

**European Bank
for Reconstruction and Development**

The Balkan Region Special Fund

**Annual Financial Report
31 December 2006**

European Bank for Reconstruction and Development

The Balkan Region Special Fund

Contents

Income statement	1
Balance sheet	1
Statement of cash flows	2
Statement of changes in contributors' resources	2
Notes to the financial statements	3 - 10
Independent auditors' report	11 - 12

The Balkan Region Special Fund

Income statement		Year to	
For the year ended 31 December 2006		31 December 2006	31 December 2005
	Note	€000	€000
Interest and similar income		223	196
Fee income		39	81
Foreign exchange (loss)/gain		(2)	2
Disbursements for technical cooperation	4,7	(159)	(262)
Other operating expenses	5,7	(7)	(28)
Net income refunded on termination of contribution agreements	6	(107)	(377)
Net loss for the year		(13)	(388)

Balance sheet		31 December		Restated
At 31 December 2006		2006		31 December
	Note	€000	€000	2005
				€000
Assets				
Placements with credit institutions			8,015	8,299
Other assets	8		588	451
Total assets			8,603	8,750
Liabilities and contributors' resources				
Other liabilities	9		1,399	315
Contributors' resources				
Contributions	10	9,779		10,997
Reserves and retained earnings		(2,575)		(2,562)
Total contributors' resources			7,204	8,435
Total liabilities			8,603	8,750

The Balkan Region Special Fund

Statement of cash flows For the year ended 31 December 2006	Year to 31 December 2006 €000	Year to 31 December 2005 €000
Cash flows from operating activities		
Operating loss for the year	(13)	(388)
Adjustment for:		
Foreign exchange	2	(2)
Operating loss before changes in operating assets	(11)	(390)
Increase in operating assets:		
Interest receivable	(24)	(1)
Advances	(80)	-
Fee income receivable	(33)	(81)
Increase/(decrease) in operating liabilities:		
Accrued expenses	1,084	(154)
Net cash from/(used in) operating activities	936	(626)
Cash flows from financing activities		
Contributions received	-	423
Contributions refunded on termination of a contribution agreement	(1,218)	(1,952)
Net cash used in financing activities	(1,218)	(1,529)
Net decrease in cash and cash equivalents	(282)	(2,155)
Cash and cash equivalents at beginning of year	8,299	10,452
Effect of foreign exchange rate changes	(2)	2
Cash and cash equivalents at 31 December	8,015	8,299

Statement of changes in contributors' resources

For the year ended 31 December 2006	Contributions €000	Accumulated loss €000	Total €000
At 31 December 2004	12,766	(2,174)	10,592
Contribution agreement	423	-	423
Termination of contribution agreement	(2,192)	-	(2,192)
Loss for the year	-	(388)	(388)
At 31 December 2005	10,997	(2,562)	8,435
Termination of contribution agreement	(1,218)	-	(1,218)
Loss for the year	-	(13)	(13)
At 31 December 2006	9,779	(2,575)	7,204

The Balkan Region Special Fund

Notes to the financial statements

1 Creation of the Special Fund

The creation of The Balkan Region Special Fund ("the Fund") was approved by the Board of Directors ("the Board") of the European Bank for Reconstruction and Development ("the Bank") on 15 September 1999 and is administered, *inter alia*, under the terms of Rules and Regulations of such Special Fund approved by the Board on that date. The Fund became operational on 7 December 1999 following the signing of the first contribution agreement.

The Fund was established in accordance with Article 18 of the Agreement Establishing the Bank. The objective of the Fund is to assist the reconstruction of Albania, Former Yugoslav Republic of Macedonia, Croatia, Bosnia and Herzegovina, Bulgaria and Romania (the "Balkan Countries"), through the Bank's Balkan Region Action Plan. The Action Plan was extended in 2001 to cover projects in Serbia and Montenegro, when it became a recipient member country of the Bank. Activities of the Fund may include investments and technical cooperation.

At 31 December 2006, the Fund had two project sub-accounts: a Trade Facilitation sub-account and a Technical Cooperation sub-account.

2 President's responsibilities

The President of the Bank is responsible for preparing the financial statements in accordance with International Financial Reporting Standards issued by the International Accounting Standards Board and the overall principles of the European Community's Council Directive on Annual Accounts and Consolidated Accounts of Banks and Other Financial Institutions.

3 Accounting policies

The principal accounting policies applied in the preparation of these financial statements are set out below. These policies have been consistently applied to all the years presented, unless otherwise stated.

i Basis of preparation

These financial statements have been prepared in accordance with International Financial Reporting Standards (IFRS) as issued by the International Accounting Standards Board (IASB) and the overall principles of the European Community's Council Directive on Annual Accounts and Consolidated Accounts of Banks and Other Financial Institutions. The financial statements have been prepared under the historical cost convention.

ii Significant changes in the financial statements

Amendments to published standards effective in 2006

IAS 39 and IFRS 4 (Amendment), Financial Guarantee Contracts

This amendment requires issued financial guarantees to be initially recognised at their fair value, and subsequently measured at the higher of the unamortised balance of the related fees received and deferred, and the expenditure required to settle the commitment at the balance sheet date. The Fund has retrospectively applied this Amendment and the effect of the restatement was to increase both other assets and other liabilities by €20,000 at 31 December 2005 to reflect guarantee fees receivable and deferred income from financial guarantees. The recognition of the present value of the fees receivable has no impact on the financial statements.

Standards early adopted by the Fund

No standards were early adopted by the Fund in 2006.

Standards, amendments and interpretations effective in 2006 but not relevant to the Fund's operations

The following new standards, amendments and interpretations to existing standards are mandatory for the Fund's 2006 financial statements but are not relevant to the Fund's operations:

- IAS 19 (Amendment), Employee Benefits;
- IAS 21 (Amendment), Net Investment in a Foreign Operation;

The Balkan Region Special Fund

Notes to the financial statements (continued)

3 Accounting policies (continued)

- IAS 39 (Amendment), Cash Flow Hedge Accounting for Forecast Intragroup Transactions;
- IAS 39 (Amendment), The Fair Value Option;
- IFRS 1 (Amendment), First-Time Adoption of International Financial Reporting Standards;
- IFRS 6, Exploration for and Evaluation of Mineral Resources;
- IFRIC 4, Determining whether an Arrangement contains a Lease;
- IFRIC 5, Rights to Interests arising from Decommissioning, Restoration and Environmental Rehabilitation Funds; and
- IFRIC 6, Liabilities arising from Participating in a Specific Market – Waste Electrical and Electronic Equipment.

Interpretations to existing standards that are not yet effective and have not been early adopted by the Fund

The following interpretations to existing standards have been published that are mandatory for the Fund's accounting period beginning on 1 January 2007 or later periods but that the Fund has not early adopted:

IFRS 7, Financial Instruments: Disclosures, and the complementary Amendment to IAS 1, Presentation of Financial Statements – Capital Disclosures (effective for accounting periods from 1 January 2007)

IFRS 7 introduces new disclosures to improve the information about financial instruments. It requires the disclosure of qualitative and quantitative information about exposure to risks arising from financial instruments, including specified minimum disclosures about credit risk, liquidity risk and market risk, including an analysis of sensitivity to market risk. It replaces IAS 30, Disclosures in the Financial Statements of Banks and Similar Financial Institutions, and the disclosure requirements in IAS 32, Financial Instruments: Disclosure and Presentation. IAS 1 (Amendment) introduces disclosures about the level of an entity's capital and how it manages that capital. The Fund has assessed the impact of IFRS 7 and IAS 1 (Amendment) and concluded that the main additional disclosures will be in relation to sensitivity analysis. The Fund will apply IFRS 7 and IAS 1 (Amendment) from its annual period beginning 1 January 2007.

IFRS 8, Operating Segments (effective for accounting periods from 1 January 2009)

IFRS 8 requires an entity to report financial and descriptive information about its reportable segments. Reportable segments are operating segments or aggregations of operating segments that meet specified criteria. Operating segments are components of an entity about which separate financial information is available that is evaluated regularly by the chief operating decision maker in deciding how to allocate resources and in assessing performance. Generally, financial information is required to be reported on the basis that it is used internally for evaluating operating segment performance and deciding how to allocate resources to operating segments. As the Fund currently comprises a single primary segment (Banking operations) and one geographic region (the "Balkan Countries") IFRS 8 is not expected to impact the financial statements. The Fund will apply IFRS 8 from its annual period beginning 1 January 2009.

Standards that are not yet effective and not relevant for the Fund's operations

The following standards have been published that are mandatory for the Fund's accounting period beginning on 1 January 2007 or later periods but are not relevant for the Fund's operations:

- IFRIC 7, Applying the Restatement Approach under IAS 29, Financial Reporting in Hyperinflationary Economies (effective for accounting periods from 1 March 2006);
- IFRIC 8, Scope of IFRS 2 (effective for accounting periods from 1 May 2006);
- IFRIC 9, Reassessment of Embedded Derivatives (effective for accounting periods from 1 June 2006);
- IFRIC 10, Interim Financial Reporting and Impairment (effective for accounting periods from 1 November 2006);
- IFRIC 11, IFRS 2 – Group and Treasury Share Transactions (effective for accounting periods from 1 March 2007); and
- IFRIC 12, Service Concession Arrangements (effective for accounting periods from 1 January 2008).

The Balkan Region Special Fund

Notes to the financial statements (continued)

3 Accounting policies (continued)

iii Significant accounting policies

Financial guarantees

Issued financial guarantees are initially recognised at their fair value, and subsequently measured at the higher of the unamortised balance of the related fees received and deferred, and the expenditure required to settle the commitment at the balance sheet date. The latter is determined upon consideration of objective evidence that the guarantee is impaired and is recognised when it is both probable that the guarantee will require to be settled and that the settlement amount can be reliably estimated.

iv Foreign currencies

The unit of measurement for the presentation of the financial statements of the Fund is euro (€). Transactions, including disbursements, in foreign currencies are translated into euro at exchange rates ruling at the time of the transaction. Commitments net of disbursements made, in currencies other than euro, are translated at spot rates as at 31 December 2006. Monetary assets denominated in currencies other than euro are translated into euro at spot rates as at 31 December 2006. Revenue and expense items are translated into euro at the exchange rate on the date on which they occurred.

Exchange gains or losses arising from the translation of assets, liabilities and transactions during the year are taken to the income statement.

v Interest, fees and commissions

Interest is recorded on an accruals basis. Fees received in respect of services provided over a period of time are recorded as income over the period during which the services are provided. Other fees and commissions are taken to income when received.

vi Contributions

Contributions are recognised as receivable in the balance sheet on the date of signature of a contribution agreement by the Bank and a contributor. Contributions received in currencies other than euro are translated into euro at the exchange rates ruling at the time of the transaction.

vii Disbursements for technical cooperation

Disbursements for technical cooperation, which represent payments for consultancy services provided to the Fund over a period of time, are recorded as expenditure over the period during which the services are received.

viii Cash and cash equivalents

For the purposes of the cash flow statement, cash and cash equivalents comprise balances with less than three months' maturity from the date of acquisition, which are available for use at short notice and which are subject to insignificant risk of changes in value. This definition includes balances of cash and current accounts with foreign banks.

ix Taxation

In accordance with Article 53 of the Agreement Establishing the Bank dated 29 May 1990, within the scope of its official activities, the Bank, its assets, property and income are exempt from all direct taxes and all taxes and duties levied upon goods and services acquired or imported.

The Balkan Region Special Fund

Notes to the financial statements (continued)

4 Disbursements for technical cooperation	Commitments approved €000	Disbursements €000	Undrawn commitments €000
Projects in operation			
At 1 January 2005	2,459	2,047	412
Movement in the year	256	86	170
At 31 December 2005	2,715	2,133	582
Movement in the year	(134)	42	(176)
At 31 December 2006	2,581	2,175	406
Completed projects			
At 1 January 2005	1,378	1,378	-
Movement in the year	176	176	-
At 31 December 2005	1,554	1,554	-
Movement in the year	117	117	-
At 31 December 2006	1,671	1,671	-
Total projects			
At 1 January 2005	3,837	3,425	412
Movement in the year	432	262	170
At 31 December 2005	4,269	3,687	582
Movement in the year	(17)	159	(176)
At 31 December 2006	4,252	3,846	406

5 Other operating expenses

Other operating expenses comprise administrative expenses directly relating to the Fund and include fees payable to the Bank for operating the Fund, calculated as 2.5 and 5 per cent of each contribution instalment received relating to investment and technical cooperation activities respectively.

6 Contributions and net income refunded on termination of contribution agreements

A contribution agreement between the Bank and the Netherlands FMO N.V. ("FMO") for €3.00 million was terminated by mutual consent on 15 September 2002. Contributions have been refunded to FMO periodically since termination as the underlying trade facilitation transactions expire. At 31 December 2006, no further contributions or net income payments were due to FMO.

A contribution agreement between the Bank and Germany for €2.25 million was terminated by mutual consent on 15 March 2005. Contributions have been refunded to Germany periodically since termination as the underlying trade facilitation transactions expire. At 31 December 2006, no further contributions or net income payments were due to Germany.

A contribution agreement between the Bank and Netherlands for €1.16 million was terminated by mutual consent on 31 December 2004. The amount contributions refundable to the Netherlands is disclosed in "Other liabilities" on the balance sheet together with Netherlands's share of retained net income to the date of termination of €107,450.

7 External auditors' remuneration

Other operating expenses include external auditors' remuneration of €7,400 (2005: €7,100). There were no payments made to the external auditors for consultancy services provided under the heading "Disbursements for technical cooperation" in 2006 (2005: Nil).

The Balkan Region Special Fund

Notes to the financial statements (continued)

8 Other assets	2006	Restated
	€000	2005 €000
Interest receivable on placements	68	44
Business Advisory Services Programme advances	80	-
Fee income receivable	440	407
At 31 December	588	451

9 Other liabilities	2006	Restated
	€000	2005 €000
Contributions and net income refundable	1,267	240
Disbursements for technical cooperation payable	110	27
Deferred income from financial guarantees	14	20
Other	8	28
At 31 December	1,399	315

10 Contributions

Cumulative contributions received from the donor countries are set out below:

	2006	2006	2005	2005
	€000	%	€000	%
Austria	276	2.8	276	2.5
Canada	1,472	15.1	1,472	13.4
Denmark	750	7.7	750	6.8
Germany	-	-	58	0.5
Netherlands	-	-	1,160	10.6
Norway	1,568	16.0	1,568	14.2
Switzerland	4,218	43.1	4,218	38.4
Taipei China	1,495	15.3	1,495	13.6
At 31 December	9,779	100.0	10,997	100.0

11 Guarantees

At 31 December 2006, the Bank had outstanding guarantees under the Balkan Region Trade Facilitation Programme for which, in the event of a future default, losses incurred by the Bank will be refunded from the resources of the Fund. At 31 December 2006, the Fund's maximum exposure under such guarantees was €4.7 million (2005: €6.2 million). No provisions have been recognised against this exposure.

<i>Analysis by geographic area</i>	2006	2005
	€000	€000
Bosnia and Herzegovina	1,335	1,928
Former Yugoslav Republic of Macedonia	3,184	2,434
Serbia and Montenegro	200	1,807
At 31 December	4,719	6,169

12 Undrawn commitments

	2006	2005
	€000	€000
Disbursements for technical cooperation	406	582
Guarantees	4,719	6,169
At 31 December	5,125	6,751

The Balkan Region Special Fund

Notes to the financial statements (continued)

13 Net currency position

	United States		Total
	Euro	dollars	
	€000	€000	€000
Net currency position at 31 December 2006			
Assets			
Placements with credit institutions	8,000	15	8,015
Other assets	588	-	588
Total assets	8,588	15	8,603
Liabilities			
Other liabilities	(1,399)	-	(1,399)
Total contributors' resources	(7,204)	-	(7,204)
Total liabilities	(8,603)	-	(8,603)
Net currency position at 31 December 2006	(15)	15	-

Restated	United States		Total
	Euro	Dollars	
	€000	€000	€000
Net currency position at 31 December 2005			
Assets			
Placements with credit institutions	8,283	16	8,299
Other assets	451	-	451
Total assets	8,734	16	8,750
Liabilities			
Other liabilities	(315)	-	(315)
Total contributors' resources	(8,435)	-	(8,435)
Total liabilities	(8,750)	-	(8,750)
Net currency position at 31 December 2005	(16)	16	-

The exchange rate used for the conversion of assets and liabilities denominated in United States dollars into euro at 31 December 2006, where appropriate, was 1.3168 (2005: 1.1830).

The Balkan Region Special Fund

Notes to the financial statements (continued)

14 Liquidity position

The table below provides an analysis of assets, liabilities and contributors' resources into relevant maturity groupings based on the remaining period from the balance sheet date to the contractual maturity date. It is presented under the most prudent consideration of maturity dates. Therefore, in the case of liabilities the earliest possible repayment date is shown, while for assets it is the latest possible repayment date.

Those assets and liabilities that do not have a contractual maturity date are grouped together in the "Maturity undefined" category.

	Up to and including 1 month	Over 1 month and up to and including 3 months	Over 3 months and up to and including 1 year	Over 1 year and up to and including 5 year	Maturity undefined	Total
	€000	€000	€000	€000	€000	€000
Liquidity position at 31 December 2006						
Assets						
Placements with credit institutions	8,015	-	-	-	-	8,015
Other assets	147	410	25	6	-	588
Total assets	8,162	410	25	6	-	8,603
Liabilities						
Other liabilities	(1,267)	(114)	(13)	(5)	-	(1,399)
Total contributors' resources	-	-	-	-	(7,204)	(7,204)
Total liabilities	(1,267)	(114)	(13)	(5)	(7,204)	(8,603)
Net liquidity position at 31 December 2006	6,895	296	12	1	(7,204)	-
Cumulative net liquidity position at 31 December 2006	6,895	7,191	7,203	7,204	-	-
	Up to and including 1 month	Over 1 month and up to and including 3 months	Over 3 months and up to and including 1 year	Over 1 year and up to and including 5 year	Maturity undefined	Total
	€000	€000	€000	€000	€000	€000
Restated						
Liquidity position at 31 December 2005						
Assets						
Placements with credit institutions	8,299	-	-	-	-	8,299
Other assets	44	337	39	31	-	451
Total assets	8,343	337	39	31	-	8,750
Liabilities						
Other liabilities	(27)	(25)	(256)	(7)	-	(315)
Total contributors' resources	-	-	-	-	(8,435)	(8,435)
Total liabilities	(27)	(25)	(256)	(7)	(8,435)	(8,750)
Net liquidity position at 31 December 2005	8,316	312	(217)	24	(8,435)	-
Cumulative net liquidity position at 31 December 2005	8,316	8,628	8,411	8,435	-	-

The Balkan Region Special Fund

Notes to the financial statements (continued)

15 Interest rate risk

The table below summaries the Fund's exposure to interest rate risks. Included in the table are the assets and liabilities at carrying amounts, categorised by the earlier of contractual repricing or maturity dates.

	Up to and including 1 month €000	Non-interest- bearing funds €000	Total €000
Interest rate risk at 31 December 2006			
Assets			
Placements with credit institutions	8,015	-	8,015
Other assets	-	588	588
Total assets	8,015	588	8,603
Liabilities			
Other liabilities	-	(1,399)	(1,399)
Total contributors' resources	-	(7,204)	(7,204)
Total liabilities	-	(8,603)	(8,603)
Interest sensitivity gap at 31 December 2006	8,015	(8,015)	-
Restated			
	Up to and including 1 month €000	Non-interest- bearing funds €000	Total €000
Interest rate risk at 31 December 2005			
Assets			
Placements with credit institutions	8,299	-	8,299
Other assets	-	451	451
Total assets	8,299	451	8,750
Liabilities			
Other liabilities	-	(315)	(315)
Total contributors' resources	-	(8,435)	(8,435)
Total liabilities	-	(8,750)	(8,750)
Interest sensitivity gap at 31 December 2005	8,299	(8,299)	-

The table below summaries the effective interest rate by major currencies for monetary financial instruments:

	United		United	
	Euro 2006	States dollars 2006	Euro 2005	States dollars 2005
Assets	%	%	%	%
Placements with credit institutions	2.75	4.53	1.99	2.76

16 Segment information

In accordance with IAS 14, the primary segment of the Fund is business operation and the secondary segment is geographical. At 31 December 2006, the activities of the Fund comprised a single primary segment (Banking operations) and one geographic region (the "Balkan Countries"). Consequently, no additional disclosure is required.

17 Post balance sheet events

There have been no material post-balance sheet events that would require disclosure or adjustment to these financial statements.

Independent auditor's report to the Governors of the European Bank for Reconstruction and Development (the 'Bank')

Report on the Financial Statements

We have audited the financial statements of the Balkan Region Special Fund for the year ended 31 December 2006 which comprise the income statement, the balance sheet, the statement of changes in contributor's resources, the statement of cash flows, the accounting policies and the notes to the financial statements ("financial statements").

President's responsibility for the financial statements

The President is responsible for the preparation and fair presentation of the financial statements in accordance with the International Financial Reporting Standards issued by the International Accounting Standards Board, and in accordance with the overall principles of the European Community's Council Directive on Annual Accounts and Consolidated Accounts of Banks and Other Financial Institutions. This responsibility includes: designing, implementing and maintaining internal control relevant to the preparation and fair presentation of financial statements that are free from material misstatement, whether due to fraud or error; selecting and applying appropriate accounting policies; and making accounting estimates that are reasonable in the circumstances.

Auditor's responsibility

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

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

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

Opinion

In our opinion the financial statements present fairly, in all material respects, the financial position of the Fund at 31 December 2006 and its financial performance and cash flows for the year then ended in accordance with the International Financial Reporting Standards issued by the International Accounting Standards Board and the overall principles of the European Community's Council Directive on Annual Accounts and Consolidated Accounts of Banks and Other Financial Institutions.

Other matters

We also report to you if, in our opinion, the financial results section of the Financial Report is not consistent with the financial statements, if the Bank has not kept proper accounting records, or if we have not received all the information and explanations we require for our audit.

This report, including the opinion, has been prepared for, and only for, the Bank and for the confidential use of the Contributors to the Fund and for no other purpose. We do not, in giving this opinion, accept or assume responsibility for any other purpose or to any other person to whom this report is shown or into whose hands it may come, save where expressly agreed by our prior consent in writing.



PricewaterhouseCoopers LLP
Chartered Accountants and Registered Auditors
London

6 March 2007

The maintenance and integrity of the EBRD's website is the responsibility of the President; the work carried out by the auditors does not involve consideration of these matters and, accordingly, the auditors accept no responsibility for any changes that may have occurred to the financial statements since they were initially presented on the website. Legislation in the United Kingdom governing preparation and dissemination of financial statements may differ from legislation in other jurisdictions.