing:	loan for energy efficiency household investments
Maturity:	one-year, revolving

Ralfi loan for energy efficiency household investments (Romania)

A EUR 7 million revolving loan was provided by BSTDB to Ralfi IFN (Garanti Consumer Finance), a Romanian non-bank financial institution, to finance energy efficiency, renewable energy and water-saving solutions for the Romanian residential housing sector. About 700 Romanian households will benefit from this loan facility.

Energy efficiency is among the priorities of the Juncker Plan for the European Union. Buildings account for about 40% of the EU final energy consumption. Given the low annual new build rate (1.5%), improving the energy efficiency of existing residential buildings is needed to comply with the new EC framework, aiming for 40% Greenhouse Gas Emissions (GHG) reduction target (75% in buildings) until 2030.

The facility is BSTDB's first energy efficiency facility for residential buildings, targeting owners whose houses are of low energy class. It finances beneficiaries to carry out the most important interventions to improve the energy performance of their homes, while contributing to the country's energy efficiency and environmental goals. The project will improve the citizens' quality of life, help them save more energy and cut CO2 emissions.

In addition to the positive environmental impact, refurbishing these homes and bringing them up to standard will contribute to employment creation due to the scale of the work undertaken.

SELECTED BSTDB FINANCING IN 2018

Sovcombank trade finance loan (Russia)

BSTDB expanded its support to the trade activities of Russian companies by providing a new USD 25 million revolving trade finance facility to Sovcombank for on-lending to enterprises involved in import or export activities in Russia and for supporting the development of the real economy. Sovcombank has a growing trade finance activity and shall use the BSTDB loan to finance short-term pre-shipment and post-shipment export and import activities of its customers.

Sovcombank is one of the leading Russian banks with a strong brand name and developed branch network, thus representing an excellent intermediary to channel financial resources with clearly defined utilization purposes. The BSTDB loan is expected to support the trade financing program of Sovcombank by facilitating the diversification of its funding base.

The trade finance facility provided by BSTDB is expected to have economic benefits such as new jobs creation, enhanced export capacity and competitiveness, higher tax revenue driven by increased economic activity and positive multiplier effects in other sectors of the economy.

BSTDB amount:	USD 25 million
Type of financing:	trade finance facility
Maturity:	one year, revolving

Ameriabank loan for SMEs (Armenia)

A USD 15 million loan for SMEs was extended to Ameriabank, thus further enhancing the BSTDB support to the development of SMEss in Armenia, one of the core priorities of the Armenian government.

Ameriabank is the largest universal bank in Armenia, a market leader with a developed branch network, thus enabling BSTDB to finance SMEs which cannot be reached otherwise by BSTDB for funding.

The loan is expected to have a positive social impact by contributing to the growth of a sustainable SME sector in Armenia, improved access to finance and new jobs creation.

BSTDB has a successful partnership with Ameriabank starting in 2014 with a USD 10 million loan for SME finance used by the bank to finance about 100 SMEs and entrepreneurs in Armenia.

BSTDB amount:	USD 15 million
Type of financing:	loan for SMEs
Maturity:	5 years

NOA loan for micro-, small- and medium-sized enterprises (Albania)

BSTDB provided a EUR 2 million loan to NOA, a leading microfinance institution in Albania. The BSTDB financing will help to increase the volume and variety of lending products and services available to Albanian micro-, small- and medium-sized enterprises (MSMEs) for the creation, modernization, expansion and diversification of industrial, agricultural and service-related businesses in the country.

Supporting the development of micro and small businesses is among BSTDB's key priorities as a development bank. By starting this partnership with NOA, the Bank aims to improve access to finance for Albanian small businesses.

NOA's mission to empower Albanian families and businesses is in line with the BSTDB priority to support such non-bank financial institutions and facilitate economic growth. NOA is the second microfinance organization receiving BSTDB financing in Albania.

BSTDB amount:	EUR 2 million
Type of financing:	loan for micro-, small- and medium-sized enterprises
Maturity:	3 years

Technical Assistance Support

Black Sea Project Promotion Facility

Aiming to improve investment access for SMEs in the Black Sea Region in 2017, the Russian Federation initiated the establishment of the Black Sea Project Promotion Facility (BSPPF), funding it by an initial contribution of USD 1 million. BSPPF finances technical assistance services for the preparation of feasibility studies, business plans, due diligence analyses, creation of networks or partnerships for activities mostly related to energy efficiency and renewables, environmentally friendly technologies, infrastructure, trade exchanges, and knowledge-sharing. Financing requests may be brought by BSTDB and the Permanent International Secretariat of the Organization of the Black Sea Economic Cooperation (BSEC PERMIS).

BSPPF focuses on pilot medium-sized projects meeting the established criteria and requirements of BSEC PERMIS and BSTDB. In 2018 the BSPPF funded a second assignment submitted by BSTDB for a consultant to undertake the environmental and social impact assessment for the construction of a coal trans-shipment terminal.

Technical Assistance Fund provided by the Development Bank of Austria

BSTDB administers a Technical Cooperation Special Fund established in 2008 with the Development Bank of Austria (OeEB). 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 was 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 eligible countries of the Black Sea region. The Fund represented the first financial facility of this kind, provided to BSTDB by an institution not based in the BSTDB countries of operation. It has been used for assignments in the BSTDB member countries that are eligible to receive ODA.

The Fund ended its activity in March 2018. Since its establishment, it disbursed EUR 411,100, mainly for project preparation assignments.

Technical Assistance Fund provided by the Government of Greece

The Bank administers a special fund (the 'Hellenic Fund') established in 2001 by a Contribution Agreement between the Government of the Hellenic Republic and BSTDB. The fund was set up with an initial amount of EUR 800,000 and was replenished in 2003 with EUR 500,000. This was the Bank's first special fund and responded to a need for better quality of information provided to the Bank by prospective clients.

The Hellenic Fund is tied to consulting companies based in Greece. However, up to 25% of an assignment cost could be allocated to consultants who are nationals of the other member countries of the Bank.

Since its inception, the Hellenic Fund disbursed around EUR 1.3 million for 40 consulting assignments. The companies benefitting from these funds operate in manufacturing, telecommunications, oil and gas, transportation, agribusiness, renewable energy, tourism, real estate, retail and banking. The Hellenic Fund has been used for consultancy services in nine BSTDB member countries: Albania, Armenia, Bulgaria, Georgia, Greece, Moldova, Romania, Russia and Ukraine.

Addressing Sustainability

The Approach

BSTDB has committed to address environmental and social sustainability by applying the core principles in its operating model and financing decision-making. Thus, pollution prevention and mitigation; respect for fundamental human rights in the working environment; addressing climate change; promoting efficient use of natural resources; protection and conservation of biodiversity; and disclosure of information on environmental and social performance of its operations; and engagement in open dialogue with stakeholders, are all part of the general sustainability approach of the Bank.

Environmental and Social Due Diligence

All operations considered by the Bank for financing undergo mandatory environmental and social due diligence. Depending on the associated potential environmental and social risks and impacts, and the scope of the environmental and social due diligence that is necessary to identify, assess and mitigate these risks and impacts, all operations are screened into A, B+, B, C and FI categories.

The due diligence of operations financed directly by BSTDB, depending on relevance in each specific case, focuses on such issues as the environmental and social management applied by the Borrowers; labor and working conditions and how people are treated in the working environment; the applied pollution prevention and abatement measures and how efficient the resources are being used; potential risks on the local communities, their health, safety and security; issues related to land acquisition, involuntary resettlement and economic displacement; impacts on biodiversity, ecosystem services and sustainable use of living natural resources; protection of any cultural heritage; and potential risks and impacts on Indigenous Peoples if present in the area of influence of the operation.

The due diligence of operations financed by BSTDB through Financial Intermediaries (FIs) normally focuses on the capability of such FIs to manage the environmental and social risks and impacts associated with their business activity in a manner that is compliant with the requirements of the Bank's Environmental and Social Policy and the national legislation in effect, including the country's commitments under international law. If these are found to be satisfactory the Bank normally delegates the function and responsibility for environmental and social issues to its FI Borrower.

Category A operations are subject to Environmental and Social Impact Assessment (ESIA) process and require meaningful consultation with the public that may be affected by such operations. This includes setting of procedures for public notification, disclosure of related information about the operation and its potential E&S risks and impacts, public review and comment. Category A operations are also publicly disclosed on a 30/60 calendar day scheme before these may be submitted to the Board of Directors for consideration.

Compliance Requirements and Standards Followed

All operations considered by BSTDB need to comply with the following minimal environmental and social requirements: 1) compliance with national and applicable EU environmental, labor, health and safety, and public information laws and regulations, including national commitments under international law; 2) availability of permits, approvals, licenses and certificates required under relevant laws and regulations; 3) Category A operations need to meet the requirements applied by EU, namely the Environmental Impact Assessment (EIA) Directive and relevant sector-specific and cross-cutting Directives, or the requirements applied by WB/IFC. Category A operations that are likely to generate transboundary impacts need to meet

the requirements stipulated under the Espoo and Aarhus Conventions irrespective of whether the country of operation is a party to the Convention; and 4) meet the requirements of the BSTDB Environmental and Social Exclusion List.

BSTDB makes its best efforts to apply good international environmental and social practices in all the operations it finances. By good practices, the Bank recognizes the performance standards and requirements of the leading Multilateral Development Banks (MDBs), development agencies, the European Union (EU) E&S standards, the ILO CLS, the World Health Organization (WHO) standards, relevant IMO conventions, as well as relevant international conventions. This includes the Convention on the Protection of the Black Sea Against Pollution, and the multilateral environmental agreements under the United Nations Economic Commission for Europe (UNECE), in particular, the Convention on Access to Information, Public Participation in Decision-Making and Access to Justice in Environmental Matters (Aarhus Convention), and the Convention on Environmental Impact Assessment in a Transboundary Context (Espoo Convention).

Public Disclosure of Environmental and Social Information

The Bank, as part of its sustainability approach, is committed to inform the public in a transparent and timely manner about the environmental and social aspects associated with its operations. This information is posted on the Bank's website as Operation Summary Documents (OSDs) and includes general information about the operation financed, as well as information on E&S categorization, the potential risks and impacts, and how these will be addressed throughout the life of the BSTDB financing. OSDs are disclosed to the public after such operations are approved by the Bank's BoD.

BSTDB also discloses to the general and/or interested public relevant environmental and social information of its Category A operations - operations associated with potentially significant risks and impacts. For private sector operations this information is disclosed not later than 30 calendar days before the BoD meeting, and 60 calendar days for public sector operations. Thus, any stakeholders directly or indirectly affected by the Bank's Category A operations, or who have an interest in such operations, can review the relevant information, make enquiries, and provide comments.

In 2018, BSTDB disclosed before the Board approval for environmental and social information of public interest related to two Category A operations, namely: construction of the greenfield Lavna Coal Transshipment Terminal on Kola Bay in Murmansk, Russian Federation, and construction of the 250 MW Syvash Wind Farm project in Southern Ukraine.

Monitoring and Institutional Aspects

All the operations financed by the Bank are monitored against the agreed environmental and social compliance requirements in order to ensure that relevant terms and conditions stipulated in the legal agreement are met. In addition to that, monitoring helps the Bank to determine whether the prevention and mitigation measures employed in managing the environmental and social risks and impacts are effective or need adjustments.

All aspects of environmental and social sustainability of the Bank are led by the Environmental and Social Sustainability Office, which is in charge of developing and implementing relevant strategic objectives, policy statements, and internal procedures. It leads the independent environmental and social due diligence process of operations and advises the Senior Management on the relevant risks and impacts of the financing decision-making, and the general E&S performance of the Bank thus, ensuring the Bank's activities do not affect the state of environment and human well-being, and contributing to a more efficient fulfillment of the Bank's development mandate.

BSTDB has committed to allocate the necessary resources in order to ensure that its sustainability approach is effectively followed and implemented, is fully integrated into its operation cycle, and is applied in a systematic manner to all the operations financed by the Bank.

International Cooperation

BSTDB is actively cooperating with governmental bodies from its Member States, partner multilateral and bilateral financial institutions, businesses, civil society, and public to ensure that its sustainable development objectives are met effectively and in a transparent manner.

Since its founding, the Bank has established closed ties with its partner Multilateral Financial Institutions (MFI) within the Working Group on Environmental and Social Standards (WGESS). WGESS is a high-level forum represented by the key environmental and social representatives of MFIs and development agencies around the world. It aims to harmonize the environmental and social assessment practices by sharing experiences, discussing issues of concern, developing common approaches, and working in partnership.

Participants at the EDFI Working Group on Environmental and Social Issues hosted by BSTDB. Thessaloniki,Oct 9-10, 2018

BSTDB is also actively involved at the European level in the European Development Finance Institutions (EDFIs) Working Group on Environmental and Social Issues, which is another high-level forum where the European Bilateral Financial Institutions join efforts to harmonize their environmental and social practices and achieve more effective development of their financing. On 9-10 October 2018, the Bank had the privilege to host the autumn session of the working group meeting. The environmental and social experts from 14 European development banks met in Thessaloniki and discussed issues of common interest such as climate change and GHG emission reduction in projects; quality of due diligence; environmental and social compliance and performance of borrowers; and the issue of decent work, gender, as well as human rights in development finance.

Evaluation of BSTDB's Medium-Term Strategy and Business Plan 2015-2018

1. Introduction

The Board of Directors asked the Evaluation Office to prepare an independent report on the implementation performance and continued relevance of the Bank's Medium-Term Strategy and Business Plan 2015-2018 (MTSBP). This evaluation was conducted to ensure both accountability and learning from past performance, to support an informed further strategy, based on evidence and lessons learned. The evaluation distills and analyzes lessons learned through the implementation of Strategy 2018, reflecting the existing and emerging development challenges of the Bank's shareholders, as well as the key findings of all evaluation overviews performed in the last 4 years.

2. Implementation of Key MTSBP Targets

The evaluation finds that the Bank has aligned its MTSBP and most operations with Strategy 2020.

2.1. Ambitious Portfolio Growth of 7.5% p.a.

This target per se is considered ambitious as it is generally higher than previously sustained growth rates. Since 2009, the Bank's average growth was 5.7%. Based on the MTSBP mid-term review, the aimed (and achieved) growth peaked to a record high level of 9% in 2016.

During 2015-2017, BSTDB exceeded its annual base case targets for Board approvals and signings of new operations. The (revised in 2016) cumulative 2015-2018 targets for both Board approvals and signings were exceeded substantially – at 142.9% and 151.7% respectively.

The increased pace of processing and approval of new/larger operations, including a substantial number of syndications and corporate bond participations, resulted in higher, often front-loaded disbursements that exceeded substantially the MTSBP annual approval targets. This was, however, offset by a wave of repayments, pushing repayment levels well beyond the MTSBP projections (146.2%), thus shrinking the actual active (outstanding) portfolio below the levels of signings but within the MTSBP target (103.4%). Several factors caused the unexpected prepayments: (i) a sustained decline in interest rates, triggering incentives to refinancing the BSTDB loans; (ii) a policy of some countries towards reducing exposure to external borrowing; (iii) the inability of the Bank to promptly offer better terms and/or re-negotiate prepaid loans, mostly as a result of increased borrowing cost associated with the 500 million USD benchmark bond issued by BSTDB in 2016. Consequently, the Bank responded with substitution of large scale front-loaded disbursement operations to offset the decline in the outstanding portfolio.

The combined effect of unanticipated prepayments and the appreciation of the US dollar relative to the Euro resulted in a below-target outstanding portfolio. The Bank's response was to further increase new operational activity, often re-focusing on larger and promptly disbursing operations. Despite the response-driven impressive exceeding of approval and signing targets, the Bank was unable to prevent a relative decline in its outstanding portfolio.

The Bank's inability to grow its outstanding portfolio in line with the aggressive increase in approvals is mainly due to the prevalence of the approval targets, backed by the assumption that more commitments will bring a growth of the outstanding component. However, the actual focus on approvals, and the lack of quality-based cascading of institutional Key Performance Indicators, caused a displacement effect – new operations were quickly displacing existing active operations as the relative devotion to portfolio maintenance was insufficient.

Table 1: Quantitative Targets and Results

Millions of Euros	*2015*	*2016*	*2017*	*2018*	*Cumulative*	*% Actual/ Target*
MTSBP Target for Outstanding	€1,056.0	€1,200.0	€1,280.0	€1,322.0		
End of Year Actual Outstanding	€1,113.4	€1,191.8	€1,166.4	€1,367.0		
Surplus/ Shortfall BP vs. Actual	€57.4	-€8.2	-€113.6	€45.0		103.4%
MTSBP Target for BoD Approvals	€304.0	€326.0	€376.0	€404.0	€1,410.0	
Actual BoD Approvals	€487.2	€433.3	€524.6	€569.7	€2,014.8	
Surplus/ Shortfall BP vs. Actual	€183.2	€107.3	€148.6	€165.7		142.9%
MTSBP Target for Signings	€266.0	€286.0	€329.0	€353.0	€1,234.0	
Actual Signings	€480.3	€373.2	€400.7	€617.9	€1,872.1	
Surplus/ Shortfall BP vs. Actual	€214.3	€87.2	€71.7	€15.2		151.7%
MTSBP Target for New Disbursements	€296.0	€309.0	€296.0	€299.0	€1,200.0	
Actual New Disbursements	€378.8	€454.5	€393.8	€302.0	€1,800.9	
Surplus/ Shortfall BP vs. Actual	€82.8	€145.5	€97.8	€3.0		150.1%
MTSBP Target for Repayments	€180.0	€231.0	€233.0	€248.0	€892.0	
Actual Repayments	€221.7	€383.1	€316.3	€382.7	€1,303.8	
Surplus/Shortfall BP vs. Actual	€41.7	€152.1	€83.3	€1.0		146.2%

Notes: Targets for 2015-2016 based on MTSBP 2015-2018; Targets for 2017-2018 based on Mid-Term Review; Data for 2018 may be subject to minor changes based on fair valuation of equity investments; A positive figure in surplus/ shortfall row means target was exceeded; A negative figure means target was not met; Percentages in last column compare cumulative actual to cumulative target.

2.2. Diversify Portfolio by Country and Sector – Considerable Progress, Some Disparity Remains

The strategy aimed at reduced country concentration, a share of non-Bank operations of at least 55% as well as increasing the share of sovereign and public sector operations to 20% of the portfolio by end 2018.

While the Bank made substantial progress in achieving a better geographical balance, it came short of eliminating large portfolio disparities across countries. The quantitative country targets of the MTSBP 2015-2018 and the Country Strategies were exceeded in nine of the eleven shareholder countries. In five countries the signings targets were exceeded by over 50%.

Table 2: Targeted and Actual Portfolio Shares by Country (EUR million)

	Signings Target 2015-2018 EUR Million	Actual Signings 2015-2018 EUR Million	% of Signings Target Met
Albania	67.9	35.8	52.7%
Armenia	67.9	86.0	126.7%
Azerbaijan	123.4	91.1	73.8%
Bulgaria	135.7	206.0	151.8%
Georgia	49.4	150.8	305.6%
Greece	160.4	265.6	165.6%
Moldova	37.0	47.5	128.3%
Romania	148.1	174.8	118.0%
Russia	197.4	248.6	125.9%
Turkey	197.4	433.1	219.4%
Ukraine	49.4	132.9	269.2%
Totals	1,234.0	1,872.1	151.7%

Notes: A figure above (below) 100% means the target was exceeded (not met); Targets for 2015-16 based on MTSBP 2015-18; Targets for 2017-18 based on Mid-Term Review; Data for 2018 may be subject to minor changes based on fair valuation of equity investments.

In contrast, in two countries the targets were not met by a substantial margin – Albania (52.7% of target met) and Azerbaijan (73.8%).

Financial institutions stand out representing one third of Board approvals and signings in 2015-2018. The other key sectors are distributed relatively evenly among consumer staples, health sector, energy, industrials, materials, and utilities.

While the Bank consistently paid attention to the (revised downward at mid-term) original target of 20% share of public sector operations, it came short of reaching it. The two underlying reasons for this shortcoming are (i) the insufficient price competitiveness relative to AAA-rated MDBs who offer public sector lending at flat low rates, as well as (ii) the limited experience and capacity of the Bank to structure deals in the public and quasi-sovereign domain.

Private sector operations comprise over 85% of the outstanding portfolio (versus 95% at end 2014).

The average size of operations grew significantly in the 2015-2018 period. New signed operations averaged EUR 20.1 million, about 94% larger than the average size of EUR 10.4 million between 2011-2014. This reflects the focus on volumes and approvals that in turn caused a relative shrinking of the outstanding share of the portfolio, addressed above. The volumetric priority also caused a relative erosion of the development profile, as addressed further.

2.3. Portfolio Quality

The MTSBP addressed portfolio quality through a single key performance indicator. It states that the positively rated operations upon independent ex-post evaluation should be at least 70% at any given year. As this is a complex composite indicator, involving measurement time-lags (5-year moving average, reflecting operations maturity dynamics), its actual value will be measured and presented during the next strategy period. However, the data from the last four years indicate a stagnating and even deteriorating development performance of the new additions to the portfolio.

Table 3: Independent Ex-post Evaluation Ratings of Completed Operations

Criterion / Period	Prior MTSBP 2015-2018		Within MTSBP 2015-2018		Comment/ Recommendation
Positive ex-post ratings	**2010-2014**	**2012-2016**	**2013-2017**	**2014-2018**	
Relevance	73%	72%	71%	70%	trend setting ex-ante forward indicator, at margins, revisit
Effectiveness	74%	73%	74%	73%	Adequate, but modest ex-ante targets
Efficiency	56%	58%	57%	56%	scale-driven, capital-cost constrained, substandard
Sustainability	58%	60%	61%	57%	constrained by focus on volumes
Institutional Development Impact	57%	58%	52%	51%	as above, high potential
Overall (MTSBP target: 70% or more)	72%	71%	71%	70%	just on target, relevance-sensitive
Ex-ante/ex-post alignment	62%	66%	67%	67%	higher ex-ante / monitoring rigor/ incentives needed to reach 90% (MDB standard)
Mandate-based selectivity share	61%	62%	59%	58%	as above

While overall performance increased over the years, the share of operations rated excellent at ex-post has declined from 17% in the early years to 6% during latest periods. This merits attention as highly successful operations are a benchmarking source of valuable learning, motivation and replication. The diminishing cases of excellently-rated operations reflect a combination of unrealistic expectations (ex-ante mandate compliance optimism driven by efforts to obtain approval) and lower actual achievement. There are several cases which imply that a closer alignment of operations with country analysis/strategies tends to deliver a higher number of outstanding performances, both at operational and institutional planes.

The two most frequent key causes of mandate-related underperformance are: (i) risks identified at due diligence that were not covered by adequate covenants and/or monitoring; (ii) mitigating the risk of poor corporate governance is very challenging, particularly when not done at the outset of operation handling.

While since 2008, BSTDB maintains its performance generally in line with peer institutions, the Bank lags in the areas of ex-ante indicators setting/tracking, as well as in certain self-evaluations. Returning to mandate compliance growth requires revisiting indicator cascading/balance in order to offset shortfalls, such as volume-dominated incentives, as well as related waves of premature cancellations and pre-payments.

Contrary to certain prejudice, development performance is positively co-related to general portfolio quality and financial outcomes.

2.4. Institutional Developments

The MTSBP 2015-2018 focused on the following institutional enhancements, aiming at becoming a recognized regional Multilateral Development Bank of high relevance and impact:

- **Membership expansion:** Although BSTDB does not control the decision-making process, it recognized the benefit of scope enlargement, seeking to attract an AAA-rated institutional shareholder as well as another country from the region. While there is evidence of maintained efforts, this target has not been reached, although there are some prospects.

- **Enhanced institutional recognition:** The focus was placed at enhanced recognition by the Basel Committee, as well as certifications and/or accreditation for participation in global or regional initiatives that are consistent with the Bank's mandate. Certain success, resulting from a pro-active engagement of the Bank, has been noted in light of the recent risk-weight reduction by Basel regarding A-rated MDBs (from 50 to 30%). While the gap with AAA-rated institutions is disproportionately high, this is a long-awaited sign of recognition.

  BSTDB has also become a recognized partner of well-established peers, with a particular focus on ex-post evaluation standards and indicator harmonization. In 2018 it led major international events on ex-post evaluations and ex-ante indicators. As of November 2018 it chairs the Evaluation Cooperation Group of the MDBs, for the first time.

  The launch of a 500 million USD benchmark bond on the international markets is another example of institutional maturity and recognition, raising awareness and building a track record of institutional borrowing.

- **Enhanced shareholder support:** Substantial progress was made in resolving long-pending capital arrears.

3. Lessons Learned and Conclusions

The predominant focus on volumes alone, particularly at a departmental indicators level, erodes mandate relevance of certain large-scale operations, undermining future compliance with the higher mandate institutional goals and profile. The MTSBP 2015-2018 set an approval growth of 7.5% that became hard to sustain at the outstanding portfolio level. The Bank's response was to further maximize new approvals and commitments, but this overshadowed the development mandate indicators and screening, as evident by ex-post evaluations on operations relevance. Despite improvements in recent years, the success rates of completed projects in several aspects were lower than the benchmarks. This calls for enhancing of institutional relevance and effectiveness on the basis of improved indicator-based selectivity (addressing the principle of financial and non-financial additionality, among other core criteria) and better ex-ante anchoring, implying rigorous application of relevant knowledge, standards, skills, incentives and business processes. Volume-dominated incentives often trigger premature cancellations and pre-payments, as well as substandard mandate compliance.

Ex-post evaluation evidence suggests that development performance is positively co-related to general portfolio quality and financial outcomes. Decline in efficiency is typically in line with stagnating share or volatility of outstanding portfolio, as well as substandard mandate fulfillment.

The efforts towards institutional improvements and recognition were in most cases successful, elevating the international profile and leverage capability of BSTDB. Examples of immediate advantages include, but are not limited to, the ability to raise funding and standards of high impact and ex-post evaluation. The Bank should maintain the momentum and build upon the progress made towards further partnerships and mobilization of finance for its region and mandate.

Despite the efforts to reach the 20% target of public sector share in portfolio, the Bank was constrained by the challenge of funding costs, as well as the need for specific experience and capacity. This target was based on certain underlying assumptions that did not materialize, e.g. attracting a highly-rated shareholder.

On a number of occasions the Bank enhanced its relevance and risk sharing in an effort to become more responsive to clients. A good example is the increase in local currency finance that turned particularly valuable to non-exporting borrowers, as their currency risk exposure was better mitigated. While this trend could be encouraged, the evaluation notes its limitations, based on the risk absorption and fund-raising constraints.

Soon after the influx of liquidity, resulting from the issue of the benchmark bond in 2016, the Bank took the course of blending its treasury and mandate operations, to make best use of available resources. The rationale was to engage idle liquidity on a temporary basis, with a focus on short-term trade finance, to maintain a coherent asset-liability management. With due respect to this rationale, the ex-post evaluation reveals a trend of revolving what was intended as a short-term trade finance lending, at rather low margins. Temporary asset-liability management solutions should not displace development-driven portfolio structuring, as this erodes the Bank's efficiency and additionality.

Other Institutional Activities

Human Resources

Human capital and staff resources are a key factor in the success of BSTDB. The institution strives to maintain its status as a competitive employer following international standards and best practices, applying meritocratic recruitment, and a remuneration system that promotes excellence and positive incentives.

HR Development

The year 2018 was marked by the implementation and improvement of certain important HR policies. Important modifications to the recruitment and appointment policy, and to the performance management policy were identified and implemented; a comprehensive revision of the benefits and allowances policy was conducted; important benefits under the Bank's social security scheme were introduced; and the implementation of the new electronic leave administration system was finalized.

Following is a more detailed description of each of these achievements:

The revision of the recruitment and appointment policy was aimed at the implementation of a more balanced and transparent modality for the management of different types of appointment.

A new performance management system was implemented as of 1 January 2016. This system features increased objectivity, introduces performance-related rewards, and links individual performance to the performance of the institution through a process of cascading objectives at different organizational levels: institutional objectives are cascaded down from the institutional to the departmental level and thus are included in the calculation of individual performance scores. The accumulated experience necessitated a review of these objectives in order to ensure the comprehensiveness and accuracy of the cascading process, and prompted suggestions on the modification of the system's structure within the same conceptual framework. Also, a more efficient system for the management of unsatisfactory performance was introduced.

A thorough revision of the Bank's benefits and allowances system resulted in the identification of modifications aimed at streamlining certain administration processes, and increasing the flexibility of the system to the staff's benefit and at no additional cost to the Bank based on the lessons learned and the best practices of the other IFIs.

The Bank's staff pension plan rules were modified to provide more flexibility to the staff for the management of their pension plan benefits on separation from service. Also, the coverage of post-separation medical insurance costs for a certain period of time and for certain categories of staff was undertaken by the Bank.

In 2018, the Bank made significant progress towards the ultimate goal of transferring most of its HR processes to the SAP platform. More specifically, the transfer of the leave administration module was finalized.

Staffing and Recruitment

BSTDB conducts recruitment on a wide geographical basis. While preference is given to citizens of the member countries, recruitment is competitive and is based on the professional qualifications of the candidates. As of the end of 2018, the Bank's total headcount was 110 full-time employees.

Staff Development

BSTDB offers learning opportunities, addressing the development needs of its staff within the context of organizational business requirements. The policy on training, learning and development establishes a clear link between the institution's business needs and the development of professional and technical skills of the staff. In 2018, the share of the staff's learning and development needs addressed through in-house group training activities continued to increase.

Staff Benefit System

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. BSTDB also offers optional post-separation medical coverage.

The BSTDB pension plan, launched in January 2003, is comprised of a fully-funded defined benefit and a matched defined contribution component. This combination offers the flexibility required for best meeting the needs of a multinational workforce.

Information Technologies

The dependency of business on IT increases daily in today's business environment. More companies and customers work online to achieve better and faster results. Information remains the king in doing business and in making business decisions. Therefore, management and handling of information is key in supporting the Bank's operations.

The Bank uses Opentext's Enterprise Information Management (EIM) and Content Suite 16 version to manage its information. During 2018, the IT Department created personalized user interfaces for BSTDB's departments, focusing more in business process automation and in capturing corporate content. In this framework, a prototype subsystem was created for automating the creation of the Supervisory Monitoring Reports; integrating information flows from different departments and content from different sources such as SAP or internet-based services; and finally, furnishing automatically and disseminating appropriately the final records. The business and technology experience gained during the previous process will be utilized soon in further business processes' automation and the automated documents' creation and dissemination.

During 2018, the IT Department hosted in Thessaloniki the annual meeting of Electronic Records Management Systems User Group for International Organizations (ERMSUGIO). The IT Department introduced new technologies for interactive communication and collaboration among the group's members before the event, extending its EIM systems and creating a dedicated website for the event. During the event, BSTDB presented its innovative and award-winning EIM implementation and strategy to the meeting participants.

Using the Smart User Interface (SMART UI), provided by the Opentext Content Suite 16, to build and deliver business solutions, user adoption is key to gain business outcomes. Therefore, the Bank has started using Opentext Personalized Help, the online eLearning training system powered by Ancile to deliver targeted eLearning content to BSTDB employees on Content Server Smart UI Knowledge Fundamentals and new solutions implemented within Content Server. With Opentext Personalized Help, authors can easily create documents with detailed guidelines, recordings with step-by-step instructions and eLearning courses that are distributed to the relevant workforce. Employees use the training material created for them and give their feedback for any other business needs required. Easy access to training material from everywhere using a web browser, delivery in a self-paced mode for all employees without need to contact IT or training resources, reduction in Help Desk calls and support and less need for classroom training are some of the benefits that this platform has to offer.

In order to improve the delivery of documents to the Board of Directors and also cut down on the use of paper, the Bank has introduced a web-based application to deliver board documents in a structured way. The application used is also accessible from smart devices, allowing board members to have quick access to board documentation.

In close collaboration with the HR Department, several improvements have taken place in the SAP Human Capital Management (SAP HCM) solution, introducing HR reporting services, which allows the Bank to better manage its work force needs.

A SAP security and licensing review and optimization has taken place in 2018 to improve access to financial information and comply with best practices.

An implementation of SWIFT Customer Security Programme has taken place to make sure that the Bank complies with SWIFT best practices and the financial transactions using the SWIFT system are secure, allowing the Bank to support its financial obligations to its customers and third parties.

Improvements in IT operations are an ongoing process to ensure that the Bank's IT infrastructure is kept up to date and it has the capacity and capability to meet business needs and keep the

business running with minimum interruption. A new backup system has been put in place in HQ and DRS, using HP's StoreOnce devices, new tape drives, and backup reporting software, which support encryption at all levels and deduplication to reduce the storage footprint and support the backup and restore policy of the Bank.

Using VMware solutions, Bank staff can access their virtual desktops remotely via a web interface. This gives flexibility to staff to work from any device, at any place, as long as internet access is available.

Improvements in security are a continued process in the Bank and new security software and solutions are introduced to protect web-based applications.

External Relations and Communications

BSTDB's external relations and communications activities aim to support the achievement of the Bank's strategic institutional and business objectives by promoting the corporate image and increased awareness of the Bank in the Black Sea Region and beyond. In 2018, the Bank enhanced institutional cooperation with the development community, business partners, and other stakeholders while improving corporate transparency in line with international best practices.

Strengthening collaboration with partners in development for the benefit of the Black Sea region

During the year, the Bank was active in promoting synergies and business contacts with peer IFIs and other development institutions aimed at facilitating co-financing of operations in the Region and the exchange of information and good practices.

BSTDB organized the Workshop on the Local Currency Lending Opportunities in the Black Sea region with the participation of the relevant authorities from member countries, partner IFIs and private financial institutions.

The Bank signed a Cooperation Agreement with the OPEC Fund for International Development (OFID) to promote the economic and social development of countries in the Black Sea region through co-financing private sector projects, trade transactions and private equity investments.

Leading multilateral consultations on the development agenda

BSTDB continued to actively contribute to multilateral consultation mechanisms established by development finance institutions aimed at facilitating knowledge sharing and promoting developmental effectiveness. During 2018, BSTDB chaired and hosted in Thessaloniki six multilateral meetings, including those on the ERMSUGIO and on IFIs Compensation and Benefits, EDFI working groups on Corporate Governance, Development Effectiveness, and Environmental and Social Standards, and the IFIs experts meeting on Harmonized Indicators for Private Sector Operations. Also in 2018, the Bank's Evaluation Office assumed the duty and honor of becoming the Chair of the Evaluation Cooperation Group of the Multilateral Development Banks.

Promoting regional cooperation and business generation

BSTDB maintained strategic support for regional cooperation, contributing to the joint efforts of the Organization of the Black Sea Economic Cooperation (BSEC) and its family regional institutions, with special attention paid to maintaining close collaboration with the Parliamentary Assembly of BSEC. BSTDB strengthened further its involvement and support for BSEC project-oriented activities.

In the framework of the Annual Meeting, the Bank organized a Business Forum titled 'BSTDB: Supporting Russia's Growth and Regional Cooperation' on 2 July, 2018. The Forum held in cooperation with the business association 'Business Russia' and the Chamber of Commerce and Industry of the Krasnodar region gathered 200 participants, a large proportion of them women, mostly from the South of Russia. BSTDB made a detailed presentation of its financial products, business practices and technical assistance opportunities offered to Russian businesses. BSTDB bankers had B2B meetings with interested companies to discuss investment initiatives and cooperation opportunities.

During the Forum, the Bank and the Russian business association 'Delovaya Rossiya' signed a Cooperation Agreement aimed to jointly promote regional trade and economic cooperation in Russia.

In 2018, BSTDB senior management and staff promoted the Black Sea region as an investment destination and shared the Bank's expertise on doing business in the Region while contributing as speakers and panelists in 14 major international events, including: the Russian Investment Forum (Sochi), First International Banking Conference (Ankara), Innovative Approaches for Mobilizing Finance for Sustainable Growth organized by the New Development Bank (Shanghai), Thessaloniki Summit, and Balkans and Black Sea Business Forum (Athens), Strategic Planning in the Regions and Cities of Russia (St. Petersburg), and Tirana Economic Forum (Albania).

Enhancing institutional transparency and outreach

In 2018, the Bank made a major breakthrough in its social media presence. The number of the Bank's followers exceeded 26,000 across Facebook, Twitter and LinkedIn, a 99% gain over 2017. BSTDB's content had over 3.2 million impressions during the year, thus becoming an increasingly important 'voice' in the Black Sea region for people to find out about the Bank's activities, but also to discover news about the region and learn about economic development and learn about cooperation in member countries.

BSTDB strives to promote regional cooperation beyond its immediate business mandate. With this in mind, the Bank started hosting art exhibitions from member countries at its premises in Thessaloniki. In 2018, two exhibitions of Turkish and Bulgarian painters were organized by the Bank, as well as an exhibition of paintings by the children of the Bank's staff.

Administrative Services

During 2018, the Administrative Services continued efforts to improve the overall efficiency of the Bank and to provide a higher quality of service.

- **Space utilization:** The new exhibition gallery was inaugurated, while the storage area doubled in size through internal adjustments and the exercise facilities were expanded.
- **Security:** The last tranche of additional safety measures, based on the overhaul of the security system, was implemented.
- **New premises:** All necessary preparatory steps were completed towards identifying potential buildings that would permanently host the Bank's headquarters, prior to the corresponding strategic decisions of the Board of Directors.
- **Residence permits:** The assignment of residence permits to staff members' children coming of age was finally resolved, with the assistance of the Greek authorities.
- **Event support:** The reassignment of human resources improved event support, in line with the increased emphasis on outreach events serving the Bank's marketing plan.

Nominee Directors

In 2018, the Bank appointed its second external nominee director, this time to a real estate development client, moving further ahead in following international best practices on director nominations to investee companies.

Financial Statements for the Year Ended 31 December 2018

Together with Auditor's Report

INTERNAL CONTROLS OVER EXTERNAL FINANCIAL REPORTING

Responsibility for external financial reporting

Management's responsibility

Management's report regarding the effectiveness of internal controls 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 auditing 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 controls 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 controls over financial reporting and any other matters they believe should be brought to the attention of the Audit Committee.

The Bank has assessed its internal controls over external financial reporting for 2018. 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, at 31 December 2018, the Bank maintained effective internal controls over its financial reporting as contained in the Financial Statements for 2018.

The Bank's external auditors have issued an audit report on the fairness of the financial statements presented within this report. In addition, they have issued a reasonable assurance report on the effectiveness of the Bank's internal controls over financial reporting.

Dmitry Pankin
President

Black Sea Trade and Development Bank
Thessaloniki
19 April 2019

Valeriy Piatnytskyi
Vice President Finance

Independent Reasonable Assurance

KPMG

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

Report on the effectiveness of internal control over financial reporting

We were engaged by the Board of Directors of the Black Sea Trade and Development Bank to report on the effectiveness of the Black Sea Trade and Development Bank's ('the Bank') internal control over financial reporting as of 31 December 2018 in the form of an independent reasonable assurance conclusion about whether the internal control over financial reporting is effective based on criteria established in 'Internal Control - Integrated Framework' issued by the Committee of Sponsoring Organisations of the Treadway Commission (the COSO criteria).

Bank's responsibilities

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 responsibilities

Our responsibility is to express an opinion on the Bank's internal control over financial reporting based on the evidence obtained. We conducted our audit in accordance with the International Standard on Assurance Engagements (ISAE) 3000. That standard requires that we comply with ethical requirements, including independence requirements, and plan and perform our procedures to obtain reasonable assurance about whether the internal control over financial reporting is effective, in all material respects.

The procedures selected depend on our judgment, including the assessment of the risks of material misstatement of the effectiveness of internal control over financial reporting whether due to fraud or error.

Our engagement also 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. Reasonable assurance is less than absolute assurance.

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 includes 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.

Conclusion

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

In our opinion, Black Sea Trade and Development Bank maintained, in all material respects, effective internal control over financial reporting, as of 31 December 2018, based on the COSO criteria.

KPMG Certified Auditorrs S.A.

Athens, Greece
19 April 2019

INCOME STATEMENT

For the year ended 31 December

Presented in thousands of EUR	Note	2018	2017
Interest income	7	78,717	68,146
Interest expense	8	(37,974)	(37,225)
Net interest (expense) on derivatives		(7,599)	(3,153)
Net interest income		**33,144**	**27,768**
Net fees and commissions	9	1,652	2,087
Dividend income		-	1,715
Net gains from equity investments through profit or loss	15	572	4,263
Net gains from debt investment securities through OCI		29	482
Foreign exchange income (losses)		(1,352)	2,110
Other (loss) income		(3)	(3)
Operating income		**34,042**	**38,422**
Personnel expenses	10,25	(15,952)	(14,775)
Other administrative expenses	10	(4,770)	(4,505)
Depreciation and amortization	17,18	(453)	(461)
Income before impairment		**12,867**	**18,681**
Impairment (losses) on loans at amortized cost	11	(6,292)	(9,125)
Impairment (losses) on guarantees		-	(8)
Impairment (losses) on debt investment securities through OCI	12	(368)	(276)
Fair value (losses) on loans through profit or loss	14	(446)	(2,217)
Fair value gains (losses) on equity investments through profit or loss	15	(585)	1,600
Net income for the year		**5,176**	**8,655**

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

STATEMENT OF OTHER COMPREHENSIVE INCOME

For the year ended 31 December

Presented in thousands of EUR	Note	2018	2017
Net income for the year		5,176	8,655
Other comprehensive income:			
Items that will not be reclassified to profit or loss:			
Remeasurements of defined benefit liability (asset)	23	2,414	231
Net change in equity investments financial assets	23	713	(21,641)
Items that are or may be reclassified to profit or loss:			
Net change in investment securities financial assets	23	(8,929)	2,347
Total comprehensive income (loss) for the year		**(626)**	**(10,408)**

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

STATEMENT OF FINANCIAL POSITION

At 31 December

Presented in thousands of EUR	Note	2018	2017
Assets			
Cash and cash equivalents	24	48,598	81,481
Debt investment securities at amortized cost	12,24	49,339	-
Debt investment securities at fair value through other comprehensive income	12,24	346,640	292,524
Less: impairment losses	12	(644)	(276)
Debt investment securities net		395,335	292,248
Derivative financial instruments – assets	13	662	1,659
Loans at amortized cost	14,16	1,318,418	1,132,359
Less: deferred income	14	(3,052)	(6,219)
Less: impairment losses	11,14	(34,775)	(47,996)
Loans at fair value through profit or loss	14	12,277	2,722
Loans net of impairment		1,292,868	1,080,866
Equity investments at fair value through profit or loss	15,16	1,015	1,600
Equity investments at fair value through other comprehensive income	15,16	26,640	29,761
Equity investments at fair value		27,655	31,361
Property and equipment	17	455	501
Intangible assets	18	653	653
Other assets	19	29,541	26,157
Total Assets		**1,795,767**	**1,514,926**
Liabilities			
Borrowings	20	954,030	722,592
Derivative financial instruments – liabilities	13	24,164	18,242
Payables and accrued interest	21	15,973	15,422
Total liabilities		994,167	756,256
Member's Equity			
Authorized share capital	22	3,450,000	3,450,000
Less: unallocated share capital	22	(1,161,500)	(1,161,500)
Subscribed share capital	22	2,288,500	2,288,500
Less: callable share capital	22	(1,601,950)	(1,601,950)
Less: payable share capital	22	-	(44,984)
Less: payable share capital past due	22,28	(1,428)	-
Paid-in share capital		685,122	641,566
Reserves	23	32,957	33,583
Retained earnings		83,521	83,521
Total members' equity		801,600	758,670
Total Liabilities and Members' Equity		**1,795,767**	**1,514,926**
Off-balance-sheet items			
Commitments	16	252,801	185,563

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

STATEMENT OF CHANGES IN MEMBERS' EQUITY

For the year ended 31 December

Presented in thousands of EUR	Share capital					
	Subscribed	Callable	Payable	Reserves	Retained Earnings	Total
At 31 December 2016	**2,288,500**	**(1,601,950)**	**(72,741)**	**47,177**	**91,684**	**752,670**
Impact of adoption IFRS at 1 January 2017	-	-	-	-	(11,349)	(11,349)
Restated balance at 1 January 2017	**2,288,500**	**(1,601,950)**	**(72,741)**	**47,177**	**80,335**	**741,321**
Total comprehensive income						
Net income for the year	-	-	-	-	8,655	8,655
Other comprehensive income:						
Fair value reserve (available financial assets)	-	-	-	(19,294)	-	(19,294)
Remeasurement of defined benefit liability	-	-	-	231	-	231
Total comprehensive income	-	-	-	(19,063)	8,655	(10,408)
Transactions with owners of the Bank						
Members' contributions:						
Paid-in share capital	-	-	27,757	-	-	27,757
Transfer to general reserve	-	-	-	5,469	(5,469)	-
Total contributions and distributions	-	-	27,757	5,469	(5,469)	27,757
At 31 December 2017	**2,288,500**	**(1,601,950)**	**(44,984)**	**33,583**	**83,521**	**758,670**
Total comprehensive income						
Net income for the year	-	-	-	-	5,176	5,176
Other comprehensive income:						
Fair value reserve (financial assets)	-	-	-	(8,216)	-	(8,216)
Remeasurement of defined benefit liability	-	-	-	2,414	-	2,414
Total comprehensive income	-	-	-	(5,802)	5,176	(626)
Transactions with owners of the Bank						
Members' contributions:						
Paid-in share capital	-	-	43,556	-	-	43,556
Transfer to general reserve	-	-	-	5,176	(5,176)	-
Total contributions and distributions	-	-	43,556	5,176	(5,176)	43,556
At 31 December 2018	**2,288,500**	**(1,601,950)**	**(1,428)**	**32,957**	**83,521**	**801,600**

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

STATEMENT OF CASH FLOWS

For the year ended 31 December

Presented in thousands of EUR	Note	2018	2017
Cash flows from operating activities			
Net income for the year		5,176	8,655
Adjustment for:			
Depreciation and amortization	17,18	453	461
Impairment losses	11,12	6,660	9,409
Fair value losses on loans at FVTPL	14	446	2,217
Fair value (gains) losses on equity investments at FVTPL	15	585	(1,600)
Net interest income		(33,144)	(27,768)
Foreign exchange adjustment on provisions	11	1,073	(2,124)
Operating (loss) before changes in operating assets		(18,751)	(10,750)
Changes in:			
Derivative financial instruments	13	6,919	(17,941)
Other assets	19	(189)	(1,143)
Accounts payable	21	(808)	622
Deferred income	14	(3,167)	(1,407)
Fair value movements	23	(8,216)	(19,294)
Cash generated from operations		(24,212)	(49,913)
Proceeds from repayment of loans	14	377,988	318,214
Proceeds from repayment of equity investments		4,756	9,408
Funds advanced for loans	14	(572,966)	(386,211)
Funds advanced for equity investments		(859)	(7,556)
Foreign exchange and other adjustments		(827)	91,542
Interest income received		75,522	68,784
Interest expense paid		(44,214)	(41,155)
Net cash from / (used in) operating activities		(184,812)	3,113
Cash flows from investing activities			
Proceeds from investment securities at FVTOCI		409,139	573,130
Purchase of investment securities at FVTOCI		(523,141)	(575,025)
Purchase of property, software and equipment	17,18	(408)	(630)
Net cash from / (used in) investing activities		(114,410)	(2,525)
Cash flows from financing activities			
Proceeds received from share capital	22	43,556	27,757
Proceeds from borrowings	20	433,639	106,736
Repayments of borrowings	20	(202,201)	(246,677)
Net cash from / (used in) financing activities		274,994	(112,184)
Net increase in cash and cash equivalents		**(24,228)**	**(111,596)**
Cash and cash equivalents at beginning of year	24	196,481	308,077
Cash and cash equivalents at end of year	24	**172,253**	**196,481**

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

NOTES TO THE FINANCIAL STATEMENTS

1. ESTABLISHMENT OF THE BANK

Agreement Establishing the Bank

Black Sea Trade and Development Bank ('Bank'), whose headquarters is located at 1 Komninon Street, Thessaloniki, in the Hellenic Republic, was established as an international financial organization under the Agreement Establishing the Bank dated 30 June 1994 ('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 customers.

As at financial position date the Bank's shareholders comprised of the following 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 Hellenic Republic are defined in the Headquarters Agreement between the Government of the Hellenic Republic and the Bank ('Headquarters Agreement') signed on 22 October 1998.

2. BASIS OF PREPARATION OF FINANCIAL STATEMENTS

Statement of Compliance

The financial statements have been prepared in accordance with International Financial Reporting Standards (IFRS) as published by the International Accounting Standards Board (IASB). The financial statements for the year ended 2018 were submitted by the Management Committee to the Board of Directors (BoD) for approval on 19 April 2019, 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 (BoG) in their Annual Meeting to be held on 16 June 2019.

Basis of Measurement

The financial statements have been prepared on a historical cost basis except for certain financial assets and derivative contracts which are measured at fair value.

Functional and Presentation Currency

The Bank's functional currency is the Euro (EUR) as defined by the European Central Bank (ECB). The Euro is most representative of the Bank's operations and environment as a significant percentage of the Bank's lending operations are in Euro, and the administrative expenses and capital expenditures are primarily denominated and settled in this currency. The Bank's presentation currency is the EUR.

Judgments and Assumptions

The preparation of the financial statements in accordance with IFRS requires Management to make judgments and assumptions that affect the application of accounting policies and the reported amounts of assets and liabilities, income and expenses. Actual results may differ from these estimates.

Estimates and underlying assumptions are reviewed on an ongoing basis. Revisions to accounting estimates are recognized in the year in which the estimates are revised and in any future periods affected.

Information about significant areas of estimations uncertainty and critical judgments in applying accounting policies that have the most significant effect on the amounts recognized in the financial statements are included in Note 4.

3. SIGNIFICANT ACCOUNTING POLICIES

A summary of the Bank's accounting policies applied in the preparation of these financial statements are presented in this section. These policies have been consistently applied to all periods presented in the financial statements.

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 denominated in foreign currencies at the end of year are recorded in the income statement.

The Bank uses the official exchange rates published for the EUR by the ECB. The exchange rates used by the Bank at the financial position date were as follows.

			31 December 2018	31 December 2017
1 EUR	=	United States dollar	1.14500	1.19930
	=	Pound sterling	0.89453	0.88723
	=	Russian ruble	79.71530	69.39200
	=	Azerbaijan manat	1.94680	2.03070
	=	Georgian lari	3.07010	3.11690
	=	Armenian dram	553.65000	568.10000
	=	Romanian leu	4.66350	4.65850

Recognition and Derecognition of Financial Instruments

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

The Bank derecognizes a financial asset or a portion of financial asset 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 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.

On derecognition of a financial asset, the difference between the carrying amount of the asset (or the carrying amount allocated to the portion of the asset derecognized) and the sum of (i) the consideration received (including any new asset obtained less any new liability assumed) and (ii) any cumulative gain or loss that had been recognized in OCI is recognized in net income or loss.

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 of change in value due to the movements in market rates.

Financial Assets

The classification of financial assets defines how existing information is reflected in the financial statements. In particular, the valuation method and the impairment calculation are defined by this classification, which are based on criteria established by the Bank.

Classification

The Bank recognizes a financial asset in its financial statements at the time of the creation of the contractual claim (that is, the day the transaction took place). In recognition, the Bank determines the business model to which it belongs. Financial assets are classified in three categories:

1. Financial assets measured at amortized cost (AC): this category classifies each asset or group of assets for which the Bank's business model constitutes its holding for the purpose of collecting contractual cash flows. The possible sale of financial assets should not be the result of business planning for their management.

2. Financial assets measured at fair value through other comprehensive income (FVOCI), and are after reclassified at fair value through profit or loss (FVTPL) on derecognition: gains or losses arising from the measurement are recorded in a separate members' equity account. This category classifies each asset or group of assets for which the Bank's business model recommends that it be held for the purpose of collecting contractual cash flows and selling them when the business planning of their acquisition has been achieved.

3. Financial assets (equity instruments) measured at fair value through other comprehensive income. The Bank made an irrevocable election to designated equity instruments at fair value through other comprehensive income. This designation is made at initial recognition and on an instrument basis. Gains and losses on these instruments , including where derecognized, are

recorded in other comprehensive income and are not subsequently reclassified to the income statement. Dividends received are recorded in the income statement.

In order to classify assets in the above two categories, contractual cash flows should consist solely of payments of principal and interest (SPPIs).

4. Financial assets measured at FVTPL: this category classifies items that do not meet the SPPI criterion as well as the items that the Bank holds for trading. Their classification depends primarily on the following two important factors (i) the Bank's business model for these assets and (ii) the characteristics of the contractual cash flows of the asset.

Measurement

The Bank measures financial assets at fair value on initial recognition. Assets classified at FVTPL are valued at their transaction price. Assets classified at AC, any transaction costs, or creation costs are included in their transaction price at their measurement. In the event the Bank considers that the fair value on initial recognition differs from the transaction price, that difference is recognized as a gain or loss on initial recognition but only if the fair value is based on a requested active market price for identical assets or is based on a valuation technique using data solely from identified markets. In all other cases the fair value is adjusted to the amount of the transaction price.

Financial assets that are subsequently measured at either AC or debt instruments at fair value through other comprehensive income, are subject to provisions for impairment.

Treasury operations 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.

Based on the Bank's credit policy, the Bank does not originate credit-impaired financial assets, nor does the Bank purchase credit-impaired assets as, for example, those loans would be acquired at a deep discount.

Financial assets are not reclassified subsequent to their initial recognition, except in the period after the Bank changes its business model for managing financial assets.

Business model assessment

The factor of the business model refers, amongst others, to the manner in which the Bank manages its financial assets by classifying them in portfolios that are part of its business model. The assessment process applied by the Bank through its business model, based on strategic objectives, classifies its assets in the following three categories in accordance with IFRS 9:

i) Hold to collect

Each asset or bank of assets for which the Bank's business model recommends that it be held for the purpose of collecting contractual cash flows is classified as 'Hold to collect'.

ii) Hold to collect and sell

Each asset or bank of assets for which the Bank's business model recommends that it be held for the purpose of collecting contractual cash flows and selling them when the strategic planning of their acquisition has been achieved is classified as 'Hold to collect and sell'.

iii) Trading portfolio

The financial assets held for trading are classified as 'Trading portfolio'.

The adopted business model determines the source of revenue, as it arises from individual portfolios either through the collection of contractual cash flows or from the sale of financial assets or the combination of the above.

The assessment of the business model reflects the Bank's strategy under normal business conditions. The assessment is not affected by actions required in 'emergency situations' (e.g. liquidity needs, non-inherent capital requirements for credit risk, etc.). Also, Management decisions taken to comply with new regulatory guidelines are not included in the assessment.

In general, the Bank has included the majority of its loan portfolios in the hold-to-collect business model. The assessment of a business model is made within the definition of operational objectives as defined by the Bank's Management, as well as in the operational management of its assets. The assessment is effected at portfolio level rather than individual assets.

The Business Model applied to loan portfolio, treasury portfolio and equity investment portfolio is reassessed at each reporting period. The reassessment of Business Model has been established in order to determine if evidence initially used has been changed.

Impairment

IFRS 9 provides that impairment of financial assets will occur regardless of whether a loss event has already occurred and therefore all financial assets measured at AC will be tested to determine whether their fair value has changed significantly since the date of their creation. This resulted in the classification of the data in 3 stages, which in ascending order indicates the credit risk and corresponding provisioning charge of each item.

As such, Stage 1 includes assets whose credit quality is not significantly degraded and the impairment that they will incur will be equal to a 12-month Expected Credit Loss (ECL). Stage 2 includes assets whose credit quality has been substantially downgraded and are subject to lifetime ECL. The same applies to the items classified in Stage 3, where all the impaired items, including non-performing loans (NPLs), fall.

Calculation of expected credit loss

The Bank recognizes allowance for ECLs that reflect changes in credit quality since initial recognition to financial assets that are measured at AC and FVOCI, including loans, debt securities, and loan commitments. No ECLs are recognized on equity investments. ECLs are a probability-weighted average estimate of credit losses that reflects the time value of money. Upon initial recognition of the financial instruments in scope of the impairment policy, the Bank records a loss allowance equal to a 12-month ECL, being the ECL that results from default events that are possible within the next 12 months. Subsequently, for those financial instruments that have experienced a significant increase in credit risk (SICR) since initial recognition, a loss allowance equal to lifetime ECL is recognized, arising from default events that are possible over the expected life of the instrument. The expected credit losses are weighted on the basis of three macroeconomic scenarios (adverse, basic and favorable).

Classification of loans into stages based on credit risk (Staging)

The Bank has introduced a number of criteria for the classification of financial assets in stages. These criteria are intended to check whether there has been a significant deterioration in the credit quality of financial assets since their creation. Essentially, the Bank examines:

- Days past due;
- If there has been a significant downgrade of the credit rating of the assets;
- Qualitative parameters indicating a change in credit quality (e.g. dealing with financial difficulties); and
- Whether a financial asset is characterized as credit impaired.

Basic parameters used for the calculation of expected credit loss

The calculation of expected credit losses is based on the probability of default (PD), loss given default (LGD), exposure at default (EAD) and other parameters such as the credit conversion factor (CCF) and the prepayment rate. The Bank has obtained from an external provider a system of calculating expected credit losses. The basic parameters have been drawn from statistical models developed in cooperation with the external provider, utilizing the existing risk management infrastructure and practices of the Bank and the know-how and experience of the provider.

PD represents the probability that a debtor will default on his debt obligations either over the next 12 months or over the remaining maturity of his debt. In accordance with IFRS 9, the Bank uses non-discriminatory point-in-time PDs that adjust to macroeconomic assumptions using the ECL.

EAD is defined as the estimate of the exposure in the event of a default of the debtor. The EAD of a financial asset represents its gross carrying amount in the event of a default.

LGD represents the extent of the loss that the Bank expects for exposures that are in default and is defined as the difference between the contractual cash flows and those that the Bank expects to collect, including collateral amounts. LGD, which is usually expressed as a percentage of the EAD, varies according to the category of the counterparty, the category and priority of the claim, the existence of collateral and other credit enhancements.

CCF is used to convert credit lines and other off-balance-sheet exposures into EAD amounts. It is considered as an assumption representing the percentage of undrawn exposures expected to be disbursed prior to the occurrence of the default event. The prepayment rate is an estimate of premature repayments of a financial exposure that exceeds contractual repayments on the basis of the repayment schedule and is expressed as a percentage of the EAD in each reporting period, resulting in a reduction in the EAD.

The Bank has made use of three macroeconomic scenarios (adverse, basic and favorable) taking into account the relative chances of each of the scenarios. The baseline scenario is the most likely scenario and is in line with the Bank's information for strategic planning and budgeting purposes.

Hedge Accounting

IFRS 9 introduces a new general hedge accounting model, which links hedge accounting to risk management activities by the Bank's Management. According to the new model, additional hedging strategies may meet the hedge accounting criteria, new requirements apply to the effectiveness of hedging, while terminating hedge accounting will be permissible only under certain conditions. The International Accounting Standards

Board with regard to the macro-hedging accounting is carrying out a separate work that is in progress. Until such work is completed as an accounting policy, the Bank will continue to apply the requirements of IAS 39 for hedge accounting.

a) Financial assets, at amortized cost (AC)

Financial assets are classified at AC only if both of the following criteria are met:

1. The objective of the Bank's business model is to hold the asset in order to collect the contractual cash flows; and
2. The contractual terms give rise on specified dates to cash flows that are solely payments of principal and interest on the principal outstanding:
   (i) Principal is the fair value of the financial asset at initial recognition.
   (ii) Interest consists of consideration for the time value of money, for the credit risk associated with the principal amount outstanding during a particular period of time and for other basic lending risks and costs, as well as a profit margin.

The Bank's operations, which are non-derivative with fixed or determinable payments and with fixed maturities, meeting the above criteria are measured initially at fair value plus transaction costs and including any premium or discount that may arise on the date of acquisition. Third party expenses, such as legal fees, incurred in securing a loan are treated as part of the cost of the transaction. These financial assets are subsequently measured at ACt using the effective interest method, less any provision for impairment or uncollectability. All other fees and related income generated are reported in the income statement (see note: 'Net fees and commissions'). All such financial assets are recognized on settlement date.

These financial assets include cash and cash equivalents, loans and advances on amounts disbursed to operations, receivables accrued, and certain debt investments that meet the above criteria.

b) Financial assets, at fair value through other comprehensive income

b1. Debt instruments

Debt instruments are classified and subsequently measured at FVTOCI only if both of the following criteria are met:

1. The objective of the Bank's business model is achieved by both collecting the contractual cash flows and selling the financial asset; and
2. The contractual terms give rise on specified dates to cash flows that are solely payments of principal and interest on the principal outstanding:
   (i) Principal is the fair value of the financial asset at initial recognition.
   (ii) Interest consist of consideration for the time value of money, for the credit riskassociated with the principal amount outstanding during a particular period of time and for other basic lending risks and costs, as well as a profit margin.

This category includes financial assets such as Euro Commercial Paper (ECP) or bonds that are intended to be held to maturity, which may or may not be sold in the future. Their fair value is determined by reference to quoted market bid prices. 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 are recognized directly in income. All such financial assets are recognized on trade date.

Financial assets not meeting the above criteria, as well as those financial assets designated shall be measured at FVTPL.

b2. Equity instruments

On initial recognition the Bank can make an irrevocable election, on an instrument-by-instrument basis, to designate investments in an equity instrument not held for trading nor contingent consideration, as a financial asset measured at FVTOCI. Those not elected are measured at FVTPL.

After initial recognition at cost, plus transaction costs, these financial assets are subsequently measured at fair value with all gains and losses arising from changes in fair value (realized and unrealized), including foreign exchange gains and losses, recognized in other comprehensive income as a separate component of members' equity. For those not purchased from an active market the fair value is determined using accepted valuation techniques. These valuation techniques used are net asset value and earnings-based valuations using comparable information and discounting cash flows. All such financial assets are recognized on settlement date.

The cumulative gains or losses are not reclassified, e.g. not recycled, to income on disposal of the investments and no provisions for impairments are recognized in the income statement. However, the cumulative gain or loss after the investment is subsequently derecognized can be transferred within members' equity.

Dividends received are included in income statement.

c) Financial asset, at fair value through profit or loss (FVTPL)

Financial assets that are classified at FVTPL are initially measured at their fair value and subsequently carried at fair value on the statement of financial position with all changes in fair value gains and losses and foreign exchange gains and losses, recognized in the income statement in the period in which they occur. Transaction costs on these financial assets are expensed in the income statement.

This category includes any treasury assets held for trading or resale to realize short-term fair value changes as well as any loans for which either of the criteria for recognition at AC is not met. It can also include a debt instrument or an equity instrument that is not within the category nor measured at FVTOCI. Derivative instruments are also categorized as financial assets at FVTPL. All such financial assets are recognized on trade date.

In addition, a debt instrument that could meet AC criteria can be designated and measured at FVTPL. Upon initial recognition, if such designation significantly reduces or eliminates a measurement or recognition inconsistency, referred to as an 'accounting mismatch', which would arise from measuring assets or recognizing the gains and losses on them on different bases.

Financial Liabilities

The Bank recognizes a financial liability in its financial statements at the time of the arising from the item (that is, the day the transaction took place). Financial liabilities primarily include (a) borrowings and (b) other liabilities.

a) Borrowings

Borrowing transactions are recognized in the statement of financial position at the time the funds are transferred to the Bank. They are measured initially 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 AC value is adjusted to fair value by the hedged risks, with any changes in value recognized in income. Relevant interest expenses are reported in the income statement using the effective interest rate method.

b) Other liabilities

Other liabilities that are not derivatives or designated at FVTPL, are recorded at AC. The amounts include accrued finance charges on borrowings and other accounts payable.

Offsetting of Financial Assets and Liabilities

Offsetting 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 realize the asset and settle the liability simultaneously.

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 the income statement. Fair values are obtained from quoted market prices, to the extent publicly available, discounted cash flows and options pricing models as appropriate.

a) Hedge accounting

The Bank has chosen to continue to apply the hedge accounting requirements of IAS 39, instead of the requirements of IFRS 9. The Bank has applied this accounting policy to all its hedging relationships.

In order to manage particular risks, the Bank applies hedge accounting for derivative transactions which meet specified criteria relative to debt securities issued by the Bank. A valid hedge relationship exists when a specific relationship can be identified between two or more financial instruments in which the change in value of one instrument (the hedging instrument) is highly negatively correlated to the change in value of the other (the hedged item). The Bank only applies hedge accounting treatment to individually identified hedge relationships on a one-to-one basis.

The Bank documents the relationship between hedging instruments and hedged items upon initial recognition of the transaction.

If the hedging instrument expires or is sold, terminated or exercised, or where the hedge no longer meets the criteria for hedge accounting, the hedge relationship is discontinued prospectively. Any fair value adjustment is recognized immediately in the income statement. At the financial position date the Bank did not have any cash flow hedge.

i) Fair value hedge

Changes in the fair value of the derivatives that are designated and qualify as fair value hedges, and that prove to be highly effective in relation to hedged risk, are included in the income statement as fair value hedges under 'net gains or losses at fair value on hedging activities', along with the corresponding change in fair value of the hedged asset or liability that is attributable to that specific hedged risk.

Impairment

For the Bank, and in accordance with IFRS 9, a loss allowance for expected credit losses is recognized on financial assets that are measured (i) at amortized cost (ii) at fair value through other comprehensive income (iii) lease receivable contracts (iv) loan commitments and (v) financial guarantee contracts.

Financial instruments, including equity instruments, carried at FVTPL are not subject to impairment requirements as their fair value reflects the credit of these exposures. Additionally, equity investments measured at FVTOCI are also not subject to impairment requirements, but a negative reserve balance in relation to the carrying amount of that equity investment, e.g. representing an impairment loss, shall be recognized in other comprehensive income and shall not be recycled (reclassified and transferred) to net income or loss.

Definition of default

The definition of default used for determining the risk of a default occurring shall be applied consistently to all financial instruments unless information becomes available that demonstrates that another default definition is more appropriate for a particular financial instrument. The Bank's definition of default is based on the regulatory definition under Article 178 of the 'Regulation (EU) No 575/2013 of the European Parliament and of the Council of the European Union of 26 June 2013 on prudential requirements for credit banks and investment firms and amending Regulation (EU) 648/2012' (CRR). A default is considered to have occurred when either of the following conditions have taken place.

i) Qualitative

Unlikeliness to Pay (UTP) criterion: the Bank considers that the obligor is unlikely to pay its credit obligations to the Bank without recourse by the Bank to actions such as realizing security. Below are some elements taken as indications of unlikeliness to pay (in line with CRR (Article 178)).

- The Bank puts the credit obligation on non-accrued status.
- The Bank recognizes a specific credit adjustment resulting from a significant perceived decline in credit quality subsequent to the institution taking on the exposure.

- The Bank has filed for the obligor's bankruptcy or a similar order in respect of an obligor's credit obligation to the institution, the parent undertaking or any of its subsidiaries.
- The obligor has sought or has been placed in bankruptcy or similar protection where this would avoid or delay repayment of a credit obligation to the institution, the parent undertaking or any of its subsidiaries.

ii) Quantitative

Past due criterion: the exposure is past due more than 90 days on any credit obligation to the Bank.

The definition of default is applied in the relevant parameters used for the ECL measurement, those being the EAD, PD and LGD models.

a) Financial assets

The impairment requirements of IFRS 9 apply to financial assets that are measured at AC or FVTOCI, and off-balance-sheet lending commitments such as loan commitments and financial guarantees.

Impairment losses and allowance are determined based on an expected loss model, where provisions for impairment are taken upon initial recognition of the financial asset (or the date that the Bank becomes a party to the loan commitment or financial guarantee), based on expectations of potential credit losses at that time.

Under IFRS 9 for financial assets originated or purchased on initial recognition the Bank recognizes an impairment loss at an amount equal to 12-month ECL. This shall continue if the credit risk at the reporting date has not increased significantly since initial recognition; therefore, was and shall remain in Stage 1. Such provision charge represents the ECL resulting from default events that are possible within the next 12 months.

IFRS 9 requires the recognition of credit losses over the remaining life of the financial assets ('Lifetime expected credit losses') which are considered to have experienced a significant increase in credit risk (e.g. Stage 2) and for financial assets that are credit impaired at the reporting date (e.g. Stage 3). The lifetime ECLs represent all possible default events over the expected life of a financial instrument. The Bank leverages existing risk management indicators (e.g. watch list and threshold trigger), credit rating changes and takes into consideration reasonable and supportable information which allows it to identify whether the credit risk of financial assets has significantly increased. This process includes considering forward-looking information, including macroeconomic factors. Forward looking information, including macroeconomic factors are taken into account to measure IFRS 9 compliant ECLs. Furthermore, financial assets would be transferred to Stage 2 if more than 30 days past due.

Interest income is calculated on the gross carrying amount for financial assets in Stage 1 and 2. As the primary definition for credit impaired financial assets moving to Stage 3, the Bank applies the definition of default as stated above. Interest income is calculated on the net carrying amount for these financial assets only.

Credit loss is defined as the difference between all contractual cash flows that are due in accordance with the contract and all the cash flows expected to be received (i.e. all cash shortfalls), discounted at the original effective interest rate (EIR). All contractual cash flows of the loan and cash flows resulting from the sale of collateral or other credit enhancements are considered.

According to IFRS 9, probability-weighted scenarios have to be taken into account over the expected life of the financial instrument for the estimation of expected losses. The assessment consists of an evaluation of a range of possible outcomes which involves identifying possible scenarios that specify the amount and timing of the cash flows for each particular outcome and the estimated probability of that particular outcome.

The Bank measures impairment losses on an individual basis. Similarly, the assessment for transferring financial assets between Stages 1, 2 and 3 are also made on an individual basis. The Bank applies three main components to measure expected credit losses which are a LGD, PD and EAD. In order to perform the ECL calculation, the Bank uses the Moody's Analytics IFRS ImpairmentCalc tool. Within the tool, the Bank provides probabilities of default and loss given defaults, and assigns scenarios for potential credit risk deterioration. There can be transfers of exposures from one stage to another, depending on whether there is a change in the credit risk of that exposure. Probability of default is an estimate of the likelihood of default over a given time horizon. The Bank uses information obtained from the Global Emerging Markets (GEMs) database in order to assign PDs to its lending asset classes. GEMs is an IFI-wide initiative designed to pool default and recovery rates experienced by IFIs in emerging markets. Treasury asset classes derive their PDs from the assigning rating agency.

LGD is an estimate of the loss arising on default. It is based on the difference between the contractual cash flows due and those that the Bank would expect to receive, including the cash flows from the liquidation of any collateral. The Bank uses information obtained from the GEMs database in order to assign LGDs to its banking asset classes. Treasury asset classes derive their LGDs from the assigning rating agency.

Exposure at default is an estimate of the exposure at a future default date, taking into account expected changes in the exposure after the reporting date, including repayments of principal and interest, and expected drawdowns on off-balance-sheet commitments.

i) Credit-impaired

A financial asset is credit-impaired when one or more events that have a detrimental impact on the estimated future cash flows of that financial asset have occurred. Evidence that a financial asset is credit-impaired includes observable data about the following events:

- Significant financial difficulty of the issuer or the borrower;
- A breach of contract, such as a default or past due event;
- The lender(s) of the borrower, for economic or contractual reasons relating to the borrower's financial difficulty, having granted to the borrower a concession(s) that the lender(s) would not otherwise consider;
- It is becoming probable that the borrower will enter bankruptcy or other financial reorganization;
- The disappearance of an active market for that financial asset because of financial difficulties; or
- The purchase or origination of a financial asset at a deep discount that reflects the incurred credit losses.

It may not be possible to identify a single discrete event – instead, the combined effect of several events may have caused financial assets to become credit-impaired.

ii) Significant increase in credit risk

At each reporting date, the Bank assesses whether the credit risk on a financial instrument has increased significantly since initial recognition. When making the assessment, the Bank compares the risk of a default occurring on the financial instrument as at the reporting date with the risk of a default occurring on the financial instrument as at the date of initial recognition and considers reasonable and supportable information that is available without undue cost or effort, that is indicative of significant increases in credit risk since initial recognition.

Generally, there will be a significant increase in credit risk before a financial asset becomes credit-impaired or an actual default occurs. The assessment of significant increase in credit risk is key in transferring an exposure from Stage 1 to Stage 2 or 3 and the respective change in the ECL measurement from 12-month to lifetime ECL. A combination of quantitative and qualitative factors structured as primary and secondary drivers will be considered, and are also supplemented with backstop options. The backstop triggers automatic stage transfers even though the primary and secondary indicators may not trigger such transfer, unless this result is due to a data error, operational issues, or timing difference in applying cash, received up to 30 days, to the customer account.

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.

Impairment losses for guarantees are recognized while a guarantee is in effect and the amounts are determined based on the level of utilization of the guarantee. The methodology is consistent to that of loan commitments, and such losses are included in 'Other liabilities'.

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.

b) 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.

c) Renegotiated financial assets

When necessary, the Bank seeks to restructure a financial asset that may involve extending the payment arrangements and the agreement of new loan conditions. These are generally renegotiated in response to an adverse change in the financial conditions of the borrower.

Modifications occur when the contractual cash flows of a financial asset are renegotiated or otherwise modified. Some modifications result in derecognition of the existing asset and recognition of a new asset, while other modifications do not result in derecognition. Modifications that result in derecognition are considered to be substantial modifications. A significant or substantial change is defined when the customer enters into a new loan contract (i.e. completely new product and new pricing) that has a different interest rate type, loan amount, term period (temporary term extension is excluded), and/or customer (e.g. from single customer to joint or change in one of the joint customer names).

A distressed restructuring is an indication of unlikeliness to pay where this is likely to result in a diminished financial obligation caused by the material forgiveness, or postponement of principal interest or, where relevant, fees. Distressed restructuring occurs when forbearance measures have been extended towards a debtor. Therefore, those forborne exposures where the forbearance measures are likely to result in a diminished financial obligation are classified as defaulted.

Restructured operations will be considered cured and normalized after two successful repayments and could therefore be subject to a stage movement.

d) Write-offs

According to the IFRS 9 (B5.4.9), the gross carrying amount of a financial asset may be directly reduced when there is no reasonable expectation of recovering the financial asset in its entirety or a portion of it. As such, the Bank may record a write-off of Stage 3 loans. The Bank may also, on an ad-hoc basis, examine the need for any further write-offs of Stage 2 loans if there is relevant evidence.

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 to write off the cost of each asset to their residual values on a straight-line basis over their estimated useful lives. The annual depreciation rates applied are as follows:

- 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 all Member Countries.

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 also included and elaborated upon in Article 12 of the Headquarters Agreement with the Hellenic Government, ratified by Greek Law 2380/No.38/7.3.1996.

Provisions

The Bank records 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 10% of the subscribed capital including all paid, unpaid but payable, and unpaid but callable share capital.

Reserves and Retained Earnings

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

The revaluation reserve represents the accumulated change in fair value of those financial assets that are measured at fair value through other comprehensive income of the Bank.

The retained earnings of the Bank are the accumulated undistributed and unallocated net income over the years.

Income and Expense

Interest income and expense are recognized in the income statement loss using the effective interest method. The EIR is the rate that exactly discounts estimated future cash payments or receipts through the expected life of the financial instrument (or, where appropriate, a shorter period) to:

- The gross carrying amount of the financial asset; or
- The amortized cost of the financial liability.

When calculating the EIR for financial instruments other than purchased or originated credit-impaired assets, the Bank estimates future cash flows considering all contractual terms of the financial instrument, but not ECL. For purchased or originated credit-impaired financial assets, a credit-adjusted EIR is calculated using estimated future cash flows including ECL.

The calculation of the EIR includes transaction costs and fees paid or received that are an integral part of the effective interest rate. Transaction costs include incremental costs that are directly attributable to the acquisition or issue of a financial asset or financial liability.

i) Amortized cost and gross carrying amount

The AC of a financial asset or financial liability is the amount at which the financial asset or financial liability is measured on initial recognition minus the principal repayments, plus or minus the cumulative amortization using the effective interest method of any difference between that initial amount and the maturity amount and, for financial assets, adjusted for any expected credit loss allowance.

The 'gross carrying amount of a financial asset' is the AC of a financial asset before adjusting for any ECL allowance.

ii) Calculation of interest income and expense

The EIR of a financial asset or financial liability is calculated on initial recognition of a financial asset or a financial liability. In calculating interest income and expense, the EIR is applied to the gross carrying amount of the asset (when the asset is not credit- impaired) or to the AC of the liability. The EIR is revised as a result of periodic re-estimation of cash flows of floating rate instruments to reflect movements in market rates of interest. The EIR is also revised for fair value hedge adjustments at the date amortization of the hedge adjustment begins.

However, for financial assets that have become credit-impaired subsequent to initial recognition, interest income is calculated by applying the EIR to the AC of the financial asset. If the asset is no longer credit-impaired, then the calculation of interest income reverts to the gross basis.

For financial assets that were credit-impaired on initial recognition, interest income is calculated by applying the credit-adjusted EIR to the AC of the asset. The calculation of interest income does not revert to a gross basis, even if the credit risk of the asset improves.

iii) Fees and commissions

Fee and commission income and expense that are integral to the EIR on a financial asset or financial liability are included in the EIR. Other fee and commission income – including account servicing fees, investment management fees, sales commission, placement fees and syndication fees – is recognized as the related services are performed. If a loan commitment is not expected to result in the draw-down of a loan, then the related loan commitment fee is recognized on a straight-line basis over the commitment period. A contract with a customer that results in a recognized financial instrument in the Bank's financial statements may be partially in the scope of IFRS 9 and partially in the scope of IFRS 15. If this is the case, then the Bank first applies IFRS 9 to separate and measure the part of the contract that is in the scope of IFRS 9 and then applies IFRS 15 to the residual.

Fee and commission income from contracts with customers under the scope of IFRS 15 is measured based on the consideration specified in a contract with a customer. The Bank recognizes revenue when it transfers control over a service to a customer. The adoption of IFRS 15 had no impact on the Bank's financial statements as the execution and completion of the transaction requested by the customer is done at point in time and this is consistent with the Bank's existing accounting policy.

Other fee and commission expenses relate mainly to transaction and service fees, which are expensed as the services are received.

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 eligible employees, consisting of three pillars:

a. The first pillar is a defined benefit scheme financed entirely by the Bank. The scheme's funding level and the Bank's contributions are determined on the basis of actuarial valuations performed annually by qualified, independent actuaries. The Bank is under the obligation to maintain the scheme fully funded and, to this effect, has always liquidated any past service deficit in the course of the year following the relevant actuarial valuation. Actuarial and asset gains or losses are recognized in 'Other comprehensive income', and net gains or losses are included in remeasurements where any change in the effect of the asset ceiling, excluding those amounts that have been already included in personnel expenses, are also included.

b. The second pillar is a defined contribution scheme to which both the employee and the Bank contribute equally at a rate of 0-12% of basic salary. Each employee determines his/her contribution rate and the mode of investment of the contributions.

c. The third pillar is a defined contribution scheme funded entirely by each employee, up to 40% of basic salary.

As an alternative, 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 'Personnel expenses'.

The Bank may offer termination benefits to employees that are separated based on the Bank's separation policy. These benefits, including indemnities and any related retirement benefits, are recognized in income as an expense in the same period they are incurred.

Government Grants

Government grants are recognized 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.

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 the termination takes place.

New and Amended Standards and Interpretations

The following new standards, amendments to standards, and new interpretations as issued by the International Accounting Standards Board (IASB) and the IFRS Interpretations Committee (IC), apply from 1 January 2018:

- ### IFRIC 22, Foreign Currency Transactions and Advance Consideration

IFRIC 22 provides requirements about which exchange rate to use in reporting foreign currency transactions that involve an advance payment or receipt. The interpretation clarifies that in this case, the date of the transaction for the purpose of determining the exchange rate to use on initial recognition of the related asset, expense or income is the date of the advance consideration, i.e. when the entity initially recognized the non-monetary asset (prepayment asset) or non-monetary liability (deferred income liability) arising from the advance consideration. If there are multiple payments or receipts in advance, the entity must determine a date of transaction for each payment or receipt. The adoption of the interpretation had no impact on the Bank's financial statements.

- ### IFRS 4, Amendment-Applying IFRS 9 Financial Instruments with IFRS 4 Insurance Contracts

The amendment addresses the accounting consequences of the different effective dates of IFRS 9 'Financial Instruments' and the forthcoming new insurance contracts standard. It introduces two options for entities that issue insurance contracts: a temporary exemption from applying IFRS 9 and an overlay approach.

The optional temporary exemption from IFRS 9 is available to entities whose activities are predominantly connected with insurance, allowing them to continue to apply IAS 39 'Financial Instruments: Recognition and Measurement' while they defer the application of IFRS 9 until 1 January 2021 at the latest.

The overlay approach is an option for entities that adopt IFRS 9 and issue insurance contracts, to adjust profit or loss for eligible financial assets, effectively resulting in IAS 39 accounting for those designated financial assets. This approach can be used provided that the entity applies IFRS 9 in conjunction with IFRS 4 and classifies financial assets at fair value through profit or loss in accordance with IFRS 9, when those assets were previously classified at AC or as available-for-sale in accordance with IAS 39.

The amendment is not relevant to the Bank's activities.

- ### IFRS 2, Amendment-Classification and Measurement of Share-based Payment Transactions

The amendment addresses (a) the measurement of cash-settled share-based payments, (b) the accounting for modifications of a share-based payment from cash-settled to equity-settled and c) the classification of share-based payments settled net of tax withholdings.

Specifically, the amendment clarifies that a cash-settled share-based payment is measured using the same approach as for equity-settled share-based payments. It also clarifies that the liability of cash-settled share-based payment modified to equity-settled one is derecognized and the equity-settled share-based payment is accounted from the modification date of the fair value of the equity instrument granted and any difference is recognized in profit or loss immediately.

Furthermore, a share-based payment net by withholding tax on the employee's behalf (a net settlement feature) is classified as equity settled in its entirety, provided it would have been classified as equity-settled had it not included the net settlement feature.

The adoption of the amendment had no impact on the Bank's financial statements.

- IAS 40, Amendment-Transfers of Investment Property

The amendment clarifies that a transfer of property, including property under construction or development, into or out of investment property, should be made only when there has been a change in use of the property. Such a change in use occurs when the property meets, or ceases to meet, the definition of investment property and should be supported by evidence. The adoption of the amendment had no impact on the Bank's financial statements.

- Annual Improvements to IFRSs 2014-2016 Cycle

The IASB through the 2014-2016 annual improvements cycle, provided a clarification for IAS 28 'Investments in Associates and Joint Ventures': It is clarified that venture capital organizations, mutual funds, unit trusts and similar entities are allowed to elect measuring their investments in associates or joint ventures at fair value through profit or loss. Such election can be performed on an investment-by-investment basis in associates or joint ventures. The adoption of the amendment had no impact on the Bank's financial statements.

- IFRS 15, Revenue from Contracts with Customers and IFRS 15 Amendments

IFRS 15 establishes a single, comprehensive revenue recognition model for determining when and how much revenue to recognize and replaces existing revenue recognition guidance, including IAS 18 'Revenue', IAS 11 'Construction Contracts' and IFRIC 13 'Customer Loyalty Programs'.

IFRS 15 applies to all contracts with customers, except those in the scope of other standards such as:

- Financial instruments and other contractual rights or obligations within the scope of IFRS 9 'Financial Instruments', IFRS 10 'Consolidated Financial Statements', IFRS 11 'Joint Arrangements', IAS 27 'Separate Financial Statements' and IAS 28 'Investments in Associates and Joint Ventures';
- Lease contracts within the scope of IAS 17 'Leases' (or IFRS 16 'Leases'); and
- Insurance contracts within the scope of IFRS 4 'Insurance Contracts'.

Therefore, interest and fee income integral to financial instruments will continue to fall outside the scope of IFRS 15.

IFRS 15 specifies that revenue should be recognized at an amount that reflects the consideration to which the entity expects to be entitled in exchange for transferring goods or services. It introduces the concept of recognizing revenue for performance obligations as they are satisfied and the control of a good or service (i.e. the ability to direct the use of and obtain the benefits from them), is obtained by the customer. For services provided over time, such as management fee income earned for asset management services provided, and variable performance fee income based on the return of the underlying asset at a particular date, consideration is recognized as the service is provided to the customer, provided it is probable that a significant reversal of consideration will not occur.

IFRS 15 was amended in April 2016 to provide several clarifications, including the identification of the performance obligations within a contract.

The adoption of the standard and its amendment had no impact on the Bank's financial statements as net interest income, which is a primary revenue stream of the Bank. Furthermore, regarding the Bank's revenue from contracts with customers, including fee and commission income, there was no change in the accounting treatment as transactions executed at point in time, as it is consistent with the Bank's existing accounting policy.

New standards, amendments to standards and interpretations not yet adopted by the Bank

A number of new standards, amendments to existing standards and interpretations are effective after 2018, as they have not been early applied by the Bank. Those that may be relevant to the Bank are set out below:

- ### IFRS 9, Amendment–Prepayment Features with Negative Compensation (effective 1 January 2019)

The amendment changes IFRS 9 requirements in order to allow measurement of a financial asset at AC or at FVOCI, depending on the business model, even in the case of prepayment options which could result in the party that triggers the early termination receiving compensation from the other party (negative compensation). Therefore, measurement of these financial assets will be regardless of the event or circumstance that caused the early termination of the contract and irrespective of which party pays or receives reasonable compensation for the early termination. Applying IFRS 9 before the amendment would probably result in the measurement of these financial assets at FVTPL.

The amendment also confirms the modification accounting of financial liabilities under IFRS 9. Specifically, when a financial liability measured at AC is modified without this resulting in derecognition, a gain or loss, calculated as the difference between the original contractual cash flows and the modified cash flows discounted at the original EIR, should be recognized in profit or loss.

The adoption of the amendment is not expected to impact the Bank's financial statements.

- ### IFRS 16, Leases (effective 1 January 2019)

IFRS 16, which supersedes IAS 17 'Leases' and related interpretations, introduces a single, on-balance sheet lease accounting model for lessees, under which the classification of leases for a lessee, as either operating leases or finance leases, is eliminated and all leases are treated similarly to finance leases under IAS 17.

The definition of a lease under IFRS 16 mainly relates to the concept of control. The new standard distinguishes between leases and service contracts on the basis of whether the use of an identified asset is controlled by the customer. Control is considered to exist if the customer has:

- The right to obtain substantially all of the economic benefits from the use of an identified asset; and
- The right to direct the use of that asset.

IFRS 16 provides for the recognition of a 'right-of-use-asset' and a 'lease liability' upon lease commencement in case that there is a contract, or part of a contract, that conveys to the lessee the right to use an asset for a period of time in exchange for a consideration.

The right-of-use-asset is, initially, measured at cost, consisting of the amount of the lease liability, plus any lease payments made to the lessor at or before the commencement date less any lease incentives received, the initial estimate of restoration costs and any initial direct costs incurred by the lessee and, subsequently, at cost less accumulated depreciation and impairment.

The lease liability is initially recognized at an amount equal to the present value of the lease payments during the lease term that are not yet paid.

Consequently, the typical straight-line operating lease expense of operating leases under IAS 17 is replaced by the depreciation charge of the 'right-of-use-asset' and the interest expense on the 'lease liability'. The recognition of assets and liabilities by lessees, as described above, is not required for certain short-term leases and leases of low value assets. The accounting treatment for lessors is not substantially affected by the requirements of IFRS 16.

Transition to IFRS 16

The date of initial application of IFRS 16 for the Bank will be 1 January 2019. The Bank is considering to choose the modified retrospective application of IFRS 16 and therefore comparative information will not be restated.

Lessee Accounting

In accordance with IFRS 16, at the commencement date of the lease, the Bank as a lessee will recognize right-of-use assets and lease liabilities in the statement of financial position, initially measured at the present value of the future lease payments. The Bank intends to apply this initial measurement principle to all leases, except for those with lease term of 12 months or less – making use of the short-term leases and leases of low-value assets exemptions.

The Bank has not yet completed the assessment of the impact from IFRS 16 adoption; it which is not expected to be material.

With regard to subsequent measurement, the Bank, acting as a lessee, will apply the cost model for the measurement of right-of-use asset. Accordingly, the right-of-use asset will be measured at cost less any accumulated depreciation and accumulated impairment losses and adjusted for the remeasurement of the lease liability.

On the other hand, interest expense will be recognized on the lease liabilities, while their carrying amount will be reduced to reflect the lease payments made. In case of any reassessments or lease modifications specified, the carrying amount of the lease liabilities will be remeasured to reflect revised lease payments.

- ### IAS 28, Amendment - Long - Term Interests in Associates and Joint Ventures (effective 1 January 2019))

The amendment clarifies that IFRS 9 'Financial Instruments' including its impairment requirements, applies to long-term interests in associates or joint ventures that form part of the entity's net investment in the associate or joint venture but are not accounted for using equity accounting.

According to the amendment, an entity should not take into account any adjustments to the carrying amount of long-term interests (net investment in the associate or joint venture), resulting from the application of IAS 28 'Investments in Associates and Joint Ventures' when applying IFRS 9. The adoption of the amendment is not expected to impact the Bank's financial statements.

- ### IAS 19, Amendment - Plan Amendment, Curtailment or Settlement (effective 1 January 2019)

The amendment clarifies that when a change to a defined benefit plan, i.e. an amendment, curtailment or settlement takes place and a remeasurement of the net defined benefit liability or asset is required, the updated actuarial assumptions from the remeasurement should be used to determine current service cost and net interest for the remainder of the reporting period after the change to the plan. Additionally, the amendment includes clarifications about the effect of a plan amendment, curtailment or settlement on the requirements regarding the asset ceiling. The adoption of the amendment is not expected to impact the Bank's financial statements.

- ### Annual Improvements to IFRSs 2015-2017 Cycle (effective 1 January 2019)

The improvements introduce key changes to several standards as set out below: The amendments to IFRS 3 'Business Combinations' and IFRS 11 'Joint Arrangements' clarified how an entity accounts for increasing its interest in a joint operation that meets the definition of a business. Specifically, when an entity obtains control of a business that is a joint operation, then the transaction constitutes a business combination achieved in stages and the acquiring party remeasures the entire previously held interest in the assets and liabilities of the joint operation at fair value. Conversely, if a party obtains joint control of a business that is a joint operation then the previously held interest is not remeasured.

The improvement to IAS 12 'Income Taxes' clarified that all income tax consequences of dividends, including payments on financial instruments classified as equity, should be recognized in profit or loss, other comprehensive income or equity, according to where the originating transaction or event that generated distributable profits giving rise to the dividend, was recognized.

IAS 23 'Borrowing costs' amendment clarified that any borrowing originally performed to develop a qualifying asset should be treated as part of the funds that the entity borrowed generally, when substantially all of the activities necessary to prepare that asset for its intended use or sale are complete.

The adoption of the amendments is not expected to impact the Bank's financial statements.

- ### Amendments to References to the Conceptual Framework in IFRS Standards (effective 1 January 2020)

In March 2018, the IASB issued its revised Conceptual Framework. This replaces the previous version of the Conceptual Framework issued in 2010. Revisions performed by IASB introduced a new chapter of measurement, updated definitions of an asset/liability and recognition criteria, as well as clarifications on important areas. The adoption of the amendment is not expected to impact the Bank's financial statements.

- ### Amendment to IFRS 3 Business Combinations (effective 1 January 2020)

The IASB issued amendments to the definition of a business in IFRS 3 'Business Combinations' to help entities determine whether an acquired set of activities and assets is a business or not. They clarify the minimum requirements for a business, remove the assessment of whether market participants are capable of replacing any missing elements, and add guidance to help entities assess whether an acquired process is substantive, narrow the definitions of a business and of outputs, and introduce an optional fair value concentration test. The adoption of the amendment is not expected to impact the Bank's financial statements.

- ### Amendments to IAS 1 and IAS 8: Definition of Material (effective 1 January 2020)

The amendments to IAS 1 'Presentation of Financial Statements' and IAS 8 'Accounting Policies, Changes in Accounting Estimates and Errors' aim to align the definition of 'material' across the standards and to clarify certain aspects of the definition. According to the new definition, information is material if omitting, misstating or obscuring it could reasonably be expected to influence decisions that the primary users of general purpose financial statements make on the basis of those financial statements, which provide financial information about a specific reporting entity. The amendments clarify that materiality will depend on the nature or magnitude of information, or both. The adoption is not expected to impact the Bank's financial statements.

- ### IFRS 17, Insurance Contracts (effective 1 January 2022)

IFRS 17, which supersedes IFRS 4 'Insurance Contracts' provides a comprehensive and consistent accounting model for insurance contracts. It applies to insurance contracts issued, all reinsurance contracts and to investment contracts with discretionary participating features provided that the entity also issues insurance contracts. Financial guarantee contracts are allowed to be within the scope of IFRS 17 if the entity has previously asserted that it regarded them as insurance contracts.

According to IFRS 17 general model, groups of insurance contracts which are managed together and are subject to similar risks, are measured based on building blocks of discounted, probability-weighted future cash flows, a risk adjustment and a contractual service margin (CSM) representing the unearned profit of the contracts. Under the model, estimates are remeasured at each reporting period. A simplified measurement approach may be used if it is expected that by doing so a reasonable approximation of the general model will be produced or if the contracts are of short duration.

Revenue is allocated to periods in proportion to the value of expected coverage and other services that the insurer provides during the period, claims are presented when incurred and any investment components i.e. amounts repaid to policyholders even if the insured event does not occur, are not included in revenue and claims. Insurance services results are presented separately from the insurance finance income or expense.

IFRS 17 is not relevant to the Bank's activities.

4. USE OF ESTIMATES

The preparation of financial statements involves management estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements, and the reported amounts of revenues and expenses during the reporting period. Estimates and judgments 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 judgment in each area of estimate have been outlined in the respective accounting policy and disclosure note. The Bank's critical accounting judgments and estimates are as follows:

a. 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 and further explained in the relevant risk management policies, of this document. Provisions for loans that have an expected credit loss of 12-month amounted to EUR 3,520 thousand and those loans that have an expected lifetime credit loss but that are not credit impaired amounted to EUR 4,274 thousand.

   In determining the above provision amounts the Bank takes into consideration PD and LGD factors extracted from the GEMs database.

   Furthermore, those loans that have an expected lifetime credit loss and are credit impaired amounted to EUR 26,981 thousand. These 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 EIR to reach a net present value for a particular operation, less any collateral that can be realized.

b. Staff retirement benefits. The Bank has established a pension plan for its staff which is described in 'staff retirement and termination benefits' accounting policy and is detailed under staff retirement plan in note 'Employee benefits'. 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 such as the EUR and USD. The Bank's liability to the staff retirement plan at the financial position date was EUR 3,971 thousand.

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

5. RISK MANAGEMENT

Risk is inherent in the Bank's activities and is managed through an ongoing process of identification, measurement and monitoring, as well as being 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 BoD 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 Policies and Procedures 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's 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.

a) 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 the expected credit loss 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.

For credit risks incurred by the Bank's Treasury in its investment and hedging activities, the BoD has approved policies and guidelines for the determination of counterparty and investment exposure limits. The Bank's Risk Management Department 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.

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

Presented in EUR (000)	At 31 December 2018	At 31 December 2017
Cash and bank balances	48,598	81,481
Debt investment securities	395,979	292,524
Derivative financial instruments	662	1,659
Loans	1,330,695	1,135,081
Other assets	29,541	26,157
On-balance-sheet	**1,805,475**	**1,536,902**
Undrawn commitments	252,801	185,563
Total	**2,058,276**	**1,722,465**

b) Analysis by rating agency

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

	2018				
Presented in EUR (000)	Aaa – Aa3	A1 – A3	Baa1 – Ba3	Unrated	**Total**
Analysis by Moody's rating					
Cash and bank balances	48,598	-	-	-	**48,598**
Debt investment securities	21,813	105,979	268,187	-	**395,979**
Equity investments	-	-	-	27,655	**27,655**
At 31 December	**70,411**	**105,979**	**268,187**	**27,655**	**472,232**
Of which issued by					
Governments	8,734	8,666	25,582	-	**42,982**
Corporates	13,079	97,313	242,605	27,655	**380,652**
Cash deposits at banks	48,598	-	-	-	**48,598**
At 31 December	**70,411**	**105,979**	**268,187**	**27,655**	**472,232**
Of which classified as					
Fair value through profit or loss	-	-	-	1,015	**1,015**
Fair value through other comprehensive income	21,813	105,979	218,848	26,640	**373,280**
Amortized cost	48,598	-	49,339	-	**97,937**
At 31 December	**70,411**	**105,979**	**268,187**	**27,655**	**472,232**

	2017				
Presented in EUR (000)	Aaa – Aa3	A1 – A3	Baa1 – Ba3	Unrated	**Total**
Analysis by Moody's rating					
Cash and bank balances	81,481	-	-	-	**81,481**
Debt investment securities	28,420	144,957	119,147	-	**292,524**
Equity investments	-	-	-	31,361	**31,361**
At 31 December	**109,901**	**144,957**	**119,147**	**31,361**	**405,366**
Of which issued by					
Governments	-	11,632	41,473	-	**53,105**
Corporates	28,420	133,325	77,674	31,361	**270,780**
Cash deposits at banks	81,481	-	-	-	**81,481**
At 31 December	**109,901**	**144,957**	**119,147**	**31,361**	**405,366**
Of which classified as					
Fair value through profit or loss	-	-	-	1,600	**1,600**
Fair value through other comprehensive income	28,420	144,957	119,147	29,761	**322,285**
Amortized cost	81,481	-	-	-	**81,481**
At 31 December	**109,901**	**144,957**	**119,147**	**31,361**	**405,366**

c) Credit risk analysis

The tables below provide an analysis of the Bank's internal expected credit loss rating scale from 1 (lowest risk) to 15 (highest risk) and how it corresponds to the external ratings of Moody's credit rating service.

Risk rating	Internal risk rating category	External rating equivalent	Grade of investment
1	Excellent	Aaa	Investment
1	Very strong	Aa1 – Aa3	Investment
2	Strong	A1 – A3	Investment
3,4,5	Good	Baa1 – Baa3	Investment
6,7,8	Fair	Ba1 – Ba3	Investment
9,10,11	Weak	B1 – B3	Investment
12,13,14	Special attention	Caa1 – Caa3	Classified
15	Expected loss	Ca – C	Classified

c1. Credit risk in loans portfolio

The table provides overview of the exposure amount and allowance for credit losses by financial asset class broken down into stages as per IFRS 9 requirements. Internally, loans that are within the 12-month ECL are categorized as standard.

	Presented in EUR (000)							
					Provisions for impairment			
Internal risk rating category	12-month ECL	Lifetime ECL not credit impaired	Lifetime ECL credit impaired	**Total**	12-month ECL	Lifetime ECL not credit impaired	Lifetime ECL credit impaired	**Total**
Excellent	-	-	-	-	-	-	-	-
Very strong	-	-	-	-	-	-	-	-
Strong	-	-	-	-	-	-	-	-
Good	8,442	-	-	**8,442**	1	-	-	**1**
Fair	669,613	44,020	-	**713,633**	1,461	891	-	**2,352**
Weak	372,775	139,822	-	**512,597**	2,058	1,985	-	**4,043**
Special attention	-	42,009	41,737	**83,746**	-	1,398	26,981	**28,379**
Expected loss	-	-	-	-	-	-	-	-
At 31 December 2018	**1,050,830**	**225,851**	**41,737**	**1,318,418**	**3,520**	**4,274**	**26,981**	**34,775**

	Presented in EUR (000)							
					Provisions for impairment			
Internal risk rating category	12-month ECL	Lifetime ECL not credit impaired	Lifetime ECL credit impaired	**Total**	12-month ECL	Lifetime ECL not credit impaired	Lifetime ECL credit impaired	**Total**
Excellent	-	-	-	-	-	-	-	-
Very strong	-	-	-	-	-	-	-	-
Strong	-	-	-	-	-	-	-	-
Good	9,739	-	-	**9,739**	1	-	-	**1**
Fair	646,611	-	-	**646,611**	608	-	-	**608**
Weak	339,240	36,481	-	**375,721**	823	833	-	**1,656**
Special attention	-	39,142	51,982	**91,124**	21	255	36,291	**36,567**
Expected loss	-	-	9,164	**9,164**	-	-	9,164	**9,164**
At 31 December 2017	**995,590**	**75,623**	**61,146**	**1,132,359**	**1,453**	**1,088**	**45,455**	**47,996**

d) 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, guarantees, covenants and comfort letters.

- Loans and advances. The BoD approved guidelines for taking security under lending operations set the levels and types of collateral and other credit enhancements recommended for a given risk profile.

  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. If necessary, the Bank reassesses the value of collateral in order to determine if additional collateral is needed to be provided by the borrower. As at 31 December 2018 the secured portfolio was 52.4% (2017: 57.9%) of the outstanding loans balance.

- Other financial instruments. Collateral held as security for financial assets other than loans and advances is determined by the nature of the instrument. Bonds and ECP held by the Bank as investment securities are generally unsecured. The Bank may hold cash or government securities as collateral against its derivative contract counterparties. At 31 December 2018 the Bank had pledged cash collateral in an amount of EUR 22,810 thousand (2017: EUR 17,670 thousand).

e) Liquidity risk

Liquidity risk concerns the ability of the Bank to fulfill 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 takes into consideration, to the extent feasible, the guidance documents issued by the Basel Committee on Banking Supervision. The Bank sets limits to control its liquidity risk exposure and vulnerabilities and regularly reviews such limits. The limit framework also includes measures ensuring that in a period of market stress, available liquidity exceeds liquidity needs and that the Bank can continue to operate.

The Bank's commitment to maintaining a strong liquidity position is established in policies, approved by the BoD, including a minimum liquidity ratio of 50% of the Bank's net cash requirements over the next twelve months on a rolling basis. 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 include estimated interest amounts, 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	18,240	24,107	232,861	754,250	27,958	**1,057,416**
Derivative financial instruments	-	24,164	-	-	-	**24,164**
Payables and accrued interest	-	12,002	3,971	-	-	**15,973**
Financial Liabilities at 31 December 2018	**18,240**	**60,273**	**236,832**	**754,250**	**27,958**	**1,097,553**
Borrowings	601	2,482	68,552	730,352	11,199	**813,186**
Derivative financial instruments	-	18,242	-	-	-	**18,242**
Payables and accrued interest	-	10,190	5,232	-	-	**15,422**
Financial Liabilities at 31 December 2017	**601**	**30,914**	**73,784**	**730,352**	**11,199**	**846,850**

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 possibility 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.

a) 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 mirror 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 assets 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 on 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	Swiss franc	Other	**Total**
Assets					
Cash and bank balances	46,266	1,691	-	64	**48,598**
Debt investment securities	165,120	230,859	-	-	**395,979**
Impairment losses on debt investment securities	(103)	(541)	-	-	**(644)**
Derivatives financial instruments	662	-	-	-	**662**
Loans	744,365	466,721	-	119,609	**1,330,695**
Deferred income	1,454	(3,483)	-	(1,023)	**(3,052)**
Impairment losses on loans	(13,342)	(17,263)	-	(4,170)	**(34,775)**
Equity investments	12,988	14,667	-	-	**27,655**
Other assets	15,095	12,732	141	1,573	**29,541**
Total	972,505	705,383	141	116,630	**1,794,659**
Liabilities					
Borrowings	126,794	595,473	88,860	142,903	**954,030**
Derivative financial instruments	24,164	-	-	-	**24,164**
Payables and accrued interest	6,134	8,595	51	1,193	**15,973**
Total	157,092	604,068	88,911	144,096	**994,167**
Net financial instruments	815,413	101,315	(88,770)	(27,466)	**800,492**
Derivative financial instruments	11,376	(103,351)	88,739	22,568	**19,332**
Currency balance at 31 December 2018	**826,789**	**(2,036)**	**(31)**	**(4,898)**	**819,824**

Presented in EUR (000)	Euro	United States dollar	Swiss franc	Other	**Total**
Assets					
Cash and bank balances	69,084	12,034	-	363	**81,481**
Debt investment securities	135,077	157,447	-	-	**292,524**
Impairment losses on debt investment securities	(127)	(149)	-	-	**(276)**
Derivatives financial instruments	1,659	-	-	-	**1,659**
Loans	595,412	487,161	-	52,508	**1,135,081**
Deferred income	(2,567)	(3,280)	-	(372)	**(6,219)**
Impairment losses on loans	(26,358)	(21,222)	-	(416)	**(47,996)**
Equity investments	16,682	14,679	-	-	**31,361**
Other assets	13,004	11,589	222	1,342	**26,157**
Total	801,866	658,259	222	53,425	**1,513,772**
Liabilities					
Borrowings	76,756	500,214	85,667	59,955	**722,592**
Derivative financial instruments	18,242	-	-	-	**18,242**
Payables and accrued interest	7,197	7,073	52	1,100	**15,422**
Total	102,195	507,287	85,719	61,055	**756,256**
Net financial instruments	699,671	150,972	(85,497)	(7,630)	**757,516**
Derivative financial instruments	75,757	(155,250)	85,455	7,485	**13,447**
Currency balance at 31 December 2017	**775,428**	**(4,278)**	**(42)**	**(145)**	**770,963**

b) 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 re-price to a market rate of interest before maturity, the next repricing 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	48,581	-	-	-	17	**48,598**
Debt investment securities	72,407	45,000	76,451	202,121	-	**395,979**
Derivative financial instruments	-	-	-	-	662	**662**
Loans	200,385	273,619	617,183	239,508	-	**1,330,695**
Equity investments	-	-	-	-	27,655	**27,655**
Other assets	-	-	-	-	29,541	**29,541**
Total	321,373	318,619	693,634	441,629	57,875	**1,833,130**
Liabilities						
Borrowings	36,698	185,835	207,952	523,545	-	**954,030**
Derivative financial instruments	-	-	-	-	24,164	**24,164**
Payables and accrued interes	-	-	-	-	15,973	**15,973**
Total	36,698	185,835	207,952	523,545	40,137	**994,167**
Derivative financial instruments	1,250	(109,698)	(310,072)	418,520	-	**-**
Interest rate risk at 31 December 2018	**285,925**	**23,086**	**175,610**	**336,604**	**17,738**	838,963

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	81,478	-	-	-	3	**81,481**
Debt investment securities	59,297	60,000	9,169	164,058	-	**292,524**
Derivative financial instruments	-	-	-	-	1,659	**1,659**
Loans	184,975	228,824	549,697	171,585	-	**1,135,081**
Equity investments	-	-	-	-	31,361	**31,361**
Other assets	-	-	-	-	26,157	**26,157**
Total	325,750	288,824	558,866	335,643	59,180	**1,568,263**
Liabilities						
Borrowings	-	53,071	77,687	591,834	-	**722,592**
Derivative financial instruments	-	-	-	-	18,242	**18,242**
Payables and accrued interest	-	-	-	-	15,422	**15,422**
Total	-	53,071	77,687	591,834	33,664	**756,256**
Derivative financial instruments	(12,351)	(98,071)	(371,615)	482,037	-	-
Interest rate risk at 31 December 2017	**313,399**	**137,682**	**109,564**	**225,846**	**25,516**	812,007

c) Sensitivity analysis

The Bank's interest rate sensitivity analysis comprises 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 minimizing 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.

The table below details the repricing gap by currency. A parallel upward or downward shift in the EUR and USD curves of 50 basis points would have generated the maximum loss or gain respectively.

Presented in EUR (000)	At 31 December 2018	At 31 December 2017
Euro	936,000	588,000
United states dollar	191,000	200,000
Total repricing gap	1,127,000	788,000
Shift of 50 basis points in the EUR curve	**5,637**	**3,938**

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. The Bank is committed to following the best practices and market standards in the area of accountability, transparency and business ethics. Due diligence on customers and counterparties takes into consideration the Anti-Fraud Corruption and Monetary Laundering Policy and Know-Your Customer Procedures.

Classification and Fair Value

a) Classification

All loans are classified as at amortised cost (AC), except for those loans classified as at fair value through profit or loss (FVTPL) that do not meet the solely payments of principal and interest (therefore had not passed the SPPI test) as determined by the Bank.

Investment securities classified as at fair value through other comprehensive income (FVTOCI) include government and corporate bonds and ECP, and their fair value has been determined using quoted prices.

Equity investments classified as at FVTPL include investments that are quoted on an exchange (i.e. private equity) or those elected having their fair value based on cash outflows and inflows. Equity investments classified as at FVTOCI 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.

b) Financial assets and liabilities

The tables below identify the Bank's financial assets and financial liabilities in accordance with their categories. The fair value of the financial assets and financial liabilities is disclosed as equal to the carrying value, plus accrued interest, as all bear a variable interest rate and are given at market terms and conditions.

	At 31 December 2018		
Presented in EUR (000)	Fair value through profit or loss (mandatory)	Amortized cost	**Carrying amount**
Assets			
Cash and bank balances	-	48,598	**48,598**
Debt investment securities	-	49,339	**49,339**
Loans	12,277	1,318,418	**1,330,695**
Deferred income	-	(3,052)	**(3,052)**
Impairment losses on loans	-	(34,775)	**(34,775)**
Other assets	-	29,541	**29,541**
Total financial assets	**12,277**	**1,408,069**	**1,420,346**
Liabilities			
Borrowings	-	954,030	**954,030**
Payables and accrued interest	-	15,973	**15,973**
Total financial liabilities	-	**970,003**	**970,003**

	At 31 December 2017		
Presented in EUR (000)	Fair value through profit or loss (mandatory)	Amortized cost	**Carrying amount**
Assets			
Cash and bank balances	-	81,481	**81,481**
Loans	2,722	1,132,358	**1,135,080**
Deferred income	-	(6,219)	**(6,219)**
Impairment losses on loans	-	(47,996)	**(47,996)**
Other assets	-	26,157	**26,157**
Total financial assets	**2,722**	**1,185,781**	**1,188,503**
Liabilities			
Borrowings	-	722,592	**722,592**
Payables and accrued interest	-	15,422	**15,422**
Total financial liabilities	-	**738,014**	**738,014**

c) Fair value hierarchy

For those above financial instruments measured at fair value, the Bank 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
Derivative financial instruments – assets	-	662	-	**662**
Fair value through profit or loss:				
Loans	-	-	12,277	**12,277**
Equity investments	-	-	1,015	**1,015**
Fair value through other comprehensive income:				
Debt investment securities	346,640	-	-	**346,640**
Equity investments	-	-	26,640	**26,640**
Derivative financial instruments – liabilities	-	(24,164)	-	**(24,164)**
At 31 December 2018	**346,640**	**(23,502)**	**39,932**	**363,070**

There have been no transfers between Level 1 and Level 2 during the year. For Level 1 and Level 2 the valuation techniques used are broker quotes and observable market data, or discounted cash flow models. For Level 3 the valuation technique used is the net asset value (NAV),, and equity calculations based on EBITDA and market data.

Presented in EUR (000)	Level 1	Level 2	Level 3	Carrying Amount
Derivative financial instruments – assets	-	1,659	-	**1,659**
Fair value through profit or loss:				
Loans	-	-	2,722	**2,722**
Equity investments	-	-	1,600	**1,600**
Fair value through other comprehensive income:				
Debt investment securities	292,524	-	-	**292,524**
Equity investments	-	-	29,761	**29,761**
Derivative financial instruments – liabilities	-	(18,242)	-	**(18,242)**
At 31 December 2017	**292,524**	**(16,583)**	**34,083**	**310,024**

d) Fair value measurement in Level 3

The table provides a reconciliation of the fair values of the Bank's Level 3 financial assets of the fair value hierarchy.

Presented in EUR (000)	At 31 December 2018	At 31 December 2017
At 1 January	31,361	52,766
Total gains or (losses) recognized in the income statement	(585)	1,600
Total gains or (losses) recognized in other comprehensive income	713	(21,641)
Purchases, sales, issues and settlements	(3,834)	(1,364)
At end of year	**27,655**	**31,361**

e) Sensitivity analysis for Level 3

The table below indicates a possible impact on net income for the Level 3 financial instruments carried at fair value at the financial position date, on an estimated 5% increase or decrease in net assets value of the equity investments based on the Bank's participation.

Presented in EUR (000)	Carrying amount	Favorable change	Unfavorable change
Equity investments	27,655	1,383	(1,383)

Capital Management

At the inception of the Bank, initial authorized share capital was SDR 1 billion, which was fully subscribed by the Member States. In December 2007 the BoG approved an increase 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. The increase allows 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 Member 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.

Pursuant to Resolution 131 of the BoG a unanimously adopted the first amendment to the Establishing Agreement, which became effective on 21 June 2013. As of this effective date, and as per Resolution 131 of the BoG, the unit of account of the Bank became the EUR and all of the Bank's authorized share capital was redenominated from SDR to EUR. The conversion rate applied was SDR to EUR fixed at 1:1.15.

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 BoD 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. This limit on the total amount of operations which includes all callable capital is approximately EUR 2.4 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 BoG 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.

6. OPERATING SEGMENTS

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, liquidity and interest rate risks.

	2018			2017		
Presented in EUR (000)	Lending	Treasury	Total	Lending	Treasury	Total
Income statement						
Interest income	70,129	8,588	78,717	61,512	6,634	68,146
Net fees and commissions	1,652	-	1,652	2,087	-	2,087
Other income (expense)	569	29	598	5,975	482	6,457
Total segment revenues	72,350	8,617	80,967	69,574	7,116	76,690
Less: interest expense	(37,513)	(461)	(37,974)	(36,726)	(499)	(37,225)
Less: net interest expense on derivatives	-	(7,599)	(7,599)	-	(3,153)	(3,153)
Foreign exchange	-	(1,352)	(1,352)	-	2,110	2,110
Less: personnel and other admin. expenses	(19,283)	(1,439)	(20,722)	(18,195)	(1,085)	(19,280)
Less: depreciation and amortization	(442)	(11)	(453)	(451)	(10)	(461)
Segment income before impairment	15,112	(2,245)	12,867	14,202	4,479	18,681
Less: impairment / fair value (losses)	(7,323)	(368)	(7,691)	(9,750)	(276)	(10,026)
Net income for the year	**7,789**	**(2,613)**	**5,176**	**4,452**	**4,203**	**8,655**

	31 December 2018			31 December 2017		
Presented in EUR (000)	Lending	Treasury	Total	Lending	Treasury	Total
Financial position						
Segment assets	1,351,172	444,595	1,795,767	1,139,538	375,388	1,514,926
At end of year			**1,795,767**			**1,514,926**
Segment liabilities	970,003	24,164	994,167	738,014	18,242	756,256
Members' equity	-	-	801,600	-	-	758,67
At end of year			**1,795,767**			**1,514,926**

The geographical segment reporting of the Bank is presented in note 16 'Operational analysis'.

7. INTEREST INCOME

Interest and similar income is analyzed as follows

Presented in EUR (000)	Year to 31 December 2018	Year to 31 December 2017
From loans and advances	70,129	61,512
From placements with financial institutions	126	7
From investment securities at amortized cost	51	-
From investment securities at fair value through OCI	8,411	6,627
Interest income	**78,717**	**68,146**

8. INTEREST EXPENSE

Interest and similar expense is analyzed as follows:

Presented in EUR (000)	Year to 31 December 2018	Year to 31 December 2017
From borrowed funds	6,435	8,045
From issued debt	29,619	27,132
From amortized issuance and arrangement costs	1,459	1,549
From other charges	461	499
Interest expense	**37,974**	**37,225**

9. NET FEES AND COMMISSIONS

Net fees and commissions is analyzed as follows:

Presented in EUR (000)	Year to 31 December 2018	Year to 31 December 2017
Guarantee fees	276	235
Management fees	371	461
Appraisal fees	195	259
Administration fees	36	57
Arrangement fees	132	-
Surveillance fees	54	71
Prepayment / cancellation fees	489	884
Other fees	99	120
Net Fees and commissions	**1,652**	**2,087**

10. PERSONNEL AND OTHER ADMINISTRATIVE EXPENSES

Administrative expenses are analyzed as follows:

Presented in EUR (000)	Year to 31 December 2018	Year to 31 December 2017
Salaries and benefits	12,672	11,505
Staff retirement plans	3,280	3,270
Personnel expenses	**15,952**	**14,775**
Professional fees and related expenses	1,094	1,003
Utilities and maintenance	1,474	1,454
Other administrative	2,202	2,048
Other administrative expenses	**4,770**	**4,505**

The average number of staff employed during the year: 111 (2017: 112). The number of staff at 31 December 2018 was 110 (2017: 112). Further analysis of the staff retirement plan is presented in note 'Employee benefits'.

11. IMPAIRMENT LOSSES ON LOANS

Loans that are measured at amortized cost are stated net of provisions for impairment, which includes also their related provisions for impairment on undrawn commitments. A summary of the movements in provisions for impairment were as follows:

Presented in EUR (000)	Stage 1	Stage 2	Stage 3	Total
At 31 December 2016	-	-	-	30,131
IFRS 9 transition	(3,711)	2,289	12,771	11,349
At 1 January 2017	2,234	4,515	34,731	41,480
Charge	401	-	19,238	19,639
Release	(3,388)	(6,918)	(208)	(10,514)
Transfer	2,578	3,794	(6,372)	-
Against write-offs	-	-	(485)	(485)
Foreign exchange adjustments	(372)	(303)	(1,449)	(2,124)
At 31 January 2017	1,453	1,088	45,455	47,996
Charge	3,284	3,239	7,221	13,744
Release	(1,656)	(2,608)	(3,188)	(7,452)
Against write-offs	-	-	(20,586)	(20,586)
Foreign exchange adjustments	439	2,555	(1,921)	1,073
At 31 December 2018	**3,520**	**4,274**	**26,981**	**34,775**

At each reporting date, the Bank recognizes loss allowances based on either 12-month ECL or lifetime ECL, depending on whether there has been a significant movement in credit risk on the financial instrument since its initial recognition. The IFRS 9 transition is the amount arising from the first time adoption of IFRS 9, which reduced the retained earnings.

Staging Criteria 12-month ECL (Stage 1)

As IFRS 9 does not distinguish between individually significant or not individually significant financial instruments, the Bank measures potential credit losses for all non-impaired operations (Stage 1 and Stage 2) on an individual operation basis based on the asset class. Their PD and LGD are multiplied by general market scenarios assigned within the Moody's Analytics IFRS ImpairmentCalc tool. Provisions for impairment in Stage 1 are therefore affected by specifics of any particular operation together by general market scenarios. They are meant to protect against potential risks that are considered present, or within a 12-month horizon, and derived from potentially adverse developments in operating conditions beyond the control of individual borrowers.

Staging Criteria lifetime ECL (Stages 2 and 3)

When an operation deteriorates substantially in credit quality, it enters Stage 2 and an expected credit loss calculation is performed on a Lifetime Expected Credit Loss (LECL) basis. Stage 2 operations are those that have experienced an overall credit quality downgrade but are still performing. They are not considered credit impaired.

Stage 3 operations have objective evidence of impairment that immediately impacts the ECL.

Revolving facilities and undrawn commitments

Revolving credit facilities have no fixed term and they can be cancelled at the discretion of the Bank at any point in time. These facilities are subject to, at a minimum, an annual credit review. In this regard, the date of the latest credit review provides the relevant date to assess if there is any increase in credit risk, as at that point in time. The Bank may amend the terms and conditions of the exposure.

The estimate of the ECLs on irrevocable loan commitments is consistent with its expectations of drawdowns on that loan commitment. Therefore, the Bank considered (i) the expected portion of the loan commitment that will be drawn down within 12 months of the reporting date when estimating 12-month expected credit losses and (ii) the expected portion of the loan commitment that will be drawn down over the expected life of the reporting date when estimating lifetime expected credit losses. At 31 December 2018 the amount of expected credit losses was EUR 376 thousand (2017: EUR 112 thousand).

12. DEBT INVESTMENT SECURITIES

Debt investment securities are analyzed as follows:

Presented in EUR (000)	At 31 December 2018	At 31 December 2017
Government bonds	141,268	53,105
Corporate bonds	141,043	129,419
Commercial papers	113,668	110,000
Debt investment securities	395,979	292,524
Less: impairment losses	(644)	(276)
Debt investment securities net of impairment	**395,335**	**292,248**

At each reporting date, the Bank recognizes loss allowances based on either 12-month ECL or LECL. All debt investment securities are recognized only on a 12-month ECL as there has been no significant movement in credit risk since their initial recognition.

13. DERIVATIVE FINANCIAL INSTRUMENTS

The table below shows the Bank's outstanding forward foreign exchange contracts. The first column shows the sum of notional amounts, which is the amount of a derivative's nominal value, and is the basis upon which changes in the value are measured. The second column shows the market value of the notional amounts and also the net valuation attributable to fair value hedges.

	At 31 December 2018			At 31 December 2017		
Presented in EUR (000)	Notional amount	Fair value		Notional amount	Fair value	
		Assets	Liabilities		Assets	Liabilities
Currency swap purchases	33,012	-	33,019	52,174	52,174	-
Currency swap sales	(33,569)	-	(33,569)	(51,543)	(50,968)	-
Designated fair value hedges	-	662	(23,614)	-	453	(18,242)
Derivative financial instruments	**(557)**	**662**	**(24,164)**	**631**	**1,659**	**(18,242)**

The above derivative financial instrument contracts with financial counterparties have been documented under International Swaps and Derivative Association (ISDA) Master Agreements with Credit Support Annexes (CSAs) . Pursuant to such arrangements the Bank is eligible to offset assets and liabilities in the event of a counterparty default occurrence.

The Bank's hedge accounting is based on a clearly documented relationship between the item hedged and the hedging instrument, having a one-on-one relationship, which is documented at the time a hedge transaction is entered into. This relationship arises within the context of the Bank's borrowing activities in which the Bank's issued bonds are combined with swaps to achieve floating-rate debt in a currency sought by the Bank.

14. LOANS

The Bank offers a range of loan facilities directed to investments for both project and trade financing, and 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 2018	At 31 December 2017
Loans at amortized cost:		
At 1 January	1,132,359	1,139,072
Disbursements	572,966	386,211
Less: repayments	(377,988)	(318,214)
Disposal	-	-
Write-offs	(20,586)	(485)
Foreign exchange movements	11,667	(74,225)
Outstanding disbursements	1,318,418	1,132,359
Less: deferred income	(3,052)	(6,219)
Less: impairment losses	(34,775)	(47,996)
Loans at fair value:		
Outstanding disbursements	14,939	4,939
Fair value adjustment	(2,662)	(2,217)
Loans net of impairment	**1,292,868**	**1,080,866**

At 31 December 2018 the principal amount of outstanding disbursements was EUR 1,333,357 thousand (2017: EUR 1,137,298 thousand).

In 2018 the Bank had two restructured loan operations for the reporting year.

The carrying amount of loans with respect to their related stages and allowance for impairment is analyzed as follows:

Presented in EUR (000)	At 31 December 2018	At 31 December 2017
Stage 1	1,050,830	995,590
Less: deferred income	(3,052)	(6,219)
Less: allowance for impairment	(3,520)	(1,453)
Carrying amount	1,044,258	987,918
Stage 2	225,851	75,623
Less: allowance for impairment	(4,274)	(1,088)
Carrying amount	221,577	74,535
Stage 3	41,737	61,146
Less: allowance for impairment	(26,981)	(45,455)
Carrying amount	14,756	15,691
Fair value through profit or loss	12,277	2,722
Carrying amount	**1,292,868**	**1,080,866**

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 Operational analysis.

15. EQUITY INVESTMENTS

A primary focus of the Bank is to facilitate access to funding for those small- and medium-sized 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 2018		At 31 December 2017	
Presented in EUR (000)	% of Investment	Cost	Fair value	Cost	Fair value
Balkan Accession Fund	9.09	-	1,015	-	1,600
At fair value through profit or loss		-	1,015	-	1,600
SEAF Caucasus Growth Fund	21.39	5,488	4,289	7,040	5,499
Access Bank, Azerbaijan	20.00	14,759	-	14,148	-
A-Park Kaluga, Russia	19.99	1,714	340	1,714	340
Emerging Europe Accession Fund	10.15	2,303	5,981	1,840	6,921
Rusal	0.01	4	123	4	248
ADM Ceecat Recovery Fund	5.65	4,988	5,652	6,636	7,422
European Virgin Fund	21.05	8,264	10,255	8,724	8,933
Teamnet International	8.33	5,599	-	5,599	398
Natfood	0.01	-	-	-	-
EOS Hellinic Renaissance Fund	3.18	47	-	-	-
At fair value through other comprehensive income		43,166	26,640	45,705	29,761
Equity investments at fair value		**43,166**	**27,655**	**45,705**	**31,361**

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 2018, as Management considers that is the best available estimate of the investments' fair value. The techniques applied to perform these valuations include equity calculations based on EBITDA and market data.

During the year the Bank had realized a net income of EUR 572 thousand from its investment in the Balkan Accession Fund.

On disposal or exit of an equity investment for those at fair value through other comprehensive income, the cumulative gain or loss is realized with a corresponding reversal of the unrealized gain or loss that was recorded prior to the exit from that investment, is not recycled to the income statement.

As of 31 December 2018 the Bank has a committed amount of EUR 8,680 thousand towards the above entities participation. Further analysis of the equity investment portfolio is presented in note 'Operational analysis'.

As at 31 December 2018 the Bank has three equity investments where it holds slightly more than 20% 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.

16. OPERATIONAL ANALYSIS

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

	At 31 December 2018		At 31 December 2017	
Presented in EUR (000)	Outstanding balance	Undrawn commitments	Outstanding balance	Undrawn commitments
Analysis by instrument				
Loans	1,330,695	233,099	1,135,081	166,733
Equity investments	27,655	8,680	31,361	6,417
Guarantees	-	11,022	-	12,413
At end of year	**1,358,350**	**252,801**	**1,166,442**	**185,563**
Analysis by country				
Albania	37,629	87	42,468	175
Armenia	91,730	431	84,051	447
Azerbaijan	53,867	6,544	60,710	18,791
Bulgaria	153,265	32,418	100,252	526
Georgia	113,856	20,802	67,025	21,552
Greece	202,146	2,953	173,203	7,500
Moldova	38,909	2,181	36,060	8,100
Romania	172,322	7,707	116,332	15,734
Russia	128,113	59,940	180,383	505
Turkey	306,218	70,322	273,993	110,707
Ukraine	60,295	49,416	31,965	1,526
At end of year	**1,358,350**	**252,801**	**1,166,442**	**185,563**
Analysis by sector				
Consumer discretionary	13,634	30,247	26,129	-
Consumer staples	103,029	118	108,635	7,284
Energy	155,586	-	106,176	-
Financial institutions	537,037	85,109	416,712	55,457
Health care	75,021	42,177	61,177	107,492
Industrials	182,167	-	158,241	2,917
Information technology	5,734	-	9,398	-
Materials	110,200	33,987	129,313	-
Real estate	2,617	32,000	3,063	-
Telecom services	16,665	-	33,330	-
Utilities	156,660	29,163	114,268	12,413
At end of year	**1,358,350**	**252,801**	**1,166,442**	**185,563**

The Bank is restricted to operating in its 11 Member States and individual country limits are set as a maximum at 30% of planned commitments. This limit is calculated on the basis of the BoD 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 coordinated by the Department of Project Implementation and Monitoring, with inputs from the originated Banking Teams regarding the availability of financial data. Monitoring reports are completed by the Bank's Department of Project Implementation and Monitoring based on financial analysis prepared by the Department of Financial Analysis. Risk asset reviews, based on the mentioned monitoring reports, are performed by the Department of Risk Management, and may result in a downgrade or upgrade of an operation's status and, if a significant deterioration is noted, trigger an impairment test.

17. PROPERTY AND EQUIPMENT

Property and equipment is analyzed as follows:

Presented in EUR (000)	Buildings (leasehold)	Vehicle	Furniture and office accessories	Computers and office equipment	Total
Cost					
At 31 December 2016	827	105	577	1,520	3,029
Additions	23	1	20	219	263
Disposals	-	-	(47)	(17)	(64)
At 31 December 2017	850	106	550	1,722	3,228
Additions	26	-	54	111	191
Disposals	-	-	(11)	(28))	(39)
At 31 December 2018	**876**	**106**	**593**	**1,805**	**3,380**
Accumulated depreciation					
At 31 December 2016	745	12	504	1,258	2,519
Charges	52	22	34	164	272
Disposals	-	-	(47)	(17)	(64)
At 31 December 2017	797	34	491	1,405	2,727
Charges	39	21	31	146	237
Disposals	-	-	(11)	(28)	(39)
At 31 December 2018	**836**	**55**	**511**	**1,523**	**2,925**
Net book value					
At 31 December 2018	**40**	**51**	**82**	**282**	**455**
At 31 December 2017	53	72	59	317	501
At 31 December 2016	82	93	73	262	510

18. INTANGIBLE ASSETS

Intangible assets comprising computer software are analyzed as follows:

Presented in EUR (000)	Total
Cost	
At 31 December 2016	3,975
Additions	367
At 31 December 2017	4,342
Additions	217
At 31 December 2017	**4,559**
Accumulated amortization	
At 31 December 2016	3,496
Charges	193
At 31 December 2017	3,689
Additions	217
At 31 December 2018	**3,906**
Net book value	
At 31 December 2018	**653**
At 31 December 2017	653
At 31 December 2016	479

19. OTHER ASSETS

Other assets are analyzed as follows:

Presented in EUR (000)	At 31 December 2018	At 31 December 2017
Accrued interest	20,169	16,974
Advances and prepaid expenses	5,690	5,850
Other prepayments	187	184
Guarantee deposits	3,495	3,149
Other assets	**29,541**	**26,157**

20. BORROWINGS

Borrowing facilities and bond issuance, arranged as at the financial position date, are analyzed below. In addition to medium- or long-term borrowings and bond issuance, the Bank utilizes short-term financing in the form of ECP issuance or borrowings from commercial banks for cash management purposes. At 31 December 2018 the Bank had issued debt securities in the amount of EUR 726,921 thousand.

	At 31 December 2018		At 31 December 2017	
Presented in EUR (000)	Amount used	Amount arranged	Amount used	Amount arranged
Euro	126,794	146,794	76,756	96,756
United States dollar	595,473	595,473	500,214	583,596
Swiss franc	88,860	88,860	85,667	85,667
Romanian lei	56,227	56,227	21,850	21,850
Georgian lari	83,059	83,059	34,650	34,650
Armenian dram	3,617	3,617	3,455	3,455
Total	**954,030**	**974,030**	**722,592**	**825,974**

The interest rate on borrowings falls within an approximate range of Euribor or USD Libor of +0 to +375 basis points. There is no collateral against the above borrowed funds. The fair value of the borrowings is approximately equal to their carrying value.

21. PAYABLES AND ACCRUED INTEREST

Payables and accrued interest is analyzed as follows:

Presented in EUR (000)	At 31 December 2018	At 31 December 2017
Accrued interest	10,495	9,136
Social insurance fund (IKA) contributions	4	5
Pension plan obligation	3,971	5,232
Suppliers and other accrued expenses	1,444	990
Other	59	59
Payables and accrued interest	**15,973**	**15,422**

22. SHARE CAPITAL

From the Bank's inception, and in accordance with Article 4 of the Establishing Agreement, the Bank denominated its authorized share capital in the Special Drawing Right (SDR) as defined by the International Monetary Fund (IMF). Resolution 131 of the BoG unanimously adopted the requisite amendments to paragraph 1 of Article 4 and Articles 23 and 24 of the Establishing Agreement, to expressly include among the exclusive powers of the BoG the change of the unit of account of the Bank, and the redenomination of all capital stock of the Bank. These amendments to the Establishing Agreement became effective on 21 June 2013 (the 'Effective Date'). In accordance with such Resolution 131 of the BoG as of the Effective Date the unit of account of the Bank became the EUR and the authorized capital stock of the Bank was

redenominated into three billion four hundred and fifty million EUR (3,450,000,000), divided into three million (3,000,000) shares having a par value of one thousand and one hundred and fifty EUR (1,150) each, inclusive of all subscribed and unallocated shares. Accordingly, as of the Effective Date, all outstanding share capital commitments of participating members in respect of their subscribed shares were converted into EUR.

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 (fully paid and payable in installments) and callable shares. Payment for the paid-in shares subscribed to by members was made over a period of years in accordance with Article 6 of the Establishing Agreement for the initial capital raising purpose of the Bank, and as determined in advance by the Bank for capital increases (in the only capital increase of the Bank so far, the structure of payments specified was similar to the one in Article 6). The same Article states that payment of the amount subscribed to in respect of 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 a notice 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 50 % reduction of their portion of subscribed capital, from 2% to 1% of the initial authorized capital the BoG approved their request. On 5 October 2008 the new shares pursuant to the capital increase of the Bank were offered in the same structure as the initial authorized share capital, in the amount of EUR 1.15 billion, and were fully subscribed by the Member States. Furthermore, Azerbaijan also subscribed to the 3% of

the initial authorized share capital that remained unallocated, after the above mentioned participation reduction, while Romania subscribed both to their allocation of new shares and to those that would have been allocated to Georgia had it chosen to participate in the capital increase. This subscription process followed a decision taken by the BoG in December 2007 to triple the Bank's authorized capital to EUR 3.45 billion and to double the subscribed capital to EUR 2.3 billion, while leaving authorized capital of EUR 1.15 billion unallocated. On October 2011 the BoG approved the request from Moldova for a 50% reduction of its portion of subscribed capital, from 1% to 0.5%, and those shares were released to unallocated share capital.

The above share capital is analyzed as follows:

Presented in EUR (000)	At 31 December 2018	At 31 December 2017
Authorized share capital	3,450,000	3,450,000
Less: unallocated share capital*	(1,161,500)	(1,161,500)
Subscribed share capital	2,288,500	2,288,500
Less: shares not yet called	(1,601,950)	(1,601,950)
Less: shares payable but not yet due	-	(44,984)
Less: shares payments past due	(1,428)	-
Paid-up share capital	685,122	641,566
Advance against future call	-	-
Paid-in share capital	**685,122**	**641,566**

* Shares available to new or existing Member States.

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% (EUR 115 million) fully paid and 20% (EUR 230 million) payable by promissory notes or other obligations which were not negotiable and non-interest bearing in eight equal successive annual installments in the years 1998 to 2005.

Capital Increase

The capital increase of EUR 1.15 billion is divided into EUR 345 million paid in capital and EUR 805 million callable capital. Pursuant to the BoG decision in October 2008, the EUR 345 million paid in portion is divided into 10% (EUR 115 million) fully paid shares in 2010 and 20% (EUR 230 million) payable shares by promissory notes or other obligation issued by members in eight equal successive annual installments in the years 2011 to 2018. As of October 2011, the capital increase was reduced by EUR 11.5 million of the subscribed share capital, due to an approved reduction by the BoG in participation by Moldova.

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

	At 31 December 2018		
Presented in EUR (000)	Initial capital	Capital increase	**Total**
Authorized share capital	1,150,000	2,300,000	**3,450,000**
Less: unallocated share capital	(34,500)	(1,127,000)	**(1,161,500)**
Subscribed share capital	1,115,500	1,173,000	**2,288,500**
Less: shares not yet called	(780,850)	(821,100)	**(1,601,950)**
Less: shares payable but not yet due	-	-	**-**
Less: shares payable that are past due	-	(1,428)	**(1,428)**
Paid-up share capital	334,650	350,472	**685,122**
Advance against future call	40	(40)	**-**
Paid-in share capital	**334,690**	**350,432**	**685,122**

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 the current financial position date is analyzed as follows:

		Subscribed	Callable	Payable	Paid
Member	Shares	Presented in EUR (000)			
Albania	40,000	46,000	32,200	1,403	12,397
Armenia	20,000	23,000	16,100	-	6,900
Azerbaijan	100,000	115,000	80,500	-	34,500
Bulgaria	270,000	310,500	217,350	-	93,150
Georgia	10,000	11,500	8,050	-	3,450
Greece	330,000	379,500	265,650	25	113,825
Moldova	10,000	11,500	8,050	-	3,450
Romania	280,000	322,000	225,400	-	96,600
Russian Fed.	330,000	379,500	265,650	-	113,850
Turkey	330,000	379,500	265,650	-	113,850
Ukraine	270,000	310,500	217,350	-	93,150
Total	**1,990,000**	**2,288,500**	**1,601,950**	**1,428**	**685,122**

23. RESERVES

Reserves are analyzed as follows:

Presented in EUR (000)	General	Other comprehensive income	Other	Total
At 31 December 2016	55,406	(4,864)	(3,365)	47,177
Gains (losses) on revaluation of investments	-	(19,294)	-	(19,294)
Remeasurements of defined benefit scheme	-	-	231	231
Transferred from retained earnings	5,469	-	-	5,469
At 31 December 2017	60,875	(24,158)	(3,134)	33,583
Gains (losses) on revaluation of investments	-	(8,216)	-	(8,216)
Remeasurements of defined benefit scheme	-	-	2,414	2,414
Transferred from retained earnings	5,176		-	5,176
At 31 December 2018	**66,051**	**(32,374)**	**(720)**	**32,957**

The Bank's general reserve is maintained for meeting any unforeseeable risks or contingencies that do not qualify as provisions for impairment and is normally built up from those released impairment charges during the year.

24. CASH AND CASH EQUIVALENTS

Cash and cash equivalents are analyzed as follows:

Presented in EUR (000)	At 31 December 2018	At 31 December 2017
Cash on hand	17	3
Investments maturing up to 1 month:		
Cash deposits at banks	48,581	81,478
At fair value through other comprehensive income portfolio	78,655	55,000
Investment maturing from 1 month to 3 months:		
At fair value through other comprehensive income portfolio	45,000	60,000
Cash and cash equivalents	**172,253**	**196,481**

The commercial papers held in the Bank's portfolio were short-term rated at a minimum of A2 by Standard and Poor's or P2 by Moody's rating agencies, in accordance with internal financial policies.

25. EMPLOYEE BENEFITS

Under the Defined Benefit Scheme

If separated at or after the normal retirement age (60 years old), a staff member will be entitled to a full immediate pension equal to 1% of his annual 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. If separated at or after the early retirement

age (55 years old), a staff member will be entitled to a reduced immediate pension, or deferred pension payable from any month until the staff member's normal retirement age. If separated before the early retirement age, a staff member will be entitled to a deferred pension payable from any month between the staff member's early and normal retirement age. Upon separation at any age, a staff member will have a choice between the appropriate type of pension and a lump sum termination benefit.

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 2018. 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 2018	At 31 December 2017
Amounts recognized in the statement of financial position		
Present value of the defined benefit obligations	24,445	27,111
Fair value of plan assets	(20,474)	(21,879)
Net liability at end of the year	**3,971**	**5,232**
Amounts recognized in the income statement		
Service cost	2,095	2,124
Net interest on the net defined benefit liability/(asset)	81	75
Administration expense	48	47
Total included in personnel expenses	**2,224**	**2,246**
Remeasurements recognized in other comprehensive income		
At 31 December	(6,721)	(6,952)
Liability gain (loss) due to changes in assumptions	4,167	(505)
Liability experiences gain (loss) arising during the year	(359)	419
Return on plan assets excluding income statement amounts	(1,394)	317
Total amount recognized in OCI during the year	2,414	231
Cumulative in other comprehensive income (expense)	**(4,307)**	**(6,721)**
Principal actuarial assumptions used		
Discount rate	2.04%	1.78%
Expected return on plan assets	2.04%	1.78%
Future salary increase	1.50%	2.00%
Future pension increase	1.50%	2.00%
Average remaining working life of employees	11 years	12 years

The discount rate arises from the yield curves that use data from double A-rated iBoxx bond indices produced by the International Index Company.

The expected return on assets as per provision of the revised IAS 19, has been set equal to the discount rate assumption, i.e. at 2.04% pa.

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

Presented in EUR (000)	At 31 December 2018	At 31 December 2017
Major categories of plan assets		
Cash instruments	16%	14%
Fixed interest	47%	45%
Equities	33%	38%
Other	4%	3%
Reconciliation of plan assets		
Market value at 1 January	21,879	20,373
Expected return	401	395
Contributions paid	1,070	1,431
Benefit pensions and lump sum paid to pensioners	(1,434)	(590)
Expenses	(48)	(47)
Asset gain (loss)	(1,394)	317
Fair value of plan assets	**20,474**	**21,879**

The actual investment return on assets of the Fund for the year was -3.8%. 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 2019 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)	2018	2017	2016	2015	2014
Defined benefit obligations	24,445	27,111	25,021	19,879	20,321
Plan assets	(20,474)	(21,879)	(20,373)	(18,696)	(15,657)
Plan deficit (surplus)	3,971	5,232	4,648	1,183	4,664
Net experience adjustments on plan liabilities (assets)	**359**	**(419)**	**4,032**	**(1,822)**	**(5,624)**

Sensitivity analysis

Reasonable possible changes at the financial position date to one of the relevant actuarial assumptions, holding other assumptions constant, would have affected the defined benefit obligation by the amounts shown below.

	At 31 December 2018		At 31 December 2017	
Presented in EUR (000)	Increase	Decrease	Increase	Decrease
Discount rate (1% movement)	(3,041)	3,041	(3,926)	3,926
Future salary growth (1% movement)	1,843	(1,843)	1,438	(1,438)

Although the analysis does not take account of the full distribution of cash flows expected under the plan, it does provide an approximation of the sensitivity of the assumptions shown under the Defined Contribution Scheme.

Under the Defined Contribution Scheme

Upon separation, 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. The pension expense under this scheme was EUR 1,027 thousand (2017: EUR 997 thousand) and is included in 'Personnel expenses'.

Under the Greek State Social Insurance Fund

The pension expense of staff that is alternatively entitled to retirement benefits from this fund was EUR 29 thousand (2017: EUR 27 thousand) and is included in 'Personnel expense'.

26. 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 'Other administrative expenses' totaled EUR 693 thousand (2017: EUR 691 thousand).

27. RELATED PARTIES

The Bank has the following 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, covered by medical insurance, participation in the Bank's retirement schemes and are eligible to receive other short-term benefits. The amounts paid to key management personnel during the year were EUR 1,600 thousand (2017: EUR 1,217 thousand). Key management personnel may receive post-employment benefits, other long-term benefits and termination benefits, but do not receive any share-based payments.

The members of the BoD are not personnel of the Bank and do not receive any fixed term salaries nor any staff benefits. The governments of the Member States are not related parties.

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 2018 the Bank administered two special funds. Extracts from the audited financial statements are included under the 'Summary of special funds'.

28. EVENTS AFTER THE REPORTING PERIOD

Prior to approval of these financial statements by the BoD, Greece had fully discharged obligations to the share of paid-in capital while Albania needs to be paid-in EUR 283 thousand.

29. 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 2018	At 31 December 2017
Statement of movements		
Balance brought forward	8	8
Net income (loss) for the year	-	-
Less: disbursements	-	-
Balance of available funds	**8**	**8**
Financial position		
Placements with other financial institutions	8	8
Total Assets	**8**	**8**
Unallocated fund balance	8	8
Total Liabilities and Contributor Resources	**8**	**8**

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 2018	At 31 December 2017
Statement of movements		
Balance brought forward	84	92
Net income (loss) for the year	-	-
Less: disbursements	-	(8)
Liquidation	(84)	-
Balance of available funds	-	**84**
Financial position		
Placements with other financial institutions	-	84
Total Assets	**-**	**84**
Unallocated fund balance	-	84
Total Liabilities and Contributor Resources	**-**	**84**

INDEPENDENT AUDITOR'S REPORT

TO THE BOARD OF DIRECTORS AND GOVERNORS OF THE BLACK SEA TRADE AND DEVELOPMENT BANK

Report on the Audit of the Financial Statements

Opinion

We have audited the accompanying financial statements of Black Sea Trade and Development Bank ('the Bank'), which comprise the statement of financial position as at 31 December 2018, the statements of income and other comprehensive income, changes in member's equity and cash flows for the year then ended, and notes, comprising significant accounting policies and other explanatory information.

In our opinion, the accompanying financial statements present fairly, in all material respects, the financial position of the Bank as at 31 December 2018, and its financial performance and its cash flows for the year then ended in accordance with International Financial Reporting Standards (IFRSs).

Basis for Opinion

We conducted our audit in accordance with International Standards on Auditing (ISAs). Our responsibilities under those standards are further described in the Auditor's Responsibilities for the Audit of the Financial Statements section of our report. We are independent of the Bank in accordance with the ethical requirements that are relevant to the audit of the financial statements in the International Ethics Standards Board for Accountants Code of Ethics for Professional Accountants (IESBA Code), and we have fulfilled our ethical responsibilities in accordance with these requirements. We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our opinion.

Key Audit Matters

Key audit matters are those matters that, in our professional judgment, were of most significance in our audit of the financial statements of the current period. These matters were addressed in the context of our audit of the financial statements as a whole, and in forming our opinion thereon, and we do not provide a separate opinion on these matters.

Key audit matter	How the matter was addressed in our audit
Impairment Losses on Loans at amortized cost As described in the notes to the financial statements, the impairment losses have been determined in accordance with IFRS 9 Financial Instruments. This was considered a key audit matter as IFRS 9 is a complex accounting standard which requires significant judgment to determine the impairment reserve. Key areas of judgment included: - The interpretation of the requirements to determine impairment under application of IFRS 9, which is reflected in the Bank's expected credit loss model. - The identification of exposures with a significant deterioration in credit quality. - Assumptions used in the expected credit loss model such as the financial condition of the counterparty, expected future cash flows and forward looking macroeconomic factors (unemployment rates, gross domestic product growth). - The need to apply additional overlays to reflect current or future external factors that are not appropriately captured by the expected credit loss model. Refer to pages 17 to 21 of the financial statements for a description of the accounting policies and to pages 31 to 34 for an analysis of credit risk.	In assessing impairment reserve, we performed the following procedures: – We assessed the modeling techniques and methodology against the requirements of IFRS 9. – We assessed the design and tested the operating effectiveness of relevant controls over the: - Data used to determine the impairment reserve, including transactional data captured at loan origination, ongoing internal credit quality assessments, storage of data and interfaces to the expected credit loss model. - Expected credit loss model, including model build and approval, ongoing monitoring/validation, model governance and mathematical accuracy. – We assessed and tested the material modeling assumptions as well as overlays with a focus on the: - Key modeling assumptions adopted by the Bank. - Basis for and data used to determine overlays. - Sensitivity of the provisions to changes in modeling assumptions. – We examined a sample of exposures and performed procedures to evaluate the: - Timely identification of exposures with a significant deterioration in credit quality. - Expected loss calculation for exposures assessed on an individual basis. – We involved our own specialists for evaluating areas of credit models that required specific expertise. – We assessed the accuracy of the disclosures in the financial statements.

Other Information

Management is responsible for the other information. The other information comprises the information included in the Annual report, but does not include the financial statements and our auditors' report thereon.

Our opinion on the financial statements does not cover the other information and we do not express any form of assurance conclusion thereon.

In connection with our audit of the financial statements, our responsibility is to read the other information and, in doing so, consider whether the other information is materially inconsistent with the financial statements or our knowledge obtained in the audit, or otherwise appears to be materially misstated. If, based on the work we have performed, we conclude that there is a material misstatement of this other information, we are required to report that fact. We have nothing to report in this regard.

Responsibilities of Management and Those Charged with Governance for the Financial Statements

Management is responsible for the preparation and fair presentation of the financial statements in accordance with IFRSs and for such internal control as management determines is necessary to enable the preparation of financial statements that are free from material misstatement, whether due to fraud or error.

In preparing the financial statements, management is responsible for assessing the Bank's ability to continue as a going concern, disclosing, as applicable, matters related to going concern and using the going concern basis of accounting unless management either intends to liquidate the Bank or to cease operations, or has no realistic alternative but to do so.

Those charged with governance are responsible for overseeing the Bank's financial reporting process.

Auditor's Responsibilities for the Audit of the Financial Statements

Our objectives are to obtain reasonable assurance about whether the financial statements as a whole are free from material misstatement, whether due to fraud or error, and to issue an auditor's report that includes our opinion. Reasonable assurance is a high level of assurance, but is not a guarantee that an audit conducted in accordance with ISAs will always detect a material misstatement when it exists. Misstatements can arise from fraud or error and are considered material if, individually or in the aggregate, they could reasonably be expected to influence the economic decisions of users taken on the basis of these financial statements.

As part of an audit in accordance with ISAs, we exercise professional judgment and maintain professional skepticism throughout the audit. We also:

- Identify and assess the risks of material misstatement of the financial statements, whether due to fraud or error, design and perform audit procedures responsive to those risks, and obtain audit evidence that is sufficient and appropriate to provide a basis for our opinion. The risk of not detecting a material misstatement resulting from fraud is higher than for one resulting from error, as fraud may involve collusion, forgery, intentional omissions, misrepresentations, or the override of internal control.

- Obtain an understanding of internal control relevant to the audit 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 Bank's internal control.

- Evaluate the appropriateness of accounting policies used and the reasonableness of accounting estimates and related disclosures made by management.

- Conclude on the appropriateness of management's use of the going concern basis of accounting and, based on the audit evidence obtained, whether a material uncertainty exists related to events or conditions that may cast significant doubt on the Bank's ability to continue as a going concern. If we conclude that a material uncertainty exists, we are required to draw attention in our auditors' report to the related disclosures in the financial statements or, if such disclosures are inadequate, to modify our opinion. Our conclusions are based on the audit evidence obtained up to the date of our auditors' report. However, future events or conditions may cause the Bank to cease to continue as a going concern.
- Evaluate the overall presentation, structure and content of the financial statements, including the disclosures, and whether the financial statements represent the underlying transactions and events in a manner that achieves fair presentation.

We communicate with those charged with governance regarding, among other matters, the planned scope and timing of the audit and significant audit findings, including any significant deficiencies in internal control that we identify during our audit.

We also provide those charged with governance with a statement that we have complied with relevant ethical requirements regarding independence, and communicate with them all relationships and other matters that may reasonably be thought to bear on our independence, and where applicable, related safeguards.

From the matters communicated with those charged with governance, we determine those matters that were of most significance in the audit of the financial statements of the current period and are therefore the key audit matters. We describe these matters in our auditors' report unless law or regulation precludes public disclosure about the matter or when, in extremely rare circumstances, we determine that a matter should not be communicated in our report because the adverse consequences of doing so would reasonably be expected to outweigh the public interest benefits of such communication.

The engagement partner on the audit resulting in this independent auditor's report is Nikolaos Vouniseas.

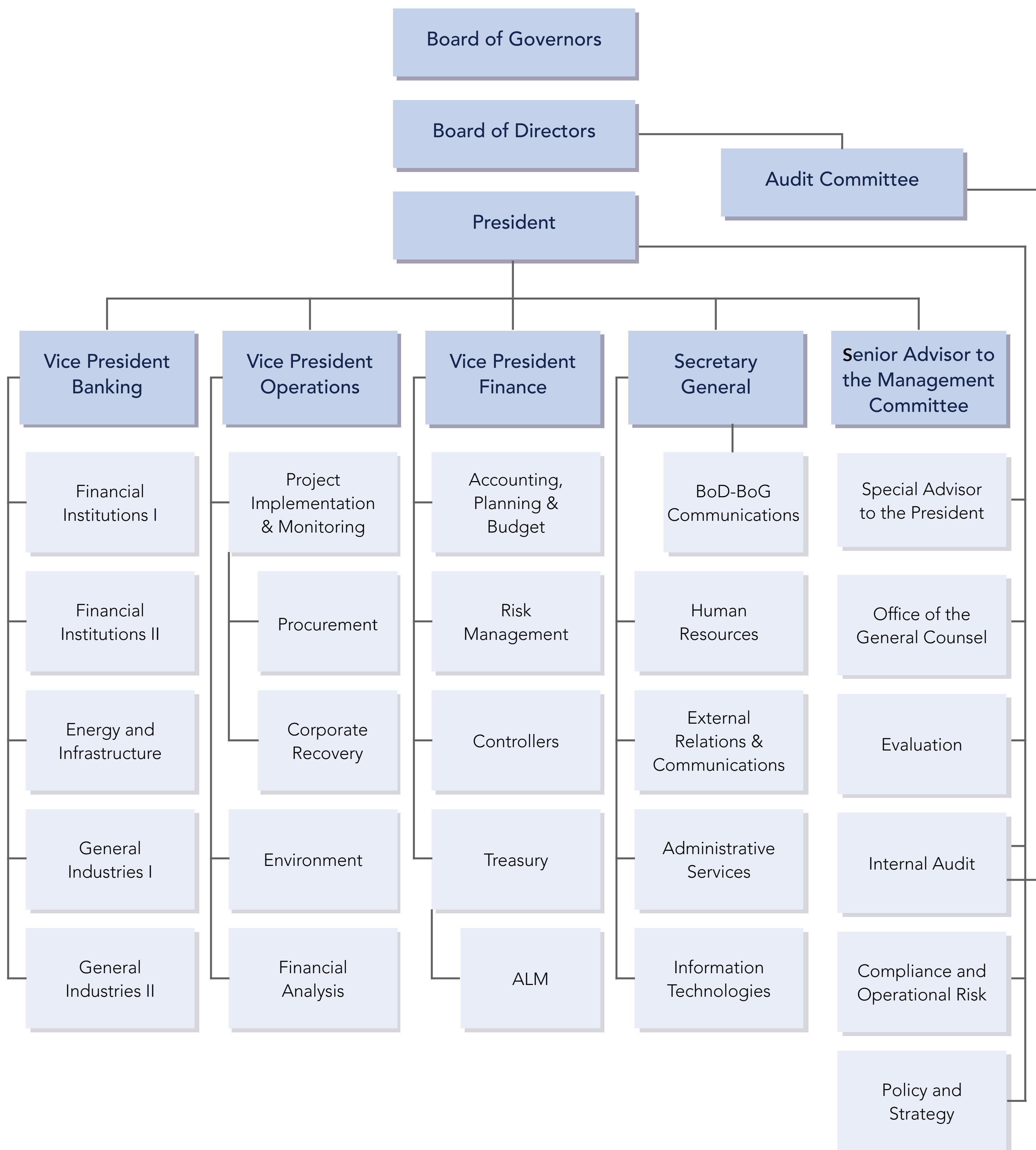
KPMG Certified Auditors S.A.

Athens, Greece

19 April 2019

Organizational Chart

As of 31 December 2018



Annex A

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