

International Investment Bank

Separate financial statements

Year ended 31 December 2013

Together with Independent Auditors' Report

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Independent auditors' report

To the Council of the International Investment Bank

We have audited the accompanying separate financial statements of the International Investment Bank (hereinafter the "Bank"), which comprise the separate statement of financial position as at 31 December 2013, and the separate income statement, separate statement of comprehensive income, separate statement of changes in equity and separate statement of cash flows for the year then ended, and a summary of significant accounting policies and other explanatory information.

Management's responsibility for the separate financial statements

Management is responsible for the preparation and fair presentation of these separate financial statements in accordance with International Financial Reporting Standards, 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.

Auditors' responsibility

Our responsibility is to express an opinion on these separate financial statements based on our audit. We conducted our audit in accordance with International Standards on Auditing. Those standards require that we comply with ethical requirements and plan and perform the audit to obtain reasonable assurance about whether the separate financial statements are free from material misstatement.

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

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

Opinion

In our opinion, the separate financial statements present fairly, in all material respects, the financial position of the Bank as at 31 December 2013, and its financial performance and its cash flows for the year then ended in accordance with International Financial Reporting Standards.

Consolidated financial statements presented separately

Without qualifying our opinion, we draw attention to Note 2 to the separate financial statements which states that the International Investment Bank is the parent entity of the Group of the International Investment Bank and that consolidated financial statements of the Group of the International Investment Bank prepared in accordance with International Financial Reporting Standards have been issued separately. We have audited the consolidated financial statements of the Group of the International Investment Bank as at and for the year ended 31 December 2013 and expressed an unqualified opinion thereon in our auditors' report dated 31 March 2014.

31 March 2014

SEPARATE STATEMENT OF FINANCIAL POSITION**As at 31 December 2013***(Thousands of Euros)*

	<i>Note</i>	<i>31 December 2013</i>	<i>31 December 2012</i>
Assets			
Cash and cash equivalents	5	19,272	8,392
Deposits with banks and other financial institutions	6	39,127	91,807
Financial assets at fair value through profit or loss	7	151	–
Available-for-sale investment securities	8	129,876	100,104
Held-to-maturity investment securities	9	5,910	–
Long-term loans to banks	10	58,795	–
Loans to customers	11	37,625	49,130
Assets held for sale	12	–	10,744
Investments in subsidiary	2	11,161	0
Investment property	13	53,480	52,409
Property and equipment	14	49,997	51,449
Other assets	15	8,384	3,049
Total assets		413,778	367,084
Liabilities			
Due to banks and other financial institutions	16	49,586	3,788
Current customer accounts		3,313	2,396
Other liabilities	15	5,144	5,803
Total liabilities		58,043	11,987
Equity			
Subscribed capital	17	1,300,000	1,300,000
Callable capital		(1,058,685)	(1,134,752)
Paid-in capital		241,315	165,248
Revaluation reserve for available-for-sale investment securities		214	4,340
Revaluation reserve for property and equipment		33,375	33,375
Retained earnings less net income for the year		76,067	149,144
Net income for the year		4,764	2,990
Total equity		355,735	355,097
Total equity and liabilities		413,778	367,084

Signed and authorized for release on behalf of the Board of the Bank

Nikolay Kosov



Chairman of the Board

Eugeny Atanassov



Managing Director of the Financial Department

31 March 2014

The accompanying notes 1 to 30 are an integral part of these separate financial statements.

SEPARATE INCOME STATEMENT**Year ended 31 December 2013***(Thousands of Euros)*

	<i>Note</i>	2013	2012
Interest income	20	13,318	8,737
Interest expenses	20	(432)	(32)
Net interest income		12,886	8,705
Allowance for impairment of loans to customers	11	(8,778)	(4,782)
Net interest income after allowance for loan impairment		4,108	3,923
Fee and commission income		114	238
Fee and commission expense		(72)	(68)
Net fee and commission income		42	170
Net (losses)/gains from foreign currencies	21	(2,682)	763
Net gains from available-for-sale investment securities	17	5,659	3,727
Income from lease of investment property	13	7,983	7,333
Net (losses)/gains from impairment/disposal of assets held for sale	12	(3,588)	75
Income from revaluation of investment property	13	–	1,615
Dividend income		362	182
Other income	22	10,750	201
Net non-interest income		18,484	13,896
Operating income		22,634	17,989
Allowance for impairment of other assets		(152)	(161)
General and administrative expenses	23	(15,537)	(13,495)
Other operating expenses on banking operations		(2,181)	(1,343)
Operating expenses		(17,870)	(14,999)
Net income for the year		4,764	2,990

The accompanying notes 1 to 30 are an integral part of these separate financial statements.

SEPARATE STATEMENT OF COMPREHENSIVE INCOME**Year ended 31 December 2013***(Thousands of Euros)*

	<i>Note</i>	2013	2012
Net income for the year		<u>4,764</u>	<u>2,990</u>
Other comprehensive income/(loss)			
<i>Other comprehensive income/(loss) to be reclassified to profit or loss in subsequent periods:</i>			
Net unrealized (losses)/gains on available-for-sale investment securities		<u>(4,126)</u>	<u>6,691</u>
Net other comprehensive income to be reclassified to profit or loss in subsequent periods		<u>(4,126)</u>	<u>6,691</u>
<i>Other comprehensive income not to be reclassified to profit or loss in subsequent periods:</i>			
Revaluation of property and equipment	14	<u>–</u>	<u>2,284</u>
Net other comprehensive income not to be reclassified to profit or loss in subsequent periods		<u>–</u>	<u>2,284</u>
Other comprehensive income/(loss)		<u>(4,126)</u>	<u>8,975</u>
Total comprehensive income for the year		<u><u>638</u></u>	<u><u>11,965</u></u>

The accompanying notes 1 to 30 are an integral part of these separate financial statements.

SEPARATE STATEMENT OF CHANGES IN EQUITY**Year ended 31 December 2013***(Thousands of Euros)*

	<i>Subscribed capital</i>	<i>Callable capital</i>	<i>Revaluation reserve for available-for-sale investment securities</i>	<i>Revaluation reserve for property and equipment</i>	<i>Retained earnings</i>	<i>Total equity</i>
At 31 December 2011	1,300,000	(1,085,505)	(2,351)	31,091	99,897	343,132
Profit for the year	–	–	–	–	2,990	2,990
Other comprehensive income for the year	–	–	6,691	2,284	–	8,975
Total comprehensive income	–	–	6,691	2,284	2,990	11,965
Withdrawal of the member countries (Note 17)	–	(49,247)	–	–	49,247	–
At 31 December 2012	1,300,000	(1,134,752)	4,340	33,375	152,134	355,097
Profit for the year	–	–	–	–	4,764	4,764
Other comprehensive income for the year	–	–	(4,126)	–	–	(4,126)
Total comprehensive income	–	–	(4,126)	–	4,764	638
Subscribed capital withdrawal (Note 17)	–	76,067	–	–	(76,067)	–
At 31 December 2013	1,300,000	(1,058,685)	214	33,375	80,831	355,735

The accompanying notes 1 to 30 are an integral part of these separate financial statements.

SEPARATE STATEMENT OF CASH FLOWS**Year ended 31 December 2013***(Thousands of Euros)*

	<i>Note</i>	2013	2012
Cash flows from operating activities			
Interest, fees and commissions received from deposits and long-term loans to banks and other financial institutions, and loans to customers		7,122	3,146
Interest, fees and commissions paid		(443)	(96)
Net receipts/(payments) from trading with foreign currencies		56	(160)
Cash flows from lease of investment property		7,983	7,333
Income from disposal of assets held for sale		–	75
General and administrative expenses		(12,776)	(11,342)
Other operating expenses on banking operations		(585)	(1,347)
Cash flows from operating activities before changes in operating assets and liabilities		1,357	(2,391)
<i>Net (increase)/decrease in operating assets</i>			
Deposits with banks and other financial institutions		52,481	19,893
Long-term loans to banks		(58,787)	–
Loans to customers		7,377	(10,828)
Assets held for sale		5,985	–
Other assets		(110)	554
<i>Net increase/(decrease) in operating liabilities</i>			
Due to banks and other financial institutions		46,208	3,819
Current customer accounts		921	17
Other liabilities		(674)	(40)
Net cash flows from operating activities		54,758	11,024
Cash flows from investing activities			
Purchase of available-for-sale investment securities		(187,058)	(153,836)
Proceeds from sale and redemption of investment securities		161,660	138,776
Purchase of held-to-maturity investment securities		(5,958)	–
Investments in subsidiaries		(11,161)	(0)
Investment in investment property	13	(43)	(507)
Acquisition of property and equipment	14	(786)	(982)
Net cash flows from investing activities		(43,346)	(16,549)
Effect of exchange rate changes on cash and cash equivalents		(532)	16
Net increase/(decrease) in cash and cash equivalents		10,880	(5,509)
Cash and cash equivalents, beginning		8,392	13,901
Cash and cash equivalents, ending	5	19,272	8,392

The accompanying notes 1 to 30 are an integral part of these separate financial statements.

(Thousands of Euros)

1. Principal activities

The International Investment Bank (the "Bank") was founded in 1970 and has operated since 1 January 1971.

The Bank is an international institution operating on the basis of the Intergovernmental Agreement on the Establishment of the International Investment Bank (the "Agreement") and the Statutes. The Agreement was ratified by the member countries of the Bank and registered with the Secretariat of the United Nations in December 1971. The Bank is primarily engaged in commercial lending for the benefit of national investment projects in the member countries of the Bank and for other purposes defined by the Council of the Bank. The Bank also performs transactions with securities and foreign currency. The Bank operates from its office at 7 Mashki Poryvaevoi St., Moscow, Russia.

The Bank had an average of 159 staff employees during 2013 (2012: 148).

In 2013, activities of the Bank was focused on implementation of the IIB Relaunch Program, which was unanimously approved at the 98th meeting of the Bank's Council in November 2012 and designed to transform the Bank into a full-service multilateral development institution. IIB consistently implemented its mandate, under which the Bank supports SMEs and socially important projects in member countries. The results of this work confirm the achievement of key strategic goals set by the Bank as a part of "optimistic" scenario for the expired year. Key developments are as follows:

- ▶ Creation of a qualitatively new loan portfolio under new principles of credit policy: focus on offering credit products with a low risk level, reduction of share of direct lending to ultimate borrowers and refocus to lending via partner banks (providing special purpose credit facilities for the development of the SME sector in the member countries, participating in syndicated lending), extension of geographical diversification of investments;
- ▶ Fulfillment of the old loan portfolio rehabilitation program;
- ▶ Alignment of the majority of internal regulations with best practices of modern international development institutions (credit policy, strategic and current planning), introduction of a new system of risk management consistent with recommendations of the Basel Committee on Banking Supervision, operation of a full-service compliance control;
- ▶ Completion of preparations for a transit to a new organizational structure (with division on front, middle and back office) and employee motivation system consistent with best practices of leading multilateral development banks;
- ▶ Strategic focus on the development of partnership relations and IIB's brand recognition. Conclusion of 20 agreements on cooperation with leading financial institutions of member countries (agreements with VEB Group came into practical effect (including OJSC SME Bank, OJSC Russian Agency for Export Credit and Investment Insurance, CJSC State Specialized Russian Export-Import Bank), as well as with several major Vietnamese and Mongolian banks). The following leading development banks invite the Bank to participate in syndicated lending: IFC (International Financial Corporation, 2 syndicates), EBRD (European Bank for Reconstruction and Development, 1 syndicate), the Netherlands Development Finance Company (Nederlandse Financierings-Maatschappij voor Ontwikkelingslanden N.V., 1 syndicate). As a matter of fact, IIB is starting to be a catalyst for investments. Official accession of the Bank to the Master Cooperation Agreement with IFC on 31 January 2014 means IIB joins 19 leading development institutions and gets an opportunity to participate in syndicated lending projects on a regular basis. The Bank works on practical directions of cooperation with such financial institutions as European Investment Bank, KfW, The Black Sea Trade and Development Bank;
- ▶ Completion of a long-term process on settlement of debt of the Republic of Cuba to IIB. The Board and delegations of member countries did considerable work to find mutually acceptable solutions to the Cuban issue. The result of this work is the Agreement on debt restructuring signed by the Bank and the Cuban government, which does not affect the Bank's composition;
- ▶ The 99th meeting of the Bank's Council (Bratislava, 6 June 2013) led to a decision on capitalization of the Bank in the amount of EUR 176 million, of which EUR 100 million are additional contributions of member countries.

The favorable trend of development and reforming IIB, as well as the support from member countries, helped the Bank to receive an international credit rating of investment level from Fitch Ratings in 2013 (long-term issuer default rating at BBB- with a stable outlook and short-term issuer default rating at F3).

The first rating of this level gives the Bank an opportunity to start shaping a qualitatively new financial agenda through fulfillment of a key task, which is a significant accumulation of assets and diversification of a resource base through using a wide range of funding sources, including syndicated loans, bonded loans and other instruments.

(Thousands of Euros)

1. Principal activities (continued)

Therefore, the stage of IIB's active reforming under the Development strategy was practically finished in 2013, the Bank acquired self-identification, created conditions for increasing confidence in the Bank, which facilitate broadening its activities both in member countries and multilateral framework.

Member countries of the Bank

The member countries of the Bank include (share in the paid-in capital of the Bank, %):

<i>Member countries</i>	2013 %	2012 %
Russian Federation	58.026	58.026
Czech Republic	12.587	12.587
Republic of Bulgaria	12.365	12.365
Romania	7.647	7.647
Slovak Republic	6.294	6.294
Republic of Cuba	2.222	2.222
Mongolia	0.435	0.435
Socialist Republic of Vietnam	0.424	0.424
	100.000	100.000

In accordance with the Agreement, each member country of the Bank may withdraw from membership upon notice to the Council of the Bank at least six months in advance. In this case the Bank must settle all obligations to the relevant member country.

The member countries of the Bank may vote at the meetings of the Council and each member country has one vote regardless of the size of its contribution to the Bank's capital.

Conditions of the Bank's financial and business operations in the member countries

In the member countries, the Bank is not subject to taxation and enjoys all privileges available to diplomatic representations.

The Bank is not subject to regulation by the Central Banks of the member countries, including the country of residence.

Business environment in the member countries

The member countries have experienced political and economic change, which has affected, and may continue to affect, the activities of enterprises operating in these countries. Consequently, operations in some member countries involve risks, which do not typically exist in developed markets.

The accompanying separate financial statements reflect the management's assessment of the impact of the member countries' business environment on the results of operations and financial position of the Bank. Future evolution of the conditions in which the Bank operates may differ from the assessment made by the management for the purposes of these separate financial statements.

2. Basis of preparation

General

The Bank, as a parent company, prepares consolidated financial statements in accordance with International Financial Reporting Standards ("IFRS") approved by the International Accounting Standards Board. The consolidated financial statements of the IIB Group for the year ended 31 December 2013 was signed and authorized for release on behalf of the Board of the Bank on 31 March 2014.

These financial statements have been prepared on a separate basis in accordance with International Financial Reporting Standards ("IFRS"). The separate financial statements have been prepared to be included in the report on activities of the International Investment Bank for 2013, which is to be submitted for consideration of the Revision Commission and the Bank's Board.

(Thousands of Euros)

2. Basis of preparation (continued)

Subsidiary

On 2 July 2012, the Bank adopted the decision to establish CJSC IIB Capital (a 100% subsidiary). The share capital of the subsidiary at its establishment amounted to RUB 10 thousand (EUR 250). In 2013, the Bank made an additional contribution to the share capital of the subsidiary in the amount of EUR 11,161 thousand.

On 17 February 2012, the Bank sold a 100% interest in the share capital of LLC StroyProektInvest.

Basis of measurement

These separate financial statements have been prepared under the historical cost convention with the exception of the financial instruments under fair value convention, the changes of which are translated through profit or loss account for the period, available-for-sale financial instruments also stated at fair value, and buildings and investment property are stated at revalued amounts.

Preparation and presentation of financial statements

In accordance with the Statutes of the Bank, the financial year begins on 1 January and ends on 31 December.

Functional and presentation currency

In accordance with the Statutes of the Bank, the management has determined the Bank's functional and presentation currency to be the Euro ("EUR") as it reflects the economic substance of the underlying operations conducted by the Bank and circumstances affecting its operations, because most financial assets and financial liabilities as well as income and expenses of the Bank are denominated in EUR.

These separate financial statements are presented in thousands of Euros ("Thousands of Euros"), unless otherwise indicated.

3. Summary of accounting policies

Changes in accounting policies

The Bank has adopted the following amended IFRS during the year:

IFRS 10 Consolidated Financial Statements, IAS 27 Separate Financial Statements

IFRS 10 establishes a single control model that applies to all entities including special purpose entities. IFRS 10 replaces the parts of previously existing IAS 27 *Consolidated and Separate Financial Statements* that dealt with consolidated financial statements and SIC-12 *Consolidation – Special Purpose Entities*. IFRS 10 changes the definition of control such that an investor controls an investee when it is exposed, or has rights, to variable returns from its involvement with the investee and has the ability to affect those returns through its power over the investee. To meet the definition of control in IFRS 10, all three criteria must be met, including: (a) an investor has power over an investee; (b) the investor has exposure, or rights, to variable returns from its involvement with the investee; and (c) the investor has the ability to use its power over the investee to affect the amount of the investor's returns. IFRS 10 had no impact on the separate financial statements of the Bank.

IFRS 13 Fair Value Measurement

IFRS 13 *Fair Value Measurement* establishes a single source of guidance under IFRS for all fair value measurements. IFRS 13 does not change when an entity is required to use fair value, but rather provides guidance on how to measure fair value under IFRS when fair value is required or permitted. The application of IFRS 13 has not materially impacted the fair value measurements carried out by the Bank.

IFRS 13 also requires specific disclosures on fair values, some of which replace existing disclosure requirements in other standards, including IFRS 7 *Financial Instruments: Disclosures*. Some of these disclosures are specifically required for financial instruments by IAS 34.16A(j), thereby affecting the interim condensed separate financial statements. The Bank provided these disclosures in Note 25.

(Thousands of Euros)

3. Summary of accounting policies (continued)

Changes in accounting policies (continued)

Amendments to IAS 19 Employee Benefits

The IASB has published amendments to IAS 19 *Employee Benefits*, effective for annual periods beginning on or after 1 January 2013, which involve major changes to the accounting for employee benefits, including the removal of the option for deferred recognition of changes in pension plan assets and liabilities (known as the "corridor approach"). In addition, these amendments will limit the changes in the net pension asset (liability) recognized in profit or loss to net interest income (expense) and service costs. These amendments had no impact on the Bank's financial position.

IFRS 12 Disclosure of Interests in Other Entities

IFRS 12 sets out the requirements for disclosures relating to an entity's interests in subsidiaries, joint arrangements, associates and structured entities. The requirements in IFRS 12 are more comprehensive than the previously existing disclosure requirements for subsidiaries. For example, where a subsidiary is controlled with less than a majority of voting rights. The Bank does not have subsidiaries with non-controlling interests as well as unconsolidated structured entities.

Amendments to IAS 1 Changes to the Presentation of Other Comprehensive Income

The amendments to IAS 1 change the grouping of items presented in other comprehensive income. Items that could be reclassified (or recycled) to profit or loss at a future point in time (for example, net losses or gains on available-for-sale financial assets) would be presented separately from items that will never be reclassified (for example, revaluation of buildings). The amendment affects presentation only and has no impact on the Bank's financial position or performance.

IAS 1 Clarification of the Requirement for Comparative Information (amendment)

These amendments clarify the difference between voluntary additional comparative information and the minimum required comparative information. An entity must include comparative information in the related notes to the financial statements when it voluntarily provides comparative information beyond the minimum required comparative period. The amendments clarify that the opening statement of financial position, presented as a result of retrospective restatement or reclassification of items in financial statements does not have to be accompanied by comparative information in the related notes. The amendments affect presentation only and have no impact on the Bank's financial position or performance.

Amendments to IFRS 7 Disclosures – Offsetting Financial Assets and Financial Liabilities

These amendments require an entity to disclose information about rights to set-off and related arrangements (e.g., collateral agreements). The disclosures would provide users with information that is useful in evaluating the effect of netting arrangements on an entity's financial position. The new disclosures are required for all recognized financial instruments that are set off in accordance with IAS 32 *Financial Instruments: Presentation*. The disclosures also apply to recognized financial instruments that are subject to an enforceable master netting arrangement or similar agreements, irrespective of whether they are set off in accordance with IAS 32. These amendments had no impact on the Bank's financial position or performance. The new disclosures are presented in Note 27.

Foreign currency transactions

The separate financial statements are presented in Euro, which is the Bank's functional and presentation currency. Every currency except Euro is considered foreign currency. Transactions in foreign currencies are initially translated in the functional currency, converted at the rate of exchange ruling at the date of the transaction. Monetary assets and liabilities denominated in foreign currencies are retranslated at the functional currency rate of exchange ruling at the reporting date. Gains and losses resulting from the translation of foreign currency transactions are recognized in the separate income statement as "Net gains/(losses) from foreign currencies". Non-monetary assets and liabilities that are measured in terms of historical cost in a foreign currency are translated using the exchange rates as at the dates of the initial transactions. Non-monetary assets and liabilities measured at fair value in a foreign currency are translated using the exchange rates at the date when the fair value was determined.

Differences between the contractual exchange rate of a transaction in a foreign currency and the Bank's exchange rate on the date of the transaction are included in "Net gains/(losses) from dealing in foreign currencies".

(Thousands of Euros)

3. Summary of accounting policies (continued)

Subsidiaries and associates

Subsidiaries are those entities, in which the Bank has an interest of more than one half of the voting rights or equity interest, or otherwise has power to exercise control over their operations. Associates are entities in which the Bank generally has between 20% and 50% of the voting rights or equity interest, or is otherwise able to exercise significant influence, but which it does not control or jointly control. These financial statements of the Bank contain no consolidated interests of the Bank and no investments recognized under the equity method.

Investments in subsidiaries and associates are carried in the separate financial statements at actual acquisition cost. Management regularly measures the recoverable value of such investments and, when necessary, provides for impairment.

Cash and cash equivalents

Cash and cash equivalents include cash on hand and amounts due from banks and other financial institutions, including reverse repurchase agreements, which mature within ninety days from the origination date and are free from contractual encumbrances.

Fair value measurement

The Bank measures financial instruments, such as trading and available-for-sale securities, derivatives and non-financial assets such as investment property and buildings (within property and equipment), at fair value at each reporting date. Also, fair values of financial instruments measured at amortized cost are disclosed in Note 25.

Fair value is the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date. The fair value measurement is based on the presumption that the transaction to sell the asset or transfer the liability takes place either:

- ▶ In the principal market for the asset or liability; or
- ▶ In the absence of a principal market, in the most advantageous market for the asset or liability.

The principal or the most advantageous market must be accessible by the Bank. The fair value of an asset or a liability is measured using the assumptions that market participants would use when pricing the asset or liability, assuming that market participants act in their economic best interest. A fair value measurement of a non-financial asset takes into account a market participant's ability to generate economic benefits by using the asset in its highest and best use or by selling it to another market participant that would use the asset in its highest and best use.

The Bank uses valuation techniques that are appropriate in the circumstances and for which sufficient data are available to measure fair value, maximizing the use of relevant observable inputs and minimizing the use of unobservable inputs.

All assets and liabilities for which fair value is measured or disclosed in the financial statements are categorized within the fair value hierarchy, described as follows, based on the lowest level input that is significant to the fair value measurement as a whole:

- ▶ Level 1 – Quoted (unadjusted) market prices in active markets for identical assets or liabilities
- ▶ Level 2 – Valuation techniques for which the lowest level input that is significant to the fair value measurement is directly or indirectly observable
- ▶ Level 3 – Valuation techniques for which the lowest level input that is significant to the fair value measurement is unobservable.

For assets and liabilities that are recognized in the financial statements on a recurring basis, the Bank determines whether transfers have occurred between Levels in the hierarchy by re-assessing categorization (based on the lowest level input that is significant to the fair value measurement as a whole) at the end of each reporting period.

(Thousands of Euros)

3. Summary of accounting policies (continued)

Financial assets

Initial recognition

Financial assets in the scope of IAS 39 are classified as either financial assets at fair value through profit or loss, loans and receivables, held-to-maturity investments, or available-for-sale financial assets, as appropriate. The Bank determines the classification of its financial assets upon initial recognition, and subsequently can reclassify financial assets in certain cases as described below.

Date of recognition

All regular way purchases and sales of financial assets are recognized on the trade date i.e. the date that the Bank commits to purchase the asset. Regular way purchases or sales are purchases or sales of financial assets that require delivery of assets within the period generally established by regulation or convention in the marketplace.

Financial assets at fair value through profit or loss

Financial assets classified as held for trading are included in the category "financial assets at fair value through profit or loss". Financial assets are classified as held for trading if they are acquired for the purpose of selling in the near term. Derivatives are also classified as held for trading unless they are designated and effective hedging instruments. Gains or losses on financial assets held for trading are recognized in profit or loss.

Held-to-maturity investments

Non-derivative financial assets with fixed or determinable payments and fixed maturity are classified as held-to-maturity when the Bank has the positive intention and ability to hold them to maturity. Investments intended to be held for an undefined period are not included in this classification. Held-to-maturity investments are subsequently measured at amortized cost. Gains and losses are recognized in profit or loss when the investments are impaired, as well as through the amortization process.

Loans and receivables

Loans and receivables are non-derivative financial assets with fixed or determinable payments that are not quoted in an active market. They are not entered into with the intention of immediate or short-term resale and are not classified as trading securities or designated as investment securities available-for-sale. Such assets are carried at amortized cost using the effective interest method. Gains and losses are recognized in profit or loss when the loans and receivables are derecognized or impaired, as well as through the amortization process.

Available-for-sale financial assets

Available-for-sale financial assets are those non-derivative financial assets that are designated as available-for-sale or are not classified in any of the three preceding categories. After initial recognition available-for-sale financial assets are measured at fair value with gains or losses being recognized in other comprehensive income until the investment is derecognized or until the investment is determined to be impaired at which time the cumulative gain or loss previously reported in other comprehensive income is reclassified to the separate income statement. However, interest calculated using the effective interest method is recognized in profit or loss.

Reclassification of financial assets

If a non-derivative financial asset classified as held for trading is no longer held for the purpose of selling in the near term, it may be reclassified out of the fair value through profit or loss category in one of the following cases:

- ▶ a financial asset that would have met the definition of loans and receivables above may be reclassified to loans and receivables category if the Bank has the intention and ability to hold it for the foreseeable future or until maturity;
- ▶ other financial assets may be reclassified to available for sale or held to maturity categories only in rare circumstances.

(Thousands of Euros)

3. Summary of accounting policies (continued)

Financial assets (continued)

A financial asset classified as available for sale that would have met the definition of loans and receivables may be reclassified to loans and receivables category of the Bank has the intention and ability to hold it for the foreseeable future or until maturity.

Financial assets are reclassified at their fair value on the date of reclassification. Any gain or loss already recognized in profit or loss is not reversed. The fair value of the financial asset on the date of reclassification becomes its new cost or amortized cost, as applicable.

Repurchase and reverse repurchase agreements and securities lending

Sale and repurchase agreements ("repos") are treated as secured financing transactions. Securities sold under sale and repurchase agreements are retained in the separate statement of financial position and, in case the transferee has the right by contract or custom to sell or repledge them, reclassified as securities pledged under sale and repurchase agreements. The corresponding liability is presented within amounts due to credit institutions or customers. Securities purchased under agreements to resell ("reverse repo") are recorded as cash equivalents, amounts due from credit institutions or loans to customers as appropriate. The difference between sale and repurchase price is treated as interest and accrued over the life of repo agreements using the effective yield method.

Securities lent to counterparties are retained in the separate statement of financial position. Securities borrowed are not recorded in the separate statement of financial position, unless these are sold to third parties, in which case the purchase and sale are recorded within gains less losses from trading securities in the separate income statement. The obligation to return them is recorded at fair value as a trading liability.

Derivative financial instruments

In the normal course of business, the Bank enters into various derivative financial instruments including forwards and swaps in the foreign exchange market. Such financial instruments are held for trading and are recorded at fair value. The fair values are estimated based on quoted market prices or pricing models that take into account the current market and contractual prices of the underlying instruments and other factors. Derivatives are carried as assets when their fair value is positive and as liabilities when it is negative. Gains and losses resulting from these instruments are included in the separate income statement as net (losses)/gains from foreign currencies dealing.

Derivatives embedded in other financial instruments are treated as separate derivatives and recorded at fair value if their economic characteristics and risks are not closely related to those of the host contract, and the host contract is not itself held for trading or designated at fair value through profit or loss. The embedded derivatives separated from the host are carried at fair on the trading portfolio with changes in fair value recognized in profit or loss.

Borrowings

Issued financial instruments or their components are classified as liabilities, where the substance of the contractual arrangement results in the Bank having an obligation either to deliver cash or another financial asset to the holder, or to satisfy the obligation other than by the exchange of a fixed amount of cash or another financial asset for a fixed number of own equity instruments. Such instruments include amounts due to credit institutions. After initial recognition, borrowings are subsequently measured at amortized cost using the effective interest method. Gains and losses are recognized in profit or loss when the borrowings are derecognized as well as through the amortization process.

Leases

Operating – Bank as lessee

Leases of assets under which the risks and rewards of ownership are effectively retained by the lessor are classified as operating leases. Lease payments under an operating lease are recognized as expenses on a straight-line basis over the lease term and included into general and administrative expenses.

(Thousands of Euros)

3. Summary of accounting policies (continued)

Leases (continued)

Operating – Bank as lessor

The Bank presents assets subject to operating leases in the separate statement of financial position according to the nature of the asset. Lease income from operating leases is recognized in the separate income statement over the lease term within net non-interest income on "Income from lease of investment property". The aggregate cost of incentives provided to lessees is recognized as a reduction of rental income over the lease term on a straight-line basis. Initial direct costs incurred specifically to earn revenues from an operating lease are added to the carrying amount of the leased asset.

Measurement of financial instruments at initial recognition

When financial instruments are recognized initially, they are measured at fair value, adjusted, in the case of instruments not at fair value through profit or loss, for directly attributable fees and costs.

The best evidence of the fair value of a financial instrument at initial recognition is normally the transaction price. If the Bank determines that the fair value at initial recognition differs from the transaction price, then:

- ▶ if the fair value is evidenced by a quoted price in an active market for an identical asset or liability (i.e., a Level 1 input) or based on a valuation technique that uses only data from observable markets, the Bank recognizes the difference between the fair value at initial recognition and the transaction price as a gain or loss;
- ▶ in all other cases, the initial measurement of the financial instrument is adjusted to defer the difference between the fair value at initial recognition and the transaction price. After initial recognition, the Bank recognizes that deferred difference as a gain or loss only when the inputs become observable, or when the instrument is derecognized.

Offsetting of financial instruments

Financial assets and liabilities are offset and the net amount is reported in the separate statement of financial position when there is a legally enforceable right to set off the recognized amounts and there is an intention to settle on a net basis, or to realize the asset and settle the liability simultaneously. This is not generally the case with master netting agreements, and the related assets and liabilities are presented gross in the separate statement of financial position.

Impairment of financial assets

The Bank assesses at each reporting date whether there is any objective evidence that a financial asset or a group of financial assets is impaired. A financial asset or a group of financial assets is deemed to be impaired if, and only if, there is objective evidence of impairment as a result of one or more events that has occurred after the initial recognition of the asset (an incurred "loss event") and that loss event (or events) has an impact on the estimated future cash flows of the financial asset or the group of financial assets that can be reliably estimated.

Evidence of impairment may include indications that the borrower or a group of borrowers is experiencing significant financial difficulty, default or delinquency in interest or principal payments, the probability that they will enter bankruptcy or other financial reorganization and where observable data indicate that there is a measurable decrease in the estimated future cash flows, such as changes in arrears or economic conditions that may be related to defaults.

Short-term and long-term amounts due from banks and other credit institutions and loans to customers

For amounts due from banks and other credit institutions and loans to customers carried at amortized cost, the Bank first assesses individually whether objective evidence of impairment exists individually for financial assets that are individually significant, or collectively for financial assets that are not individually significant. If the Bank determines that no objective evidence of impairment exists for an individually assessed financial asset, whether significant or not, it includes the asset in a group of financial assets with similar credit risks characteristics and collectively assesses them for impairment. Assets that are individually assessed for impairment and for which an impairment loss is, or continues to be, recognized are not included in a collective assessment of impairment.

(Thousands of Euros)

3. Summary of accounting policies (continued)

Impairment of financial assets (continued)

If there is an objective evidence that an impairment loss exists, the amount of the loss is measured as the difference between the assets' value in the separate statement of financial position and the present value of estimated future cash flows (excluding future expected credit losses that have not yet been incurred). The value of the asset in the separate statement of financial position is reduced through the use of an allowance account and the amount of the loss is recognized in the separate income statement. Interest income continues to be accrued on the reduced carrying amount of asset based on the original effective interest rate of the asset. Loans together with the associated allowance are written off when there is no realistic prospect of future recovery and all collateral has been realized or has been transferred to the Bank. If, in a subsequent year, the amount of the estimated impairment loss increases or decreases because of an event occurring after the impairment was recognized, the previously recognized impairment loss is increased or reduced by adjusting the allowance account. If amounts previously written off are later recovered, the recovery is credited to the separate income statement.

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

Future cash flows on a group of financial assets that are collectively evaluated for impairment are estimated on the basis of historical loss experience for assets with credit risk characteristics similar to those in the group. Historical loss experience is adjusted on the basis of current observable data to reflect the effects of current conditions that did not affect the years on which the historical loss experience is based and to remove the effects of conditions in the historical period that do not exist currently. Estimates of changes in future cash flows reflect, and are directionally consistent with, changes in related observable data from year to year (such as changes in unemployment rates, property prices, commodity prices, payment status, or other factors that are indicative of incurred losses in the group or their magnitude).

The methodology and assumptions used for estimating future cash flows are reviewed regularly to reduce any differences between loss estimates and actual loss experience.

Held-to-maturity financial investments

For held-to-maturity investments the Bank assesses individually whether there is objective evidence of impairment. If there is objective evidence that an impairment loss has been incurred, the amount of the loss is measured as the difference between the asset's carrying amount and the present value of estimated future cash flows. The carrying amount of the asset is reduced and the amount of the loss is recognized in profit or loss.

If, in a subsequent year, the amount of the estimated impairment loss decreases because of an event occurring after the impairment was recognized, any amounts formerly charged are credited to the separate income statement.

Available-for-sale financial investments

For available-for-sale financial instruments, the Bank determines at each reporting date whether there is objective evidence that an instrument or a group of instruments is impaired.

In the case of equity investments classified as available-for-sale, objective evidence would include a significant or prolonged decline in the fair value of the investment below its acquisition cost. Where there is evidence of impairment, the cumulative loss – measured as the difference between the acquisition cost and the current fair value, less any impairment loss on that investment previously recognized in the separate income statement – is reclassified from other comprehensive income to the separate income statement. Impairment losses on equity investments are not reversed through the separate income statement; increases in their fair value after impairment are recognized in other comprehensive income.

In the case of debt instruments classified as available-for-sale, impairment is assessed based on the same criteria as financial assets carried at amortized cost. Future interest income is based on the reduced carrying amount and is accrued using the rate of interest used to discount the future cash flows for the purpose of measuring the impairment loss. The interest income is recorded in the separate income statement. If, in a subsequent year, the fair value of a debt instrument increases and the increase can be objectively related to an event occurring after the impairment loss was recognized in the separate income statement, the impairment loss is reversed through the separate income statement.

(Thousands of Euros)

3. Summary of accounting policies (continued)

Impairment of financial assets (continued)

Renegotiated loans

Where possible, the Bank seeks to restructure loans rather than to take possession of collateral. This may involve extending the payment arrangements and the agreement of new loan conditions. The accounting treatment of such restructuring is as follows:

- ▶ If the currency of the loan has been changed the old loan is derecognized and the new loan is recognized in the separate statement of financial position.
- ▶ If the loan restructuring is not caused by the financial difficulties of the borrower the Bank uses the same approach as for financial liabilities described below.
- ▶ If the loan restructuring is due to the financial difficulties of the borrower and the loan is impaired after restructuring, the Bank recognizes the difference between the present value of the new cash flows discounted using the original effective interest rate and the carrying amount before restructuring in the provision charges for the period. In case loan is not impaired after restructuring the Bank recalculates the effective interest rate.

Once the terms have been renegotiated, the loan is no longer considered past due. Management continuously reviews renegotiated loans to ensure that all criteria are met and that future payments are likely to occur. The loans continue to be subject to an individual or collective impairment assessment, calculated using the loan's original or current effective interest rate.

Derecognition of financial assets and liabilities

Financial assets

A financial asset (or, where applicable a part of a financial asset or part of a group of similar financial assets) is derecognized in the separate statement of financial position where:

- ▶ the rights to receive cash flows from the asset have expired;
- ▶ the Bank has transferred its rights to receive cash flows from the asset, or retained the right to receive cash flows from the asset, but has assumed an obligation to pay them in full without material delay to a third party under a "pass-through" arrangement; and
- ▶ the Bank either (a) has transferred substantially all the risks and rewards of the asset, or (b) has neither transferred nor retained substantially all the risks and rewards of the asset, but has transferred control of the asset.

Where the Bank has transferred its rights to receive cash flows from an asset and has neither transferred nor retained substantially all the risks and rewards of the asset nor transferred control of the asset, the asset is recognized to the extent of the Bank's continuing involvement in the asset. Continuing involvement that takes the form of a guarantee over the transferred asset is measured at the lower of the original carrying amount of the asset and the maximum amount of consideration that the Bank could be required to repay.

Where continuing involvement takes the form of a written and/or purchased option (including a cash-settled option or similar provision) on the transferred asset, the extent of the Bank's continuing involvement is the amount of the transferred asset that the Bank may repurchase, except that in the case of a written put option (including a cash-settled option or similar provision) on an asset measured at fair value, the extent of the Bank's continuing involvement is limited to the lower of the fair value of the transferred asset and the option exercise price.

Financial liabilities

A financial liability is derecognized when the obligation under the liability is discharged or cancelled or expires.

Where an existing financial liability is replaced by another from the same lender on substantially different terms, or the terms of an existing liability are substantially modified, such an exchange or modification is treated as a derecognition of the original liability and the recognition of a new liability, and the difference in the respective carrying amounts is recognized in the separate income statement.

(Thousands of Euros)

3. Summary of accounting policies (continued)

Property and equipment

Property and equipment are carried in the separate financial statements at cost, excluding the costs of day-to-day servicing, less accumulated depreciation and any accumulated impairment, excluding buildings carried at revalued cost, as described below. Such cost includes the cost of replacing part of equipment when that cost is incurred if the recognition criteria are met.

The carrying amounts of property and equipment are reviewed for impairment when events or changes in circumstances indicate that the carrying value may not be recoverable.

Where an item of property and equipment comprises major components having different useful lives, they are accounted for as separate items of property and equipment.

Following initial recognition at cost, buildings are carried at a revalued amount, which is the fair value at the date of the revaluation less any subsequent accumulated depreciation and subsequent accumulated impairment losses. Valuations of buildings are performed frequently enough to ensure that the fair value of a revalued asset does not differ materially from its carrying amount.

Accumulated depreciation as at the revaluation date is eliminated against the gross carrying amount of the asset and the net amount is restated to the revalued amount of the asset. Any revaluation surplus is credited to the revaluation reserve for property and equipment included in other comprehensive income, except to the extent that it reverses a revaluation decrease of the same asset previously recognized in the separate income statement, in which case the increase is recognized in profit or loss. A revaluation deficit is recognized in the separate income statement, except that a deficit directly offsetting a previous surplus on the same asset is directly offset against the surplus in the revaluation reserve for property and equipment.

Upon disposal, any revaluation reserve relating to the particular asset being sold is transferred to retained earnings.

Depreciation of property and equipment (including self-constructed property and equipment) begins when it is available for use and is recognized in the separate income statement.

Depreciation is calculated on a straight-line basis over the following estimated useful lives:

	<u>Years</u>
Buildings	85
Equipment	3-7
Computers	3-6
Office furniture	5-10
Motor vehicles	4

The asset's residual values, useful lives and methods are reviewed and adjusted as appropriate, at each financial year-end.

Costs related to repairs and renewals are charged when incurred and included in general and administrative expenses, unless they qualify for capitalization.

Investment property

Investment property is a part of building held to earn rental income or for capital appreciation and which is not used by the Bank or held for the sale in the ordinary course of business. Property that is being constructed or developed or redeveloped for future use as investment property is also classified as investment property.

Investment property is initially recognized at cost, including transaction costs, and subsequently remeasured at fair value reflecting market conditions at the end of the reporting period. Fair value of the Bank's investment property is determined on the base of various sources including reports of independent appraisers, who hold a recognized and relevant professional qualification and who have recent experience in valuation of property of similar location and category.

(Thousands of Euros)

3. Summary of accounting policies (continued)

Investment property (continued)

Subsequent expenditure is subject to capitalization only when it is probable that future economic benefits associated with an asset will flow to the Bank and it can be measured reliably. All other repairs and maintenance costs are expensed when incurred. If an investment property becomes owner-occupied, it is reclassified to buildings, and its carrying amount at the date of reclassification becomes its deemed cost to be subsequently depreciated.

Intangible assets

Intangible assets include computer software.

Intangible assets acquired by the Bank are recognized in the separate financial statements at their acquisition cost.

Intangible assets acquired separately are measured on initial recognition at cost. The cost of intangible assets acquired in a business combination is fair value as at the date of acquisition. Following initial recognition, intangible assets are carried at cost less any accumulated amortization and any accumulated impairment losses. The useful lives of intangible assets are assessed to be either finite or indefinite. Intangible assets with finite lives are amortized over the useful economic lives of 3 years and assessed for impairment whenever there is an indication that the intangible asset may be impaired. Amortization periods and methods for intangible assets with indefinite useful lives are reviewed at least at each financial year-end.

Assets classified as held for sale

The Bank classifies a non-current asset as held for sale if its carrying amount will be recovered principally through a sale transaction rather than through continuing use. For this to be the case, the non-current asset must be available for immediate sale in its present condition subject only to terms that are usual and customary for sales of such assets and its sale must be highly probable.

The sale qualifies as highly probable if the Bank's management is committed to a plan to sell the non-current asset and an active program to locate a buyer and complete the plan must have been initiated. Further, the non-current asset must have been actively marketed for a sale at price that is reasonable in relation to its current fair value and in addition the sale should be expected to qualify for recognition as a completed sale within one year from the date of classification of the non-current asset as held for sale.

The Bank measures an asset classified as held for sale at the lower of its carrying amount and fair value less costs to sell. The Bank recognizes an impairment loss for any initial or subsequent write-down of the asset to fair value less costs to sell if events or changes in circumstance indicate that their carrying amount may be impaired.

Provisions

Provisions are recognized when the Bank has a present legal or constructive obligation as a result of past events, and it is probable that an outflow of resources embodying economic benefits will be required to settle the obligation and a reliable estimate of the amount of obligation can be made.

Equity

In accordance with amendments to IAS 32, *Financial Instruments: Presentation*, and IAS 1, *Presentation of Financial Statements – Puttable Financial Instruments and Obligations Arising on Liquidation*, that were issued in February 2008, participants' shares are recognized in equity and not in liabilities.

Contingencies

Contingent liabilities are not recognized in the separate statement of financial position but are disclosed unless the possibility of any outflow in settlement is remote. A contingent asset is not recognized in the separate statement of financial position but disclosed in the separate financial statements, when an inflow of economic benefits is probable.

(Thousands of Euros)

3. Summary of accounting policies (continued)

Recognition of income and expenses

Revenue is recognized to the extent that it is probable that the economic benefits will flow to the Bank and the revenue can be reliably measured. The following specific recognition criteria must also be met before revenue is recognized in the separate financial statements:

Interest and similar income and expense

For all financial instruments measured at amortized cost and interest bearing securities classified as trading or available-for-sale, interest income or expense is recorded at the effective interest rate, which is the rate that exactly discounts estimated future cash payments or receipts through the expected life of the financial instrument or a shorter period, where appropriate, to the net carrying amount of the financial asset or financial liability. The calculation takes into account all contractual terms of the financial instrument (for example, prepayment options) and includes any fees or incremental costs that are directly attributable to the instrument and are an integral part of the effective interest rate, but not future credit losses. The carrying amount of the financial asset or financial liability is adjusted if the Bank revises its estimates of payments or receipts. The adjusted carrying amount is calculated based on the original effective interest rate and the change in carrying amount is recorded as interest income or expense.

Once the recorded value of a financial asset or a group of similar financial assets has been reduced due to an impairment loss, interest income continues to be recognized using the original effective interest rate applied to the new carrying amount.

Fee and commission income

The Bank earns fee and commission income from a diverse range of services it provides to its customers. Fee income can be divided into the following two categories:

- ▶ *Fee income earned from services that are provided over a certain period of time*

Fees earned for the provision of services over a period of time are accrued over that period. These fees include commission income and credit and deposit fees. Loan commitment fees for loans that are likely to be drawn down and other credit related fees are deferred (together with any incremental costs) and recognized as an adjustment to the effective interest rate on the loan.

- ▶ *Other fee and commission income*

Fees earned for the provision of transaction services are recognized on completion of the underlying transaction. Fees or components of fees that are linked to a certain performance are recognized after fulfilling the corresponding criteria.

Fee and commission expense

Fee and commission expenses comprise commissions on securities transactions and commissions on cash settlement transactions. Commissions paid on purchase of securities classified as financial instruments at fair value through profit or loss are recognized in the separate income statement at the purchase date. Commissions paid on all other purchases of securities are recognized as an adjustment to the carrying amount of the instrument with corresponding adjustment to its effective yield.

Dividend income

Revenue is recognized when the Bank's right to receive the payment is established.

Segment reporting

The reportable segments of the Bank comprise the following operating segments: Credit and investment activity, Treasury, Other operations.

(Thousands of Euros)

3. Summary of accounting policies (continued)

Future changes in accounting policies

Standards and interpretations issued but not yet effective

IFRS 9 Financial Instruments

IFRS 9, as issued, reflects two of the three phases of the IASB project on replacement of IAS 39 and applies to classification and measurement of financial assets and financial liabilities and hedge accounting. The standard has no mandatory effective date and may be applied voluntarily. The adoption of IFRS 9 will have an effect on the classification and measurement of the Bank's financial assets, but will not have an impact on classification and measurements of the Bank's financial liabilities. The Bank will quantify the effect when the remaining part of the standard containing guidance on impairment of financial assets is issued.

Investment Entities (amendments to IFRS 10, IFRS 12 and IAS 27)

These amendments are effective for annual periods beginning on or after 1 January 2014 provide an exception to the consolidation requirement for entities that meet the definition of an investment entity under IFRS 10. The exception to consolidation requires investment entities to account for subsidiaries at fair value through profit or loss. This amendment shall not have effect on the separate financial statements of the Bank.

IAS 32 Offsetting Financial Assets and Financial Liabilities – Amendments to IAS 32

These amendments clarify the meaning of "currently has a legally enforceable right to set-off" and the criteria for non-simultaneous settlement mechanisms of clearing houses to qualify for offsetting. These are effective for annual periods beginning on or after 1 January 2014. These amendments are not expected to be relevant to the Bank.

IFRIC Interpretation 21 Levies (IFRIC 21)

IFRIC 21 clarifies that an entity recognizes a liability for a levy when the activity that triggers payment, as identified by the relevant legislation, occurs. For a levy that is triggered upon reaching a minimum threshold, the interpretation clarifies that no liability should be anticipated before the specified minimum threshold is reached. IFRIC 21 is effective for annual periods beginning on or after 1 January 2014. The Bank does not expect that IFRIC 21 will have a material impact on its separate financial statements.

IAS 39 Novation of Derivatives and Continuation of Hedge Accounting – Amendments to IAS 39

These amendments provide relief from discontinuing hedge accounting when novation of a derivative designated as a hedging instrument meets certain criteria. These amendments are effective for annual periods beginning on or after 1 January 2014. The Bank has not novated its derivatives during the current period. However, these amendments would be considered for future novations.

4. Significant accounting judgments and estimates

Assumptions and estimation uncertainty

In the process of applying the Bank's accounting policies, management has made its professional judgments, used several assumptions and estimates on determining the amounts of assets and liabilities recognized in the separate financial statements, which have the most significant effect on the amounts recognized in the separate financial statements and the carrying amount of assets and liabilities in the following financial year. Estimates and assumptions are continuously assessed and are based on the management experience and other factors, including expectations of future events that are believed to be reasonable under the circumstances. The most significant uses of judgments and estimates are as follows:

Allowance for impairment of loans and other financial assets carried at amortized cost

Financial assets are recorded in the Bank's separate statement of financial position less allowances for impairment. The Bank regularly reviews its financial assets to assess impairment. When assessing impairment losses, the Bank uses its professional judgment in relation to objective evidences that future contractual cash flows on financial asset shall decrease. These evidences may include information on financial difficulties of the borrower or other observable data on adverse changes in the payment status of borrowers, or national or local economic conditions that correlate with defaults on assets. The Bank uses its professional judgment to adjust observable data for financial assets to reflect current circumstances. Impairment loss may be reversed only if a subsequent increase of estimated contractual cash flows can be objectively related to an event occurring after the impairment loss was recognized.

(Thousands of Euros)

4. Significant accounting judgments and estimates (continued)

Assumptions and estimation uncertainty (continued)

Fair value of financial instruments

Where the fair values of financial assets and financial liabilities recorded in the statement of financial position cannot be derived from active markets, they are determined using a variety of valuation techniques that include the use of mathematical models. The input to these models is taken from observable markets where possible, but where this is not feasible, a degree of judgment is required in establishing fair values. Additional details are provided in Note 25.

Impairment of available-for-sale equity securities

The Bank determines that available-for-sale equity investment securities are impaired when there has been a significant or prolonged decline in the fair value below their cost. The determination of what is significant or prolonged requires judgment. In making this judgment, the Bank evaluates, among other factors, the volatility of share prices. In addition, impairment may take place when there is evidence of a deterioration in the financial health of the investee, industry and sector performance, changes in technology, and operating or financing cash flows.

Fair values of buildings and investment property

As disclosed in Note 3, the Bank applies the fair value model with regard to buildings and investment property.

As for buildings within property and equipment, the Bank monitors the compliance of the present value of buildings with their fair value and performs revaluation to ensure that there are no significant differences. Changes in the fair value are recognized in other comprehensive income. The most recent revaluation of the Bank's building was carried out as at 26 December 2012 by an independent firm of professional appraisers applying an appropriate valuation methodology and information on transactions with similar real estate objects on the local market. However, valuation results based on the above valuation method may differ from the prices of actual transactions on the real estate market. Starting from 26 December 2012, the revalued building is depreciated in accordance with the remaining useful life.

As for investment property, the Bank monitors changes in its fair value at each reporting date to ensure that the present value of investment property does not differ materially from its fair value. Changes in the fair value of investment property are recognized in the separate income statement. The most recent revaluation of the Bank's investment property was carried out as at 26 December 2012 by an independent firm of professional appraisers applying an appropriate valuation methodology and information on transactions with similar real estate objects on the local market. However, valuation results based on the above valuation method may differ from the prices of actual transactions on the real estate market. The Bank believes that as at 31 December 2013, the fair value of investment property did not change significantly.

In particular, information on significant areas of estimation uncertainty and critical judgments in applying accounting policies is presented in the following notes:

- ▶ Note 7 – Financial liabilities at fair value through profit or loss;
- ▶ Note 8 – Available-for-sale investment securities;
- ▶ Note 10 – Long-term loans to banks;
- ▶ Note 11 – Loans to customers;
- ▶ Note 13 – Investment property;
- ▶ Note 14 – Property and equipment;
- ▶ Note 18 – Contingencies and lending commitments.

(Thousands of Euros)

5. Cash and cash equivalents

Cash and cash equivalents comprise:

	<u>2013</u>	<u>2012</u>
Cash on hand	197	88
Nostro accounts with banks and other financial institutions		
<i>Credit rating AAA</i>	2,148	820
<i>Credit rating from A- to A+</i>	838	1,513
<i>Credit rating from BBB- to BBB+</i>	198	51
<i>No credit rating</i>	–	4
Total Nostro accounts with banks and other financial institutions	3,184	2,388
Short-term deposits with banks:		
Term deposits with banks		
<i>Credit rating from A- to A+</i>	6,500	–
<i>Credit rating from BBB- to BBB+</i>	4,272	5,916
Total short-term deposits with banks	10,772	5,916
Collateral on credit transactions with banks		
<i>No credit rating</i>	5,119	–
Cash and cash equivalents	19,272	8,392

Cash and cash equivalents are neither impaired, nor past due.

In December 2013, the Mongolian customer with no credit rating was provided a long-term mortgage loan (Note 11). The surety bank placed a short-term interest-free collateral deposit with IIB prior to the mortgage registration in Mongolia (Note 16). The deposit in the amount of EUR 5,119 thousand is placed by the Bank on the correspondent account of the surety bank.

6. Deposits with banks and other financial institutions

Deposits with banks and other financial institutions comprise:

	<u>2013</u>	<u>2012</u>
Term deposits with banks up to 1 year		
<i>Credit rating from A- to A+</i>	–	10,017
<i>Credit rating from BBB- to BBB+</i>	–	25,069
<i>Credit rating from BB- to BB+</i>	–	25,085
<i>Credit rating B+</i>	39,127	18,759
<i>No credit rating</i>	–	12,877
Deposits with banks and other financial institutions	39,127	91,807

Amounts due from the National Bank of the Republic of Cuba

As at 31 December 2013, the Bank placed deposits with the National Bank of the Republic of Cuba (without credit rating). As part of restructuring of reciprocal claims and liabilities, the 100th meeting of the IIB Council approved an Agreement under which the parties confirmed the debt of the Republic of Cuba to IIB, converted the debt into the Bank's functional currency and made a partial write off of loans issued to borrowers in the Republic of Cuba (Note 11). Under this Agreement the parties also approved the principles and terms of debt settlement. Despite the restructuring, the Bank did not reverse previously accrued allowances for impairment, therefore as at 31 December 2013, the Bank created a 100% allowance for impairment of these deposits.

	<u>2013</u>	<u>2012</u>
Term deposits with the National Bank of the Republic of Cuba without credit rating	34,967	35,119
Less: allowance for impairment	(34,967)	(35,119)
Term deposits with the National Bank of the Republic of Cuba	–	–

*(Thousands of Euros)***6. Deposits with banks and other financial institutions (continued)****Amounts due from the National Bank of the Republic of Cuba (continued)**

Information on change in the allowance for impairment of deposits with the National Bank of the Republic of Cuba is presented below:

	<u>2013</u>	<u>2012</u>
At 1 January	35,119	35,049
(Reversal)/charge of allowance for impairment due to changes in exchange rates	(152)	70
At 31 December	<u>34,967</u>	<u>35,119</u>

Concentration of deposits with banks and other financial institutions

As at 31 December 2013, the Bank had one counterparty (2012: no counterparties) accounting for over 20% of the Bank's total deposits with banks and other financial institutions, except for deposits with the National Bank of the Republic of Cuba.

7. Financial instruments at fair value through profit or loss

Financial instruments at fair value through profit or loss include derivative transactions. Derivative financial instruments are generally traded in an over-the-counter market with professional market counterparties on standardized contractual terms and conditions. Derivative financial instruments are either assets or liabilities depending on the fluctuations in the market which can have either favorable or unfavorable effect on these instruments. Thus, the fair value of derivative financial instruments may significantly change depending on potentially favorable or unfavorable conditions.

Foreign currency transactions

The table below shows the fair value of derivative financial instruments as of 31 December 2013 and notional amounts of term contracts for the purchase and sale of foreign currency specifying weighted average contractual exchange rates (31 December 2012: no).

	<u>Notional amount</u>		<u>Weighted average exchange rate</u>	<u>Fair value</u>
	<u>Purchase</u>	<u>Sale</u>		<u>Assets</u>
Term foreign currency transactions	14,400 EUR'000	19,646 USD'000	1.36	151

The notional amount, recorded gross, is the amount of a derivative's underlying asset and liability and is the basis upon which changes in the value of derivatives are measured. The notional amounts indicate the volume of transactions outstanding at the year end and are not indicative of the credit risk.

As at 31 December 2013, the Bank has positions in the following types of derivatives:

Swaps: Swaps are contractual agreements between two parties to exchange movements in interest and foreign currency rates and equity indices, and (in the case of credit default swaps) to make payments with respect to defined credit events based on specified notional amounts.

(Thousands of Euros)

8. Available-for-sale investment securities

Available-for-sale investment securities comprise:

	<u>2013</u>	<u>2012</u>
Quoted debt securities		
Government bonds of member countries and bonds of regional governments:		
<i>Eurobonds issued by governments of member countries</i>	32,126	34,853
<i>Bonds of regional governments</i>	3,252	12,774
Government bonds of member countries and bonds of regional governments	<u>35,378</u>	<u>47,627</u>
Corporate bonds:		
<i>Credit rating from A- to A+</i>	46,488	3,877
<i>Credit rating from BBB- to BBB+</i>	45,193	41,959
<i>Credit rating from BB- to BB+</i>	–	4,258
Corporate bonds	<u>91,681</u>	<u>50,094</u>
Total quoted debt securities	<u>127,059</u>	<u>97,721</u>
Quoted equity instruments		
<i>Credit rating BB</i>	2,817	2,383
Total quoted equity instruments	<u>2,817</u>	<u>2,383</u>
Available-for-sale investment securities	<u><u>129,876</u></u>	<u><u>100,104</u></u>

Government bonds of member countries represent EUR-denominated and USD-denominated securities issued and guaranteed by the Ministries of Finance of these countries, maturing in 2017-2020 (2012: maturing in 2015-2025). The annual coupon rate for these bonds varies from 3.6% to 6.5% (2012: from 3.6% to 5.3%).

Bonds of regional governments represent EUR-denominated bonds issued by the city of Moscow, maturing in 2016 (2012: maturing in 2016). The annual coupon rate for these bonds is 5.1% (2012: 5.1%).

Corporate bonds are represented by the bonds issued by major companies and banks of member countries and EU countries, maturing in 2016-2023 (2012: maturing in 2013-2022). The annual coupon rate for these bonds varies from 2.9% to 7.9% (2012: from 4.3% to 8.5%).

Quoted equity securities are represented by shares of a major Russian company.

9. Held-to-maturity investment securities

As at 31 December 2013, held-to-maturity investment securities included quoted Eurobonds of Corporate Commercial Bank (city of Sofia, Bulgaria) with the carrying amount of EUR 5,910 thousand (2012: no).

10. Long-term loans to banks

In 2013, the Bank changed priorities in its lending policy in terms of institutional and industry orientation and principles of selecting partners and counterparties. The principal lending activity is to facilitate the development of small and medium-sized businesses in the member countries and participate in financing of socially important infrastructure projects in these countries. The Bank considers national development institutes, export and import banks and agencies, international financial organizations and development banks as its key counterparties.

In 2013, the Bank provided long-term loans to banks operating in the following countries:

	<u>2013</u>
Mongolia	23,522
Russian Federation	20,058
Socialist Republic of Vietnam	15,215
Total long-term loans to banks	<u><u>58,795</u></u>

(Thousands of Euros)

10. Long-term loans to banks (continued)

As at 31 December 2013, outstanding long-term loans to banks are neither past due nor impaired, and allowances for impairment of these loans were not made.

Analysis of collateral for long-term loans to banks

The following table provides an analysis of the portfolio of long-term loans to banks by type of collateral as at 31 December 2013:

	<i>2013</i>	
	<i>Long-term loans to banks</i>	<i>Share in the total loans, %</i>
Pledge of real property (mortgage) and title	6,012	10.2
Uncollateralized part of the loans	52,783	89.8
	58,795	100.0

The amounts shown in the table above represent the carrying amount of the portfolio of long-term loans to banks, and do not necessarily represent the fair value of the collateral.

Concentration of long-term loans to banks

As at 31 December 2013, long-term loans to five banks (2012: no) with the total amount of loans to each of them exceeding 10% of total long-term loans to banks were recorded in the Bank's statement of financial position. As at 31 December 2013, the total amount of such major loans was EUR 48,647 thousand.

11. Loans to customers

The Bank issued loans to customers operating in the following countries:

	<i>2013</i>	<i>2012</i>
Mongolia	23,935	23,377
Slovak Republic	7,915	7,465
Republic of Bulgaria	5,775	6,153
Russian Federation	–	91,226
Total loans to customers	37,625	128,221
Less: allowance for loan impairment	–	(79,091)
Loans to customers	37,625	49,130

In December 2013, following the decision of the 100th meeting of the Council, IIB signed the Agreement with the Government of the Republic of Cuba in order to settle reciprocal claims and liabilities. According to the terms of the Agreement, outstanding loans to borrowers in the Republic of Cuba originated during the period of 1985-1990 were fully written off against previously charged allowances.

	<i>2013</i>	<i>2012</i>
Loans to customers in the Republic of Cuba	–	44,117
Less: allowance for loan impairment	–	(44,117)
Loans to customers	–	–

Overdue loans to customers

As at 31 December 2013, there were no overdue loans to customers. As at 31 December 2012, total loans for which the principal and/or interest is overdue amounted to EUR 96,586 thousand. An allowance for impairment of EUR 76,830 thousand was created for overdue loans.

As at 31 December 2013 and 31 December 2012, there were no overdue but not impaired loans.

(Thousands of Euros)

11. Loans to customers (continued)**Allowance for impairment of loans to customers**

A reconciliation of the allowance for loan impairment by country is as follows:

	<i>Russian Federation</i>	<i>Mongolia</i>	<i>Republic of Bulgaria</i>	<i>Total</i>
At 1 January 2013	70,356	5,808	2,927	79,091
Net charge/(reversal) for the year	8,650	131	(3)	8,778
Write off against previously charged allowance upon sale of the debt	(39,629)	(5,010)	–	(44,639)
Write off against previously charged allowance based on the Council's decision	(39,377)	(891)	(2,924)	(43,192)
Change in allowance resulting from changes in exchange rates	–	(38)	–	(38)
At 31 December 2013	–	–	–	–
	<i>Russian Federation</i>	<i>Mongolia</i>	<i>Republic of Bulgaria</i>	<i>Total</i>
At 1 January 2012	69,205	5,526	–	74,731
Net charge for the year	1,553	302	2,927	4,782
Interest accrued on impaired loans	(402)	–	–	(402)
Change in allowance resulting from changes in exchange rates	–	(20)	–	(20)
At 31 December 2012	70,356	5,808	2,927	79,091
Individual impairment	70,356	5,808	2,927	79,091
Gross amount of loans, individually determined to be impaired, before deducting any individually assessed impairment allowance	91,201	11,791	2,927	105,919

Analysis of collateral for loans to customers

The following table provides an analysis of the customer loan portfolio, net of allowance for impairment, by types of collateral as at 31 December 2013 and 31 December 2012:

	2013		2012	
	<i>Loans net of allowance for impairment</i>	<i>Share in the total loans, %</i>	<i>Loans net of allowance for impairment</i>	<i>Share in the total loans, %</i>
Pledge of real property (mortgage) and title	28,006	74.4	30,795	62.7
Pledge of equipment and goods in turnover	–	–	7,118	14.5
Other	–	–	286	0.6
Uncollateralized part of the loans	9,619	25.6	10,931	22.2
Total loans to customers	37,625	100.0	49,130	100.0

The amounts shown in the table above represent the carrying amount of the customer loan portfolio, and do not necessarily represent the fair value of the collateral.

As at 31 December 2013, pledge of real property (mortgage) cost EUR 5,119 thousand was not registered but the surety bank placed a short-term interest-free collateral deposit with IIB prior to the registration of mortgage in Mongolia (Note 16).

As at 31 December 2012, the fair value of collateral taken into account when creating the allowance for impairment was EUR 26,695 thousand.

*(Thousands of Euros)***11. Loans to customers (continued)****Concentration of loans to customers**

As at 31 December 2013, loans to four borrowers (2012: two) with the total amount of loans to each of the two borrowers exceeding 10% of total loans to customers were recorded in the Bank's statement of financial position. As at 31 December 2013, these loans total comprised EUR 37,625 thousand (2012: EUR 38,252 thousand) and no impairment allowances (2012: allowances in the amount of EUR 24,479 thousand) has been made for them.

Analysis of loans to customers by industry

The Bank issued loans to borrowers operating in the following industries:

	<u>2013</u>	<u>2012</u>
Construction of buildings	20,188	52,068
Food and beverage	9,522	24,476
Specialized construction	7,915	7,465
Production, transmission and distribution of electricity, gas and steam	–	22,968
Timber manufacturing	–	10,005
Mining	–	8,922
Rubber and plastic manufacturing	–	1,365
Air transport	–	927
Other	–	25
Total loans to customers	<u>37,625</u>	<u>128,221</u>

12. Assets held for sale

As at 31 December 2012, the Bank recognized assets held for sale in the amount of EUR 10,744 thousand. In June 2012, as a result of repayment of a portion of an impaired loan, the Bank received power equipment. The loan was issued to a borrower operating in the electric power industry. During the annual period, following the receipt of an asset the Bank was active in offering it to its customers but, considering specific characteristics of the equipment and a limited number of potential customers, the annual period was extended. In 2013, the Bank recognized the asset impairment in the amount of EUR 3,588 thousand within "Net (losses)/gains from impairment/disposal of assets held for sale" in the separate income statement, and the decrease in value due to changes in EUR/RUB exchange rate in the amount of EUR 1,171 thousand within "Net (losses)/gains from foreign currencies" in the separate income statement. In December 2013, the asset was sold to an independent customer at its carrying amount.

13. Investment property

In 2013 and 2012, the following changes occurred in the cost of property under operating lease:

	<u>2013</u>	<u>2012</u>
At 1 January	52,409	50,287
Transfers	1,028	–
Inseparable improvements	43	507
Effect of revaluation	–	1,615
Carrying amount at 31 December	<u>53,480</u>	<u>52,409</u>

The Bank rents part of the building under operating lease agreements. In 2013, the Bank's income from lease of investment property amounted to EUR 7,983 thousand (2012: EUR 7,333 thousand).

As at 31 December 2012, the fair value of investment property is determined based on the results of valuation performed on 26 December 2012. The valuation services were performed by an independent firm of professional appraisers which have acknowledged qualification and relevant professional experience in appraising real property of a similar category and in a similar location.

*(Thousands of Euros)***13. Investment property (continued)**

Based on the analysis performed, management believes that the fair value of investment property as at 31 December 2013 does not significantly differ from its carrying amount at that date.

The fair value is determined by reference to market-based evidence. For further details on the fair value of investment property refer to Note 25.

If the investment property was measured using the cost method, the carrying amounts as at 31 December 2013 and 31 December 2012 would be as follows:

	<u>2013</u>	<u>2012</u>
Cost	29,331	29,055
Accumulated depreciation	<u>(10,903)</u>	<u>(10,450)</u>
Net book value	<u>18,428</u>	<u>18,605</u>

The Bank has neither restrictions on the realizability of its investment property nor contractual obligations to purchase, construct or develop investment properties, or to repair, maintain and enhance them.

14. Property and equipment

The movements in property and equipment for the year ended 31 December 2013 were as follows:

	<u>Buildings</u>	<u>Equipment</u>	<u>Computers and software</u>	<u>Office furniture</u>	<u>Vehicles</u>	<u>Total</u>
Cost						
At 1 January 2013	50,354	8,233	3,478	493	583	63,141
Inseparable improvements	72	–	–	–	–	72
Additions	–	113	396	24	181	714
Transfers	(1,028)	–	–	–	–	(1,028)
Disposals	–	(1,022)	(1,016)	(20)	(15)	(2,073)
At 31 December 2013	<u>49,398</u>	<u>7,324</u>	<u>2,858</u>	<u>497</u>	<u>749</u>	<u>60,826</u>
Accumulated depreciation						
At 1 January 2013	–	(7,598)	(3,179)	(357)	(558)	(11,692)
Charge for the year	(757)	(183)	(196)	(19)	(25)	(1,180)
Disposals	–	1,015	994	19	15	2,043
At 31 December 2013	<u>(757)</u>	<u>(6,766)</u>	<u>(2,381)</u>	<u>(357)</u>	<u>(568)</u>	<u>(10,829)</u>
Net book value						
At 31 December 2012	<u>50,354</u>	<u>635</u>	<u>299</u>	<u>136</u>	<u>25</u>	<u>51,449</u>
At 31 December 2013	<u>48,641</u>	<u>558</u>	<u>477</u>	<u>140</u>	<u>181</u>	<u>49,997</u>

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(Thousands of Euros)

14. Property and equipment (continued)

The movements in property and equipment for the year ended 31 December 2012 were as follows:

	<i>Buildings</i>	<i>Equipment</i>	<i>Computers and software</i>	<i>Office furniture</i>	<i>Vehicles</i>	<i>Total</i>
Cost						
At 1 January 2012	48,315	8,013	3,256	496	555	60,635
Inseparable improvements	487	–	–	–	–	487
Additions	–	225	222	20	28	495
Disposals	–	(5)	–	(23)	–	(28)
Accounting for accumulated depreciation at revaluation	(732)	–	–	–	–	(732)
Effect of revaluation	2,284	–	–	–	–	2,284
At 31 December 2012	50,354	8,233	3,478	493	583	63,141
Accumulated depreciation						
At 1 January 2012	–	(7,286)	(2,538)	(355)	(516)	(10,695)
Charge for the year	(732)	(316)	(641)	(18)	(42)	(1,749)
Disposals	–	4	–	16	–	20
Accounting for accumulated depreciation at revaluation	732	–	–	–	–	732
At 31 December 2012	–	(7,598)	(3,179)	(357)	(558)	(11,692)
Net book value						
At 31 December 2011	48,315	727	718	141	39	49,940
At 31 December 2012	50,354	635	299	136	25	51,449

As at 31 December 2013, the cost of fully depreciated property and equipment still used by the Bank was EUR 9,057 thousand (2012: EUR 10,056 thousand).

As at 31 December 2012, the fair value of a group of buildings owned by the Bank is determined based on the results of valuation performed on 26 December 2012. The valuation services were performed by an independent firm of professional appraisers which have acknowledged qualification and relevant professional experience in appraising real property of a similar category and in a similar location.

Based on the analysis performed, management believes that the fair value of a group of buildings as at 31 December 2013 does not significantly differ from its carrying amount at that date.

The fair value is determined by reference to market-based evidence. For further details on the fair value of investment property refer to Note 25.

If the buildings were measured using the cost method, the carrying amounts as at 31 December 2013 and 31 December 2012 would be as follows:

	<i>2013</i>	<i>2012</i>
Cost	28,179	28,123
Accumulated depreciation	(10,459)	(10,022)
Net book value	17,720	18,101

15. Other assets and liabilities

Other assets comprise:

	<i>2013</i>	<i>2012</i>
Other accounts receivable	7,890	492
Advance payments and future period expenses	905	1,026
Property rights to participatory construction objects	–	1,811
	8,795	3,329
Less: allowance for impairment of accounts receivable	(411)	(280)
Other assets	8,384	3,049

(Thousands of Euros)

15. Other assets and liabilities (continued)

The movements in other impairment allowance are as follows:

	<u>2013</u>	<u>2012</u>
Allowance at 1 January	280	119
Net charge for the year	152	161
Change in allowance resulting from changes in exchange rates	(21)	–
Allowance at 31 December	<u>411</u>	<u>280</u>

Other liabilities comprise:

	<u>2013</u>	<u>2012</u>
Other accounts payable	3,911	3,098
Settlements with employees	682	621
Provision for potential VAT payments related to income from leases	–	1,962
Other	551	122
Other liabilities	<u>5,144</u>	<u>5,803</u>

Based on the decision of the Bank's Board, in 2013 a provision for potential VAT payments related to income from leases was reversed since the statute of limitations for the tax inspectorate's claim had expired (Note 22).

16. Due to banks and other financial institutions

Due to banks and other financial institutions comprise:

	<u>2013</u>	<u>2012</u>
Correspondent accounts of banks without rating	1	1
Term deposits of banks:		
<i>Credit rating from BBB- to BBB+</i>	35,021	–
<i>No credit rating</i>	9,445	3,787
Collateral deposit:		
<i>No credit rating</i>	5,119	–
Due to banks and other financial institutions	<u>49,586</u>	<u>3,788</u>

Collateral deposit is provided by a Mongolian surety bank for a short term required to register mortgage in Mongolia (Note 11). Collateral deposit does not assume any accrual of interest expense and is placed by the Bank on the correspondent account with the Mongolian bank without credit rating (Note 5).

Concentration of deposits from banks and other financial institutions

As at 31 December 2013, the Bank has one counterparty accounting for over 20% of the Bank's total deposits from banks and other financial institutions in the amount of EUR 10,001 thousand.

17. Equity**Subscribed and paid-in capital**

The Bank's subscribed capital amounts to EUR 1,300,000 thousand which represents the Bank's equity stated in the Agreement on the Establishment of the International Investment Bank. The Bank's member countries make contributions to the Bank's equity pursuant to their shares stipulated in the Agreement.

As at 31 December 2013, unpaid portion of the Bank's subscribed capital in the amount of EUR 1,058,685 thousand (2012: EUR 1,134,752 thousand) is the amount of contributions by the Bank's member countries which have not been made yet and the amount of unallocated equity contributions totaling EUR 296,900 thousand (2012: EUR 296,900 thousand).

*(Thousands of Euros)***17. Equity (continued)****Subscribed and paid-in capital (continued)**

On 6 June 2013, the 99th regular meeting of the Bank's Council adopted a decision on including a portion of the IIB's retained earnings for the previous years in the amount of EUR 76,067 thousand into the paid-in portion of the Bank's share capital proportionally to the shares of member countries in the paid-in share capital at the date of such decision.

Additionally, during the 99th meeting of the Council member countries supported the need for additional capitalization of the Bank by making additional contributions of at least EUR 100 million to the share capital. Therefore, member countries perform internal statutory procedures required to ensure additional capitalization of the Bank.

In 2012, based on the Council's decision, the Bank's paid-in share capital decreased by EUR 49,247 thousand (shares of the Republic of Poland and the Republic of Hungary). The Bank had no liabilities to the Republic of Poland and the Republic of Hungary, because per Bank's estimates the net assets of the International Investment Bank were negative as of the date the countries applied for withdrawal. Therefore, the Bank deems liabilities to the Republic of Poland and the Republic of Hungary as settled. The shares (quotes) of the Republic of Poland and the Republic of Hungary in the subscribed capital were transferred to equity unallocated between the member countries. And the shares from the Bank's paid-in capital were transferred to retained earnings.

Revaluation reserve for available-for-sale investment securities and revaluation reserve for property and equipment

The movements in the revaluation reserve for available-for-sale investment securities and revaluation reserve for property and equipment were as follows:

	<i>Revaluation reserve for available-for-sale investment securities</i>	<i>Revaluation reserve for property and equipment</i>
At 1 January 2012	(2,351)	31,091
Net unrealized gains on available-for-sale investment securities	10,418	–
Realized gains on available-for-sale investment securities reclassified to the income statement	(3,727)	–
Revaluation of buildings	–	2,284
At 31 December 2012	4,340	33,375
Net unrealized gains on available-for-sale investment securities	1,533	–
Realized gains on available-for-sale investment securities reclassified to the income statement	(5,659)	–
At 31 December 2013	214	33,375

Revaluation reserve for available-for-sale investment securities

The revaluation reserve for available-for-sale investment securities records fair value changes of available-for-sale investments.

Revaluation reserve for property and equipment

The revaluation reserve for property and equipment is used to record increases in the fair value of buildings and decreases to the extent that such decrease relates to an increase on the same asset previously recognized in equity.

*(Thousands of Euros)***18. Contingencies and loan commitments****Legal**

In the ordinary course of business, the Bank is subject to legal actions and complaints. Management believes that the ultimate liability, if any, arising from such actions or complaints will not have a material adverse effect on the financial position or the results of future operations of the Bank. In accordance with the Agreement on the establishment of the Bank, its assets (irrespective of their location) enjoy immunities from any administrative and legal claims.

The Bank takes all necessary legal and other actions to collect the bad debt and to realize respective repossession rights. When the estimated amount of costs resulting from the Bank's further actions to collect bad debt and/or realize respective repossession rights is higher than the amount collected and also when the Bank holds necessary and sufficient documents and/or regulations issued by the governmental authorities, it decides to write off such bad debt against the respective provision.

Insurance

The Bank obtained insurance coverage for a group of buildings, equipment and car park as well as liability insurance against damages caused by operating assets of a hazardous nature. However, the Bank did not obtain insurance coverage related to temporarily discontinued operations or the Bank's obligations to third parties.

Commitments and contingencies

At any time the Bank has outstanding commitments to extend loans. These commitments take the form of approved loan agreements.

As at 31 December, commitments and contingencies of the Bank comprised undrawn loan facilities in the amount of EUR 53,466 thousand (2012: EUR 20,419 thousand). The amounts of commitments assume that amounts will be fully withdrawn.

19. Leases**Bank as lessor**

The Bank provides its real estate for operating leases. As at 31 December 2013, the Bank's non-cancellable operating lease rentals amount to EUR 8,281 thousand (2012: EUR 7,300 thousand) and will be settled within 1 year.

20. Interest income and interest expense

Net interest income comprises:

	<u>2013</u>	<u>2012</u>
Deposits with banks and other financial institutions, including cash and cash equivalents	2,449	1,724
Available-for-sale investment securities and held-to-maturity investment securities	4,362	3,366
Long-term loans to banks	1,013	–
Loans to customers	5,494	3,647
Interest income	<u>13,318</u>	<u>8,737</u>
Due to banks and other financial institutions	(349)	(2)
Current customer accounts	(71)	(30)
Other borrowed funds	(12)	–
Interest expenses	<u>(432)</u>	<u>(32)</u>
Net interest income	<u><u>12,886</u></u>	<u><u>8,705</u></u>

In 2013, interest income accrued on impaired loans to customers amounted to EUR 105 thousand (2012: EUR 1,615 thousand).

*(Thousands of Euros)***21. Net gain/(loss) from foreign currencies**

Net gains less losses from foreign currencies comprise:

	<u>2013</u>	<u>2012</u>
Net (loss)/gain from revaluation of assets and liabilities in foreign currencies	(2,738)	923
Net gain/(loss) from trading in foreign currencies	56	(160)
Net (loss)/gain from foreign currencies	<u>(2,682)</u>	<u>763</u>

22. Other income

The Bank's other income comprised:

	<u>2013</u>	<u>2012</u>
Income from sale of loans	4,837	–
Income from sale of property rights to participatory construction objects	2,835	–
Income from recovery of provision for potential payments (Note 15)	1,764	–
Other	1,314	201
Total other income	<u>10,750</u>	<u>201</u>

23. General and administrative expenses

General and administrative expenses comprise:

	<u>2013</u>	<u>2012</u>
Employee compensations and employment taxes	9,521	7,619
IT-expenses, inventory and occupancy expenses	1,756	1,473
Expenses related to business travel, representative and accommodation expenses	1,281	1,291
Depreciation of property and equipment (Note 14)	1,180	1,749
Consulting and audit expenses	909	466
Other	890	897
General and administrative expenses	<u>15,537</u>	<u>13,495</u>

24. Risk management***Risk management framework***

The Bank's risk management policy is based on the conservative assessments and is mainly aimed at mitigation of adverse impact of risks on the Bank's results, i.e. on the safety and reliability of fund allocation while maintaining the reasonable level of profitability. The prudent assessment assumes that the Bank does not enter into potential transactions with high or undeterminable risk level, regardless of profitability.

The Bank's risk management activities are intended to:

- ▶ identify, analyze and manage risks faced by the Bank;
- ▶ establish ratios and limits that restrict level of the appropriate types of risks;
- ▶ monitor the level of the risk and its compliance with established limits;
- ▶ develop and implement regulative and methodological documents as well as software applications that ensure the professional risk management for the bank transactions.

Risk management policies and procedures are reviewed regularly to reflect changing situation on the financial markets.

(Thousands of Euros)

24. Risk management (continued)

Risk management system

The Bank's Council, the Board, the Asset, Liability and Risk Committee (ALRCO), the Credit Committee and the Risk Management Department are responsible for managing the Bank's risks.

The Bank's Council is responsible for the general control over the risk management system, determines its development strategy and sets strategic limits and risk appetite.

The Board is the executive body of the Bank, which is responsible for compliance with risk management policies and procedures and exercises control over ratios, limits and risk appetite set by the Council. The Board ensures co-operation among all business units and committees of the Bank with regard to risk management.

ALRCO is the Bank's collegial body responsible for development and implementation of the risk management policy in the course of transactions. ALRCO is engaged in ongoing monitoring of liquidity, market and credit risks.

The Credit Committee is the Board's collegial body responsible for lending and assessment of risks arising from all types of credit-related transactions.

Committees meet on a regular basis and provide to the Board their recommendations on how to perform transactions and improve risk management policies and procedures.

The Risk Management Department collects and analyzes information related to all types of bank risks, develops and implements risk management methodology, performs their qualitative and quantitative assessment, prepares recommendations for the Board and committees of the Bank to mitigate risk impact on the Bank's performance.

In 2013, the risk management system was developed through the implementation of Basel standards and best practices of development banks within the Bank:

- ▶ new methodological and regulatory documents relating to risk management have been elaborated. The 100th meeting of the IIB Council approved the new Risk management strategy, strategic limits of the Bank and risk appetite indicators for 2014;
- ▶ a comparative analysis of top rating agencies' requirements to the risk management within the Bank and other IIB institutions has been performed, based on which a target model of the risk management system, map of the most significant risks of the Bank and scheme for allocating functions and powers between risk management items have been developed.

In strict compliance with the existing procedures, twice a year the Bank set limits for counterparties for the purpose of performing financial transactions and assessing their creditworthiness. As part of the lending activity analysis, classes of loan assets risk were continuously monitored and the fair value of pledged items was regularly determined. During the reporting period, the Bank's specialists visited certain borrowers in order to monitor the implementation of the projects and identify potential primary evidence of loans' impairment.

To control and monitor the compliance with limits, the Bank performs daily monitoring of compliance with restrictions set in the list of the Bank's limits applied to transactions on money, currency and equity markets, as well as structural limits included in key risk ratios and stop-loss and take-profit limits. In addition, the Bank's management receives regular reports on the status of risks within the Bank.

Risk identification

The Bank identifies and manages both external and internal risk factors throughout its organizational structure. As a result of regular analysis of the Bank's exposure to different types of risks performed by the Risk Management Department, the Bank identifies factors leading to the increase of the risk level and determines the level of assurance over the current risk mitigation procedures. Apart from the standard credit and market risk analysis, the Risk Management Department monitors financial and non-financial risks influencing the results of banking transactions. Current risks exposures and their projected changes are discussed during the meetings of ALRCO and also communicated to the Management Board along with the recommendations on possible risk mitigation measures.

(Thousands of Euros)

24. Risk management (continued)

Risk assessment, management and control

The Bank's risk exposure is primarily reduced by means of collective decision making. Strict allocation of responsibilities between business units and officers of the Bank, precise description of instructions and procedures and assignment of competencies and powers to departments and their heads are also important risk mitigation factors. Appropriate methodologies are used to assess the risks. Instructions, procedures and methodologies are regularly reviewed and updated by the Bank in order to reflect changed market conditions and improve risk management methods.

The risk monitoring system comprises:

- ▶ Establishing limits to assume risks based on the respective risk assessment;
- ▶ Exercising control over the Bank's exposure by means of compliance with the established limits, regular assessment of the Bank's risk exposure and internal audit of risk management systems.

The Bank identifies the following major risks inherent in its various activities:

- ▶ credit risk;
- ▶ liquidity risk;
- ▶ market risk;
- ▶ operational risk.

Credit risk

Credit risk is the risk that the Bank will incur a loss because its counterparty fails to discharge its contractual financial obligations to the Bank, or discharged them in an untimely fashion or not in full. Credit risk arises principally from loans and advances to customers and other banks and other on and off balance sheet credit exposures. For risk reporting purposes, the Bank considers and consolidates all elements of credit risk exposures such as individual borrower or counterparty default risk.

System of credit risk management

The Bank's regulatory documents establish the following:

- ▶ procedures to review and approve loan/credit applications;
- ▶ methodology for the credit assessment of borrowers, counterparties, issuers and insurance companies;
- ▶ requirements to the credit documentation;
- ▶ procedures for the ongoing monitoring of loans and other credit exposures.

The Credit Committee approves each new loan as well as changes in and amendments to loan agreements. The Credit Department is responsible for ongoing control over the quality of the Bank's loan portfolio.

Upon preparation of a transaction by the initiating unit it is approved by the Credit Committee, and then – the Board. The Board is responsible for all direct credit risk exposures in the amount of up to 15% of the Bank's share capital and for the period of up to 7 years. Direct credit risks exposures exceeding the specified amount or the period of 7 years should be approved by the Bank's Council.

The corporate loan/credit application and appropriate project documents are reviewed by the Credit Department. In case of a positive decision, the set of documents from the Credit Department required for reviewing the loan/credit application shall be analyzed by the Legal Department, Risk Management Department, Security Department, Strategic Planning and Analysis Department, Internal Audit Department and Compliance Control Department. For the purpose of comprehensive analysis of the loan/credit application received from the Credit Department, the Legal Department and Risk Management Department jointly prepare Description of the Investment Transaction. The loan/credit application is subject to review by the Credit Committee based on the Description of the Investment Transaction, report of the Security Department and Strategic Planning and Analysis Department, report on risks of the Risk Management Department and compulsory judgment of the Legal Department in respect of the legal compliance of the proposed transaction. The procedure of making lending decisions comprises the following steps: Step 1 includes reviewing application by the Credit Committee; Step 2 includes making decision by the Board of the Bank (if such issue falls within its competence); Step 3 includes sending a set of respective documents approved by the Board of the Bank to the member countries in order to obtain the final approval from the country of origin of the borrower; Step 4 includes making decision by the Council of the Bank (if such issue falls within its competence).

(Thousands of Euros)

24. Risk management (continued)

Credit risk (continued)

Apart from individual customer analysis, the Risk Management Department assesses the whole loan portfolio with regard to credit concentration and market risks.

To mitigate credit risk, the Bank limits concentrations of exposure to individual customers, counterparties and issuers, groups of related customers, counterparties and issuers as well as by industry and credit rating (for securities). Credit risk management process is based on regular analysis of the creditworthiness the borrowers and their ability to repay interest and principal of debt, and on correspondent limits modification (if necessary).

The Bank continuously monitors the quality of individual credit exposures and regularly reassesses the creditworthiness of its customers. The revaluation is based on the customer's most recent financial statements, past-due status, performance of its business plan and other information submitted by the borrower, or otherwise obtained by the Bank. Based on this information, the borrower's internal credit rating (class of the loan) may be revised and, accordingly, the appropriate loan impairment provision may be created or changed.

Collateral and other credit enhancements

Credit risk is also managed by obtaining pledge of real estate, assets and securities, and other collateral, including corporate and personal guarantees, as well as monitoring availability and value of collateral.

As availability of collateral is important to mitigate credit risk, this factor is a priority for the Bank when reviewing loan/credit applications if their terms and conditions are similar. To ensure recovery of its resources associated with conducting lending and project-financing transactions, the Bank applies the following types of collateral for recovery of loans and fulfillment of obligations:

- ▶ pledge of equipment and goods in turnover;
- ▶ pledge of real property (mortgage) and title;
- ▶ pledge of rights of demand and construction.

Quality of the collateral provided is assessed by the following criteria: safety, adequacy and liquidity. Collateral is not generally held over loans and deposits, except where securities are held as collateral in reverse repurchase agreements.

The Bank assumes that the fair value of the collateral is its value estimate recognized by the Bank to calculate the discounted impairment allowance based on its liquidity and possibility of selling such property in the event of borrower's default considering the time needed for such sale, litigation and other costs. Current market value of the collateral, if necessary, is assessed by accredited appraisers or based on the Bank's internal expert estimate, or carrying amount of the collateral including adjustment coefficient (discount). The Bank's internal expert opinion on the fair value of the collateral and feasibility of the adjustment coefficient (discount), which adjusts the market value, shall be approved/ reconciled with the Risk Management Department. The adjustment coefficient (discount) is established based on the table of recommended discounts "Regulations on lending operations" as at initial measurement of the collateral value. Where the market value of the collateral is assessed as impaired, the clients are usually required to provide additional collateral.

Portfolio of long-term loans to banks and other financial institutions and customers (less allowance for impairment) by type of the Bank's collateral is analyzed in Notes 10 and 11.

Maximum exposure to credit risk

The maximum exposure to credit risk for the components of the separate statement of financial position, including derivatives, before the effect of mitigation through the use of master netting and collateral agreements, is best represented by their carrying amounts.

Where financial instruments are recorded at fair value, the carrying value represents the current credit risk exposure but not the maximum risk exposure that could arise in the future as a result of changes in values.

Analysis of credit risk concentration by customers' industry is presented in Note 11.

Maximum credit risk exposure by credit related commitment represents all the amount of these commitments (Note 18).

(Thousands of Euros)

24. Risk management (continued)**Credit risk (continued)***Derivative financial instruments*

Credit risk arising from derivative financial instruments is, at any time, limited to those with positive fair values, as recorded in the separate statement of financial position.

Credit quality per class of financial assets

The assessment of credit quality of assets is based on the qualitative and quantitative assessment of credit risk.

Deposit contracts with banks and other financial institutions are concluded with counterparties with acceptable credit ratings assigned by such internationally recognized rating agencies as Standard & Poor's, Fitch and Moody's.

Assessment of credit quality of loans is based on a 5 grade system of risk factor categories: standard, sub-standard, doubtful, impaired and uncollectible. The risk factor category is assigned on the basis of the assessment of the client's financial position, payment discipline, credit history, compliance with business plan and production discipline, additional characteristics such as management quality, compliance with other terms and conditions of the loan agreement, strength of positions in the market, competitive potential, administrative resources, industry specifics and country rating.

As at 31 December 2013, there was no evidence of impairment of long-term loans to banks and all such loans were classified as standard. As at 31 December 2012, there were no such loans.

The following table provides information on the credit quality of long-term loans to banks (Note 10) and loans to customers (Note 11) as at 31 December 2013 and 31 December 2012:

<i>2013</i>	<i>Loan amount</i>	<i>Impairment</i>	<i>Loan amount, including impairment</i>	<i>Impairment to loan amount ratio, %</i>
Long-term loans to banks without any signs of impairment identified				
Standard loans				
- <i>Mongolia</i>	23,522	–	23,522	–
- <i>Russian Federation</i>	20,058	–	20,058	–
- <i>Socialist Republic of Vietnam</i>	15,215	–	15,215	–
	58,795	–	58,795	–
Loans to customers without any signs of impairment identified				
Standard loans				
- <i>Mongolia</i>	23,955	–	23,955	–
- <i>Slovak Republic</i>	7,915	–	7,915	–
- <i>Republic of Bulgaria</i>	5,775	–	5,775	–
	37,625	–	37,625	–
Total loans	96,420	–	96,420	–

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(Thousands of Euros)

24. Risk management (continued)**Credit risk (continued)**

2012	Loan amount	Impairment	Loan amount, including impairment	Impairment to loan amount ratio, %
Loans to customers without any signs of impairment identified				
Standard loans				
- Mongolia	11,586	–	11,586	–
- Slovak Republic	7,465	–	7,465	–
- Republic of Bulgaria	3,226	–	3,226	–
- Russian Federation	25	–	25	–
Impaired loans				
Loans not past due				
- Russian Federation	9,332	(2,260)	7,072	24
Loans overdue less than 90 days				
- Mongolia	10,864	(4,881)	5,983	45
Uncollectible loans				
- Russian Federation	81,869	(68,096)	13,773	83
- Republic of Bulgaria	2,927	(2,927)	–	100
- Mongolia	927	(927)	–	100
Total loans	128,221	(79,091)	49,130	62

Where possible, the Bank seeks to restructure loans rather than to take possession of collateral. This may involve extending the payment arrangements and the agreement of new loan conditions. Once the terms have been renegotiated, the loan is no longer considered past due. Renegotiated loans are continuously reviewed to ensure that all criteria are met and that future payments are likely to occur. The loans continue to be subject to an individual impairment assessment, calculated using the loan's original effective interest rate.

Impairment assessment

The Bank creates allowance for loan impairment that represents its estimate of losses incurred in its loan portfolio. The Bank writes off a loan balance against related allowances for loan losses only subject to the approval of the Council and where the loan is determined as uncollectible and when all necessary steps to collect the loan are completed. Such decision is made after consideration of the information on significant changes in the client's financial position such as inability to repay the loan, and when proceedings from disposal of the collateral are insufficient to cover the debt amount in full.

Individually assessed allowances

The Bank determines the allowances appropriate for each individually significant loan on an individual basis. Due to a limited number of borrowers, the Bank considers each loan as individually significant. Items considered when determining allowance amounts include the sustainability of the counterparty's business plan, its ability to improve performance once a financial difficulty has arisen, projected receipts and the expected payout should bankruptcy ensue, the availability of financial support, the realizable value of collateral, and the timing of the expected cash flows. The impairment losses are evaluated at each reporting date, unless unforeseen circumstances require more careful attention.

For uncollectible financial assets, the Bank makes allowance in the amount equal to 100% of the amount of a financial asset.

The total amount of impairment allowance is approved by the Credit Committee on a monthly basis.

(Thousands of Euros)

24. Risk management (continued)

Liquidity risk

Liquidity risk is the risk of loss resulting from the Bank's inability to meet its payment obligations in full when they fall due under normal and stress circumstances. Liquidity risk results from improper balance between the Bank's financial assets and financial liabilities by period and amount (including due to untimely discharge of its financial obligations by one or several counterparties of the Bank) and/or an unforeseen need of immediate and simultaneous discharge of its financial obligations.

The Bank's approach to management of liquidity is to ensure, as far as possible, that it will always have sufficient liquidity to meet its obligations when due, under both normal and stressed conditions, without incurring unacceptable losses or taking risk of damage to the Bank's reputation.

In the course of liquidity management the Bank's management relies on the following principles:

- ▶ liquidity has priority over return;
- ▶ continuous liquidity management;
- ▶ distribution of authorities between management bodies and divisions;
- ▶ planning and limitation of liquidity consistent with the size, nature of business and financial position of the Bank;
- ▶ forecasting of cash flows.

Liquidity risk is managed to ensure the Bank's ability to meet its financial obligations in full and on a timely basis. For this purpose the Bank:

- ▶ determines an acceptable liquidity level;
- ▶ continuously monitors liquidity;
- ▶ takes measures to maintain liquidity at the acceptable level;
- ▶ in case of liquidity crisis performs a set of procedures for its recovery.

The Bank manages its liquidity in two areas: the Treasury Department manages the liquidity, and Risk Management Department performs control over liquidity risk.

The Treasury Department receives on a weekly basis information from business units regarding the liquidity profile of their financial assets and liabilities and forecasts of projected cash flows arising from projected future business. Further, the Treasury Department manages the Bank's liquidity in accordance with the existing regulatory documents of the Bank and ALRCO's decisions.

The Risk Management Department performs control on a weekly basis over actual values of the current and overall liquidity and compares these values with standards. In case of non-compliance of these standards, the Risk Management Department immediately notifies ALRCO about it in order to develop and perform activities for recovering liquidity.

Due to the fact that all the Bank's significant liabilities are short-term with maturity of up to 1 year, the Bank does not estimate contractual undiscounted liabilities' cash flows since the expected cash outflow will not be significantly different from the carrying amount of the Bank's financial liabilities as at 31 December 2013 and 31 December 2012.

The table below shows the contractual expiry by maturity of the Bank's off-balance credit-related commitments. Each undrawn loan commitment is included in the time band containing the earliest date it can be drawn down.

(Thousands of Euros)

24. Risk management (continued)**Liquidity risk (continued)**

The following table provides an analysis of assets and liabilities on the basis of the remaining period from the reporting date to the contractual maturity date:

	2013						2012						Past due	Total	
	Less than 1 month	1 to 3 months	3 months to 1 year	Over 1 to 5 years	Over 5 years	No stated maturity	Total	Less than 1 month	1 to 3 months	3 months to 1 year	Over 1 to 5 years	Over 5 years			No stated maturity
Assets:															
Cash and cash equivalents	19,272	–	–	–	–	–	19,272	8,392	–	–	–	–	–	–	8,392
Deposits with banks and other financial institutions	–	23,112	16,015	–	–	–	39,127	12,877	53,845	25,085	–	–	–	–	91,807
Financial assets at fair value through profit or loss	–	97	54	–	–	–	151	–	–	–	–	–	–	–	–
Available-for-sale investment securities	150	674	1,754	44,061	80,420	2,817	129,876	–	830	2,091	42,048	52,752	2,383	–	100,104
Held-to-maturity investment securities	117	–	5,793	–	–	–	5,910	–	–	–	–	–	–	–	–
Long-term loans to banks	–	374	2,014	56,407	–	–	58,795	–	–	–	–	–	–	–	–
Loans to customers	–	430	7,832	27,463	1,900	–	37,625	–	1,026	7,125	10,573	10,650	–	19,756	49,130
Other assets	180	4,508	2,791	–	–	–	7,479	1,053	6	178	–	–	–	–	1,237
Total assets	19,719	29,195	36,253	127,931	82,320	2,817	298,235	22,322	55,707	34,479	52,621	63,402	2,383	19,756	250,670
Liabilities:															
Due to banks and other financial institutions	(24,566)	(25,020)	–	–	–	–	(49,586)	(3,788)	–	–	–	–	–	–	(3,788)
Current customer accounts	(3,313)	–	–	–	–	–	(3,313)	(2,396)	–	–	–	–	–	–	(2,396)
Other liabilities	(434)	(2,540)	(1,619)	–	–	–	(4,593)	(2,418)	(215)	(3,170)	–	–	–	–	(5,803)
Total liabilities	(28,313)	(27,560)	(1,619)	–	–	–	(57,492)	(8,602)	(215)	(3,170)	–	–	–	–	(11,987)
Net position	(8,594)	1,635	34,634	127,931	82,320	2,817	240,743	13,720	55,492	31,309	52,621	63,402	2,383	19,756	238,683
Accumulated net position	(8,594)	(6,959)	27,675	155,606	237,926	240,743		13,720	69,212	100,521	153,142	216,544	218,927	238,683	
Off-balance credit-related commitments	–	(48,466)	(5,000)	–	–	–	(53,466)	–	(2,997)	(17,422)	–	–	–	–	(20,419)

The accumulated negative liquidity gap in the periods of “less than 1 month” and “1 to 3 months” can be offset with high liquid available for sale investment securities, that can be realized at any moment on market terms. If it is necessary the gained liquid assets can be used to meet the short term liabilities of the Bank.

(Thousands of Euros)

24. Risk management (continued)

Market risk

Market risk is the risk that the Bank shall incur losses due to adverse fluctuations in market rate of financial instruments, interest rates, foreign exchanges, and securities' prices. Market risk includes equity risk on securities, interest rate risk and currency risk.

The Bank is exposed to market risk due to open positions in currency. Equity risk on securities arises from open positions in debt and equity instruments, which are exposed to general and specific market changes.

The Board of the Bank performs overall management of market risk.

ALRCO, led by the Deputy Chairman of the Bank's Management Board, coordinates the Bank's market risk management policy, considers and provides to the Management Board recommendations on management of market risks, as well as assets and liabilities.

The Treasury Department performs operative management of market risks. The Risk Management Department performs the assessment of equity and currency risks exposure. The Treasury Department manages open positions within the established limits in order to increase the Bank's income on a daily basis.

Currency risk and price risk

Currency risk is the risk of loss resulting from adverse changes in exchange rates with respect to the Bank's open positions in foreign currencies. Price risk is the risk that the fair values of securities decrease as the result of changes in the levels of indices and the value of individual securities.

The Bank applies a VaR methodology to assess currency and equity risks. VaR is a method used in measuring maximum risk of the Bank, i.e. the level of losses on a certain position in relation to a financial instrument/currency/precious metals or a portfolio, which shall not be exceeded at a given confidence level and over a specified time horizon.

The Bank uses an assumption that the accuracy of assessment of maximum value at risk (confidence level) is 99%, and the time horizon is 10 days. The assessment of value at risk in relation to currency position of the Bank is carried out in major currencies and financial instruments of the Bank attributable to a securities portfolio.

At estimating value at risk, the Bank uses a parameter method, which allows assessing the volatility of yield on the basis of the most current market data.

The choice of a respective approach to value at risk estimation is made on the basis of data on statistical analysis of changes in fair values of financial instruments and exchange rates.

Selection period used by the Bank for modeling purposes depends on types of instruments: 250 days for currency and securities. In order to monitor the accuracy of assessment of above mentioned risks, the Bank carries out regular testing (back-testing) based on historical data, which allows evaluating the compliance of risk assessment model with the actual market situation.

As at 31 December 2013 and 31 December 2012, final data on value at risk assessment in relation to currency and price risks assumed by the Bank are represented as follows:

	<u>2013</u>	<u>2012</u>
Fixed income securities price risk	2,174	1,520
Equity securities price risk	335	414
Currency risk	1,211	1,259

Despite measurement of value at risk is a standard industry method for risk assessment, this method has a number of limitations:

- ▶ Analysis based on value at risk assessment is correct in case current market conditions remain unchanged. Using historical data for assessment of future events are not taken into account.
- ▶ Assessment of value at risk is sensitive to market liquidity in relation to a particular financial instrument, and the lack of liquidity may lead to biased volatility data.
- ▶ If a confidence level of 99% is used, losses exceeding the confidence range are not taken into account.
- ▶ 10-day time horizon implies the entire Bank's position over this period could have been closed or hedged. Results of value at risk assessment may be incorrect in case of market liquidity deterioration.
- ▶ Fluctuations that may occur in the course of the day are not taken into account at calculating value at risk on the basis of the results of a business day.

*(Thousands of Euros)***24. Risk management (continued)****Market risk (continued)**

The Bank's exposure to currency risk as at 31 December 2013 and 31 December 2012 is presented below:

	2013					2012				
	EUR	USD	RUB	Other currencies	Total	EUR	USD	RUB	Other currencies	Total
Assets:										
Cash and cash equivalents	9,222	331	4,397	5,322	19,272	1,010	1,321	5,929	132	8,392
Deposits with banks and other financial institutions	23,112	16,015	–	–	39,127	91,807	–	–	–	91,807
Available-for-sale investment securities	102,911	22,940	4,025	–	129,876	77,961	22,143	–	–	100,104
Held-to-maturity investment securities	–	5,910	–	–	5,910	–	–	–	–	–
Long-term loans to banks	41,285	17,510	–	–	58,795	–	–	–	–	–
Loans to customers	37,625	–	–	–	37,625	49,105	–	25	–	49,130
Other assets	12	–	7,467	–	7,479	332	173	732	–	1,237
	214,167	62,706	15,889	5,322	298,084	220,215	23,637	6,686	132	250,670
Liabilities:										
Due to banks and other financial institutions	(19,035)	(25,432)	–	(5,119)	(49,586)	–	(3,788)	–	–	(3,788)
Current customer accounts	(3,162)	(151)	–	–	(3,313)	(2,247)	(149)	–	–	(2,396)
Other liabilities	(2,513)	(187)	(1,853)	(40)	(4,593)	(2,033)	(275)	(3,495)	–	(5,803)
	(24,710)	(25,770)	(1,853)	(5,159)	(57,492)	(4,280)	(4,212)	(3,495)	–	(11,987)
Net balance sheet position	189,457	36,936	14,036	163	240,592	215,935	19,425	3,191	132	238,683
Derivative financial instruments										
Receivable	14,400	–	–	–	14,400	–	–	–	–	–
Payable	–	(14,249)	–	–	(14,249)	–	–	–	–	–
Net balance sheet position including derivative financial instruments	203,857	22,687	14,036	163	240,743	215,935	19,425	3,191	132	238,683

*(Thousands of Euros)***24. Risk management (continued)****Market risk (continued)*****Interest rate risk***

The Bank is exposed to the effects of fluctuations in the prevailing levels of market interest rates in its financial position and cash flows. Interest margins may increase as a result of such changes but may also reduce or create losses in the event that unexpected movements arise.

Sensitivity analysis of the Bank's equity to changes in interest rate (based on simplified scenario of a 100 basis point (bp) and positions of available-for-sale debt securities parallel fall or rise in all yield curves as at 31 December 2013 and 31 December 2012) is as follows:

	<u>31 December 2013</u>	<u>31 December 2012</u>
	<u>The Bank's equity</u>	<u>The Bank's equity</u>
100 bp parallel rise	(6,342)	(5,085)
100 bp parallel fall	6,342	5,085

Operational risk

Operational risk is a risk of loss arising from inadequate management and control procedures, fraud, inconsistent business solutions, system failures due to human errors and abuse of power, technical deficiencies, calculation errors, disasters and misuse of the Bank's property.

Generally, the Board controls the risk management process as well as compliance with internal policies, approves internal regulations relating to risk management, establishes operational risks monitoring limits and allocates duties relating to operational risk management among various agencies.

The Risk Management Department controls and monitors operational risks and provides respective reporting to the Board. The current control enables to timely identify and eliminate deficiencies in policies and procedures aimed at operational risk management, as well as to cut the possibility and amount of related losses. The Bank continuously seeks to enhance its business processes, operating structure and personnel incentives system in order to minimize the impact of operational risk.

25. Fair values of financial instruments

Fair value is the amount at which a financial instrument could be exchanged in a current transaction between willing parties, other than in a forced sale or liquidation, and is best evidenced by a quoted market price.

The estimated fair values of financial instruments have been determined by the Bank using available market information, where it exists, and appropriate valuation methodologies. However, judgment is necessarily required to interpret market data to determine the estimated fair value. While Management has used available market information in estimating the fair value of financial instruments, the market information may not be fully reflective of the value that could be realized in the current circumstances.

Fair value hierarchy

The Bank uses the following hierarchy for determining and disclosing the fair value of financial instruments by valuation technique:

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

(Thousands of Euros)

25. Fair value hierarchy (continued)**Fair value hierarchy (continued)**

For the purpose of fair value disclosures, the Bank has determined classes of assets and liabilities on the basis of their nature, characteristics and risks of the asset or liability and the level of the fair value hierarchy.

	<i>Valuation date</i>	<i>Level 1 2013</i>	<i>Level 2 2013</i>	<i>Level 3 2013</i>	<i>Total 2013</i>
Assets measured at fair value					
Derivative financial assets	31 December 2013	–	151	–	151
Government bonds of member countries and bonds of regional governments	31 December 2013	35,378	–	–	35,378
Corporate bonds	31 December 2013	91,681	–	–	91,681
Quoted equity instruments	31 December 2013	2,817	–	–	2,817
Investment property	31 December 2013	–	–	53,480	53,480
Property and equipment	31 December 2013	–	–	49,997	49,997
Assets for which fair values are disclosed					
Cash and cash equivalents	31 December 2013	–	–	19,272	19,272
Deposits with banks and other financial institutions	31 December 2013	–	–	39,127	39,127
Held-to-maturity investment securities	31 December 2013	5,928	–	–	5,928
Long-term loans to banks	31 December 2013	–	–	58,795	58,795
Loans to customers	31 December 2013	–	–	37,625	37,625
Liabilities for which fair values are disclosed					
Due to banks and other financial institutions	31 December 2013	–	–	49,586	49,586
Current customer accounts	31 December 2013	–	–	3,313	3,313

The following table shows an analysis of financial instruments recorded at fair value by level of the fair value hierarchy as at 31 December 2012:

	<i>Valuation date</i>	<i>Level 1 2012</i>	<i>Level 2 2012</i>	<i>Level 3 2012</i>	<i>Total 2012</i>
Financial assets					
Available-for-sale investment securities	31 December 2012	98,936	1,168	–	100,104

Fair value of financial assets and liabilities not recorded at fair value

Set out below is a comparison of the carrying amounts and fair values of the Bank's financial instruments that are carried in the separate financial statements. The table does not include the fair values of non-financial assets and non-financial liabilities.

	<i>Carrying amount 2013</i>	<i>Fair value 2013</i>	<i>Unrecognized gain/(loss) 2013</i>	<i>Carrying amount 2012</i>	<i>Fair value 2012</i>	<i>Unrecognized gain/(loss) 2012</i>
Financial assets						
Cash and cash equivalents	19,272	19,272	–	8,392	8,392	–
Deposits with banks and other financial institutions	39,127	39,127	–	91,807	91,807	–
Financial assets at fair value through profit or loss	151	151	–	–	–	–
Held-to-maturity investment securities	5,910	5,928	18	–	–	–
Long-term loans to banks	58,795	58,795	–	–	–	–
Loans to customers	37,625	37,625	–	49,130	48,062	(1,068)
Financial liabilities						
Due to banks and other financial institutions	49,586	49,586	–	3,788	3,788	–
Current customer accounts	3,313	3,313	–	2,396	2,396	–
Total unrecognized change in fair value			18			(1,068)

(Thousands of Euros)

25. Fair values of financial instruments (continued)

Methodologies and assumptions

The following describes the methodologies and assumptions used to determine fair values of those financial instruments which are not recorded at fair value in these financial statements.

Assets for which fair value approximates carrying amount

For financial assets and financial liabilities that are liquid or having a short term maturity (less than three months) it is assumed that the carrying amounts approximate their fair value.

Cash and cash equivalents, deposits with banks and other financial institutions

Management has estimated that at 31 December 2013 and 31 December 2012 the fair value of deposits with banks and other financial institutions and cash and cash equivalents was not significantly different from their respective carrying amount. This is due to the fact that it is practice to renegotiate interest rates to reflect current market conditions and, therefore, a majority of balances carry interest at rates approximating market interest rates.

Fixed rate financial instruments

The fair value of fixed rate financial assets and liabilities carried at amortized cost is estimated by comparing market interest rates at their initial recognition with current market rates offered for similar financial instruments.

The estimated fair value of fixed interest bearing long-term loans to banks, loans to customers, and deposits in banks is based on discounted cash flows using prevailing money-market interest rates for debts with similar credit risk and maturity. Management has estimated that at 31 December 2013 the fair value of long-term loans to banks and loans to customers was not significantly different from their respective carrying amount.

26. Segment information

For management purposes, the Bank identifies the following three operating segments based on its lines of services:

Credit investment activity	Credit investment banking services include long-term corporate and interbank financing
Treasury	Operations in financial markets, transactions with securities, derivative financial instruments, foreign currency and liquidity management
Other operations	Operational leasing services, Legal Department activities on credit portfolio rehabilitation, other operations

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(Thousands of Euros)

26. Segment information (continued)

Management monitors the operating results of its business units separately for the purpose of making decisions about resource allocation and performance assessment. Segment performance, as explained in the table below, is measured differently from profit or loss in the separate financial statements. The following table presents revenue, profit, assets and liabilities of the Bank's operating segments:

<i>2013</i>	<i>Credit investment activity</i>	<i>Treasury</i>	<i>Other operations</i>	<i>Total</i>
Income				
External customers				
Interest income	6,507	6,811	–	13,318
Net gains from trading in foreign currencies	–	56	–	56
Net gains from available-for-sale investment securities	–	5,659	–	5,659
Income from lease of investment property	–	–	7,983	7,983
Net (losses)/gains from impairment/disposal of assets held for sale	–	–	(3,588)	(3,588)
Other segment income	–	362	7,672	8,034
Total income	6,507	12,888	12,067	31,462
Interest expenses	–	(432)	–	(432)
Allowance for loans impairment	(8,778)	–	–	(8,778)
Segment performance results	(2,271)	12,456	12,067	22,252
Other unallocated income				3,192
Other unallocated expense				(20,680)
				4,764
Profit for the year				
Segment assets	101,539	189,217	123,022	413,778
Segment liabilities	5,119	44,467	8,457	58,043
Other segment information				
Capital expenditures	–	–	115	115
<i>2012</i>	<i>Credit investment activity</i>	<i>Treasury</i>	<i>Other operations</i>	<i>Total</i>
Income				
External customers				
Interest income	3,647	5,090	–	8,737
Net losses from trading in foreign currencies	–	(160)	–	(160)
Net gains from available-for-sale investment securities	–	3,727	–	3,727
Income from lease of investment property	–	–	7,333	7,333
Net (losses)/gains from impairment/disposal of assets held for sale	75	–	–	75
Other segment income	–	182	–	182
Total income	3,722	8,839	7,333	19,894
Interest expenses	–	(32)	–	(32)
Allowance for loan impairment	(4,782)	–	–	(4,782)
Segment performance results	(1,060)	8,807	7,333	15,080
Other unallocated income				2,977
Other unallocated expense				(15,067)
				2,990
Profit for the year				
Segment assets	49,130	200,303	117,651	367,084
Segment liabilities	–	3,788	8,199	11,987
Other segment information				
Capital expenditures	–	–	994	994

*(Thousands of Euros)***26. Segment information (continued)**

In 2013 and 2012 the Bank had one counterparty with lease operations revenue exceeding 10% of total Bank's revenue (2013: EUR 5,473 thousand; 2012: EUR 5,026 thousand).

Geographical information

Allocation of the Bank's revenue from transactions with external customers and non-current assets based on the location of these customers and assets as at 31 December 2013 and 31 December 2012 and for the years then ended is presented in the tables below:

	2013				2012			
	<i>Russia</i>	<i>Other member countries</i>	<i>Other countries</i>	<i>Total</i>	<i>Russia</i>	<i>Other member countries</i>	<i>Other countries</i>	<i>Total</i>
Interest income	5,378	7,098	842	13,318	3,492	4,497	748	8,737
Income from lease of investment property	7,983	–	–	7,983	7,333	–	–	7,333
Non-current assets	103,477	–	–	103,477	103,858	–	–	103,858

Non-current assets include property and equipment and investment property.

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(Thousands of Euros)

26. Segment information (continued)**Geographical information (continued)**

The geographical concentration of the Bank's financial assets and liabilities as at 31 December 2013 and 31 December 2012 is presented below:

	<i>2013</i>									
	<i>Russian Federation</i>	<i>Republic of Bulgaria</i>	<i>Romania</i>	<i>Slovak Republic</i>	<i>Republic of Cuba</i>	<i>Mongolia</i>	<i>Socialist Republic of Vietnam</i>	<i>Czech Republic</i>	<i>Other countries</i>	<i>Total</i>
Assets:										
Cash and cash equivalents	4,667	–	–	6,500	–	5,119	–	–	2,986	19,272
Deposits with banks and other financial institutions	23,112	–	–	–	–	16,015	–	–	–	39,127
Financial instruments at fair value through profit or loss	–	–	–	–	–	–	–	–	151	151
Investment securities:										
- available-for-sale	61,673	7,712	12,324	–	–	1,679	–	–	46,488	129,876
- held-to-maturity	–	5,910	–	–	–	–	–	–	–	5,910
Long-term loans to banks less allowances for impairment	20,058	–	–	–	–	23,522	15,215	–	–	58,795
Loans to customers less allowances for impairment	–	5,775	–	7,915	–	23,935	–	–	–	37,625
Assets	109,510	19,397	12,324	14,415	–	70,270	15,215	–	49,625	290,756
Liabilities:										
Due to banks and other financial institutions	35,021	9,446	–	–	–	5,119	–	–	–	49,586
Liabilities	35,021	9,446	–	–	–	5,119	–	–	–	49,586

(Thousands of Euros)

26. Segment information (continued)**Geographical information (continued)**

	2012									
	<i>Russian Federation</i>	<i>Czech Republic</i>	<i>Republic of Bulgaria</i>	<i>Romania</i>	<i>Slovak Republic</i>	<i>Republic of Cuba</i>	<i>Mongolia</i>	<i>Socialist Republic of Vietnam</i>	<i>Other countries</i>	<i>Total</i>
Assets:										
Cash and cash equivalents	6,058	–	–	–	–	–	–	–	2,334	8,392
Deposits with banks and other financial institutions	37,962	–	15,033	–	10,018	–	18,759	–	10,035	91,807
Available-for-sale investment securities	49,317	15,078	3,326	10,915	12,267	–	1,168	–	8,033	100,104
Loans to customers less allowances for impairment	20,870	–	3,226	–	7,465	–	17,569	–	–	49,130
Assets	114,207	15,078	21,585	10,915	29,750	–	37,496	–	20,402	249,433
Liabilities:										
Due to banks and other financial institutions	–	–	3,788	–	–	–	–	–	–	3,788
Liabilities	–	–	3,788	–	–	–	–	–	–	3,788

Other countries include members of the Organization for Economic Development (OECD).

(Thousands of Euros)

27. Offsetting of financial instruments

The table below shows financial assets offset against financial liabilities in the separate statement of financial position, as at 31 December 2013 as well as the effect of enforceable master netting agreements and similar arrangements that do not result in an offset in the separate statement of financial position:

2013	Gross amount of recognized financial assets	Gross amount of recognized financial liabilities set off in the statement of financial position	Net amount of financial assets presented in the statement of financial position	Related amounts not set off in the statement of financial position Cash collateral received	Net amount
Financial assets					
Cash and cash equivalents	19,272	–	19,272	(5,119)	14,153
Total	19,272	–	19,272	(5,119)	14,153
Financial liabilities					
Due to banks and other financial institutions	49,586	–	49,586	(5,119)	44,467
Total	49,586	–	49,586	(5,119)	44,467

There was no financial assets offset against financial liabilities in the separate statement of financial position, as at 31 December 2012 as well as the effect of enforceable master netting agreements and similar arrangements that do not result in an offset in the separate statement of financial position.

28. Related party disclosures

Parties are considered to be related if one party has the ability to control the other party or exercise significant influence over the other party in making financial or operational decisions as defined by IAS 24 *Related Party Disclosures*. In considering each possible related party relationship, attention is directed to the substance of the relationship, not merely the legal form.

Transactions and settlements with related parties were carried out on conditions similar to those, which prevail in transactions between independent parties.

The volumes of related party transactions, outstanding balances at the year end, and related expense and income for 2013 and 2012 are as follows:

Related party	31 December 2013		31 December 2012		
	Carrying amount	Average interest rate, %	Carrying amount	Average interest rate, %	
Separate statement of financial position					
Loans to customers	Subsidiary	–	–	25	8.3
Other liabilities	Key management personnel	120	–	75	1.5

(Thousands of Euros)

28. Related party disclosures (continued)

		<u>2013</u>	<u>2012</u>
	<i>Related party</i>	<i>Income/(expense)</i>	<i>Income/(expense)</i>
<i>Separate income statement</i>			
Interest income on loans to customers	Subsidiary	4	47
Interest expense on current customer accounts	Key management personnel	(14)	(6)
Net interest (expense)/income after allowance for loans impairment		<u>(10)</u>	<u>41</u>
Income from lease of investment property	Subsidiary	7	2
Net non-interest income		<u>7</u>	<u>2</u>
Operating gains/(losses)		<u><u>(3)</u></u>	<u><u>43</u></u>
Employee benefits	Key management personnel	(1,134)	(744)
Compensation for travel expenses and medical insurance	Key management personnel	(84)	(106)
Operating expenses		<u>(1,221)</u>	<u>(850)</u>
Net losses for the year		<u><u>(1,221)</u></u>	<u><u>(807)</u></u>

29. Capital adequacy

Capital adequacy ratio is the most important financial indicator characterizing credibility of the credit institutions and is estimated as ratio of capital base to risk weighted assets expressed as a percentage. Approval of the capital adequacy ratio is the sole power of the Bank's Council.

The Basel Committee on Banking Regulations recommends maintaining the ratio of capital to risk weighted assets ("statutory capital ratio") above the prescribed minimum level. As at 31 December 2013, this minimum level was 8% (2012: 8%).

Besides, taking into account the Bank's status as the multilateral development institution and the structure of the Bank's member countries and respective decision of the Council, the capital adequacy ratio was set at the level of not less than 25% as of 31 December 2013 (2012: 25%).

From 2013 the Bank monitors the capital adequacy ratio, computed in accordance with the Basel Capital Accord (commonly known as Basel II) as defined in the International Convergence of Capital Measurement and Capital Standards and Amendment to the Capital Accord to incorporate market risks.

The following table shows the composition of the Bank's capital position computed in accordance with the Basel Accord (Basel II), as of 31 December 2013 and 31 December 2012.

	<u>31 December 2013</u>	<u>31 December 2012</u>
Capital:		
Tier 1 capital	306,221	314,392
Tier 2 capital	33,589	37,714
Total regulatory capital	<u>339,810</u>	<u>352,106</u>
Risk-weighted assets:		
<i>Credit risk</i>	156,151	140,782
<i>Market risk</i>	114,548	93,210
<i>Operational risk</i>	59,016	116,492
Total risk-weighted assets	<u><u>329,715</u></u>	<u><u>350,484</u></u>
Total capital expressed as a percentage of risk-weighted assets, % ("capital adequacy ratio")	103.06%	100.46%
Total tier 1 capital expressed as a percentage of risk-weighted assets, % ("tier 1 capital ratio")	92.87%	89.70%

(Thousands of Euros)

30. Subsequent events

On 27 February 2014 Government of the Slovak Republic was the first among the member countries of the International Investment Bank to fulfill its obligations over additional capitalization of the bank. EUR 6,294 thousand were transferred to the Bank's accounts against Slovak additional contribution to the Bank's share capital. As a result, the paid-in capital of International Investment Bank amounted to EUR 247,609 thousand with increase of Slovak share to 8.67%.

(The end).