

ELECTRONIC TRANSMISSION DISCLAIMER

STRICTLY NOT TO BE FORWARDED TO ANY OTHER PERSONS

IMPORTANT: You must read the following disclaimer before continuing. This electronic transmission applies to the attached document and you are therefore advised to read this disclaimer carefully before reading, accessing or making any other use of the attached offering circular relating to **International Investment Bank** (the “**Issuer**”). In accessing the attached document, you agree to be bound by the following terms and conditions, including any modifications to them from time to time, each time you receive any information from us as a result of such access. You acknowledge that this electronic transmission and the delivery of the attached document is confidential and intended for you only and you agree you will not forward, reproduce or publish this electronic transmission or the attached document to any other person. This electronic transmission and the attached document has been prepared solely in connection with the proposed offering via private placements addressed to persons in Member States of the European Economic Area (“**EEA**”) (i) who are “qualified investors” within the meaning of Article 2(1)(e) of the Prospectus Directive (“**Qualified Investors**”); in addition, in the United Kingdom, this electronic transmission and the attached document is being distributed only to, and is directed only at, Qualified Investors (a) who have professional experience in matters relating to investments falling within Article 19(5) of the Financial Services and Markets Act 2000 (Financial Promotion) Order 2005, as amended (the “**Order**”) and Qualified Investors falling within Article 49(2)(a) to (d) of the Order, and (b) to whom it may otherwise lawfully be communicated (all such persons together being referred to as “**Relevant Persons**”) and/or (ii) to less than 150 natural or legal persons, other than qualified investors per Member State, and to such other investors in Hungary or such other Member States of the EEA, in reliance on the exemptions set out in article 3 para. 2. of the Prospectus Directive, as implemented in the relevant national implementation measures and in reliance of Regulation S (“**Regulation S**”) under the U.S. Securities Act of 1933, as amended (the “**U.S. Securities Act**”) (the “**Offering**”) of fixed interest rate HUF-denominated bonds, and having a maturity of three (3) years, issued by the Issuer (the “**Bonds**”). The publication of this offering circular (the “**Offering Circular**”) in connection with the listing of the Bonds on the Budapest Stock Exchange (“**Listing**”) was approved by the National Bank of Hungary (in Hungarian, *Magyar Nemzeti Bank*) (the “**NBH**”) under its resolution H-KE-III-147/2019. on 13 March 2019. The Offering Circular will be published and following publication will be available on the Issuer’s website at <https://www.iib.int/en>, on each of the Managers’ websites <https://www.otpbank.hu> and <https://www.unicreditbank.hu> respectively, on the website of the Budapest Stock Exchange www.bet.hu, on the website of the NBH www.kozzetetelek.hu and, to the extent required by law or so elected by the Issuer, on an online medium. Pricing information and other related disclosures are expected to be published on these websites. Prospective investors are advised to access such information prior to making an investment decision.

NOTHING IN THIS ELECTRONIC TRANSMISSION OR THE OFFERING CIRCULAR CONSTITUTES AN OFFER OF SECURITIES FOR SALE IN THE UNITED STATES OR ANY JURISDICTION WHERE IT IS UNLAWFUL TO DO SO. THE SECURITIES REFERRED TO IN THE OFFERING CIRCULAR HAVE NOT BEEN, AND WILL NOT BE, REGISTERED UNDER THE U.S. SECURITIES ACT OF 1933, AS AMENDED (THE “**SECURITIES ACT**”), OR THE SECURITIES LAWS OF ANY STATE OF THE UNITED STATES (“**U.S.**”) OR OTHER JURISDICTION OF THE U.S. AND SUCH SECURITIES MAY NOT BE OFFERED OR SOLD WITHIN THE UNITED STATES OR TO, OR FOR THE ACCOUNT OR BENEFIT OF, U.S. PERSONS (AS DEFINED IN REGULATION S (“**REGULATION S**”) UNDER THE SECURITIES ACT).

NEITHER THE OFFERING CIRCULAR NOR ANY PART OR COPY OF IT MAY BE FORWARDED OR DISTRIBUTED TO ANY OTHER PERSON AND MAY NOT BE REPRODUCED IN ANY MANNER WHATSOEVER AND IN PARTICULAR MAY NOT BE FORWARDED TO ANY U.S. PERSON OR TO ANY U.S. ADDRESS. ANY FORWARDING, DISTRIBUTION OR REPRODUCTION OF THE OFFERING CIRCULAR IN WHOLE OR IN PART IS UNAUTHORISED. FAILURE TO COMPLY WITH THIS DIRECTIVE MAY RESULT IN A VIOLATION OF THE SECURITIES ACT OR APPLICABLE LAWS OF OTHER JURISDICTIONS.

THIS ELECTRONIC TRANSMISSION, THE OFFERING CIRCULAR AND THE OFFERING IS AVAILABLE ONLY TO NON-US PERSONS (AS DEFINED IN REGULATION S) OUTSIDE OF THE U.S.

Confirmation of Your Representation: This electronic transmission and the attached document is delivered to you on the basis that you are deemed to have represented to the Issuer and OTP Bank Nyrt. and UniCredit Bank Hungary Zrt. (the “**Managers**”) that (i) you are acquiring such securities in “offshore transactions”, as defined in, and in reliance on, Regulation S under the Securities Act (“**Regulation S**”); (ii) if you are in the UK, you are a Relevant Person, and/or a Relevant Person who is acting on behalf of, Relevant Persons in the United Kingdom and/or Qualified Investors to the extent you are acting on behalf of persons or entities in the UK or the EEA; (iii) if you are in any member state of the EEA other than the UK, you are a Qualified Investor and/or a Qualified Investor acting on behalf of, Qualified Investors

or Relevant Persons, to the extent you are acting on behalf of persons or entities in the EEA or the UK; or (iv) you are an institutional investor or an investor that is otherwise eligible to receive this document and you consent to delivery by electronic transmission.

You are reminded that you have received this electronic transmission and the attached document on the basis that you are a person into whose possession this document may be lawfully delivered in accordance with the laws of the jurisdiction in which you are located and you may not nor are you authorized to deliver this document, electronically or otherwise, to any other person. If you receive this electronic transmission and the attached document by e-mail, you should not reply by e-mail. Any reply to e-mail communications, including those you generate by using the “reply” function on your e-mail software, will be ignored or rejected. If you receive the attached document in electronic format by e-mail, your use of such document in electronic format and such e-mail is at your own risk and it is your responsibility to take precautions to ensure that each is free from viruses and other items of a destructive nature. The materials relating to the Offering do not constitute, and may not be used in connection with, an offer or solicitation in any place where such offers or solicitations are not permitted by law. If a jurisdiction requires that the Offering be made by an authorized broker or dealer and the underwriters or any affiliate of the underwriters is an authorized broker or dealer in that jurisdiction, the Offering shall be deemed to be made by the underwriters or such affiliate on behalf of the Issuer in such jurisdiction.

This document has been made available to you in an electronic form. You are reminded that documents transmitted via this medium may be altered or changed during the process of electronic transmission and consequently neither the Issuer, the Managers nor any of their respective affiliates accepts any liability or responsibility whatsoever in respect of any difference between the document distributed to you in electronic format and the hard copy version made available to you upon request from any of the Managers. By accessing the linked document, you consent to receiving it in electronic form. Neither the Managers nor any of their respective affiliates accepts any responsibility whatsoever for the contents of this document or for any statement made or purported to be made by it, or on its behalf, in connection with the Issuer or the Bonds. The Issuer and each of its respective affiliates, each accordingly disclaims all and any liability whether arising in tort, contract or otherwise which they might otherwise have in respect of such document or any such statement. No representation or warranty express or implied, is made by the Managers or any of their respective affiliates as to the accuracy, completeness or sufficiency of the information set out in this document.

The Managers are acting exclusively for the Issuer and no one else in connection with the Offering. They will not regard any other person (whether or not a recipient of this document) as their client in relation to the Offering and will not be responsible to anyone other than the Issuer for providing the protections afforded to its clients nor for giving advice in relation to the Offering or any transaction or arrangement referred to herein.

IMPORTANT NOTICE

THIS OFFERING OF THE BONDS DESCRIBED HEREIN IS AVAILABLE ONLY TO (I) INVESTORS IN HUNGARY WHO ARE “QUALIFIED INVESTORS” WITHIN THE MEANING OF ARTICLE 2(1)(E) OF THE DIRECTIVE 2003/71/EC OF THE EUROPEAN PARLIAMENT AND OF THE COUNCIL OF 4 NOVEMBER 2003 ON THE PROSPECTUS TO BE PUBLISHED WHEN SECURITIES ARE OFFERED TO THE PUBLIC OR ADMITTED TO TRADING AND AMENDING, AS AMENDED (THE “**PROSPECTUS DIRECTIVE**”), AS IMPLEMENTED IN HUNGARY BY SECTIONS 48 TO 51 OF ACT CXXXVIII OF 2007 ON INVESTMENT FIRMS AND COMMODITY EXCHANGE SERVICE PROVIDERS AND THE RULES OF THEIR ACTIVITIES; AND/OR (II) LESS THAN 150 NATURAL OR LEGAL PERSONS, OTHER THAN QUALIFIED INVESTORS PER MEMBER STATE, AND TO SUCH OTHER INVESTORS IN HUNGARY OR SUCH OTHER MEMBER STATES OF THE EUROPEAN ECONOMIC AREA WHERE IT IS POSSIBLE TO DO SO, IN RELIANCE OF REGULATION S (“**REGULATION S**”) UNDER THE U.S. SECURITIES ACT OF 1933, AS AMENDED (THE “**U.S. SECURITIES ACT**”) AND WITHOUT THE NEED TO PUBLISH A PROSPECTUS OR UNDERTAKE ANY OTHER FORMALITIES WHATSOEVER UNDER ANY APPLICABLE LAW, IN RELIANCE ON ARTICLE 3(2) OF THE PROSPECTUS DIRECTIVE, TO THE EXTENT, AND ONLY PROVIDED THAT, AN INVESTMENT IN THE BONDS DOES NOT CONSTITUTE A VIOLATION OF ANY APPLICABLE LAW BY SUCH INVESTORS. IN ADDITION, IN THE UNITED KINGDOM, THE OFFERING OF THE BONDS DESCRIBED HEREIN IS DIRECTED ONLY AT QUALIFIED INVESTORS WITHIN THE MEANING OF ARTICLE 2(1)(E) OF THE PROSPECTUS DIRECTIVE (“**QUALIFIED INVESTORS**”) (X) WHO HAVE PROFESSIONAL EXPERIENCE IN MATTERS RELATING TO INVESTMENTS FALLING WITHIN ARTICLE 19(5) OF THE FINANCIAL SERVICES AND MARKETS ACT 2000 (FINANCIAL PROMOTION) ORDER 2005, AS AMENDED (THE “**FINANCIAL PROMOTION ORDER**”) AND QUALIFIED INVESTORS FALLING WITHIN ARTICLE 49(2)(A) TO (D) OF THE FINANCIAL PROMOTION ORDER AND (Y) TO WHOM IT MAY OTHERWISE LAWFULLY BE DIRECTED (ALL SUCH PERSONS TOGETHER BEING REFERRED TO AS “**RELEVANT PERSONS**”). INVESTOR TO WHOM THE OFFERING OF THE BONDS DESCRIBED HEREIN IS AVAILABLE IN ACCORDANCE WITH THE FOREGOING ARE HEREIN REFERRED TO AS “**ELIGIBLE INVESTORS**”.

IMPORTANT: You must read the following before continuing. The following applies to the Offering Circular (the “**Offering Circular**”) following this notice, and you are therefore advised to read this carefully before reading, accessing or making any other use of the Offering Circular. In accessing the Offering Circular, you agree to be bound by the following terms and conditions, including any modifications to them any time you receive any information from us as a result of such access.

The Offering Circular has been prepared in connection with the proposed offer and sale of the Bonds described therein.

NOTHING IN THIS OFFERING CIRCULAR CONSTITUTES AN OFFER OF SECURITIES FOR SALE IN THE UNITED STATES OR ANY JURISDICTION WHERE IT IS UNLAWFUL TO DO SO. THE BONDS HAVE NOT BEEN, AND WILL NOT BE, REGISTERED UNDER THE U.S. SECURITIES ACT, OR THE SECURITIES LAWS OF ANY STATE OF THE UNITED STATES (“U.S.”) OR OTHER JURISDICTION AND SUCH BONDS MAY NOT BE OFFERED OR SOLD WITHIN THE UNITED STATES OR TO, OR FOR THE ACCOUNT OR BENEFIT OF, U.S. PERSONS (AS DEFINED IN REGULATION S UNDER THE U.S. SECURITIES ACT). THE BONDS ARE OFFERED AND SOLD ONLY TO INVESTORS IN HUNGARY OR SUCH OTHER JURISDICTIONS WHERE IT IS POSSIBLE TO DO SO WITHOUT THE NEED TO PUBLISH A PROSPECTUS OR UNDERTAKE ANY OTHER FORMALITIES WHATSOEVER UNDER APPLICABLE LAW, IN RELIANCE ON REGULATION S UNDER THE U.S. SECURITIES ACT.

NONE OF THE U.S. SECURITIES AND EXCHANGE COMMISSION, ANY STATE SECURITIES COMMISSION OR ANY OTHER U.S. REGULATORY AUTHORITY, HAS APPROVED OR DISAPPROVED THE BONDS NOR HAVE ANY OF THE FOREGOING AUTHORITIES PASSED UPON OR ENDORSED THE MERITS OF THIS OFFERING OR THE ACCURACY OR ADEQUACY OF THIS OFFERING CIRCULAR. ANY REPRESENTATION TO THE CONTRARY IS A CRIMINAL OFFENSE.

THE FOLLOWING OFFERING CIRCULAR MAY NOT BE FORWARDED OR DISTRIBUTED TO ANY OTHER PERSON AND MAY NOT BE REPRODUCED IN ANY MANNER WHATSOEVER. ANY FORWARDING, DISTRIBUTION OR REPRODUCTION OF THIS DOCUMENT IN WHOLE OR IN PART IS UNAUTHORIZED. FAILURE TO COMPLY WITH THIS DIRECTIVE MAY RESULT IN A VIOLATION OF THE U.S. SECURITIES ACT OR THE APPLICABLE LAWS OF OTHER JURISDICTIONS. IF YOU HAVE GAINED ACCESS TO THIS TRANSMISSION CONTRARY TO ANY OF THE FOREGOING RESTRICTIONS, YOU ARE NOT AUTHORIZED AND WILL NOT BE ABLE TO PURCHASE ANY OF THE BONDS DESCRIBED THEREIN.

Confirmation of your representation: In order to be eligible to view the Offering Circular or make an investment decision with respect to the Bonds, you must be an Eligible Investor. The Offering Circular is being sent at your request. By accepting the e-mail or otherwise accessing the Offering Circular, you shall be deemed to have represented to us that:

- (1) you consent to delivery of such Offering Circular by electronic transmission, and
- (2) you and any customers you represent are Eligible Investors or, if you are in the United Kingdom, you are a relevant person and/or a relevant person who is acting on behalf of, relevant persons in the United Kingdom and/or Qualified Investors to the extent you are acting on behalf of persons or entities in the United Kingdom or the European Economic Area, and
- (3) the e-mail address that you gave us and to which the e-mail has been delivered is not located in the United States, its territories and possessions (including Puerto Rico, the U.S. Virgin Islands, Guam, American Samoa, Wake Island and the Northern Mariana Islands), any State of the United States or the District of Columbia, or any other territory which is not in the European Economic Area.

You are reminded that the Offering Circular has been delivered to you on the basis that you are a person into whose possession the Offering Circular may be lawfully delivered in accordance with the laws of the jurisdiction in which you are located, and you may not, nor are you authorized to, deliver the Offering Circular to any other person.

Under no circumstances shall the Offering Circular constitute an offer to sell or the solicitation of an offer to buy nor shall there be any sale of these securities in any jurisdiction in which such offer, solicitation or sale would be unlawful.

In addition, in the United Kingdom, this electronic transmission and the attached document is being distributed only to, and is directed only at, Qualified Investors (i) who have professional experience in matters relating to investments falling within Article 19(5) of the Financial Promotion Order and Qualified Investors falling within Article 49(2)(a) to (d) of the Financial Promotion Order, and (ii) to whom it may otherwise lawfully be communicated. The Offering Circular has been sent to you in an electronic form. You are reminded that documents transmitted via this medium may be altered or changed during the process of electronic transmission, and consequently none of the Issuer or the Managers, nor any of their affiliates, nor any of their or its directors, officers, employees, advisers or agents accepts any liability or responsibility whatsoever in respect of any difference between the Offering Circular distributed to you in electronic format and the hard copy version made available to you on request from any of the Managers.

None of the Managers nor any of their affiliates accept any responsibility whatsoever for the contents of this electronic transmission or the Offering Circular or for any other statement made or purported to be made by them, or on their behalf, in connection with the Issuer or the securities or the Offering referred to herein. The Managers and each of their affiliates disclaim all and any liability whether arising in tort, contract, or otherwise which they might otherwise have in respect of this electronic transmission, the Offering Circular or any such statement. No representation or warranty, express or implied, is made by the Managers or any of their affiliates or advisors as to the accuracy, completeness or sufficiency of the information set out in this electronic transmission or the Offering Circular.

MIFID II product governance / Retail investors, professional investors and eligible counterparties – Solely for the purposes of the manufacturer's product approval process, the target market assessment in respect of the Bonds has led to the conclusion that: (i) the target market for the Bonds is eligible counterparties, professional clients and retail clients, each as defined in MiFID II; (ii) retail clients are only considered target market if they have (a) the ability to understand relevant financial products and transactions and their risks; (b) knowledge regarding investments; (c) knowledge regarding trading procedures; (d) financial industry experience, interest, and knowledge; (e) the respective counterparty or client understands that he/she can incur capital losses; (iii) all channels for distribution to eligible counterparties and professional clients are appropriate; and (iv) the following channels for distribution of the Bonds to retail clients are appropriate - investment advice, portfolio management, unsolicited sales and pure execution services, subject to the distributor's suitability and appropriateness obligations under MiFID II, as applicable. The product is incompatible for any client outside the positive target market identified above. Any person subsequently offering, selling or recommending the Bonds (a distributor) should take into consideration the manufacturer's target market assessment; however, a distributor subject to MiFID II is responsible for undertaking its own target market assessment in respect of the Bonds (by either adopting or refining the manufacturer's target market assessment) and determining appropriate distribution channels, subject to the distributor's suitability and appropriateness obligations under MiFID II, as applicable.



INTERNATIONAL INVESTMENT BANK

OFFERING OF HUF BONDS

International Investment Bank (the “**Issuer**”), an international organisation operating on the basis of the intergovernmental Agreement on the Establishment of the International Investment Bank of 10 July 1970 and the Charter of the International Investment Bank attached to the Establishment Agreement, initially registered with the Secretariat of the United Nations on 1 December 1971 under number 11417, is offering fixed interest rate HUF-denominated bonds, and having a maturity of three (3) years (the “**Bonds**”), in a private placement (the “**Offering**”) to investors in Hungary who are “qualified investors” within the meaning of article 2(1)(e) of the Prospectus Directive, as implemented in Hungary by sections 48 to 51 of Act CXXXVIII of 2007 on Investment Firms and Commodity Exchange Service Providers and the Rules of their Activities; and/or to less than 150 natural or legal persons, other than qualified investors per member state, and to such other investors in Hungary or such other members states of the European Economic Area where it is possible to do so, in reliance of Regulation S (“**Regulation S**”) under the U.S. Securities Act of 1933, as amended (the “**U.S. Securities Act**”) and without the need to publish a prospectus or undertake any other formalities whatsoever under applicable law in reliance on article 3(2) of the Prospectus Directive, to the extent, and only provided that an investment in the Bonds does not constitute a violation of any applicable law by such investors. This offering circular (the “**Offering Circular**”) has been prepared for the Offering and constitutes an “*információs összeállítás*” for the purposes of section 8(1) of 285/2001 (XII. 26.) Government Decree on bonds.

IN ACCORDANCE WITH SECTION 18 OF ACT CXX OF 2001 ON THE CAPITAL MARKETS (“THE CAPITAL MARKETS ACT”) THIS DOCUMENT MUST HIGHLIGHT THAT THE OFFERING IS A PRIVATE PLACEMENT IN HUNGARY.

Each Bond has a nominal value of HUF 10,000 (the “**Nominal Value**”). The interest on the Bonds shall be paid in twelve-months arrears. The Bonds and any payments thereunder are governed by the relevant provisions of the “*Terms and conditions of the Bonds*” section of this Offering Circular. The Bonds are issued in dematerialised form (in Hungarian: *dematerializált értékpapír*). The entity in charge of keeping the records of the Bonds is KELER Központi Értéktár Zrt. the Hungarian central depository, a Hungarian company having its registered office at Rákóczi út 70-72., 1074 Budapest, Hungary (the “**Central Depository**”). The Bonds shall be registered in the system of the Central Depository in accordance with the regulations thereof, by the crediting of the accounts of the Bondholders opened with the Central Depository, directly or through a participant who has an account with the Central Depository (the “**Participant**”).

Under section 45(1) of the Capital Markets Act the public offering or listing on a regulated market of the Bonds in Hungary is subject to the publication of a document called “*ismertető*” approved by the National Bank of Hungary (the “**NBH**”). The Issuer will apply for the Bonds to be listed on the Regulated Market of the Budapest Stock Exchange. The Regulated Market of the Budapest Stock Exchange is a regulated market in the European Economic Area for the purposes of Directive 2004/39/EC, as amended. Accordingly, this Offering Circular has been prepared also for the listing of the Bonds on the Budapest Stock Exchange and constitutes an “*ismertető*” for the purposes of section 45(1) of the Capital Markets Act. The publication of this Offering Circular has been approved by the NBH on 13 March 2019 in its resolution No. H-KE-III-147/2019. However, this Offering Circular constitutes neither a prospectus nor a base prospectus for the purposes of the Directive 2003/71/EC, as amended (the “**Prospectus Directive**”). Accordingly, this Offering Circular does not purport to meet the format and the disclosure requirements set forth under the Prospectus Directive and Commission Regulation (EC) No 809/2004 implementing the Prospectus Directive, as amended, and it has not been and will not be submitted for approval to any competent authority within the meaning of the Prospectus Directive.

The first day of trading of the Bonds on the Regulated Market of the Budapest Stock Exchange is expected to occur on or about 26 March 2019. At the discretion of the Issuer, an application may also be made for the Bonds to be admitted to trading on any other regulated market in the European Union.

The Issuer has been rated A3 with stable outlook by Moody's Investors Service, Inc. (“**Moody's**”), BBB+ with stable outlook by Fitch Ratings CIS Ltd (“**Fitch**”), A- with stable outlook by Standard & Poor's Credit Market Services Europe Limited (“**S&P**”) and A with positive outlook by Dagong Global Credit Rating Co.,

Ltd (“**Dagong**”). Fitch and S&P are established in the European Union and registered under the Regulation (EC) No. 1060/2009, as amended (the “**CRA Regulation**”) and are included in the list of registered credit rating agencies published by the European Securities and Markets Authority on its website in accordance with the CRA Regulation, whereas Moody’s is a leading market intelligence services provider based in the United States and Dagong is a notable credit rating agency based in the People’s Republic of China.

An investment in the Bonds involves risks. See “*Risk factors*” for a discussion of certain matters that investors should consider prior to making an investment in the Bonds.

AS THE MANAGERS WILL NOT UNDERTAKE JOINT AND SEVERAL LIABILITY WITH THE ISSUER FOR THE CONTENT OF THIS OFFERING CIRCULAR, THEREFORE UNDER SECTION 38(4b) OF THE CAPITAL MARKETS ACT THE BONDS ARE DEEMED AS HIGH RISK INVESTMENTS.

ALSO, SINCE THE VALUE OF THE TOTAL ASSETS OF THE ISSUER, WHEN AGGREGATED WITH THE MAXIMUM AGGREGATE PRINCIPAL VALUE OF THE BONDS AND DECREASED BY THE EQUITY OF THE ISSUER, IS, IN ACCORDANCE WITH ITS MOST RECENT AUDITED ANNUAL ACCOUNTS, 2.43 TIMES HIGHER THAN ITS EQUITY, UNDER SECTION 38(4b) OF THE CAPITAL MARKETS ACT THE BONDS ARE DEEMED AS HIGH RISK INVESTMENTS.

According to the provisions of the Capital Markets Act, a credit institution would only be considered as a high risk investment from the perspective of asset / equity ratio if its assets are 20 times higher than its equity. Although the Issuer does not qualify as credit institution under Hungarian law, it has many features similar to credit institutions and adopted best practices and a prudent risk management framework similar with those required for credit institutions (see “*Description of the Issuer*”). Therefore, since the Capital Markets Act does not treat specifically multilateral development banks for these purposes, the categorisation of the Bonds as high risk investment from the asset / equity ratio perspective should be interpreted accordingly.

The Offering does not constitute an offer to sell, or solicitation of an offer to buy, securities in any jurisdiction in which such offer or solicitation would be unlawful. The Bonds have not been and will not be registered under the U.S. Securities Act of 1933 or with any securities regulatory authority of any state or other jurisdiction of the United States and may not be offered or sold within the United States. For a discussion of certain further restrictions on offers, sales and transfers of the Bonds and the distribution of this Offering Circular, see “*General information – Selling and transfer restrictions*”.

MANAGERS

OTP BANK NYRT.

UNICREDIT BANK HUNGARY ZRT.

Offering Circular dated 11 March 2019

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IMPORTANT NOTICES

General notices to investors

This Offering Circular is personal to each offeree and does not constitute an offer to any other person or to the public generally to subscribe for or otherwise acquire Bonds. Distribution of this Offering Circular to any person other than the prospective investor and any person retained to advise such prospective investor with respect to the purchase of Bonds is unauthorized. Each prospective investor, by accepting delivery of this Offering Circular, agrees to the foregoing.

This Offering Circular contains information provided by the Issuer in connection with the issue of the Bonds. The Issuer accepts responsibility for the information contained in this Offering Circular.

The Issuer confirms that this Offering Circular is true and accurate in all material respects and is not misleading in any material respect, that any opinions, predictions or intentions expressed herein are honestly held or made and are not misleading in any material respect, that to the best of the Issuer's knowledge and belief this Offering Circular does not omit to state any material fact necessary to make such information, opinions, predictions or intentions (in the context of the issue, offering and sale of the Bonds) not misleading in any material respect, and that all reasonable enquiries have been made to verify the foregoing. However, the information set out under the section "*Description of the Issuer – Relevant geographic markets*" includes extracts from information and data released by publicly available sources in Europe and elsewhere. While we accept responsibility for the accurate extraction and summarization of such information and data, we have not independently verified the accuracy of such information and data and we accept no further responsibility in respect thereof. In addition, this Offering Circular contains summaries believed to be accurate with respect to certain documents, but reference is made to the actual documents for complete information. All such summaries are qualified in their entirety by such reference. However, as far as we are aware, no information or data has been omitted which would render reproduced information inaccurate or misleading.

Pursuant to a mandate letter dated 28 January 2019, the Issuer has appointed OTP Bank Nyrt. ("**OTP Bank**") and UniCredit Bank Hungary Zrt. ("**UniCredit**") as joint lead managers (the "**Joint Lead Managers**") and UniCredit as paying agent (the "**Paying Agent**"), in connection with the issuance of the Bonds, subject to terms of the contractual arrangements entered into by the foregoing parties (OTP Bank and UniCredit are hereinafter each referred to as a "**Manager**", and collectively referred to as the "**Managers**").

Neither the Managers nor any of their affiliates make any representation, warranty or undertaking, express or implied, or accept any responsibility or liability, as to the accuracy or completeness at any time of the information contained in this Offering Circular. No person has been authorised by the Issuer or any of the Managers to give any information or to make any representation not contained herein, and, if given or made, such information or representation must not be relied upon as having been authorised by the Issuer or the Managers. Neither the delivery of this Offering Circular, nor the offering, sale or delivery of any Bonds shall, under any circumstances, create any implication that the information contained in this Offering Circular is true subsequent to the date hereof or the date upon which this Offering Circular has been most recently amended or supplemented or that there has been no change in the financial situation of the Issuer or the information presented herein since the date hereof or, if later, the date upon which this Offering Circular has been most recently amended or supplemented or that any other information supplied in connection with the Bonds is correct at any time subsequent to the date on which it is supplied or, if different, to the date indicated in the document containing the same.

Neither this Offering Circular, nor any other information supplied in connection with the issue of the Bonds: (i) is intended to provide the basis for any credit or other evaluation; or (ii) should be considered as a recommendation by the Issuer or any Manager that any recipient of this Offering Circular, or any other information supplied relating to the issue of the Bonds, should purchase any Bonds. Each investor contemplating the purchase of any Bonds should make its own independent investigation of the financial condition and affairs, and its own appraisal of the creditworthiness, of the Issuer, as well as the risks involved, as it deems necessary. Neither this Offering Circular, nor any other information supplied in connection with the issue of any Bonds, constitutes an offer or invitation by or on behalf of the Issuer or any Manager to any person to subscribe to or purchase any Bonds. In addition, neither the Issuer nor the Managers or any of their affiliates are making any representation regarding the legality of an investment in the Bonds, and investors should not construe anything in this Offering Circular as legal, business or tax advice. Investors should consult their own advisors as to legal, tax, business, financial and

related aspects of an investment in the Bonds. Investors must comply with all laws applicable in any jurisdiction in which they buy, offer or sell the Bonds or possess or distribute this Offering Circular, and must obtain all applicable consents and approvals; neither the Issuer nor any Manager shall have any responsibility for any of the foregoing legal requirements.

The distribution of this Offering Circular and the offering, sale and delivery of the Bonds in certain jurisdictions may be restricted by law. Persons who come into possession of this Offering Circular are required to inform themselves of and observe any such restrictions. In particular, such persons are required to comply with the restrictions on the offer or sale of Bonds and on the distribution of this Offering Circular and other information in relation to the Bonds set out under “*General information – Selling and transfer restrictions*” section below.

By receiving this Offering Circular, investors acknowledge that they have had an opportunity to request from the Issuer for review, and that they have received, all additional information they deem necessary to verify the accuracy and completeness of the information contained in this Offering Circular. Investors also acknowledge that they have not relied on any Manager in connection with their investigation of the accuracy of this information or their decision whether to invest in the Bonds.

NOTHING IN THIS OFFERING CIRCULAR CONSTITUTES AN OFFER OF SECURITIES FOR SALE IN THE UNITED STATES OR ANY JURISDICTION WHERE IT IS UNLAWFUL TO DO SO. THE BONDS HAVE NOT BEEN, AND WILL NOT BE, REGISTERED UNDER THE U.S. SECURITIES ACT, OR THE SECURITIES LAWS OF ANY STATE OF THE UNITED STATES (“U.S.”) OR OTHER JURISDICTION AND SUCH BONDS MAY NOT BE OFFERED OR SOLD WITHIN THE UNITED STATES OR TO, OR FOR THE ACCOUNT OR BENEFIT OF, U.S. PERSONS (AS DEFINED IN REGULATION S UNDER THE U.S. SECURITIES ACT). NONE OF THE U.S. SECURITIES AND EXCHANGE COMMISSION, ANY STATE SECURITIES COMMISSION OR ANY OTHER U.S. REGULATORY AUTHORITY, HAS APPROVED OR DISAPPROVED THE BONDS NOR HAVE ANY OF THE FOREGOING AUTHORITIES PASSED UPON OR ENDORSED THE MERITS OF THIS OFFERING OR THE ACCURACY OR ADEQUACY OF THIS OFFERING CIRCULAR. ANY REPRESENTATION TO THE CONTRARY IS A CRIMINAL OFFENSE.

The Issuer and the Managers reserve the right to reject any offer to purchase the Bonds, in whole or in part for any reason or no reason and to allot to any prospective purchaser less than the full amount of the Bonds sought by it. The Managers and certain of its affiliates may acquire a portion of the Bonds for their own accounts.

Neither the Issuer nor the Managers can guarantee that the application made to the Budapest Stock Exchange for the Bonds to be listed on the Regulated Market thereof will be approved as of the settlement date for the Bonds or at any time thereafter, and settlement of the Bonds is not conditional on obtaining this listing approval.

Each purchaser of the Bonds will be deemed to have made the representations, warranties and acknowledgements that are described in this Offering Circular under the “*Important notices*” section of this Offering Circular.

The Offering is only addressed to investors in Hungary who are “qualified investors” within the meaning of article 2(1)(e) of the Prospectus Directive, as implemented in Hungary by sections 48 to 51 of Act CXXXVIII of 2007 on Investment Firms and Commodity Exchange Service Providers and the Rules of their Activities (“**Qualified Investors**”) and/or to less than 150 natural or legal persons, other than Qualified Investors per member state and to such other investors in Hungary or such other member states of the European Economic Area where it is possible to do so, in reliance of Regulation S and without the need to publish a prospectus or undertake any other formalities whatsoever under applicable law in reliance on article 3(2) of the Prospectus Directive, to the extent, and only provided that, an investment in the Bonds does not constitute a violation of any applicable law by such investors. In addition, in the United Kingdom, the Offering is directed only at Qualified Investors (x) who have professional experience in matters relating to investments falling within article 19(5) of the Financial Services and Markets Act 2000 (Financial Promotion) Order 2005, as amended (the “**Financial Promotion Order**”) and Qualified Investors falling within article 49(2)(a) to (d) of the Financial Promotion Order and (y) to whom it may otherwise lawfully be directed (all such persons together being referred to as “**relevant persons**”).

Presentation of financial and other information

The unaudited reviewed interim condensed consolidated financial statements of the Issuer’s group for the six-month period ended 30 June 2017 and, respectively, 30 June 2018 (the “**Interim Unaudited Financial**

Statements”) and the audited consolidated financial statements of the Issuer’s group for the years ended 31 December 2016, 31 December 2017 and, respectively, 31 December 2018 (the “**Audited Financial Statements**” collectively with the Interim Unaudited Financial Statements, the “**Financial Statements**”) are attached to this Offering Circular.

The Audited Financial Statements have been prepared in accordance with the International Financial Reporting Standards (“**IFRS**”). Presentation of financial information in accordance with IFRS requires management to make various estimates and assumptions which may impact the values shown in the financial statements and bonds thereto. The actual values may differ from such assumptions. The Interim Unaudited Financial Statements have been prepared in accordance with International Accounting Standard (IAS) 34.

The Financial Statements are presented in EUR, the functional and presentation currency of the Issuer. Furthermore, unless otherwise indicated, financial and statistical data included in this Offering Circular is expressed in EUR million. All financial data on the Issuer are presented on a consolidated basis, unless indicated otherwise.

Unless otherwise stated, all annual information is based on calendar years. Statistical data appearing in this Offering Circular has, unless otherwise stated, been principally obtained from the Eurostat, European Commission, International Monetary Fund, World Bank, Standard and Poor's, Moody's and Fitch. Similar statistics may be obtainable from other sources, although the underlying assumptions and methodology, and consequently the resulting data, may vary from source to source. Certain statistical information relating to 2018 and future periods should be treated as preliminary and any statistical information may be subject to future adjustment.

Certain financial measures are presented in this Offering Circular, including some of the measures presented in “*Description of the Issuer – Risk management*”. Because these measures are not standardized, companies can define and calculate these measures differently and therefore investors are advised not to use these measures for comparing the Issuer’s results with those of other companies or issuers.

Certain figures included in this Offering Circular have been subject to rounding adjustments and presented in EUR million or EUR billion (not in EUR thousand as in the Financial Statements). Accordingly, in certain instances the sum of numbers in a column or a row in tables contained in this Offering Circular may not conform exactly to the total figure given for that column or row. Some percentages in the tables and/or text in this Offering Circular have also been rounded, and accordingly the totals in these tables and/or text may not exactly add up to 100%. Percentage changes during the compared periods were computed on the basis of the original amounts.

Documents incorporated by reference. Website

This Offering Circular should be read and construed in conjunction with the Financial Statements of the Issuer which shall be incorporated in, and form part of, this Offering Circular. Any documents themselves incorporated by reference in the documents incorporated by reference shall not form part of this Offering Circular.

The contents of the Issuer’s websites do not form any part of this Offering Circular. The website is mainly addressed to potential clients of the Issuer’s services and, therefore, information available on the Issuer’s website may differ in content or may be organized differently than information in this Offering Circular. For the purposes of making an investment decision regarding the Bonds, you should not rely on the information on the Issuer’s website.

Cautionary note regarding forward-looking statements

Certain statements in this Offering Circular are not historical facts and are forward-looking. The Issuer may from time to time make written or oral forward-looking statements in reports to shareholders and in other communications. In addition, this Offering Circular includes forward-looking information that has been extracted from third-party sources. Forward-looking statements include statements concerning the Issuer’s plans, expectations, projections, objectives, targets, goals, strategies, future events, future operating revenues or performance, capital expenditures, financing needs, plans or intentions relating to business, competitive strengths and weaknesses, strategy, and the trends the Issuer anticipates in the industries and the political and legal environments in which the Issuer operates and other information that is not historical information.

Words such as “believe”, “anticipate”, “estimate”, “target”, “potential”, “expect”, “intend”, “predict”, “project”, “could”, “should”, “may”, “will”, “plan”, “aim”, “seek” and similar expressions are intended to identify forward-looking statements but are not the exclusive means of identifying such statements.

The forward-looking statements contained in this Offering Circular are largely based on the Issuer’s expectations, which reflect estimates and assumptions made by its management. These estimates and assumptions reflect the Issuer’s management best judgment based on currently known market conditions and other factors, some of which are discussed below. Although the Issuer believes such estimates and assumptions to be reasonable, they are inherently uncertain and involve a number of risks and uncertainties that are beyond the Issuer’s control. In addition, management’s assumptions about future events may prove to be inaccurate. The Issuer cautions all readers that the forward-looking statements contained in this Offering Circular are not guarantees of future performance, and the Issuer does not undertake any obligation and cannot assure any reader that such statements will be realized or the forward-looking events and circumstances will occur.

By their very nature, forward-looking statements involve inherent risks and uncertainties, both general and specific, many of which are beyond the Issuer’s control, and risks exist that the predictions, forecasts, projections and other forward-looking statements will not be achieved. These risks, uncertainties and other factors include, among other things, those listed under “*Risk Factors*”, as well as those included elsewhere in this Offering Circular. You should be aware that a number of important factors could cause actual results to differ materially from the plans, objectives, expectations, estimates and intentions expressed in such forward-looking statements.

This list of important factors and the other factors discussed in “*Risk Factors*” is not exhaustive. Other sections of this Offering Circular describe additional factors that could adversely affect the Issuer’s results of operations, financial condition, liquidity and the development of the industry in which the Issuer operates. New risks can emerge from time to time, and it is not possible for the Issuer to predict all such risks, nor can the Issuer assess the impact of all such risks on its business or the extent to which any risks, or combination of risks and other factors, may cause actual results to differ materially from those contained in any forward-looking statements. Given these risks and uncertainties, investors should not rely on forward-looking statements as a prediction of actual results.

Any forward-looking statements are only made as of the date of this Offering Circular. Accordingly, the Issuer does not intend, and does not undertake any obligation, to update forward-looking statements set forth in this Offering Circular. Investors should interpret all subsequent written or oral forward-looking statements attributable to the Issuer or to persons acting on its behalf as being qualified by the cautionary statements in this Offering Circular. As a result, investors should not place undue reliance on such forward-looking statements.

Currencies

In this Offering Circular, references to "euro," "EUR," "€" or "eurocents" are to the currency of the member states of the European Union participating in the European Monetary Union, references to "U.S. dollar" or "USD" are to the currency of the United States, references to “Hungarian forint” or “HUF” are to the currency of Hungary, references to "RUB" are to the currency of the Russian Federation, references to “CZK” are to the currency of the Czech Republic and references to "RON" are to the currency of Romania.

No representation is made that any specific currency amount in this Offering Circular could have been converted into any of the other currencies presented in this Offering Circular at any particular rate or at all. There are limited markets for the Hungarian forint outside Hungary. The limited availability of such currencies may lead to volatility of exchange rates.

Unless otherwise indicated herein and unless such amounts are derived from the Financial Statements, the EUR equivalent of amounts denominated in RUB, USD, RON and other currencies has been computed based on the average and rounded exchange rate applicable as of 31.12.2018. The above rates may differ from the actual rates used in the preparation of the Financial Statements and other financial information appearing in this Offering Circular.

OVERVIEW OF THE BONDS

The following is only a brief summary of key features of the issue of the Bonds, does not purport to be complete description of the Bonds or the Offering and should be read in conjunction with the rest of this Offering Circular. Certain of the terms and conditions described below are subject to important limitations and exceptions. In particular, prospective investors are advised to consult the “Terms and conditions of the Bonds” section of this Offering Circular for a more detailed description of the terms and conditions governing the Bonds, including definitions of certain terms used in this overview.

Issuer	International Investment Bank <i>7 Mashi Poryvaevoy St., Moscow, 107078, Russian Federation</i>
Managers	OTP Bank Nyrt. <i>Nádor utca 16., 1051, Budapest, Hungary (performing the functions of Joint Lead Manager and joint bookrunner in connection with the Offering)</i> UniCredit Bank Hungary Zrt. <i>Szabadság tér 5-6., 1054, Budapest, Hungary (performing the functions of Joint Lead Manager, joint bookrunner and paying agent in connection with the Offering)</i> <i>(OTP Bank Nyrt. and UniCredit Bank Hungary Zrt. are hereinafter each referred to as a “Manager” and collectively referred to as the “Managers”)</i>
Paying Agent	UniCredit Bank Hungary Zrt. <i>Szabadság tér 5-6., 1054, Budapest, Hungary</i>
Central Depository	KELER Központi Értéktár Zrt. <i>Rákóczi út 70-72., 1074, Budapest, Hungary</i>
Aggregate principal value of the Bonds offered	The aggregate principal value of the Bonds offered is HUF 15,000,000,000 which may (i) increase up to HUF 30,000,000,000 as a result of the Issuer accepting offers in the auction process for Bonds of a higher number than originally offered; or (ii) decrease by any amount to HUF 0 as a result of insufficient demand for the Bonds (see Part “ <i>Subscription and Sale</i> ”).
Denomination	Hungarian forint (HUN)
Form of the Bonds	The Bonds are in dematerialised form. In accordance with paragraph (4) of section 6:573 of the Civil Code and section 7(2) of the Capital Markets Act, the Issuer issues and deposits with the Central Depository a document (the “ Document ”), which does not qualify as a security, with the particulars of the Bonds. The Document will remain to be deposited with the Central Depository, or (if applicable) the Central Depository’s successor, until all claims of the Bondholders under the Bonds will be satisfied.

Nominal Value	HUF 10,000
Issue Date	22 March 2019
Maturity Date	The tenor and the maturity date of the Bonds offered hereunder shall be of three (3) years from the Issue Date.
Issue Price	The issue price of the Bonds will be determined in an auction process (see Part “ <i>Subscription and Sale</i> ”).
Interest Rate	The Bonds shall bear fixed interest rate.
Interest Payment Dates	The Bonds bear interest from and including 22 March 2019 at the rate of 2.0 per cent. per annum, payable annually in arrear on 22 March of each year.
Status and ranking of the Bonds	The obligations under the Bonds will constitute direct, unsecured, unconditional and unsubordinated obligations of the Issuer ranking <i>pari passu</i> among themselves and as to the order of their satisfaction and at least <i>pari passu</i> to all other current and future direct, unsecured, unconditional and unsubordinated obligations of the Issuer, except for those obligations of the Issuer so identified by the mandatory provisions of law and provided, however, that the Issuer shall have no obligation to effect equal or rateable payment(s) at any time with respect to any such other obligations and, in particular, the Issuer shall have no obligation to pay other obligations at the same time or as a condition of paying sums due on the Bonds and/or applicable interest and <i>vice versa</i> .
Redemption	The Bonds shall be redeemed at par on the Maturity Date.
Early redemption at the Issuer’s option	The Bonds may not be redeemed by the Issuer before their respective Maturity Date. However, the Issuer may at any time purchase any Bonds on the secondary market, under any conditions and for any market price. The Bonds thus purchased by the Issuer shall not cease to exist and may be kept, resold or cancelled by the Issuer, at its sole discretion. The rights and obligations under the Bonds purchased by the Issuer shall cease to exist due to their amalgamation in a single person at the earlier of: (i) cancellation by the Issuer and (ii) their respective Maturity Date.
Early redemption upon an Event of Default	Each Bondholder will have the right to declare all Bonds (but not some only) held by that Bondholder immediately due and payable and require the Issuer to pay the Nominal Value of each Bond held by that Bondholder together with any accrued interest, by a written notification to the Issuer, if an Event of Default occurs and is continuing.
No Gross-up	All payments in respect of Bonds will be made free and clear of withholding taxes of Hungary, unless the withholding is required by law. In that event, the Issuer will not pay such additional amounts as may be necessary in order that the net amounts received by the Bondholders after the withholding or deduction shall equal the respective amounts which would have been receivable in respect of the Bonds in the absence of the withholding or deduction.
Taxation	For certain considerations regarding the taxation of payments related to the Bonds see Part “ <i>Taxation</i> ”.
Governing law and jurisdiction	Any rights and obligations (including any non-contractual obligations) arising under or in connection with the Bonds will be governed and construed in accordance with the laws of Hungary. Any disputes which may arise out of or in connection with the Bonds, the issue thereof or

any document created in connection with such issue (including a dispute relating to any non-contractual obligations arising out of or in connection with the Bonds), shall be subject to the exclusive jurisdiction of Hungarian courts.

Listing

The Issuer will apply for the listing of the Bonds on the Regulated Market of the Budapest Stock Exchange. The Issuer may apply for admission of the Bonds to trading on other regulated markets in the European Union.

Use of proceeds

The Bonds will be issued, and the net proceeds of the Offering shall be used by the Issuer, to finance its existing loan portfolio and new lending to its EU Member States and for debt refinancing (see Part “*Description of the Issuer – Mission*” and “*Description of the Issuer – Strategy*”).

Risk factors

Investing in the Bonds involves risk. See Part “*Risk factors*” section for a description of certain of the risks investors should carefully consider before investing in the Bonds.

Selling and transfer restrictions

The Bonds are subject to certain restrictions on sale and transfer. For a description of certain restrictions on offers, sales and deliveries of Bonds and on the distribution of offering materials see Part “*General information – Selling and transfer restrictions*”.

RISK FACTORS

An investment in the Bonds involves a high degree of risk. Prospective investors should carefully consider the risks described below, together with the information contained elsewhere in this Offering Circular, before deciding whether to invest in the Bonds. Any of the following risks, individually or together, could have a material adverse effect on the Issuer's or the Issuer's group's (the "Group") business, financial condition and results of operations or prospects, which could impair the Issuer's ability to fulfil its obligations under the Bonds or the trading price of the Bonds, potentially causing a loss of all or part of the investment made when purchasing the Bonds.

The Issuer has described below certain risks and uncertainties that it believes are material as at the date of this Offering Circular, but these risks and uncertainties may not be the only ones the Issuer or the Group faces. Additional risks and uncertainties relating to the Issuer or the Group may also have adverse effects on the Issuer or the Group's business, financial condition, results of operations and future prospects and, consequently, on the trading price of the Bonds. Any of such risks could impair the Issuer's ability to fulfil its obligations under the Bonds or the trading price of the Bonds, and investors could lose all or part of their investment.

The following risks relate to the Issuer's and the Group's business and the environment in which the Issuer and the Group operate. The order in which the risks are presented does not necessarily reflect the likelihood of their occurrence or the magnitude of their potential impact on the Issuer's or the Group's business, financial condition, results of operations, future prospects or the trading price of the Bonds.

In particular, the Issuer's operations are carried out across a wide region. As an international organisation composed of its Member States, its results of operations are significantly affected by economic conditions in its Member States which may be, in turn, adversely affected by the global financial and European sovereign debt crises and remain vulnerable to further external shocks.

Investors should consider carefully whether an investment in the Bonds is suitable for them and determine for themselves the relevance of the information contained in this Offering Circular. Any investment in the Bonds should be based upon individual investigation, assessment of the risks involved and determination of the suitability of an investment in the Bonds, by each prospective investor, with particular reference to its own investment objectives and experience and any other factors that may be relevant to such investor in connection with the investment in the Bonds.

Risk factors related to the Issuer and its Group

Risks related to global events in financial and economic markets

Social and economic disruptions stemming from the crises in Europe have affected in the past and may affect in the future the geographic market in which the Issuer operates (see "*Description of the Issuer – Relevant Geographic Markets*"). Such crises may result in a downturn and decrease in spending and investment in the relevant markets, potentially leading to an increase in costs due to currency fluctuations and legal and regulatory changes. These factors could increase the Issuer's operating costs or otherwise adversely affect the Issuer's business, prospects, results of operations and financial condition.

In particular, the reduction in recent years quantitative easing and the exit from the era of ultra-low interest rates in the Eurozone may lead to spill-over effects for some of the Issuer's key markets, notably the five EU countries in Central and Eastern Europe. These countries are an intrinsic part of the European supply chain as well as a major recipient of financial flows coming from core European Union countries. Higher interest rates in the Eurozone may negatively impact both the economic growth of core Europe countries (Germany, France, Netherlands etc.) and thus spill over into the Central and Eastern European region as well as more directly through higher interest rates in the Central and Eastern European region as financial fund flows return to core Europe.

An additional risk is any potential for a trade war that could cause a restructuring of global supply chains and thus it may negatively impact the growth potential of the Central and Eastern European region. Many of the Issuer's operating countries are open economies with a large share of exports to GDP and in the event of slowdown in global trade this would negatively impact the growth dynamics of these countries.

Another event which has spurred significant volatility in the global financial markets is the vote cast in the United Kingdom referendum in favour of United Kingdom's exit from the European Union. Concerns that other member states of the European Union may express their intention to leave the European Union have also been amplified by the results of the United Kingdom referendum. Until the legal, political and economic terms and consequences of United Kingdom's exit from the European Union are settled, it is likely that the situation is likely to continue to adversely affect European and worldwide economic conditions.

Prospective investors should ensure that they have sufficient knowledge and awareness of global financial and economic developments, the crises faced by the European Union and the economic situation and outlook in the states in which the Issuer operates, or whose economical or financial situation may otherwise impact the Issuer, as they consider necessary to enable them to make their own evaluation (including in consultation with any tax, legal and financial advisors as it deems necessary) of the risks and merits of an investment in the Bonds. In particular, prospective investors should take into account the current uncertainty as to how the crises faced by the European Union and the wider global economic situation will develop over time and how they will affect the Issuer's financial condition, as well as its business, prospects and results of operations.

Risk related to the operations in emerging markets in general

An investment in emerging markets, such as some of the Member States of the Issuer, being the respective jurisdictions of the Issuer's Member States in which a significant part of its business is undertaken and its customers and assets are located, is subject to greater risks, including in some cases significant legal, economic and political risks, than an investment in more developed markets. Investors should be aware that these risks may be applicable to the Issuer notwithstanding that its status as an international organisation affords it certain privileges, immunities and political protection. Investors should also note that emerging markets are subject to rapid change and that the information set out in this Offering Circular may become outdated relatively quickly.

In addition, international investors' reactions to events occurring in one country sometimes demonstrate a "contagion" effect, in which an entire region or class of investment is disfavoured by international investors. Therefore, investment in the Bonds, as in any other comparable security, could be adversely affected by negative economic or financial developments in other countries, particularly its Member States. There also can be no assurance that conditions resulting from any crises similar to the global financial and economic crisis that started in 2008, the European sovereign debt crisis or the recent social and political turmoil in Europe, the Middle East and Africa and disruption in European financial markets caused by the United Kingdom's envisaged exit from the European Union will not negatively affect the economic performance of, or investor confidence in, developing markets, including the Member States and, hence, the Bonds.

Deterioration of Russia's relations with other countries may adversely impact the Issuer's operations and financial condition

The Issuer is a supranational multilateral development bank with nine sovereign shareholders. Therefore, the Issuer is measured and rated in the context of the specific country risks and credit ratings of its sovereign members. The Issuer's mission is to facilitate connectivity and integration between the economies of its Member States in order to ensure sustainable and inclusive growth, competitiveness of national economies, backed by the existing historical tie" and to this end the Issuer maintains a political impartiality.

In this context, the recent crisis in Ukraine and responses by the EU, the United States, and other countries to the Russian Federation's actions relating to Ukraine create significant political and economic uncertainty, which could adversely impact the Group's business and financial condition.

The significant civil unrest and political instability in Ukraine has affected the relations between the Russian Federation and other countries. In March 2014, the European Union (EU) and United States (U.S.) enacted sanctions against Russia in response to its actions in Crimea and support for groups in eastern Ukraine.

The foregoing events have resulted, and may result in the future, in significant volatility on Russian stock exchanges and the securities of Russian issuers traded on foreign exchanges, significant overall price declines and capital outflow, and significant volatility in the exchange rate of the RUB against the USD and the EUR. These and other sanctions, restrictions or other measures may result in a further deterioration of economic conditions in the Russian Federation.

The Issuer is an international organisation which is directly exempted from the sanctions imposed by the Council Regulation (EU) 833/2014 of 31 July 2014 concerning restrictive measures in view of Russia's actions destabilising the situation in Ukraine

Another recent point of tension and debate between Russia and Western governments has been the Russian role in the Syrian crisis and its support for the Syrian Government.

This conflict still remains an inflection point in Russia's relationship with Western countries, with the U.S., the European Union and a number of other states voicing the possibility of sanctions to be imposed on Russia in case it decides to increase its profile in the Syrian conflict.

To the extent the Issuer (although being a self-standing international organisation) is perceived as having a strong connection to the Russian Federation and since the Issuer is directly and indirectly financially exposed to entities in the Russian Federation, a downturn in general economic conditions in the Russian Federation and other Member States as a result of the Ukraine-related sanctions and/or the ongoing conflict between the Russian Federation and Ukraine could have a material adverse effect on the Group's business, results of operations, financial condition or prospects. Ongoing or heightened tensions between Russia and the United States, member states of the EU, Ukraine or other countries, the imposition of further sanctions on Russian persons and entities, or the impact of actions taken by the Russian government in response to actions by the United States, EU and other governments, could have a further adverse effect on the Russian economy and consequently, could have an adverse effect on the Group's business, financial condition, results of operations and prospects. However, the diverse shareholding of the Issuer and its strategy of diversification its treasury assets, source of funding and lending portfolio has reduced significantly the idiosyncratic effects of negative consequences derived from various exogenous factors such as sanctions this being proved by the developments of the Issuer financials in the latest years as well as the recent rating upgrades from Standard and Poor's, Moody's (both in April 2018) and Fitch (in November 2018) in the context of a set of sanctions applied by US on Russian individuals in April 2018. Therefore, IIB's ratings and outlook was decoupled from the rating or developments in a market of a specific Member State (such as in the case Russia). Moreover, the strategic decision taken in Varadero by IIB's Board of Governors regarding the relocation of IIB's headquarter from Moscow to Budapest is seen as credit and rating positive by both Fitch and Moody's as they underlined it in their public releases made in November 22nd and respectively December 12th 2018.

Credit risk faced by the Issuer in general

The Issuer's business exposes it to credit risk. The quality of the Issuer's credit exposures will have a significant impact on its earnings. While the Issuer estimates and establishes allowances for losses resulting from credit risks and expected credit losses inherent in its credit exposure, in accordance with IFRS, there is no assurance that the models and techniques used by the Issuer prove accurate in their predictions of future behaviour, valuations or estimates, particularly considering the uncertainty associated with current financial and economic market conditions. Any failure by the Issuer to accurately assess the creditworthiness of its clients or to estimate the value of potential losses for which allowances should be established could result in increased default rates of the Issuer's clients, adversely impacting the Issuer's cash flow and, potentially, its ability to comply with the obligations under its own borrowings.

As a result of the current economic uncertainty, the demand for borrowing from creditworthy customers may decline. In addition, there is a greater likelihood that more of the Issuer's customers or counterparties (including other financial institutions) could become delinquent on their loans or other obligations to the Issuer, which, in turn, could result in a higher level of write-offs and provisions for credit losses or requirements that the Issuer purchase assets or provide other funding, any of which could adversely affect the Issuer's and its customers' business, prospects, financial condition, cash flows and results of operations.

The Issuer is building a track record of low and sustainable NPL levels (< 6%) following its relaunch in 2012, fact that is one of the pillars of the recent positive rating actions by the international rating agencies.

Credit risk due to lending concentration

For the purpose of achieving the Issuer's mission, which is to ensure sustainable and inclusive growth of the Member States, the Issuer's loan and trading portfolio includes, and is likely to continue to include, concentrations in particular Member States. Also, as at 31 December 2018, the Issuer had corporate gross loan portfolio in the amount of EUR 593.25 million, out of which 17% was provided to corporate clients based in the Russian Federation, 23% to corporate clients based in the Republic of Bulgaria, 15% to corporate clients based in Romania, 6% to corporate clients based in Hungary, 15% to corporate clients based in Slovak Republic, 5% to corporate clients based in Mongolia and 19% to corporate clients based in other countries.

In terms of sector concentration, as at 31 December 2018, 21% out of the Issuer's gross loan portfolio to corporate clients was provided to corporate clients active in the leasing industry and 31% to corporate clients active in the production and transmission of electricity, 8% was provided to clients active in communications, 5% to clients active in each of crude oil refining and wholesale and retail trade, 4% to clients active in each of food and beverage, financial services and mining, 3% to clients active in real estate industry, 2% to clients active in production of each of pharmaceutical products, agriculture, manufacturing of electrical equipment and oil and gas production industries.

Concerning the Issuer's portfolio of loans extended to banks, loans granted to top six bank clients are concentrated. As at 31 December 2018, the outstanding value of each of the loans extended by the Issuer to five bank clients exceeded 10% of the aggregate gross value of the Issuer's portfolio of long-term loans to banks and trade financing loans. As at 31 December 2018, the Issuer's exposure to such major bank clients amounted to EUR 148.6 million out of the total EUR 176.6 million long-term loans extended by the Issuer to banks. As at 31 December 2018, 27% of the long-term loans provided to banks are banks based in Mongolia, 28% to banks based in Republic of Cuba, 14% to banks based in Vietnam and 31% in the other countries.

The concentration may result in an adverse impact on the business, prospects, financial condition, cash flows and results of operations of the Issuer if short-term economic changes particularly affect its largest customers, or its customers in the countries or business sectors to which its loan portfolio is concentrated and exposed. As a result, the Issuer is potentially subject to high credit risk concentration and earnings volatility.

Foreign exchange rate risk and interest rate risk

The Group conducts its business in various currencies including EUR, USD, RUB, RON, HUF, CZK and CNY. As a financial institution, the Issuer is exposed to foreign exchange rate risk. Movements in foreign exchange rates may adversely impact the Issuer's borrowers, which may in turn adversely impact the nature of its exposure to these borrowers.

The Issuer manages its currency risk by seeking to match the currency of its assets with that of its liabilities on a currency-by-currency basis within the limits established by the Board. The Issuer is running a prudent open currency position, having set open currency position limits at 10% for single currency position and 15% for a cumulative currency position. The factual results are comfortable well within the established limits at 0.48% of the capital for a single currency position and 0.71% for a cumulative currency position as of 31 December 2018,

The performances of the Issuer are influenced by the trend and by the fluctuation in interest rates in the markets in which the Issuer carries out its activities. Any misalignment between interest incomes accrued by the Issuer and interest expense payable by the same (in the absence of suitable instruments for protecting against this misalignment), could have significant effects on the financial position and the Issuer's operating results.

Even though the Issuer has implemented certain hedging strategies, the hedging arrangements entered into by the Issuer may not adequately offset the risks of foreign exchange rate fluctuations and may result in losses. Volatility in foreign exchange rates and interest rates could adversely affect the Issuer's ability to meet its obligations under the Bonds and its business, financial condition and results of operations. Movements in interest rates may also affect the trading prices of the Bonds.

Market risk in connection with the investment portfolio

As of 31 December 2018, consolidated securities at fair value through other comprehensive income (2017: available-for-sale securities) balance of the Group was EUR 204.3 million. Since 1 January 2018, the Group reclassified a part of its securities previously classified as 'available for sale' to 'debt instruments measured at amortized cost' amounted EUR 41.5 million as of 31 December 2018. The majority of the portfolio is composed

of sovereign bonds denominated in EUR and USD. Government bonds account for 20% of the portfolio and represent securities issued and guaranteed by governments of Member States and by governments of other countries. Corporate bonds, mainly issued by large companies and banks of Member States, as well as international companies and development banks that have similar goals and missions with the Group, account for 79% of the portfolio. As a significant part of the Group's business is generated by trading activities relating to this portfolio, which is susceptible to market fluctuation and price volatility, prospects of the Group may be impaired by its ability to further finance this portfolio or to regain its investments. Market price fluctuations in the large investment security portfolio may therefore materially and adversely affect the Group's business, financial condition, results of operations and prospects. As of 31 December 2018, investment grade bonds represented 63% (including AAA-BBB-) of the total Issuer's debt securities portfolio. The weight of A-AAA assets in the portfolio under the Treasury rule had increased by 11% from 40% as of 31 December 2017 to 51 as of 31 December 2018.

Changes to IFRS for recognition and measurement methods for financial instruments

The adoption of IFRS 9 fundamentally changes the Group's accounting for allowances for expected credit losses by replacing the IAS 39 incurred loss approach with the forward-looking expected credit loss ("ECL") approach. Starting from 1 January 2018, the Group recognizes the allowance for ECL for all loans and other debt financial instruments not measured at fair value through profit or loss, as well as for loan commitments and financial guarantee contracts, which are collectively referred to as financial instruments in this section. According to IFRS 9, requirements for impairment are not applicable to equity instruments.

The allowance for ECL is based on credit losses expected to be incurred over the life of the underlying asset (lifetime ECL), if there has been a significant increase in credit risk since the date of initial recognition. Otherwise, the allowance for ECL is based on 12-month expected credit losses, which are part of lifetime ECL and represent ECL arising from defaults on a financial instrument expected to occur 12 months after the reporting date.

The Group has established a policy to perform an assessment, at the end of each reporting period, of whether a financial instrument's credit risk has increased significantly since initial recognition, by considering the change in the risk of default occurring over the remaining life of the financial instrument. Based on the above, the Group classifies financial instruments issued and exposed to credit risk into 3 stages, stage 3 being correspondent to credit-impaired financial instruments. If the Group does not have reasonable expectations regarding recoverability of the financial asset in full or in part, the gross carrying amount of the asset should be decreased. Such a decrease is considered (a partial) derecognition of the financial asset.

The Group uses a wide range of forecast information as economic inputs for its ECL assessment models. Impairment losses and their reversal are accounted for and recorded separately from gain or loss from modification recognized as an adjustment to the gross carrying amount of financial assets.

The Group considers an increase in the credit risk related to a financial asset since the date of its initial recognition to be significant, if credit quality of a counterparty has deteriorated significantly and there are grounds to believe that this deterioration can adversely affect the counterparty's ability to meet its liabilities to the Group. In addition, the Group applies a qualitative tool to identify a significant increase in credit risk associated with an asset, e.g. a list of defaulting customers / non-performing instruments or asset restructuring.

Regardless of changes in ratings, an increase in credit risk since the date of initial recognition is considered significant, if significant negative signals are observed, contractual payments are over 30 days past due is the last moment of asset deterioration recognition.

For ECL calculation purposes, the Group considers the financial instrument to be in default, and, therefore, includes it in Stage 3 (credit-impaired assets) in case of significant negative signals of Borrower's inability to meet its obligations is observed, however 90 days past due is the last moment of asset recognition as NPL. In case of treasury or interbank transactions, the Group considers that there is a default and takes prompt remedy measures whenever the counterparty fails to make intraday payments required by specific agreements before the end of an operating day and the Group has no grounds to believe that this non-payment was a technical delay.

The Group estimates on an individual basis the ECL for all assets included in Stage 3.

This changes to financial reporting standard could however, result in substantial additional impairment charges for the Group and add volatility to its financial results. These and any other changes to IFRS that may be proposed in the future could have a material adverse effect on the Issuer's financial condition and results of operations.

The Issuer has limited operational history

Although the Issuer was founded in 1970, its post-Soviet operating history is relatively limited. The Issuer has adopted a new development strategy at the end of 2012 with an overall objective of transforming it into a modern international development bank. Most of the loans extended before 2012 were impaired and written off or sold in 2013. New risk management system and policies, as well as international standards such as the IFRS and Basel II were approved by the Council of the Issuer (supreme governing body, consisting of representatives of the Member States) and implemented only relatively recently at the level of the Issuer. As a result of the Issuer's renewed strategy implemented as of 2013 and the reinvigoration of the Issuer's activity, during the past two financial years (as at 31 December 2018 compared to 31 December 2016), the Issuer's net loan portfolio grew by 107%, whereas the Issuer's investment securities portfolio registered a 24% decrease. As of June 2017, the Issuer has reviewed and reinforced its development strategy, aiming at doubling its assets and loan portfolio within a five-year horizon, while transforming into an advanced, rapidly expanding and financially sustainable multilateral development bank.

Prospective investors may therefore base their evaluation of an investment in the Bonds on a limited operating history of the Issuer. There can be no assurance that the Issuer will be successful in implementing its business strategy in the future or that its business will continue to grow at a similar or comparable rate, and any failure to do so could have a material adverse effect on its business, prospects, financial condition, cash flows and results of operations.

Profitability is not a key driver for the Issuer

The Issuer's lending and investment activities are aimed at supporting development projects in the Member States. As for other multilateral development banks, profitability is not the key driver for Issuer. Also, operations in some of the Member States in some type of projects may involve lower rate of returns than other purely commercial lending entities would expect or demand. Profitability of the investment projects does not, therefore, represent the Issuer's main objective and may remain low despite the expected rise in the interest income as the loan portfolio grows. As a result, although the Issuer has implemented robust risk management and credit approval systems, future profitability may be restrained owing to the nature of the Issuer's development lending business, which in turn may have a negative impact on the financial conditions and prospects of the Issuer.

Withdrawal of a Member State may adversely affect the Issuer's financial condition and operations

The Issuer's Statutory Documents provide that any Member State may withdraw its membership by giving the Issuer a written six months' notice to that effect. The outstanding rights and obligations including with regard to withdrawal of contributed capital are subject to and shall be governed by the provisions of the Statute and the relevant decisions of the Board of Governors. Poland and Hungary withdrew from the Issuer in 1999 and 2000 respectively, but due to the absence of a clear procedure of a Member State's withdrawal that would apply then, a final decision concerning the settlement of their rights and obligations with the Issuer was delayed and made by the Issuer's Council only in 2012. A new withdrawal procedure may be approved in the future by the Board of Governors but the relevant provisions of the statutory documents provides with detailed withdrawal procedure which leave very few issues to further specify in the separate document.

The withdrawal of a Member State may adversely affect the Issuer's capital and financial condition, as well as its business, prospects and results of operations.

Hungary re-joined the Issuer in 2015, after having previously decided to terminate its membership in the Issuer in 2000. The Issuer's Council approved Hungary's request to re-join the Issuer in November 2014 and Hungary ratified its membership in the Issuer and finalized all necessary procedures to obtain full voting rights in the Issuer in May 2015.

Conditions and actions of Member States may affect the Issuer

Although the Issuer is an international organisation having a legal personality separate from its Member States, the Issuer and its business operations may be affected by decisions of the Member States in their relations with other nations. The Issuer's operations are also subject to risks resulting from political and economic uncertainties, default under obligations and downturns in the economies of Member States as well the policies (such as

monetary and financial) approved or pursued by Member States. The currently ongoing migrant crisis faced particularly, as of 2015, by European Member States of the Issuer also adds to civil tensions and political uncertainty within certain Member States of the Issuer. These decisions and circumstances may result in adverse effects on the Issuer and the business environment in which the Issuer and its counterparties operate, including the reduction or cessation of commercial activity by private counterparties as the result of perceived increases in operational risk, or more formal actions by countries or international organisations to limit or preclude business activity by their nationals or organisational participants with the Issuer or in the areas in which the Issuer operates.

No assurance can be given that such decisions and circumstances will not adversely affect the creditworthiness of borrowers and increase the Issuer's funding costs, and accordingly, adversely affect the Issuer's business, prospects, financial condition, cash flows and results of operations.

The Bonds are not guaranteed by any sovereign

The Issuer currently has nine members, namely: Czech Republic, Hungary, Mongolia, Republic of Bulgaria, Republic of Cuba, Romania, Russian Federation, Slovak Republic and Socialist Republic of Vietnam (the "**Member States**").

Although the Member States are sovereign states, the Issuer is a legal entity which is separate from the governments of its Member States and the agencies of such governments. The Bonds, interest or other amounts due or to become due in respect of the Bonds, constitute obligations solely of the Issuer and do not constitute the obligation of, nor are they guaranteed or insured by, the Russian Federation, Hungary or any other Member State or sovereign entity or agency thereof. However, it should be noted that beyond its regular equity the Issuer is benefiting by the so-called callable capital (amounting currently to Euro 798.5 million). This is an additional source of capital that could be called/used by the Issuer in case there is a default risk related to the payment of its debt service.

The Issuer is not subject to external regulatory oversight and, therefore, may choose to discontinue the application of international standards

The Issuer is an international organisation established and operating on the basis of the intergovernmental Agreement on the Establishment of the International Investment Bank of 10 July 1970, (the "**Establishment Agreement**") and the Statutes of the International Investment Bank attached to the Establishment Agreement (the "**Statutes**", together with the Establishment Agreement, the "**Statutory Documents**"), initially registered with the Secretariat of the United Nations on 1 December 1971 under number 11417. In May 2014, the Members have adopted the Protocol Amending the Agreement Establishing the International Investment Bank and its Charter, which after ratification by all Member States entered into force on 18 August 2018.

The Issuer is an entity acting under the rules, and subject to the provisions of the public international law. The Issuer's existence, powers, privileges, immunities, liabilities and operations are subject to and governed by the Statutory Documents.

In principle, due to its status as international organisation, the Issuer is not subject to regulation by any Member State and, therefore, exempt from the external regulatory oversight to which similar domestic financial institutions established in its Member States are subject. All policies and procedures approved by the governing bodies to govern the Issuer's internal operations in accordance with international standards, such as Basel II standards and International Financial Reporting Standards (IFRS), have been adopted by the Issuer on a voluntary basis and the Issuer has no obligation to continue to apply such standards, undergo a verification of the application of such standards or update its policies or practices in line with any amendments to such international standards. There is no assurance that, if the Issuer chooses to discontinue the application of such standards in order to pursue its mission and objectives in a different manner or by reference to other standards, the operations, business or prospects of the Issuer would remain unaffected.

The Group's ability to raise additional financing is in part dependent on the Issuer's credit ratings

The Group's ability to access the capital markets and other forms of financing (or refinancing), and the costs connected with such activities, depend in part on the Issuer's credit ratings. As at the date of this Offering Circular,

the Issuer has a long-term foreign currency issuer default rating of A3 with stable outlook by Moody's, BBB+ with a stable outlook by Fitch, A- with a stable outlook by S&P and A with a positive outlook by Dagong.

The Issuer's ability to maintain its current rating is dependent on a number of factors, some of which may be beyond its control, such as credit ratings and soundness of policies of its Member States. Particularly in the event that the Issuer's credit rating is lowered by Fitch, Moody's and/or S&P and falls into the sub-investment grade range or such rating is withdrawn, the Issuer's ability to access credit and bond markets and other forms of financing (or refinancing) could be limited. This could have an adverse effect on its business, results of operations and financial condition, as well as the trading price of the Bonds.

A credit rating is not a recommendation to buy, sell or hold securities and may be subject to suspension, reduction or withdrawal at any time by the assigning rating agency.

A malfunction, disruption or insufficient maintenance of the Group's IT systems may have material negative consequences for the Group

In the process of building and managing the IT infrastructure, the Group is guided by international practices and standards (i.e., *ITIL 3.0, ISO/IEC 27001:2005, ISO/IEC 27002:2005, ISO/IEC 27005:2011*). Several measures aiming to reduce the operational risks associated with (i) the "human factor" (i.e., enforcement of internal normative documents, organizational measures and automated control tools and change management), (ii) the failure of equipment (i.e., clustering of critical systems, including communication channels, complete back up of all data and settings to a remote server site in Bratislava and entering contracts with extended warranty and technical support from the manufacturers) and (iii) occurrence of incidents of information security breaches (for example, organizational and technical access control mechanisms using 2-step authentication and the use of specialized information leakage monitoring - DLP (Data Loss Prevention System), are in place.

However, the Group may be exposed to IT risks in connection with the development, implementation and application of its IT systems. In addition, there is a risk that there might be unauthorised access to the Group's sensitive data by third parties and improper use of such data, which may lead to the loss of company secrets and may result in a breach of applicable data protection regulations. As a result, any malfunction, breach or unauthorised use of the Group's IT systems may have a material adverse effect on the Group's business, financial condition, prospects or results of operations.

The Issuer is reliant upon skilled managers and personnel and may not be able to recruit and retain qualified personnel

Since the Issuer's relaunch in late 2012, there has been a significant renewal of the Issuer's personnel. Currently the Issuer's staff consists of highly qualified specialists, professionals in their respective field. In hiring process the Issuer uses modern recruitment methods and instruments, which helps to identify the best of the best during an open international competition.

Nowadays the Issuer's international team consists of representatives of such countries as the Republic of Bulgaria, Hungary, Mongolia, Romania, the Slovak Republic, the Russian Federation, the United Kingdom and the Republic of Belarus. At the same time, proportion of international personnel on the management level reaches 29%, and in the Management Board - 60%.

The loss of any of these key individuals could to some extent impede our financial plans, product development, network expansion, marketing and other plans. The Issuer's future results will depend, in a significant part, upon the continued contributions of its existing management and its ability to expand the personnel team by adding highly skilled new members. If any of the Issuer's management members or other key individuals ceases their employment or engagement, the Issuer's business, prospects, results of operation and financial condition could be materially affected.

In autumn 2017 the Chairman of the Board was unanimously re-elected for a new 5 year mandate.

At the 1/110th meeting of the Board of Governors, the Key Principles of Management Board Composition (Key Principles) were adopted, ensuring the transition to modern international corporate governance standards.

Before the Key Principles came into force, the practice of appointing Board members was based on a quota system and rotation principle. The Board members were appointed by the Council of the Bank from among citizens of member states presenting their candidates.

Adopted Key Principles provide a merit-based approach. The Management Board is formed on a competitive basis in line with the generally accepted standards of corporate governance, as the efficiency of the IIB's operations hinges on the work of this body. The HR and Compensations Committee under the Board of Directors has the key role in selection of candidates for vacant positions of the members of the Management Board. It performs an independent assessment of the candidates' level of qualification and formulates recommendations for the Board of Governors concerning the candidates.

To ensure a balanced and transparent system of decision-making at the level of the Management Board Principles establish the fair country representation according to which the Management Board shall include citizens of at least four Members of the Bank. At the same time all the members of the Management Board have the right to vote.

The legal infrastructure and the law enforcement systems in the Member States are less developed compared to Western Europe

The legal infrastructure and the law enforcement systems in the Member States are less developed when compared to western European countries. In some circumstances, it may not be possible to obtain legal remedies to enforce contractual or other rights in a timely manner or at all. Although institutions and legal and regulatory systems characteristic of parliamentary democracies are developed or have begun to develop in the Member States, the lack of an institutional history remains a problem. As a result, shifts in government policies and regulations tend to be less predictable than in countries with more developed democracies. A lack of legal certainty or the inability to obtain effective legal remedies *vis-a-vis* its borrowers or other counterparties in each Member State in a timely manner or at all may have a material adverse effect on the Group's business, results of operations or financial condition.

In addition, in Hungary, the courts of which shall have jurisdiction over the disputes in connection with the Bonds, there may be fewer judges specialised and experienced in complex matters involving investments in securities when compared to judges in western European countries. The risk may be more significant in cases which needs to be brought before courts of certain other Member States, *e.g.* in connection with enforcement proceedings in the local jurisdiction of a Member State. Investors should therefore be aware that matters brought before the Hungarian courts or the courts of other Member States may be subject to delays and may not be conducted in a manner similar to more developed legal systems and may, as a result, lead to delays in proceedings or losses on the Bonds.

The enforcement of judgments against the Issuer and its assets is subject to limitations and procedural rules

The Bonds are governed by the Hungarian law and any disputes arising out of or in connection with this Offering Circular are subject to jurisdiction of the Hungarian courts. Hungary is a member state of the EU and judgments rendered by Hungarian courts are generally enforceable in other member states of the EU. Claims brought by investors in a different EU Member State will be subject, *inter alia*, to the European Union conflict of laws rules included in the Regulation (EU) No 1215/2012 of the European Parliament and of the Council of 12 December 2012 on jurisdiction and the recognition and enforcement of judgments in civil and commercial matters and shall be enforceable in accordance with it.

Assets of the Issuer are, however, located in several of its Member States, mainly the Russian Federation and other non-EU Member States. Presence of the financial and other assets outside of the EU may limit an investor's legal recourse against the Issuer. Enforcement of Hungarian and other EU Member States' civil judgments in the territory of non-EU Member States may be subject to existence of relevant international treaties and international law and, mainly, their respective observance by the relevant state authorities and local procedural rules.

In addition, although the Issuer has waived its immunity against legal proceedings in the terms and conditions of the Bonds, any legal actions against the Issuer may be limited by the relevant international treaties on diplomatic and intergovernmental protection as well as principles of public international law. Several of the Issuer's assets, such as its headquarters which enjoys diplomatic privileges of an embassy may therefore be considered outside of the reach of civil courts' jurisdiction.

Furthermore, Hungarian courts are not familiar with the concept of insolvency of institutions of public international law, and consequently the procedure for, and enforcement of payment under, the Bonds in such circumstances is uncertain.

Risk factors related to the Bonds and market in general

The Bonds may not be a suitable investment for all investors

Each potential investor in the Bonds must determine the suitability of that investment in light of its own circumstances. In particular, each potential investor should:

- (i) have sufficient knowledge and experience to make a meaningful evaluation of the Bonds, the merits and risks of investing in the Bonds and the information contained or incorporated by reference in this Offering Circular or any applicable supplement;
- (ii) have access to, and knowledge of, appropriate analytical tools to evaluate, in the context of its particular financial situation, an investment in the Bonds and the impact the Bonds will have on its overall investment portfolio;
- (iii) have sufficient financial resources and liquidity to bear all of the risks of an investment in the Bonds, particularly where the currency for principal or interest payments is different from the potential investor's currency;
- (iv) understand thoroughly the terms of the Bonds and be familiar with the behaviour of any relevant indices and financial markets; and
- (v) be able to evaluate (either alone or with the help of a financial adviser) possible scenarios for economic, interest rate and other factors that may affect its investment and its ability to bear the applicable risks.

There may not be an active trading market for the Bonds

The Bonds are new securities which may not be widely distributed and for which there may not be an active trading market. If the Bonds are traded after their initial issuance, they may trade at a discount to their initial offering price, depending upon prevailing interest rates, the market for similar securities, general economic conditions and the financial condition of the Issuer. Although application was made for the Bonds to be listed on the Regulated Market of the Budapest Stock Exchange, there is no assurance that such application will be accepted or that an active trading market will develop. Accordingly, there is no assurance as to the development, maintenance or liquidity of any trading market for the Bonds. Illiquidity may have a severely adverse effect on the market value of the Bonds.

As a result of the above factors, investors may not be able to sell their Bonds easily or at prices that will provide them with a yield comparable to similar investments that have a developed secondary market.

Inability to list the Bonds on the Budapest Stock Exchange

The listing of the Bonds on the Regulated Market of the Budapest Stock Exchange requires the approval of the Budapest Stock Exchange for such purpose. The listing of the Bonds on the Regulated Market of the Budapest Stock Exchange is subject to certain requirements. The Issuer intends to take all necessary steps to ensure that the Bonds will be listed on the Regulated Market of the Budapest Stock Exchange as soon as possible after the closing of the Offering. There is no guarantee that, should the requirements for the approval by the Budapest Stock Exchange change, all such trading conditions will be met. Consequently there is no assurance that the Bonds will be listed on the Regulated Market of the Budapest Stock Exchange on the estimated date or at all.

The Bonds do not limit incurrence of additional indebtedness

The Terms and Conditions of the Bonds do not restrict the ability of the Issuer to incur additional indebtedness or require the Issuer to maintain financial ratios or specified levels of net worth or liquidity. In fact, the Issuer intends to raise funds and thus incur addition indebtedness including by way of issuing other debt instruments. If the

Issuer incurs additional indebtedness in the future, these higher levels of indebtedness may adversely affect the Issuer's creditworthiness generally and its ability to pay principal of and interest on the Bonds.

Taxation

Potential investors should be aware that they may be required to pay taxes or other documentary charges or duties in accordance with the laws and practices of the country where the Bonds are transferred or other jurisdictions. In some jurisdictions, no official statements of the tax authorities or court decisions may be available for innovative financial instruments such as the Bonds.

Potential investors are advised not to rely upon the tax summary contained in this Offering Circular but to ask their own tax adviser's for an advice on their individual taxation with respect to the acquisition, holding, sale and redemption of the Bonds. Only these advisors are in a position to duly consider the specific situation of the potential investor. The aforementioned individual tax treatment of the Bonds with regard to any potential investor may have an adverse impact on the return which any such potential investor may receive under the Bonds.

Change of law

The Terms and Conditions of the Bonds are governed by the laws of Hungary in effect as at the date of issue of the Bonds. No assurance can be given as to the impact of any possible judicial decision or change to the laws of Hungary, or administrative practice after the date of this Offering Circular.

Exchange rate risks

The Issuer will pay principal and interest on the Bonds in HUF. This presents certain risks relating to currency conversions if an investor's financial activities are denominated principally in other currency. These include the risk that exchange rates may change significantly (including changes due to devaluation of HUF or revaluation of the investor's currency) and the risk that authorities with jurisdiction over the investor's currency may impose or modify exchange controls. An appreciation in the value of the investor's currency relative to HUF would decrease (i) the investor's currency-equivalent yield on the Bonds, (ii) the investor's currency-equivalent value of the principal payable on the Bonds and (iii) the investor's currency-equivalent market value of the Bonds.

Government and monetary authorities may impose exchange controls that could adversely affect an applicable exchange rate. As a result, investors may receive less interest or principal than expected, or no interest or principal.

Risks related to interest rate

The Bonds will bear a fixed interest rate. Investment in fixed rate Bonds involves the risk that subsequent changes in market interest rates may adversely affect the value of the Bonds.

Credit ratings may not reflect all risks

As of the date of this Offering Circular, the Issuer is rated A3 with stable outlook by Moody's, BBB+ with stable outlook by Fitch, A- with a stable outlook by S&P and A with positive outlook by Dagong. The Issuer may apply for the assignment of a credit rating by one or more independent credit rating agencies. These credit rating agencies may assign other credit ratings to the Issuer or to the Bonds. The ratings may not reflect the potential impact of all risks related to structure, market, additional factors discussed above and other factors which may affect the value of the Bonds. A credit rating is not a recommendation to buy, sell or hold securities and may be revised or withdrawn by the rating agency at any time.

Transferability of the Bonds may be limited under applicable securities laws

The Bonds have not been and will not be registered under the Securities Act or the securities laws of any state of the United States or any other jurisdiction (other than Hungary). The Bonds may be subject to restrictions on transfer in certain jurisdictions. Each purchaser of Bonds will be deemed, by its acceptance of such Bonds, to have made certain representations and agreements intended by the Issuer to restrict transfers of Bonds as described under "*Subscription and sale*". It is the obligation of each purchaser of Bonds to ensure that its offers and sales of Bonds comply with all applicable securities laws.

Legal investment considerations may restrict certain investments

The investment activities of certain investors are subject to legal investment laws and regulations, or review or regulation by certain authorities. Each potential investor should consult its legal advisers to determine whether and to what extent (i) Bonds are legal investments for it, (ii) Bonds can be used as collateral for various types of borrowing and (iii) other restrictions apply to its purchase or pledge of any Bonds. Financial institutions should consult their legal advisors or the appropriate regulators to determine the appropriate treatment of Bonds under any applicable risk-based capital or similar rules.

Reliance on Budapest Stock Exchange and the Central Depository

A holder of a Bond must rely on the procedures of the Budapest Stock Exchange and the relevant clearing system to effect transfers of Bonds and receive payments under the Bonds.

The Issuer has no responsibility or liability for the implementation or defaults in the implementation of own procedures by the Budapest Stock Exchange or the Central Depository.

Automatic exchange of information in the field of taxation

Automatic exchange of information regime was implemented under Council Directive 2011/16/EU on Administrative Cooperation in the field of Taxation, as amended by Council Directive 2014/107/EU, pursuant to which Member States are required to apply various measures on mandatory automatic exchange of information from 1 January 2016, except for Austria that was allowed to start applying these measures up to one year later, starting 1 January 2017. The foregoing Directives extended the previously existing automatic exchange of information on residents of EU Member States to a full range of income (interest, dividends, and other income as well as account balances and sales proceeds from financial assets) as well as information on qualifying Account Holders in accordance with the Global Standard released by the OECD Council in July 2014 and ensured a coherent, consistent and comprehensive Union-wide approach to the automatic exchange of financial account information in the Internal Market. On 25 June 2018, Directive 2018/822 amending Directive 2011/16/EU with respect to mandatory automatic exchange of information in the field of taxation in relation to reportable cross-border arrangements entered into force. Directive 2018/822 brings extensive reporting obligations for both intermediaries and taxpayers for cross-border arrangements that contains at least one of the hallmarks listed (namely characteristics or features of a cross-border arrangement that presents an indication of a potential risk of tax avoidance). Each Member State shall take the necessary measures to require intermediaries and relevant taxpayers to file information on reportable cross-border arrangements the first step of which was implemented between the date of entry into force and the date of application of Directive 2018/822 (1 July 2020). Intermediaries and relevant taxpayers, as appropriate, shall file information on those reportable cross-border arrangements by 31 August 2020.

Investors who are in any doubt as to their position should consult their professional advisers.

USE OF PROCEEDS

The Bonds will be issued, and the net proceeds of the Offering shall be used by the Issuer, to finance its existing loan portfolio and new lending to its EU Member States and for debt refinancing (see “*Description of the Issuer – Mission*” and “*Description of the Issuer – Strategy*”).

DESCRIPTION OF THE ISSUER

INTRODUCTION AND HISTORY

The Issuer is a multilateral development institution (a public international body within the meaning of Directive 2003/71/EC, as subsequently amended (the “**Prospectus Directive**”)), operating on the basis of the intergovernmental Agreement on the Establishment of the International Investment Bank of 10 July 1970 and the Statutes of the International Investment Bank forming an integral part of the Establishment Agreement. The Statutory Documents came into force provisionally on 1 January 1971, when the Issuer commenced operations, and definitively on 5 February 1971, and were registered with the Secretariat of the United Nations on 1 December 1971 under number 11417.

In May 2014 the Member States adopted the Protocol amending the Agreement Establishing the International Investment Bank and its Charter, which after ratification by all Member States entered into force on 18 August 2018.

The Issuer currently has nine Member States, namely: Czech Republic, Hungary, Mongolia, Republic of Bulgaria, Republic of Cuba, Romania, Russian Federation, Slovak Republic and Socialist Republic of Vietnam. Membership in the Issuer is open to other states, as well as to international financial organisations.

Due to objective reasons, starting from 1991, the Issuer temporarily reduced its activity. As of 2012, the Issuer has undergone a complex reformation and major modernization process, re-launching its activity under a new management structure and on the basis of renewed development strategy and lending policy. The Issuer has reviewed and reinforced its development strategy, aiming at doubling its assets and loan portfolio within a five-year horizon, while transforming into an advanced, rapidly expanding and financially sustainable multilateral development bank, as well as a recognised player on markets in target geographical areas with a significant role to play for its shareholders and key partners (see “*Strategy*”).

Following the entry into force of the Protocol, the Issuer’s authorized capital is of EUR 2 billion. As at 31 December 2018, after the Czech Republic has increased its share to 11.47%, the Issuer’s paid-in capital amounted to EUR 325.96 million whereas the combined share of the Czech Republic, Slovakia, Hungary, Romania and Bulgaria – the Issuer’s member countries within the European Union – to the Issuer’s capital reached 50.16%. As of the same reference date, Cuba’s share in the Issuer’s paid-in capital is at 1.64% and the share of Asian members of the Issuer (Vietnam and Mongolia) is at 2.17%. Russia’s share in the Issuer’s paid-in capital is 46.03%.

The Issuer’s headquarters is located at 7 Mashi Poryvaevoy str., Moscow, 107078, Russian Federation. Being an international organization acting on the basis of the international treaty, the Issuer is exempt from the sector specific sanctions against certain state-owned Russian financial and credit institutions, imposed by the Council Regulation (EU) No 833/2014 of 31 July 2014 concerning restrictive measures in view of Russia’s actions destabilising the situation in Ukraine. As per paragraph 5 of the Regulation’s preamble, Russian-based institutions with international status established by intergovernmental agreements with Russia as one of the members, such as the Issuer, are not subject to the sanctions thereunder.

The Board of Governors of the Issuer resolved on the relocation of its Headquarters from Moscow to Budapest on December 4, 2018. Based on this decision, on 05 February 2019, the Government of Hungary and the Issuer have signed the Agreement regarding the seat of the IIB Headquarters and the Agreement was ratified by the Hungarian Parliament on 5 March 2019. Simultaneously with the relocation of its Headquarters to Budapest, the Issuer will establish a branch in Moscow.

The Issuer’s general telephone number is +7 (495) 604-73-00. For investors inquiries, please use +7 (495) 604-76-00 and/or ir@iibbank.com.

THE NEW EDITION OF THE STATUTORY DOCUMENTS

The Issuer is finalizing a large-scale institutional reform through the adoption of the Protocol amending the Agreement Establishing the International Investment Bank and its Charter. As of 25 June 2018, all Issuer’s Member States have completed the ratification of the Protocol and therefore it entered into force on 18 August 2018.

Based on the experience of international financial institutions through the ratification of the Protocol, the Issuer moves from the two-tier (i.e., Council and Board) to a three-tier governance system (i.e., Board of Governors, Board of Directors and Management Board). Three-tier governance structure provides transparency and clear delegation of authority with well-defined roles and responsibilities. The Protocol also implies the transition from the "one country – one vote" to a double majority voting system. According to the new voting system, voting powers to Member States in the Board of Governors and the Board of Directors are granted pro rata to their share in the Issuer's paid-in capital. Save for certain strategic decisions which shall require the unanimous approval of all Member States represented at the meetings of the Board of Governors (e.g., decisions on the amendment of the Establishment Agreement and the Statutes, changes in the capital of the Issuer and admission of new members, decision on the date and procedure for the termination of the Issuer's operations), under the Protocol, the resolutions of the Board of Governors and the Board of Directors are adopted based on a double majority rule, with the favourable vote of: (i) a qualified majority of at least three quarters of the total votes vested with the representatives of the Member States; and (ii) a simple majority of the representatives of the Issuer's Member States who actually voted on the relevant resolution. The Board of Governors and Board of Directors have the authority to adopt resolutions only if representatives of at least $\frac{3}{4}$ of the total number of the Issuer's Member States attend the corresponding meeting.

All resolutions of the Management Board are adopted by a simple majority. Each Member of the Management Board has one vote. In the event of a tie between the votes of the Members of the Management Board, the Chairperson of the Management Board has the decisive vote.

The new edition of the Statutory Documents also imply an increase of authorized capital of the Issuer by EUR 2 billion.

The new edition of the Statutory Documents set forth, among others, the rules regarding the admission of new Member States and the withdrawal of Member States, its governance structure as well as the scope of operations which may be undertaken by the Issuer.

The new edition of the Statutory Documents specifically provide that the Issuer benefits from distinct legal personality. They also set forth several privileges and immunities of the Issuer and the Issuer's officials, and, in particular, of the representatives of the Member States in the Issuer's Board of Governors and Board of Directors, on the territories of the Member States. Such privileges and immunities, which include immunity from judicial and administrative proceedings, are aimed at enabling the Issuer and its officials to carry out their functions and attain the purposes set forth in the new edition of the Statutory Documents. Privileges and immunities granted to officials of the Issuer (including representatives of the Member States in the Issuer's Board of Governors and Board of Directors) are applicable to such persons while in official capacity and are vested therewith only to serve the interests of the Issuer. Member States, the Board of Governors, and the Chairperson of the Management Board, as the case may be, have the right in the scope of their competency, and are under the obligation, to waive the immunity of the respective representative or official if, in their opinion, such immunity obstruct justice and can be waived with no detriment to the Issuer's interests, to the extent and on the terms and conditions that it considers would satisfy the Issuer's interests.

Certain matters related to the residence of the International Investment Bank in the Russian Federation are set forth in the agreement dated 23 December 1977 concluded between the Issuer and the former USSR (the "**Host State Agreement**"). Among others, the Host State Agreement provides for the inviolability of the Issuer's premises in the USSR (and, consequently, the Russian Federation as a successor state after the USSR dissolution) and the exemption of the Issuer's operations from the supervision of central or local authorities of the Russian Federation.

MISSION

The renewed mission of the Issuer, in accordance with its 2018-2022 Strategy, is to facilitate connectivity and integration between the economies of its Member States, in order to ensure sustainable and inclusive growth and competitiveness of their national economies, backed by the existing historical ties.

The Issuer is primarily engaged in lending activities with the participation of leading national financial institutions (partly owned by Member States) and development banks, export-import banks/agencies or in partnership with other international development institutions, mainly targeting investment projects on the territories of its Member

States. Complementary to its main lending activities, the Issuer invests in, and is involved in transactions with, securities and foreign currency, as an alternative method to manage surplus liquidity.

The Issuer is determined to extend its activity within Member States through diversified and in-depth cooperation with export credit agencies, national organisations for development, multilateral development banks and other international finance institutions with a high rate of credibility. A first step towards achieving this aim has been made in April 2014, when the Issuer executed a Multilateral Memorandum on Cooperation (the “**Memorandum**”) with a number of export credit agencies (“**ECAs**”) in Member States, including EXIAR, EXIMBANKA SR, EGAP, BAEZ and EximBank Romania. Pursuant to the Memorandum, the Issuer will act as a bridging financing institution, while the ECAs will provide insurance coverage in relation to projects carried out in cooperation by Member States. The Memorandum was subsequently joined by other ECAs. Also, in October 2016, the Issuer signed a memorandum of understanding with the European Investment Fund (“**EIF**”), which formalized the partnership between the two financial institutions in relation to the anticipated establishment of the Central Europe Fund of Funds (“**CEFoF**”) managed by the EIF. In 2017 the CEFoF was launched and approved its first operations. Moreover, aiming to promote its activities among leading development financial institutions, on 14 October 2018 the IIB became a member of in the International Development Finance Club (“**IDFC**”), an esteemed union of national and regional development institutions, whose main focus lies in areas of sustainability, including urban development, green finance, promotion of partnerships between development institutions, export finance, etc.

SUBSIDIARY AND REGIONAL OFFICE

The Group currently consists of the Issuer and one subsidiary, JSC “IIB Capital” (the “**Subsidiary**”). The Subsidiary is established in the form of a joint stock company, being 100% owned by the Issuer. The Subsidiary’s principal office is located at 107078 Moscow, Basmany lane 7, office 14.

The Subsidiary was established in 2012, in order to take over several non-core activities of the Issuer, to enable the Issuer to focus on its core objective and to expand its lending activities and evolve into a prominent development institution in the Member States. The Subsidiary’s core activity now primarily consists of managing the Issuer’s complex of premises. This separation of activities between the Subsidiary and the Issuer enables a more efficient management of the Issuer’s property, with minimum administrative and maintenance costs and enhanced personnel structure.

The share capital of the Subsidiary is RUB 44,5 thousand (approximately EUR 1,100 at the exchange rate effective at the date of incorporation).

On 14 April 2015, the Issuer opened its first regional representative office, based in Slovakia, with the particular aim to qualitatively increase the Issuer’s activity in the EU Member States and facilitate contact with EU-based financial institutions. The Issuer’s regional office has been developing contacts with local partners and potential clients, leading to a number of possible transactions. The office also hosts an additional back-up server of the Issuer and secures its business continuity. Until the end of August 2018, the Issuer’s regional office identified, arranged and assisted in conclusion of credit facilities and bank guarantees agreements with the clients in Slovakia, Czech Republic, Hungary and Romania for the overall volume exceeding EUR 270 million. . Later the Bank received the official note of the Ministry of Foreign and European Affairs of the Slovak Republic dated 25 September 2018 regarding the intention of the Slovak Republic not to become the party of the Agreement between the Slovak Republic and the International Investment Bank on the Establishment of the Office of the International Investment Bank in the Slovak Republic (provisionally adopted from the date of its signing on 14 April 2015). Therefore in accordance to the corresponding Resolution of the IIB’s Board of Governors (the Protocol of the 1st Meeting of the Board of Governors dated 04.12.2018) the Bank has closed the European Regional Office of the International Investment Bank in Bratislava, Slovak Republic on 31 December 2018.

At the 1st Meeting of the Board of Governors in December 2018, the Issuer’s Member States unanimously approved the relocation of the head-quarters of the Bank to Budapest . Simultaneously the Board of Governors took a decision to open a full-fledged branch in Moscow to oversee the Russian market and assist with smooth transition of the Bank’s operations to Budapest. In a press release made by Moody’s on December 12, 2018 the rating agency mentioned that „*The relocation decision is credit positive since it is expected to lower IIB’s cost of funding by reducing the perceived risks associated with having its headquarters in Russia. It will also increase IIB’s investor diversity and its visibility and attractiveness to potential new shareholders.*” Based on this decision,

on 5 February 2019, the Government of Hungary and the Issuer have signed the Agreement regarding the seat of the IIB Headquarters and the Agreement was ratified by the Hungarian Parliament on 5 March 2019.

STRATEGY

Re-launch Programme and 2013-2017 Strategy. Main achievements.

The Issuer's strategic development for the five-year period immediately following its 2012 re-launch, were outlined in the 2013-2017 Development Strategy (adopted in June 2012 at the Issuer's Council 97th meeting held in Hanoi, Vietnam on 6 June 2012) and the Re-launch Programme (approved with the unanimity of the Member States' votes in November 2012, at the Issuer's Council 98th meeting held in Moscow on 28-30 November (the "**Re-launch Documents**"). During the implementation of the Re-launch Documents, the Issuer went through a modernisation process, which implied fundamental work carried out by the Issuer in order to overcome negative trends and resume activity. The Issuer managed to reach considerable success in virtually all areas of its core activity, thus laying the basis for transition to the next strategic stage of its development.

As qualitative transformations resulting from the implementation of the 2013-2017 strategy and the Re-launch Programme, the following achievements can be mentioned: (i) the assignment of ratings from leading international rating agencies; (ii) building an advanced risk management, assets/liabilities management and compliance control system; (iii) expanding the Issuer's product offering through direct funding, intermediated financing, trade financing products and bank guarantees, including target support programmes; (iv) coordination with and approval by all shareholders on the amendments made to the Statutory Documents and phasing in a three-tier corporate governance structure; (v) building a qualitatively new governance structure based on best international practices; (vi) restoring Hungary's membership with the Issuer; (vii) increasing the Issuer's recognition in the reference group of development institutions and on international markets as a whole; (viii) issuing bonds in Member States, both in euro and national currencies; (ix) introducing IT systems that meet advanced requirements: a new automated banking system (ABS), a customer relationship management (CRM) system, an electronic document management (EDM) system, and automation of key business processes and (x) implementing corporate social responsibility (CSR) principles.

In terms of growth of core indicators during the implementation period of the Issuer's development strategy for 2013 - 2017, the following achievements are noteworthy:

- as of the end of 2017 the Issuer's assets increased by 24% compared with 2016 and reached EUR 1,096 million, showing a three-fold growth for the Issuer's Development Strategy 2013-2017 implementation period;
- the increase in Issuer's assets value was mainly driven by the growth of the loan and documentary portfolio, which amounted to EUR 712.4 million at the end of 2017 (almost 88% higher than in 2016) and included loans and documentary products in all 9 member states, which is in line with the targets of the optimistic scenario of the Issuer's Development Strategy 2013-2017;
- the total volume of long-term funding raised as of the end of 2017 amounted to EUR 667 million (62% growth than in 2016). During the strategic period 2013–2017, the Group diversified its fundraising effort by countries, products, timeframes and investors, including placements on the markets of the Member States and the leading EU markets; and
- in line with the implementation of the resolutions adopted at the 99th meeting of the Issuer's Council (in June 2013), by the end of 2017 the paid-in authorized capital of the Issuer reached EUR 314.96 million (see "Strong Support from Member-States").

2018-2022 Strategy

The strategic vision for the Issuer's development within the next mid-term period is outlined in the 2018-2022 Strategy adopted in June 2017 at the Issuer's 107th Council meeting held in Bucharest, Romania on 26-27 June 2017. This strategy determines the global vector of the multilateral development institution's growth path not only for the next five years, but is also intended to layout the basis for a longer-term strategic guide (until end of 2032). At the end of 2017, the Issuer in close cooperation with the delegations of the Member States prepared country strategies that detail the Issuer's strategic priorities in each Member State for the 2018-2022 planning period.

The new strategic vision is aligned and consistent with the Issuer's mission and mandate and further tailored in strategic directions to support and enhance the Issuer's long-term development. By the end of 2022, the Issuer aims to:

- become an acclaimed niche lending institution capable of executing medium-sized projects to promote the development of the national economies of Member States;
- put forward a recognisable value proposition on the markets of Member States, play a prominent role in supporting financial transactions both between them and third countries, which includes funding export/import operations and investment;
- run a partnership network in each Member State on the basis of long-term mutually advantageous relationships;
- achieve long-term financial sustainability;
- demonstrate sustainable profitability through its core activity.

Key specific strategic goals under the 2018-2022 Strategy are as follows:

- **Becoming a significant development institution for the economies of the Member States**, by taking into account the specific features of each market and its various segments, including the competitive environment. At this end, the Issuer's value proposition includes (i) providing mid-term, long-term and equity financing for projects relevant for innovative development of the national economies of Member States, (ii) covering long-term risks in sectors that experience a shortage of financing from other sources due to challenging operating conditions, through a number of means, including guarantees, (iii) allocating direct financing/coverage of target risks for financial institutions in the Member States, including in the area of trade financing (iv) participating in joint financing of long-term investment projects in collaboration with national development banks and IFIs, (v) financing mid-term and long-term investment projects to be implemented both by players from Member States beyond their borders, and by foreign investors in the territory of Member States, (vi) financing export/import operations between the Issuer's Member States and also between Member States and third countries and (vii) providing advisory services and technical assistance. Target client segments include mid-sized companies with annual revenue ranging from EUR 30 to 100 million, SMEs with a turnover of up to EUR 30 million – intermediated financing via national financing institutions, large companies with revenue exceeding EUR 100 million or infrastructure projects – syndicated financing or joint financing with other players and national financial institutions, including those that operate in the area of trade financing.
- **Assisting the economic integration of Member States**, by acting as a platform capable of carrying out foreign economic activities between Member States and their partners in a wide range of areas. Also, in order to raise its status in the international financial community, the Issuer intends to strengthen its operations especially by conducting in-house public events aimed at assisting the economic development of the Member States and participants with special status, by sponsoring events, initiatives and programmes, and by releasing researches and information materials.
- **Raising long-term financial sustainability**, which is intended to be achieved by developing the financial control and expanding the resource base. The development of financial control is envisaged to be obtained by way of (i) monitoring the profitability of the Issuer's operations; (ii) providing sufficient returns with a reasonable risk level; (iii) forecasting the Issuer's short-term development horizon and taking corrective decisions based on the forecast data; and (iv) regularly identifying the key factors affecting the Issuer's financial standing. The Issuer plans to accrue liabilities while observing the following principles: (i) ensuring the diversification of its loan portfolio; (ii) raising funds for longer periods while lowering the cost; (iii) expanding the financing activities through bond issues on Member States' national markets; (iv) increasing the number of partners; (v) broadening the range of fundraising tools; (vi) consolidating the Issuer's reputation as a trustworthy and transparent partner; and (vii) launching a debut Eurobond issue.

- **Having the Issuer’s international credit rating upgraded to A- or higher.** The Issuer aims to be assigned at least an A- rating from an international rating agency, primarily by executing the following tasks: growth and diversification of its loan portfolio; monitoring and management of the level of troubled assets; diversification and enhancement of the quality of its treasury portfolio; control over capital adequacy, financial leverage and risk profile. At the current moment in time, the Issuer is rated A3 with stable outlook by Moody's Investors Service, Inc. (“**Moody’s**”), BBB+ with stable outlook by Fitch Ratings CIS Ltd (“**Fitch**”), A- with stable outlook by Standard & Poor’s Credit Market Services Europe Limited (“**S&P**”) and A with positive outlook by Dagong Global Credit Rating Co., Ltd (“**Dagong**”).
- **Reaching beyond the Issuer’s “historical space”.** A strategic vector for the Issuer’s development is to expand the Issuer’s historical footprint by drawing in new participants. The principal objectives for admitting new members are (i) gaining access to new markets and clients; (ii) obtaining new financial resources and other forms of support; (iii) growth of assets and the loan portfolio; (iv) gaining professional skills and expertise; (v) improving the Issuer’s credit ratings; and (vi) ensuring complementarity of new and existing members.

Main achievements of the implementation of the 2018-2022 Strategy

The Issuer continues to expand its operations in accordance with its mandate and strategic objectives established in its Development Strategy 2018-2022 and Country Strategies. For the first half of 2018, a significant progress has been made in the field of expansion of the loan and trade finance portfolio, quality improvements in treasury assets as well as diversification of borrowings in terms of type, maturity, geography and currencies, as follows:

- In 2018, the Issuer’s total assets reached EUR 1.19 billion supported by the expansion of core activities. In line with the Issuer’s mission, the share of development portfolio in the Issuer’s total assets increased to 72% from 69% at end 2017. During the reporting period, the Issuer’s net loan portfolio reached EUR 752.8 million vs. EUR 664.1 million at the end of 2017. In terms of geographical diversification of loan portfolio the share of European Member States increased to 57% from 43% compared to the end of 2017;
- In line with its Trade Finance Support Program (TFSP), the Issuer continued to diversify and gradually increase the volume of trade finance transactions for the benefit of all Member States. During January-December 2018, 44 trade finance deals were issued in the total amount of EUR 151.4 million;
- The share of AAA-A-rated assets in the Issuer’ treasury portfolio reached a record high level of 51% compared to 43% at end 2017;
- As part of the 2013 capitalization programme, on 12 July 2018 the Government of Romania made an additional contribution to the Issuer’s authorized capital in the amount of EUR 4 million.
- On 25 June 2018, the Protocol Amending the Agreement Establishing the International Investment Bank and its Charter was ratified by the last remaining member country, the Slovak Republic. On 18th of August 2018, the Protocol entered into force. In this regard, the authorised charter capital increased from EUR 1.3 billion to 2 billion.
- In December 2018, the Board of Governors of the Issuer voted for the relocation of the Bank’s Headquarters from Moscow to Budapest in order to support the active development of IIB on the European territory. Based on this decision, the Host Country Agreement (HCA) has been signed on 05 February 2019 by the Government of Hungary and Issuer and it was ratified by the Hungarian Parliament on 5 March 2019. As a result, the institution will receive an European legal and fiscal address, will come closer to its main sources of funding and will receive the ability to diversify them further. An IIB branch will be established in Moscow.
- In December 2018, at the Board of Governors meeting, the shareholders also approved Capitalization Program for the purpose of implementation of IIB Development Strategy 2018-2022. The Program implies the increase of paid-in capital from current shareholders in the amount of EUR 200 million (distributed over the years 2020-2022).
- On 20 December 2018, the Czech Republic made the contribution to the Issuer’s paid-in capital in the amount of EUR 7 million in accordance with the 2013 capitalization programme, increased its share to 11.47% (EUR 37.37 million). As a result, the paid-in capital of the International Investment Bank amounted to EUR 325,96 million.

- On 12 April 2018, Standard & Poor's upgraded the Issuer long-term credit rating to BBB+ with stable outlook. On 30 April 2018, Moody's also upgraded the Issuer long-term credit rating to A3 with stable outlook. On 22 November 2018 Fitch upgraded the Issuer long-term credit rating to BBB+ with stable outlook. In addition, the Issuer was assigned the following investment grade rating: A with positive outlook (Dagong Global Credit Rating).
- In April-June 2018, the Issuer successfully placed its first CZK-denominated issue of bonds at the Vienna and Prague Stock Exchanges. The private placement issue totaled CZK 750 million.
- On October 14, 2018 during the Annual Meeting of the International Development Finance Club (IDFC), which unites 24 multilateral, regional and national development banks, International Investment Bank officially became a member of the organization by signing its charter.
- In November 2018, to promote comprehensive framework cooperation between IIB and Central American Bank for Economic Integration (CABEI) a Memorandum of understanding was signed
- In March 2019, Standard & Poor's upgraded the Issuer long-term credit rating to A- with stable outlook.

ENVIRONMENTAL AND SOCIAL RESPONSIBILITY

United Nations Global Compact

The Issuer intends to operate as a socially and environmentally responsible development institution. For this purpose, it has joined the United Nations Global Compact – the largest international initiative in the field of sustainable development, having voluntarily submitted to observe the fundamental principles of the United Nations Global Compact on human rights protection, labour relations, environment and corruption fight, in its activities.

The Issuer has been gradually incorporating such principles into its activities, including by adopting its Corporate Social Responsibility Policy and, more recently, its Environmental and Social Impact Assessment Guidelines for the investments it makes, in line with best practices across multilateral development institutions. In 2015, the Issuer started supporting environmental initiatives directly, having provided financial grants for programmes aimed at protecting and preserving rare or endangered species of animals in Mongolia and Vietnam. The commitment to environmental initiatives was reinforced in 2016, with a recent grant having been awarded by the Issuer to WWF Hungary for assessing and mapping water resource risks.

SR-IIB Technical Assistance Fund

At the end of April 2016, the Issuer set up the SR-IIB Technical Assistance Fund (TAF), with a 1-million EUR contribution by Ministry of Finance of the Slovak Republic. The fund, operating under the Issuer's management, is used to finance technical assistance and advisory services supporting the Issuer's investment activities in ODA-eligible developing countries among its Member States (by OECD classification, these countries are – Vietnam, Mongolia and Cuba) or supporting these countries' own activities in relation to reforms and modernisation.. The Issuer uses its internal procurement rules and processes to select and subsequently contract consultants.

In order to increase the pool of available resources, the Issuer co-finances 20 percent of the assignments under the TAF up to the cumulative amount of EUR 245,000, after which further projects will be financed solely from the TAF. The Issuer also actively manages temporarily unallocated resources of the TAF in order to grow the fund balance. The resources of the TAF can be used to contract exclusively Slovak-based consultants (or Slovak subsidiaries of transnational consultancies as the case may be), although up to 25 percent of the budget approved for individual assignments can be used by the contracted consultant to subcontract partners from the Issuer's other Member States.

As of December 19, 2018, the TAF has successfully completed a project aimed at assisting the Financial Regulatory Commission of Mongolia (Mongolia's financial market supervisory body) in bringing its AML/CFT regulations in line with the Financial Action Task Force (FATF) recommendations and global best practices. Currently ongoing projects include technical assistance in preparing a project of a joint Cuban and Slovak enterprise producing confectionery in Cuba, and a large energy-efficiency street lighting PPP project in Hanoi, Vietnam, as well as scientific testing of Slovak innovative agricultural technology in Vietnam. On top of the ongoing operations, a project of technical assistance for installation of biomass power plants in the Thừa Thiên-Huế province of Vietnam is currently under preparation.

Trade Finance Support Programme

In 2018, as part of the Trade Finance Support Programme (TFSP), the Issuer actively supported the delivery of hydroturbine equipment for small hydropower plants from Bulgaria and Czech Republic to Armenia. The Issuer supported the finance of such exports in the amount of EUR 8.85 million.

Grant support

As part of its environmental support practice, in 2017 the Issuer provided a EUR 30,000 grant to supporting the project of Milvus Group Association “Environmental education and awareness raising in protected areas” in central Transylvania, Romania. The project was aimed at raising awareness of local population towards natural values and the environment, and, in particular, towards Romanian territories protected as EU Natura 2000 sites. Among others, the programme facilitates 200 hours of environmental education activities in the elementary schools in Transylvania, over a period of 10 months.

In June 2018, as part of extending its environmental responsibility practice and contributing to the implementation of sustainable development principles in Member States, the Issuer provided a EUR 40,000 grant for execution of a project on restoring peatlands in Russia. This important protection initiative is being implemented by Wetlands International, an international non-governmental organisation.

In November 2018, the Issuer also provided a grant in the amount of approximately EUR 34,000 for the restoration of wetlands of the upper creek of the Tuula Gol river in central Mongolia. The aim of the project is to study the current state of wetlands in the area, biosystems and ecosystems, identify main causes for degradation of wetlands and to assess the risks of deepening processes, which negatively influence the ecosystem.

Miscellaneous

The Issuer is acting as an integrator of pharmaceutical industry’s development in Russia and Hungary. Thus, the Issuer signed an agreement for the issuance of counter-guarantees for up to RUB 1.5 billion for a key medicine distributor, one of Russia’s market leaders in the sector – Pharmaceutical Company PULSE LLC.

The Issuer is working on the introduction of the “green office” standards in its activities in accordance with the principles of responsible and sustainable development. This objective is part of the 2018-2022 Strategy and is also part of the Issuer’s initiative of responsible attitude towards the environment, which was approved in 2016. The Issuer managed to optimize its printing expenses, as well as implement specific measures to support efficient use of paper, electricity and water in its activity.

KEY BUSINESS STRENGTHS

The Issuer believes that its potential for future growth of its business are primarily due to the following strengths:

Status, privileges and immunities

The Issuer is a supranational intergovernmental organisation, benefitting of immunity from the application of all taxes or fees (with the exception of specific service fees), whether national or local, as well as from the application of customs duties and restrictions on the import and export of articles destined for official use, in the Member States. In particular, no tax is levied by Member States on the profits received from the Issuer’s banking activities. In accordance with the new edition of the Statutory Documents which came into force on 18 August 2018 the Issuer shall (i) be immune from any and all taxes or fees, whether national or local, except for specific service fees; (ii) be free from any obligations to pay, withhold, or collect any taxes; (iii) be immune from any customs duties or taxes or fees or any import or export restrictions in relation to goods intended for official use; and (iv) enjoy all benefits with regard to priority ranking, tariffs and rates of postal, telegraphic, and telephone communications offered to other international organisations and diplomatic missions in the corresponding state.

Furthermore, according to the new edition of the Statutory Documents, the Issuer itself, the representatives of the Member States in the Board of Governors and the Board of Directors, and the officers and employees of the Issuer enjoy the privileges and immunities necessary to perform the functions and achieve the aims set forth in the new edition of the Statutory Documents on the territories of the Member States.

As it is generally the case with supranational financial organizations acting on the basis of international treaties, the Issuer is not subject to local regulation by the Central Banks of the Member States or other similar bodies, while also being exempt from the general legal treatment applicable to other legal entities operating within the same business as the Issuer on the territory of the Member States. In particular, the Issuer is not subject to regulatory requirements under the Member States' legislation, including with respect to licensing, capital adequacy and information disclosure requirements.

Based on the new edition of the Statutory Documents, the Issuer also enjoys privileges which are similar to those granted to diplomatic representations in the Member States with respect to priorities, tariffs and rates applicable to postal, telegraphic, and telephone communication.

The Issuer is not subject to the specific sectoral sanctions against certain state-owned Russian financial and credit institutions, imposed by the Council Regulation (EU) No 833/2014 of 31 July 2014. Based on a special reservation in the fifth recital of the Council Regulation (EU) No 833/2014 of 31 July 2014, Russian-based institutions with international status established by intergovernmental agreements with Russia as one of the members (such as the Issuer) are not subject to the sanctions set forth thereunder.¹

Strong capital base

Following the entry into force of the Protocol, the authorised capital of the Issuer is of EUR 2 billion, out of which EUR 325.9 million represent the paid-in capital of the Issuer (following the contribution by the Czech Republic of 20 December 2018). This increase of the Issuer's authorized capital from EUR 1.3 billion to 2 billion is intended to provide room for potential contributions by new members of the Issuer or for increasing quotas of current Member States in authorized capital.

As of 31 December 2018, the authorized capital of the Bank increased to EUR 2 billion - the paid-in capital amounts to EUR 326 million, callable capital amounts to EUR 798.5 million divided between the Member States and payable by the Member States on call, in the unlikely case that the Issuer fails to meet its obligations and unallocated portion of the Bank's authorized charter capital totals EUR 875,5 million, namely the amount which is open for contribution by the actual or new members of the Issuer

The total equity of the Issuer (including retained profits and other equity funds) amounted to EUR 395.7 million as of 31 December 2017 and to EUR 376.0 million as of 31 December 2018.

The key objectives of the Issuer for the next five years also include the engagement in equity investments, as well as broadening the range of fundraising tools (see "*Strategy - 2018-2022 Strategy*").

Strong support from Member States

Reinforcing strong commitment to the Issuer's strategic goals, Mongolia, on December 27, 2017 made a contribution of more than EUR 1.9 million, which significantly increased its share in the Issuer's paid-in capital (from 0.47% to 1.08%).

As part of the Capitalisation Programme 2013, on 12 July 2018 Romania made an additional contribution to the Issuer's authorized capital in the amount of EUR 4 million (out of EUR 7.6 million planned).

On December 20, 2018, within the Capitalization Program 2013-2017 the Czech Republic made an additional contribution to the Issuer's paid-in capital in the amount of EUR 7 million (out of EUR 12.6 million planned).

Romania at the first meeting of IIB Board of Governors on 4 December, 2018 confirmed that it had initiated legal steps in order to make the remaining part of its contribution within the Capitalization Program 2013-2017 (EUR 3,6 million) in 2019.

In June 2017 the Council approved the Issuer's Development Strategy for 2018–2022 that provides for the second round of capitalisation.

¹ Recital 5 of the Council Regulation (EU) No 833/2014 of 31 July 2014 reads: *In this context, it is appropriate to prohibit transactions in or the provision of financing or investment services or dealing in new bonds or equity or similar financial instruments with a maturity exceeding 90 days issued by state-owned Russian financial institutions, excluding Russia-based institutions with international status established by intergovernmental agreements with Russia as one of the shareholders.*

The new Capitalization Program 2018-2022 was approved at the first Board of Governors Meeting on December 4, 2018. The Program implies the increase of paid-in capital from current shareholders in the amount of EUR 200 million (distributed over the years 2020-2022).

The Member States have also expressly stated their high level of support for the Issuer's activity through comfort letters issued during the process of obtaining the first Issuer's investment grade rating. By these comfort letters – although not assuming under legally enforceable guarantees – the Member States declared their support with respect to the goals and objectives of the Issuer, primarily consisting of the promotion of the development of economies of Member States, the cooperation among them, and the facilitation of their deeper integration into the world economy. Several heads of delegations of the Member States in the Issuer's Council have also confirmed the support of the Member States, which they represented, during their meetings with the rating agencies.

During the past approx. 20 years, Member States have not required any distribution of dividends. Based on a decision of the Issuer's Council, undistributed dividends for a period of more than 20 years were kept as retained earnings. Moreover, as a sign of unanimous recognition of the Issuer's mission and support of its re-launch efforts, at the Issuer's 99th Council meeting of June 2013, held in Bratislava, the Member States decided to transfer a significant portion of the Issuer's retained earnings in the amount of approx. EUR 76 million into the paid-in capital of the Issuer, thus strengthening the capital position of the Issuer. The above amount increased the nominal value of the participation of the Member States *pro rata* to their respective shares in the paid-in capital of the Issuer as at the date of such decision. The Member States undertake to facilitate the Issuer's access to national capital markets and other sources of funding. Such access may require the adoption of relevant laws or regulations in certain jurisdictions, inclusion of the Issuer in the appropriate lists of multilateral financial institutions that are allowed to make placements on the relevant Member States' market, as well as in the lists of multilateral financial institutions in which pension and other funds and private investors are allowed to invest.

The Issuer implemented bond placements in various currencies (EUR, CZK, RON, RUB) contributing to the development of its Member States' capital market. The success of these placements was due to the strong support provided by the respective Member State. As recognition for IIB's contribution to the development of Romania's capital market, the Issuer was awarded several times by the Association of Romanian Business Brokers (in 2015, 2016 and 2017) and by Bucharest Stock Exchange (in 2018 and 2019).

The Issuer registered two Bond Programs on Russian market, one with the Central Bank of Russian federation (classical one) and one with the Moscow Stock Exchange (exchange traded bonds). During 2014-2018, the Issuer successfully placed five bond issues on Russian market in the total amount of RUB 24 billion. All ruble issues are included in the Lombard list of the Central Bank of Russian Federation. Due the changes in legislation, the Issuer was added to the list of international financial institutions whose securities can be invested into with pension savings of the state management companies, with the payment reserve resources of the state management companies, and with temporary surplus funds of state corporations and state companies as well as, private pension funds. Other Member States who have also acted towards the facilitation of the Issuer's access to their national capital markets include the Slovak Republic, in which the Issuer has already successfully closed its debut issue of EUR 30,000,000 bonds in October 2014, the Czech Republic, in which the Issuer had successfully placed CZK 750 million in April and May 2018, listed on both Vienna and Prague Stock Exchanges, and Romania, in which the Issuer placed bonds, every year since 2015, first two years 2015-2016 only in RON and in the last two years 2017-2018 both in EUR and RON.

During 2017-2018, the Issuer continued to strengthen its relationships with its Member States and their institutions, including by attending various meetings of inter-governmental commissions, delivering presentations to investors and companies in the Member States, with support from state administrative authorities of the Member States, and hosting a series of events and liaison groups among institutions of the Member States and other countries. The Issuer has also signed and is implementing Memorandum on Cooperation with ministries of foreign affairs and/or economy of Hungary, the Slovak Republic, Mongolia and the Russian Federation. In order to enhance the contacts with its shareholders, the Issuer has also set-up a new platform of cooperation between Member States' representatives, namely the Club of International Investment Bank Ambassadors, under which Ambassadors of the Issuer's Member States meet regularly to discuss issues of interest on the Issuer's agenda.

A Multilateral Memorandum on Cooperation among the Issuer and Chambers of Commerce and Industry of its Member States was signed on 27 June 2017, during the Issuer's Council 107th meeting held in Bucharest, Romania. A number of cooperation agreements with various developments institutions, including the Trade and

Development Bank, the Central American Bank for Economic Integration and the International Bank for Economic Cooperation, was signed in 2018.

The Bank is in constant contact with the top public officials of Member States, including Deputy Prime-ministers, Ministers of Finance/Economy/Foreign Affairs, and Presidents of Central Banks in order to discuss the main strategic issues of the Bank's development.

Not only does the Issuer promote its activities through participation in various international events, in certain cases the Issuer takes lead and organises gatherings of development institutions aimed at exchanging views and experiences of partner banks on topics of high importance. Examples of such an initiative are an international conference "IFRS 9 Implementation in Development Banks: challenges, risks and opportunities" that was held in Moscow in September 2017 and united senior level professionals in accounting, risk management and other fields from more than 14 institutions, as well as the annual ALM and Risk Management Conference hosted by the Issuer in Moscow in September 2018, which gathered top risk and liquidity management experts from leading global international financial institutions.

On October 17, in Budapest, the IIB, with the support of a long-term partner of the Bank — the Banking Association of Central and Eastern Europe (BACEE), held an international conference on "Features of Compliance Risk Management in Development Banks: Practice of Multilateral and National Financial Institutions" dedicated to improving compliance practices in development institutions, increasing the effectiveness of the combating money laundering, corruption, and approaches to the identification and assessment of compliance risks.

In December 2018, the Issuer's Board of Governors (its new top decision-making body that replaced the former Council) has approved the relocation of the Issuer's headquarters to Budapest, Hungary, and based on this decision a HCA has been signed by the Government of Hungary and the Issuer on 5 February 2019 and the HCA was ratified by the Hungarian Parliament on 5 March 2019. After the ratification of the HCA the relocation is expected to take place in the second half of 2019. The move, which will allow the Issuer to better focus on its operations in Central Europe, has received positive feedback from rating agencies and is expected have a positive impact on the Issuer's long-term credit rating.

Robust capital adequacy and potential for attraction of funding

The Issuer's capital adequacy ratio established by the Council stands high at minimum 25%, 21 percentage points above the Basel II 4% requirement applicable to tier I capital and 17 percentage points above the Basel II 8% requirement applicable when accounting tier II capital also. As of 31 December 2018, the Issuer's capital adequacy ratio, calculated in accordance with the Basel II methodology stood at 33.73% (for tier I capital) and 34.39% (for total capital *i.e.*, including tier II capital).

As of 31 December 2018, the Issuer attracted short-term funds from financial institutions in the form of deposits amounting to EUR 67.8 million representing 8.3% of the Issuer's total liabilities as of the same date.

During the past four years, the Issuer has successfully completed a 30 million issue of EUR-denominated bonds on the Slovak market and five issues of RUB-denominated bonds in the aggregate amount of RUB 24 billion on the Russian market under two bond issuance programmes, one established in 2014 and the second in 2016. As of 31 December 2018, the outstanding debt for RUB-denominated bonds amounted to approx. EUR 230 million. In October 2015, the Issuer placed RON 111 million (approx. EUR 25 million) of 3-year maturity bonds on the Bucharest Stock Exchange. The issue was the largest concluded in Romania by any international financial institution in the past six years, including the most recent issues by the EBRD, the EIB and the BSTDB of RON 100 million, RON 88 million and RON 22 million respectively. In September 2016, the Issuer placed another RON 300 million (more than EUR 65 million) of 3-year maturity bonds on the Bucharest Stock Exchange, which became one of the largest among IFIs on the Romanian market in the past 10 years (second largest to the placement by the European Investment Bank in 2007). In September 2017, the Issuer placed two tranches of bonds, as follows: a RON 300,000,000 tranche and a EUR 60,000,000 tranche (the first EUR bonds issued on the Romanian market). In October 2018, the Issuer placed its second dual tranche bond, denominated in both RON and EUR. The size of RON tranche is 300,000,000 and the size of EUR tranche is 80,000,000. In April 2018, the Issuer had also placed its first CZK denominated bond in total amount of CZK 750 million listed on both Vienna

and Prague Stock Exchanges. Other Member States have expressed their openness for potential issues of bonds by the Issuer on their domestic capital markets.

From mid-2014 and until the date of this Offering Circular, the Issuer had also concluded more than 120 different agreements, including bilateral loan agreements, ISDA Master Agreements, long-term REPO, GMRA and trade finance agreements with financial institutions such as Bulgarian Development Bank, Credit Suisse International, Eximbanka SR, Eximbank Hungary, OTP Bank, JP Morgan Securities, Raiffeisen Bank International, Tatra Banka, VTB Capital London, VTB Europe, Česká exportní banka, Industrial and Commercial Bank of China, Eurasian Development Bank, ING Bank, Rosbank, Banca Transilvania, Sberbank Europe, Sberbank CZ, Erste Group Bank, UniCredit Russia, International Bank for Economic Cooperation etc., and more than 30 such agreements are currently pending negotiation between the Issuer and other current or potential financial partners, including New Development Bank, Goldman Sachs KBC, Bank NVNatixis and ICBC Standard Bank, UniCredit Bank (Hungary), BRD – Groupe Societe Generale.

Solid investment grade ratings from rating agencies

At the beginning of 2016, the Issuer had a Baa1 rating with a stable outlook from Moody's, a BBB- with a stable outlook rating from Fitch, and an A rating with a stable outlook from Dagong.

In June 2016, S&P assigned the Issuer a BBB rating with a stable outlook on the basis of the Issuer's strong capitalization.

In December 2016, Fitch upgraded the Issuer to BBB with a stable outlook, citing the continuing diversification of the Issuer's operations in Central and Eastern Europe, the strengthening of risk management policies and the reduction of risks related to business environment.

In May 2017, Moody's changed the rating outlook on the Issuer to positive from stable and affirmed the Issuer's Baa1 rating. According to Moody's, such change was due to the following main drivers: (i) the increased diversification of the Issuer's loan portfolio and the maintenance of relatively strong asset quality; (ii) the improved credit quality of the Issuer's treasury portfolio; and (iii) the increased diversification of the Issuer's funding sources.

In December 2017, Fitch changed the rating outlook on the Issuer to positive from stable and affirmed the Issuer's BBB rating citing the continuing diversification of the Issuer's operations in central and eastern Europe (CEE), the further strengthening of the Issuer's risk management policies and the improvement of the Issuer's business environment.

In February 2018, Dagong changed the rating outlook on the Issuer to positive from stable and affirmed the Issuer's A rating due to the economic recovery in Member States, the favourable credit environment leading to lowered funding costs of the Issuer, and the increased diversification of the Issuer's funding sources.

In April 2018, S&P upgraded the Issuer to BBB+ with a stable outlook after raising the assessment of the Issuer's financial profile to 'very strong'. S&P stated that the Issuer 'has demonstrated low credit costs and low levels of nonperforming loans since its relaunch in 2012 and has meaningfully increased the quality of its liquid assets.'

In April 2018, Moody's upgraded the Issuer to A3 with a stable outlook stating According to Moody's, the main drivers for the rating upgrade are the Issuer's improvement in asset quality, more robust risk management systems, an increasingly diversified loan book and funding strategy and the strengthened credit quality of its treasury portfolio. Moody's believes that the Issuer's new medium-term strategy will likely maintain these improved credit features.

In November 2018, Fitch upgraded the Issuer to BBB+ with a stable outlook reflecting the improvement in Fitch's assessment of the IIB's solvency to 'a' from 'a-'. This in turn results from strengthening in the IIB's overall risk profile measured by Fitch following its re-assessment of IIB's exposure to credit risk, increased geographic diversification of its loan portfolio and the strengthening of its risk management framework.

As such at the end of 2018, the Issuer has been rated A3 with stable outlook by Moody's, BBB+ with stable outlook by Fitch, BBB+ with stable outlook by S&P and A with positive outlook by Dagong.

In March 2019, S&P upgraded the Issuer to A- stable from BBB+ stable owing to the “strengthened governance and management structure, diversifying its shareholders, and clearly articulating an expansion strategy, which includes relocating its head office.”

As such, as of March 2019, the Issuer has been rated A3 with stable outlook by Moody’s, BBB+ with stable outlook by Fitch, A- with stable outlook by S&P and A with positive outlook by Dagong.

Conservative risk management policy

The Issuer’s risk management policy is based on conservative assessments aimed at preventing the adverse impact of risks on the results of the Issuer. As a principle, the Issuer does not enter into potential transactions with high or undeterminable risk level, irrespective of the potential profitability of the deal.

The Issuer upgraded its risk management objectives within the 2018-2022 Strategy. The key principles of the Issuer’s renewed risk management strategy are as follows:

In accordance with the new 2018-2022 Strategy, the Issuer’s priority objectives of evolving the risk management include:

- implementing an economic capital system according to Basel III recommendations in order to determine the amount of equity needed to cover unforeseen losses;
- developing more advanced risk-sensitive methodology of capital calculation;
- creating and developing a process for identifying early warning signals of potential problems in order to establish a second line of defence prior to credit risk deterioration;
- integrating automated risk management systems into the Issuer’s IT architecture.

In enhancing its risk management framework, the Issuer seeks to develop a risk-sensitive toolset for a more accurate assessment of all risk elements as well as to implement approaches allowing for a risk-reward assessment.

In terms of credit risk, the Issuer has created a comprehensive system for the development, collection, analysis and evaluation of early warning signals in order to identify signs of deterioration in a client’s credit standing and take the appropriate measures.

To enhance effectiveness of non-performing loans management, the Issuer have strengthened the way it deals with NPLs, through creation of a dedicated unit in charge with monitoring and managing such loans.

The whole ecosystem of the Issuer’s risk management is intended to evolve in accordance with best industry practices and global trends.

BUSINESS

The following three operating segments of the Group’s activity are identified, based on the analysis of the Group’s financial statements: (i) credit investment activity, which comprises lending activity including long-term corporate and interbank financing as well as financing through trade related loans, (ii) treasury, which includes operations in financial markets, transactions with securities, derivative financial instruments, foreign currency and liquidity management and (iii) other operations, consisting mainly of the operational leasing services, credit portfolio management and other non-core operations.

The following table presents revenues from each segment in EUR million for each year ended 31 December 2016, 31 December 2017, and, respectively, 31 December 2018, as well as for the six-month period ended 30 June 2017 and, respectively, 30 June 2018:

<i>(EUR million)</i>	31 December 2016	31 December 2017	30 June 2017	30 June 2018	31 December 2018
	(audited)	(audited)	(unaudited)	(unaudited)	(audited)
Credit investment activity ¹	1.52	(2.16)	0.50	7.81	15.33
Treasury	16.66	18.67	9.13	4.81	6.50
Other operations	1.55	3.37	1.71	1.37	4.24
Profit for the period ²	0.80	1.01	2.28	5.09	5.62

Source: The Financial Statements

¹ The figure shows the interest and commission income and other segment income net of interest and commission expenses, loan impairments and other segment expenses.

² The total profit includes other elements such as unallocated income and expenses.

³ In 2016, the Issuer introduced a new methodology for evaluating the segmentation of profit and loss. In particular, the Issuer reclassified the re-evaluation of the open currency position and derivatives as part of the treasury segmentation.

Operating income from the credit investment activity decreased by EUR 3.72 million in 2017, year-on-year, from EUR 1.52 million as of 31 December 2016 to EUR -2.16 million as of 31 December 2017 and, as of 31 December 2018, increased dramatically by EUR 17.49 million on a year-on-year basis, to EUR 15.33 million mainly due to grow interest income from credit investment activity in 2018.

Treasury operating income amounted to EUR 16.66 million as of 31 December 2016, increasing by EUR 2.04 million year-on-year, to EUR -18.7 million as of 31 December 2017. In 2018 treasury operating income decreased significantly by EUR 12.77 million or 65% to EUR 6.50 million. The decrease of income in the treasury segment was mostly due to dealing in foreign currencies and operations with derivatives.

Other operating income (such as income from lease of investment property), amounted to EUR 1.55 million as of 31 December 2016 increased to EUR 3.37 million as of 31 December 2017. In 2018 operating income from other operations amounted to EUR 4.24 million 2018, increasing by EUR 0.87 million or 26%.

In 2017 the profit increased from EUR 0.8 million as of 31 December 2016 to EUR 1.01 million or 26%. In 2018, the net profit increased by EUR 4.61 million or 456%. The increase in the net profit in 2018 is mainly due to the fact that no allowance for loans impairment was created in 2018 (in 2017 the allowance for loans impairment amounted of EUR 12.1 million).

In terms of the Group's assets, the net value of the assets of each segment in EUR million was as follows for each year ended 31 December 2016, 31 December 2017 and, respectively, 31 December 2018, as well as for the six-month period ended 30 June 2017, and respectively 30 June 2018:

<i>(EUR million)</i>	31 December 2016	31 December 2017	30 June 2017	30 June 2018	31 December 2018
	(audited)	(audited)	(unaudited)	(unaudited)	(audited)
Credit investment activity	363.4	664.4	500.81	711.28	754.24
Treasury	421.58	334.84	406.04	327.48	345.97
Other operations	96.42	96.80	95.80	94.4	94.15
Total assets	881.44	1096.04	1,002.7	1,133.16	1,194.36

Source: The Financial Statements.

Assets allocated for credit investment activity increased by EUR 281 million or 70.3% from EUR 363.4 million as of 31 December 2016 to EUR 664.4 million as of 31 December 2017, and to EUR 754.24 million as of 31 December 2018 by EUR 109.84 million or 17%, year-on-year.

Assets allocated for treasury activity amounted to EUR 421.58 million as of 31 December 2016, decreasing to EUR 334.84 million as of 31 December 2017 by 86.74 million and increasing to EUR 345.97 million as of 31 December 2018 by EUR 11.13 million.

In 2017, the value of other assets of the Group (such as investment property and other assets) increased by EUR 0.38 million or 3.94% year-on-year, from EUR 96.42 million as of 31 December 2016 to EUR 96.8 million. As of 31 December 2018, the total value of other assets decreased by EUR 2.65 million or 3% year-on-year, to EUR 94.15 million.

Credit investment activity

Lending business in general

The 2018-2022 Strategy clarifies the priorities of the Issuer's loan operations both in terms of its institutional and industry focus and in terms of principles of selecting partners and counterparties. The Issuer will focus on executing medium-sized projects to promote the development of the national economies of Member States and on supporting financial transactions both between them and third countries, which includes funding export/import operations and investment.

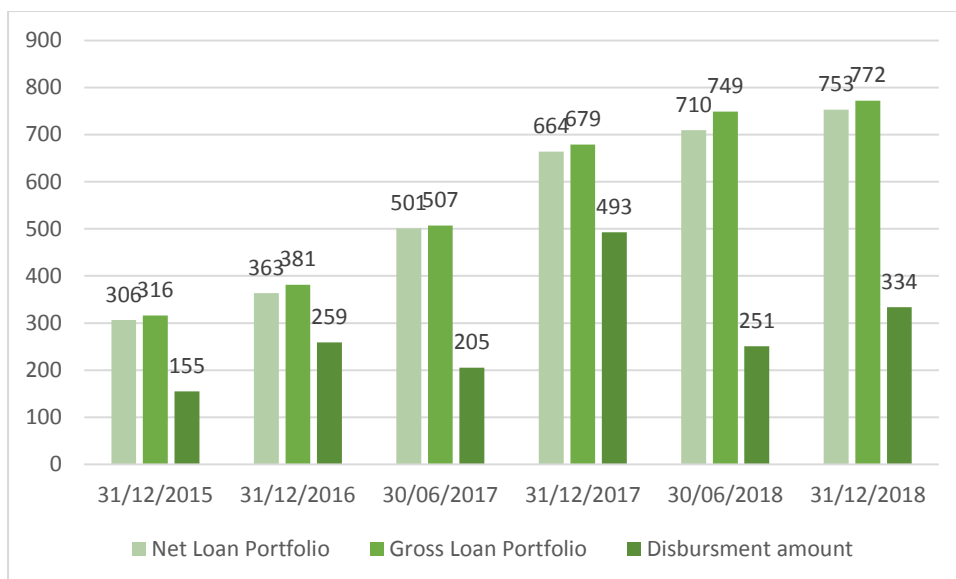
The main financial instruments developed and currently offered by the Issuer are the following:

- *for corporate and other borrowers (national development banks and other financial institutions):* project finance, modernisation, export-import support, PPP through direct financing, syndicated loans and club deals with maturity from 1 to 15 years;
- *for all client types: trade related loans and documentary transactions* with average ticket of EUR 1 million and average maturity of up to 1 years.
- *in the SME segment:* credit lines through selected financial institutions and syndicated loan facilities with maturity from one to seven years;

As of 31 December 2018, amounts of loans granted by the Issuer to clients range between EUR 4.8 and EUR 90.0 million.

In line with its key objectives under the 2018-2022 Strategy, in certain member-states the Issuer intends to further expand its investments in funds, as well as equity investments. The total size the Issuer's equity investment will be limited to 5 – 10% of the total loan portfolio.

The following chart shows the development of the Issuer's loan portfolio in the years ended 31 December 2015, 2016, 2017, 2018 and the six-month periods ended 30 June 2017 and, respectively, 2018 in EUR million:



Source: The Financial Statements and Group's management report (for disbursed amount).

The Issuer's net loan portfolio is 60.6% denominated in EUR. As of 31 December 2018, approx. 22.2% of the Issuer's loan portfolio net of allowance consisted of loans extended in USD, 6.4% of the Issuer's loan portfolio - extended in RON and HUF. No part of the Issuer's loan portfolio is securitised.

In terms of maturity, as of 31 December 2018, 0.3% of the outstanding amounts net of allowance under loans to banks are to be repaid less than one month, 19.5% are to be repaid within one to three months, 23.9% are to be repaid within three months to one year, 51.7% are to be repaid within one year to five years and 4.5% over five years.

As of 31 December 2018, 1.2% of the outstanding amounts net of allowance under loans granted to corporate clients are to be repaid within less than one month, 2.1% to be repaid within one to three months, 7.3% to be repaid within three months to one year, 37.4% to be repaid within one year to five years and 52.0% over five years.

As of 31 December 2018, non-performing loans ("NPLs") coverage ratio was of 128.9%..

Approach to SME lending

As at 31 December 2018, 8% (approx. EUR 63 million) of the Issuer's net loan portfolio was provided to the SME segment through financial intermediaries. The Issuer considers the financing of the SME segment as one of the main focus points of its mission, particularly due to the dynamic and growing importance of SMEs in the economy of its Member States. Under the current Issuer's SME support programme, funds are provided by the Issuer to its financial intermediaries who thereafter use such funds for the purposes of SME project financing. The Issuer supervises proper utilisation of the funds through monitoring a number of key parameters of the financing (e.g., business activity, structure of shareholder/ participants, annual sales) to the ultimate SME borrowers.

The following areas are considered as priorities for the Issuer's SME financing:

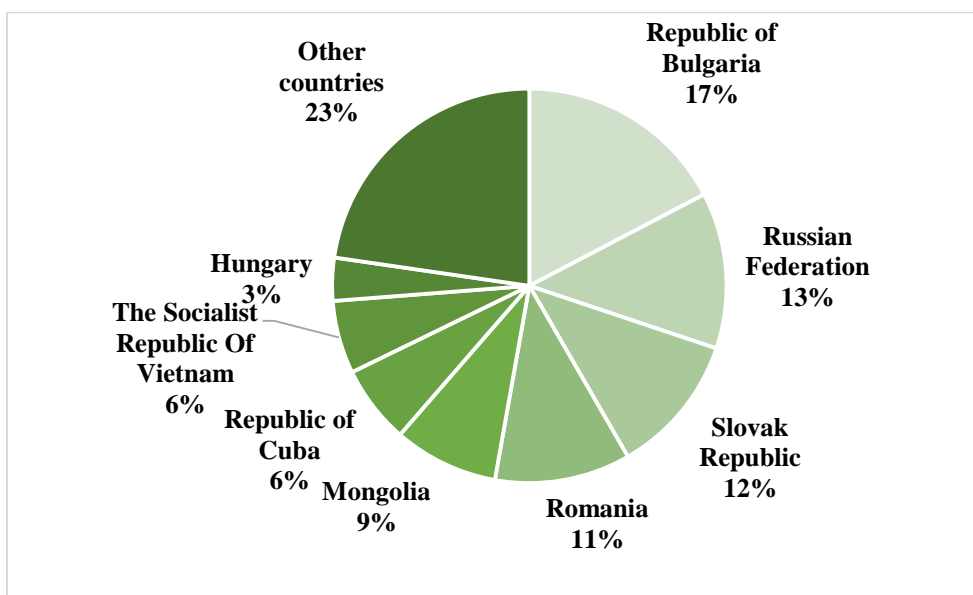
- ***Innovation***: this includes technology start-ups, companies with potential in the trade of new technologies based on its existing intellectual property and/or know-how, as well as acquisitions of new equipment (under five years old);
- ***Modernisation***: financing the acquisition of technologies, real estate and other capacities, necessary for the expansion of production;

- *Resource and energy efficiency*: this includes the financing of equipment aimed at calculating and optimizing the use of resources;
- *Social responsibility*: financing of projects aiming to encourage mutual exchange between the Member States in terms of technology transfer, know-how and workforce, as well as projects aiming to stimulate employment and the creation of new jobs in the Member States.

As part of the SME lending strategy, the Issuer, has supported the European Investment Fund (EIF), together with the Development Bank of Austria (OeEB, administering investment for the Austrian Ministry of Finance), the Czech-Moravian Guarantee and Development Bank (ČMZRB), the SZRB Asset Management (SZRB AM, asset management subsidiary of the Slovak Guarantee and Development Bank) and the Slovene Enterprise Fund (SEF), in the launch of a regional fund-of-funds initiative focused on boosting equity investments in Austria, Czech Republic, Hungary, Slovakia and Slovenia. EIF has contributed 40% of the EUR 80.3 million size of the CEFoF, which includes commitments of EUR 12 million by OeEB, EUR 8.2 million by ČMZRB, EUR 10m by SZRB AM and EUR 8 million by SEF, topped-up by EUR 10 million from the Issuer, another international financial institution. In April 2018 MFB Magyar Fejlesztési Bank Zártkörűen Működő Részvénytársaság (Hungary) joined as an investor the CEFoF increasing its size to EUR 97 million. The fund of funds is expected to mobilize at least around EUR 200 million in equity investments into SMEs and small mid-caps in the five countries, as well as additional investments in the wider region.

Industry sectors and geographic structure of the loan portfolio

In terms of geographic distribution, the structure of the gross loan portfolio (before allowance for loan impairment) as of 31 December 2018 was the following:



Source: The Financial Statements.

As at 30 June 2017, the aggregate amounts of the long-term loans and trade financing loans granted to the top four banks (in terms of the amount of the loans extended to them by the Issuer) amounted to EUR 99.80 million, representing 61% of the total amount of the loans granted to banks by the Issuer. By comparison, as at 31 December 2017, the total amount of such loans was EUR 70.1 million and as at 30 June 2018, this was of EUR 164.116 million, from which EUR 132.496 million are major or top five loans and EUR 1.577 million related allowances, representing 80.73% of the total amount of the long-term loans granted to banks by the Issuer. As at 31 December 2018 the total amount of such loans was EUR 176.63 million, from which EUR 148.61 were issued

to the top six banks with EUR 1,411 thousand related allowances, representing 84.14% of the total amount of loans granted to banks.

Out of the total amount of the loans extended to banks by the Issuer, as of 31 December 2018, 28.0% were provided to banks based in Cuba, 27.5% to banks based in Mongolia, 13.8% to banks based in Vietnam, and 30.7% to banks based in other non-member countries.

Also, as at 31 December 2018, the Issuer had extended loans to corporate clients in the amount of EUR 576.2 million loans net of allowance for loan impairment, out of which 17% was provided to corporate clients based in the Russian Federation, 23% to corporate clients based in the Republic of Bulgaria, 15% to corporate clients based in each Romania and Slovak Republic, 6% to corporate clients based in Hungary, 5% to corporate clients based in Mongolia, 4% to corporate clients based in Vietnam and 15% to corporate clients based in other countries.

In terms of sector concentration, as at 31 December 2018, 21% out of the Issuer's gross loan portfolio to corporate clients was provided to corporate clients active in the leasing industry and 31% to corporate clients active in the production and transmission of electricity industry, 8% was provided to clients active in communications, 5% to clients active in each of crude oil refining, wholesale and retail trade, 4% to clients active in each of food and beverage, financial services and mining, 3% to clients active in real estate industry, 2% to clients active in production of each of pharmaceutical products, agriculture, manufacturing of electrical equipment and oil and gas production industries.

Interest income and margin

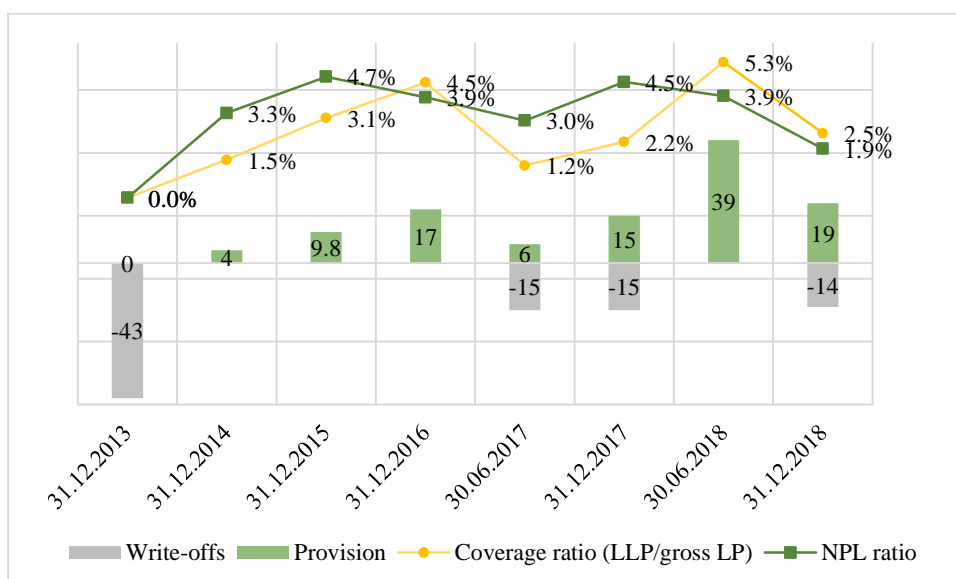
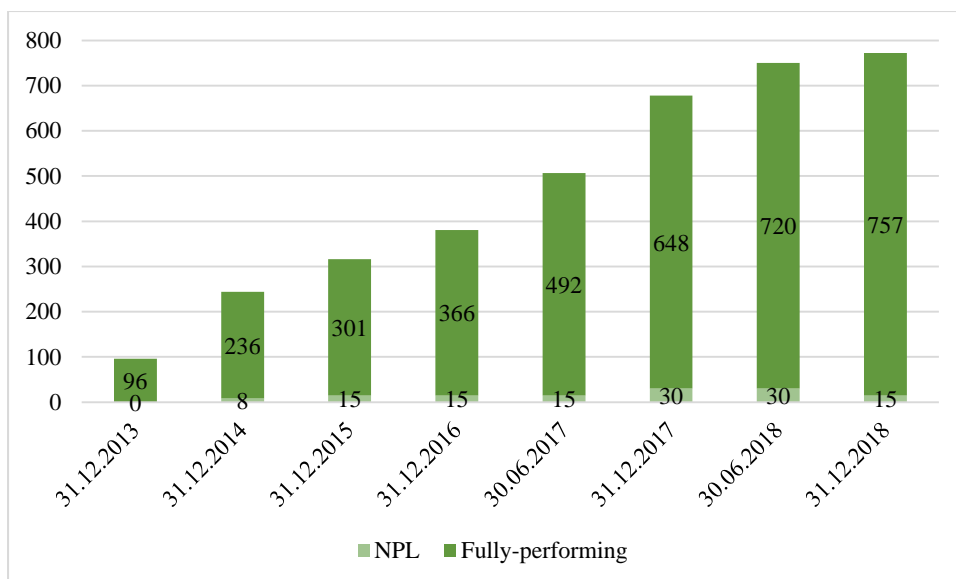
In 2017, the Issuer's interest income increased by EUR 3.4 million or 10.4% year-on-year, to EUR 35.96 million as at 31 December 2017 from EUR 32.5 million as at 31 December 2016. In 2018 the Issuer's interest income increased by EUR 9.96 million or 28% year-on-year, to EUR 45.92 million as at 31 December 2018.

The Issuer's total net interest income before allowance for loan impairment was of EUR 3.3 million as of 31 December 2017, compared to EUR 4.8 million as at 31 December 2016, representing a decrease of 31.2% or EUR 1.5 million in 2017. Since year 2018 the Issuer has begun including hedged percentages of cross-currency interest-rate SWAP to net interest income so the net interest margin as at 31 December 2017 was recalculated to EUR 21.8 million. As at 31 December 2018 the Issuer's total net interest income before allowance for loan impairment was of EUR 23.6 million, having increased by EUR 1.8 million or 8%.

The Issuer's net interest margin as of 31 December 2018 was 2.2%, compared to 2.5% as of 31 December 2017, having decreased by 0.2 percentage points year-on-year.

Non-performing loans

Until 2013, the Issuer had a significant historic burden in terms of the NPLs, which it managed to settle by 31 December 2013. Total value of NPLs as of 31 December 2012 was EUR 96.6 million, whereas total number of NPLs was 11. Significant part of the NPLs portfolio, in the amount of approx. EUR 54.7 million was sold in 2013 and the Issuer's Council agreed to write off the remaining part of the NPLs by 31 December 2013. The following charts show the development of the NPLs within the Issuer's aggregate credit portfolio and loan loss provisions as at 31 December 2014, 2015, 2016, 2017, 2018 and 30 June 2017 and 2018 respectively:



Source: The Financial Statements. The coverage ratio is calculated as ratio between the total amount of loan loss provisions and the core outstanding amounts under the loans extended by the Issuer.

Provisions for NPLs represented 1.9% (EUR 18.9 million) of the total outstanding amount under the loans granted by the Issuer as of 31 December 2018, compared to 5.3% as of 31 December 2017 decreasing by EUR 20 million due to implementation of IFRS 9 since 1st of January 2018. Changes during 2018 considered write-off of uncollectible amounts.

The total amount of provisions made according to internal provisioning instructions of the Issuer represented 2.2% (EUR 14.7 million) of total outstanding amount under the loans granted by the Issuer as of 31 December 2017, compared to 4.5% (EUR 17 million) as of 31 December 2016.

The Issuer's NPLs coverage ratio was 128.9% as of 31 December 2018, while the NPL ratio was, at the same date, of 1.9%, remaining below 5% since 2012.

Adjustment of the former sovereign debt of the Republic of Cuba

As part of the restructuring of the Cuban debt, the Issuer's Council 100th meeting of 5-6 December 2013 held in Moscow approved the conversion in EUR of the historic debt of the Republic of Cuba towards the Issuer, as well as a partial write-off of the Issuer's receivables against borrowers in the Republic of Cuba. The Issuer and the Republic of Cuba also agreed upon the principles and terms of the settlement of the remaining debt. The debt was restructured and agreed in the amount of the EUR 35 million to be repaid in 25 years.

Trade finance

As part of its re-launch strategy commenced in 2012 (see "*Strategy – Re-launch Programme and 2013-2017 Strategy. Main achievements.*"), the Issuer commenced to broaden its portfolio of trade finance products to provide its customers with the full range services, including irrevocable reimbursement undertakings, banking guarantees, counter-guarantees, standby letters of credit, trade related loans, financing under letters of credit covering trade finance operations of counterparty banks, advising letters of credit and guarantees, and ECA-covered finance, covering export and import transactions of the Member States. According to its mission, the Issuer's activities are focused on the promotion of trade and economic cooperation between the Member States and the support for the SMEs, which includes export-import supplies of hi-tech equipment, medical supplies, foodstuffs, consumer goods and services.

In April 2014, the Issuer executed a Multilateral Memorandum on Cooperation with a number of ECAs from Member States, including EXIAR, EXIMBANKA SR, EGAP, BAEZ and EximBank Romania. Pursuant to the Memorandum, the Issuer will act as a bridging financing institution, while the ECAs will provide insurance coverage in relation to projects carried out in cooperation by Member States. The Memorandum has been subsequently joined by other ECAs. Thanks to its relationships with ECAs, the Issuer was also recently included in the exclusive list of currently only 10 multilateral financial institutions rated under the OECD Export Credits Arrangements.

Since March 2015, the Issuer has participated in 140 trade finance deals supporting export from Czech & Slovak Republic, Hungary, Bulgaria, Russia and Vietnam as well as import to Russian Federation, Romania, Slovak Republic and Mongolia from Australia, Belgium, Poland, Germany, France, China, Italy, the Netherlands, Spain, Switzerland, Singapore, Oman, Turkey and Japan for total amount of EUR 260 million.

In 2015, the Issuer introduced its Trade Finance Support Programme (the "**TFSP**") and launched its new trade finance products, particularly aimed at increasing exports of goods from Member States to other countries, having successfully completed multiple trade finance deals, by issuing irrevocable reimbursement undertakings by the order of Russian, Belorussian, Armenian and Mongolian issuing banks in favour of, among others, Československá obchodní banka a.s. (Czech Republic and Slovak Republic), K&H Bank ZRT (Hungary), Raiffeisen Bank International AG (Austria), Commerzbank AG (Germany), Sberbank CZ a.s. (Czech Republic), Česká spořitelna s.a. (Czech Republic), OTP BANKA SLOVENSKO, A.S.(Slovak Republic), Aktif Yatirim Bankasi A.S. (Turkey), UniCredit Bulbank AD etc. in deals supporting export of different kinds of high-technology equipment from the Czech Republic, the Slovak Republic, Hungary to Belarus, Russia, Armenia and Mongolia as well as support of export from People Republic of China, Turkey, Australia, Germany, USA and Japan to Russia and Mongolia.

In 2016 and 2017, in line with its mandate, the Issuer continued to grow its trade finance portfolio and expand the geography of supported trade finance transactions. Still in 2016, for the first time, the Issuer has covered the risk of Mongolia's Golomt Bank towards Československá obchodní banka a.s. (ČSOB, Czech Republic), supporting delivery of automatic flour packaging line from the Czech Republic to Mongolia. This transaction is important, among other reasons, from the perspective of expanding geography with ČSOB, one of the main partners of the Issuer when it comes to trade finance.

In November 2016, the Council approved a new trade finance product – short term trade related loans ("**TRL**"). For the purposes of conducting trade finance operations, the Issuer has also concluded a number of master

agreements with financial institutions both from its Member States and from non-member countries to provide trade-related loans for such transactions.

Under the TFSP, in December 2016, the Issuer concluded its first framework agreement with Russian CB LOCKO-Bank on provision of TRL to finance foreign trade operations and carried out its first transaction in favour of the borrower in the amount of USD 1 million. The funds were used to finance supplies of products from Vietnam to the Russian Federation. In February 2017, the Issuer provided a short-term targeted trade related loan to Russian CB LOCKO-Bank for the amount of USD 3 million to finance the purchase of building and finishing materials made in Poland to be imported to the Russian Federation. From December 2016 until December 2018, the Issuer issued 35 TRLs for a total amount of approximately EUR 159 million.

On 23 March 2017, the Issuer issued the first direct guarantee as part of the TFSP, on behalf of the CJSC VTB Bank (Belarus) to secure payment obligations of the Atlant-M Farzeughandel JLLC, Volkswagen's general importer in the Republic of Belarus, to Russian Volkswagen Group Rus for the amount of RUB 260 million. The term period is one year.

In May 2017, the Issuer's TFSP was named best product at the Association of Development Financing Institutions in Asia and the Pacific (ADFIAP) Awards 2017, held in Macao, China.

In June 2017, the Issuer issued its first standby letters of credit by the order of Trade & Development Bank of Mongolia for total amount of EUR 0.5 million in favour of UniCredit bank (Russia) and securing Trade & Development Bank of Mongolia's payment obligations under its guarantees, while also signing a framework agreement on trade financing with Armenian ZAO ARMBUSINESSBANK. In August 2017, the first joint transaction was carried out under the Issuer's Trade Finance Support Programme (TFSP), consisting of an irrevocable reimbursement undertaking by the Issuer by the order of ZAO ARMBUSINESSBANK for EUR 2.2 million in favour of the Czech counterparty Československa Obchodni Banka A.S. (Prague). The first deal with ZAO ARMBUSINESSBANK expanded the geography of the Issuer's trade financing operations, guaranteed the supply of automated equipment for SHPP from the Czech producer and provided additional support to environmental initiatives in Armenia, in line with the Issuer's Development Strategy for the period 2018-2022 - under which the Issuer as a "green" development institution actively supports a number of priority sectors, including small and renewable energy.

Also, in December 2017, for the first time in its recent history, the Issuer supported an exporter from Bulgaria within its TFSP. This deal helped the Issuer to further diversify its portfolio of irrevocable off-balance sheet commitments related to trade finance.

The Issuer also consistently increases lending and investment activities in Mongolia. Since 2012, the total volume of the Issuer's investments in the Mongolian economy has amounted to over USD 650 million. Trade finance transactions are also growing at a rapid pace with the participation of Mongolian counterparts. Thus, starting from November 2016, the Issuer has executed 30 trade finance deals to support the supply of products from the Czech Republic, Japan, Oman, Switzerland, Russia, Belgium, Spain, and Germany to Mongolia for a total amount of EUR 2820.4 million. USD 12.4 million loan to Golomt Bank LLC in December 2018 supporting the import of oil products was the first trade-related financing provided by the Issuer to the Mongolian bank under Trade Finance Support Programme.

For 2018 the Issuer issued 33 trade finance deals for total amount EUR 108 million by the order of Armenian and Belorussian borrowers. In March 2018, the Issuer entered into a framework agreement on the implementation of trade finance transactions with Armenian Ardshinbank Closed Joint-Stock Company, which joined the Issuer's Trade Finance Support Programme (TFSP). As part of these arrangements, the Issuer executed the pilot transaction, issued irrevocable reimbursement undertakings by the order of Ardshinbank in favor of leading Bulgarian producer of technologies for small and medium-sized hydropower plants with the participation of UniCredit Bulbank AD (Bulgaria) as confirming bank for amount EUR 1.45 million. In April and August 2018 the Issuer provided its first trade-related loans (TRLs) to Belagroprombank, Belarus for the total amount of EUR 31.87 million in order to facilitate import of oil products from the Russian Federation to the Republic of Belarus. In October and November 2018 the first IRUs with the tenor of two years were issued on behalf JSC "Savings Bank "Belarusbank" to support the export of cotton fiber from the Czech Republic. In November-December 2018 the Issuer expanded its support of the Russian import from Belarus granting short-term target loans of EUR 30

million to OJSC “Development Bank of the Republic of Belarus” to finance deliveries of elevator equipment and automotive components.

Treasury - investment and trading activities

In 2017, the value of the Group’s treasury assets increased by EUR 86.8 million or 21% year-on-year from EUR 421.6 million as of 31 December 2016 to EUR 334.8 million as of 31 December 2017. As of 31 December 2018, the value of the Group’s treasury assets increased by EUR 11.2 million or 3.3% year-on-year, to EUR 346 million. The Group’s income generated by its investment and trading activities, has increased by EUR 2 million or 12% year-on-year in 2017 from EUR 16.7 million as of 31 December 2016 to EUR 18.7 million as of 31 December 2017, and, respectively decreased by EUR 12.2 million or 65% year-on-year to EUR 6.5 million as of 31 December 2018.

As of 31 December 2017, the value of the Group’s portfolio of available-for-sale investment securities decreased by EUR 53.9 million or 20% from EUR 269.3 million as at 31 December 2016 to EUR 215.4 million. As of 31 December 2018, the Issuer’s securities at fair value (classified under IFRS 9) portfolio decreased by EUR 11.1 million or 5% to EUR 204.3 million and consisted of (i) government bonds of the Member States *i.e.*, EUR-denominated, USD-denominated and RUB-denominated securities issued or guaranteed by the Ministries of Finance of these countries, maturing in 2023-2027, while the annual coupon rate for these bonds varied from 0.4% to 7.6%; (ii) corporate bonds issued by large companies and banks of Member States, as well as corporate international companies and development banks that have similar goals and missions as the Group, maturing in 2020-2028, with annual coupon rate for these bonds varying from 0.1% to 7.8% and (iii) equity securities, represented by shares and depositary receipts issued by large international companies.

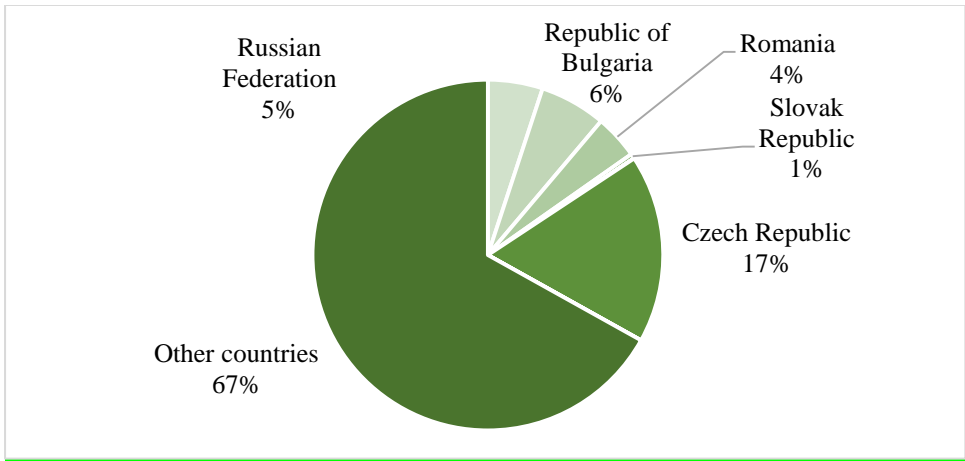
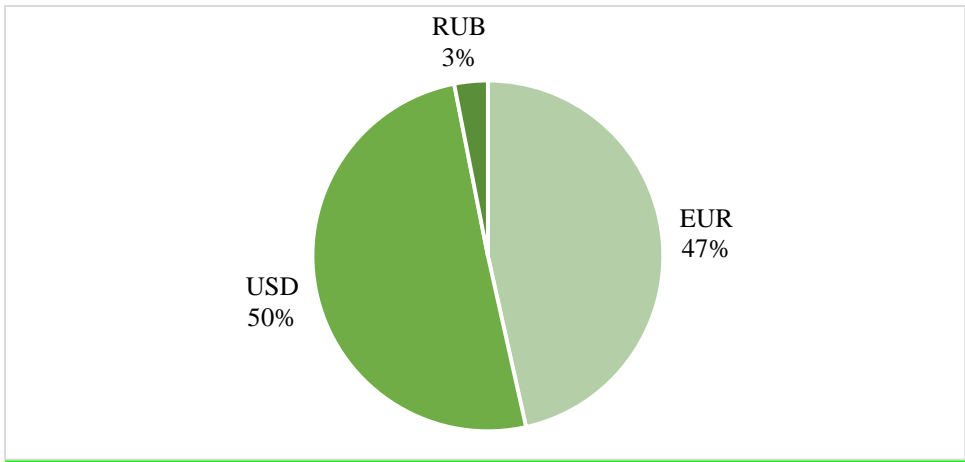
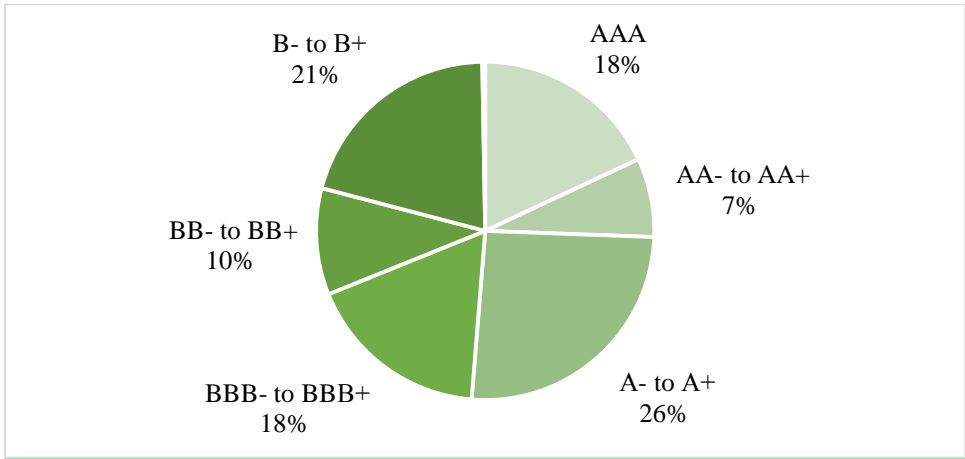
As at 1 January 2018, the Group reclassified a part of its securities previously classified as “available for sale” to “debt instruments measured at amortized cost”. These instruments satisfy the SPPI criterion and are held to collect related cash flows rather than for sale. Corporate bonds comprise investment grade bonds issued by large companies and banks of the member countries of the Issuer, as well as international companies and development banks with goals and missions similar to those of the Group. The bonds mature in 2021-2026 and the coupon rate varies from 1.8% to 2.1%.

The treasury division of the Issuer conducts its operations within a comprehensive framework set forth by regulations adopted by the competent governing bodies of the Issuer and the guidelines established by the Issuer’s Financial Committee. The treasury operations of the Issuer include short-term money market operations, including REPO operations with the Issuer’s portfolio of high-quality marketable securities. The Issuer’s treasury division is guided by the principles of transparency, accountability and profitability within conservative risk and limitations parameters.

The Issuer’s treasury policy is outlined in the 2018-2022 Strategy and the Issuer’s investment policy statement adopted on a yearly basis by the Issuer’s Management Board. In line with these documents, the main objective of Issuer’s treasury operations is to effectively manage the Issuer’s liquid assets in order to safeguard their liquidity, protect the Issuer’s capital and generate a stable financial return.

Treasury activities are regarded by the Issuer as ancillary to its main lending activities, generating return which may be further used to support the Issuer’s financing operations within the Member States.

As of 31 December 2018, the diversification of assets under Treasury management by ratings, currencies and countries was as follows:

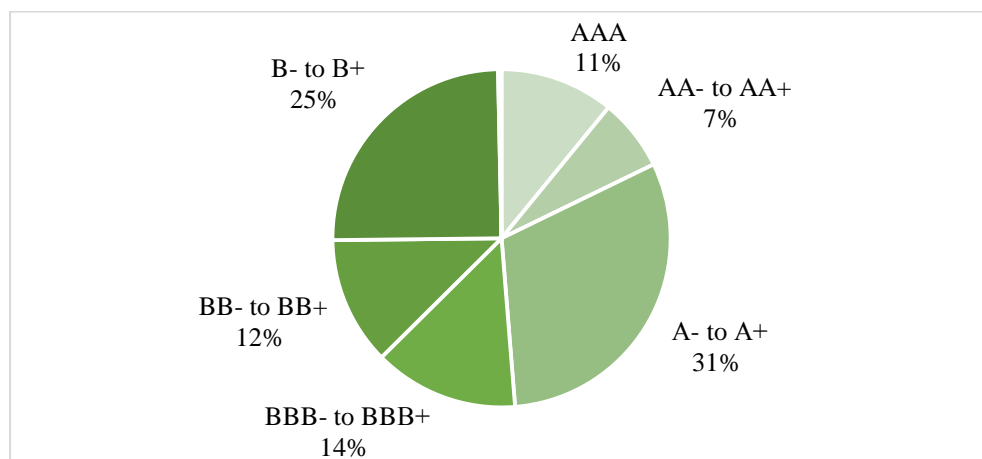
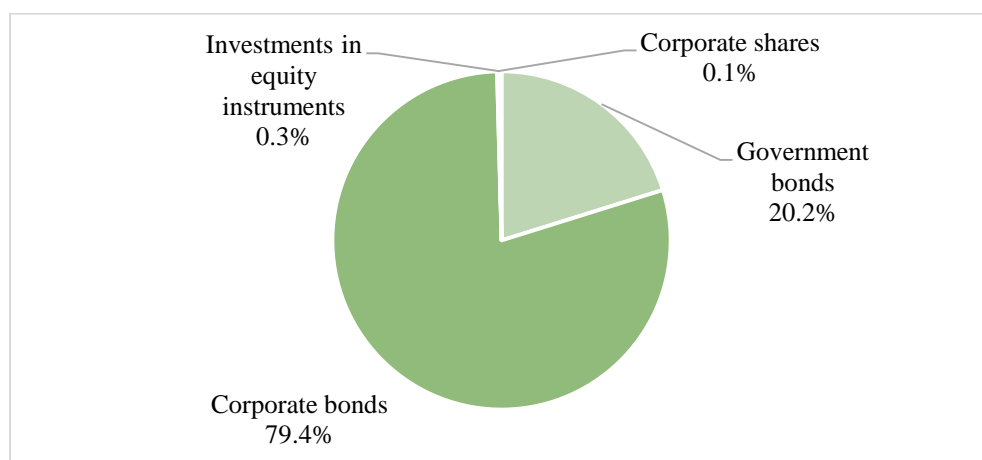


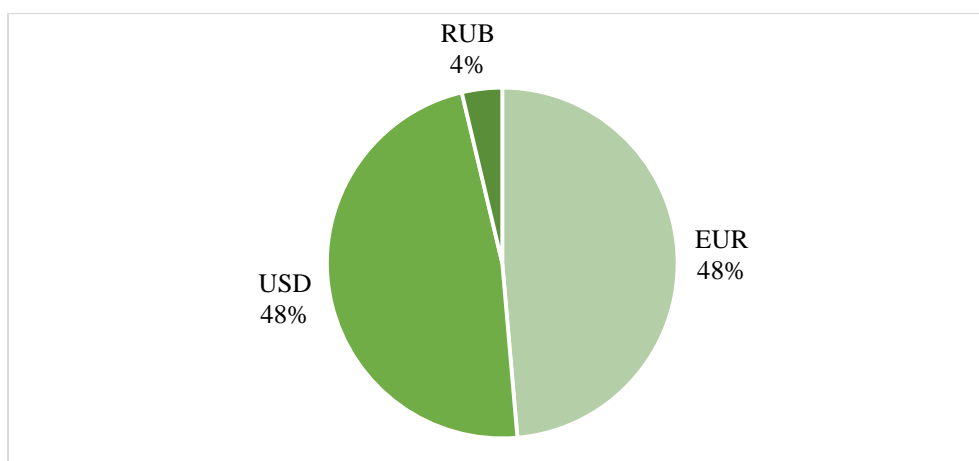
Source: The Financial Statements.

Primarily, the Issuer’s investment securities portfolio is composed of high-quality marketable sovereign and corporate debt securities with the fixed income issued by Member States and entities from Member States.

As of 31 December 2018, the Issuer’s government bonds comprise EUR- and USD-denominated securities issued and guaranteed by the Ministries of Finance of these countries. The bonds mature in 2023-2027. The coupon rate for these bonds varies from 0.4% to 7.6%, as well as corporate bonds comprise bonds issued by large companies and banks of the member countries of the Issuer, as well as international companies and development banks with goals and missions similar to those of the Group. The bonds mature in 2020-2028. The coupon rate for these bonds varies from 0.1% to 7.8%. As at 31 December 2018, bonds issued by Member States and other governments in the region represented 17% of the total value of the Issuer’s securities portfolio. Other investments bonds were made in respect in corporate of fixed income securities. As of 31 December 2018, bonds rated B- to AAA represented 100% of the total value of the Issuer’s corporate bonds portfolio.

As of 31 December 2018, the diversification of the AFS securities portfolio by types of instruments, currencies and ratings, was as follows:





Source: The Financial Statements.

The table below shows the break-down of the Issuer's available-for-sale securities, based on currency, amount and duration to maturity, as of 31 December 2018:

<i>Securities at fair value through other comprehensive income</i>	<i>Currency</i>	<i>Amount (EUR million)</i>	<i>Average Duration to Maturity</i>
	EUR	99,347	6.0Y
	USD	97,401	4.8Y
	RUB	7,584	6.1Y
	Total equivalent in EUR million:	204,332	
<i>Securities at amortized cost</i>	<i>Currency</i>	<i>Amount (EUR million)</i>	<i>Average Duration to Maturity</i>
	EUR	14,957	5.5Y
	USD	26,508	5.9Y
	Total equivalent in EUR million:	41,464	

Source: Information in column "Average Duration to Maturity" is extracted from the Group's management report.

In 2014, the Issuer decided to reclassify part of the securities portfolio as held-to-maturity in line with the International Accounting Standards IAS 39. The main goal for the reclassification was to secure earnings in form of permanent and steady coupon income at a moderate level of risk, while avoiding daily volatility in mark-to-market valuations. In July 2016, the entire held-to-maturity portfolio was transferred to available-for-sale with the additional capital gain. This action allowed the Issuer to sustain and improve its liquidity position in the face of high financial market volatility as well as to enhance its portfolio investment quality by using previously unutilized liquid assets to invest in securities with higher credit ratings, namely A-rated securities.

Foreign exchange risk is mitigated by using different hedging techniques, using derivatives or currency swaps. In line with the Issuer's commitment to keep up with regulatory environment relating to derivatives, these operations are carried out based on ISDA Master Agreements concluded with partners. The Issuer also conducts its operations by observing the standards set forth in the European Market Infrastructure Regulation (EMIR) adopted at EU level.

In 2014, the Issuer adhered to ISDA 2013 EMIR NFC Representation Protocol and ISDA 2013 EMIR Portfolio Reconciliation, Dispute Resolution and Disclosure Protocol.

Other operations

The Group also carries out several non-core activities, mainly through the Subsidiary, primarily consisting of lease operations with respect to its building. The Group rents out part of its building under operating lease agreements. As of 31 December 2017, the Group's revenues from lease of property increased by EUR 0.59 million or 17.15% to EUR 4.03 million, as compared to EUR 3.44 million as of 31 December 2016. As of 31 December 2018, such revenues increased by EUR 0.03 million or 0.1% to EUR 4.0 million, as compared to the same period of 2017.

COMPETITION

The Issuer operates in a relatively competitive market for the provision of financing for development projects. At first glance, the Issuer's principal competitors are national, regional and other international development banks as well as large local commercial banks operating within the region. As the Issuer's mission is to support economic growth and development in Member States, the Issuer attempts to avoid direct competition with commercial banks to the extent possible.

The Issuer does not, however, believe that it faces significant competition from small- or medium-sized commercial banks active in the region, which generally target different industries than the Issuer and offer shorter-term financing products, at less competitive interest rates. The Issuer also believes that its clearly defined mission and lending criteria, combined with the unique part of its mandate to foster economic cooperation between its Member States, spread on three continents, and to support relevant projects, do not generally overlap with those of other development banks active in the same region as the Issuer. On the contrary, the Issuer seeks to partner with other development banks in accomplishing its objectives, having already co-financed projects with leading development institutions such as the International Finance Corporation (IFC), the Black Sea Trade and Development Bank (BSTDB), the Eurasian Development Bank (EDB), the European Bank for Reconstruction and Development (EBRD) and the Netherlands Development Finance Company (FMO), as well as having concluded cooperation agreements with other such institutions.

RELEVANT GEOGRAPHIC MARKETS

For the reasons of achieving the Issuer's mission, which is to facilitate sustainable and inclusive growth and competitiveness of national economies of the Member States, the Issuer's loan and trading portfolio includes, and, most likely, will continue to include, concentrations in particular Member States. Accordingly, the economic situation in the Member States affects the financial conditions and prospects of the Issuer. The Issuer has specified its value proposition for each Member State, which is included in its recently adopted 2018-2022 Strategy, and is currently working to detail such strategic priorities in country strategies with, focus on the specificities of the development of the Issuer's operations within each Member State including potential partners and counterparties of the Issuer within the respective Member State.

According to its strategic vision, the Issuer's growth is associated mainly with increase of its loan portfolio in each Member State, focusing on syndications as well as integrational and flagship projects, with further diversification of its instruments, including the use of new funding sources, as well as with access to promising markets outside the Issuer's current geography. In this respect, the Regulation on the Special Status of Participation in the Activities of the International Investment Bank, approved at the Issuer's Council 106th Meeting held on 9 December 2016 in Moscow, Russia, provides for new types of cooperation between the Issuer and states, international financial institutions, or other banking, economic, or financial organizations and funds, such as those in the form of associated members (available to states and IFIs) or associated partners (available to other organizations and funds) or observer. These new identified forms of cooperation with potential partners is expected to enable the Issuer to launch dedicated work on analysing options for expanding its operating territory in the interest of its Member States.

This section of the Offering Circular sets out certain high-level information about the macroeconomic situation in the main current relevant geographic markets of the Issuer, as well as about the Issuer's main completed, pending or prospective operations in such markets.

Czech Republic

The Czech Republic has an open economy with strong links in supply chains and direct investments with Western Europe, in particular Germany. Car manufacturing is especially important; by itself it makes up 5-6% of GDP, and its weight could reach 8% when including suppliers. The economic policy framework is solid, stability-focused and counter-cyclical, which guarantees low output volatility. The Czech Republic has an independent monetary policy, based on its own currency, low amount of FX debt and an inflation target of 2%. Its fiscal policy also targets debt sustainability. These are the reasons why the World Bank ranks the Czech Republic 30th among the world's most attractive countries for doing business (source: The World Bank 2018 Doing Business Report). The Czech Republic is rated AA- with stable outlook by S&P, A1 with a positive outlook by Moody's and AA- with stable outlook by Fitch.

GDP growth slowed to around 3% in 2018 from 4.3% in 2017. Domestic demand looks set to be the main driver of GDP growth, with labour shortages and dependence on the external sector seen as potential downside risks for the economy. In 2019 and 2020 GDP growth could be 2.9% and 2.6% according to the European Commission (EC).

HICP inflation is forecast at 2.1% in 2018, down from 2.4% in 2017. Price dynamics will accelerate at the turn of 2018-2019, influenced by base effects and higher energy prices. The EC forecasts 2.2% annual HICP inflation in 2019, and 1.8% in 2020. However, the ongoing normalization of the CNB's monetary policy rates – there have been six rate hikes since August 2017 – should temper inflationary pressures.

In 2018, the general government budget had a surplus, which may have reached 1.0% of GDP (down from 1.5% in 2017), driven by almost equal increases of around 7% in both revenues and expenditures. In 2019, the headline budget surplus is expected to fall to 0.8% of GDP due to higher public wage growth and discretionary pension measures. Public wage hikes and recently adopted pension increases are expected to raise expenditures by around 0.5% of GDP. The debt-to-GDP ratio is set to decrease steadily from 34.7% of GDP in 2017 to 31.2% of GDP in 2020 according to the EC's forecast.

Trade finance products, launched by the Issuer in 2015 - 2018, have been especially popular in the Czech Republic – since from March 2015 until December 2018, the Issuer participated in 37 trade finance deals having an aggregate amount of approximately EUR 39.08 million, including IRUs in favour of CESKOSLOVENSKA OBCHODNI BANKA, A.S., Commerzbank AG, Sberbank CZ A.S., CESKA SPORITELNA A.S. supporting export operations of Czech Republic. In January 2016, the Issuer also disbursed the first tranche of a EUR 35 million credit facility signed in December 2015 with a Czech manufacturer of high-quality forgings, castings and ingots from steel and cast iron – the first loan granted by the Issuer to a Czech borrower in over 20 years.

In 2017 Československá obchodní banka, a.s. was awarded as the most active confirming bank in Czech Republic under the TFSP.

The Issuer expanded its Czech-based partnerships by concluding a Global Master Repurchase Agreement with Česká exportní banka in September 2015 and by concluding an ISDA Master Agreement with Sberbank CZ in July 2016.

On 18 September 2018, the Issuer closed its new trade finance deal with Ardshinbank CJSC (Armenia) for EUR 1.4 million where the Issuer provided its irrevocable reimbursement undertaking to confirming bank - Československá obchodní banka, a.s. (Czech Republic) – under a letter of credit. In this particular deal the Issuer supported the leading Czech producer of technologies for small and medium-sized hydropower plants. This is the fourth deal closed by the Issuer with this exporter.

In April 2018, the Issuer successfully placed its inaugural CZK denominated private placement transaction with 3-year floating rate notes amounting to CZK 501 million on the Czech market. In June 2018, the Issuer decided to go another step forward in the capital market funding strategy and tap the outstanding April 2021 CZK Floater with an amount of 249 million, totaling to CZK 750 million.

Hungary

Hungary is middle-income, small, and very open CEE country with diversified export and economic structure. Hungary is highly integrated into the EU, as around 80% of total exports go into the EU. The PPP GDP per capita

is roughly 30,000 USD. On the expenditure side, households' consumption expenditure is around 50% of GDP, fixed capital formation is around 20-23%, while exports and imports are around the 90% and 80% of GDP, respectively. Government consumption is around 20% of GDP.

Hungary is rated BBB- with a positive outlook by S&P and Fitch, Baa3 with a stable outlook by Moody's but these ratings do not reflect the Hungarian economy's high resistance against external shocks. Hungary has a C/A surplus, around the 2% of the GDP in 2018, and a budget deficit around 2% of GDP. Although public debt is around 15%points higher than the CEE average, it has significantly declined in the past few years. Furthermore, government debt owned by non-residents fell from 60% of GDP to below 30%, while the share of FX debt fell from 50% to 20%. External debt came down from around 115% of GDP to the CEE average level. The indebtedness of the private sector is low; households' loan-to-GDP ratio is around 17% of GDP, the lowest in the CEE region. Non-financial corporation' loan-stock-to-GDP ratio is also around 17-18% of GDP.

Hungary's GDP growth could be 4.5% in 2018, after 4.3% in 2017, and it can remain around 4% in 2019. The main drivers of the economic growth are households' consumption and fixed capital formation. The latter could grow by more than 15% in 2018. Households' consumption growth is supported by the very favourable labour market situation, as the unemployment rate remained at historical low levels and it boosts wage growth. Activity rate on the labour market is much closer to CEE peers than before the crisis.

From March 2015 until December 2018 the Issuer has issued 9 trade finance deals, including IRUs, in favour of Commerzbank AG, K&H Bank Zrt, UniCredit Bank Hungary ZRT and SBERBANK MAGYARORSZAG ZRT for total amount EUR 2,53 million. Supporting export operations of Hungary and has successfully covered payment under 8 expired trade finance deals.

In October 2015, the Issuer also concluded an ISDA Master Agreement with OTP Bank, followed by a Strategic Cooperation Agreement with the same party in June 2016. In June 2016, the Issuer has concluded an ISDA Master Agreement with Eximbank Hungary. Also, in June 2016, the Issuer and the Ministry of Foreign Affairs and Trade of Hungary signed a Memorandum of Understanding providing a basis for coordination of activities between the Issuer and the Hungarian authority in such areas as credit support for SMEs, implementation of export-import operations, investments and sustainable development financing.

Until August 2018 the Issuer had HUF account in KBC Bank, NV for operations in Hungarian forints. However, subsequent to increase of operations in HUF and for cost-cutting reasons, the Issuer opened HUF account in OTP Bank Nyrt in August 2018.

The Board of Governors of the Issuer resolved on the relocation of its Headquarters from Moscow to Budapest on December 4, 2018. Based on this decision, on 05 February 2019, the Government of Hungary and the Issuer have signed the Agreement regarding the seat of the IIB Headquarters and the Agreement was ratified by the Hungarian Parliament on 5 March 2019.

Mongolia

Mongolia is a country with a vast territory but small population. It is a relatively underdeveloped commodity-exporting country. Within GDP the share of mining is 25%, the share of agriculture reaches 13%, while manufacturing is underdeveloped (only 7%), just like the service sector (40%). On the expenditure side, consumption has a share of 50%, investments accounts for 20% of gross domestic growth. GDP per capita is roughly 12,000 USD on PPP basis, which ranks Mongolia in the lower third of the countries in the world.

The main export goods are metals. Its most important export partners are China (85%) and Switzerland (10%, mainly rare earth materials). Imports are coming from China (40%), Russia (30%), Japan (10%) and South Korea (10%).

Mongolia is rated B with stable outlook by S&P, B3 with stable outlook by Moody's and B with stable outlook by Fitch. The average growth in the past 30 years was just above 4%, but around 7% over the past 10 years.

Being a commodity exporter country, Mongolia is susceptible to commodity price shocks, which was highlighted during the financial crisis and again in 2014. After 2011 the Mongolian economy became overheated due to rising commodity prices, pro-cyclical fiscal policy and strong lending. This resulted in a high current account deficit, so after the fall in commodity prices, a crisis hit the country. The central bank had to spend the majority of its FX

reserves on intervention, but the MNT depreciated almost 100% against the USD between 2011 and 2016. From 2016 depreciation went on, albeit at a more moderate pace. In 2017, in order to mitigate macroeconomic vulnerabilities, Mongolia requested a three-year arrangement under the IMF's Extended Fund Facility (EFF), with access to the equivalent of USD 434.3 million. Finally, with the help of Russia, China, Japan and South Korea, the country received USD 5.5 bn worth of package. Since the start of the programme, the country has managed to introduce reforms aiming at macroeconomic stability and debt sustainability. However, as commodity prices rose again, the key structural reforms stalled. All in all, the IMF expects the country to grow by around 5% in the next five years, while inflation is likely to be around 7%. Reducing the government and current account deficit should be the key goal of the economic policy.

In 2015, the Issuer has also concluded ISDA Master Agreements and Global Master Repurchase Agreements with Trade&Development Bank of Mongolia, Khan Bank and XacBank. As of 30 June 2018, loans extended by the Issuer to clients in Mongolia amounted to more than EUR 75 million.

For 2016-2018, the Issuer has issued 30 trade finance deals for EUR 20.4 million including IRUs and standby letters of credit in favour of Československá obchodná banka, Commerzbank AG (Germany and Japan offices), UniCredit bank (Russia) and KBC Bank N.V. and a USD 12.4 million trade-related loan supporting export operations from Czech Republic, Japan, Switzerland, Belgium, Germany, Oman, Singapore, Spain, the Netherlands, and Russia to Mongolia.

Also, at the 21st meeting of the Russian-Mongolian Intergovernmental Commission (IGC) on Trade, Economic, Scientific and Technical Cooperation held in Moscow on February 28, 2018, the Issuer concluded an agreement with the Development Bank of Mongolia (DBM) on provision of the additional funding to the Mongolian party. The agreement calls for raising the Issuer's lending limit for DBM to EUR 50 million for a period of up to seven years to implement socially and economically significant projects in Mongolia.

Republic of Bulgaria

Bulgaria is a small economy with low level of diversification, dominated by cycle-sensitive industries, with tourism being one of the most important sectors. The country has a currency board system – the tightest form of a fixed exchange rate mechanism – therefore monetary policy is not available to counteract business cycle fluctuations. This role would fall solely on fiscal policy, but because of the low domestic savings rate and relatively weak institutions, fiscal tools are unable to adequately mitigate economic downturns. Consequently the Bulgarian economy is prone to overheating, and recessions tend to be longer and deeper, accompanied with persistently high unemployment.

After a prolonged period of economic weakness, robust growth returned in 2015-2017 with an annual average GDP expansion of 3.7%. Exports and household consumption were the main drivers of growth. The current account swung to an over 3% surplus, which allowed external debt to fall from 55% to 41%, significantly reducing vulnerability. Government debt increased as a result of the financial crisis and because of higher budget deficits around 2015, but fiscal discipline returned from 2016 on, setting the debt-to-GDP ratio on a downward path.

The economy slowed down in 2018 due to a mix of domestic and external factors. Unemployment rate has fallen to an all-time low this year, and combined with unfavourable demographic trends, it shows that labour market reserves have been exhausted. The external economic environment has also deteriorated (signs of slowdown from the eurozone and worries about trade war), and exports to key markets (Turkey and Russia) shrank considerable this year. The market consensus for economic growth in 2018 is 3.4%, with consumption and investment being the main drivers of expansion. From 2019 onwards, there might be a partial recovery in exports, but headline economic growth is expected to stay below the 2015-2017 dynamics, due to labour force constraints and unfavourable international economic environment.

Bulgaria is rated BBB- with a positive outlook by S&P, Baa2 with a stable outlook by Moody's and BBB with a stable outlook by Fitch.

The main operations of the Issuer in Bulgaria consist of the extension of loans to corporate clients, mainly active in the field of manufacturing, construction of buildings and transport and warehousing.

In June 2015, the Issuer has also concluded a Global Master Repurchase Agreement with Bulgarian Development Bank.

For 2017-2018, the Issuer has issued 6 trade finance deals for EUR 4.87 million including IRUs and guarantees in favour of Commerzbank AG and UniCredit Bulbank AD supporting export of technological equipment and small hydropower plants from Bulgaria to Armenia and Republic Belarus

Republic of Cuba

Cuba is a centralised economy, which started to loosen government control in some parts of the economy in 2011. Economic data from the country is very sparse and sometimes unreliable, but the estimated average annual economic growth may have been around 2% between 2008 and 2018.

In terms of trade, the country is a closed economy; its trade per GDP ratio is very low. The main hard currency revenue of the economy comes from the tourism sector, while its main consumers are the agriculture and energy sectors. Investment per GDP is 10% in Cuba, the half of its peers in South America and the Caribbean. The low level of investment cannot cover even the amortization costs. The economy is in dire need of economic reforms and foreign capital. Since 2015, the country's growth prospects have somewhat reinvigorated as diplomatic ties between the US and Cuba were restored. Moody's credit rating on Cuba is currently Caa2 with stable outlook.

After writing-off the historic debt of the Republic of Cuba in 2013, the Issuer re-affirmed its support and intention to contribute to the country's economic and social development once with the execution, on 24 June 2016, of the Agreement on Cooperation in Organising Financing between the Issuer and the Central Bank of Cuba (CBC). Under the terms of the Agreement, the parties also express their intention to improve the efficiency and the level of participation in projects and sectors that are of particular interest for the Republic of Cuba.

For 2015-2018, the Issuer has completed seven trade finance deals in the amount of EUR 21.7 million, including IRUs, in favour of KBC Bank N.V. supporting export of Cuban cane raw sugar to Republic of Belarus.

Romania

Romania is an above-average-sized, diversified, but less developed CEE country, with growth potential above the regional average. Despite moderate public and private indebtedness, volatility in growth also tends to be high in regional comparison, as debt-euroisation limits the monetary policy's room for manoeuvre, while the low amount of domestic savings and the tendency for pro-cyclical fiscal policy make the country vulnerable to external shocks.

Growth has been really strong since 2015, as the recovery from the crisis has been supported by very favourable external environment and by pro-cyclical & aggressive fiscal loosening economic policies. Public wage and pension hikes, combined with tax cuts, resulted in double-digit wage growth and fast consumption growth of 5-10%. Romania's GDP growth reached 6.9% in 2017, before decelerating to around 4% in 2018 as the impact of earlier stimulus measures faded. Unemployment fell to all-time low levels. As strong consumer demand fuels imports, the current account deficit exceeds 4% of GDP, which is high in regional comparison but could not be considered unsustainable, because the deficit is fully covered by EU transfers and FDI.

After a long period of loose monetary policy, the National Bank of Romania started monetary tightening in Q4 2017, as the RON faced depreciation pressure and inflation exceeded the 2.5% target in 2017 and 2018, because of strong demand and higher oil prices. A number of hikes sent the effective money market rates to around 3% by now, from close to zero in 2017. Recently the central bank adopted a wait-and-see approach as inflation started to moderate toward the target, after reaching the peak above 5% in the first half of 2018.

In 2019 and beyond, GDP and consumption growth rates may slow further, to around 3.5%, and then to 3%. Investment activity could remain lacklustre as in December 2018 the government announced to impose sector levies on banks, retailers, and the energy sector, in order to prevent the deficit from exceeding the 3% Maastricht threshold. As fiscal and monetary room for manoeuvre in implementing counter-cyclical policies is narrow, external shocks pose higher risk than in other CEE countries.

Romania benefits of a limited negative impact stemming from the Ukraine-Russia conflict and Western sanctions (due to low trade and financial links and the natural gas consumption being mainly covered by domestic production). International rating agencies recognize the country's quite stable financial position, thus Romania is

rated BBB- with a stable outlook by S&P, Baa3 with a stable outlook by Moody's and BBB- with a stable outlook by Fitch.

Romania is one of the Member States in which the Issuer's activity has continually increased as of its re-launch at the end of 2012 – beginning of 2013. In 2015, the Romanian direction of the Issuer's activities gained a new momentum. The Issuer has been consistently increasing the volume of investments in Romania and regularly presents its financial products and services to local businesses. Since its relaunch in 2012, and as of the date of this Offering Circular, the Issuer signed loan agreements with Romanian companies amount to more than EUR 50 million. In October 2015, the Issuer successfully placed its debut bond issue on the Bucharest Stock Exchange in the amount of RON 111 million. In relation to this placement, the Romanian Stockbrokers' Association awarded the Issuer for contribution to the development of the country's corporate bonds market. The debut issue was followed by a second successful RON 300 million bond issue in September 2016 and by two dual tranches bond issues in September 2017, *i.e.* a RON 300 million tranche and, respectively, a EUR 60 million tranche and in October 2018, a RON 300 million tranche and, respectively, a EUR 80 million tranche. Romanian market is currently the main market for IIB's funding surpassing for the first time Russia at the end of 2018.

In 2018 the Issuer participated in the subordinated bond issue of Banca Transilvania, the Issuer took in a position EUR 10 million share of the issue through its brokerage agent BRD-Groupe Societe Generale S.A.

Eximbank Romania, the export-import bank of Romania, is a party to the Multilateral Memorandum on Cooperation concluded between the Issuer and a number of export credit agencies in Member States, whereby the parties agree that the Issuer will act as a bridging financing institution, while the ECAs will provide insurance coverage in relation to projects carried out in cooperation by Member States.

In Romania, the Issuer intends to focus its investment efforts on areas that support the social sector, especially health, agriculture, tourism, manufacturing, trade, development of small and medium-sized enterprises, infrastructure, energy and other projects that may arise during the implementation of its development strategy.

Other recent activities in Romania include the execution of an ISDA Master Agreement with Banca Transilvania, in October 2015.

In 2017, the Issuer implemented a pilot deal with the B&N Bank (PJSC) by providing a short-term targeted trade related loan (TRL) for the supply of chemical additives from the Russian Federation to Romania. The volume of loan is of EUR 2.25 million, with a one-year repayment term.

In 2017 the IIB advised its first banking guarantees issued by Banca Transilvania. Total amount of advised Romanian guarantees for 2017-2018 is EUR 0,257 mln (3 guarantees).

Russian Federation

The Russian economy has witnessed a dramatic boom with an average growth rate of 7.1% in the 2000-2007 period due to surging commodity prices. As a result, it became the sixth largest economy in the world by purchasing power parity. However, the sharp drop in GDP by 7.8% during the financial crisis of 2008/2009 showed the high vulnerability of the Russian economy to external shocks and its overly high dependency on volatile commodity prices. Resurging oil prices have been a major factor of the recovery since 2010, while low investment/weak business climate, low spare labour force and lack of free capacities have hampered growth rates to return to pre-crisis levels. Even before the current geopolitical turbulences between the West and Russia, the Russian economy has substantially cooled down, as growth rates in 2012 fell to 3.7%, in 2013 to 1.8%.

In 2014-2015, the dual external shock from oil prices and sanctions from the international community triggered first a substantial slowdown, and afterwards recession (growth rate in 2015 stood at -2.5%). Eventually a moderate recovery re-emerged from 2016 and continued in 2017 (growth turned out at 0.5% and 1.5% respectively), driven by a recovery in oil prices, re-emerging lending flows in the household sector, improving labour market conditions as well as some large infrastructural projects. Nonetheless, apart from the fact that the macro-policy set-up become very solid (introduction of a medium term fiscal rule and inflation targeting in monetary policy as well as restructuring of the banking sector), the essential structure of the economy has not changed, and the dominance of the energy sector prevails. Additionally, geopolitical risks hinder foreign direct investment inflows and technology import.

Real GDP growth is expected at 1.7% for 2018, and will be followed by a slight slowdown to 1.5% for 2019 (both Focus Economics, January 2019 survey), mostly on account of a VAT hike from January. Primary growth engines are household consumption and exports, while government consumption and investments are foreseen to add a smaller contribution. The latter reflects the effect of still tight fiscal policies, although the adopted 3 year budget envisages a pick-up in infrastructural spending.

Repeated waves of US sanctions led to capital outflows, weaker currency and negative investment dynamics throughout 2018, but high oil prices and conservative macro policies helped the country to pile-up international reserves to around USD 460 bn, levels seen last time seen in 2014. Additionally, the rainy-day fund (national wealth fund) returned to around 5% of GDP. Higher reserves, flexible but tight macro policies and a restructured banking sector makes the country more resilient to adverse shocks. However tight policies come at the cost of slow growth, amidst lingering further international sanctions.

Reflecting positive economic developments, credit rating agencies upgraded either the rating (S&P) or the outlook (Moody's and Fitch) for the country throughout 2017-2018. Russia is currently rated at BBB- with a stable outlook by S&P, Ba1 with a positive outlook by Moody's and BBB- with a positive outlook by Fitch.

Russian Federation is a member of the Eurasian Economic Union, which is set to achieve free movement of goods, services, capital and labour inside the economic region. The block is expanding by setting up new trade agreements and dialogue with different country blocks, like the ASEAN and MERCOSUR regions.

On the other side, the Russian Federation is part of the consistently expanding free trade zone within the Eurasian Economic Union. After Vietnam acceded to the free trade zone in May 2015, trade activities between Russia and Vietnam gained a new impetus and are expected to increase significantly.

The Issuer's most recent activities in the Russian Federation include loans to customers active in wholesale and retail trade; repair of motor vehicles, manufacturing, transport and warehousing. During 2014 and 2015, the Issuer also successfully completed four issues of 10-year bonds (subject however, to the Issuer's put option, exercisable in accordance with the programme documentation and the relevant terms and conditions of each placement), in the aggregate amount of RUB 14 billion, admitted to trading on the Moscow Exchange. In March 2016, the Issuer registered a RUB 100 billion programme of exchange-traded bonds with the Moscow Exchange – the first of its kind by an international financial institution in the Russian Federation. In June 2017 the Issuer successfully placed a bond issue in the amount of RUB 10 billion (approx. EUR 156 million), issued under the earlier registered programme of exchange-traded bonds on Moscow Exchange.

In 2015, the Issuer has also concluded various treasury agreements and correspondent banking agreements with banks in Russian Federation, including: ING BANK (EURASIA), Gazprombank, Credit Bank of Moscow, Transcapitalbank, Expobank, Industrial and Commercial Bank of China (Moscow), Sberbank, Bank Zenit, UniCredit Bank, IBEC (IFI based in Russian Federation) and Rosbank.

In August 2018, the Issuer opened USD account with overdraft facility with PJSC Rosbank.

For 2015-2018 the Issuer has participated in 49 Russia related trade finance deals for EUR 162.5 million including IRUs, banking guarantees and TRLs.

Slovak Republic

Slovakia's economy, which has been growing by more than 3% each year since 2015, is clearly one of the best performers in the CEE region. The available data confirm the view that growth has reached its maturity phase; its structure is balanced. Preliminary figures indicate that Slovakia's economy soared more than 4.0% last year. Domestic demand (household consumption, and the resuming investment) clearly became the engine of growth, which will be firmly supported by the rising employment, the robust wage growth, and the revival of the loan market. No meaningful risks seem to surround sustainability – the budget deficit is small, government debt is on a declining trajectory, and external debt is steadily shrinking. Slovakia's public deficit stood near 1% of GDP (ESA concept) and the government debt was around 50% of GDP in 2018. On average, harmonized consumer prices grew by 2.5% year/year in the first 11 months of the year.

The slowdown in the economic growth rate of core EU countries poses downward risk to growth, which may leave its mark on the performance of Slovakia's export sector, but the new car factory's positive effect on Slovakia's export capacities and trade performance will be strong. The shrinking of 'spare' capacity on the labour

market may soon hinder production. The problem of labour shortage can become a more serious issue in 2019. There is also uncertainty about the recent political scandals and problems over the use of EU funds, as well as any possible sanctions.

The high credit ratings from major agencies rank the Slovak Republic at the top of the rating ladder, compared with other countries in the CEE region. Slovakia's sovereign rating stands high, at A+ with stable outlook (S&P), A2 with positive outlook (Moody's), and A+ with stable outlook (Fitch).

The Slovak Republic is the first EU member state in which the Issuer completed the placement of bonds on the capital markets, with the first issue in the amount of EUR 30,000,000 having been successfully finalized in October 2014. Also, the first regional office opened by the Issuer, aiming to increase the quality of the Issuer's services in EU member states, is based in the Slovak Republic.

For 2015-2018 the Issuer has issued 7 trade finance deals supporting export and import with Slovak Republic for EUR 3.84 million including IRUs and TRLs. Also, the Issuer's portfolio of loans to customers in the Slovak Republic, amounts to EUR 89 million.

Vietnam

The country has enjoyed around 7% annual economic growth over the past 30 years. This is mainly because Vietnam is an underdeveloped country. In the past couple of decades its growth has been fuelled by the reallocation between sectors and its export-oriented growth strategy, which partly stemmed from low wages.

Currently 17-19% of GDP is produced in the agricultural sector, which employs 45% of the labour force. This means that a large part of employment will flow to other sectors as the country becomes more developed. These sectors' (manufacturing and services) value added is usually higher, and this could create a growth opportunity for Vietnam.

The main destinations of Vietnam's exports are China, Japan, USA, and South Korea. The export structure is considered well-diversified. Around a quarter of exports come from low-value-added agricultural products, while machinery, equipment, and vehicles make up 32% of exports.

The country improved its trade relations and signed trade deals with various countries, but the business environment only improved slightly, as reflected in the World Bank's Doing Business report.

Overall, Vietnam is already a very open economy (with exports and import amounting to 160% of GDP). In the second half of 2019, its free trade deal with the EU will come into force, potentially boosting its growth potential. However, there are signs that economic growth may slow in the future. First of all, the 6% GDP growth rate was sustained only with the increase in private debt. The debt of the private sector exceeds 100%, and the leverage of non-financial companies is high. Furthermore, local companies' productivity is only one-fifth of the international companies operating in Vietnam. Finally, government debt has increased from 42% to 60% since 2012 – this is considered high, compared to the country's development stage. The decrease of the current 5% government deficit could dampen short-term growth prospects.

Vietnam is rated BB- with a stable outlook by S&P, Ba3 with a stable outlook by Moody's and BB with a stable outlook by Fitch.

As of 31 December 2018, 13.82% of the loans (in terms of amount thereof) extended to banks by the Issuer were granted to Vietnam-based banks. Also, the Issuer's portfolio of loans to customers in Vietnam, amounts to EUR 22 million. In the end of 2016 the Issuer provided trade related loan to LOCKO-Bank (Russia) for USD1 million under Trade Finance Support Programme as support of export from Vietnam to Russian Federation of food products.

In 2018 the Issuer advised its first letter of credit issued by VietinBank for USD 1.15 mln.

MEMBERS

The Issuer currently has nine Member States, namely: Czech Republic, Hungary, Mongolia, Republic of Bulgaria, Republic of Cuba, Romania, Russian Federation, Slovak Republic and Socialist Republic of Vietnam. The Issuer benefits from the high geographical diversification of its Member States. Their territories and, therefore, the

Issuer's relevant geographic market, cumulates approx. 19.6 million square km and a total population of more than 300 million people.

Hungary re-joined the Issuer in 2015, after having previously decided to terminate its membership in the Issuer in 2000. The Issuer's Council approved Hungary's request to re-join the Issuer in November 2014 and Hungary finalized all necessary procedures and ratified its membership in the Issuer in May 2015.

The Government of Mongolia made an additional contribution of EUR 1,909 thousand to the Issuer's equity on 27 December 2017.

On 12 July 2018, the Government of Romania made a contribution of EUR 4.0 million to the Issuer's paid-in capital. As a result, the paid-in capital of the International Investment Bank amounted to EUR 318.96 million.

On December 20, 2018, the Czech Republic made an additional contribution to the Issuer's paid-in capital in the amount of EUR 7 million (out of EUR 12.6 million planned). As a result, the paid-in capital of the International Investment Bank amounted to EUR 325,96 million.

As of 31 December 2018, the structure of the Issuer's paid-in capital is the following: the combined share of EU Member States (the Czech Republic, Slovakia, Hungary, Romania and Bulgaria) in the Issuer's paid-in capital reached 50.16%, Cuba's share is at 1.64% and the share of Asian Members of the Issuer (Vietnam and Mongolia) is at 2.17%. Russia's share in the Issuer's paid-in capital is 46.03%.

After the entry into force of the Protocol, the quotas of Member States in the authorised capital of the Issuer are as follows:

Member States	<i>Quotas in the authorised charter capital (EUR)</i>	<i>Shares in the paid-in charter capital (EUR)</i>
Republic of Bulgaria	123,000,000.00	42,203,226.32
Hungary	121,400,000.00	40,000,000.00
Socialist Republic of Vietnam.....	4,700,000.00	3,669,274.56
Republic of Cuba	23,400,000.00	5,360,773.37
Mongolia.....	6,200,000.00	3,393,184.85
Russian Federation.....	580,700,000.00	150,025,792.59
Romania	76,700,000.00	22,453,958.51
Slovak Republic	62,800,000.00	21,481,113.06
Czech Republic	125,600,000.00	37,374,957.01
Total.....	1,124,500,000.00	325,962,280.27

The unallocated portion of the Issuer's authorised charter capital is EUR 875,500,000.00.

The table below shows the paid-in capital structure of the Issuer as of 31 December 2018:

Member States	Share in the Issuer's paid-in capital	
	<i>(EUR million)</i>	<i>%</i>
EU Member States		
Czech Republic	37.37	11.47

Hungary	40.0	12.27
Republic of Bulgaria	42.2	12.94
Romania	22.45	6.89
Slovak Republic	21.48	6.59
Total contribution by EU Member States	163.5	50.16
Non-EU Member States		
Mongolia	3.39	1.04
Republic of Cuba	5.36	1.64
Russian Federation	150.03	46.03
Socialist Republic of Vietnam	3.67	1.13
Total contribution by non-EU Member States	162.45	49.84
Total contribution of Member States	325.96	100.0

Source: The Group's management report.

MANAGEMENT AND GOVERNANCE

General

The new edition of the Statutory Documents that entered into force on 18 August 2018 introduced a new governance structure. In this regard, two new governing bodies, i.e., the Board of Governors and the Board of Directors, are being formed.

The Issuer's governing bodies are the following:

- the Board of Governors, which is the supreme collective governing body of the Issuer;
- the Board of Directors, which is the Issuer's collective governing body responsible for the general management and oversight of the Issuer's operations, reporting to the to the Board of Governors; and
- the Management Board, which is the Issuer's executive body, reporting to the Board of Directors and the Board of Governors.

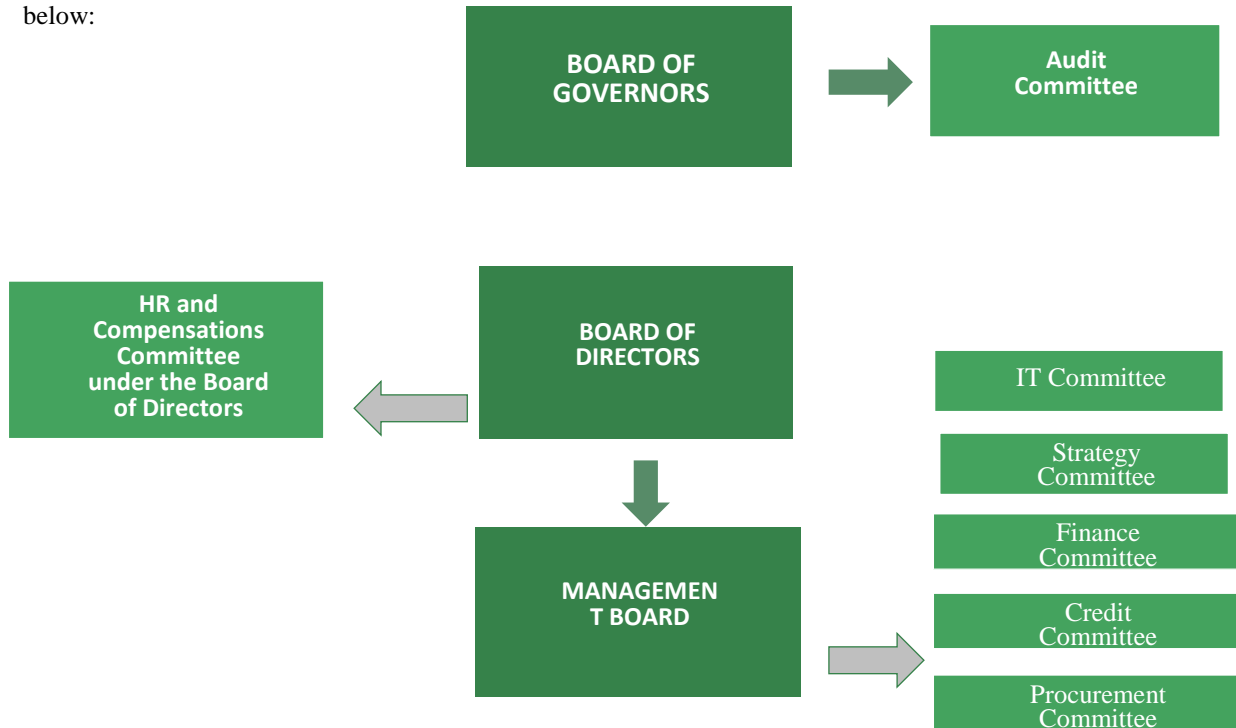
The new governance structure of the Issuer is based on the principles of transparency, accountability, responsibility and openness.

The Audit Committee is a collective governing body of the Issuer composed of Member States' representatives and responsible for auditing the Issuer's activities. The Audit Committee reports to the Board of Governors and the Board of Directors.

The HR and Compensations Committee under the Board of Directors is an advisory collective body under the Board of Directors, which main function is to control observance of staff-related policies, rules and procedures by the Issuer.

In line with best corporate governance practices of other international development banks, the Issuer has established various specialised collective bodies under the Management Board, including the Finance Committee, the Credit Committee, the Strategy Committee (under which a Coordination Sub-Committee on transition to newgovernance structure was created), the Procurement Committee, the IT Committee and various tasks groups.

According to the new edition of the Statutory Documents, the governance structure of the Issuer is presented below:



The Board of Governors

The Board of Governors is the supreme collective governing body of the Issuer. The Board of Governors meets when necessary, but not less than once a year. The main powers of the Board of Governors include making resolutions on the admission of new members and the amendments to the Statutory Documents, opening of branches and representative offices by the Issuer in Member States, as well as in other countries. The Board of Governors is also responsible for the determination of the general directions of the Issuer's operations, the Issuer's development strategy, change of the size of the Issuer's authorized capital and paid-in capital, approval of the Issuer's Annual report, balance sheet and allocation of profits, the appointment of the Chairperson and the members of the Management Board and the Audit Committee.

Each Member of the Issuer appoints one representative and his/her deputy to the Board of Governors. A Governor may nominate a temporary deputy Governor.

As of 19 February 2019, all nine IIB Member States (Cuba, Hungary, Bulgaria, Mongolia, Czech Republic, Romania, Russian Federation, Slovakia and Vietnam) have already completed internal procedures related to the appointment of their Governors to the Board of Governors.

The Hungarian Government appointed, the Deputy Prime-Minister, Minister of Finance of Hungary M. Varga to the position of Governor and State Secretary for Financial Policy Affairs of the Ministry of Finance G. Gion as Deputy Governor. The Bulgarian Government appointed the Deputy Minister of Finance M. Petrova to the position of Governor. The Government of Mongolia appointed the Minister of Finance of Mongolia Ch. Khurelbaatar to the position of the Governor, and the President of the Bank of Mongolia N. Bayartsaikhan as Deputy Governor. The Government of the Czech Republic appointed the Minister of Finance of the Czech Republic A. Schillerova to the position of Governor and Deputy Minister of Finance L. Dupakova as Deputy Governor. The Government of Romania appointed the Minister of Public Finance of Romania E. Teodorovici to the position of Governor. The Government of Russia appointed the Deputy Minister of Finance of the Russian Federation S. A. Storchak to the position of Governor and Director of the Department of Economic Cooperation of the Ministry of Foreign Affairs of the Russian Federation E. A. Stanislavov as Deputy Governor. The Government of Slovakia appointed Deputy Prime Minister and Minister of Finance of the Slovak Republic P. Kazimir to the position of Governor and State Secretary of the Ministry of Finance of the Slovak Republic D. Meager as Deputy Governor. The Republic of Cuba appointed the Minister-President of Central Bank of Cuba Irma Margarita Martínez Castrillón to the position of the Governor. Vietnam appointed the Governor of the State Bank of Vietnam Le Minh Hung to the position of the Governor.

The Board of Directors

The Board of Directors is the Issuer's collective governing body responsible for the general management and oversight of the Issuer's operations. The Board of Directors meets as often as required to manage the Issuer's affairs, but not less than once every quarter.

The Board of Directors makes decisions on credit and investment operations in the scope of its authorities, approves the key regulations, defining various aspects of the Issuer's operations, including its credit, financial, accounting, asset and liability management, risk management policies (including establishing risk appetite), the Issuer's HR Policy, supports the activities of the Board of Governors.

The Board of Directors consists of representatives of the Issuer's Members. Each Member appoints one Director and his/her deputy to the Board of Directors. A Director may nominate a temporary deputy Director. Directors are appointed for a term of three years and may be reappointed upon the expiration of said term.

As of 19 February 2019, seven out of nine IIB Member States (Bulgaria, Mongolia, Cuba, Czech Republic, Romania, Russian Federation and Slovakia) have appointed their Directors to the Board of Directors and submitted relevant official notifications to the Bank.

The Bulgarian Government appointed Director of International Financial Institutions and Cooperation Directorate of Ministry of Finance of Bulgaria G. Beremska to the position of Director, and Head of Department, International Financial Institutions and Cooperation Directorate, Ministry of Finance of Bulgaria Y. Zaharieva as Deputy Director. The Government of Mongolia appointed Director-General of the Financial Policy Department of Ministry of Finance of Mongolia Ts. Zorigbat to the position of Director. The Government of Cuba appointed Vice President of the Central Bank of Cuba Katerine Alino Carballo to the position of Director, and Head of

Department of the Central Bank of Cuba Isaac Hernandez Perez as Deputy Director. The Government of the Czech Republic appointed the Director of International Relations Department of the Ministry of Finance of the Czech Republic Z.Matyasova to the position of Director. The Government of Romania appointed General Director of the Ministry of Public Finance of Romania B.Cucu to the position of Director, and Head of Division, Ministry of Public Finance of Romania O.B. Iacobescu as Deputy Director. The Government of Russia appointed Director of Head of the Department for International Financial Relations of the Ministry of Finance of the Russian Federation A.A. Bokarev to the position of Director. The Government of Slovakia appointed General State Counsellor of the Ministry of Finance of the Slovak Republic K.Kovacova to the position of Director, and Senior State Counsellor of the Ministry of Finance of the Slovak Republic M.Babejova as Deputy Director.

Governments of Hungary and Vietnam will officially nominate their representatives to the IIB Board of Directors in the nearest future.

The Management Board

The Management Board is the executive body of the Issuer reporting to the Board of Directors and the Board of Governors. The Management Board's main task is to supervise the Issuer's operations in accordance with the new edition of the Statutory Documents, resolutions of the Board of Governors and Board of Directors. The Management Board also implements the Issuer's credit, financial, accounting, asset and liability management, and risk management policies, makes decisions on credit and investment operations in the scope of its authorities, organizes work aimed at raising and allocating available funds, adopts decisions to issue bonds, prepares necessary materials and proposals to be considered by the Board of Governors and the Board of Directors, builds and uses the Issuer's business connections and correspondent banking relationships with other banks and organizations.

The Management Board consists of the Chairperson of the Management Board and his/her deputies appointed by the Board of Governors for a five-year term, generally from among citizens of the Member States. Following the last Board of Governors' meeting in Varadero, the members of the Management Board are appointed on a competitive basis through an independent assessment of their qualifications and conformity with the Bank's requirements.

At the 1/110th meeting of the Board of Governors, the Key Principles of Management Board Composition (Key Principles) were adopted, ensuring the transition to modern international corporate governance standards.

Before the Key Principles came into force, the practice of appointing Board members was based on a quota system and rotation principle. The Board members were appointed by the Council of the Bank from among citizens of member states presenting their candidates.

Adopted Key Principles provide a merit-based approach. The Management Board is formed on a competitive basis in line with the generally accepted standards of corporate governance, as the efficiency of the IIB's operations hinges on the work of this body. The HR and Compensations Committee under the Board of Directors has the key role in selection of candidates for vacant positions of the members of the Management Board. It performs an independent assessment of the candidates' level of qualification and formulates recommendations for the Board of Governors concerning the candidates.

To ensure a balanced and transparent system of decision-making at the level of the Management Board Principles establish the fair country representation according to which the Management Board shall include citizens of at least four Members of the Bank. At the same time all the members of the Management Board have the right to vote.

The table below contains a list of current members of the Issuer's Management Board:

Nikolay Kosov, Russia

Function: Chairperson of the Management Board as of September 2012

Education, practice, other relevant information: Mr. Kosov graduated from the Moscow State Institute of International Relations majoring in Foreign Affairs. In 2000, he graduated from the Finance Academy affiliated to the Government of the Russian Federation majoring in World Economy. He holds a PhD in Economics.

1977-1992 – Assistant, Senior Assistant, Attaché, the Third, Second and then the First Secretary, Counsellor of the USSR Embassy, counsellor at the Ministry of

Foreign Affairs of the USSR.

1992-1993 – Assistant to the Vice President of the Russian Federation in the Administration of the President of the Russian Federation.

1993-1998 – First Deputy, then CEO of Automobile Russian Alliance plc., member of the Board of Directors of AutoVaz OJSC.

1998-2007 – First Deputy of the Chairman, state bank for development and external economic activity (Vnesheconombank).

2007–2012 – Member of the Board of Vnesheconombank); First Deputy of the Chairman of Vnesheconombank.

Since September 2012 – Chairman of the Board, International Investment Bank.

For his contribution to the development of the financial banking system of the Russian Federation and for his longstanding conscientious work, Mr. Kosov was awarded with the 4th class of the Order “For Merit to the Fatherland”, Order of Merit, medals of Order of “For Merit to the Fatherland” (1st and 2nd class) and the Order of Friendship. He has also been honoured with the Acknowledgment of the President of the Russian Federation numerous times and with the Acknowledgment of the Minister of economic development of the Russian Federation and awarded the badge of honour of the Leader of the Russian Economy. Mr. Kosov also has the following awards of Member States: «Samara Cross», a memorable medal of Bulgaria, Mongolian order of the Polar Star - the highest state honour of Mongolia bestowed on foreign citizens, and Order of Friendship, a high state honour of Republic of Cuba.

Jozef Kollár, Slovak Republic

Function: First Deputy Chairperson of the Management Board as of December 2018; coordinates the Treasury and Investment Attraction Section.

Education, practice, other relevant information: Mr. Kollár studied in University of Economics (Bratislava, Slovakia) in 1979 – 1983 where he gained master of economics and graduated with honors. From 1983 – 1990 studied in the Slovak Academy of Sciences from where he graduated with a Ph.D. degree in economics. In summer 1993 studied in University of Wisconsin, U.S.A. (Graduate School of Banking), in summer 1994 and 1995 in Oklahoma City University, U.S.A. (Jack T. Conn Graduate School of Community Banking) and in summer 1996 in AOTS Association for Overseas Technical Scholarship, Yokohama, Japan.

1983–1990 – Macroeconomics and Strategy Planning Analyst at the Slovak Academy of Sciences (Bratislava, Slovakia).

1990–1991 – Head of Department of Economics and Foreign Exchange Analysis at the State Bank of Czechoslovakia (Bratislava, Slovakia).

1991–2006 – Member of the Board (1993–1997), Deputy Chairman of the Board (1997–2000), Chairman of the Board and CEO (2000–2006) at Volksbank AG, (Bratislava, Slovakia).

2008–June 2010 – Owner of JK Advisory s.r.o (financial consulting in real estate development and transport infrastructure in Slovakia).

July 2010–February 2016 – Member of the Parliament at the National Council of the Slovak Republic.

Since March 2016 — Deputy Chairman of the Board, since December 2018 – First Deputy Chairperson of the Management Board, International Investment Bank.

Alexandru Florescu, Romania

Function: Deputy Chairperson of the Management Board, as of January 2016; coordinates the Finance section.

Education, practice, other relevant information: Mr. Florescu graduated with merits the International Economic Relations and Finance, Insurance, Banking and Capital Markets faculties within the Academy of Economic Studies (Romania) in September 2003.

2004 – Post-University degree in Economics of European Integration from the Academy of Economic Studies.

2006–2010 and 2012–2013 – Senior Expert at the Ministry of Public Finance, DG Treasury and Public Debt (Romania), covering mainly Romania’s participation in several IFIs and financial markets issues. Member of EFC sub-committee for IMF and related issues and EFC/EPC Joint Working Group on financial aspects related to international financing in the climate change area.

2010–2011 – Adviser to the State Secretary responsible with the coordination of Treasury and Public Debt, PPP and Management of European Funds.

September 2013–December 2015 – Head of Strategic Development and Analysis Department, International Investment Bank.

Since January 2016 – Deputy Chairman of the Board at the International Investment Bank, representative of Romania.

Rumyana Laleva Kyuchukova, Republic of Bulgaria

Function: Deputy Chairperson of the Management Board, as of February 2016; coordinates the Risk section.

Education, practice, other relevant information: Mrs. Kyuchukova finished University for National and World Economy – International Economic Relations. Studied in City University of Seattle (2000-2002), where she gained an MBA degree in Executive Management.

1998–2000 – Adviser to CEO and Head of internal audit, Mobitel AD (Bulgaria).

2001-2002 CEO of MTEL Trading, Mobitel AD,

2000-2002 CEO of Mobitel AED 2003–2004 – General manager and owner of Telecom Consulting Ltd. (Bulgaria)

2005–2011 – Senior Adviser to the ED and member of the Board of the World Bank

2012–2015 – Consultant in finance and investments.

Since February 2016 — Deputy Chairman of the Board, International Investment Bank.

Georgy Potapov, Russia

Function: Deputy Chairperson of the Management Board, since July 2018; coordinates the

Strategy section.

Education, other information: **practice, relevant information:**

1997 - Moscow State Institute of International Relations (University), Specialist in international relations with knowledge of foreign languages

2008 - Financial University under the Government of the Russian Federation, Banking and Finance, Diploma in Economics

1997-2005 - Desk officer, Attaché, Third Secretary, Second Secretary, Ministry of Foreign Affairs of Russia (including Russian Embassy in the Kingdom of Thailand).

2005-2006 - Assistant to Director General, Techsnabexport, OJSC (ROSATOM, OJSC).

2007-2008 - Head of Protocol, Bazovyi Element Company, LLC.

2006-2009 - Adviser to Director General, Universal Service System 'Executive Service', CJSC.

2009-2013 - Head of Administration, Head of Document Control Department, 'AB 'Russia', OJSC.

2012 – 2018 - Adviser to the Chairman of the Board, Director of International Financial Integration and Multilateral Cooperation Department, Head of Strategy Section, Policy Director, International Investment Bank.

Since July 2018 - Deputy Chairman of the Board, International Investment Bank.

Audit Committee

The Audit Committee is appointed by the Board of Governors and consists of the Chairperson of the Audit Committee and its members. The Audit Committee is responsible for auditing the Issuer's operations, which include review of the implementation of resolutions adopted by the Board of Governors and the Board of Directors, annual reports, cash and property, records, reports and documents of the Issuer and its branches, representative offices, and subsidiaries.

HR and Compensations Committee under the Board of Directors

The HR and Compensations Committee is established under the Board of Directors by resolution of the Board of Governors. This is an advisory collective body, the main function of which is to control the observance of staff-related policies, rules and procedures at the Issuer, and to produce recommendations on improving its HR practices.

REGULATORY CAPITAL

The approval of capital adequacy ratios applicable to the Issuer is one of the prerogatives of the Board of Directors. As of September 2013, the Council established a 25% minimum capital adequacy ratio, representing the percentage of the Issuer's capital to its risks-weighted assets. Starting with 2013, the Issuer's capital adequacy ratio is computed in accordance with the methodology set forth under the Revised Framework for International Convergence of Capital Measurement and Capital Standards ("**Basel II**").

The 25% minimum capital adequacy ratio approved by the Council is 21 percentage points above the Basel II 4% requirement applicable to tier I capital and 17 percentage points above the Basel II 8% requirement applicable when accounting tier II capital also.

In addition to the paid-in capital (*i.e.*, monetary contributions of the Member States), the regulatory capital of the Issuer also includes retained profits, reserves and other adjustments and components.

The following table shows the composition of the Issuer's capital position as of 31 December 2016, 31 December 2017, 31 December 2018 and, respectively, 30 June 2017 and 30 June 2018:

<i>(EUR million)</i>	31 December 2016	31 December 2017	30 June 2017	30 June 2018	31 December 2018
	(audited)	(audited)	(unaudited)	(unaudited)	(audited)
Tier 1 capital	378.0	380.75	378.8	351.2	368.75
Tier 2 capital	11.4	13.99	11.7	9.26	6.38
Total regulatory capital	389.15	394.73	390.5	360.46	375.13
Total risk-weighted assets	727.28	1,042.87	925.6	1,086.06	1,093.23
Total capital expressed as a percentage of risk-weighted assets, %	53.55%	37.85%	42.2%	33.19%	34.39%
Total tier 1 capital expressed as a percentage of risk-weighted assets, %	51.98%	36.51%	40.9%	32.34%	33.73%

Source: The Financial Statements.

The Issuer's believes that its capital adequacy target of 25% allows it to position above most requirements under the third Basel accord (Basel III) and, therefore does not intend to implement the proposals thereunder.

RISK MANAGEMENT

The Issuer's risk management strategy, approved by the Council in September 2013, sets forth the main principles governing the Issuer's risk management policy, as well as the risk management system, the key specificities of the Issuer's risk profile, the general system of risk limits and the rules governing the definition of the Issuer's risk appetite. A new risk management policy has been approved at the first meeting of the Board of Directors, as consequence of the entry into force of the Protocol.

In further developing its risk management system, the Issuer benefits from its membership in the Global Emerging Markets (GEMs) Risk Database Consortium, a cooperation forum aimed at sharing expertise, analysing information and creating a comprehensive database on credit risks for multilateral development banks and international financial institutions.

Main principles

The Issuer's risk management policy is based on the following governing principles:

- the Issuer's profitability is the result of the risk/return trade-off reflected in the Issuer's risk appetite;
- application of the risk management controls at all levels of internal governance and in all processes;
- continuous improvement of the risk management eco-system (skills, tools, systems, processes) following the best market practices; and
- adoption of BASEL II standardized approach with elements of Basel III (liquidity coverage ratio, net stable funding ratio, leverage ratio) since 2014.

Description of the risk management system

The Issuer's risk management system is based on consistent identification of risks, careful assessment and permanent monitoring of all risk-factors. Vertical system of risk management is one of the key points of the risk management policy, with the risk being identified, assessed and controlled at all governance levels starting from the Board of Governors, the Board of Directors, the Management Board and going down to the level of the Issuer's personnel.

The risk management system is structured on three lines of defence, as follows:

- *Risk taking*: The risks are identified, assessed and controlled across all Issuer's products, activities, processes and systems;
- *Risk management*: The independent Risk Management Department is responsible for the overall risk identification, measurement, control and monitoring of risks. Another key point of its mission is to calculate capital adequacy and regular allocation of capital for different types of risk;
- *Risk assurance*: The Internal Control Department and the Audit Committee provide independent assessment and review of the risk management system.

Risk organization and governance

The chart below summarizes the main risk management duties of the Board of Governors, the Board of Directors, the Management Board, the Financial Committee, the Credit Committee, the Risk Management Department, the Internal Audit Department, the Audit Committee and the other departments of the Issuer:

<i>Body</i>	<i>Main responsibilities</i>
<i>Board of Governors</i>	Determining the general directions of the Issuer's operations and approve the Issuer's development strategy
<i>Board of Directors</i>	<ul style="list-style-type: none"> • Approval of risk management policies • Determining the Issuer's risk appetite for each year • Overall organization of the Issuer's risk management system (including related responsibilities and tasks)
<i>Chairperson of the Management Board</i>	<ul style="list-style-type: none"> • approving the Issuer's rules and regulations regarding the process for conducting credit and banking operations in accordance with the principles determined by the Board of Governors and the Board of Directors
<i>Management Board</i>	<ul style="list-style-type: none"> • implementing the Issuer's credit, financial, accounting, asset and liability management, and risk management policies, which have been approved by the Board of Directors

Finance Committee	<ul style="list-style-type: none"> • preparing necessary materials and proposals to be considered by the Board of Governors and the Board of Directors (including risk management related materials and proposals)
	<ul style="list-style-type: none"> • Providing methodological guidance • Review of limits for specific risk categories (i.e., country, market, liquidity) • Management of assets and liabilities • Liquidity management
	<ul style="list-style-type: none"> • Management of loan portfolio • Review of credit risks limits • Approval of new credit operations
	<ul style="list-style-type: none"> • Identification, assessment, measurement, reporting and monitoring of credit, market, operational and • Liquidity risks • Management of risks limits • Development of risks policies • Assessment of counterparties • Provisioning creation
Risk Management Department	<ul style="list-style-type: none"> • Review of the efficiency of the risk management framework • Review of the risk management process, tools and organization
	<ul style="list-style-type: none"> • Monitoring and controlling risk limits • Active management of operational risks
Internal Audit Department and Audit Committee	
Other Departments	

Risk management process

At the level of the Issuer, the risk management process generally entails the following stages:

- *Risk identification*: Identification of risks at all governance levels
- *Risk assessment*: Risks are evaluated in terms of causes, circumstances of their occurrence, their negative effects and the probability of their outcome. Potential losses and the respective risk's impact in the Issuer's monthly capital adequacy ratio are calculated and accounted for when deciding on whether to accept a particular risk;
- *Limitation of risk exposure*: Based on the results of the risk assessment stage, the Issuer's Risk Management Department proposes the establishment of general limits, limits restricting credit, market and liquidity risks, which are subsequently approved by the Management Board;
- *Risk monitoring and control*: Risk indicators are monitored on a regular basis in order to ensure that the approved limits are not exceeded, as well as to identify the most effective methods of reaction to the materialized and potential risks;
- *Risk reporting*: The Risk Management Department regularly reports to the Financial Committee, the Credit Committee, and the Management Board with respect to risk levels and their potential negative impact on the Issuer's operations.

Risk profile

The risk profile of the Issuer is defined by several key considerations particularly related to the Issuer's mission, its strategic goals and the specificities of the Issuer's business, mainly including the following:

- The Issuer main goal is to develop into a modern multilateral development bank, its mission being particularly focused on the promotion of social and economic development, growth of well-being of the population, and economic cooperation, of the Member States;
- The Issuer's core activities are financed through its equity capital base and the funds raised from the Member States' or international capital markets;
- The Issuer focuses on acting as a lender in interbank and syndicated interbank loans aiming to support SMEs, as well as project investment loans; and
- The Issuer's operations with new partners and clients are preceded by due diligence investigations carried out by the Issuer in order to assess its partners' / clients' legal status.

Risk appetite

In accordance with the new edition of the Statutory Documents, the Board of Directors determines the Issuer's risk appetite. Risk Appetite determines how much risk (measured by the allocated capital) the Issuer is willing to accept taking into account the risk characteristics of the Issuer's assets and liabilities, as well as its ongoing and prospective operations. During the process, the Board of Directors assesses the Issuer's willingness to assume a certain risk-carrying operation against the amount of own funds or liquidity the Issuer is willing to expose to risk in the implementation of the respective operation and the current and anticipated situation of the following parameters:

- the Member States' expectations on profitability;
- international regulatory standards;
- volume of transactions;
- structure of significant risks;
- level of aggregate capital.

Risk appetite is a key indicator, shaping the risks limits applicable at the level of the Issuer, and defining the thresholds for key risk management indicators relevant to the Issuer.

Risks monitoring, control and reporting

In accordance with its internal procedures, the Issuer has established a system of limits based on which it assesses the creditworthiness of third parties *e.g.*, partners and clients, and evaluates potential financial transactions. This system is subject to annual review by the Issuer.

As part of the lending activity analysis, risks associated with the Issuer's asset-based lending operations are continuously monitored and the fair value of the pledged items is regularly determined. During the monitoring period, specialists appointed by the Issuer perform on-site visits to certain borrowers, in order to verify the implementation of the financed projects and assess risks of loans impairment.

The Issuer also performs daily monitoring of compliance of operations with limits applicable to cash and equity transactions, as well as with structural limits included in key risk ratios and stop-loss limits. Regular reports on the status of risks are submitted to the Issuer's management on a regular basis.

The diagram below describes the roles of the Board of Directors and, respectively, the Management Board in the establishment of key risk limits:

Board of Directors	Strategic yearly limits		Risk appetite indicators for one year			
	<ul style="list-style-type: none"> • Capital adequacy ratio (at least 25%) • Limit of exposure to one counterparty or group of related counterparties (up to 25% of the Issuer's equity) • Liquidity coverage ratio (at least 100%) • Net stable funding ratio (at least 100%) • 		<ul style="list-style-type: none"> • Risk appetite levels (capital allocation to credit, market and operational risks) • Risk appetite indicators (e.g., liquidity, portfolio, quality, rating, leverage) 			
Management Board	Individual treasury limits		Individual loan limits		Systemic limits	
	Permitted operations: <ul style="list-style-type: none"> • NOSTRO • Interbank lending • Forex • Equity/Bonds • Other 		<ul style="list-style-type: none"> • Corporate clients • Financial institutions 		<ul style="list-style-type: none"> • Credit risk limits • Market risk limits • Operational risk limits • Country limits • Sector limits • Other limits 	

The following table shows key risk parameters of the Issuer and applicable limits, as of 31 December 2016, 31 December 2017 31 December 2018 and , respectively, as of 30 June 2017 and 30 June 2018:

Indicator	31 December 2016	31 December 2017	30 June 2017	30 June 2018	31 December 2018	Limit
Capital adequacy ratio (<i>Basel II methodology</i>)	53.55%	37.85%	42.19%	33.19%	34.39%	not less than 25%
Liquidity coverage ratio (LCR) (<i>Basel II methodology</i>)	476.0%	381.5%	261.0%	145.2%	172.5%	not less than 100%
Net Stable Funding Ratio (NSFR) (<i>Basel II methodology</i>)	112.1%	112.7%	104.4%	113.3%	116.7% ¹	not less than 100%
Financial leverage ²	126.1%	177.4%	156.2%	212.5%	221.49%	up to 250%

Source: The Group.

² Starting from 2019 has been replaced by Basel 3 Leverage set at 25%

BORROWINGS

The Issuer's borrowings in the form of long-term loans from banks, long-term REPO and debt securities amounted to EUR 681.1 million as of 31 December 2018 compared to EUR 666.8 million as of 31 December 2017 and EUR 411.9 million as of 31 December 2016.

As part of its strategy to diversify its sources of funding and in order to build its track record as a borrower and issuer on the financial markets of the Member States, as well as the international financial markets, the Issuer intends to continue the attraction of funds through the issuance of bonds denominated both in hard currencies and local currencies, to set up a Medium-Term Notes (MTN) Program in order to increase its flexibility and efficiency in executing its funding program, as well as by entering into credit facilities (both bilateral and syndicated) with other financial institutions.

Bond placements

Russian Federation

In spring 2014, the Issuer has registered its first RUB 14 billion (EUR 219.4 million) bond programme with the Central Bank of Russia, after having been recognised as an international financial organisation whose securities are admitted for public placement and circulation in the Russian Federation by the Russian Federation Government Decree No. 732-r of 2 May 2013. The programme documentation provides semi-annual coupon payments and the possibility for the Issuer to benefit from put options with respect to the drawings. As a part of the bond programme with the Central bank of Russia, the Issuer issued four bond series:

- series 01: In April 2014, the Issuer placed an inaugural series 01 RUB denominated bonds in the amount of RUB 2 billion (EUR 31.3 million). The current rate of this bond was set at 0.01% p.a. The bond was fully repurchased under investor put option in October 2017.
- series 02: In April 2015, the Issuer placed series 02 RUB denominated bonds in the amount of RUB 3 billion (EUR 47.0 million). The current rate was set at 9.50% p.a. The amortized value of bond as of 31 December 2018 was EUR 37.8 million.
- series 03: In December 2014, the Issuer placed series 03 RUB denominated bonds in the amount of RUB 4 billion (EUR 62.7 million). The bond was fully repurchased in June 2017 under investor put option after setting 0.01% p.a. interest rate with the purpose of liquidity management. In November 2018 the Issuer fully repurchased the bond under investor put option.
- series 04: In November 2015, the Issuer placed series 04 RUB denominated bonds in the amount of RUB 5 billion (EUR 78.4 million). In November 2017 the Issuer reviewed the interest rate and the current rate was set at 8.15% p.a. The amortized value of bond as of 31 December 2018 was EUR 62.5 million.

As of March 2016 MOEX, registered a RUB 100 billion (or equivalent in another currency) programme of exchange-traded bonds by the Issuer. The maximum maturity period of the Issuer's bonds within the open-ended programme will be 30 years. Placement will be carried out by public subscription. The Issuer will determine the currency of each issue. Earlier, according to the Russian legislation, only resident issuers of the Russian Federation had the right to issue such bond programmes. However, due to extensive negotiations during 2015 between the Issuer and the representatives of the Bank of Russia, the Moscow Exchange and the National Settlement Depository, a common approach was agreed on in relation to IFIs' access to such bond programmes, the programme registered by the Issuer being the first of its kind in the Russian Federation.

In June 2017, the Issuer successfully placed a new bond issue in the amount of RUB 10 billion (approx. EUR 156 million), issued under the earlier registered programme of exchange-traded bonds on Moscow Exchange. The coupon rate was fixed at 8.75% p.a. The interest will be paid twice a year, with a put option exercisable in two years and nine months. The amortized value of bonds as of 31 December 2018 was EUR 125.0 million.

All RUB-denominated bonds were included in the Lombard List of the Central Bank of Russia.

The final maturity date of the RUB-denominated Bonds is subject to the Issuer's put option, exercisable in accordance with the applicable terms and conditions of the programme documentation and of each individual

issue. At the dates of the placements of the RUB-denominated bonds, the Issuer entered into cross-currency interest rate swaps for the purpose of hedging currency risks.

Romania

The Issuer placed RON 111 million (approx. EUR 25 million) of 3-year bonds on the Bucharest Stock Exchange in October 2015, with annual interest payments. The interest rate of the issue, managed by BT Capital Partners S.A. (formerly, BT Securities S.A.), was set at 4.1%. The fully domestic issue attracted demand from Romanian pension and investment funds, as well as investment and insurance companies. The issue was fully repaid in October 2018.

The Issuer returned on the Romanian capital market in September 2016, with a 300 million RON bond issue, successfully placed and admitted to trading on the Bucharest Stock Exchange. The fixed interest rate of the bonds was set at 3.4%, payable in annual arrears.

In September 2017, the Issuer successfully placed additional issue of 300 million RON with a floating coupon rate ROBOR 3M+1.5% and coupon payments made quarterly. At the same time, due to high demand from investors, the Issuer successfully placed 60 million EUR bond with a fixed rate 1.593% paid annually. Both tranches are admitted to trading on the Bucharest Stock Exchange and have 3-year maturity.

In October 2018, the issuer successfully placed another 3-year issue in two tranches of 300 million RON with a floating coupon rate ROBOR 3M+ 1.40% and quarterly coupon payments and 80 million EUR bond with a fixed coupon rate of 1.5026% paid annually.

Slovakia

On 21 October 2014, the Issuer successfully placed EUR 30 million bonds maturing on 21 October 2019 on the Slovak regulated securities market. The coupon rate was set at 3.5% p.a. and is payable once a year. The Slovak bonds' amortized value amounted to EUR 30.0 million as of 31 December 2018.

Czech Republic

As a part of a diversification of its long-term funding in April 2018 the Issuer executed its debut CZK denominated private placement transaction amounting to CZK 750 million. Listing took place on both Prague and Vienna Stock Exchanges. The 3-year bond issue has a floating rate of PRIBOR 3M + 0,55%. The amortized value of the bond amounted to EUR 29.1 million as of 31 December 2018.

Other instruments

In May 2015, the Issuer concluded a sell-buy back transaction for the amount of EUR 7.5 million with the EXIM Bank SR with a maturity of three years. The transaction was fully repaid.

In September 2015, the Issuer signed two total return swap transactions with Credit Suisse London - one denominated in USD, for the amount of 35 million and a maturity of 2.5 years, and the other denominated in EUR for the amount of 25 million and a maturity of three years. Both transactions were fully repaid in due course.

In May 2016, the Issuer concluded its first syndicated term loan facility, in the amount of EUR 60 million. The facility is unsecured, carries a margin of 175 basis points over EURIBOR and has a 2-year tenor with bullet repayment. The facility was repaid in May 2018.

In April 2017 the Issuer completed its inaugural *Schuldscheindarlehen* (SSD) – a type of traditional privately-placed German debt similar to a bond. The offer was made in multiple tranches with tenor ranging from 3 to 10 years and attracted amongst others German retail banks as well as international institutional investors. The overall volume of the transaction amounted to EUR 13 million. . Later that year, in December, IIB attracted another EUR 10 million of SSD with maturity of 7 years. Thus, total volume of the raised under both SSD transactions funds comprised EUR 23 million.

In August 2017 the Issuer signed off on its debut credit facility in Hungary. The aim of this facility is to support the expansion of the Issuer's portfolio of lending in Hungarian Forint (HUF). The Bank of Hungarian Savings Cooperatives Ltd. (TakarékBank) executed a credit facility up to 4 billion HUF (approx. EUR 13 million) with a tenor of 3 years.

On 15 August 2017, NDB, Eurasian Development Bank and the Issuer signed loan agreements for total amount of up to USD 100 million. Maturity of the facility is 12 years. In March 2018 was attracted the first tranche in the volume of USD 12.5 million under the term loan facility executed with New Development Bank. Second tranche also in the amount of USD 12.5 million was disbursed in July 2018.

The Issuer is not in breach of any of its obligations or undertakings under its issued bonds or the loan agreements to which it is a party.

COMPLIANCE

The Issuer endeavours to comply with commonly accepted compliance rules and standards. As of 2018, the Issuer developed and currently has in place a clearly defined policy which includes rules regarding compliance control standards, compliance organization, responsibilities, functions and independence of compliance control, reporting, access to information, training and interaction with departments with relevant areas of responsibility (the “**Compliance Policy**”).

The Issuer’s structure includes an independent Compliance Department which reports directly to the Chairperson of the Management Board and is responsible for identifying, managing and monitoring compliance risks under the Compliance Policy. The main duties of the Compliance Department include:

- development of recommendations for the Issuer’s management regarding compliance, and of standards and practices based on the models used by other international financial institutions with respect to the organization and implementation of compliance control;
- development and maintenance of the reporting system regarding compliance risks and disclosure of information to governing bodies of the Issuer with respect to compliance risks;
- presentation of conclusions and recommendations to the Issuer’s management with respect to the mitigation or elimination of identified compliance risks;
- preparation of recommendations and comments on developed and existing policies, regulations, rules and procedures, and monitoring observance thereof in order to mitigate compliance risks;
- developing and implementing activities to counter prohibited practices (including corruption, coercion, collusion, financing of terrorism, fraud and money laundering); organizing activities aimed at monitoring the use of insider and confidential information, and the identification, evaluation and control of conflicts of interest;
- management of complaints and reports regarding prohibited practices, misconduct (meaning failure by a staff member to observe the rules of conduct and the standards of behavior prescribed by the by-laws and policies of the Issuer) especially about fraudulent and corrupt actions on the part of Issuer’s staff and other relevant third parties;
- investigating facts or suspicions regarding prohibited practices and misconduct;
- developing and implementing procurement rules, and measures to detect, assess and control the ecological risks of the Issuer’s projects, and the Issuer’s own activities; and
- reviewing the Issuer’s projects in order to detect breaches in performance and maintain compliance rules.

The Issuer does not tolerate any actions related to prohibited practices neither as regards its own operations nor on the part of its employees or partners. Therefore, the Issuer supports international efforts to tackle the aforementioned practices while actively applying international standards for anti-money laundering and combating terrorism financing, corruption and fraud (“**AML/CFT/F/C**”) to its activities. In 2015, the Issuer has joined the Uniform Framework for Preventing and Combatting Fraud and Corruption, elaborated by the leading international financial institutions, thus strengthening its internal compliance procedures. The policies of the Compliance Department (anti-money laundering, and combating the financing of terrorism, fraud and corruption, policies and the Issuer’s Compliance Policy and Procedure for receiving and handling complaints have been amended in 2016 in order to comply with the Uniform Framework for Preventing and Combatting Fraud and Corruption.

The identification of its counterparties and the performance of related due diligence investigations, followed by continuous monitoring operations, are at the core of the Issuer's AML/CFT/F/C control system, enabling the effective identification, mitigation and control of compliance risks. Main approaches, standards and requirements for the procedures of the Issuer's AML/CFT/F/C control system aimed at preventing the participation in illicit operations are outlined by the Issuer's internal policy on anti-money laundering and combating the financing of terrorism, fraud and corruption.

The Issuer understands that its mission to promote economic growth and increase competitiveness of Member States' economies is more efficiently carried out if its corporate culture is aligned with generally accepted norms of corporate ethics and business conduct. Therefore, a Code of Conduct applicable to all employees has been prepared and implemented at the level of the Issuer. The Code of Conduct identifies key corporate values and rules of conduct in atypical situations. The Compliance Department collects information, educates and works with employees to prevent potential conflicts of interest. In 2018 the Code was reconsidered and amended following the request of the changing environment and appearance in the bank practice new cases not previously clearly described in the document. Attaching great importance to and promoting the formation of an efficient, transparent and competitive financial market, the Issuer has implemented certain internal control measures aimed at preventing, identifying, and stopping abuse in the form of unlawful use and dissemination of insider information, manipulation of prices for the Issuer's financial instruments, as well as financial instruments of third parties. To this end, in 2016 the Issuer updated its internal Regulations on the Procedure of Dealing with Insider Information and Insiders of the International Investment Bank, on the basis of the general requirements of Regulation No. 596/2014/EU of the European Parliament and of the Council on market abuse and the national legislation amendments of the Member States.

In 2016, the Issuer's Board approved certain amendments to the procedure for receiving and handling complaints in the International Investment Bank mainly aligned with the Uniform Framework for Preventing and Combatting Fraud and Corruption. The aim of the procedure is to gradually implement an independent accountability mechanism at the level of the Issuer. Under this procedure, each employee or third party may file complaint via the relevant communication channels with the Compliance Department on breaches in the activities by the Issuer, its staff members, or its counterparties related to prohibited practices. Consistent implementation of the independent accountability mechanism corresponds to the Member States' common intention to increase the Issuer's overall efficiency and social responsibility as an international entity.

In 2017, further steps to increasing compliance levels were taken. One such step is the implementation of an automated compliance system which is meant for the systematization, processing and control of the KYC requests regarding all the Issuer's counterparties. Another initiative put into practice since 2017 was to run compliance checks on the auditors of the financial reports appointed by the potential borrowers of the Issuer. Moreover, the Compliance Department gained access to information from credit bureaus and corporate registers and databases from the Member States. These measures, enhancing the capacity of the Issuer to perform efficient KYC procedures, along with an updated version of the Regulation on Measures for Combating Money Laundering, Financing Terrorism, Fraud and Corruption in the care of the Compliance Department came as responses to the increased complexity of the regulatory environment in the Member States and by the multitude of corruption investigations carried out thereto. Another landmark for 2017 is the signing of the Memorandum of Understanding in the field of compliance control by the Issuer and the Eurasian Development Bank in December, the implementation of which being scheduled for 2018.

In 2018, the Issuer updated the internal methodology and requirements for anti-money laundering, counter financing terrorism, combatting fraud and corruption. The document was aligned with the changes in the international guidelines issued by the relevant bodies (FATF, Basel Committees) and good practices of other IFI's.

LEGAL AND ARBITRATION PROCEEDINGS

There are no governmental, legal or arbitration proceedings, (including any such proceedings which are pending or threatened, of which the Issuer is aware), which may have, or have had, during the 12 (twelve) months prior to the date of this Offering Circular, a significant effect on the financial position or prospects of the Group.

MATERIAL CONTRACTS

There are no material contracts to which a member of the Group is a party, concluded outside of the ordinary course of the Group's business, which could result in any Group member being under an obligation or entitlement that is material to the Issuer's ability to meet its obligation to the bondholders in respect of the Bonds.

RELATED PARTIES TRANSACTIONS

The Group had no transactions with related parties, except in relation to maintaining current accounts for and payments of employee benefits and compensations to the key management personnel. The expenses in respect of such related parties transactions amounted to EUR 1.76 million as of 31 December 2018, of which most represented employee benefits to the key management personnel (in the amount of EUR 1.69 million).

TREND INFORMATION

There has been no material adverse change in the prospects of the Issuer since the date of its last published consolidated audited financial statements. Except as set out herein, the Issuer is not aware of any other trends, uncertainties, demands, commitments or events that should be reasonably likely to have a material effect on the Issuer's prospects within the current financial year.

STATUTORY AUDITORS

The consolidated financial statements of the Group for the years ended 31 December 2016, 31 December 2017 and, respectively, 31 December 2018 prepared in accordance with the IFRS have been audited, and the interim condensed consolidated financial statements of the Group for the six-month periods ended 30 June 2017 and, respectively, 30 June 2018 prepared in accordance with International Accounting Standard IAS 34 Interim Financial Reporting have been reviewed, by Ernst & Young Vneshaudit LLC, with its registered office at Sadovnicheskaya Nab., 77, bld.1, Moscow, 115035, Russia.

Ernst & Young Vneshaudit LLC is registered in the State Register of Legal Entities on 4 February 2016, State Registration Number 1167746123478. Ernst & Young Vneshaudit LLC is a member of Self-regulated organization of auditors "Russian Union of Auditors" (Association). Ernst & Young Vneshaudit LLC is included in the control copy of the register of auditors and audit organizations, main registration number 11603050953.

No qualifications have been included in the reports prepared by the Group's financial auditors with respect to the Group's consolidated financial statements for the years ended 31 December 2016, 31 December 2017 and, respectively, 31 December 2018 and the six-month periods ended 30 June 2017 and, respectively, 30 June 2018.

TERMS AND CONDITIONS OF THE BONDS

The following are the Terms and Conditions of the Bonds which will form part of each Document (as defined below).

1. DEFINITIONS AND INTERPRETATION

Capitalised term used in these Terms and Conditions shall have the following meaning:

Agency Agreement	has the meaning given in Condition 17.1;
Bondholders	has the meaning given in Condition 6;
Bonds	means the HUF denominated, fixed interest rate, registered, dematerialised bonds due 2022 (name: IIB 2022/I HUF Bond; short name: IIB 2022/I; ISIN Code: HU0000358825);
Business Day	means a day which is both a day on which commercial banks settle payments and are open for general business in Budapest and a day on which the Central Depository effects payments and securities transfers;
Central Depository	KELER Központi Értéktár Zrt.;
Document	has the meaning given in Condition 4.2;
Event of Default	has the meaning given in Condition 15.1;
Financial Indebtedness	means an indebtedness for or in respect of (i) moneys borrowed and debit balances at banks; (ii) any acceptance credit (including any dematerialised equivalent); (iii) any bond, note, debenture, loan stock or other similar instrument; (iv) any finance lease; (v) receivables sold or discounted (other than any receivables to the extent they are sold or discounted on a non-recourse basis); (vi) any other transaction (including any forward sale or purchase agreement) which has the commercial effect of a borrowing and (vii) any counter-indemnity obligation in respect of any guarantee, indemnity, bond, letter of credit or any other instrument issued by a bank or financial institution;
Guarantee	means in relation to any Financial Indebtedness of any person, any obligation to pay such Financial Indebtedness including (without limitation): (i) any obligation to purchase such Financial Indebtedness; (ii) any obligation to lend money, to purchase or subscribe shares or other securities or to purchase assets or services in order to provide funds for the payment of such Financial Indebtedness; (iii) any indemnity against the consequences of a default in the payment of such Financial Indebtedness; and (iv) any other agreement to be responsible for such Financial Indebtedness;
Interest Payment Date	has the meaning given in Condition 11.1;
Interest Rate	has the meaning given in Condition 11.1;
Issue Date	has the meaning given in Condition 4.3;
Material Subsidiary	means, as of any date, an entity (i) whose affairs and policies are controlled by the Issuer, whether by ownership of share capital,

contract, the power to appoint or remove members of the governing body or otherwise; or (ii) whose financial statements are, in accordance with applicable law and generally accepted accounting principles, consolidated with those of the Issuer and (iii) whose consolidated (or in the case of an entity that does not itself have any subsidiaries, unconsolidated) total assets represent 10% or more of the total book value of all assets of the Issuer's group as reflected in the Issuer's most recent consolidated annual audited financial statements;

Maturity Date	has the meaning given in Condition 4.6;
new Document	has the meaning given in Condition 4.2;
Nominal Value	has the meaning given in Condition 4.4;
Participant	means any entity holding a securities accounts with the Central Depository;
Paying Agent	has the meaning given in Condition 17.1;
Permitted Security Interest	means (i) any Security Interest in respect of a Financial Indebtedness the secured amount of principal of which does not at any time exceed 20% of the total book value of all assets of the Issuer's group as reflected in the Issuer's most recent consolidated annual audited financial statements; (ii) any Security Interest arising in the ordinary course of banking transactions (including, without limitation, such as sale and repurchase transactions and share, loan and bond lending transactions and any netting or set-off arrangements entered into by the Issuer or any Material Subsidiary for the purpose of netting any debit and credit balances), provided that the Security Interest is limited to the assets which are the subject of the relevant transaction; (iii) Security Interests imposed or required by statute or operation of law (but not through any act or omission to act on the part of the Issuer or any of its Material Subsidiaries); and (iv) any extension, renewal, refunding or replacement, as a whole or in part, of any Security Interest referred to in clauses (i) to (iii), inclusive, for amounts not exceeding the principal amount of indebtedness secured by such Security Interest so extended, renewed or replaced (plus improvements thereon or additions or accessions thereto);
Reference Date	has the meaning given in Condition 13.1;
Relevant Indebtedness	means (i) any indebtedness (whether being principal, premium, interest or other amounts) for or in respect of any bond, note, debenture, loan stock or other debt securities which with the consent of the Issuer are for the time being listed on any stock exchange and (ii) any guarantee or indemnity in respect of any such indebtedness;
Restricted Party	means any person or entity which is (i) listed on a Sanctions List, or a person acting on behalf of such a person; or (ii) the subject of any Sanctions;
Sanctions	means any country- or territory-wide trade, economic or financial sanctions laws, regulations, embargoes or restrictive measures administered, enacted or enforced by a Sanctions Authority;

Sanctions Authority	means each entity under (i) to (v) of the definition of the Sanction List;
Sanctions List	means the Specially Designated Nationals and Blocked Persons list maintained by Office of Foreign Assets Control of the US Department of the Treasury (OFAC), the Consolidated List of Financial Sanctions Targets and the Investment Ban List maintained by Her Majesty's Treasury, or any similar list maintained by, or public announcement of a Sanctions designation made by (i) the Security Council of the United Nations; (ii) the United States of America; (iii) the European Union; (iv) the member states of the European Union and (v) the governments and official institutions or agencies of any of paragraphs (i) to (iv) (including OFAC, the US Department of State and Her Majesty's Treasury), each as amended, supplemented or substituted from time to time; and
Security Interest	means any mortgage, charge, pledge, lien or other security interest including, without limitation, anything analogous to any of the foregoing under the laws of any jurisdiction.

2. THE ISSUER

The International Investment Bank, an international organisation under, and subject to, public international law, established and operating on the basis of the intergovernmental Agreement on the Establishment of the International Investment Bank dated 10 July 1970 and the Charter of the International Investment Bank attached to the Establishment Agreement, initially registered with the Secretariat of the United Nations on 1 December 1971 under number 11417, with its official seat at 7 Mashi Poryvaevoy Street, 107 078 Moscow, Russian Federation (the “**Issuer**”).

3. AUTHORISATION

The issue of the Bonds by the Issuer has been authorised pursuant to the resolution No. 2 of the Issuer’s Management Board on 25 January 2019.

4. THE BONDS

4.1 Type

The Bonds are issued in accordance with section 12/B of Act CXX of 2001 on the Capital Markets (the “**Capital Markets Act**”), 285/2001 (XII. 26.) Government Decree on bonds and Act V of 2013 on the Civil Code (the “**Civil Code**”) as registered debt securities in one series.

4.2 Form

The Bonds are in dematerialised form. In accordance with paragraph (4) of section 6:573 of the Civil Code and section 7(2) of the Capital Markets Act, the Issuer issues and deposits with the Central Depository a document (the “**Document**”), which does not qualify as a security, with the particulars of the Bonds. The Document will remain to be deposited with the Central Depository, or (if applicable) the Central Depository’s successor, until all claims of the Bondholders under the Bonds will be satisfied.

Should any Bonds be cancelled prior to their maturity by the Issuer in accordance with these Conditions, the Document will be cancelled and a new Document (the “**new Document**”) with the particulars of the outstanding number of Bonds will be issued and deposited with the Central Depository in order to reflect the change in the number of outstanding Bonds which arises due to such cancellation. These Conditions form a part of the Bonds and, accordingly, also the Document or new Document, as the case may be.

4.3 Place and date of the private placement, issue and creation of the Bonds

The place of the private placement (in Hungarian *zártkörű forgalomba hozatal*), issue and creation (in Hungarian *kiállítás és keletkeztetés*) of the Bonds is in each case: Budapest, Hungary.

The issue and private placement of the Bonds will take place on 22 March 2019 (the “**Issue Date**”).

4.4 Number of Bonds and denomination

The Bonds are issued in one series consisting of maximum 3,000,000 Bonds.

Each Bond is issued with a denomination of HUF 10,000 (the “**Nominal Value**”).

4.5 Kind

The Bonds are fixed rate bonds.

4.6 Term of the Bonds

The term of the Bonds is a three years period commencing on 22 March 2019 and ending on 22 March 2022 (the “**Maturity Date**”).

5. FURTHER ISSUES

5.1 The Issuer may from time to time, without the consent of the Bondholders, create and issue further bonds having the same terms and conditions as the Bonds or the same in all respects save for the amount and date of the first payment of interest which may be consolidated and form a single series with the outstanding Bonds.

5.2 Notwithstanding and without prejudice to clauses 5.1, the Issuer may at any time issue any further bonds under terms and conditions similar to or different from the Conditions, such bonds representing a different issue than the Bonds. The Issuer may sell any number of such bonds by any means, and at any such price, the Issuer may deem fit in its sole discretion.

6. BONDHOLDERS

In accordance with section 6:578 of the Civil Code and section 138(2) of the Capital Markets Act, any reference to a “**Bondholder**” or the “**Bondholders**” in relation to any Bonds shall mean the person or persons to whose securities account the Bonds are credited until the opposite is proven. A Bond will be transferred by debiting the transferor's securities account with the Bond and crediting the same to the transferee's securities account.

The holder of any Bond who acquired the Bonds in accordance with the paragraph above will (except as otherwise required by law) be deemed and treated as its absolute owner for all purposes (whether or not it is overdue) and no person will be liable for so treating the holder.

7. TRANSFERABILITY AND RIGHTS ATTACHED TO THE BONDS

7.1 The Issuer does not restrict the transfer of the Bonds.

7.2 The Central Depository's rules may specify limitations and closed periods in relation to the transfer of the Bonds between the respective securities accounts of the relevant Participants which shall apply to, and be binding on, the Bondholders.

7.3 No rights of exchange or pre-emption rights are attached to the Bonds.

8. STATUS OF THE ISSUER'S OBLIGATIONS

8.1 The obligations under the Bonds will constitute direct, unsecured, unconditional and unsubordinated obligations of the Issuer ranking *pari passu* among themselves and as to the order of their satisfaction and at least *pari passu* to all other current and future direct, unsecured, unconditional and unsubordinated obligations of the Issuer, except for those obligations of the Issuer so identified by the mandatory provisions of law and provided, however, that the Issuer shall have no obligation to effect equal or rateable payment(s) at any time with respect to any such other obligations and, in particular, the Issuer shall have no obligation to pay other obligations at the same time or as a condition of paying sums due on the Bonds and/or applicable interest and *vice versa*.

8.2 The Issuer undertakes to treat the holders of Bonds equally.

9. NEGATIVE PLEDGE

So long as any Bond remains outstanding, the Issuer shall not, and the Issuer shall procure that none of its Material Subsidiaries will, create or permit to subsist any Security Interest, except for any Permitted Security Interest, upon the whole or any part of its present or future undertaking, assets or revenues (including uncalled capital) to secure any Relevant Indebtedness without at the same time or prior thereto securing the Bonds equally and rateably therewith.

10. UNDERTAKINGS IN RESPECT OF USE OF PROCEEDS

The Issuer undertakes that it will not contrary to the Sanctions use, lend, contribute, or otherwise make available any part of the proceeds of the Bonds directly or indirectly for the purpose of financing any trade, business or other activities involving, or for the benefit of, any person that is a Restricted Party.

11. INTEREST ON THE BONDS

11.1 Interest Rate and Interest Payment Dates

The Bonds bear interest from and including 22 March 2019 at the rate of 2.0 per cent. per annum, payable annually in arrear on 22 March (each an “**Interest Payment Date**”). The first payment (representing a full year's interest) shall be made on 22 March 2020.

11.2 Calculation of Broken Interest

When interest is required to be calculated in respect of a period of less than a full year, it shall be calculated by applying the rate of 2.0 per cent. per annum to the Nominal Value of the Bonds and on the basis of the actual number of days in the relevant period divided by 365.

11.3 End of interest accruing

The Bonds will cease to bear interest from and including the Maturity Date, unless at the moment of all conditions and requirements being satisfied, the repayment of the outstanding amount is refused or delayed by the Issuer without justification. In such case, interest will continue to accrue on the Bonds at the applicable interest rate and by reference to the Nominal Value until the Bondholders are paid all amounts payable as of that day in accordance with these Conditions.

12. MATURITY OF THE BONDS AND REPURCHASE

12.1 Final repayment

If the Bonds do not become early payable under these Conditions, the Nominal Value is payable as a bullet payment on the Maturity Date.

12.2 No redemption at the option of the Issuer

The Issuer shall have no right to early redeem any of the Bonds.

12.3 Purchase, resale and cancellation of the Bonds by the Issuer

The Issuer may at any time purchase any Bonds on the secondary market, under any conditions and for any market price. The Bonds thus purchased by the Issuer shall not cease to exist and may be kept, resold or cancelled by the Issuer, at its sole discretion. The rights and obligations under the Bonds purchased by the Issuer shall cease to exist due to their amalgamation in a single person at the earlier of: (i) cancellation by the Issuer and (ii) their respective Maturity Date.

13. PAYMENTS

13.1 Payments in respect of Bonds

Payments of principal and interest in respect of the Bonds will be made through the Paying Agent in accordance with the rules and regulations of the Central Depository as effective from time to time, and taking into consideration the relevant laws on taxation, through those Participants whose securities account at the Central Depository such Bonds are credited to at the close of business on the Reference Date for that payment, as designated in the regulations of the Central Depository effective from time to time (the “**Reference Date**”). Pursuant to current rules and regulations of the Central Depository, the Reference Date is the day falling two Business Days immediately prior to the relevant Interest Payment Date. Payments shall be due to that person who is deemed to be the Bondholder on the Reference Date.

13.2 Non-Business Days

If the date for payment of any amount in respect of any Bond is not a Business Day, the Bondholder thereof shall not be entitled to payment until the next following Business Day and shall not be entitled to further interest, default interest or other payment in respect of such delay.

14. TAXATION

All payments of principal and interest in respect of the Bonds by the Issuer will be made without withholding or deduction for or on account of any present or future taxes or duties of whatever nature imposed or levied by or on behalf of Hungary or any political subdivision or any authority thereof or therein having power to tax unless such withholding or deduction is required by law. In that event, the Issuer will not pay such additional amounts as may be necessary in order that the net amounts received by the Bondholders after the withholding or deduction shall equal the respective amounts which would have been receivable in respect of the Bonds in the absence of the withholding or deduction.

15. EARLY REPAYMENT OF THE BONDS ON DEFAULT

15.1 Events of Default

If any of the following events occurs and is continuing (each of them an “**Event of Default**”):

- (a) *Non-payment*: the Issuer does not pay an amount payable under the Bonds within 15 calendar days from its due date;
- (b) *Breach of other obligations*: the Issuer breaches any other obligation under or in connection with the Bonds and does not remedy this breach within 30 calendar days from the day on which any Bondholder notified the Issuer of this fact by a written notice delivered to the Issuer;

(c) *Cross-Acceleration of Issuer or Material Subsidiary*: either of the following events occurs in respect of the Issuer or its Material Subsidiary:

- (i) any Financial Indebtedness of the Issuer or any of its Material Subsidiaries is not paid when due or (as the case may be) within any applicable grace period;
- (ii) any such Financial Indebtedness becomes due and payable prior to its stated maturity as a result of an event of default and otherwise than at the option of the Issuer or (as the case may be) the relevant Material Subsidiary or (provided that no event of default, howsoever described, has occurred) any person entitled to such Financial Indebtedness; or
- (iii) the Issuer or any of its Material Subsidiaries fails to pay when due any amount payable by it under any Guarantee of any Financial Indebtedness of any other person;

provided that no event in this paragraph (c) shall constitute an Event of Default unless the amount of Financial Indebtedness and/or the amount payable under any Guarantee, individually or when aggregated (without duplication) with any other Financial Indebtedness or amount payable under Guarantee as a result of any other event specified in this paragraph (c) which has occurred and is continuing, exceeds EUR 15,000,000 (or its equivalent in any other currency or currencies);

(d) *Inability to pay debts*: either of the following events occurs in respect of the Issuer or its Material Subsidiary:

- (i) the Issuer or any of its Material Subsidiaries becomes insolvent or is unable to pay its debts as they fall due;
- (ii) an administrator or liquidator is appointed (or an application for any such appointment is made by or with the consent of the Issuer) in respect of the Issuer or any of its Material Subsidiaries;
- (iii) the Issuer or any of its Material Subsidiaries takes any action for a readjustment or deferment of its material obligations or makes a general assignment or an arrangement or composition with or for the benefit of its creditors or declares a moratorium in respect of its Financial Indebtedness or any Guarantee of any Financial Indebtedness given by it;
- (iv) the Issuer or any of its Material Subsidiaries ceases or threatens to cease to carry on all or any substantial part of its business (otherwise than, in the case of a Material Subsidiary of the Issuer, for the purposes of or pursuant to an amalgamation, reorganisation or restructuring whilst solvent); or
- (v) an effective resolution is passed for the winding up, liquidation or dissolution of the Issuer or any of its Material Subsidiaries (otherwise than, in the case of a Material Subsidiary of the Issuer, for the purposes of or pursuant to an amalgamation, consolidation, reorganisation or restructuring whilst solvent);

(e) *Unlawfulness*: it is or will become unlawful for the Issuer to perform or comply with any of its obligations under or in respect of the Bonds;

then each Bondholder will have the right to declare all Bonds (but not some only) held by that Bondholder immediately due and payable and require the Issuer to pay the Nominal Value of each Bond held by that Bondholder together with any accrued interest, by a written notification to the Issuer.

15.2 Duty to inform

The Issuer must without undue delay notify the Bondholders and the Paying Agent of the occurrence of any Event of Default. Any such notification must specify the nature of the Event of Default and the circumstances giving rise to it.

16. STATUTE OF LIMITATIONS

Claims against the Issuer for payment under the Bonds may not be prescribed unless otherwise permitted by Hungarian law.

17. PAYING AGENT

17.1 The Bonds are issued subject to and with the benefit of a Paying Agency Agreement (such agreement as amended and/or supplemented and/or restated from time to time, the “**Agency Agreement**”) made between the Issuer and UniCredit Bank Hungary Zrt., with its registered seat at Szabadság tér 5-6., 1054, Budapest, Hungary, as paying agent (the “**Paying Agent**”). Pursuant to the Agency Agreement, the Paying Agent agrees to provide interest and principal paying agency services set out therein.

17.2 The Issuer is entitled to vary or terminate the appointment of the Paying Agent and/or appoint additional or other Paying Agents, provided that there will at all times be a paying agent in relation to the Bonds in Hungary.

17.3 In acting under the Agency Agreement, the Paying Agent acts solely as agent of the Issuer and does not assume any obligation to, or relationship of agency or trust with, any Bondholders.

18. AMENDMENTS

18.1 The Conditions may be amended without the consent of the Bondholders for the purposes of the rectification of manifest errors.

18.2 Any amendment to the Conditions hereunder will be published in English language (unless Hungarian language is required under law) in accordance with Condition 19.

19. NOTICES

19.1 Notices to the Bondholders

All notices regarding the Bonds will be deemed to be validly given if published on the Issuer's website (www.iib.int/en) and/or the website of the Budapest Stock Exchange (www.bet.hu). The Issuer shall also ensure that notices are duly published in a manner which complies with the Capital Markets Act and the rules of any stock exchange or other relevant authority on which the Bonds are for the time being listed or by which they have been admitted to trading. Any such notice will be deemed to have been given on the date of the first publication or, where required to be published in more than one medium, on the date of the first publication in all required media.

19.2 Notices from the Bondholders

Notices to be given by any Bondholder shall be in writing and sent to the Issuer at the following address: 7 Mashki Poryvaevoy St., Moscow, 107078, Russian Federation, together with evidence satisfactory to the Issuer concerning the identity of the Bondholder and its title to the Bonds.

19.3 Any notice to the Paying Agent must be delivered in writing to its address set out in Condition 17.1.

19.4 Notices to the Issuer and the Paying Agent must be delivered by registered mail and shall be deemed delivered to the respective party on the date indicated in the delivery confirmation.

20. GOVERNING LAW, LANGUAGE AND DISPUTES

- 20.1** Any rights and obligations (including any non-contractual obligations) arising under or in connection with the Bonds will be governed and construed in accordance with the laws of Hungary.
- 20.2** The Issuer and the Bondholders agree to subject any disputes which may arise out of or in connection with the Bonds, the issue thereof or any document created in connection with such issue (including a dispute relating to any non-contractual obligations arising out of or in connection with the Bonds), to the exclusive jurisdiction of Hungarian courts.
- 20.3** These Conditions are prepared in the English language and shall be binding on the Issuer and the Bondholders. The English language version of these Conditions shall prevail over any translation thereof.

21. WAIVER OF IMMUNITIES

To the extent that the Issuer, at any time and in any jurisdiction, is entitled or may otherwise claim for itself or its assets or properties or revenues, whether of a commercial or a non-commercial nature, immunity from suit, execution, enforcement proceedings or attachment or other legal process and to the extent that such immunity (whether or not claimed) may be attributed in any such jurisdiction to the Issuer or its assets or properties or revenues, whether of a commercial or a non-commercial nature, the Issuer irrevocably and unconditionally waives, and agrees not to plead or claim, any such immunity. For the avoidance of doubt, the irrevocable waiver in this clause extends to any bank account of the Issuer and includes a waiver of any right of immunity in respect of pre-judgment interim relief and post-judgment execution of any judgment or arbitral award.

TAXATION

The following is a general discussion of certain Hungarian tax consequences of the acquisition, ownership and disposal of the Bonds. It does not purport to be a comprehensive description of all tax considerations which may be relevant to a decision to purchase the Bonds, and, in particular, does not consider any specific facts or circumstances that may apply to a particular purchaser of the Bonds. This summary is based on the laws of Hungary currently in force and as applied on the date of this Offering Circular, which are subject to change, possibly with retroactive effect.

Prospective purchasers of the Bonds are advised to consult their own tax advisors as to the tax consequences of the purchase, ownership and disposal of the Bonds, including the effect of any state or local taxes, under the tax laws of Hungary and each country in which they are tax-resident. The acquisition of the Bonds by non-Hungarian tax-resident Bondholders or the payment of interest under the Bonds may trigger additional tax payments in the country of tax residence of the Bondholder. Such payments are not covered by this summary; it is, therefore, advisable to review the provisions of the applicable treaties on the avoidance of double taxation.

Taxation of non-Hungarian tax-resident Bondholders other than individuals

Non-Hungarian tax-resident Bondholders other than individuals are not subject to Hungarian withholding tax on interest received on the Bonds. Profits realised by non-Hungarian tax-resident Bondholders, other than individuals in the form of interest or as capital gains on the disposal of the Bonds, are not subject to corporate income tax in Hungary, provided that the acquisition, ownership and disposal of the Bonds are not attributable to any Hungarian permanent establishment of such Bondholders.

Taxation of individual non-Hungarian tax-resident Bondholders

Individual non-Hungarian tax-resident Bondholders are subject to tax in Hungary only with respect to their Hungarian source income or income that is otherwise taxable in Hungary if the applicable treaty on the avoidance of double taxation, reciprocity, or in the absence of a tax treaty/reciprocity, Act CXVII of 1995 on Personal Income Tax ("**Personal Income Tax Act**") so requires.

Payments received with respect to debt securities such as the Bonds are treated as income under Hungarian law. The tax withheld is personal income tax (at 15 per cent.). However, provided that Hungary has an applicable treaty on the avoidance of double taxation in place with the country of tax-residence of the Bondholder, such treaty may fully exempt the Bondholder from withholding (personal income) tax or may reduce the applicable withholding (personal income) tax rate, with the right to credit any Hungarian withholding tax against the income tax payable in the country of his or her tax residence.

The tax on interest income is to be withheld by the "Payor" (*kifizető*) (as defined below).

Pursuant to Act CL of 2017 on the Rules of Taxation ("**ART**") a "**Payor**" means a Hungarian resident legal person, other organisation, or private entrepreneur that provides taxable income, irrespective of whether such payment is made directly or through an intermediary (post office, credit institution). In respect of interest, Payor means the borrower of a loan or, the issuer of a note, including, the investment service provider or credit institution providing the interest instead of the borrower/issuer. In respect of revenues originating from a transaction concluded with the involvement of a licensed stockbroker, Payor means such stockbroker. The Hungarian permanent establishment of a foreign resident entity is also considered as a Payor.

Capital gains may only be taxed in the state of residence of the private individual Bondholder and therefore, no Hungarian taxes are to be withheld or paid with respect to capital gains realised by individual non-Hungarian tax-resident Bondholders.

Taxation of Hungarian tax-resident Bondholders other than individuals

Under Act LXXXI of 1996 on Corporate Tax and Dividend Tax ("**Corporation Tax Act**"), Hungarian tax-resident taxpayers other than individuals are subject to full, all-inclusive corporate income tax liability. Tax-

resident entities are those established under the laws of Hungary. Foreign entities having their place of management in Hungary are also considered to be Hungarian tax-residents. Taxable income is based on the pre-tax profit as shown in the financial statements calculated under Hungarian GAAP or IFRS Standards and adjusted by certain increasing and decreasing items set forth by tax legislation. Taxable income includes all types of income realised during the financial year, such as interest income and income from capital gains. The rate of Hungarian corporate income tax is 9 per cent.

Financial institutions, financial enterprises, insurance companies and investment enterprises may be subject to local business tax and innovation tax on the basis of the proceeds realised on the Bonds.

Taxation of individual Hungarian tax-resident Bondholders

Individual Hungarian tax-resident Bondholders are subject to tax on their worldwide income. Interest received with respect to debt securities, such as the Bonds, are treated as income. The tax withheld is personal income tax (at 15 per cent.).

Capital gains realised on such Bonds are subject to personal income tax at 15 per cent.

According to the Personal Income Tax Act, Individual Hungarian tax residents are:

- (a) any citizen of Hungary (with the exception of dual citizens without a permanent home or habitual abode in Hungary);
- (b) any individual whose stay in Hungary exceeds 183 days, including the day of entry and the day of exit;
- (c) any individual who has permanent resident status, or is a stateless person; and
- (d) any individual, other than those mentioned in points (a) to (c) above:
 - (i) whose only permanent home is in Hungary;
 - (ii) whose centre of vital interests (*léteérdek központja*) is in Hungary if they have no permanent home in Hungary or if Hungary is not the only country where they have a permanent home;
 - (iii) whose habitual abode is in Hungary if there is no permanent home in Hungary or if Hungary is not the only country where they have a permanent home, and if their centre of vital interests is unknown;

where “centre of vital interests” means the country to which the individual is most closely connected due to family ties and business relations.

An applicable treaty on the avoidance of double taxation may define tax residence prevailing over the domestic definition of tax residence.

The rules of the Personal Income Tax Act may in certain circumstances impose a requirement upon the Payor to deduct tax on the interest payments to individual Bondholders.

SUBSCRIPTION AND SALE

General information about the Offering

The Offering is addressed only to investors in Hungary who are “qualified investors” within the meaning of article 2(1)(e) of Directive 2003/71/EC, as amended (the “**Prospectus Directive**”), as implemented in Hungary by sections 48 to 51 of Act CXXXVIII of 2007 on Investment Firms and Commodity Exchange Service Providers and the Rules of their Activities (“**Qualified Investors**”); and/or to less than 150 natural or legal persons, other than Qualified Investors per member state, and to such other investors in Hungary or such other member states of the European Economic Area where it is possible to do so, in reliance of Regulation S and without the need to publish a prospectus or undertake any other formalities whatsoever under applicable law in reliance on article 3(2) of the Prospectus Directive, to the extent, and only provided that, an investment in the Bonds does not constitute a violation of any applicable law by such investors (the “**Eligible Investors**”). In addition, in the United Kingdom, the offering of the Bonds described herein is directed only at Qualified Investors (x) who have professional experience in matters relating to investments falling within article 19(5) of the Financial Services and Markets Act 2000 (Financial Promotion) Order 2005, as amended (the “**Financial Promotion Order**”) and Qualified Investors falling within article 49(2)(a) to (d) of the Financial Promotion Order and (y) to whom it may otherwise lawfully be directed.

Eligible Investors who intend to invest in the Bonds must be aware of, and comply with the laws, restrictions and limitations applicable to the Offering in their jurisdiction and the restrictions and limitations set out in “*General information*” below. By investing in the Bonds, investors undertake any liability arising in the event that such investment is deemed unlawful under their country of residence.

Under section 45(1) of Act CXX of 2001 on the Capital Markets (the “**Capital Markets Act**”) the public offering or listing on a regulated market of debt securities issued by international financial institutions specified in Schedule 23 of the Capital Markets Act and which has at least one member that is a member state of the European Union, such as the Issuer, requires the publication of an offering circular approved by the National Bank of Hungary (the “**NBH**”). Since the Issuer wishes to list the Bonds on the Regulated Market of the Budapest Stock Exchange (the “**BSE**”), it applied for the NBH to approve the publication of this offering circular (the “**Offering Circular**”). The publication of this Offering Circular has been approved by the NBH on 13 March 2019 in its resolution No. H-KE-III-147/2019. However, this Offering Circular constitutes neither a prospectus nor a base prospectus for the purposes of the Prospectus Directive. Accordingly, this Offering Circular does not purport to meet the format and the disclosure requirements set forth under the Prospectus Directive and Commission Regulation (EC) No 809/2004 implementing the Prospectus Directive, as amended, and it has not been and will not be submitted for approval to any competent authority, other than the NBH, within the meaning of the Prospectus Directive.

No underwriting commitment (in Hungarian: “*jegyzési garanciavállalás*”) is undertaken by any of the Managers with respect to the Offering.

Offering by Auction on the Budapest Stock Exchange

The Bonds will be offered through the MMTS1 auction facility of the BSE (the “**Auction**”). The rules applicable to the auction process are the “Rules of the Budapest Stock Exchange regarding auction trading on the auction board in the MMTS1 trading system” as approved by Resolution No. 385/2018 of the CEO of the BSE (the “**BSE Auction Rules**”).

The Issuer appointed UniCredit to initiate the Auction (the “**Auctioneer**”). Pursuant to the BSE Auction Rules the Auctioneer elected Multiple-Price Trade-Matching Algorithm for the purposes of matching orders. The Auctioneer appointed OTP Bank and UniCredit to tender counter offers (i.e. the purchase offers of investors) (the “**Bidders**”).

Investors shall make their purchase offers either by (i) using auction forms (the “**Auction Form**”) in the form as Annex 1 of this Offering Circular; or (ii) (in case the Investor has a relevant framework agreement with any of the Bidders) submitting their purchase offer to any of the Bidders via Bloomberg.

In case investors make their purchase offers using the Auction Form they must duly complete the Auction Form and either

(i) duly sign the Auction Form and send it in original written form to the following address of any of the Bidders;

OTP Bank: 1131 Budapest, Babér utca 9.

UniCredit: 1054 Budapest, Szabadság tér 5-6.

(ii) or duly sign as an electronic document of the Auction Form with qualified electronic signature³ and send it to OTP Bank using the email address tre_kibocsatas@otpbank.hu

during a period commencing at 10:00 a.m. (Budapest time) on 20 March 2019 and ending at 13:00 (Budapest time) on 20 March 2019 (the “**Auction Period**”). Purchase offers received by the Bidders after the Auction Period shall be considered null and void. Investors must transfer the corresponding payment to the deposit account of UniCredit (IBAN HU98 1091 8001 0000 0001 2176 0007) or OTP Bank (IBAN HU75 1179 4008 2222 5555 0000 0000) not later than 12:00 (noon) (Budapest time) on 22 March 2019 (the “**Issue Date**”). A purchase offer will only be accepted by the Issuer if such offer is made by an Eligible Investor.

Since the Bonds are issued in dematerialised form, a purchase offer will only be accepted if the relevant investor has specified on the Auction Form (i) the details of the entity operating the securities account of the investor; (ii) the number of its securities account; and (iii) the number of its bank account.

The Issuer offers 1,500,000 Bonds in the Auction. However, it reserves the right to accept offers, in whole or in part, for a higher number of Bonds up to 3,000,000 Bonds or a lower number of Bonds or to cancel the Auction or the Offering completely.

Purchase offers will be accepted in increasing order of the yields specified in the respective purchase offers, starting with the purchase offer indicating the lowest yield (not exceeding the aggregate maximum number of Bonds offered as indicated in the previous paragraph). If more than one investor submit purchase offers indicating the same yield and these purchase offers cannot be accepted in full, the Bonds will be allotted pro-rata to the number of Bonds in respect of which the purchase offer was made in accordance with the BSE Action Rules by no later than 15:00 (Budapest time) on 20 March 2019.

The results of the Offering and the Auction will be sent to the National Bank of Hungary.

Listing on the Budapest Stock Exchange

After the completion of the Offering, the Issuer will apply for the listing of the Bonds on the Regulated Market of the Budapest Stock Exchange. Subject to the approval of the Budapest Stock Exchange, the first trading date of the Bonds is expected to occur on or about 26 March 2019.

The Issuer may apply for admission of the Bonds to trading on other regulated markets in the European Union.

Market Making Services

It is the Issuer’s intention to enter into a market making agreement with OTP Bank and UniCredit (the “**Market Makers**”) with the effective date of the first trading day of the Bonds on the Budapest Stock Exchange (the “**First Trading Day**”).

Each Market Maker bilaterally would agree with the Issuer to provide market making services in relation to the Bonds on the Budapest Stock Exchange from the First Trading Day for a period ending on the day when the Bonds are redeemed (the “**Redemption Date**”), by undertaking the obligation to purchase Bonds from Bondholders and sell Bonds to investors (the “**BSE Market Making Services**”), on each day when the BSE is open for business (“**BSE Trading Day**”), subject to the following conditions:

³ Under section 50(3) of the Capital Markets Act “minősített elektronikus aláírással ellátott elektronikus okirat”.

- each Market Maker shall provide the BSE Market Making Services by simultaneously bidding to purchase, and offering to sell, the same number of Bonds with a bid-offer spread of 100 basis point in yield terms;
- each Market Maker shall bid to purchase Bonds in an aggregate principal amount of at least HUF 10,000,000, and offer to sell, Bonds in an aggregate principal amount of at least HUF 10,000,000 on each BSE Trading Day; and
- each Market Maker shall provide the BSE Market Making Services for a continuous period of 2 hours on each BSE Trading Day and shall ensure that the relevant price offered by it for the Bonds is displayed by the BSE during that period.

Each Market Maker bilaterally would agree with the Issuer to provide market making services in relation to the Bonds via Bloomberg Systems from the First Trading Day for a period ending on the Redemption Date, by showing indication of interest to purchase Bonds from Bondholders and to sell Bonds to investors (the “**Bloomberg Market Making Services**”), on each BSE Trading Day when the Bloomberg System is open (“**Bloomberg Business Day**”), subject to the following conditions:

- each Market Maker shall provide the Bloomberg Market Making Services by simultaneously bidding to purchase, and offering to sell, the same number of Bonds with a bid-offer spread of 50 basis point in yield terms;
- each Market Maker shall bid to purchase Bonds in an aggregate principal amount of at least HUF 100,000,000, and offer to sell Bonds in an aggregate principal amount of at least HUF 100,000,000 on each Bloomberg Business Day; and
- each Market Maker shall ensure that the relevant price offered by it for the Bonds is displayed by Bloomberg Systems.

Each Market Maker would have the right to suspend the Market Making Services in case of extreme volatility or market disruptions determined by the Market Maker unilaterally with consideration to market conditions, as evaluated by a prudent service provider.

Any of the parties would be able to terminate the market making agreement with a 30 days’ notice.

SETTLEMENT

General

The Bonds are in dematerialised form. In accordance with paragraph (4) of section 6:573 of Act V of 2013 on the Civil Code (the “**Civil Code**”) and section 7(2) of Act CXX of 2001 on the Capital Markets (the “**Capital Markets Act**”), the Issuer issues and deposits with KELER Központi Értéktár Zrt. (the “**Central Depository**”) a document (the “**Document**”), which does not qualify as a security, with the particulars of the Bonds. The Document will remain to be deposited with the Central Depository, or (if applicable) the Central Depository’s successor, until all claims of the Bondholders under the Bonds will be satisfied.

Should any Bonds be cancelled prior to their maturity by the Issuer, the Document will be cancelled and a new Document with the particulars of the outstanding number of Bonds will be issued and deposited with the Central Depository in order to reflect the change in the number of outstanding Bonds which arises due to such cancellation.

Title to the Bonds

In accordance with section 6:578 of the Civil Code and section 138(2) of the Capital Markets Act, any reference to a “**Bondholder**” or the “**Bondholders**” in relation to any Bonds shall mean the person or persons to whose securities account the Bonds are credited until the opposite is proven. A Bond will be transferred by debiting the transferor’s securities account with the Bond and crediting the same to the transferee’s securities account.

The holder of any Bond who acquired the Bonds in accordance with the paragraph above will (except as otherwise required by law) be deemed and treated as its absolute owner for all purposes (whether or not it is overdue) and no person will be liable for so treating the holder.

Payments

Payments of principal and interest in respect of the Bonds will be made through the Paying Agent in accordance with the rules and regulations of the Central Depository as effective from time to time, and taking into consideration the relevant laws on taxation, through those Participants (as defined below) whose securities account at the Central Depository such Bonds are credited to at the close of business on the reference date for that payment, as designated in the regulations of the Central Depository effective from time to time (the “**Reference Date**”). Pursuant to current rules and regulations of the Central Depository, the Reference Date is the day falling two Business Days immediately prior to the relevant Interest Payment Date. Payments shall be due to that person who is deemed to be the Bondholder on the Reference Date. “**Participant**” means any entity which has a securities accounts with the Central Depository.

GENERAL INFORMATION

Authorisations

The Issuer hereby confirms that, as of the Issue Date, it shall have obtained all consents, approvals and authorisations by its competent governance bodies in connection with the issue of the Bonds and the listing thereof on the Regulated Market of the Budapest Stock Exchange.

Listing and trading

The Issuer will apply for the listing of the Bonds on the Regulated Market of the Budapest Stock Exchange. However, no assurance can be given that the Bonds will be admitted to trading on the Budapest Stock Exchange.

The Issuer may also apply, if it so deems fit, for the admission of the Bonds to listing, trading and/or quotation on any other listing authorities, stock exchanges, regulated markets and/or quotation systems.

Paying Agent

As of the date of this Offering Circular, UniCredit Bank Hungary Zrt., with its registered seat at Szabadság tér 5-6., 1054, Budapest, Hungary, is appointed as Paying Agent.

Selling and transfer restrictions

The distribution of this Offering Circular and the offering, purchase or transfer of the Bonds in certain jurisdictions may be restricted by law and, therefore, persons into whose possession this Offering Circular comes or which otherwise intend to subscribe for, purchase or otherwise transfer the Bonds should inform themselves about and observe any restrictions, including those set out in the paragraphs which follow. Any failure to comply with these restrictions may constitute a violation of the securities laws of any such jurisdiction. By subscribing for or purchasing the Bonds, whether in this Offering or subsequently, investors assume any liability arising in the event that such subscription or purchase is deemed unlawful under the country of residence.

No action has been or will be taken in any country or jurisdiction, other than Hungary, that would permit a public trading of the Bonds or possession or distribution of this Offering Circular (or any other offering or publicity material relating to the Bonds) in any country or jurisdiction where action for that purpose is required or doing so may be restricted by law.

Accordingly, the Bonds may not be offered or sold, directly or indirectly, and neither this Offering Circular nor any other offering material or advertisements in connection with the Bonds may be distributed or published in or from any country or jurisdiction, except under circumstances that will result in compliance with any applicable rules and regulations of any such country or jurisdiction.

This offering of the Bonds described herein is available only to investors in Hungary who are “qualified investors” within the meaning of article 2(1)(e) of the Prospectus Directive, as implemented in Hungary by sections 48 to 51 of Act CXXXVIII of 2007 on Investment Firms and Commodity Exchange Service Providers and the Rules of their Activities; and/or to less than 150 natural or legal persons, other than qualified investors per member state and to such other investors in Hungary or such other member states of the European Economic Area where it is possible to do so, in reliance of Regulation S and without the need to publish a prospectus or undertake any other formalities whatsoever under applicable law, in reliance on article 3(2) of the Prospectus Directive, to the extent, and only provided that, an investment in the Bonds does not constitute a violation of any applicable law by such investors. In addition, in the United Kingdom, the offering of the Bonds described herein is directed only at Qualified Investors (x) who have professional experience in matters relating to investments falling within article 19(5) of the Financial Promotion Order and Qualified Investors falling within article 49(2)(a) to (d) of the Financial Promotion Order and (y) to whom it may otherwise lawfully be directed.

In particular, the Bonds have not been and will not be registered under the U.S. Securities Act or with any securities regulatory authority of any state or other jurisdiction and, accordingly, may not be offered or sold within the United States.

Each purchaser of the Bonds outside the United States, by accepting delivery of this Offering Circular, will be deemed to have represented, agreed and acknowledged that it complies with all applicable laws and regulations of

the United States. The Issuer will not recognise any resale or other transfer, or attempted resale or other transfer, in respect of the Bonds made other than in compliance with the restrictions under any applicable laws and regulations of the United States.

ANNEX 1

Auction Form⁴

in relation to the purchase by way of an auction procedure of HUF 15,000,000,000 2.0 per cent. Fixed Rate bonds due 2022 (name: IIB 2022/I HUF Bond; short name: IIB 2022/I; ISIN Code: HU0000358825) (the “**Bonds**”) to be issued by the International Investment Bank (7 Mashki Poryvaevoy Street, 107 078 Moscow, Russian Federation) (the “**Issuer**”).

Capitalised terms used in this Auction Form have the same meaning given to them in the offering circular relating to the Bonds dated 11 March 2019 (the “**Offering Circular**”), unless the context indicates otherwise or there is an explicit reference to a different interpretation. The provisions of the Offering Circular apply to this Auction Form accordingly.

Name of the Bidder:	[OTP Bank][UniCredit]
Offeror’s name (the Offeror):	.....
Address / seat:	.....
Classification ⁵ :	foreign currency resident legal entity / not foreign currency resident (name of the country)
Court Registry number / Registration number:	.....
Tax number:	.....
Offeror’s Bank account keeping institution’s name:	.....
Offeror’s Bank account keeping institution’s account number:	.....
Securities account number, account number at Central Depository:	.....
Representative’s / authorised representative’s name, personal ID number / passport number:	.....
Representative’s / authorised representative’s address / seat:	.....
Telephone number:	.....
E-mail address:	.....

As Offeror, I make an irrevocable purchase offer in relation to:

_____, that is _____ Bonds with a denomination of HUF 10,000 per Bond,

at the price of _____ per cent. (rounded up to four decimals),

amount payable: HUF _____.

I acknowledge that this offer may be accepted in part (up to a specified amount) and the corresponding payment must be made not later than 12:00 (noon) (Budapest time) on 22 March 2019 (the “**Issue Date**”).

⁴ Please complete using capital letters.

⁵ To be underlined appropriately.

The Offeror acknowledges that the Offeror's bank account will be debited with the amount of the purchase price by [OTP Bank][UniCredit] as Bidder simultaneously with the Offeror's execution of this Auction Form, but in any event not later than 12:00 (noon) (Budapest time) on the Issue Date. Offerors may pay the purchase price by way of bank transfer from a bank other than the one held with the Bidder to the following separate deposit account of [UniCredit (IBAN HU98 1091 8001 0000 0001 2176 0007)][OTP Bank (IBAN HU75 1179 4008 2222 5555 0000 0000)]. In the event of a bank transfer, the purchase price must be credited to the above deposit account at no later than 12:00 (noon) (Budapest time) on the Issue Date.

The Offeror agrees not to make any claim against the Issuer or the Bidder (other than reclaiming amounts paid to the Bidder for Bonds which were not allocated to the Offeror), for the payment of interest or damages with respect to any part of this purchase offer which is not accepted by the Issuer or the Bidder.

The Offeror accepts, that the relevant business conditions of the Bidder apply in connection with the performance of the services provided under the Offering Circular and the present Auction Form.

By signing this Auction Form I acknowledge that I have the duty to become familiar with the contents of the Offering Circular and the relevant business conditions of the Bidder and I give my consent to the Bidder to transfer any data / personal data set out in this Auction Form to the Issuer or its affiliates for the purposes of using such data by the Issuer or its affiliates in connection with any tasks related to the offering of the Bonds. This statement is made by me on the basis of my sole decision with full knowledge of the contents of the Offering Circular. I acknowledge that after having signed this Auction Form it cannot be amended or revoked by me.

The Offeror declares as being qualified as [professional client] [eligible counterparty] in accordance with MiFID regulations and Act CXXXVIII of 2007 on Investment Firms and Commodity Exchange Service Providers and the Rules of their Activities.

I declare that the information supplied by me in this Auction Form is accurate and acknowledge that the provision of any untrue information may result in this Auction Form becoming null and void.

Place: _____, _____ (day) _____ (month) _____ (year)

(authorised) signature

ANNEX 2

INTERNATIONAL INVESTMENT BANK

IIB 2022/I HUF Bond (short name: IIB 2022/I)

DEMATERIALIZED BOND DOCUMENT

(THIS DOCUMENT DOES NOT CONSTITUTE A SECURITY OR A BOND)

The Terms and Conditions of the Bond in the Offering Circular dated 11 March 2019 shall form part of this Document.

1. Details of the Issuer:

Complete name:	International Investment Bank
Abbreviated name:	IIB
Registered seat:	Mashi Poryvaevoy Street, 107 078 Moscow, Russian Federation
Registration number:	registered with the Secretariat of the United Nations on 1 December 1971 under number 11417
Name of the first signatory:	...
Authority (position):	...
Name of the second signatory:	...
Authority (position):	...

2. Details of the authority and decision for the issuance the Bonds

Type and date of the decision on the issuance by the Issuer:	The issue of the Bonds by the Issuer has been authorised pursuant to the resolution No. 2 of the Issuer's Management Board on 25 January 2019.
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3. Details of the Bonds

Name of the Bond:	IIB 2022/I HUF Bond (short name: IIB 2022/I)
ISIN Code:	HU0000358825
Specified Currency:	HUF
Denomination (Nominal Value):	HUF 10,000
Number of Bonds issued:	...
The aggregate principal amount of the Bonds:	HUF ...
Method of issuance:	Private placement
Issue Date:	22 March 2019
Effective date:	22 March 2019
Term of the Bonds:	The term of the Bonds is a three (3) years period commencing on 22

	March 2019 and ending on the Maturity Date.
Maturity Date:	22 March 2022
Interest provisions:	Fixed rate
Rate of interest:	2.0 per cent. per annum
Day count fraction for broken interest periods:	Actual/365
Interest Payment Dates:	The Bonds bear interest from and including 22 March 2019 at the rate of 2.0 per cent. per annum, payable annually in arrear on 22 March.
Schedule of Interest Payment Dates:	22 March 2020 22 March 2021 22 March 2022
Business Day Convention:	If the date for payment of any amount in respect of any Bond is not a Business Day, the Bondholder thereof shall not be entitled to payment until the next following Business Day and shall not be entitled to further interest, default interest or other payment in respect of such delay.
Business Day:	means a day which is both a day on which commercial banks settle payments and are open for general business in Budapest and a day on which KELER Központi Értéktár Zrt. effects payments and securities transfers.
Redemption:	The Bonds will be redeemed on the Maturity Date.
Transferability:	Transferability of the Bonds is not restricted.
Status of the Bonds:	The obligations under the Bonds will constitute direct, unsecured, unconditional and unsubordinated obligations of the Issuer ranking <i>pari passu</i> among themselves and as to the order of their satisfaction and at least <i>pari passu</i> to all other current and future direct, unsecured, unconditional and unsubordinated obligations of the Issuer, except for those obligations of the Issuer so identified by the mandatory provisions of law and provided, however, that the Issuer shall have no obligation to effect equal or rateable payment(s) at any time with respect to any such other obligations and, in particular, the Issuer shall have no obligation to pay other obligations at the same time or as a condition of paying sums due on the Bonds and/or applicable interest and <i>vice versa</i> .
Security for the performance of obligations under the Bonds:	The Bonds are unsecured.
Purpose of the issue of the Bonds:	The proceeds from the issue of the Bonds will be used to finance the existing loan portfolio of the Issuer and new lending to its EU Member States and for debt financing.

Budapest, 22 March 2019

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International Investment Bank

Consolidated financial statements

Year ended 31 December 2015

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 consolidated financial statements of the International Investment Bank (hereinafter the "Bank") and its subsidiaries (collectively, the "Group"), which comprise the consolidated statement of financial position as at 31 December 2015, and the consolidated income statement, consolidated statement of comprehensive income, consolidated statement of changes in equity and consolidated 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 consolidated financial statements

Management is responsible for the preparation and fair presentation of these consolidated financial statements in accordance with International Financial Reporting Standards, and for such internal control as management determines is necessary to enable the preparation of consolidated 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 consolidated 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 consolidated financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the consolidated financial statements. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the consolidated 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 consolidated 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 consolidated 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 consolidated financial statements present fairly, in all material respects, the financial position of the Group as at 31 December 2015, and its financial performance and its cash flows for the year then ended in accordance with International Financial Reporting Standards.



15 March 2016


Moscow, Russia

CONSOLIDATED STATEMENT OF FINANCIAL POSITION**As at 31 December 2015***(Thousands of Euros)*

	<i>Note</i>	<i>31 December 2015</i>	<i>31 December 2014</i>
Assets			
Cash and cash equivalents	5	59,519	65,918
Deposits with banks and other financial institutions	6	100,392	34,371
Financial assets at fair value through profit or loss	7	1,844	311
Available-for-sale investment securities	8	93,031	24,973
Available-for-sale investment securities pledged under repurchase agreements	8	23,028	13,903
Held-to-maturity investment securities	9	50,034	81,000
Held-to-maturity investment securities pledged under repurchase agreements	9	73,194	42,634
Long-term loans to banks	10	140,597	132,032
Loans to customers	11	165,742	108,276
Investment property	12	33,819	52,879
Property and equipment	13	66,393	53,207
Other assets	14	1,810	2,028
Total assets		809,403	611,532
Liabilities			
Due to banks and other financial institutions	15	113,373	58,669
Current customer accounts		7,430	4,788
Financial liabilities at fair value through profit or loss	7	29,898	21,705
Long-term loans of banks	16	44,187	20,540
Debt securities issued	17	212,724	112,759
Other liabilities	14	4,088	3,656
Total liabilities		411,700	222,117
Equity			
Subscribed capital	20	1,300,000	1,300,000
Callable capital		(996,947)	(1,027,382)
Paid-in capital		303,053	272,618
Revaluation reserve for available-for-sale investment securities	18	(1,664)	(999)
Revaluation reserve for property and equipment	3	31,453	35,095
Foreign currency translation reserve		(120)	(224)
Retained earnings less net income for the year		62,925	78,687
Net income for the year		2,056	4,238
Total equity		397,703	389,415
Total equity and liabilities		809,403	611,532

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

Nikolay Kosov



Chairman of the Board

Eugeny Atanassov



Head of the Financial Department

15 March 2016

The accompanying notes 1-30 are an integral part of these consolidated financial statements.

CONSOLIDATED INCOME STATEMENT**Year ended 31 December 2015***(Thousands of Euros)*

	<i>Note</i>	2015	2014
Financial result from continuing operations			
Interest income	21	27,132	16,799
Interest expenses	21	(17,744)	(4,777)
Net interest income		9,388	12,022
Allowance for impairment of loans to customers	11	(6,166)	(3,572)
Net interest income after allowance for loan impairment		3,222	8,450
Fee and commission income		548	42
Fee and commission expense		(133)	(117)
Net fee and commission income/(expense)		415	(75)
Net losses from dealing in foreign currencies and operations with foreign currency derivatives		(11,963)	(17,993)
Net gains from revaluation of assets and liabilities in foreign currencies		22,983	20,354
Net gains from available-for-sale investment securities	21	3,204	5,165
Income from lease of investment property	12	5,214	8,116
Income from revaluation of investment property	12	(2,500)	257
Revenues from sales of inventory		–	3,569
Other expenses		(296)	(225)
Net non-interest income		16,642	19,243
Operating income		20,279	27,618
Reversal of allowance/(allowance) for impairment of other assets	14	89	(1,730)
General and administrative expenses	22	(16,908)	(16,931)
Cost of inventories sold		–	(4,305)
Other operating expenses		(1,404)	(414)
Operating expenses		(18,223)	(23,380)
Net income for the year		2,056	4,238

The accompanying notes 1-30 are an integral part of these consolidated financial statements.

CONSOLIDATED STATEMENT OF COMPREHENSIVE INCOME**Year ended 31 December 2015***(Thousands of Euros)*

	<i>Note</i>	2015	2014
Net income for the year		<u>2,056</u>	<u>4,238</u>
Other comprehensive income/(loss)			
<i>Other comprehensive income/(loss) to be reclassified to profit or loss in subsequent periods</i>			
Net unrealized losses on available-for-sale investment securities		(665)	(1,213)
Translation differences		<u>104</u>	<u>995</u>
Net other comprehensive loss to be reclassified to profit or loss in subsequent periods		<u>(561)</u>	<u>(218)</u>
<i>Other comprehensive income not to be reclassified to profit or loss in subsequent periods</i>			
Revaluation of property and equipment	13	<u>(3,642)</u>	<u>1,720</u>
Net other comprehensive income not to be reclassified to profit or loss in subsequent periods		<u>(3,642)</u>	<u>1,720</u>
Other comprehensive (loss)/income		<u>(4,203)</u>	<u>1,502</u>
Total comprehensive (loss)/income for the year		<u><u>(2,147)</u></u>	<u><u>5,740</u></u>

The accompanying notes 1-30 are an integral part of these consolidated financial statements.

CONSOLIDATED STATEMENT OF CHANGES IN EQUITY**Year ended 31 December 2015***(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>Foreign currency translation reserve</i>	<i>Retained earnings</i>	<i>Total equity</i>
At 31 December 2013	1,300,000	(1,058,685)	214	33,375	(1,219)	78,687	352,372
Profit for the year	-	-	-	-	-	4,238	4,238
Other comprehensive loss for the year	-	-	(1,213)	1,720	995	-	1,502
Total comprehensive income	-	-	(1,213)	1,720	995	4,238	5,740
Contributions to capital (Note 18)	-	31,303	-	-	-	-	31,303
At 31 December 2014	1,300,000	(1,027,382)	(999)	35,095	(224)	82,925	389,415
Profit for the year	-	-	-	-	-	2,056	2,056
Other comprehensive (income)/loss for the year	-	-	(665)	(3,642)	104	-	(4,203)
Total comprehensive income	-	-	(665)	(3,642)	104	2,056	(2,147)
Contributions to capital (Note 18)	-	30,435	-	-	-	(20,000)	10,435
At 31 December 2015	1,300,000	(996,947)	(1,664)	31,453	(120)	64,981	397,703

The accompanying notes 1-30 are an integral part of these consolidated financial statements.

CONSOLIDATED STATEMENT OF CASH FLOWS**Year ended 31 December 2015***(Thousands of Euros)*

	<i>Note</i>	2015	2014
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		17,498	8,495
Interest, fees and commissions paid		(1,497)	(1,342)
Realised gains less losses from dealing in foreign currencies and operations with foreign currency derivatives		(5,420)	3,426
Cash flows from lease of investment property		5,214	8,116
General and administrative expenses		(15,814)	(16,592)
Other operating expenses on banking operations		(932)	(426)
Cash flows from operating activities before changes in operating assets and liabilities		(951)	1,677
<i>Net (increase)/decrease in operating assets</i>			
Deposits with banks and other financial institutions		(76,379)	10,857
Long-term loans to banks		(5,904)	(70,127)
Loans to customers		(61,048)	(72,944)
Other assets		401	6,744
<i>Net increase/(decrease) in operating liabilities</i>			
Due to banks and other financial institutions		60,572	6,978
Current customer accounts		2,618	1,452
Other liabilities		135	(541)
Net cash flows from operating activities		(80,556)	(115,904)
Cash flows from investing activities			
Purchase of available-for-sale investment securities		(245,442)	(295,580)
Proceeds from sale and redemption of available-for-sale investment securities		166,802	284,823
Purchase of held-to-maturity investment securities		–	(7,139)
Proceeds from redemption of held-to-maturity investment securities		20,868	5,626
Investments in investment property		(33)	(154)
Acquisition of property and equipment		(2,764)	(1,817)
Net cash flows from investing activities		(60,569)	(14,241)
Cash flows from financing activities			
Long-term interbank financing raised		21,448	17,852
Long-term interbank financing repaid		(1,123)	(262)
Placement of bonds		184,399	131,070
Redemption of bonds		(78,725)	(1,846)
Contributions to capital		10,435	31,303
Net cash flows from financing activities		136,434	178,117
Effect of exchange rate changes on cash and cash equivalents		(1,708)	(2,099)
Net increase in cash and cash equivalents		(6,399)	45,873
Cash and cash equivalents, beginning		65,918	20,045
Cash and cash equivalents, ending	5	59,519	65,918

The accompanying notes 1-30 are an integral part of these consolidated financial statements.

(Thousands of Euros)

1. Principal activities

These consolidated financial statements include the financial statements of the International Investment Bank (the "Bank") and its subsidiaries. The Bank and its subsidiaries are hereinafter referred together as the "Group". The International Investment Bank is the parent company of the Group. The list of the Bank's subsidiaries is presented in Note 2.

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 Group had an average of 237 staff employees during 2015 (2014: 179).

On 31 July 2014, the EU Council imposed sectoral sanctions against Russia. The preamble of the Decision of the EU Council of 31 July 2014 (paragraph 9) and Council Regulation (EU) No 833/2014 of 31 July 2014 (paragraph 5), which was developed based on the Decision, emphasize that the sanctions do not cover Russia-based institutions with international status established by intergovernmental agreements in which Russia is one of the parties. Therefore, International Investment Bank is not subject to the restrictive measures.

Despite the existing difficult international environment and the risk of unpredictable deterioration in 2015 of the financial climate in the country where the Bank's head office is located, the Bank continues to expand its operations.

- ▶ Hungary re-entered the Bank. At the 102nd meeting of the IIB's Council (Sofia, 20-21 November 2014), member countries unanimously approved the Hungary's re-entering the Bank. In May 2015, Hungary completed all the required domestic procedures and became a full-fledged member of the Bank by making a contribution to its share capital. At the end of 2015, Hungary's share in the IIB's paid-in capital was EUR 30 million.
- ▶ As a result of the Hungary's re-entering, the respective share of the Russian Federation fell below 50% and was 49.5%. The share of the EU countries grew up to 47%.
- ▶ The program for the additional capitalization of the Bank announced during the 99th meeting of the IIB's Council is about to be completed: in December 2015, Mongolia made its contribution of EUR 0.43 million.
- ▶ In April 2015, the Bank opened its first European regional office in Bratislava with the assistance of the Ministry of Finance of the Slovak Republic.
- ▶ The Bank continues to implement a new corporate governance structure and introduce the respective changes to its constituent documents: The Protocol on introducing changes to the Agreement on the Establishment of the IIB and the Statutes elaborated in May 2014 has been signed by all member countries, and the respective ratification procedures have been implemented.
- ▶ The Bank is assigned the following investment grade ratings: BBB- (outlook stable) by Fitch Ratings and Baa1 (outlook stable) by Moody's. In October 2015, the Bank was assigned the A rating (outlook stable) by Dagong Global Credit Rating. The IIB became the first international financial institution that was rated by the Chinese agency.
- ▶ The Bank continues to improve its risk management system.
- ▶ The Bank's operations have been diversified on a country-by-country basis due to the implementation of projects practically in all member countries (or with their participation).
- ▶ Loan tools continue to undergo modification. For example, the Bank has focused on providing syndicated lending together with leading financial institutions. The first bank guarantee has been issued.
- ▶ In 2015, the IIB sold additional issues of its securities in Russia, completed offering procedures with regard to securities of previous issues, made the first national currency-denominated issue in Romania, received long-term loans from banks, including funds from Credit Suisse, soft financing from Eximbank Slovakia, and funds from Bulgarian partners.

*(Thousands of Euros)***1. Principal activities (continued)****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>	<i>2015</i> %	<i>2014</i> %
Russian Federation	49.505	55.031
Republic of Bulgaria	13.926	15.481
Czech Republic	10.023	11.142
Hungary	9.899	–
Slovak Republic	7.088	7.880
Romania	6.089	6.769
Republic of Cuba	1.769	1.966
Socialist Republic of Vietnam	1.211	1.346
Mongolia	0.490	0.385
	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 consolidated 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 Group. Future evolution of the conditions in which the Group operates may differ from the assessment made by the management for the purposes of these consolidated financial statements.

2. Basis of preparation**General**

These consolidated financial statements have been prepared in accordance with International Financial Reporting Standards ("IFRS"), approved by the International Accounting Standards Board.

Subsidiary

The Bank is a parent company of the Group, which owns CJSC IIB Capital (a 100% subsidiary established in 2012) as at 31 December 2014. 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. During 2015, the share capital of the subsidiary was decreased by EUR 7,138 thousand.

(Thousands of Euros)

2. Basis of preparation (continued)

Basis of measurement

These consolidated 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

The financial year of the Group begins on 1 January and ends on 31 December.

Functional and presentation currency

Euro ("EUR") is the Group's functional and presentation currency as it reflects the economic substance of the underlying operations conducted by the Group and circumstances affecting its operations, because most financial assets and financial liabilities as well as income and expenses of the Group are denominated in EUR.

These consolidated financial statements are presented in thousands of Euros ("Thousands of Euros" or "EUR thousand"), unless otherwise indicated.

3. Summary of accounting policies

Changes in accounting policies

The Group has adopted the following amended IFRS and IFRIC which are effective for annual periods beginning on or after 1 January 2015:

Amendments to IAS 19 Defined Benefit Plans: Employee Contributions

IAS 19 requires an entity to consider contributions from employees or third parties when accounting for defined benefit plans. Where the contributions are linked to service, they should be attributed to periods of service as a negative benefit. These amendments clarify that, if the amount of the contributions is independent of the number of years of service, an entity is permitted to recognize such contributions as a reduction in the service cost in the period in which the service is rendered, instead of allocating the contributions to the periods of service. This amendment is not relevant to the Group, since the Group does not have defined benefit plans with contributions from employees or third parties.

Annual improvements 2010-2012 Cycle

These improvements are effective from 1 July 2014 and the Group has applied these amendments for the first time in these consolidated financial statements. They include:

IFRS 2 Share-based Payment

This improvement is applied prospectively and clarifies various issues relating to the definitions of performance and service conditions which are vesting conditions, including:

- ▶ A performance condition must contain a service condition.
- ▶ A performance target must be met while the counterparty is rendering service.
- ▶ A performance target may relate to the operations or activities of an entity, or to those of another entity in the same group.
- ▶ A performance condition may be a market or non-market condition.
- ▶ If the counterparty, regardless of the reason, ceases to provide service during the vesting period, the service condition is not satisfied.

(Thousands of Euros)

3. Summary of accounting policies (continued)

Changes in accounting policies (continued)

The above definitions are consistent with how the Group has identified any performance and service conditions which are vesting conditions in previous periods, and thus these amendments do not impact on the Group's accounting policies.

IFRS 3 Business Combinations

The amendment is applied prospectively and clarifies that all contingent consideration arrangements classified as liabilities (or assets) arising from a business combination should be subsequently measured at fair value through profit or loss whether or not they fall within the scope of IAS 39. This is consistent with the Group's current accounting policy, and thus this amendment does not impact the Group's accounting policy.

IFRS 8 Operating Segments

The amendments are applied retrospectively and clarify that:

- ▶ An entity must disclose the judgments made by management in applying the aggregation criteria in paragraph 12 of IFRS 8, including a brief description of operating segments that have been aggregated and the economic characteristics (e.g., sales and gross margins) used to assess whether the segments are "similar".
- ▶ The reconciliation of segment assets to total assets is only required to be disclosed if the reconciliation is reported to the chief operating decision maker, similar to the required disclosure for segment liabilities.

The Group has not applied the aggregation criteria in IFRS 8.12. The Group has presented the reconciliation of segment assets to total assets in previous periods and continues to disclose the same in Note 25 to these consolidated financial statements, as the reconciliation is reported to the chief operating decision maker for the purpose of decision making.

IFRS 13 Fair Value Measurement

This amendment to IFRS 13 clarifies in the Basis for Conclusions that short-term receivables and payables with no stated interest rates can be measured at invoice amounts when the effect of discounting is immaterial. This is consistent with the Group's current accounting policy, and thus this amendment does not impact the Group's accounting policy.

IAS 16 Property, Plant and Equipment and IAS 38 Intangible Assets

The amendment is applied retrospectively and clarifies in IAS 16 and IAS 38 that the asset may be revalued by reference to observable data on either the gross or the net carrying amount. In addition, the accumulated depreciation or amortization is the difference between the gross and carrying amounts of the asset. The Group recorded adjustments based on revaluation of the buildings owned by the Group during the current period.

IAS 24 Related Party Disclosures

The amendment is applied retrospectively and clarifies that a management entity (an entity that provides key management personnel services) is a related party subject to the related party disclosures. In addition, an entity that uses a management entity is required to disclose the expenses incurred for management services. This amendment is not relevant for the Group as it does not receive any management services from other entities.

Annual improvements 2011-2013 Cycle

These improvements are effective from 1 July 2014 and the Group has applied these amendments for the first time in these consolidated financial statements. They include:

IFRS 3 Business Combinations

The amendment is applied prospectively and clarifies for the scope exceptions within IFRS 3 that:

- ▶ Joint arrangements, not just joint ventures, are outside the scope of IFRS 3.
- ▶ This scope exception applies only to the accounting in the financial statements of the joint arrangement itself.

(Thousands of Euros)

3. Summary of accounting policies (continued)

Changes in accounting policies (continued)

The Group is not a joint arrangement, and thus this amendment is not relevant for the Group and its subsidiaries.

IFRS 13 Fair Value Measurement

The amendment is applied prospectively and clarifies that the portfolio exception in IFRS 13 can be applied not only to financial assets and financial liabilities, but also to other contracts within the scope of IAS 39. The Group does not apply the portfolio exception in IFRS 13.

IAS 40 Investment Property

The description of ancillary services in IAS 40 differentiates between investment property and owner-occupied property (i.e., property, plant and equipment). The amendment is applied prospectively and clarifies that IFRS 3, and not the description of ancillary services in IAS 40, is used to determine if the transaction is the purchase of an asset or business combination. In previous periods, the Group has relied on IFRS 3, not IAS 40, in determining whether an acquisition is of an asset or is a business acquisition. Thus, this amendment does not impact the accounting policy of the Group.

Meaning of 'Effective IFRSs' – Amendments to IFRS 1

The amendment clarifies in the Basis for Conclusions that an entity may choose to apply either a current standard or a new standard that is not yet mandatory, but permits early application, provided either standard is applied consistently throughout the periods presented in the entity's first IFRS financial statements. This amendment to IFRS 1 had no impact on the Group, since the Group is an existing IFRS preparer.

Foreign currency transactions

The consolidated financial statements are presented in Euro, which is the Group'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 consolidated 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 Group's exchange rate on the date of the transaction are included in "Net gains/(losses) from dealing in foreign currencies".

Basis of consolidation

Subsidiaries, which are those entities in which the Group has an interest of more than one half of the voting rights, or otherwise has power to exercise control over their operations, are consolidated. Subsidiaries are consolidated from the date on which control is transferred to the Group and are no longer consolidated from the date that control ceases. All intra-group transactions, balances and unrealized gains on transactions between group companies are eliminated in full; unrealized losses are also eliminated unless the transaction provides evidence of an impairment of the asset transferred. Where necessary, accounting policies for subsidiaries have been changed to ensure consistency with the policies adopted by the Group.

A change in the ownership interest of a subsidiary, without a change of control, is accounted for as an equity transaction. Losses are attributed to the non-controlling interests even if that results in a deficit balance.

If the Group loses control over a subsidiary, it derecognizes the assets (including goodwill) and liabilities of the subsidiary, the carrying amount of any non-controlling interests, the cumulative translation differences, recorded in equity; recognizes the fair value of the consideration received, the fair value of any investment retained and any surplus or deficit in profit or loss and reclassifies the parent's share of components previously recognized in other comprehensive income to profit or loss.

(Thousands of Euros)

3. Summary of accounting policies (continued)

Investments in associates

Associates are entities in which the Group generally has between 20% and 50% of the voting rights (interest), or is otherwise able to exercise significant influence, but which it does not control or jointly control. Investments in associates are accounted for under the equity method and are initially recognized at cost, including goodwill. Subsequent changes in the carrying value reflect the post-acquisition changes in the Group's share of net assets of the associate. The Group's share of its associates' profits or losses is recognized in the consolidated income statement, and its share of movements in reserves is recognized in other comprehensive income. However, when the Group's share of losses in an associate equals or exceeds its interest in the associate, the Group does not recognize further losses, unless the Group is obliged to make further payments to, or on behalf of, the associate.

Unrealized gains on transactions between Group and its associates are eliminated to the extent of the Group's interest in the associates; unrealized losses.

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 Group measures financial instruments, such as trading and available-for-sale securities, derivatives and non-financial assets such as investment property, at fair value at each reporting date. Also, fair values of financial instruments measured at amortized cost are disclosed in Note 24.

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 Group. 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 Group 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 Group 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 Group 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 Group 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 Group 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 from change in fair value 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 consolidated 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 Group 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 Group 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 consolidated 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 Group 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 consolidated 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 Group 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 – Group 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 – Group as lessor

The Group presents assets subject to operating leases in the consolidated statement of financial position according to the nature of the asset. Lease income from operating leases is recognized in the consolidated 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 Group 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 Group 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 Group 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 consolidated 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 consolidated statement of financial position.

Impairment of financial assets

The Group 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, long-term loans to banks and loans to customers carried at amortized cost, the Group 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 Group 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 consolidated 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 consolidated statement of financial position is reduced through the use of an allowance account and the amount of the loss is recognized in the consolidated 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 Group. 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 consolidated 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 Group 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 consolidated income statement.

Available-for-sale financial investments

For available-for-sale financial investments, the Group 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 consolidated income statement – is reclassified from other comprehensive income to the consolidated 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.

(Thousands of Euros)

3. Summary of accounting policies (continued)

Impairment of financial assets (continued)

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 consolidated 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 consolidated income statement, the impairment loss is reversed through the consolidated income statements.

Renegotiated loans

Where possible, the Group 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 consolidated statement of financial position.
- ▶ If the loan restructuring is not caused by the financial difficulties of the borrower the Group 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 Group 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.

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 consolidated statement of financial position where:

- ▶ the rights to receive cash flows from the asset have expired;
- ▶ the Group 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 Group 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 Group 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 Group'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 Group 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 Group's continuing involvement is the amount of the transferred asset that the Group 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 Group's continuing involvement is limited to the lower of the fair value of the transferred asset and the option exercise price.

*(Thousands of Euros)***3. Summary of accounting policies (continued)****Derecognition of financial assets and liabilities (continued)*****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 consolidated income statement.

Property and equipment

Property and equipment are carried in the consolidated 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 consolidated income statement, in which case the increase is recognized in profit or loss. A revaluation deficit is recognized in the consolidated 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 consolidated 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.

(Thousands of Euros)

3. Summary of accounting policies (continued)

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 Group 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 Group'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.

Subsequent expenditure is subject to capitalization only when it is probable that future economic benefits associated with an asset will flow to the Group 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 Group are recognized in the consolidated 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 Group 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 Group'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 Group measures an asset classified as held for sale at the lower of its carrying amount and fair value less costs to sell. The Group 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 Group 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.

(Thousands of Euros)

3. Summary of accounting policies (continued)

Contingencies

Contingent liabilities are not recognized in the consolidated 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 consolidated statement of financial position but disclosed in the consolidated financial statements, when an inflow of economic benefits is probable.

Recognition of income and expenses

Revenue is recognized to the extent that it is probable that the economic benefits will flow to the Group and the revenue can be reliably measured. The following specific recognition criteria must also be met before revenue is recognized in the consolidated 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 Group 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 Group 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. 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 consolidated 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 Group's right to receive the payment is established.

(Thousands of Euros)

3. Summary of accounting policies (continued)

Segment reporting

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

Standards issued but not yet effective

The standards issued, but not yet effective, up to the date of issuance of the Group's consolidated financial statements are disclosed below. The Group intends to adopt these standards, if applicable, when they become effective.

IFRS 9 Financial Instruments

In July 2014, the IASB issued the final version of IFRS 9 *Financial Instruments* which reflects all phases of the financial instruments project and replaces IAS 39 *Financial Instruments: Recognition and Measurement* and all previous versions of IFRS 9. The standard introduces new requirements for classification and measurement, impairment, and hedge accounting.

IFRS 9 becomes effective for annual periods beginning on or after 1 January 2018, with early adoption permitted. Retrospective application is required, but comparative information is not compulsory. Early application of previous versions of IFRS 9 (2009, 2010 and 2013) is permitted if the date of initial application is before 1 February 2015. The adoption of IFRS 9 will have an effect on the classification and measurement of the Group's financial assets, but no impact on the classification and measurement of the Group's financial liabilities. The Group expects a significant impact on its equity due to adoption of IFRS 9 impairment requirements, but it will need to perform a more detailed analysis which considers all reasonable and supportable information, including forward-looking elements to determine the extent of the impact.

IFRS 15 Revenue from Contracts with Customers

IFRS 15 was issued in May 2014 and establishes a new five-step model that will apply to revenue arising from contracts with customers. Revenue arising from lease contracts within the scope of IAS 17 *Leases*, insurance contracts within the scope of IFRS 4 *Insurance Contracts* and financial instruments and other contractual rights and obligations within the scope of IAS 39 *Financial Instruments: Recognition and Measurement* (or IFRS 9 *Financial Instruments*, if early adopted) is out of IFRS 15 scope and is dealt by respective standards.

Under IFRS 15 revenue is recognized at an amount that reflects the consideration to which an entity expects to be entitled in exchange for transferring goods or services to a customer. The principles of IFRS 15 provide a more structured approach to measuring and recognizing revenue.

The new revenue standard is applicable to all entities and will supersede all current revenue recognition requirements under IFRS. Either a full or modified retrospective application is required for annual periods beginning on or after 1 January 2018, with early adoption permitted. The Group is currently assessing the impact of IFRS 15 and plans to adopt the new standard on the required effective date.

IFRS 14 Regulatory Deferral Accounts

IFRS 14 is an optional standard that allows an entity, whose activities are subject to rate-regulation, to continue applying most of its existing accounting policies for regulatory deferral account balances upon its first-time adoption of IFRS. Entities that adopt IFRS 14 must present the regulatory deferral accounts as separate line items on the statement of financial position and present movements in these account balances as separate line items in the statement of profit or loss and other comprehensive income. The standard requires disclosures on the nature of, and risks associated with, the entity's rate-regulation and the effects of that rate-regulation on its financial statements. IFRS 14 becomes effective for annual periods beginning on or after 1 January 2016. Since the Group is an existing IFRS preparer, this standard would not apply.

IFRS 16 Leases

In January 2016, the IASB issued IFRS 16 *Leases* which replaces IAS 17 *Leases*. The standard introduces new requirements for recognition, measurement, presentation and disclosure of leases. The standard is effective for annual periods beginning on or after 1 January 2019.

(Thousands of Euros)

3. Summary of accounting policies (continued)

Standards issued but not yet effective (continued)

Amendments to IFRS 11 Joint Arrangements: Accounting for Acquisitions of Interests

The amendments to IFRS 11 require that a joint operator accounting for the acquisition of an interest in a joint operation, in which the activity of the joint operation constitutes a business must apply the relevant IFRS 3 principles for business combinations accounting. The amendments also clarify that a previously held interest in a joint operation is not remeasured on the acquisition of an additional interest in the same joint operation while joint control is retained. In addition, a scope exclusion has been added to IFRS 11 to specify that the amendments do not apply when the parties sharing joint control, including the reporting entity, are under common control of the same ultimate controlling party.

The amendments apply to both the acquisition of the initial interest in a joint operation and the acquisition of any additional interests in the same joint operation and are prospectively effective for annual periods beginning on or after 1 January 2016, with early adoption permitted. These amendments are not expected to have any impact on the Group.

Amendments to IAS 16 and IAS 38 – Clarification of Acceptable Methods of Depreciation and Amortization

The amendments clarify the principle in IAS 16 and IAS 38 that revenue reflects a pattern of economic benefits that are generated from operating a business (of which the asset is part) rather than the economic benefits that are consumed through use of the asset. As a result, a revenue-based method cannot be used to depreciate property, plant and equipment and may only be used in very limited circumstances to amortize intangible assets. The amendments are effective prospectively for annual periods beginning on or after 1 January 2016, with early adoption permitted. These amendments are not expected to have any impact to the Group given that the Group has not used a revenue-based method to depreciate its non-current assets.

Amendments to IAS 16 and IAS 41 – Agriculture: Bearer Plants

The amendments change the accounting requirements for biological assets that meet the definition of bearer plants. Under the amendments, biological assets that meet the definition of bearer plants will no longer be within the scope of IAS 41. Instead, IAS 16 will apply. After initial recognition, bearer plants will be measured under IAS 16 at accumulated cost (before maturity) and using either the cost model or revaluation model (after maturity). The amendments also require that produce that grows on bearer plants will remain in the scope of IAS 41 measured at fair value less costs to sell. For government grants related to bearer plants, IAS 20 *Accounting for Government Grants and Disclosure of Government Assistance* will apply. The amendments are retrospectively effective for annual periods beginning on or after 1 January 2016, with early adoption permitted. These amendments are not expected to have any impact to the Group as the Group does not have any bearer plants.

Amendments to IAS 27 – Equity Method in Consolidated Financial Statements

The amendments will allow entities to use the equity method to account for investments in subsidiaries, joint ventures and associates in their consolidated financial statements. Entities already applying IFRS and electing to change to the equity method in its consolidated financial statements will have to apply that change retrospectively. For first-time adopters of IFRS electing to use the equity method in its consolidated financial statements, they will be required to apply this method from the date of transition to IFRS. The amendments are effective for annual periods beginning on or after 1 January 2016, with early adoption permitted. The Group currently considers whether to apply these amendments for preparation of its consolidated financial statements. These amendments will not have any impact on the Group's consolidated financial statements.

Amendments to IFRS 10 and IAS 28 – Sale or Contribution of Assets between an Investor and its Associate or Joint Venture

The amendments address the acknowledged inconsistency between the requirements in IFRS 10 and IAS 28 in dealing with the loss of control of a subsidiary that is contributed to an associate or a joint venture. The amendments clarify that an investor recognizes a full gain or loss on the sale or contribution of assets that constitute a business, as defined in IFRS 3, between an investor and its associate or joint venture. In December 2015, the IASB decided to postpone the date of entry into force of the amendments for an indefinite period.

(Thousands of Euros)

3. Summary of accounting policies (continued)

Standards issued but not yet effective (continued)

Amendments to IAS 1 – Disclosure Initiative

The amendments to IAS 1 *Presentation of Financial Statements* clarify, rather than significantly change, existing IAS 1 requirements. The amendments clarify:

- ▶ The materiality requirements in IAS 1.
- ▶ That specific line items in the statement(s) of profit or loss and OCI and the statement of financial position may be disaggregated.
- ▶ That entities have flexibility as to the order in which they present the notes to financial statements.
- ▶ That the share of OCI of associates and joint ventures accounted for using the equity method must be presented in aggregate as a single line item, and classified between those items that will or will not be subsequently reclassified to profit or loss.

Furthermore, the amendments clarify the requirements that apply when additional subtotals are presented in the statement of financial position and the statement(s) of profit or loss and OCI. These amendments are effective for annual periods beginning on or after 1 January 2016, with early adoption permitted. These amendments are not expected to have any impact on the Group.

Amendments to IFRS 10, IFRS 12 and IAS 28 – Investment Entities: Applying the Consolidation Exception

The amendments address issues that have arisen in applying the investment entities exception under IFRS 10. The amendments to IFRS 10 clarify that the exemption from presenting consolidated financial statements applies to a parent entity that is a subsidiary of an investment entity, when the investment entity measures all of its subsidiaries at fair value.

Furthermore, the amendments to IFRS 10 clarify that only a subsidiary of an investment entity that is not an investment entity itself and that provides support services to the investment entity is consolidated. All other subsidiaries of an investment entity are measured at fair value. The amendments to IAS 28 allow the investor, when applying the equity method, to retain the fair value measurement applied by the investment entity associate or joint venture to its interests in subsidiaries. These amendments must be applied retrospectively and are effective for annual periods beginning on or after 1 January 2016, with early adoption permitted. These amendments are not expected to have any impact on the Group.

Annual improvements, 2012-2014 Cycle

These improvements are effective on or after 1 January 2016 and are not expected to have a material impact on the Group. They include:

IFRS 5 Non-current Assets Held for Sale and Discontinued Operations – changes in methods of disposal

Assets (or disposal groups) are generally disposed of either through sale or through distribution to owners. The amendment to IFRS 5 clarifies that changing from one of these disposal methods to the other should not be considered to be a new plan of disposal, rather it is a continuation of the original plan. There is therefore no interruption of the application of the requirements in IFRS 5. The amendment also clarifies that changing the disposal method does not change the date of classification. The amendment must be applied prospectively to changes in methods of disposal that occur in annual periods beginning on or after 1 January 2016, with earlier application permitted.

IFRS 7 Financial Instruments: Disclosures – servicing contracts

IFRS 7 requires an entity to provide disclosures for any continuing involvement in a transferred asset that is derecognized in its entirety. The Board was asked whether servicing contracts constitute continuing involvement for the purposes of applying these disclosure requirements. The amendment clarifies that a servicing contract that includes a fee can constitute continuing involvement in a financial asset. An entity must assess the nature of the fee and arrangement against the guidance for continuing involvement in paragraphs IFRS 7.B30 and IFRS 7.42C in order to assess whether the disclosures are required. The amendment is effective for annual periods beginning on or after 1 January 2016, with early adoption permitted. The amendment is to be applied such that the assessment of which servicing contracts constitute continuing involvement will need to be done retrospectively. However, the required disclosures would not need to be provided for any period beginning before the annual period in which the entity first applies the amendments.

(Thousands of Euros)

3. Summary of accounting policies (continued)

Standards issued but not yet effective (continued)

IFRS 7 Financial Instruments: Disclosure – applicability of the offsetting disclosures to condensed interim financial statements

In December 2011, IFRS 7 was amended to add guidance on offsetting of financial assets and financial liabilities. In the effective date and transition for that amendment IFRS 7 states that "An entity shall apply those amendments for annual periods beginning on or after 1 January 2013 and interim periods within those annual periods". The interim disclosure standard, IAS 34, does not reflect this requirement, however, and it is not clear whether those disclosures are required in the condensed interim financial report.

The amendment removes the phrase "and interim periods within those annual periods", clarifying that these IFRS 7 disclosures are not required in the condensed interim financial report. The amendment must be applied retrospectively and is effective for annual periods beginning on or after 1 January 2016, with early adoption permitted.

IAS 19 Employee Benefits – regional market issue regarding discount rate

The amendment to IAS 19 clarifies that market depth of high quality corporate bonds is assessed based on the currency in which the obligation is denominated, rather than the country where the obligation is located. When there is no deep market for high quality corporate bonds in that currency, government bond rates must be used. The amendment is effective for annual periods beginning on or after 1 January 2016, with early adoption permitted.

IAS 34 Interim Financial Reporting – disclosure of information "elsewhere in the interim financial report"

The amendment states that the required interim disclosures must either be in the interim financial statements or incorporated by cross-reference between the interim financial statements and wherever they are included within the greater interim financial report (e.g., in the management commentary or risk report). The Board specified that the other information within the interim financial report must be available to users on the same terms as the interim financial statements and at the same time. If users do not have access to the other information in this manner, then the interim financial report is incomplete. These amendments must be applied retrospectively and are effective for annual periods beginning on or after 1 January 2016, with early adoption permitted.

4. Significant accounting judgments and estimates

Assumptions and estimation uncertainty

In the process of applying the Group'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 consolidated financial statements, which have the most significant effect on the amounts recognized in the consolidated 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 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 Group's consolidated statement of financial position less allowances for impairment. The Group regularly reviews its financial assets to assess impairment. When assessing impairment losses, the Group 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 Group 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 consolidated 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. More details are provided in Note 24.

Impairment of available-for-sale equity securities

The Group 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 Group 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 Group applies the fair value model with regard to investment property. Buildings included in fixed assets are stated at revalued amount.

As for buildings within property and equipment, the Group 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 Group's building was carried out as at 31 December 2015 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 technique may differ from the prices of actual transactions in the real estate market. Starting from 31 December 2015, the revalued building is depreciated in accordance with the remaining useful life.

As for investment property, the Group 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 consolidated income statement. The most recent revaluation of the Group's investment property was carried out as at 31 December 2015 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 technique may differ from the prices of actual transactions in the real estate market. The Group believes that as at 31 December 2015, 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 12 – Investment property.
- ▶ Note 13 – Property and equipment.
- ▶ Note 19 – Contingencies and lending commitments.

*(Thousands of Euros)***5. Cash and cash equivalents**

Cash and cash equivalents comprise:

	<u>2015</u>	<u>2014</u>
Cash on hand	66	392
Nostro accounts with banks and other financial institutions		
<i>Credit rating AAA</i>	–	11
<i>Credit rating from A- to A+</i>	21,106	13,377
<i>Credit rating from BBB- to BBB+</i>	3,059	25
<i>Credit rating from BB- to BB+</i>	350	–
Total Nostro accounts with banks and other financial institutions	24,515	13,413
Short-term deposits with banks:		
Term deposits with banks		
<i>Credit rating from AA- to AA+</i>	–	16,464
<i>Credit rating from A- to A+</i>	–	8,232
<i>Credit rating from BBB- to BBB+</i>	18,304	255
<i>Credit rating from BB- to BB+</i>	16,634	10,005
<i>Credit rating from B- to B+</i>	–	17,157
Total short-term deposits with banks	34,938	52,113
Cash and cash equivalents	59,519	65,918

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

6. Deposits with banks and other financial institutions

Deposits with banks and other financial institutions comprise:

	<u>2015</u>	<u>2014</u>
Term deposits with banks		
<i>Credit rating from A- to A+</i>	15,067	–
<i>Credit rating from BBB- to BBB+</i>	–	3,479
<i>Credit rating from BB- to BB+</i>	6,049	432
<i>Credit rating from B- to B+</i>	79,276	30,460
Deposits with banks and other financial institutions	100,392	34,371

Amounts due from the National Bank of the Republic of Cuba

	<u>2015</u>	<u>2014</u>
Term deposits with the National Bank of the Republic of Cuba without credit rating	34,967	34,967
Less: allowance for impairment	(34,967)	(34,967)
Term deposits with the National Bank of the Republic of Cuba	–	–

Concentration of deposits with banks and other financial institutions

As at 31 December 2015, the Group had one counterparty (31 December 2014: one counterparty) accounting for over 20% of the Group's total deposits with banks and other financial institutions, except for deposits with the National Bank of the Republic of Cuba.

(Thousands of Euros)

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 at 31 December 2015 and 31 December 2014 and notional amounts of term contracts for the purchase and sale of foreign currency specifying contractual exchange rates.

	<i>31 December 2015</i>				
	<i>Notional amount</i>		<i>Weighted average exchange rate</i>	<i>Fair value</i>	
	<i>Purchase</i>	<i>Sale</i>		<i>Assets</i>	<i>Liabilities</i>
Swaps	12,136,720 RUB'000	185,914 EUR'000	65.28	–	29,034
	110,300 RON'000	24,972 EUR'000	4.42	–	864
	61,000 EUR'000	64,982 USD'000	1.07	1,775	–
Term transactions	30,000 EUR'000	32,721 USD'000	1.09	69	–
Financial instruments at fair value through profit or loss				1,844	29,898

	<i>31 December 2014</i>				
	<i>Notional amount</i>		<i>Weighted average exchange rate</i>	<i>Fair value</i>	
	<i>Purchase</i>	<i>Sale</i>		<i>Assets</i>	<i>Liabilities</i>
Swaps	3,700,000 RUB'000	67,565 EUR'000	54.76	–	16,494
Term transactions	1,930,050 RUB'000	30,000 EUR'000	64.34	–	4,155
	2,800 EUR'000	195,020 RUB'000	69.65	311	–
	33,000 EUR'000	41,345 USD'000	1.25	–	1,056
Financial instruments at fair value through profit or loss				311	21,705

Due to issuing bond loans denominated in currencies other than the Group's functional currency (Note 17), the Group concluded cross currency interest rate swaps and currency forwards on an arm's length basis with large international and Russian credit institutions. These swaps are used to regulate long-term currency risks of the Group. Payment netting is not applied to the parties' obligations in respect of interest and principal payments.

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 end of the reporting period and are not indicative of the credit risk.

(Thousands of Euros)

7. Financial instruments at fair value through profit or loss (continued)**Foreign currency transactions (continued)**

As at 31 December 2015 and 31 December 2014, the Group has positions in the following types of derivatives:

Forwards: Forwards contracts are contractual agreements to buy or sell a specified financial instrument at a specific price and date in the future. Forwards are customized contracts transacted in the over-the-counter market.

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.

Fair value measurement is based on the corresponding forward curves that depend on exchange rates, interest rates and swap contract maturity. For the fair value of swaps, the discount rate was calculated on the basis of zero coupon yield curve and credit risk. Changes in the fair value of swaps were mainly due to the increase in the forward EUR to RUB exchange rate.

8. Available-for-sale investment securities

Available-for-sale investment securities comprise:

	<u>2015</u>	<u>2014</u>
<i>Owned by the Group</i>		
Quoted debt securities		
Government bonds of member countries and bonds of regional governments:		
<i>Eurobonds issued by governments of member countries</i>	93,027	11,202
<i>Bonds of regional governments</i>	–	3,395
Government bonds of member countries and bonds of regional governments	<u>93,027</u>	<u>14,597</u>
Corporate bonds		
<i>Credit rating from BBB- to BBB+</i>	–	10,373
Corporate bonds	<u>–</u>	<u>10,373</u>
Total quoted debt securities	<u>93,027</u>	<u>24,970</u>
Quoted equity instruments		
<i>No credit rating</i>	4	3
Total quoted equity instruments	<u>4</u>	<u>3</u>
Available-for-sale investment securities	<u>93,031</u>	<u>24,973</u>
<i>Pledged under repurchase agreements</i>		
Quoted debt securities		
<i>Eurobonds issued by governments of member countries</i>	21,646	13,903
Eurobonds by governments of member countries	<u>21,646</u>	<u>13,903</u>
Corporate bonds		
<i>Credit rating from BBB- to BBB+</i>	1,382	–
Corporate bonds	<u>1,382</u>	<u>–</u>
Total quoted available-for-sale debt securities pledged under repurchase agreements	<u>23,028</u>	<u>13,903</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 2018-2027 (31 December 2014: maturing in 2017-2024). The annual coupon rate for these bonds varies from 2.0% to 6.0% (2014: from 2.9% to 5.0%).

Corporate bonds are represented by the bonds issued by European development banks and banks of member countries, maturing in 2020 (31 December 2014: maturing in 2015-2020). The annual coupon rate for these bonds is 5.0% (31 December 2014: from 5.0% to 8.1%).

(Thousands of Euros)

9. Held-to-maturity investment securities

Held-to-maturity investment securities comprise:

	<u>2015</u>	<u>2014</u>
<i>Owned by the Group</i>		
Quoted debt securities		
<i>Eurobonds issued by governments of member countries</i>	1,272	11,951
Government bonds of member countries	<u>1,272</u>	<u>11,951</u>
Corporate bonds		
<i>Credit rating from A- to A+</i>	–	17,536
<i>Credit rating from BBB- to BBB+</i>	17,442	45,683
<i>Credit rating from BB- to BB+</i>	31,320	5,830
Corporate bonds	<u>48,762</u>	<u>69,049</u>
Total quoted held-to-maturity debt securities	<u>50,034</u>	<u>81,000</u>
<i>Pledged under repurchase agreements</i>		
Quoted debt securities		
<i>Eurobonds issued by governments of member countries</i>	10,489	–
Government bonds of member countries	<u>10,489</u>	<u>–</u>
Corporate bonds		
<i>Corporate bonds with credit rating BBB-</i>	62,705	42,634
Total corporate bonds	<u>62,705</u>	<u>42,634</u>
Held-to-maturity investment securities pledged under repurchase agreements	<u>73,194</u>	<u>42,634</u>

Government bonds of member countries represent EUR-denominated and RUB-denominated securities issued and guaranteed by the Ministries of Finance of these countries, maturing in 2018-2020 (31 December 2014: maturing in 2018-2020). The annual coupon rate for these bonds varies from 3.6% to 7.9% (31 December 2014: from 3.6% to 7.9%).

Corporate bonds are represented by the bonds issued by major companies and banks of member countries and EU countries, maturing in 2016-2023 (31 December 2014: maturing in 2016-2025). The annual coupon rate for these bonds varies from 3.0% to 7.9% (31 December 2014: from 3.4% to 7.9%).

10. Long-term loans to banks

During 2015 the Group continued its lending activities, being guided by the key priorities of the Development Strategy of the IIB. 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 Group considers national development institutes, export and import banks and agencies, international financial organizations and development banks as its key counterparties.

In 2015 and 2014, the Group provided long-term loans to banks operating in the following countries:

	<u>2015</u>	<u>2014</u>
Russian Federation	64,223	89,874
Mongolia	43,044	26,986
Socialist Republic of Vietnam	33,330	15,172
Total long-term loans to banks	<u>140,597</u>	<u>132,032</u>

As at 31 December 2015 and 31 December 2014, outstanding long-term loans to banks are neither past due nor impaired, and allowances for impairment of these loans were not made.

(Thousands of Euros)

10. Long-term loans to banks (continued)**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 2015 and 31 December 2014:

	2015		2014	
	<i>Long-term loans to banks</i>	<i>Share in the total loans, %</i>	<i>Long-term loans to banks</i>	<i>Share in the total loans, %</i>
Pledge of real property (mortgage) and title	6,933	4.9	5,964	4.5
Uncollateralized part of the loans	133,664	95.1	126,068	95.5
	140,597	100.0	132,032	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 2015, long-term loans to five banks (31 December 2014: five banks) with the total amount of loans to each of them exceeding 10% of total long-term loans to banks were recorded on the Group's balance sheet. As at 31 December 2015, the total amount of such major loans was EUR 85,238 thousand (31 December 2014: EUR 85,049 thousand) and no impairment allowances (31 December 2014: no allowances) has been made for them.

11. Loans to customers

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

	2015	2014
Republic of Bulgaria	57,917	31,094
Russian Federation	28,160	2,646
Romania	25,844	5,958
Slovak Republic	23,437	48,345
Mongolia	21,890	23,822
Other	18,249	–
Loans to customers	175,497	111,865
Less: allowance for loan impairment	(9,755)	(3,589)
Loans to customers	165,742	108,276

The information on the overdue loans as at 31 December 2015 and 31 December 2014 is stated below:

	2015	2014
Loans with overdue principal and/or interest	14,858	8,107
Less: allowance for loan impairment	(9,755)	(3,589)
Overdue loans to customers	5,103	4,518

As at 31 December 2015 and 31 December 2014, there were no overdue but not impaired loans.

Allowance for impairment of loans to customers

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

	<i>Slovak Republic</i>	<i>Republic of Bulgaria</i>	<i>Total</i>
At 1 January 2015	3,589	–	3,589
Net (reversal)/charge for the period	(589)	6,755	6,166
At 31 December 2015	3,000	6,755	9,755
Individual impairment	3,000	6,755	9,755
Gross amount of loans, individually determined to be impaired, before deducting any individually assessed impairment allowance	8,103	6,755	14,858

(Thousands of Euros)

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

	<i>Russian Federation</i>	<i>Republic of Bulgaria</i>	<i>Slovak Republic</i>	<i>Total</i>
At 1 January 2014	–	–	–	–
Net charge/(reversal) for the period	(2)	(15)	3,589	3,572
Recoveries	2	15	–	17
At 31 December 2014	–	–	3,589	3,589
Individual impairment	–	–	3,589	3,589
Gross amount of loans, individually determined to be impaired, before deducting any individually assessed impairment allowance	–	–	8,107	8,107

The following table provides an analysis of the customer loan portfolio, net of allowance for impairment, by types of collateral as at 31 December 2015 and 31 December 2014:

	<i>2015</i>		<i>2014</i>	
	<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	35,896	21.6	29,508	27.3
Pledge of equipment and goods in turnover	31,530	19.0	1,706	1.6
Pledge of shares	29,952	18.1	25,947	24.0
Pledge of right of claim	18,492	11.2	12,517	11.6
Uncollateralized part of the loans	49,872	30.1	38,598	35.6
Total loans to customers	165,742	100.0	108,276	100.0

Analysis of collateral for loans to customers

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.

Concentration of loans to customers

As at 31 December 2015, loans to two borrowers (2014: four) with the total amount of loans to each of the two borrowers exceeding 10% of total loans to customers were recorded on the Group's balance sheet. As at 31 December 2015, these loans comprised EUR 40,991 thousand (2014: EUR 65,405 thousand) in total and no impairment allowances (2014: no allowances) has been made for them.

Analysis of loans to customers by industry

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

	<i>2015</i>	<i>2014</i>
Leasing	44,114	19,427
Chemical production	22,743	–
Manufacturing of electrical equipment	21,208	–
Construction of buildings	21,076	20,948
Transport	15,001	–
Pipeline transportation	14,688	25,080
Crude oil refining	9,989	–
Specialized construction	8,103	8,107
Food and beverage	7,569	9,443
Trading	5,418	2,646
Investing activities	4,942	–
Production of vehicles	348	14,892
Communication service	–	11,056
Other	298	266
	175,497	111,865
Less: allowance for loan impairment	(9,755)	(3,589)
Total loans to customers	165,742	108,276

(Thousands of Euros)

12. Investment property

In 2015 and 2014, the following changes occurred in the cost of property under operating lease:

	<u>2015</u>	<u>2014</u>
At 1 January	52,879	53,480
Inseparable improvements	33	154
Transfers in the property and equipment	(16,593)	(1,012)
Effect of revaluation	(2,500)	257
Carrying amount at 31 December	<u>33,819</u>	<u>52,879</u>

The Group rents part of the building under operating lease agreements. In 2015, the Group's income from lease of investment property amounted to EUR 5,214 thousand (2014: EUR 8,116 thousand).

As at 31 December 2015, the fair value of investment property is determined based on the results of valuation performed on 31 December 2015. 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 investment property as at 31 December 2015 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 24.

If the investment property was measured using the cost method, the carrying amounts as at 31 December 2015 and 31 December 2014 would be as follows:

	<u>2015</u>	<u>2014</u>
Cost	20,264	29,486
Accumulated depreciation	(8,092)	(11,360)
Net book value	<u>12,172</u>	<u>18,126</u>

The Group 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.

13. Property and equipment

The movements in property and equipment for the year ended 31 December 2015 were as follows:

	<u>Buildings</u>	<u>Equipment</u>	<u>Computers and software</u>	<u>Office furniture</u>	<u>Vehicles</u>	<u>Capital expenditure</u>	<u>Total</u>
Cost or revalued amount							
At 1 January 2015	50,806	7,069	3,255	486	923	766	63,305
Inseparable improvements	52	-	-	-	-	-	52
Additions	-	-	-	-	-	1,780	1,780
Transfers from the investment property	16,593	-	-	-	-	-	16,593
Transfers	-	179	670	4	102	(955)	-
Disposals	-	(175)	(322)	(18)	(217)	-	(732)
Recovery of accumulated depreciation upon revaluation	(1,002)	-	-	-	-	-	(1,002)
Effect of revaluation	(3,642)	-	-	-	-	-	(3,642)
At 31 December 2015	<u>62,807</u>	<u>7,073</u>	<u>3,603</u>	<u>472</u>	<u>808</u>	<u>1,591</u>	<u>76,354</u>
Accumulated depreciation							
At 1 January 2015	(67)	(6,523)	(2,591)	(319)	(598)	-	(10,098)
Charge for the period	(935)	(176)	(341)	(24)	(96)	-	(1,572)
Disposals	-	152	322	16	217	-	707
Recovery of accumulated depreciation upon revaluation	1,002	-	-	-	-	-	1,002
At 31 December 2015	<u>-</u>	<u>(6,547)</u>	<u>(2,610)</u>	<u>(327)</u>	<u>(477)</u>	<u>-</u>	<u>(9,961)</u>
Net book value							
At 31 December 2014	<u>50,739</u>	<u>635</u>	<u>664</u>	<u>167</u>	<u>325</u>	<u>766</u>	<u>53,207</u>
At 31 December 2015	<u>62,807</u>	<u>526</u>	<u>993</u>	<u>145</u>	<u>331</u>	<u>1,591</u>	<u>66,393</u>

*(Thousands of Euros)***13. Property and equipment (continued)**

The movements in property and equipment for the year ended 31 December 2014 were as follows:

	<i>Buildings</i>	<i>Equipment</i>	<i>Computers and software</i>	<i>Office furniture</i>	<i>Vehicles</i>	<i>Capital expenditure</i>	<i>Total</i>
Cost or revalued amount							
At 1 January 2014	49,398	7,329	2,858	497	749	–	60,831
Inseparable improvements	149	–	–	–	–	–	149
Additions	–	180	475	51	215	766	1,687
Transfers from the investment property	1,012	–	–	–	–	–	1,012
Disposals	–	(440)	(78)	(62)	(41)	–	(621)
Recovery of accumulated depreciation upon revaluation	(1,473)	–	–	–	–	–	(1,473)
Effect of revaluation	1,720	–	–	–	–	–	1,720
At 31 December 2014	50,806	7,069	3,255	486	923	766	63,305
Accumulated depreciation							
At 1 January 2014	(757)	(6,768)	(2,381)	(357)	(568)	–	(10,831)
Charge for the period	(783)	(195)	(288)	(20)	(71)	–	(1,355)
Disposals	–	440	78	58	41	–	617
Recovery of accumulated depreciation upon revaluation	1,473	–	–	–	–	–	1,473
At 31 December 2014	(67)	(6,523)	(2,591)	(319)	(598)	–	(10,098)
Net book value							
At 31 December 2013	48,641	561	477	140	181	–	50,000
At 31 December 2014	50,739	546	664	167	325	766	53,207

As at 31 December 2015, the cost of fully depreciated property and equipment still used by the Group was EUR 7,977 thousand (31 December 2014: EUR 8,834 thousand).

As at 31 December 2015, the fair value of a group of buildings owned by the Group is determined based on the results of valuation performed on 31 December 2015. 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 2015 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 property and equipment refer to Note 24.

If the buildings were measured using the cost method, the carrying amounts as at 31 December 2015 and 31 December 2014 would be as follows:

	<i>2015</i>	<i>2014</i>
Cost	37,635	28,327
Accumulated depreciation	(15,029)	(10,880)
Net book value	22,606	17,447

*(Thousands of Euros)***14. Other assets and liabilities**

Other assets comprise:

	<i>2015</i>	<i>2014</i>
Other accounts receivable	2,256	2,900
Advance payments and future period expenses	1,144	841
Inventories – real estate objects	43	50
	3,443	3,791
Less: allowance for impairment of accounts receivable	(1,633)	(1,763)
Other assets	1,810	2,028

The movements in other impairment allowance are as follows:

	<i>2015</i>	<i>2014</i>
Allowance at 1 January	1,763	411
Net (reversal)/charge for the year	(89)	1,730
Change in allowance resulting from changes in exchange rates	(41)	(378)
Allowance at 31 December	1,633	1,763

Other liabilities comprise:

	<i>2015</i>	<i>2014</i>
Other accounts payable	2,971	2,482
Settlements with employees	1,067	931
Deferred income	50	243
Other liabilities	4,088	3,656

15. Due to banks and other financial institutions

Due to banks and other financial institutions comprise:

	<i>2015</i>	<i>2014</i>
Term deposits of banks and other financial institutions	49,238	19,783
Repurchase agreements	64,756	41,320
Due to banks and other financial institutions	113,994	61,103

The Group performs daily monitoring of the repurchase agreements and the value of collateral when placing/returning additional collateral, if necessary.

Concentration of deposits from banks and other financial institutions

As at 31 December 2015, the Group has two counterparties (31 December 2014: four counterparties) accounting for over 20% of the Group's total deposits from banks and other financial institutions in the amount of EUR 87,788 thousand (31 December 2014: EUR 53,669 thousand).

*(Thousands of Euros)***16. Long-term loans of banks**

As at 31 December 2015, the Group received three long-term loans in the amount of EUR 44,187 thousand granted the Bank maturing in April 2016, June 2017 and May 2020 (31 December 2014: April 2016). The Group raised long-term loans from banks operating in the following countries:

	<i>31 December 2015</i>	<i>31 December 2014</i>
Russian Federation	22,953	20,540
Republic of Bulgaria	13,740	–
Slovak Republic	7,494	–
Long-term loans of banks	44,187	20,540

17. Debt securities issued

On 29 April 2015, the Group placed RUB-denominated bonds, series 02, in the amount of RUB 3 billion (EUR 51,633 thousand) maturing on the 3,640th day after the first day of placement. The coupon rate on bonds was set at 13.25% p.a. and is payable twice a year, with the first coupon payment to be paid on 28 October 2015. As at 30 September 2015, issued RUB-denominated bonds, series 02, recorded at amortized cost amounted to EUR 43,020 thousand. The Group used the proceeds from the offerings for expanding its loan portfolio.

In June 2015 the Group repurchased RUB-denominated bonds for the total amount of RUB 2.31 billion (EUR 39,283 thousand) under investor put option and set a new coupon rate at 12.00% p.a. for the coupon periods 2-5. In September 2015 the Group made a secondary placement of RUB-denominated bonds of these series among investors in the amount of RUB 2.31 billion (EUR 31,487 thousand). Therefore, all RUB-denominated bonds, series 03, are outstanding again.

On 14 October 2015 the Group issued bonds denominated in Romanian lei in the amount of 111.0 million lei (EUR 25,133,000), maturing in three years. The coupon rate on the bonds was set at 4.1% p.a., payable annually, with the first coupon payment to be made on 14 October 2016.

In October 2015 the Group redeemed ruble-denominated bonds, series 01, worth a total of RUB 1.51 billion (EUR 21,315,000), in connection with an investor put option and set a new coupon rate of 12.00% p.a. for coupon periods 2 through 5.

On 19 November 2015, the Group issued ruble-denominated bonds, series 04, in the amount of RUB 5 billion (EUR 72,362,000), maturing on the 3,640th day after the date of issue. The coupon rate on the bonds was set at 11.9% p.a., payable semiannually, with the first coupon payment to be made on 19 May 2016.

At the dates of placement of RUB-denominated bonds, the Group entered into cross-currency interest rate swaps and a currency forward for the purpose of regulating currency risks (Note 7).

18. 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 2015, unpaid portion of the Bank's subscribed capital in the amount of EUR 996,947 thousand (31 December 2014: EUR 1,027,382 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 175,500 thousand (31 December 2014: EUR 296,900 thousand).

*(Thousands of Euros)***18. Equity (continued)****Subscribed and paid-in capital (continued)**

On 18 May 2015, the Government of Hungary contributed EUR 10,000 thousand to the Bank's equity to resume its full membership. In accordance with the Memorandum of Understanding signed at the 102nd meeting of the IIB's Council (20-21 November 2014), the Bank added EUR 10,000 thousand to the contribution of Hungary out of retained earnings for the previous years. On 29 July in accordance with the Memorandum of Understanding signed at the 102nd meeting of the IIB's Council (20-21 November 2014), the Bank fulfilled its obligations to transfer the second payment in the amount of EUR 10,000 thousand out of retained earnings for the previous years as Hungary's additional contribution to the Bank's share capital.

On 28 December 2015, the Government of Mongolia met its obligation, assumed at the 99th IIB Council Meeting, to provide additional capitalization for the Bank. The Bank received EUR 434,800 as part of Mongolia's additional contribution to the Bank's authorized capital.

As a result, the paid-in capital of the International Investment Bank totaled EUR 303,053 thousand (31 December 2014: EUR 272,618 thousand).

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 2014	214	33,375
Net unrealized gains on available-for-sale investment securities	3,952	–
Realized gains on available-for-sale investment securities reclassified to the income statement	(5,165)	–
Revaluation of buildings	–	1,720
At 31 December 2014	(999)	35,095
Net unrealized gains on available-for-sale investment securities	2,539	–
Realized gains on available-for-sale investment securities reclassified to the income statement	(3,204)	–
Revaluation of buildings	–	(3,642)
At 31 December 2015	(1,664)	31,453

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)***19. Contingencies and loan commitments****Legal**

In the ordinary course of business, the Group 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 Group. 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 Group 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 Group's further actions to collect bad debt and/or realize respective repossession rights is higher than the amount collected and also when the Group 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 Group 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 Group did not obtain insurance coverage related to temporarily discontinued operations or the Group's obligations to third parties.

Commitments and contingencies

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

As at 31 December 2015, commitments and contingencies of the Group comprised off-balance credit-related commitments, in particular undrawn loan facilities and reimbursement obligations.

Off-balance credit-related commitments are presented in the table below as at 31 December 2015 and 31 December 2014.

	<u>2015</u>	<u>2014</u>
Undrawn loan facilities	52,376	69,296
Guarantees issued	4,556	–
Reimbursement obligations	6,796	–
Total off-balance commitments	<u>63,728</u>	<u>69,296</u>

20. Leases**Group as lessor**

The Group provides its investment property for operating leases. As at 31 December 2015, the Group's non-cancellable operating lease rentals amount to EUR 5,938 thousand (31 December 2014: EUR 4,742 thousand) and will be settled within 1 year.

*(Thousands of Euros)***21. Interest income and interest expense**

Net interest income comprises:

	<u>2015</u>	<u>2014</u>
Available-for-sale investment securities and held-to-maturity investment securities	8,109	5,813
Loans to customers	8,022	3,932
Long-term loans to banks	7,058	4,793
Deposits with banks and other financial institutions, including cash and cash equivalents	3,943	2,261
Interest income	<u>27,132</u>	<u>16,799</u>
Debt securities issued	(14,812)	(3,405)
Long-term loans of banks	(1,247)	(417)
Funds raised under repurchase agreements	(819)	(208)
Due to banks and other financial institutions	(609)	(601)
Current customer accounts	(257)	(146)
Interest expenses	<u>(17,744)</u>	<u>(4,777)</u>
Net interest income	<u>9,388</u>	<u>12,022</u>

In 2015, interest income accrued on impaired loans to customers amounted to EUR 185 thousand (2014: EUR 192 thousand).

22. General and administrative expenses

General and administrative expenses comprise:

	<u>2015</u>	<u>2014</u>
Employee compensations and employment taxes	11,471	11,405
IT-expenses, inventory and occupancy expenses	1,293	1,447
Depreciation of property and equipment (Note 13)	1,572	1,357
Expenses related to business travel, representative and accommodation expenses	1,277	1,309
Professional services	466	1,008
Other	829	405
General and administrative expenses	<u>16,908</u>	<u>16,931</u>

23. Risk management**Risk management framework**

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

The Group's risk management activities are intended to:

- ▶ Identify, analyze and manage risks faced by the Group.
- ▶ 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 global financial markets.

(Thousands of Euros)

23. Risk management (continued)

Risk management framework (continued)

Integrated into the whole vertical organizational structure of the Group and all areas of the Group's activities, the risk management system makes it possible to identify in a timely manner and effectively manage different types of risks.

Risk management involves all of the Group's divisions in evaluating, assuming, and controlling risks ("Three lines of defense"):

- ▶ Risk-taking (1st line of defense): the Group's divisions directly preparing and conducting transactions, involved in the identification, assessment, and monitoring of risks and comply with internal regulations on risk management, as well as give due consideration to the risk level in the preparation of transactions.
- ▶ Risk management (2nd line of defense): the division responsible for risk management develops risk management tools and methodology, assesses and monitors the risk level, prepares reports on risks, carries out risk aggregation, and calculates the amount of total capital requirements.
- ▶ Internal audit (3rd line of defense): independent quality assessment for existing risk management processes, identification of violations, and proposals for the improvement of the risk management system.

The Group's operations are managed taking into account the level of the risk appetite approved by the Council and integrated into a system of limits and restrictions insuring the acceptable level of risk for aggregated positions, transparent distribution of total risk limit between the activities of the Group.

The Bank's Council, the Board, the Finance Committee, the Credit Committee and the Risk Management Department are responsible for managing the Group'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 cooperation among all departments and committees of the Bank.

The Finance Committee determines the Bank's approaches to forming the optimal structure of the Bank's balance sheet, taking into account information of current and expected level of risks associated with assets and liabilities management within the established limits and other restrictions. It also ensures management and control over the credit risk, market risk, operational risk, reputational risk, legal risk and liquidity risk and reviews the limit-setting offers.

Risk management system

The Credit Committee manages the Bank's loan portfolio in accordance with its effective lending policy, aligns operation of the Bank's divisions in terms of the credit risk management and also reviews the offers for setting credit risk limits in respect of certain counterparties.

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 Group's performance.

During 2015 further development of the risk management system, started in 2013, was aimed at implementation of Basel standards and best practices of development banks within the Group:

- ▶ New methodological and regulatory documents relating to credit and operational risk management have been elaborated.
- ▶ The Group continued to implement the target model of the risk management system, based on requirements of the leading rating agencies.

(Thousands of Euros)

23. Risk management (continued)

Risk management system (continued)

In compliance with the existing procedures, twice a year the Group sets and reviews limits for counterparties for the purpose of performing financial transactions and assessing their creditworthiness. As part of the lending activity analysis, the Group continuously monitors the level of its loan assets risk. During the reporting period, the Bank sent its specialists to certain borrowers in order to monitor the implementation of the projects and identify potential primary evidence of impairment of loan assets.

To control and monitor the compliance with limits, the Group 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 and stop-loss limits. In addition, the Group's management receives regular reports on the status of risks within the Group.

Risk appetite

The risk appetite is the aggregate amount of risk taken by the Group to achieve its strategic goals and objectives. By approving the level of risk appetite, the Bank's Council determines the willingness to accept a risk or the amount of equity and liquidity that the Bank is willing to risk in the implementation of this strategy.

Risk appetite consists of 4 main components:

- ▶ The allocation of capital and liquidity (if necessary).
- ▶ Target allocation of capital across the main types of risk.
- ▶ The level of risk and target risk appetite in the context of the main performance indicators of the Group and significant risks for the Group.
- ▶ Determining levels of tolerance.

The procedure for determining the Group's risk appetite shall be defined by the Credit Risk Management Department and submitted for review by the Board and approval by the Council of the Bank.

The risk appetite shall be approved by the Council of the Bank on an annual basis for the next year and shall be a major factor of the Group's strategic limits determining the thresholds for the Group's key performance indicators and the Group's significant risks.

In determining the risk appetite, the Group assesses whether the specified risk appetite is acceptable in the current time period and whether it will be acceptable in the future, taking into account:

- ▶ Expectations of the founders concerning the level of profitability.
- ▶ International regulatory standards.
- ▶ Current and expected future volume of transactions.
- ▶ Current and expected future structure of significant risks.
- ▶ Current and expected future level of aggregate capital.

Based on the risk appetite determined by the Council, the Board annually approves the Group's limits, sublimits, and risk indicators, which should not exceed the target values of the risk appetite.

Risk identification

The Group identifies and manages both external and internal risk factors throughout its organizational structure. As a result of regular analysis of the Group's exposure to different types of risks performed by the Risk Management Department, the Group 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 the Finance Committee and, if necessary, also communicated to the Management Board along with the recommendations on possible risk mitigation measures.

(Thousands of Euros)

23. Risk management (continued)

Risk assessment, management and control

The Group's risk exposure is primarily reduced by means of collective decision making. Strict allocation of responsibilities between departments and officers of the Group, 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, if necessary, updated by the Group in order to reflect changed market conditions and improve the risk management methodology.

The risk monitoring system comprises:

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

The Group 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 Group will incur a loss because its counterparty fails to discharge its contractual financial obligations to the Group, 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 Group considers and consolidates all elements of credit risk exposures such as consolidated borrower or counterparty default risk.

System of credit risk management

The Group'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 establishes the limits per borrower/group of related borrowers. The Credit Committee structures the transaction to minimize credit risk. The Loan Operations Analysis Department is responsible for ongoing control over the quality of the Group's loan portfolio.

Upon preparation of a transaction by the initiating unit it is reviewed by the Credit Committee, and then it is approved by the Board. The Board is responsible for all direct credit risk exposures in the amount of up to 15% of the counterparty'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 Customer Relations Department. In case of a positive decision, the set of documents from the Loan Operations Analysis Department required for reviewing the loan/credit application shall be analyzed by the Legal Department, Risk Management Department, Security Department, Strategic Development 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, Security 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 Credit Department's Description of the Investment Transaction, report of the Security Department and Strategic Development 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)

23. 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 by industry.

To mitigate credit risk, the Group 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 Group 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 Group. 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 Group 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 Group applies the following types of collateral for recovery of loans and fulfillment of obligations:

- ▶ Pledge of equipment and goods in turnover;
- ▶ Pledge of real estate (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 Group assumes that the fair value of the collateral is its value estimate recognized by the Group 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 Group's internal expert estimate, or carrying amount of the collateral including adjustment coefficient (discount). Where the market value of the collateral is assessed as impaired, the borrowers 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 collateral is analyzed in Notes 10 and 11.

Maximum exposure to credit risk

The maximum exposure to credit risk for the components of the consolidated 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 the financial instruments are recorded at fair value, their carrying amount represents the current credit risk exposure but not the maximum credit 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 19).

(Thousands of Euros)

23. 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 consolidated 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 customer'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 2015 and 31 December 2014, there was no evidence of impairment of long-term loans to banks and all such loans were classified as standard. 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 2015 and 31 December 2014:

2015	Loan amount	Impairment	Loan amount, including impairment	Impairment to loan amount ratio, %
Long-term loans to banks without any signs of impairment identified				
Standard loans				
- Russian Federation	64,223	–	64,223	–
- Mongolia	43,044	–	43,044	–
- Socialist Republic of Vietnam	33,330	–	33,330	–
	140,597	–	140,597	–
Loans to customers without any signs of impairment identified				
Standard loans				
- Republic of Bulgaria	51,162	–	51,162	–
- Russian Federation	28,160	–	28,160	–
- Romania	25,844	–	25,844	–
- Mongolia	21,890	–	21,890	–
- Slovak Republic	15,334	–	15,334	–
- Other	18,249	–	18,249	–
Uncollectible loans				
- Slovak Republic	8,103	(3,000)	5,103	37
- Republic of Bulgaria	6,755	(6,755)	–	100
	175,497	(9,755)	165,742	5.6
Total loans	316,094	(9,755)	306,339	3.1

(Thousands of Euros)

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

2014	Loan amount	Impairment	Loan amount, including impairment	Impairment to loan amount ratio, %
Long-term loans to banks without any signs of impairment identified				
Standard loans				
- Russian Federation	89,874	–	89,874	–
- Mongolia	26,986	–	26,986	–
- Socialist Republic of Vietnam	15,172	–	15,172	–
	132,032	–	132,032	–
Loans to customers without any signs of impairment identified				
Standard loans				
- Slovak Republic	40,238	–	40,238	–
- Republic of Bulgaria	31,094	–	31,094	–
- Mongolia	23,822	–	23,822	–
- Romania	5,958	–	5,958	–
- Russian Federation	2,646	–	2,646	–
Uncollectible loans				
- Slovak Republic	8,107	(3,589)	4,518	44
	111,865	(3,589)	108,276	3
Total loans	243,897	(3,589)	240,308	–

Where possible, the Group 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 Group creates allowance for impairment of loans that represents its estimate of losses incurred in its loan portfolio. The Group writes off a loan balance against related allowances for impairment of loans 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 borrower'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 Group determines the allowances appropriate for each individually significant loan on an individual basis. Due to a limited number of borrowers, the Group 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 dividend 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, or more frequently, unless unforeseen circumstances require more careful attention.

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

*(Thousands of Euros)***23. Risk management (continued)****Liquidity risk**

Liquidity risk is the risk of loss resulting from the Group'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 Group'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 Group) and/or an unforeseen need of immediate and simultaneous discharge of its financial obligations.

Liquidity management is an integral part of general policy for the Group's assets and liabilities management (ALM) and operates within the established limits and restrictions related to management of risks (liquidity, interest rate and currency risk) and the Group's balance sheet items, and in accordance with the documents of strategic, tactic and operating planning.

Procedures for the Group's liquidity position management, ensuring the Group's ability to meet its obligations in full and on a timely basis and efficient resources management, are stipulated in the *Regulations for IIB's Liquidity Position Management* that enables the development of the liquidity position management function provided for by the *IIB's Assets and Liabilities Management Policy*, as an integral part of general function of the Group's management.

Decision making matrix related to liquidity management includes a strategic level of liquidity management (the Council), tactic level (the Board and special-purpose committees) and operational level (responsible structural divisions). In 2014, the Group updated its approaches to the assets and liabilities management. Starting from 2015, Department for Analytical Support of Treasury Operations (DASKO or ALM Unit) became responsible for organizing and aligning management of the Group's liquidity position. The Group manages its liquidity position in accordance with planning horizons (up to 6 months) and possible scenarios of movements in liquidity position (stable, stressed).

Main instrument of liquidity position management under the stable scenario is a Plan of cash flows defining the cash flow by balance sheet products/instruments and taking into account the plan of future financial operations. The Bank determines the balance sheet gaps, payment schedule and need in financing of future operations based on the Plan of cash flows. As a result of application of these instruments, DASKO issues appropriate recommendations to responsible structural divisions.

The Group has implemented a liquidity buffer to manage the Group's liquidity under the stressed scenario. Application of the liquidity buffer enables the Group to promptly monitor the sustainability and stability of the Group's balance sheet structure in case of liquidity shortage that is critical to the Group's solvency.

The liquidity buffer is formed primarily by liquidity reverses, namely securities recognized on the Group's balance sheet and included in the Lombard lists of the European Central Bank and Bank of Russia. The Group calculates its liquidity reserves as at the reporting date and for the next six monthly reporting dates (forecast). Liquidity buffer may be used to close the negative net position. As at 31 December 2015, the liquidity buffer amounts to EUR 65.1 mln (31 December 2014: EUR 64.6 mln).

The table below shows the contractual expiry by maturity of the Group'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.

	<u>2015</u>	<u>2014</u>
Less than 1 month	52,376	69,296
1 to 3 months	178	–
3 months to 1 year	7,254	–
1 to 5 years	3,920	–
Off-balance credit-related commitments	<u>63,728</u>	<u>69,296</u>

(Thousands of Euros)

23. 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: Quoted available-for-sale debt securities were included in "Less than 1 month" category as they are highly liquid investment securities, which the Group may sell in the short-term on the arm-length basis. Available-for-sale investment securities pledged under repurchase agreements are presented on the basis of periods from the reporting date to the expiry date of respective contractual obligations of the Group.

	2015							2014								
	<i>Less than 1 month</i>	<i>1 to 3 months</i>	<i>3 months to 1 year</i>	<i>1 to 5 years</i>	<i>Over 5 years</i>	<i>No stated maturity</i>	<i>Past due</i>	<i>Total</i>	<i>Less than 1 month</i>	<i>1 to 3 months</i>	<i>3 months to 1 year</i>	<i>1 to 5 years</i>	<i>Over 5 years</i>	<i>No stated maturity</i>	<i>Past due</i>	<i>Total</i>
Assets																
Cash and cash equivalents	59,519	–	–	–	–	–	–	59,519	65,918	–	–	–	–	–	–	65,918
Deposits with banks and other financial institutions	15,352	15,627	54,346	15,067	–	–	–	100,392	8,327	20,347	5,697	–	–	–	–	34,371
Financial assets at fair value through profit or loss	69	–	1,775	–	–	–	–	1,844	311	–	–	–	–	–	–	311
Available-for-sale investment securities	93,027	230	65	22,733	11,948	4	–	116,059	42	7,669	750	13,599	16,813	3	–	38,876
Held-to-maturity investment securities	64	972	2,981	76,728	30,535	–	–	123,228	70	942	1,146	39,791	81,685	–	–	123,634
Long-term loans to banks	–	3,160	41,112	76,374	19,951	–	–	140,597	–	1,531	13,139	117,362	–	–	–	132,032
Loans to customers	982	1,872	26,573	85,268	45,944	–	5,103	165,742	–	901	24,168	53,763	24,926	–	4,518	108,276
Other assets	69	81	473	–	–	–	–	623	58	75	994	10	–	–	–	1,137
Total assets	169,082	21,942	127,325	276,170	108,378	4	5,103	708,004	74,726	31,465	45,894	224,525	123,424	3	4,518	504,555
Liabilities																
Due to banks and other financial institutions	(28,421)	–	(20,196)	(64,756)	–	–	–	(113,373)	(45,436)	(13,233)	–	–	–	–	–	(58,669)
Current customer accounts	(7,430)	–	–	–	–	–	–	(7,430)	(4,788)	–	–	–	–	–	–	(4,788)
Financial liabilities at fair value through profit or loss	–	–	(16,191)	(13,707)	–	–	–	(29,898)	–	–	(21,705)	–	–	–	–	(21,705)
Long-term loans of banks	(102)	–	(24,529)	(19,556)	–	–	–	(44,187)	(97)	–	–	(20,443)	–	–	–	(20,540)
Debt securities issued	–	–	(40,111)	(172,613)	–	–	–	(212,724)	–	–	(82,884)	(29,875)	–	–	–	(112,759)
Other liabilities	(475)	(1,103)	(2,460)	–	–	–	–	(4,038)	(1,356)	(49)	(2,251)	–	–	–	–	(3,656)
Total liabilities	(36,428)	(1,103)	(103,487)	(270,632)	–	–	–	(411,650)	(51,677)	(13,282)	(106,840)	(50,318)	–	–	–	(222,117)
Net position	132,653	20,839	23,838	5,538	108,378	4	5,103	296,354	23,049	18,183	(60,946)	174,207	123,424	3	4,518	282,438
Accumulated net position	132,653	153,493	177,331	182,869	291,247	291,251	296,354		23,049	41,232	(19,714)	154,493	277,917	277,920	282,438	

*(Thousands of Euros)***23. Risk management (continued)****Analysis of financial liabilities by remaining contractual maturities**

The table below summarizes the maturity profile of the Group's financial liabilities at 31 December 2015 and 31 December 2014 based on contractual undiscounted repayment obligations except for gross settled derivatives which are shown by contractual maturity. Debt securities with put options (offers) are presented as if investors will exercise their options at the earliest possible date. The Group expects that it will have to make payment on current bond offers.

<i>As at 31 December 2015</i>	<i>Less than 1 month</i>	<i>1 to 3 months</i>	<i>3 to 12 months</i>	<i>1 to 5 years</i>	<i>Total</i>
Financial liabilities					
Due to banks and other financial institutions	–	28,443	20,293	69,386	118,122
Current customer accounts	–	7,430	–	–	7,430
Net settled derivative liabilities	(69)	–	–	–	(69)
Gross settled derivative financial instruments					
- Contractual amounts payable	–	–	118,408	160,641	279,049
- Contractual amounts receivable	–	–	(117,884)	(151,321)	(269,205)
Long-term loans of banks	–	–	23,473	22,303	45,776
Debt securities issued	–	–	50,936	201,220	252,156
Other liabilities	475	1,103	2,460	–	4,038
Total undiscounted financial liabilities	406	36,976	97,686	302,229	437,297
<i>As at 31 December 2014</i>	<i>Less than 1 month</i>	<i>1 to 3 months</i>	<i>3 to 12 months</i>	<i>1 to 5 years</i>	<i>Total</i>
Financial liabilities					
Due to banks and other financial institutions	–	58,746	–	–	58,746
Current customer accounts	–	4,788	–	–	4,788
Net settled derivative liabilities	(310)	–	–	–	(310)
Gross settled derivative financial instruments					
- Contractual amounts payable	–	–	132,244	–	132,244
- Contractual amounts receivable	–	–	(113,142)	–	(113,142)
Long-term loans of banks	–	–	284	21,019	21,303
Debt securities issued	–	–	87,926	35,072	122,998
Other liabilities	1,356	518	2,493	–	4,367
Total undiscounted financial liabilities	1,046	63,583	109,563	56,091	230,283

Market risk

Market risk is the risk that the Group may 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 Group 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.

The Finance Committee coordinates the Group's market risk management policy and reviews and provides recommendations on management of market risks to the Management Board.

The Treasury Department performs strategic 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 Group'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 Group'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.

*(Thousands of Euros)***23. Risk management (continued)****Market risk (continued)**

The Group applies a VaR methodology to assess currency and equity risks. VaR is a method used in measuring maximum risk of the Group, 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 Group assumes 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 Group is carried out in major currencies and financial instruments of the Group attributable to a securities portfolio.

At estimating value at risk, the Group 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 Group 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 Group 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 2015 and 31 December 2014, final data on value at risk assessment (VaR) in relation to currency and price risks assumed by the Group are represented as follows:

	<u>2015</u>	<u>2014</u>
Fixed income securities price risk	1,536	364
Currency risk	126	945

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.
- ▶ 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 Group'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)***23. Risk management (continued)****Market risk (continued)**

The Group's exposure to currency risk as at 31 December 2015 and 31 December 2014 is presented below:

	2015					2014				
	EUR	USD	RUB	Other currencies	Total	EUR	USD	RUB	Other currencies	Total
Assets										
Cash and cash equivalents	37,363	20,147	1,907	102	59,519	33,801	31,655	360	102	65,918
Deposits with banks and other financial institutions	99,990	–	402	–	100,392	32,895	1,044	432	–	34,371
Available-for-sale investment securities	89,426	26,633	–	–	116,059	32,355	6,521	–	–	38,876
Held-to-maturity investment securities	55,416	63,636	4,176	–	123,228	55,566	63,561	4,507	–	123,634
Long-term loans to banks	106,063	34,534	–	–	140,597	110,815	21,217	–	–	132,032
Loans to customers	124,751	40,991	–	–	165,742	108,276	–	–	–	108,276
Other assets	12	–	171	440	623	111	2	1,024	–	1,137
	513,021	185,941	6,656	542	706,160	373,819	124,000	6,323	102	504,244
Liabilities										
Due to banks and other financial institutions	(52,785)	(59,706)	(882)	–	(113,373)	(16,804)	(41,181)	(684)	–	(58,669)
Current customer accounts	(7,220)	(210)	–	–	(7,430)	(4,605)	(183)	–	–	(4,788)
Long-term loans of banks	(7,494)	(36,693)	–	–	(44,187)	–	(20,540)	–	–	(20,540)
Debt securities issued	(30,030)	–	(158,099)	(24,595)	(212,724)	(30,079)	–	(82,680)	–	(112,759)
Other liabilities	(3,103)	(51)	(852)	(32)	(4,038)	(2,879)	(74)	(703)	–	(3,656)
	(100,632)	(96,660)	(159,833)	(24,627)	(381,752)	(54,367)	(61,978)	(84,067)	–	(200,412)
Net balance sheet position	412,389	89,281	(153,177)	(24,085)	324,408	319,452	62,022	(77,744)	102	303,832
Derivative financial instruments										
Claims	61,068	–	156,879	24,108	242,055	33,310	–	76,915	–	110,225
Liabilities	(210,884)	(59,225)	–	–	(270,109)	(97,564)	(34,056)	–	–	(131,620)
Net balance sheet position including derivative financial instruments	262,573	30,056	3,702	23	296,354	255,198	27,966	(829)	102	282,437

*(Thousands of Euros)***23. Risk management (continued)****Market risk (continued)*****Interest rate risk***

The Group 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 fluctuations but may also reduce or create losses in the event that unexpected movements arise.

Analysis of the Group's equity sensitivity to changes in interest rates (based on simplified scenario of the 100 basis points (bp) parallel shifts (up and down) in yield curves and positions of available-for-sale debt securities as at 31 December 2015 and 31 December 2014) is as follows:

	<u>2015</u>	<u>2014</u>
	<i>The Group's equity</i>	<i>The Group's equity</i>
100 bp parallel shift up	(6,758)	(1,387)
100 bp parallel shift down	6,758	1,387

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 Group'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 Group continuously seeks to enhance its business processes, operating structure and personnel incentives system in order to minimize the impact of operational risk.

24. 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 Group 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 Group 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)***24. Fair values of financial instruments (continued)****Fair value hierarchy (continued)**

For the purpose of fair value disclosures, the Group 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 2015</i>	<i>Level 2 2015</i>	<i>Level 3 2015</i>	<i>Total 2015</i>
Assets measured at fair value					
Derivative financial assets	31 December 2015	–	1,844	–	1,844
Government bonds of member countries and bonds of regional governments	31 December 2015	114,673	–	–	114,673
Corporate bonds	31 December 2015	1,382	–	–	1,382
Quoted equity instruments	31 December 2015	–	4	–	4
Investment property	31 December 2015	–	–	33,819	33,819
Property and equipment - buildings	31 December 2015	–	–	62,807	62,807
Liabilities measured at fair value					
Derivative financial liabilities	31 December 2015	–	29,898	–	29,898
Assets for which fair values are disclosed					
Cash and cash equivalents	31 December 2015	–	–	59,519	59,519
Deposits with banks and other financial institutions	31 December 2015	–	–	100,392	100,392
Held-to-maturity investment securities	31 December 2015	114,876	–	–	114,876
Long-term loans to banks	31 December 2015	–	–	139,891	139,891
Loans to customers	31 December 2015	–	–	165,742	165,742
Liabilities for which fair values are disclosed					
Due to banks and other financial institutions	31 December 2015	–	–	113,373	113,373
Current customer accounts	31 December 2015	–	–	7,430	7,430
Long-term loans of banks	31 December 2015	–	–	44,187	44,187
Debt securities issued	31 December 2015	–	214,734	–	214,734

The following table shows an analysis of financial instruments recorded at fair value by level of the fair value hierarchy as at 31 December 2014:

	<i>Valuation date</i>	<i>Level 1 2014</i>	<i>Level 2 2014</i>	<i>Level 3 2014</i>	<i>Total 2014</i>
Assets measured at fair value					
Derivative financial assets	31 December 2014	–	311	–	311
Government bonds of member countries and bonds of regional governments	31 December 2014	28,500	–	–	28,500
Corporate bonds	31 December 2014	10,373	–	–	10,373
Quoted equity instruments	31 December 2014	–	3	–	3
Investment property	31 December 2014	–	–	52,879	52,879
Property and equipment - buildings	31 December 2014	–	–	50,739	50,739
Liabilities measured at fair value					
Derivative financial liabilities	31 December 2014	–	21,705	–	21,705
Assets for which fair values are disclosed					
Cash and cash equivalents	31 December 2014	–	–	65,918	65,918
Deposits with banks and other financial institutions	31 December 2014	–	–	34,371	34,371
Held-to-maturity investment securities	31 December 2014	99,872	–	–	99,872
Long-term loans to banks	31 December 2014	–	–	126,485	126,485
Loans to customers	31 December 2014	–	–	108,276	108,276
Liabilities for which fair values are disclosed					
Due to banks and other financial institutions	31 December 2014	–	–	58,669	58,669
Current customer accounts	31 December 2014	–	–	4,788	4,788
Long-term loans of banks	31 December 2014	–	–	20,540	20,540
Debt securities issued	31 December 2014	–	106,351	–	106,351

*(Thousands of Euros)***24. Fair values of financial instruments (continued)****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 Group's financial instruments that are carried in the consolidated financial statements. The table does not include the fair values of non-financial assets and non-financial liabilities.

	<i>Carrying amount 2015</i>	<i>Fair value 2015</i>	<i>Unrecognized gain/(loss) 2015</i>	<i>Carrying amount 2014</i>	<i>Fair value 2014</i>	<i>Unrecognized gain/(loss) 2014</i>
Financial assets						
Cash and cash equivalents	59,519	59,519	–	65,918	65,918	–
Deposits with banks and other financial institutions	100,392	100,392	–	34,371	34,371	–
Held-to-maturity investment securities	123,228	114,876	(8,352)	123,634	99,872	(23,762)
Long-term loans to banks	140,957	139,891	(706)	132,032	126,485	(5,547)
Loans to customers	165,742	165,742	–	108,276	108,276	–
Financial liabilities						
Due to banks and other financial institutions	113,373	113,373	–	58,669	58,669	–
Current customer accounts	7,430	7,430	–	4,788	4,788	–
Long-term loans of banks	44,187	44,187	–	20,540	20,540	–
Debt securities issued	212,724	214,734	(2,010)	112,759	106,351	6,408
Total unrecognized change in unrealized fair value			(11,068)			(22,901)

Fair value measurements

The Group determines the policies and procedures for both recurring fair value measurement, such as unquoted derivatives, investment property, and buildings, and for non-recurring measurement, such as inventories.

External appraisers are involved for valuation of significant assets, such as building and property. Involvement of external appraisers is decided upon by the Bank's Finance Department. Unquoted derivatives are measured by the Finance Department.

Selection criteria include market knowledge, reputation, independence and whether professional standards are maintained.

In the course of audit procedures, the Bank's Finance Department presents the valuation results to the Group's independent auditors upon requests. This includes a discussion of the major assumptions used in the valuations.

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 have 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 2015 and 31 December 2014 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 existing practice of renegotiating interest rates to reflect current market conditions, and, therefore, a majority of balances carry interest at rates approximating market interest rates.

*(Thousands of Euros)***24. Fair values of financial instruments (continued)****Methodologies and assumptions (continued)*****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 for similar financial instruments.

The estimated fair value of fixed rate 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 2015 and 31 December 2014 the fair value of loans to customers and long-term loans of banks was not significantly different from their respective carrying amount.

Investment property

The Group engages an independent appraiser for the investment property fair value measurement. As at the valuation date (31 December 2015), the fair values of investment property were based on the results of valuation performed by an accredited independent appraiser and the prices of market transactions using the market, cost and income approaches to fair value measurement.

The duration of the cash flows and the specific timing of inflows and outflows are determined by events such as rent reviews, lease renewal and related re-letting, redevelopment, or refurbishment. The appropriate duration is typically driven by market behavior that is a characteristic of the class of real property. Periodic cash flow is typically estimated as gross income less expenses related to vacant premises, non-recoverable expenses, collection losses, lease incentives, maintenance costs, agent and commission costs, and other operating and management expenses. The series of periodic net operating income, along with an estimate of the terminal value anticipated at the end of the projection period, is then discounted.

Property and equipment – buildings

Fair value of the properties was determined by using the market approach. This means that valuations performed by the appraiser are based on market transaction prices, significantly adjusted for difference in the nature, location or condition of the specific property. As at the valuation date (31 December 2015), the properties' fair values are based on valuations performed by an accredited independent appraiser and the prices of market transactions using the market, cost and income approaches to fair value measurement.

Significant unobservable inputs used in determining the fair value of real estate properties

As at the valuation date (31 December 2015), the significant unobservable inputs used in determining the fair value of real estate properties included the average asking prices for sale of similar properties ranging from EUR 2,899 per sq. m (range minimum) to EUR 4,023 per sq. m (range maximum), and lease rates ranging from EUR 365 per sq. m a year (minimum) to EUR 486 per sq. m a year (maximum).

There were no transfers of financial instruments between level 2 and level 1 in 2015 and 2014.

Movements in level 3 assets and liabilities at fair value

The following tables show a reconciliation of the opening and closing amount of Level 3 assets and liabilities which are recorded at fair value:

	<i>At 1 January 2015</i>	<i>Total gain/ (loss) recorded in profit or loss</i>	<i>Total gains/ (losses) recorded in other comprehensive income</i>	<i>Purchases</i>	<i>Transfer in property and equipment</i>	<i>At 31 December 2015</i>
Assets						
Property and equipment – buildings	50,739	(935)	(3,642)	52	16,593	62,807
Investment property	52,879	(2,500)	–	33	(16,593)	33,819
Total	103,618	(3,435)	(3,642)	85	–	96,626

(Thousands of Euros)

24. Fair values of financial instruments (continued)**Movements in level 3 assets and liabilities at fair value (continued)**

	<i>At 1 January 2014</i>	<i>Total gain/ (loss) recorded in profit or loss</i>	<i>Total gains/ (losses) recorded in other comprehensive income</i>	<i>Purchases</i>	<i>Transfer in property and equipment</i>	<i>At 31 December 2014</i>
Assets						
Property and equipment – buildings	48,641	(783)	1,720	149	1,012	50,739
Investment property	53,480	257	–	154	(1,012)	52,879
Total	102,121	(526)	1,720	303	–	103,618

25. Transferred financial assets that are not derecognized

The table below provides a summary of the financial assets transferred by the Group under repurchase agreements in such a way that all the transferred financial assets do not qualify for derecognition:

<i>Transferred financial asset</i>	<i>Available-for-sale investment securities</i>		<i>Held-to-maturity investment securities</i>		<i>Total 2015</i>
	<i>Government bonds of member countries</i>	<i>Corporate bonds</i>	<i>Government bonds of member countries</i>	<i>Corporate bonds</i>	
	<i>2015</i>	<i>2015</i>	<i>2015</i>	<i>2015</i>	
Carrying amount of assets	21,646	1,382	10,489	62,705	96,222
Carrying amount of associated liabilities	(16,350)	(930)	(6,998)	(40,478)	(64,756)
Net position	5,296	452	3,491	22,227	31,466

<i>Transferred financial asset</i>	<i>Available-for-sale investment securities</i>		<i>Held-to-maturity investment securities</i>		<i>Total 2014</i>
	<i>Government bonds of member countries</i>	<i>Corporate bonds</i>	<i>Government bonds of member countries</i>	<i>Corporate bonds</i>	
	<i>2014</i>	<i>2014</i>	<i>2014</i>	<i>2014</i>	
Carrying amount of assets	13,903	–	–	42,634	56,537
Carrying amount of associated liabilities	(12,488)	–	–	(28,832)	(41,320)
Net position	1,415	–	–	13,802	15,217

Securities sold under repurchase agreements are transferred to a third party and the Group receives cash in exchange. If the securities increase or decrease in value, the Group may, in certain circumstances, require, or be required, to pay additional collateral in the form of cash and/or other securities. The Group has determined that it retains substantially all the risks and rewards of these securities, which include credit risk, market risk, country risk and operational risk, and therefore has not derecognized them. In addition, it recognizes a financial liability for cash received.

The fair value of investment securities available for sale sold under repurchase agreements is equal to their carrying amount. The fair value of bonds classified as investments securities held to maturity and sold under repurchase agreements is disclosed in respective Notes (Note 24).

The related liabilities, which are recorded against the cash received for such transactions, are presented in amounts due to banks and other financial institutions in the consolidated statement of financial position as at 31 December 2015 (as at 31 December 2014: in amounts due to banks and other financial institutions).

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

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

Credit investment activity	Investment banking services, including long-term corporate and interbank financing
Treasury	Operations in financial markets, transactions with securities, derivative financial instruments and foreign currency, and liquidity management
Other operations	Operational leasing services, other operations

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 consolidated financial statements. The following table presents income, profit, assets and liabilities of the Group's operating segments:

2015	<i>Credit investment activity</i>	<i>Treasury</i>	<i>Other operations</i>	<i>Total</i>
Income				
<i>External customers</i>				
Interest income	15,080	11,904	148	27,132
Net gains from available-for-sale investment securities	–	3,204	–	3,204
Net gains from held-to-maturity investment securities	–	45	–	45
Income from lease of investment property	–	–	5,214	5,214
Recovery of provision	–	–	89	89
Other segment income	460	–	79	539
Total income	15,540	15,153	5,530	36,223
Interest expenses	(7,260)	(10,484)	–	(17,744)
Net losses from trading in foreign currencies	–	(5,302)	(25)	(5,327)
Allowance for impairment of loans	(6,166)	–	–	(6,166)
Net gains from revaluation of investment property	–	–	(2,500)	(2,500)
Other segment expenses	–	(114)	(1,344)	(1,458)
Segment results	2,114	(747)	1,661	3,028
Other unallocated income				15,936
Other unallocated expenses				(16,908)
Profit for the year				2,056
Segment assets	306,339	400,201	102,863	809,403
Segment liabilities	116,138	291,474	4,088	411,700
Other segment information				
Capital expenditures	–	–	85	85

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(Thousands of Euros)

26. Segment information (continued)

<i>2014</i>	<i>Credit investment activity</i>	<i>Treasury</i>	<i>Other operations</i>	<i>Total</i>
Income				
<i>External customers</i>				
Interest income	8,725	7,966	108	16,799
Net gains from trading in foreign currencies	–	3,426	–	3,426
Net gains from available-for-sale investment securities	–	5,165	–	5,165
Income from lease of investment property	–	–	8,116	8,116
Recovery of provision	–	–	17	17
Net gains from revaluation of investment property	–	–	257	257
Revenue from sales of inventories	–	–	3,569	3,569
Other segment income	42	–	280	322
Total income	8,767	16,557	12,347	37,671
Interest expenses	(1,622)	(3,155)	–	(4,777)
Allowance for impairment of loans	(3,589)	–	–	(3,589)
Losses from impairment of investments in subsidiary	–	–	(4,305)	(4,305)
Other segment expenses	(47)	(640)	(5,120)	(5,807)
Segment results	3,509	12,762	2,922	19,193
Other unallocated income				1,976
Other unallocated expenses				(16,931)
Profit for the year				4,238
Segment assets	240,308	262,399	108,825	611,532
Segment liabilities	56,569	161,892	3,656	222,117
Other segment information				
Capital expenditures	–	–	303	303

In 2015 and 2014, the Group's revenue from lease operations with one external counterparty exceeded 20% of the Group's total revenue (2015: EUR 3,196 thousand; 2014: EUR 5,718 thousand).

Geographical information

Allocation of the Group's revenue from transactions with external customers and non-current assets based on the location of these customers and assets for the years ended 31 December 2015 and 31 December 2014 is presented in the table below:

	<i>2015</i>				<i>2014</i>			
	<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	12,147	11,721	3,264	27,132	7,987	8,096	716	16,799
Income from lease of investment property	5,214	–	–	5,214	8,116	–	–	8,116
Revenue from sales of inventories					3,569	–	–	3,569
Non-current assets	100,212	–	–	100,212	106,086	–	–	106,086

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

(Thousands of Euros)

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

The geographical concentration of the Group's assets and liabilities based on the location of the Group's counterparties as at 31 December 2015 is presented below:

	<i>2015</i>									
	<i>Russian Federation</i>	<i>Republic of Bulgaria</i>	<i>Romania</i>	<i>Slovak Republic</i>	<i>Hungary</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	2,026	219	17	15	–	–	–	–	57,242	59,519
Deposits with banks and other financial institutions	6,049	–	–	–	–	30,539	–	–	63,804	100,392
Financial instruments at fair value through profit or loss	669	–	–	–	–	–	–	–	1,175	1,844
Investment securities:										
- available-for-sale	–	26,889	31,150	13,208	12,056	13,746	11,506	6,118	1,386	116,059
- held-to-maturity	105,785	–	–	–	–	–	–	–	17,443	123,228
Long-term loans to banks less allowances for impairment	64,223	–	–	–	–	43,044	33,330	–	–	140,597
Loans to customers less allowances for impairment	28,160	51,162	25,844	20,437	–	21,890	–	–	18,249	165,742
Assets	206,912	78,270	57,011	33,660	12,056	109,219	44,836	6,118	159,299	707,381
Liabilities										
Due to banks and other financial institutions	992	–	–	7,508	–	–	–	20,086	84,787	113,373
Financial instruments at fair value through profit or loss	18,723	–	864	–	–	–	–	–	10,311	29,898
Long-term loans of banks	22,953	13,740	–	7,494	–	–	–	–	–	44,187
Long-term securities issued	158,067	–	24,557	30,100	–	–	–	–	–	212,724
Liabilities	200,735	13,740	25,421	45,102	–	–	–	20,086	95,098	400,182

(Thousands of Euros)

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

	<i>2014</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	23,698	–	–	8,241	–	–	–	16,464	17,515	65,918
Deposits with banks and other financial institutions	432	–	–	–	–	30,460	–	–	3,479	34,371
Financial instruments at fair value through profit or loss	311	–	–	–	–	–	–	–	–	311
Investment securities:										
- available-for-sale	10,381	14,642	2,584	1,177	–	1,948	1,702	3,567	2,875	38,876
- held-to-maturity	106,097	–	–	–	–	–	–	–	17,537	123,634
Long-term loans to banks less allowances for impairment	89,874	–	–	–	–	26,986	15,172	–	–	132,032
Loans to customers less allowances for impairment	2,646	31,094	5,958	44,756	–	23,822	–	–	–	108,276
Assets	233,439	45,736	8,542	54,174	–	83,216	16,874	20,031	41,406	503,418
Liabilities										
Due to banks and other financial institutions	–	29,837	–	–	–	–	–	–	28,832	58,669
Financial instruments at fair value through profit or loss	21,143	–	–	–	–	–	–	–	562	21,705
Long-term loans of banks	20,540	–	–	–	–	–	–	–	–	20,540
Long-term securities issued	82,679	–	–	30,080	–	–	–	–	–	112,759
Liabilities	124,362	29,837	–	30,080	–	–	–	–	29,394	213,673

Other countries include members of the Organization for Economic Co-operation and Development (OECD).

(Thousands of Euros)

27. Offsetting of financial instruments

The table below shows the effect of enforceable master netting agreements and similar arrangements that do not result in an offset in the consolidated statement of financial position as at 31 December 2015:

	<i>Gross amount of recognized financial assets</i>	<i>Gross amount of recognized financial liabilities set off in the statement of financial position</i>	<i>Net amount of financial assets presented in the statement of financial position</i>	<i>Related amounts not set off in the statement of financial position</i>		<i>Net amount</i>
				<i>Financial instruments</i>	<i>Cash collateral received</i>	
2015						
Financial assets						
Financial assets pledged under repurchase agreements	96,222	–	96,222	(64,756)	–	31,466
Total	96,222	–	96,222	(64,756)	–	31,466
Financial liabilities						
Repurchase agreements with banks	64,756	–	64,756	(64,756)	–	–
Total	64,756	–	64,756	(64,756)	–	–

The table below shows financial assets offset against financial liabilities in the consolidated statement of financial position as at 31 December 2014 as well as the effect of enforceable master netting agreements and similar arrangements that do not result in an offset in the consolidated statement of financial position:

	<i>Gross amount of recognized financial assets</i>	<i>Gross amount of recognized financial liabilities set off in the statement of financial position</i>	<i>Net amount of financial assets presented in the statement of financial position</i>	<i>Related amounts not set off in the statement of financial position</i>		<i>Net amount</i>
				<i>Financial instruments</i>	<i>Cash collateral received</i>	
2014						
Financial assets						
Financial assets pledged under repurchase agreements	56,537	–	56,537	(41,320)	–	15,217
Total	56,537	–	56,537	(41,320)	–	15,217
Financial liabilities						
Repurchase agreements with banks	41,320	–	41,320	(41,320)	–	–
Total	41,320	–	41,320	(41,320)	–	–

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.

(Thousands of Euros)

28. Related party disclosures (continued)

The volumes of related party transactions, outstanding balances at the year end, and related expenses and income for 2015 and 2014 are as follows:

	<i>Related party</i>	<i>31 December 2015</i>		<i>31 December 2014</i>	
		<i>Carrying amount</i>	<i>Average interest rate, %</i>	<i>Carrying amount</i>	<i>Average interest rate, %</i>
Consolidated statement of financial position					
Current customer accounts	Key management personnel	493	–	369	–
Consolidated income statement					
	<i>Related party</i>	<i>2015</i>		<i>2014</i>	
		<i>Income/ (expense)</i>		<i>Income/ (expense)</i>	
Interest expenses on current customer accounts	Key management personnel	(95)		(42)	
Employee benefits	Key management personnel	(1,524)		(1,451)	
Compensation for travel expenses and medical insurance	Key management personnel	(89)		(71)	
		(1,708)		(1,564)	

29. Capital adequacy

Capital adequacy ratio is the most important financial indicator characterizing credibility of 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 Supervision recommends maintaining the ratio of capital to risk-weighted assets ("capital adequacy ratio") above the prescribed minimum level. As at 31 December 2015, this minimum level was 8% (2014: 8%).

Besides, taking into account the Bank's status as the multilateral development institution as well as the structure of the Bank's member countries and the respective decision of the Council, the capital adequacy ratio was set for the Bank at the level of not less than 25% as at 31 December 2015 (2014: 25%).

The following table shows the composition of the Group's capital position computed in accordance with the Basel Accord (Basel II) as at 31 December 2015 and 31 December 2014.

	<i>2015</i>	<i>2014</i>
Capital		
Tier 1 capital	365,978	351,305
Tier 2 capital	29,789	33,871
Total regulatory capital	395,767	385,176
Risk-weighted assets		
Credit risk	560,094	384,656
Market risk	70,461	58,352
Operational risk	55,548	50,141
Total risk-weighted assets	686,103	493,149
Total capital expressed as a percentage of risk-weighted assets, % ("capital adequacy ratio")	57.68%	78.11%
Total tier 1 capital expressed as a percentage of risk-weighted assets, % ("tier 1 capital adequacy ratio")	53.34%	71.24%

(Thousands of Euros)

30. Events after the reporting period

On 9 March, in accordance with the Memorandum of Understanding signed at the 102nd IIB Council Meeting (20-21 November 2014), Hungary fully met its obligation to contribute EUR 10,000,000 to the Bank's authorized capital. As a result, the paid-in capital of the International Investment Bank came to EUR 313,053,000, and Hungary increased its share to 12.78%.

(The end)

Independent auditor's report
on the consolidated financial statements of
International Investment Bank and its subsidiaries
for 2016

March 2017

**Independent auditor's report
on the consolidated financial statements of
International Investment Bank and its subsidiaries**

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Independent auditor's report

To the Council of the International Investment Bank

Opinion

We have audited the consolidated financial statements of International Investment Bank (the "Bank") and its subsidiaries (the "Group"), which comprise the consolidated statement of financial position as at 31 December 2016, and the consolidated income statement, consolidated statement of comprehensive income, consolidated statement of changes in equity and consolidated statement of cash flows for 2016, and notes to the consolidated financial statements, including a summary of significant accounting policies.

In our opinion, the accompanying consolidated financial statements present fairly, in all material respects, the financial position of the Group as at 31 December 2016 and its financial performance and its cash flows for 2016 in accordance with International Financial Reporting Standards (IFRSs).

Basis for opinion

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

Key audit matters

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

We have fulfilled the responsibilities described in the *Auditor's responsibilities for the audit of the consolidated financial statements* section of our report, including in relation to these matters. Accordingly, our audit included the performance of procedures designed to respond to our assessment of the risks of material misstatement of the consolidated financial statements. The results of our audit procedures, including the procedures performed to address the matters below, provide the basis for our audit opinion on the accompanying consolidated financial statements.

Provisions for impairment of loans to customers

The assessment of provisions for impairment of loans to customers is a key area of judgement for management of the Group. The identification of impairment and the determination of the recoverable amount are inherently uncertain processes involving significant judgements, various assumptions and factors including the financial standing of borrowers and expected future cash flows. Information on the impairment of loans to customers is included in Note 11, *Loans to customers*, Note 23, *Risk management*, to the consolidated financial statements. The use of different models and assumptions could produce significantly different estimates of impairment of loans to customers. Due to materiality of the loans to customers represented 31% of the total assets and significant judgements the assessment of provisions for impairment was one of the key audit matters.

Our audit procedures included an evaluation of the methodology of the assessment of provisions, testing of inputs, evaluation of the assumptions used by the Group in the calculation of the impairment and the assessment of the adequacy of provisions for loans to customers with individual signs of impairment. We analysed expected future cash flows in respect of significant individually impaired loans to customers.

We also assessed whether the disclosures in the consolidated financial statements about the Group's provision for impairment of loans to customers are compliant with applicable IFRS requirements.

Valuation of the buildings classified to "property and equipment" and "investment property"

The Group's aggregate value of the buildings classified to "property and equipment" and "investment property" was 10% of the total Group's assets. Group's management measured the value the buildings classified to "property and equipment" and "investment property" with involvement of the independent appraiser.

The valuation of the assets utilises unobservable inputs and assumptions. Changes of these inputs and assumptions may have a significant impact on the valuation. The significance and subjectivity of these valuations make them a key audit matter. Information of the valuation of the buildings classified to "property and equipment" and "investment property" is included in Note 12, *Investment property*, Note 13, *Property, equipment and intangible assets*, and Note 24, *Fair value measurements*, to the consolidated financial statements.

Our audit procedures in respect of the buildings classified to “property and equipment” and “investment property” included evaluation of competence and objectivity of the Group’s independent appraiser involved, examination of the significant assumptions applied and comparison of inputs used to available market prices and other observable information. We involved our real estate valuation specialists to evaluate the methodology and assumptions used. We also assessed whether the Group’s disclosures in relation to the valuation of the buildings classified to “property and equipment” and “investment property”, in particular, the sensitivity of fair value to changes to key assumptions, are compliant with applicable IFRS requirements.

Other information included in the Group’s Annual Report for 2016

Other information consists of the information included in the Annual Report of International Investment Bank for 2016 other than the consolidated financial statements and our auditor’s report thereon. Management is responsible for the other information. The Annual Report of International Investment Bank for 2016 is expected to be made available to us after the date of this auditor’s report.

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

In connection with our audit of the consolidated financial statements, our responsibility is to read the other information identified above when it becomes available and, in doing so, consider whether the other information is materially inconsistent with the consolidated financial statements or our knowledge obtained in the audit or otherwise appears to be materially misstated.

Responsibilities of management and Council of the International Investment Bank for the consolidated financial statements

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

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

Council of the International Investment Bank are responsible for overseeing the Group’s financial reporting process.

Auditor's responsibilities for the audit of the consolidated financial statements

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

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

- ▶ Identify and assess the risks of material misstatement of the consolidated financial statements, whether due to fraud or error, design and perform audit procedures responsive to those risks, and obtain audit evidence that is sufficient and appropriate to provide a basis for our opinion. The risk of not detecting a material misstatement resulting from fraud is higher than for one resulting from error, as fraud may involve collusion, forgery, intentional omissions, misrepresentations, or the override of internal control.
- ▶ Obtain an understanding of internal control relevant to the audit in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Group's internal control.
- ▶ Evaluate the appropriateness of accounting policies used and the reasonableness of accounting estimates and related disclosures made by management.
- ▶ Conclude on the appropriateness of management's use of the going concern basis of accounting and, based on the audit evidence obtained, whether a material uncertainty exists related to events or conditions that may cast significant doubt on the Group's ability to continue as a going concern. If we conclude that a material uncertainty exists, we are required to draw attention in our auditor's report to the related disclosures in the consolidated financial statements or, if such disclosures are inadequate, to modify our opinion. Our conclusions are based on the audit evidence obtained up to the date of our auditor's report. However, future events or conditions may cause the Group to cease to continue as a going concern.
- ▶ Evaluate the overall presentation, structure and content of the consolidated financial statements, including the disclosures, and whether the consolidated financial statements represent the underlying transactions and events in a manner that achieves fair presentation.
- ▶ Obtain sufficient appropriate audit evidence regarding the financial information of the entities or business activities within the Group to express an opinion on the consolidated financial statements. We are responsible for the direction, supervision and performance of the group audit. We remain solely responsible for our audit opinion.

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



Совершенство бизнес,
улучшаем мир

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

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

The partner in charge of the audit resulting in this independent auditor's report is O.V. Youshenkov.

O.V. Youshenkov
Partner
Ernst & Young Vneshaudit LLC

15 March 2017

Details of the audited entity

Name: International Investment Bank
Bank operates on the basis of the Agreement on the Establishment of the International Investment Bank dated 10 July 1970, registered in the UN Secretariat on 1 December 1971 under No 11417.
Address: Russia 107078, Moscow, Mashi Poryvaevoy str., 7.

Details of the auditor

Name: Ernst & Young Vneshaudit LLC
Record made in the State Register of Legal Entities on 4 February 2016, State Registration Number 1167746123478.
Address: Russia 115035, Moscow, Sadovnicheskaya naberezhnaya, 77, building 1.
Ernst & Young Vneshaudit LLC is a member of Self-regulated organization of auditors "Russian Union of auditors" (Association) ("SRO RUA"). Ernst & Young Vneshaudit LLC is included in the control copy of the register of auditors and audit organizations, main registration number 11603050953.

CONSOLIDATED STATEMENT OF FINANCIAL POSITION**As at 31 December 2016***(Thousands of euros)*

	<i>Note</i>	<i>31 December 2016</i>	<i>31 December 2015</i>
Assets			
Cash and cash equivalents	5	93,031	59,519
Deposits with banks and other financial institutions	6	45,337	100,392
Derivative financial assets	7	14,362	1,844
Available-for-sale investment securities	8	170,849	93,031
Available-for-sale investment securities pledged under repurchase agreements	8	98,458	23,028
Held-to-maturity investment securities	9	–	50,034
Held-to-maturity investment securities pledged under repurchase agreements	9	–	73,194
Loans to banks	10	94,367	140,597
Loans to customers	11	269,036	165,742
Investment property	12	21,840	33,819
Property, equipment and intangible assets	13	71,844	66,393
Other assets	14	2,319	1,810
Total assets		881,443	809,403
Liabilities			
Due to banks and other financial institutions	15	118,925	113,373
Derivative financial liabilities	7	11,623	29,898
Current customer accounts		9,218	7,430
Long-term loans of banks	16	73,349	44,187
Debt securities issued	17	272,528	212,724
Other liabilities	14	5,582	4,088
Total liabilities		491,225	411,700
Equity			
Subscribed capital	18	1,300,000	1,300,000
Callable capital		(986,947)	(996,947)
Paid-in capital		313,053	303,053
Revaluation reserve for available-for-sale investment securities		(1,506)	(1,664)
Revaluation reserve for property and equipment		12,945	31,453
Foreign currency translation reserve		(57)	(120)
Retained earnings less net income for the year		64,981	62,925
Net income for the year		802	2,056
Total equity		390,218	397,703
Total equity and liabilities		881,443	809,403

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

Alexandru Florescu



Acting Chairman of the Board

Eugeniy Atanasov



Head of the Financial Department

15 March 2017

The accompanying notes 1-29 are an integral part of these consolidated financial statements.

CONSOLIDATED INCOME STATEMENT**Year ended 31 December 2016***(Thousands of euros)*

	<i>Note</i>	2016	2015
Interest income	21	32,455	27,132
Interest expenses	21	(27,651)	(17,744)
Net interest income		4,804	9,388
Allowance for loan impairment	11	(7,557)	(6,166)
Net interest income after allowance for loan impairment		(2,753)	3,222
Fee and commission income		843	548
Fee and commission expense		(138)	(133)
Net fee and commission income		705	415
Net gains/(losses) from revaluation of derivative financial instruments		32,330	(6,661)
Net losses from revaluation of hedging instruments		(246)	–
Net gains/(losses) from dealing in foreign currencies and operations with derivatives		9,068	(5,302)
Net (losses)/gains from revaluation of assets and liabilities in foreign currencies		(31,173)	22,983
Net gains from available-for-sale investment securities		10,515	3,204
Income from lease of investment property	12	3,442	5,214
Losses from revaluation of investment property	12	(2,174)	(2,500)
Other income/(expenses)		447	(296)
Net non-interest income		22,209	16,642
Operating income		20,161	20,279
Reversal of allowance for impairment of other assets	14	67	89
General and administrative expenses	22	(18,939)	(16,908)
Other operating expenses on banking operations		(487)	(1,404)
Operating expenses		(19,359)	(18,223)
Net income for the year		802	2,056

The accompanying notes 1-29 are an integral part of these consolidated financial statements.

CONSOLIDATED STATEMENT OF COMPREHENSIVE INCOME**Year ended 31 December 2016***(Thousands of euros)*

	<i>Note</i>	2016	2015
Net income for the year		<u>802</u>	<u>2,056</u>
Other comprehensive loss			
<i>Other comprehensive income/(loss) to be reclassified to profit or loss in subsequent periods:</i>			
Change in unrealized revaluation of available-for-sale investment securities	18	158	(665)
Translation differences		<u>63</u>	<u>104</u>
Net other comprehensive income/(loss) to be reclassified to profit or loss in subsequent periods		<u>221</u>	<u>(561)</u>
<i>Other comprehensive loss not to be reclassified to profit or loss in subsequent periods:</i>			
Revaluation of property and equipment	13	<u>(18,508)</u>	<u>(3,642)</u>
Net other comprehensive loss not to be reclassified to profit or loss in subsequent periods		<u>(18,508)</u>	<u>(3,642)</u>
Other comprehensive loss		<u>(18,287)</u>	<u>(4,203)</u>
Total loss for the year		<u><u>(17,485)</u></u>	<u><u>(2,147)</u></u>

The accompanying notes 1-29 are an integral part of these consolidated financial statements.

CONSOLIDATED STATEMENT OF CHANGES IN EQUITY**Year ended 31 December 2016***(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>Foreign currency translation reserve</i>	<i>Retained earnings</i>	<i>Total equity</i>
At 31 December 2014	1,300,000	(1,027,382)	(999)	35,095	(224)	82,925	389,415
Profit for the year	–	–	–	–	–	2,056	2,056
Other comprehensive (loss)/income for the year	–	–	(665)	(3,642)	104	–	(4,203)
Total comprehensive (loss)/income	–	–	(665)	(3,642)	104	2,056	(2,147)
Contributions to capital (Note 18)	–	30,435	–	–	–	(20,000)	10,435
At 31 December 2015	1,300,000	(996,947)	(1,664)	31,453	(120)	64,981	397,703
Profit for the year	–	–	–	–	–	802	802
Other comprehensive income/(loss) for the year	–	–	158	(18,508)	63	–	(18,287)
Total comprehensive income/(loss)	–	–	158	(18,508)	63	802	(17,485)
Contributions to capital (Note 18)	–	10,000	–	–	–	–	10,000
At 31 December 2016	1,300,000	(986,947)	(1,506)	12,945	(57)	65,783	390,218

The accompanying notes 1-29 are an integral part of these consolidated financial statements.

CONSOLIDATED STATEMENT OF CASH FLOWS**Year ended 31 December 2016***(Thousands of euros)*

	<i>Note</i>	2016	2015
Cash flows from operating activities			
Interest, fees and commissions received		24,092	17,498
Interest, fees and commissions paid		(3,364)	(1,497)
Realized gains less losses from dealing in foreign currencies and operations with derivatives		9,079	(5,420)
Cash flows from lease of investment property		3,442	5,214
General and administrative expenses		(16,094)	(15,814)
Other operating expenses on banking operations		(78)	(932)
Cash flows from operating activities before changes in operating assets and liabilities		17,077	(951)
<i>Net (increase)/decrease in operating assets</i>			
Deposits with banks and other financial institutions		54,498	(76,379)
Loans to banks		47,598	(5,904)
Loans to customers		(118,231)	(61,048)
Other assets		(5)	401
<i>Net increase/(decrease) in operating liabilities</i>			
Due to banks and other financial institutions		1,589	60,572
Current customer accounts		1,481	2,618
Other liabilities		68	135
Net cash flows from operating activities		4,075	(80,556)
Cash flows from investing activities			
Interest received		11,458	10,805
Purchase of available-for-sale investment securities		(668,584)	(245,442)
Proceeds from sale and redemption of available-for-sale investment securities		618,419	161,597
Proceeds from sale and redemption of held-to-maturity investment securities		30,373	15,268
Investments in investment property		(50)	(33)
Acquisition of property, equipment and intangible assets		(1,754)	(2,764)
Net cash flows from investing activities		(10,138)	(60,569)
Cash flows from financing activities			
Interest paid		(26,324)	(14,759)
Long-term interbank financing raised		60,000	21,448
Long-term interbank financing repaid		(29,569)	–
Placement of bonds		67,398	184,399
Redemption of bonds		(43,910)	(65,089)
Contributions to capital		10,000	10,435
Net cash flows from financing activities		37,595	136,434
Effect of exchange rate changes on cash and cash equivalents		1,980	(1,708)
Net increase/(decrease) in cash and cash equivalents		33,512	(6,399)
Cash and cash equivalents, beginning		59,519	65,918
Cash and cash equivalents, ending	5	93,031	59,519

The accompanying notes 1-29 are an integral part of these consolidated financial statements.

(Thousands of euros)

1. Principal activities

The International Investment Bank (hereinafter, 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 Group is primarily engaged in commercial lending for the benefit of national investment projects in the member countries of the Group and for other purposes defined by the Council of the Bank. The Group also performs transactions with securities and foreign currency. The Group operates from its office at 7 Mashi Poryvaevoi St., Moscow, Russia, and the European regional office in Bratislava (Eurovea Central 1, Pribinova 4, Bratislava, 81109, Slovak Republic).

The Group had an average of 230 staff employees during 2016 (2015: 237).

On 31 July 2014, the EU Council imposed sectoral sanctions against Russia. The preamble of the Decision of the EU Council of 31 July 2014 (paragraph 9) and Council Regulation (EU) No 833/2014 of 31 July 2014 (paragraph 5), which was developed based on the Decision, emphasize that the sanctions do not cover Russia-based institutions with international status established by intergovernmental agreements in which Russia is one of the parties. Therefore, the International Investment Bank is not subject to the restrictive measures.

The Group continues to expand its operations despite the ongoing market volatility in member countries:

- ▶ Hungary re-entered the Bank in 2015 and in 2016 made an ahead-of-schedule final contribution to the Group’s equity. As at the end of 2016, Hungary’s share in the Bank’s paid-in capital was EUR 40 million or 12.78%.
- ▶ As a result of the Hungary’s re-entering, the respective share of the EU countries in the Bank’s paid-in capital grew up to 48.72% exceeding the share of the Russian Federation, which decreased to 47.92%.
- ▶ The Bank winds up the introduction of changes to its constituent documents and implementation of the three-level corporate governance structure. The Protocol on Introducing Changes to the Agreement on the Establishment of the International Investment Bank and the Statutes (hereinafter, the “Protocol”) signed at the end of 2015 is at the stage of ratification (internal state procedures) by member countries of the Bank. The Protocol will enter into force upon completion of those ratification procedures. As at the end of 2016, the Protocol was ratified by Hungary, Vietnam, Romania, and Russia (4 countries out of 9).
- ▶ In December 2016, Fitch Ratings upgraded the rating of the Group to BBB with a stable outlook, for the first time since rating in 2013. Also, the Bank is assigned the following investment grade ratings: Baa1 (stable outlook) by Moody’s and A (stable outlook) by Dagong Global Credit Rating. In June 2016, the Bank was assigned the BBB rating (stable outlook) by Standard & Poor’s.
- ▶ In June 2016, the Group concluded a cooperation agreement on fund raising with the Central Bank of Cuba. The agreement confirms the special status of the International Investment Bank in Cuba, which implies that the Cuban party shall fulfill its liabilities to the IIB under the projects in Cuba financed by the Group.
- ▶ The IIB completed a large-scale IT-project to upgrade its core banking system (CBS) – a digital platform to manage, process and protect the Bank’s data. A data-processing center was launched in the IIB European Regional Office in Bratislava to ensure security and uninterrupted service of the new CBS.
- ▶ In April 2016 the Group signed an agreement with the Ministry of Finance of Slovakia concerning the creation of a Technical Assistance Fund, which will be a new instrument supporting the activities of the IIB in country shareholders. The aim of the Fund is to finance the consulting services and technical assistance rendered, for projects in which the IIB is investing in fulfilling its mission. The countries in scope are Mongolia, Vietnam and Cuba. Within this given scope the Group is undertaking consultation and negotiations with CAF (The Development Bank of Latin America) in order to identify potential projects in which to invest or to finance.

*(Thousands of euros)***1. Principal activities (continued)****Member countries of the Group**

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

<i>Member countries</i>	<i>2016, %</i>	<i>2015, %</i>
Russian Federation	47.923	49.505
Republic of Bulgaria	13.481	13.926
Hungary	12.777	9.899
Czech Republic	9.703	10.023
Slovak Republic	6.862	7.088
Romania	5.895	6.089
Republic of Cuba	1.713	1.769
Socialist Republic of Vietnam	1.172	1.211
Mongolia	0.474	0.490
	100.000	100.000

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

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

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

Business environment in the member countries

Economic and political development of the Bank's member countries affects the activities of enterprises operating in these countries. Considering this fact, the Bank performs its operations with reference to the regional features of its member countries to ensure overall assessment and control of credit and operational risks.

The accompanying consolidated 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 Group. Future evolution of the conditions in which the Group operates may differ from the assessment made by the management for the purposes of these consolidated financial statements.

2. Basis of preparation**General**

These consolidated financial statements of the Group have been prepared in accordance with International Financial Reporting Standards ("IFRS") approved by the International Accounting Standards Board.

Subsidiary

The Bank is a parent company of the Group, which owns CJSC IIB Capital (a 100% subsidiary established in 2012 for the purpose of the acting of the Bank, in particular, for the property trust of the Bank) as at 31 December 2016. The authorized capital of the subsidiary is 44.5 thousand rubles (1.1 thousand of euros at the historical exchange rate at the date of established).

Basis of measurement

These consolidated 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.

(Thousands of euros)

2. Basis of preparation (continued)

Preparation and presentation of financial statements

The financial year of the Group begins on 1 January and ends on 31 December.

Functional and presentation currency

Euro (“EUR”) is the Group’s functional and presentation currency as it reflects the economic substance of the underlying operations conducted by the Group and circumstances affecting its operations, because most financial assets and financial liabilities as well as income and expenses of the Group are denominated in EUR.

These consolidated financial statements are presented in thousands of euros (“thousands of euros” or “EUR thousand”), unless otherwise indicated.

3. Summary of accounting policies

Changes in accounting policies

The Group has adopted the following amended IFRS which are effective for annual periods beginning on or after 1 January 2016:

Amendments to IAS 1 Disclosure Initiative

The amendments to IAS 1 clarify, rather than significantly change, existing IAS 1 requirements. The amendments clarify:

- ▶ The materiality requirements in IAS 1;
- ▶ That specific line items in the statements of profit or loss and OCI and the statement of financial position may be disaggregated;
- ▶ That entities have flexibility as to the order in which they present the notes to financial statements;
- ▶ That the share of OCI of associates and joint ventures accounted for using the equity method must be presented in aggregate as a single line item, and classified between those items that will or will not be subsequently reclassified to profit or loss.

Furthermore, the amendments clarify the requirements that apply when additional subtotals are presented in the statement of financial position and the statements of profit or loss and OCI. These amendments are effective for annual periods beginning on or after 1 January 2016. These amendments do not have any impact on the Group and presentation of other comprehensive income in consolidated financial statements of the Group.

Amendments to IFRS 10, IFRS 12 and IAS 28 Investment Entities: Applying the Consolidation Exception

The amendments address issues that have arisen in applying the investment entities exception under IFRS 10 *Consolidated Financial Statements*. The amendments to IFRS 10 clarify that the exemption from presenting consolidated financial statements applies to a parent entity that is a subsidiary of an investment entity, when the investment entity measures all of its subsidiaries at fair value.

Furthermore, the amendments to IFRS 10 clarify that only a subsidiary of an investment entity that is not an investment entity itself and that provides support services to the investment entity is consolidated. All other subsidiaries of an investment entity are measured at fair value. The amendments to IAS 28 *Investments in Associates and Joint Ventures* allow the investor, when applying the equity method, to retain the fair value measurement applied by the investment entity associate or joint venture to its interests in subsidiaries.

These amendments must be applied retrospectively and are effective for annual periods beginning on or after 1 January 2016. These amendments do not have any impact on the Group as the Group does not apply the consolidation exception.

(Thousands of euros)

3. Summary of accounting policies (continued)

Changes in accounting policies (continued)

Annual improvements 2012-2014 cycle

These improvements are effective for annual periods beginning on or after 1 January 2016. They include, in particular:

IFRS 5 Non-current Assets Held for Sale and Discontinued Operations

Assets (or disposal groups) are generally disposed of either through sale or distribution to owners. The amendment clarifies that changing from one of these disposal methods to the other would not be considered a new plan of disposal, rather it is a continuation of the original plan. There is, therefore, no interruption of the application of the requirements in IFRS 5. This amendment must be applied prospectively.

IFRS 7 Financial Instruments: Disclosures

The amendment clarifies that a servicing contract that includes a fee can constitute continuing involvement in a financial asset. An entity must assess the nature of the fee and the arrangement against the guidance for continuing involvement in IFRS 7 in order to assess whether the disclosures are required. The assessment of which servicing contracts constitute continuing involvement must be done retrospectively. However, the required disclosures would not need to be provided for any period beginning before the annual period in which the entity first applies the amendments.

Foreign currency transactions

The consolidated financial statements are presented in euro, which is the Group'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 consolidated income statement as "Net (losses)/gains from revaluation of assets and liabilities in 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 Group's exchange rate on the date of the transaction are included in "Net gains/(losses) from dealing in foreign currencies".

Basis of consolidation

Subsidiaries, which are those entities in which the Group has an interest of more than one half of the voting rights, or otherwise has power to exercise control over their operations, are consolidated. Subsidiaries are consolidated from the date on which control is transferred to the Group and are no longer consolidated from the date that control ceases. All intra-group transactions, balances and unrealized gains on transactions between group companies are eliminated in full; unrealized losses are also eliminated unless the transaction provides evidence of an impairment of the asset transferred. Where necessary, accounting policies for subsidiaries have been changed to ensure consistency with the policies adopted by the Group.

A change in the ownership interest of a subsidiary, without a change of control, is accounted for as an equity transaction. Losses are attributed to the non-controlling interests even if that results in a deficit balance.

If the Group loses control over a subsidiary, it derecognizes the assets (including goodwill) and liabilities of the subsidiary, the carrying amount of any non-controlling interests, the cumulative translation differences, recorded in equity; recognizes the fair value of the consideration received, the fair value of any investment retained and any surplus or deficit in profit or loss and reclassifies the parent's share of components previously recognized in other comprehensive income to profit or loss.

(Thousands of euros)

3. Summary of accounting policies (continued)

Investments in associates

Associates are entities in which the Group generally has between 20% and 50% of the voting rights (interest), or is otherwise able to exercise significant influence, but which it does not control or jointly control. Investments in associates are accounted for under the equity method and are initially recognized at cost, including goodwill. Subsequent changes in the carrying value reflect the post-acquisition changes in the Group's share of net assets of the associate. The Group's share of its associates' profits or losses is recognized in the consolidated income statement, and its share of movements in reserves is recognized in other comprehensive income. However, when the Group's share of losses in an associate equals or exceeds its interest in the associate, the Group does not recognize further losses, unless the Group is obliged to make further payments to, or on behalf of, the associate.

Unrealized gains on transactions between Group and its associates are eliminated to the extent of the Group's interest in the associates; unrealized losses are also eliminated unless the transaction provides evidence of an impairment of the asset transferred.

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 Group measures financial instruments, such as trading and available-for-sale securities, derivatives and non-financial assets such as investment property, at fair value at each reporting date. Also, fair values of financial instruments measured at amortized cost are disclosed in Note 24.

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 Group. 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 Group 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 consolidated 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 consolidated financial statements on a recurring basis, the Group 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 Group 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 Group 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 Group 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 from change in fair value 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 consolidated 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 Group 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 Group 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 (“repo”) are treated as secured financing transactions. Securities sold under sale and repurchase agreements are retained in the consolidated 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, deposits with banks and other financial institutions as appropriate. The difference between sale and repurchase price is treated as interest and accrued over the life of repo agreements using the effective interest rate method.

Securities lent to counterparties are retained in the consolidated statement of financial position. Securities borrowed are not recorded in the consolidated 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 consolidated 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 Group 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 consolidated income statement as net gains/(losses) from dealing in foreign currencies and operations with derivatives.

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 separate from the host are carried at fair on the trading portfolio with changes in fair value recognized in profit or loss.

Hedge accounting

To manage the risks associated with fluctuations in cash flows from receipt and payment of interest, as well as with fluctuations in the fair value of certain items, the Group uses derivative financial instruments. As a result, the Group applies hedge accounting for transactions that meet specified criteria.

At inception of the hedge accounting relationship, the Group formally documents the relationship between the hedged item and the hedging instrument, including the nature of the risk, the risk management objective and strategy for undertaking the hedge and the method that will be used to assess the effectiveness of the hedging relationship at inception and on an ongoing basis.

At each hedge effectiveness assessment date, a hedge relationship must be expected to be highly effective on a prospective basis and demonstrate that it was highly effective (retrospective effectiveness) for the designated period in order to qualify for hedge accounting. A formal assessment is undertaken both at inception and at each month end on an ongoing basis. A hedge is expected to be highly effective if the changes in fair value or cash flows attributable to the hedged risk during the period for which the hedge is designated were offset by the hedging instrument in a range of 80% to 125% during the hedging period.

(Thousands of euros)

3. Summary of accounting policies (continued)

Hedge accounting (continued)

Fair value hedges

For designated and qualifying fair value hedges, the cumulative change in the fair value of a hedging derivative is recognised in the consolidated income statement in Net gains (losses) from revaluation of hedging instruments. Meanwhile, the cumulative change in the fair value of the hedged item attributable to the risk hedged is recorded as part of the carrying value of the hedged item in the consolidated statement of financial position and is also recognised in the consolidated income statement in Net gains (losses) from revaluation of hedging instruments.

If the hedging instrument expires or is sold, terminated or exercised, or where the hedge no longer meets the criteria for hedge accounting, or the Group decides to voluntarily discontinue the hedging relationship, the hedge relationship is discontinued prospectively. When the hedge ceases, the adjustment of the carrying amount of the hedged financial instrument is amortized over the remaining period until date of maturity of the hedged financial instrument. If the hedged item is derecognised, the unamortized amount of the adjustment is recognized in profit or loss.

Cash flow hedges

For designated and qualifying cash flow hedges, the effective portion of the cumulative gain or loss on the hedging instrument is initially recognized in consolidated other comprehensive income and is recorded through other comprehensive income. An ineffective portion of the gain or loss on the hedging instrument is recognized in the consolidated income statement.

When a hedging instrument expires, is sold, terminated, exercised, or when a hedge no longer meets the criteria for hedge accounting, the total amount of income or expense accumulated at that time in equity is transferred from equity and recognized in the consolidated statement of income in the same period or periods during which hedged projected cash flows affect profit or loss. When a forecast transaction is no longer expected, the cumulative gain or loss recognized in equity is immediately transferred to the consolidated income statement.

Borrowings

Issued financial instruments or their components are classified as liabilities, where the substance of the contractual arrangement results in the Group 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 banks and other financial institutions, long-term loans of banks and debt securities issued. 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 – Group 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.

Operating – Group as lessor

The Group presents assets subject to operating leases in the consolidated statement of financial position according to the nature of the asset. Lease income from operating leases is recognized in the consolidated 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.

(Thousands of euros)

3. Summary of accounting policies (continued)

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 Group 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 Group 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 Group 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 consolidated 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 consolidated statement of financial position.

Impairment of financial assets

The Group 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.

Deposits with banks and other financial institutions, long-term loans to banks, trade financing loans, and loans to customers

For deposits with banks and other financial institutions, long-term loans to banks, trade financing loans, and loans to customers carried at amortized cost, the Group 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 Group 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.

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 consolidated 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 consolidated statement of financial position is reduced through the use of an allowance account and the amount of the loss is recognized in the consolidated 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 Group. 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 consolidated income statement.

(Thousands of euros)

3. Summary of accounting policies (continued)

Impairment of financial assets (continued)

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 Group 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 consolidated income statement.

Available-for-sale financial investments

For available-for-sale financial investments, the Group 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 consolidated income statement – is reclassified from other comprehensive income to the consolidated income statement. Impairment losses on equity investments are not reversed through the consolidated 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 consolidated 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 consolidated income statement, the impairment loss is reversed through the consolidated income statements.

(Thousands of euros)

3. Summary of accounting policies (continued)

Impairment of financial assets (continued)

Renegotiated loans

Where possible, the Group 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 consolidated statement of financial position.
- ▶ If the loan restructuring is not caused by the financial difficulties of the borrower the Group 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 Group 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.

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 consolidated statement of financial position where:

- ▶ The rights to receive cash flows from the asset have expired.
- ▶ The Group 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.
- ▶ The Group 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 Group 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 Group'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 Group 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 Group's continuing involvement is the amount of the transferred asset that the Group 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 Group'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 canceled 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 consolidated income statement.

*(Thousands of euros)***3. Summary of accounting policies (continued)***Financial guarantees*

In the ordinary course of business, the Group gives financial guarantees, consisting of letters of credit, guarantees and acceptances. Financial guarantees are initially recognised in the consolidated financial statements at fair value, in “Other liabilities”, being the premium received. Subsequent to initial recognition, the Group’s liability under each guarantee is measured at the higher of the amortised premium and the best estimate of expenditure required to settle any financial obligation arising as a result of the guarantee.

Any increase in the liability relating to financial guarantees is taken to the consolidated statement of profit or loss. The premium received is recognised in profit or loss on a straight-line basis over the life of the guarantee.

Property and equipment

Property and equipment are carried in the consolidated 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 consolidated income statement, in which case the increase is recognized in profit or loss. A revaluation deficit is recognized in the consolidated 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 consolidated 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.

*(Thousands of euros)***3. Summary of accounting policies (continued)****Investment property**

Investment property includes buildings held to earn rental income or for capital appreciation and which are not used by the Group 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 Group'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.

Investment property that is being redeveloped for continuing use as investment property or for which the market has become less active continues to be measured at fair value. Earned rental income is recorded in the consolidated income statement within Income from lease of investment property. Gains and losses resulting from changes in the fair value of investment property are recorded in the consolidated income statement and presented within gains/(losses) from revaluation of investment property.

Subsequent expenditure is subject to capitalization only when it is probable that future economic benefits associated with an asset will flow to the Group 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

The useful lives of intangible assets are assessed to be finite and include the value of computer software. Intangible assets acquired are measured on initial recognition at cost. Following initial recognition, intangible assets are carried at cost less any accumulated amortisation and any accumulated impairment losses. Amortisation is calculated using the straight-line method. Intangible assets are tested for impairment if any indication of impairment exists. The amortisation period and the amortisation method for an intangible asset with a indefinite useful life are reviewed at least at each financial year-end. Amortisation is calculated using the straight-line method to write down the cost of intangible assets to their residual values over their estimated useful lives, as follows:

	<u>Years</u>
Automated banking system	20
Other computer software	1-5

Intangible assets with finite lives are amortized over the useful economic lives 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 Group 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 Group'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 Group measures an asset classified as held for sale at the lower of its carrying amount and fair value less costs to sell. The Group 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.

(Thousands of euros)

3. Summary of accounting policies (continued)

Provisions

Provisions are recognized when the Group 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 consolidated 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 consolidated statement of financial position but disclosed in the consolidated financial statements, when an inflow of economic benefits is probable.

Recognition of income and expenses

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

(Thousands of euros)

3. Summary of accounting policies (continued)

Recognition of income and expenses (continued)

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 consolidated 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 Group's right to receive the payment is established.

Assets under trust

Assets under trust management are not reported in consolidated financial statements, as they are not assets of the Group.

Segment reporting

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

Standards issued but not yet effective

The standards and interpretations issued, but not yet effective, up to the date of issuance of the Group's consolidated financial statements are disclosed below. The Group intends to adopt these standards when they become effective.

IFRS 9 Financial Instruments

In July 2014, the IASB issued the final version of IFRS 9 *Financial Instruments* which reflects all phases of the financial instruments project and replaces IAS 39 *Financial Instruments: Recognition and Measurement* and all previous versions of IFRS 9. The standard introduces new requirements for classification and measurement, impairment, and hedge accounting.

From a classification and measurement perspective, the new standard will require all financial assets, except equity instruments and derivatives, to be assessed based on a combination of the entity's business model for managing the assets and the instruments' contractual cash flow characteristics. The IAS 39 measurement categories will be replaced by: fair value through profit or loss (FVPL), fair value through other comprehensive income (FVOCI), and amortized cost categories. IFRS 9 will also allow entities to continue to irrevocably designate instruments that qualify for amortized cost or FVOCI instruments as FVPL, if doing so eliminates or significantly reduces a measurement or recognition inconsistency. Equity instruments that are not held for trading may be irrevocably designated as FVOCI, with no subsequent reclassification of gains or losses to the income statement. The accounting for financial liabilities will largely be the same as the requirements of IAS 39.

IFRS 9 will also fundamentally change the approach to loan impairment. The standard will replace IAS 39's incurred loss approach with a forward-looking expected credit loss (ECL) approach. The Group will be required to record an allowance for expected losses for all loans and other debt financial assets not carried at FVPL, as well as for loan commitments and financial guarantee contracts. The allowance is based on the expected credit losses associated with the probability of default in the next twelve months unless there has been a significant increase in credit risk since origination, in which case the allowance would be based on the probability of default over the life of the asset.

(Thousands of euros)

3. Summary of accounting policies (continued)

Standards issued but not yet effective (continued)

IFRS 9 is effective for annual periods beginning on or after 1 January 2018, with early application permitted. Retrospective application is required, but restatement of comparative information is not required; the effect on the transition date – 1 January 2018 – would be recorded in retained earnings. The adoption of IFRS 9 is not expected to have a significant effect on the classification and measurement of the Group's financial assets and will have no impact on the classification and measurement of the Group's financial liabilities. The Group expects to measure investment securities at fair value through OCI as the Group expects not only to hold the assets to collect contractual cash flows but also to sell a significant amount on a relatively frequent basis. Deposits with banks and other financial institutions, loans to banks and loans to customers are held to collect contractual cash flows and are expected to give rise to cash flows representing solely payments of principal and interest. Thus, the Group expects to continue measuring those financial assets at amortized cost under IFRS 9. The Group plans to adopt the new standard on the required effective date. In 2016, the Group made a general assessment of the impact of all three phases of IFRS 9. This preliminary assessment is based on currently available information and may be subject to changes arising from further detailed analyses or additional reasonable and supportable information that will become available to the Group in the future. On the whole, the Group does not expect the adoption of the new requirements to have a significant impact on its balance sheet or equity, except for the effect of adoption of IFRS 9 impairment requirements. The Group expects increase in level of provisions which will influence an equity, and will perform a detailed assessment to determine the amount of such increase. The Group believes that all existing hedge relationships currently designated at the discretion of the Group in effective hedging relationships will still qualify for hedge accounting under IFRS 9. As IFRS 9 does not change the general principles of how an entity accounts for effective hedges, the Group does not expect a significant impact as a result of adoption of IFRS 9. The Group will assess possible changes related to the accounting for the time value of options, forward points or the currency basis spread in more detail in the future.

IFRS 15 Revenue from Contracts with Customers

In May 2014, the IASB issued IFRS 15 *Revenue from Contracts with Customers*, effective for periods beginning on 1 January 2018 with early adoption permitted. IFRS 15 defines principles for recognizing revenue and will be applicable to all contracts with customers. However, interest and fee income integral to financial instruments and leases will continue to fall outside the scope of IFRS 15 and will be regulated by the other applicable standards (e.g., IFRS 9, and IFRS 16 *Leases*).

Revenue under IFRS 15 will need to be recognized as goods and services are transferred, to the extent that the transferor anticipates entitlement to goods and services.

The standard will also specify a comprehensive set of disclosure requirements regarding the nature, extent and timing as well as any uncertainty of revenue and corresponding cash flows with customers.

The Group does not anticipate early adopting IFRS 15 and is currently evaluating its impact.

IFRS 16 Leases

The IASB issued the new standard for accounting for leases – IFRS 16 *Leases* in January 2016. The new standard does not significantly change the accounting for leases for lessors. However, it does require lessees to recognize most leases on their balance sheets as lease liabilities, with the corresponding right of-use assets. Lessees must apply a single model for all recognized leases, but will have the option not to recognize 'short-term' leases and leases of 'low-value' assets. Generally, the profit or loss recognition pattern for recognized leases will be similar to today's finance lease accounting, with interest and depreciation expense recognized separately in the consolidated statement of profit or loss.

IFRS 16 is effective for annual periods beginning on or after 1 January 2019. Early application is permitted provided the new revenue standard, IFRS 15, is applied on the same date.

The Group does not anticipate early adopting IFRS 16 and is currently evaluating its impact.

(Thousands of euros)

3. Summary of accounting policies (continued)

Standards issued but not yet effective (continued)

Amendments to IAS 12 Income Taxes

In January 2016, through issuing amendments to IAS 12, the IASB clarified the accounting treatment of deferred tax assets of debt instruments measured at fair value for accounting, but measured at cost for tax purposes. The Group does not anticipate that adopting the amendments would have a material impact on its consolidated financial statements.

Amendments to IAS 7 Statement of Cash Flows

In January 2016, the IASB issued amendments to IAS 7 *Statement of Cash Flows* with the intention to improve disclosures of financing activities and help users to better understand the reporting entities' liquidity positions. Under the new requirements, entities will need to disclose changes in their financial liabilities as a result of financing activities such as changes from cash flows and non-cash items (e.g., gains and losses due to foreign currency movements). The amendment is effective from 1 January 2017. The Group is currently studying the application of these amendments.

Amendments to IFRS 2 Share-based Payment

The IASB issued amendments to IFRS 2 *Share-based Payment* in relation to the classification and measurement of share-based payment transactions. The amendments are intended to eliminate diversity in practice, but are narrow in scope and address specific areas of classification and measurement. The amendments address three main areas:

- ▶ The effects of vesting conditions on the measurement of a cash-settled share-based payment transaction.
- ▶ The classification of a share-based payment transaction with net settlement features for withholding tax obligations.
- ▶ The accounting where a modification to the terms and conditions of a share-based payment transaction changes its classification from cash-settled to equity-settled.

These amendments are effective for annual periods beginning on or after 1 January 2018. On adoption, entities are required to apply the amendments without restating prior periods, but retrospective application is permitted if elected for all three amendments and other criteria are met. Early application is permitted. The amendments are not expected to have any impact on the Group.

Applying IFRS 9 Financial Instruments with IFRS 4 Insurance Contracts – Amendments to IFRS 4

The amendments address concerns arising from implementing the new financial instruments Standard, IFRS 9, before implementing the new insurance contracts standard that the Board is developing to replace IFRS 4. The amendments introduce two options for entities issuing insurance contracts: a temporary exemption from applying IFRS 9 and an overlay approach. The optional temporary exemption from IFRS 9 is available to entities whose activities are predominantly connected with insurance. The temporary exemption permits such entities to continue to apply IAS 39 *Financial Instruments: Recognition and Measurement* while they defer the application of IFRS 9 until 1 January 2021 at the latest. The overlay approach requires an entity to remove from profit or loss additional volatility that may arise if IFRS 9 is applied with IFRS 4.

The temporary exemption is first applied for reporting periods beginning on or after 1 January 2018. An entity may elect the overlay approach when it first applies IFRS 9 and apply that approach retrospectively to financial assets designated on transition to IFRS 9. The amendments are not expected to have any impact on the Group.

Applying IFRS 10 and IAS 28 – Sale or transfer of assets between an investor and its associate or joint venture

The amendments eliminate a known discrepancy between the requirements of IFRS 10 and IAS 28 for the loss of control of a subsidiary that is transferred to an associate or a joint venture as a contribution to equity. The amendments clarify that the income or loss arising from the sale or transfer by an investor of assets that are business in accordance with the definition in IFRS 3 in favor of its associate or joint venture should be fully reflected. In December 2015, the IASB decided to postpone the effective date of these amendments indefinitely.

(Thousands of euros)

3. Summary of accounting policies (continued)

Standards issued but not yet effective (continued)

Transfers of investment property (amendments to IAS 40).

The amendments clarify when an entity should transfer property, including property under construction or development into, or out of investment property. The amendments state that a change in use occurs when the property meets, or ceases to meet, the definition of investment property and there is evidence of the change in use.

Entities should apply the amendments prospectively to changes in use that occur on or after the beginning of the annual reporting period in which the entity first applies the amendments. An entity should reassess the classification of property held at that date and, if applicable, reclassify property to reflect the conditions that exist at that date. The amendments effective for annual periods beginning on or after 1 January 2018. Early application of the amendments is permitted and must be disclosed.

IFRIC Interpretation 22 Foreign Currency Transactions and Advance Consideration

The interpretation clarifies that in determining the spot exchange rate to use on initial recognition of the related asset, expense or income (or part of it) on the derecognition of a non-monetary asset or non-monetary liability relating to advance consideration, the date of the transaction is the date on which an entity initially recognises the non-monetary asset or non-monetary liability arising from the advance consideration. If there are multiple payments or receipts in advance, then the entity must determine a date of the transactions for each payment or receipt of advance consideration. Entities may apply the amendments on a fully retrospective basis. Early application of interpretation is permitted and must be disclosed. The Group does not anticipate early adopting of interpretation and is currently evaluating its impact. The interpretation is effective for annual periods beginning on or after 1 January 2018.

4. Significant accounting judgments and estimates

Assumptions and estimation uncertainty

In the process of applying the Group'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 consolidated financial statements, which have the most significant effect on the amounts recognized in the consolidated 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 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 Group's consolidated statement of financial position less allowances for impairment. The Group regularly reviews its financial assets to assess impairment. When assessing impairment losses, the Group 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 Group 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.

Fair value of financial instruments

Where the fair values of financial assets and financial liabilities recorded in the consolidated 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. More details are provided in Note 24.

(Thousands of euros)

4. Significant accounting judgments and estimates (continued)

Assumptions and estimation uncertainty (continued)

Impairment of available-for-sale equity securities

The Group 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 Group 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 Group applies the fair value model with regard to investment property. Buildings included in fixed assets are stated at revalued amount.

As for buildings within property and equipment, the Group 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 Group's building was carried out as at 31 December 2016 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 technique may differ from the prices of actual transactions in the real estate market. Starting from 31 December 2016, the revalued building is depreciated in accordance with the remaining useful life.

As for investment property, the Group 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 consolidated income statement. The most recent revaluation of the Group's investment property was carried out as at 31 December 2016 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 technique may differ from the prices of actual transactions in the real estate market.

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

- ▶ Note 7 – Derivative financial instruments.
- ▶ Note 8 – Available-for-sale investment securities.
- ▶ Note 10 – Loans to banks.
- ▶ Note 11 – Loans to customers.
- ▶ Note 12 – Investment property.
- ▶ Note 13 – Property, equipment and intangible assets.
- ▶ Note 19 – Contingencies and lending commitments.

(Thousands of euros)

5. Cash and cash equivalents

Cash and cash equivalents comprise:

	<u>2016</u>	<u>2015</u>
Cash on hand	104	66
Nostro accounts with banks and other financial institutions		
<i>Credit rating from A- to A+</i>	62,548	21,106
<i>Credit rating from BBB- to BBB+</i>	4,526	3,059
<i>Credit rating from BB- to BB+</i>	551	350
Total nostro accounts with banks and other financial institutions	67,625	24,515
Short-term deposits with banks		
Term deposits with banks		
<i>Credit rating from BBB- to BBB+</i>	–	18,304
<i>Credit rating from BB- to BB+</i>	25,302	16,634
Total short-term deposits with banks	25,302	34,938
Cash and cash equivalents	93,031	59,519

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

6. Deposits with banks and other financial institutions

Deposits with banks and other financial institutions are presented based on contractual terms and include the following items:

	<u>2016</u>	<u>2015</u>
Term deposits up to 1 year		
<i>Credit rating from BB- to BB+</i>	–	6,049
<i>Credit rating from B- to B+</i>	37,126	79,276
Total term deposits up to 1 year	37,126	85,325
Term deposits over 1 year		
<i>Credit rating from A- to A+</i>	5,821	15,067
<i>Credit rating from BB- to BB+</i>	2,390	–
Total term deposits over 1 year	8,211	15,067
Total deposits with banks and other financial institutions	45,337	100,392

Amounts due from the National Bank of the Republic of Cuba

	<u>2016</u>	<u>2015</u>
Term deposits with the National Bank of the Republic of Cuba without credit rating	34,967	34,967
Less: allowance for impairment	(34,967)	(34,967)
Term deposits with the National Bank of the Republic of Cuba	–	–

Concentration of deposits with banks and other financial institutions

As at 31 December 2016, the Group had three counterparties (31 December 2015: five counterparty) accounting for over 10% of the Group's total deposits with banks and other financial institutions, except for deposits with the National Bank of the Republic of Cuba.

*(Thousands of euros)***7. Derivative financial instruments**

The Group performs the operations with currency and other derivative financial instruments which are generally traded in an over-the-counter market with professional market counterparties on standardized contractual terms and conditions. Derivative financial instruments have either potentially favorable terms (and are assets) or potentially unfavorable conditions (and are liabilities) as a result of fluctuations in the exchange rates or other variable factors associated with these instruments. The fair value of derivative financial instruments can vary significantly depending on the potentially favorable and unfavorable conditions.

The table below shows the fair value of derivative financial instruments as at 31 December 2016 and 31 December 2015 and notional amounts of term contracts for the purchase and sale of foreign currency specifying contractual exchange rates.

	31 December 2016				
	Notional amount		Weighted average exchange rate	Fair value	
	Purchase	Sale		Assets	Liabilities
Derivative financial assets and liabilities at fair value through profit or loss					
Swaps	RUB 9,136,720 thousand	EUR 132,150 thousand	69.42	14,246	883
	RON 110,300 thousand	EUR 24,971 thousand	4.44	–	632
	EUR 117,000 thousand	USD 128,825 thousand	1.10	116	5,704
	EUR 8,000 thousand	RUB 572,280 thousand	71.54	–	788
Forwards	EUR 34,000 thousand	USD 37,896 thousand	1.11	–	2,080
Total derivative financial assets and liabilities at fair value through profit or loss				14,362	10,087
Derivative financial assets and liabilities designated as hedging instruments					
Swaps	RON 298,300 thousand	EUR 67,068 thousand	4.45	–	1,536
Total derivative financial assets and liabilities designated as hedging instruments				–	1,536
Derivative financial instruments				14,362	11,623
31 December 2015					
	Notional amount		Weighted average exchange rate	Fair value	
	Purchase	Sale		Assets	Liabilities
Derivative financial assets and liabilities at fair value through profit or loss					
Swaps	RUB 12,136,720 thousand	EUR 185,914 thousand	65.28	–	29,034
	RON 110,300 thousand	EUR 24,972 thousand	4.42	–	864
	EUR 61,000 thousand	USD 64,982 thousand	1.07	1,775	–
Forwards	EUR 30,000 thousand	USD 32,721 thousand	1.09	69	–
Total derivative financial assets and liabilities at fair value through profit or loss				1,844	29,898
Derivative financial instruments				1,844	29,898

(Thousands of euros)

7. Derivative financial instruments (continued)

Due to issuing bond loans denominated in currencies other than the Group's functional currency (Note 17), the Group concluded cross currency interest rate swaps and currency forwards on an arm's length basis with large international and Russian credit institutions. These swaps are used to manage long-term currency risks of the Group. Payment netting is not applied to the parties' obligations in respect of interest and principal payments.

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 end of the reporting period and are not indicative of the credit risk.

As at 31 December 2016 and 31 December 2015, the Group has positions in the following types of derivatives:

Forwards: Forward contracts are contractual agreements to buy or sell a specified financial instrument at a specific price and date in the future. Forwards are customized contracts transacted in the over-the-counter market.

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.

Fair value measurement is based on the corresponding forward curves that depend on exchange rates, interest rates and swap contract maturity. For the fair value of swaps, the discount rate was calculated on the basis of zero coupon yield curve and credit risk. Changes in the fair value of swaps were mainly due to the increase in the forward EUR to RUB exchange rates.

8. Available-for-sale investment securities

Available-for-sale investment securities comprise:

	<u>2016</u>	<u>2015</u>
Owned by the Group		
Quoted debt securities		
Government bonds:		
<i>Eurobonds issued by governments of member countries</i>	52,678	93,027
Government bonds	<u>52,678</u>	<u>93,027</u>
Corporate bonds		
<i>Credit rating from A- to A+</i>	21,152	–
<i>Credit rating from BBB- to BBB+</i>	21,861	–
<i>Credit rating from BB- to BB+</i>	57,579	–
<i>Credit rating from B- to B+</i>	17,575	–
Corporate bonds	<u>118,167</u>	<u>–</u>
Total quoted debt securities	<u>170,845</u>	<u>93,027</u>
Quoted equity instruments		
<i>No credit rating</i>	4	4
Total quoted equity instruments	<u>4</u>	<u>4</u>
Available-for-sale investment securities	<u>170,849</u>	<u>93,031</u>
Pledged under repurchase agreements		
Quoted debt securities		
<i>Eurobonds issued by governments of member countries</i>	10,286	21,646
<i>Eurobonds issued by governments of non-member countries</i>	7,597	–
Government bonds	<u>17,883</u>	<u>21,646</u>
Corporate bonds		
<i>Credit rating AAA</i>	22,486	–
<i>Credit rating from AA- to AA+</i>	4,688	–
<i>Credit rating from A- to A+</i>	32,521	–
<i>Credit rating from BBB- to BBB+</i>	4,994	1,382
<i>Credit rating from BB- to BB+</i>	15,886	–
Corporate bonds	<u>80,575</u>	<u>1,382</u>
Total quoted available-for-sale debt securities pledged under repurchase agreements	<u>98,458</u>	<u>23,028</u>

(Thousands of euros)

8. Available-for-sale investment securities (continued)

Government bonds represent EUR-denominated, USD-denominated and RUB-denominated securities issued and guaranteed by the Ministries of Finance of these countries, maturing in 2018-2027 (31 December 2015: maturing in 2018-2027). The annual coupon rate for these bonds varies from 0.4% to 7.9% (31 December 2015: from 2.0% to 6.0%).

Corporate bonds are represented by the bonds issued by large companies and banks of member countries of the Bank, as well as corporate international companies and Development Banks that have similar goals and missions with the Group, maturing in 2018-2031 (31 December 2015: maturing in 2020). The annual coupon rate for these bonds varies from 0.6% to 10.25% (31 December 2015: 5.0%).

9. Held-to-maturity investment securities

In July 2016, due to changes in the Bank's management's intent to withhold investment securities to maturity, the Bank reclassified these securities into investment securities available for sale. At the date of reclassification, the amortized cost of securities amounted to 92,105 thousand euros.

Held-to-maturity investment securities comprise:

	<u>2016</u>	<u>2015</u>
Owned by the Bank		
Quoted debt securities		
<i>Eurobonds issued by governments of member countries</i>	–	1,272
Government bonds of member countries	–	1,272
Corporate bonds		
<i>Credit rating from BBB- to BBB+</i>	–	17,442
<i>Credit rating from BB- to BB+</i>	–	31,320
Corporate bonds	–	48,762
Total quoted held-to-maturity debt securities	–	50,034
Held-to-maturity investment securities pledged under repurchase agreements		
Quoted debt securities		
<i>Eurobonds issued by governments of member countries</i>	–	10,489
Government bonds of member countries	–	10,489
Corporate bonds		
<i>Credit rating from BB- to BB+</i>	–	62,705
Corporate bonds	–	62,705
Total held-to-maturity investment securities pledged under repurchase agreements	–	73,194

Government bonds of member countries represent EUR-denominated and RUB-denominated securities issued and guaranteed by the Ministries of Finance of these countries maturing as at 31 December 2015 in 2018-2020. The annual coupon rate for these bonds as at 31 December 2015 varies from 3.6% to 7.9%.

Corporate bonds are represented by the bonds issued by major companies and banks of member countries and EU countries, maturing as at 31 December 2015 in 2016-2023. The annual coupon rate for these bonds as at 31 December 2015 varies from 3.0% to 7.9%.

(Thousands of euros)

10. Loans to banks

During 2016, the Group continued its lending activities, being guided by the key priorities of the Development Strategy of the IIB. 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 Group considers national development institutes, export and import banks and agencies, international financial organizations and development banks as its key counterparties.

In 2016 and 2015, the Group provided trade financing loans and long-term loans to banks operating in the following countries:

	<u>2016</u>	<u>2015</u>
Trade financing loans:		
Russian Federation	953	–
Trade financing loans	<u>953</u>	<u>–</u>
Long-term loans to banks		
Mongolia	47,970	43,044
Russian Federation	26,425	64,223
Socialist Republic of Vietnam	19,019	33,330
Long-term loans to banks	<u>93,414</u>	<u>140,597</u>
Total loans to banks	<u>94,367</u>	<u>140,597</u>

As at 31 December 2016 and 31 December 2015, outstanding trade financing loans and long-term loans to banks are neither past due nor impaired, and no allowances for impairment of these loans were made.

Analysis of collateral for loans to banks

The following table provides an analysis of the portfolio of trade financing loans and long-term loans to banks by type of collateral as at 31 December 2016 and 31 December 2015:

	<u>2016</u>		<u>2015</u>	
	<i>Loans to banks</i>	<i>Share in the total loans, %</i>	<i>Loans to banks</i>	<i>Share in the total loans, %</i>
Pledge of real property (mortgage) and title	7,247	7.7	6,933	4.9
Uncollateralized part of the loans	87,120	92.3	133,664	95.1
	<u>94,367</u>	<u>100.0</u>	<u>140,597</u>	<u>100.0</u>

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

Concentration of long-term loans to banks

As at 31 December 2016, long-term loans and trade financing loans to five banks (31 December 2015: five banks) with the total amount of loans to each of them exceeding 10% of total loans to banks were recorded on the Group's balance sheet. As at 31 December 2016, the total amount of such major loans was EUR 74,787 thousand (31 December 2015: EUR 85,238 thousand) and no impairment allowances (31 December 2015: no allowances) have been made for them.

(Thousands of euros)

11. Loans to customers

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

	<u>2016</u>	<u>2015</u>
Republic of Bulgaria	65,922	57,917
Russian Federation	61,213	28,160
Romania	40,235	25,844
Republic of Ecuador	39,570	18,249
Republic of Panama	36,276	–
Czech Republic	22,930	–
Slovak Republic	8,411	23,437
USA	6,108	–
Mongolia	5,683	21,890
Gross loans to customers	286,348	175,497
Less: allowance for loan impairment	(17,312)	(9,755)
Loans to customers	269,036	165,742

The information on the overdue loans as at 31 December 2016 and 31 December 2015 is stated below:

	<u>2016</u>	<u>2015</u>
Loans with overdue principal and/or interest	14,769	14,858
Less: allowance for loan impairment	(14,769)	(9,755)
Overdue loans to customers	–	5,103

As at 31 December 2016 and 31 December 2015, there were no overdue but not impaired loans.

Allowance for impairment of loans to customers

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

	<i>Slovak Republic</i>	<i>Republic of Bulgaria</i>	<i>Romania</i>	<i>Total</i>
At 1 January 2016	3,000	6,755	–	9,755
Net charge for the period	5,103	200	2,254	7,557
At 31 December 2016	8,103	6,955	2,254	17,312
Individual impairment	8,103	6,666	–	14,769
Gross amount of loans, individually determined to be impaired, before deducting any individually assessed impairment allowance	8,103	6,666	–	14,769
	<i>Slovak Republic</i>	<i>Republic of Bulgaria</i>	<i>Total</i>	
At 1 January 2015	3,589	–	3,589	
Net (reversal)/charge for the period	(589)	6,755	6,166	
At 31 December 2015	3,000	6,755	9,755	
Individual impairment	3,000	6,755	9,755	
Gross amount of loans, individually determined to be impaired, before deducting any individually assessed impairment allowance	8,103	6,755	14,858	

*(Thousands of euros)***11. Loans to customers (continued)**

The following table provides an analysis of the customer loan portfolio, net of allowance for impairment, by types of collateral as at 31 December 2016 and 31 December 2015:

	2016		2015	
	<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>
State guarantees	75,845	28.2	18,249	11.0
Pledge of real property (mortgage) and title	25,811	9.6	35,896	21.6
Pledge of right of claim	22,970	8.5	18,492	11.2
Corporate guarantees	22,930	8.5	–	–
Pledge of equipment and goods in turnover	22,641	8.4	13,281	8.0
Pledge of shares	21,579	8.0	29,952	18.1
Pledge of vehicles	2,756	1.0	–	–
Uncollateralized part of the loans	74,504	27.8	49,872	30.1
Total loans to customers	269,036	100.0	165,742	100.0

Analysis of collateral for loans to customers

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.

Concentration of loans to customers

As at 31 December 2016, loans to three borrowers (2015: two) with the total amount of loans to each of the two borrowers exceeding 10% of total loans to customers were recorded on the Group's balance sheet. As at 31 December 2016, these loans comprised EUR 107,191 thousand (2015: EUR 40,991 thousand) in total and no impairment allowances (2015: no allowances) have been made for them.

Analysis of loans to customers by industry

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

	2016	2015
Leasing	85,897	44,114
Production and transmission of electricity	39,570	14,688
Food and beverage	27,504	7,569
Chemical production	23,831	22,743
Metal working industry	22,930	–
Manufacturing of electrical equipment	20,809	21,208
Construction	14,769	29,179
Agriculture	14,295	4,942
Transport	13,752	15,001
Crude oil refining	10,002	9,989
Production of pharmaceutical products	6,645	–
Trading	6,036	5,418
Other	308	646
	286,348	175,497
Less: allowance for loan impairment	(17,312)	(9,755)
Loans to customers	269,036	165,742

*(Thousands of euros)***12. Investment property**

In 2016 and 2015, the following changes occurred in the cost of property under operating lease:

	<u>2016</u>	<u>2015</u>
At 1 January	33,819	52,879
Additions	14,324	–
Inseparable improvements	50	33
Transfers in the property and equipment	(24,179)	(16,593)
Effect of revaluation	(2,174)	(2,500)
Carrying amount at 31 December	<u>21,840</u>	<u>33,819</u>

In 2016, the Group received collateral in the form of an administrative building in the city of Ulan Bator, Mongolia.

The Group rents buildings under operating lease agreements. In 2016, the Group's income from lease of investment property amounted to EUR 3,442 thousand (2015: EUR 5,214 thousand).

As at 31 December 2016, the fair value of investment property is determined based on the results of valuation performed on 31 December 2016. 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.

The fair value is determined by reference to market-based evidence. For further details on the fair value of investment property refer to Note 24.

If the investment property was measured using the cost method, the carrying amounts as at 31 December 2016 and 31 December 2015 would be as follows:

	<u>2016</u>	<u>2015</u>
Cost	20,091	20,264
Additions	50	–
Accumulated depreciation	(2,370)	(8,092)
Net book value	<u>17,771</u>	<u>12,172</u>

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

*(Thousands of euros)***13. Property, equipment and intangible assets**

The movements in property, equipment and intangible assets for the years 2016 and 2015 were as follows:

	<i>Buildings</i>	<i>Equipment</i>	<i>Computers and software</i>	<i>Office furniture</i>	<i>Vehicles</i>	<i>Intangible assets</i>	<i>Other</i>	<i>Capital expenditure</i>	<i>Total</i>
Cost or revalued amount									
At 1 January 2016	62,807	7,073	3,278	296	808	325	176	1,591	76,354
Additions	–	–	–	–	–	–	–	1,754	1,754
Transfers from the investment property	24,179	–	–	–	–	–	–	–	24,179
Transfers	223	436	83	22	–	2,147	7	(2,918)	–
Disposals	–	(9)	–	(11)	–	–	–	–	(20)
Recovery of accumulated depreciation upon revaluation	(1,057)	–	–	–	–	–	–	–	(1,057)
Effect of revaluation	(18,508)	–	–	–	–	–	–	–	(18,508)
At 31 December 2016	67,644	7,500	3,361	307	808	2,472	183	427	82,702
Accumulated depreciation									
At 1 January 2016	–	(6,547)	(2,445)	(228)	(477)	(165)	(99)	–	(9,961)
Charge for the period	(1,174)	(209)	(285)	(19)	(103)	(178)	(6)	–	(1,974)
Disposals	–	9	–	11	–	–	–	–	20
Recovery of accumulated depreciation upon revaluation	1,057	–	–	–	–	–	–	–	1,057
At 31 December 2016	(117)	(6,747)	(2,730)	(236)	(580)	(343)	(105)	–	(10,858)
Net book value									
At 31 December 2015	62,807	526	833	68	331	160	77	1,591	66,393
At 31 December 2016	67,527	753	631	71	228	2,129	78	427	71,844

*(Thousands of euros)***13. Property, equipment and intangible assets (continued)**

	<i>Buildings</i>	<i>Equipment</i>	<i>Computers and software</i>	<i>Office furniture</i>	<i>Vehicles</i>	<i>Intangible assets</i>	<i>Other</i>	<i>Capital expenditure</i>	<i>Total</i>
Cost or revalued amount									
At 1 January 2015	50,806	7,069	3,095	298	923	160	188	766	63,305
Inseparable improvements	52	–	–	–	–	–	–	–	52
Additions	–	–	–	–	–	–	–	1,780	1,780
Transfers from the investment property	16,593	–	–	–	–	–	–	–	16,593
Transfers	–	179	505	4	102	165	–	(955)	–
Disposals	–	(175)	(322)	(6)	(217)	–	(12)	–	(732)
Recovery of accumulated depreciation upon revaluation	(1,002)	–	–	–	–	–	–	–	(1,002)
Effect of revaluation	(3,642)	–	–	–	–	–	–	–	(3,642)
At 31 December 2015	62,807	7,073	3,278	296	808	325	176	1 591	76,354
Accumulated depreciation									
At 1 January 2015	(67)	(6,523)	(2,537)	(214)	(598)	(53)	(106)	–	(10,098)
Charge for the period	(935)	(176)	(229)	(18)	(96)	(112)	(6)	–	(1,572)
Disposals	–	152	321	4	217	–	13	–	707
Recovery of accumulated depreciation upon revaluation	1,002	–	–	–	–	–	–	–	1,002
At 31 December 2015	–	(6,547)	(2,445)	(228)	(477)	(165)	(99)	–	(9,961)
Net book value									
At 31 December 2014	50,739	546	558	84	325	107	82	766	53,207
At 31 December 2015	62,807	526	833	68	331	160	77	1,591	66,393

As at 31 December 2016, the cost of fully depreciated property and equipment still used by the Group was EUR 7,982 thousand (31 December 2015: EUR 7,977 thousand).

*(Thousands of euros)***13. Property, equipment and intangible assets (continued)**

As at 31 December 2016, the fair value of a group of buildings owned by the Group is determined based on the results of valuation performed on 31 December 2016. 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.

The fair value is determined by reference to market-based evidence. For further details on the fair value of property and equipment refer to Note 24.

If the buildings were measured using the cost method, the carrying amounts as at 31 December 2016 and 31 December 2015 would be as follows:

	<u>2016</u>	<u>2015</u>
Cost	52,132	37,583
Additions	223	52
Accumulated depreciation	(20,871)	(15,029)
Net book value	<u>31,484</u>	<u>22,606</u>

14. Other assets and liabilities

Other assets comprise:

	<u>2016</u>	<u>2015</u>
Financial assets		
Settlements on bank transactions	1,814	1,525
Accounts receivable on business operations	1,394	1,202
Other financial assets	136	–
	<u>3,344</u>	<u>2,727</u>
Less: allowance for impairment	(1,924)	(1,633)
Total financial assets less allowance	<u>1,420</u>	<u>094</u>
Non-financial assets		
Assets held-for-sale – real estate	89	–
Inventories – real estate	55	43
Other non-financial assets	755	673
Total non-financial assets	<u>899</u>	<u>716</u>
Total other assets	<u>2,319</u>	<u>1,810</u>

The movements in other impairment allowance are as follows:

	<u>2016</u>	<u>2015</u>
Allowance at 1 January	1,633	1,763
Reversal charge for the year	(67)	(89)
Change in allowance resulting from changes in exchange rates	358	(41)
Allowance at 31 December	<u>1,924</u>	<u>1,633</u>

*(Thousands of euros)***14. Other assets and liabilities (continued)**

Other liabilities comprise:

	<u>2016</u>	<u>2015</u>
Financial liabilities		
Other accounts payable on business operations	1,182	1,063
Other accounts payable on bank transactions	662	–
Other financial liabilities	19	–
Total financial liabilities	<u>1,863</u>	<u>1,063</u>
Non-financial liabilities		
Settlements with employees	3,647	2,975
Other non-financial liabilities	72	50
Total non-financial liabilities	<u>3,719</u>	<u>3,025</u>
Total other liabilities	<u>5,582</u>	<u>4,088</u>

15. Due to banks and other financial institutions

Due to banks and other financial institutions are presented based on contractual terms and include the following items:

	<u>2016</u>	<u>2015</u>
Due to banks up to 1 year		
Term deposits of banks and other financial institutions	52,856	48,617
Total due to banks up to 1 year	<u>52,856</u>	<u>48,617</u>
Due to banks over 1 year		
Repurchase agreements	66,069	64,756
Total due to banks over 1 year	<u>66,069</u>	<u>64,756</u>
Total due to banks	<u>118,925</u>	<u>113,373</u>

The Group performs daily monitoring of the repurchase agreements and the value of collateral when placing/returning additional collateral, if necessary.

Concentration of deposits from banks and other financial institutions

As at 31 December 2016, the Group has two counterparties (31 December 2015: three counterparties) accounting for over 10% of the Group's total deposits from banks and other financial institutions in the amount of EUR 111,418 thousand (31 December 2015: EUR 104,873 thousand).

16. Long-term loans of banks

Long-term loans of banks comprise:

	<u>2016</u>	<u>2015</u>
Syndicated loans	59,039	–
Loans of banks	14,310	44,187
Total long-term loans of banks	<u>73,349</u>	<u>44,187</u>

In June 2016 the Group received a syndicated loan in the amount of EUR 60,000 thousand with a floating rate of EURIBOR (6 months) + 1.75% p. a. and maturing in May 2018.

*(Thousands of euros)***17. Debt securities issued**

Debt securities issued comprise:

	<i>Interest rate, % p.a.</i>	<i>Maturity</i>	<i>2016</i>	<i>2015</i>
RUB-denominated bonds	0.1-12.3	2024-2025	151,516	158,067
EUR-denominated bonds	3.5	2019	30,127	30,100
RON-denominated bonds	3.4-4.1	2018-2019	90,885	24,557
Total bonds			<u>272,528</u>	<u>212,724</u>

On 27 September 2016, the Group issued bonds denominated in Romanian lei in the amount of RON 300 million (EUR 67,398 thousand) maturing in three years. The coupon rate on the bonds was set at 3.4% payable annually with the first coupon payment to be made on 27 September 2017.

Among other things, the Group used the proceeds from the offerings to expand its loan portfolio.

At the dates of placement of the RUB-denominated bonds, the Group entered into cross-currency interest rate swaps for the purpose of managing currency risks (Note 7).

On 31 October 2016, the Bank offered to repurchase RUB-denominated bonds, series 02, and repurchased almost the total amount of those bonds RUB 2 998,0 thousand (EUR 43,327 thousand) from investors. A new coupon rate of 0.1% p.a. was set.

18. 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 2016, the unpaid portion of the Bank's subscribed capital in the amount of EUR 986,947 thousand (31 December 2015: EUR 996,947 thousand) is the amount of contributions that have not been made yet by the Bank's member countries and the amount of unallocated equity contributions totaling EUR 175,500 thousand (31 December 2015: EUR 175,500 thousand).

On 9 March 2016, in accordance with the Memorandum of Understanding signed at the 102nd meeting of the IIB's Council (20-21 November 2014), the Government of Hungary contributed EUR 10,000 thousand to the Bank's equity. On 18 May 2015, the Government of Hungary contributed EUR 10,000 thousand to the Bank's equity to resume its full membership. In accordance with the Memorandum of Understanding signed at the 102nd meeting of the IIB's Council (20-21 November 2014), the Bank added EUR 10,000 thousand to the contribution of Hungary out of retained earnings for the previous years. On 29 July in accordance with the Memorandum of Understanding signed at the 102nd meeting of the IIB's Council (20-21 November 2014), the Bank fulfilled its obligations to transfer the second payment in the amount of EUR 10,000 thousand out of retained earnings for the previous years as Hungary's additional contribution to the Bank's share capital.

As a result, the paid-in capital of the International Investment Bank totaled EUR 313,053 thousand (31 December 2015: EUR 303,053 thousand).

*(Thousands of euros)***18. Equity (continued)****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 2015	(999)	35,095
Net unrealized gains on available-for-sale investment securities	2,539	–
Realized gains on available-for-sale investment securities reclassified to the income statement	(3,204)	–
Revaluation of buildings	–	(3,642)
At 31 December 2015	(1,664)	31,453
Net unrealized gains on available-for-sale investment securities	10,673	–
Realized gains on available-for-sale investment securities reclassified to the income statement	(10,515)	–
Revaluation of buildings	–	(18,508)
At 31 December 2016	(1,506)	12,945

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.

19. Contingencies and loan commitments**Legal**

In the ordinary course of business, the Group 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 Group. In accordance with the Agreement on the Establishment of the Group, its assets (irrespective of their location) enjoy immunities from any administrative and legal claims.

The Group 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 Group's further actions to collect bad debt and/or realize respective repossession rights is higher than the amount collected and also when the Group 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 Group 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 Group did not obtain insurance coverage related to temporarily discontinued operations or the Group's obligations to third parties.

*(Thousands of euros)***19. Contingencies and loan commitments (continued)****Commitments and contingencies**

At any time the Group may have outstanding commitments to extend loans. These commitments take the form of approved loan agreements.

As at 31 December 2016, commitments and contingencies of the Group comprised off-balance credit-related commitments, in particular undrawn loan facilities and reimbursement obligations.

Off-balance credit-related commitments are presented in the table below as at 31 December 2016 and 31 December 2015.

	<u>2016</u>	<u>2015</u>
Undrawn loan facilities	33,103	52,376
Reimbursement obligations	9,898	6,796
Guarantees issued	4,934	4,556
Total off-balance commitments	<u>47,935</u>	<u>63,728</u>

20. Leases**Group as lessor**

The Group provides its investment property for operating leases. As at 31 December 2016, the Group's non-cancelable operating lease rentals amount to EUR 4,752 thousand (31 December 2015: EUR 5,938 thousand) and will be settled within 1-5 years.

21. Interest income and interest expense

Net interest income comprises:

	<u>2016</u>	<u>2015</u>
Loans to customers	13,886	8,022
Loans to banks	6,462	7,058
Available-for-sale investment securities	5,091	2,165
Held-to-maturity investment securities	2,975	5,944
Deposits with banks and other financial institutions, including cash and cash equivalents	4,041	3,943
Interest income	<u>32,455</u>	<u>27,132</u>
Debt securities issued	(22,511)	(14,812)
Funds raised under repurchase agreements	(1,839)	(819)
Long-term loans of banks	(1,798)	(1,247)
Due to banks and other financial institutions	(1,198)	(609)
Current customer accounts	(305)	(257)
Interest expenses	<u>(27,651)</u>	<u>(17,744)</u>
Net interest income	<u>4,804</u>	<u>9,388</u>

In 2016, there was no interest income accrued on impaired loans issued (2015: EUR 185 thousand).

*(Thousands of euros)***22. General and administrative expenses**

General and administrative expenses comprise:

	<u>2016</u>	<u>2015</u>
Employee compensations and employment taxes	13,001	11,471
Depreciation of property, equipment and intangible assets (Note 13)	1,974	1,572
IT-expenses, inventory and occupancy expenses	1,715	1,293
Professional services	1,019	466
Expenses related to business travel, representative and accommodation expenses	682	1,277
Other	548	829
General and administrative expenses	<u>18,939</u>	<u>16,908</u>

23. Risk management**Risk management framework**

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

The Group's risk management activities are intended to:

- ▶ Identify, analyze and manage risks faced by the Group.
- ▶ 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 professional risk management for the bank transactions.

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

Integrated into the whole vertical organizational structure of the Group and all areas of the Group's activities, the risk management system makes it possible to identify in a timely manner and effectively manage different types of risks.

Risk management involves all of the Group's divisions in the evaluating, assuming, and controlling risks ("Three lines of defense"):

- ▶ Risk-taking (1st line of defense): the Group's divisions directly preparing and conducting transactions, involved in the identification, assessment, and monitoring of risks and comply with internal regulations on risk management, as well as give due consideration to the risk level in the preparation of transactions.
- ▶ Risk management (2nd line of defense): the division responsible for risk management develops risk management tools and methodology, assesses and monitors the risk level, prepares reports on risks, carries out risk aggregation, and calculates the amount of total capital requirements.
- ▶ Internal audit (3rd line of defense): independent quality assessment for existing risk management processes, identification of violations, and proposals for the improvement of the risk management system.

The Group's operations are managed taking into account the level of the risk appetite approved by the Council and its integration into a system of limits and restrictions insuring the acceptable level of risk for aggregated positions, transparent distribution of total risk limit among the activities of the Group.

The Bank's Council, the Board, the Finance Committee, the Credit Committee and the Risk Management Department are responsible for managing the Group's risks.

(Thousands of euros)

23. Risk management (continued)

Risk management framework (continued)

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 divisions and committees of the Bank.

The Finance Committee determines the Bank's approaches to forming the optimal structure of the Bank's balance sheet, taking into account information of current and expected level of risks associated with assets and liabilities management within the established limits and other restrictions. It also ensures management and control over the credit risk, market risk, operational risk, reputational risk, legal risk and liquidity risk and reviews the limit-setting offers.

The Credit Committee manages the Bank's loan portfolio in accordance with its effective lending policy, aligns operation of the Group's divisions in terms of the credit risk management and reviews the offers for setting credit risk limits in respect of the certain counterparties.

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 Group's performance.

During 2016, further development of the risk management system started in 2013 was aimed at implementation of Basel standards and best practices of development banks within the Group:

- ▶ New methodological and regulatory documents relating to credit and operational risk management have been elaborated.
- ▶ The Group continued to implement the target model of the risk management system, based on requirements of the leading rating agencies.

In compliance with the existing procedures, twice a year the Group sets and reviews limits for counterparties for the purpose of performing financial transactions and assessing their creditworthiness. As part of the lending activity analysis, the Group continuously monitored the level of its loan assets risk. During the reporting period, the Group sent its specialists to certain borrowers in order to monitor the implementation of the projects and identify potential primary evidence of impairment of loan assets.

To control and monitor the compliance with limits, the Group 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 and stop-loss limits. In addition, the Group's management receives regular reports on the status of risks within the Group.

Risk appetite

The risk appetite is the aggregate amount of risk taken by the Group to achieve its strategic goals and objectives. By approving the level of risk appetite, the Bank's Council determines the willingness to accept a risk or the amount of equity and liquidity that the Bank is willing to risk in the implementation of this strategy.

Risk appetite consists of 4 main components:

- ▶ The allocation of capital and liquidity (if necessary).
- ▶ Target allocation of capital across the main types of risk.
- ▶ The level of risk and target risk appetite in the context of the main performance indicators of the Group and risks significant for the Group.
- ▶ Determining levels of tolerance.

(Thousands of euros)

23. Risk management (continued)

Risk management framework (continued)

The procedure for determining the Group's risk appetite shall be defined by the Credit Risk Management Department and submitted for review by the Board and approval by the Council of the Bank.

The risk appetite shall be approved by the Council of the Bank on an annual basis for the next year and shall be a major factor of the Group's strategic limits determining the thresholds for the Group's key performance indicators and the Group's significant risks.

In determining the risk appetite, the Group assesses whether the specified risk appetite is acceptable in the current time period and whether it will be acceptable in the future, taking into account:

- ▶ Expectations of the founders concerning the level of profitability.
- ▶ International regulatory standards.
- ▶ Current and expected future volume of transactions.
- ▶ Current and expected future structure of significant risks.
- ▶ Current and expected future level of aggregate capital.

Based on the risk appetite determined by the Council, the Board annually approves the Group's limits, sublimits, and risk indicators, which should not exceed the target values of the risk appetite.

Risk identification

The Group identifies and manages both external and internal risk factors throughout its organizational structure. As a result of regular analysis of the Group's exposure to different types of risks performed by the Risk Management Department, the Group 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 the Finance Committee and, if necessary, also communicated to the Board along with the recommendations on possible risk mitigation measures.

Risk assessment, management and control

The Group's risk exposure is primarily reduced by means of collective decision-making. Strict allocation of responsibilities between divisions and officers of the Group, 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, if necessary, updated by the Group in order to reflect changed market conditions and improve the risk management methodology.

The risk monitoring system comprises:

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

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

- ▶ Credit risk;
- ▶ Liquidity risk;
- ▶ Market risk;
- ▶ Operational risk.

(Thousands of euros)

23. Risk management (continued)

Credit risk

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

System of credit risk management

The Group'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 establishes the limits per borrower/group of related borrowers. The Credit Committee structures the transaction to minimize credit risk. The Loan Operations Analysis Department is responsible for ongoing control over the quality of the Group's loan portfolio.

Upon preparation of a transaction by the initiating unit it is reviewed by the Credit Committee, and then it is approved by the Board. The Board is responsible for all direct credit risk exposures in the amount of up to 15% of the Group'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 Customer Relations Department. Customer Relations Department takes a decision on the preliminary of starting information on the deal whether to continue work with the client or not. In case of a positive decision, Credit Department makes full examination of the deal and sends the full set of required documents for reviewing the loan/credit application to Legal Department, Risk Management Department, Security Department, Strategic Development and Analysis Department, Internal Control Department, Compliance Control Department, Operational Department, Financial Department, Structured and Debt financing Department. These departments prepare expert opinions in the framework of their competence. The loan/credit application is subject to review by the Credit Committee based on the Credit Department's Description of the Investment Transaction and expert opinions received from the departments. The procedure of making lending decisions comprises the following steps: Step 1 includes reviewing application and making decision by the Credit Committee (if such issue falls within its competence); Step 2 includes making decision by the Board of the Group (if such issue falls within its competence); Step 3 includes sending a set of respective documents approved by the Board of the Group to the member country in order to obtain the final approval from the country of origin of the borrower or making decision by the Council of the Group (if such issue falls within its competence).

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

To mitigate credit risk, the Group 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 of the borrowers and their ability to repay interest and principal of debt, and on correspondent limits modification (if necessary).

The Group 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 Group. 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.

(Thousands of euros)

23. Risk management (continued)

Credit risk (continued)

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 Group 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 Group applies the following types of collateral for recovery of loans and fulfillment of obligations:

- ▶ Pledge of equipment and goods in turnover;
- ▶ Pledge of real estate (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 Group assumes that the fair value of the collateral is its value estimate recognized by the Group 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 Group's internal expert estimate, or carrying amount of the collateral including adjustment coefficient (discount). Where the market value of the collateral is assessed as impaired, the borrowers are usually required to provide additional collateral.

Portfolio of loans to banks and customers (less allowance for impairment) by type of collateral is analyzed in Notes 10 and 11.

Maximum exposure to credit risk

The maximum exposure to credit risk for the components of the consolidated 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 the financial instruments are recorded at fair value, their carrying amounts represent the current credit risk exposure but not the maximum credit 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 the whole amount of these commitments (Note 19).

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 consolidated 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.

(Thousands of euros)

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

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 customer'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.

The following table provides information on the credit quality of long-term loans to banks and trade financing loans (Note 10) and loans to customers (Note 11) as at 31 December 2016 and 31 December 2015:

2016	Loan amount	Allowance for impairment	Loan amount, including allowance for impairment	Impairment to loan amount ratio, %
Trade financing loans without any signs of impairment identified				
Standard loans				
- Russian Federation	953	–	953	–
Long-term loans to banks without any signs of impairment identified				
Standard loans				
- Mongolia	47,970	–	47,970	–
- Russian Federation	26,425	–	26,425	–
- Socialist Republic of Vietnam	19,019	–	19,019	–
	94,367	–	94,367	–
Loans to customers without any signs of impairment identified				
Standard loans				
- Russian Federation	61,213	–	61,213	–
- Republic of Bulgaria	53,477	–	53,477	–
- Republic of Ecuador	39,570	–	39,570	–
- Republic of Panama	36,276	–	36,276	–
- Romania	25,205	–	25,205	–
- Czech Republic	22,930	–	22,930	–
- USA	6,108	–	6,108	–
- Mongolia	5,683	–	5,683	–
- Slovak Republic	308	–	308	–
Watch loans to customers				
- Romania	15,030	(2,254)	12,776	15.0
Restructured loans				
- Republic of Bulgaria	5,779	(289)	5,490	5.0
Uncollectible loans				
- Slovak Republic	8,103	(8,103)	–	100
- Republic of Bulgaria	6,666	(6,666)	–	100
	286,348	(17,312)	269,036	6.0
Total loans	380,715	(17,312)	363,403	4.5

(Thousands of euros)

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

2015	Loan amount	Allowance for impairment	Loan amount, including allowance for impairment	Impairment to loan amount ratio, %
Long-term loans to banks without any signs of impairment identified				
Standard loans				
- Russian Federation	64,223	–	64,223	–
- Mongolia	43,044	–	43,044	–
- Socialist Republic of Vietnam	33,330	–	33,330	–
	140,597	–	140,597	–
Loans to customers without any signs of impairment identified				
Standard loans				
- Republic of Bulgaria	51,162	–	51,162	–
- Russian Federation	28,160	–	28,160	–
- Romania	25,844	–	25,844	–
- Mongolia	21,890	–	21,890	–
- Republic of Ecuador	18,249	–	18,249	–
- Slovak Republic	15,334	–	15,334	–
Uncollectible loans				
- Slovak Republic	8,103	(3,000)	5,103	37
- Republic of Bulgaria	6,755	(6,755)	–	100
	175,497	(9,755)	165,742	5.6
Total loans	316,094	(9,755)	306,339	3.1

Where possible, the Group 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 Group creates allowance for impairment of loans that represents its estimate of losses incurred in its loan portfolio. The Group writes off a loan balance against related allowances for impairment of loans 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 borrower'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 Group determines the allowances appropriate for each individually significant loan on an individual basis. Due to a limited number of borrowers, the Group 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 dividend 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, or more frequently, unless unforeseen circumstances require more careful attention.

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

*(Thousands of euros)***23. Risk management (continued)****Liquidity risk**

Liquidity risk is the risk of loss resulting from the Group'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 Group'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 Group) and/or an unforeseen need of immediate and simultaneous discharge of its financial obligations.

Liquidity management is an integral part of general policy for the Group's assets and liabilities management (ALM) and operates within the established limits and restrictions related to management of risks (liquidity, interest rate and currency risk) and the Group's balance sheet items, and in accordance with the documents of strategic, tactical and operating planning.

Procedures for the Group's liquidity position management, ensuring the Group's ability to meet its obligations in full and on a timely basis and efficient resources management, are stipulated in the *Regulations for IIB's Liquidity Position Management* that enables the development of the liquidity position management function provided for by the *IIB's Assets and Liabilities Management Policy*, as an integral part of general function of the Group's management.

Decision making matrix related to liquidity management includes a strategic level of liquidity management (the Council), tactical level (the Board and special-purpose committees) and operational level (responsible structural divisions). In 2015, the Group updated its approaches to the assets and liabilities management. Asset and Liability Management Department (DUAP or ALM Unit) became responsible for organizing and aligning management of the Group's liquidity position. The Group manages its liquidity position in accordance with planning horizons (up to 6 months) and possible scenarios of movements in liquidity position (stable, stressed).

Main instrument of liquidity position management under the stable scenario is a Plan of cash flows defining the cash flow by balance sheet products/instruments and taking into account the plan of future financial operations. The Group determines the balance sheet gaps, payment schedule and need in financing of future operations based on the Plan of cash flows. As a result of application of these instruments, DUAP issues appropriate recommendations to responsible structural divisions.

The Group has implemented a liquidity buffer to manage the Group's liquidity under the stressed scenario. Application of the liquidity buffer enables the Group to promptly monitor the sustainability and stability of the Group's balance sheet structure in case of liquidity shortage that is critical to the Group's solvency.

The liquidity buffer is formed primarily due to liquidity reserves, namely securities recognized in the Group's balance sheet and included in the Lombard lists of the European Central Bank and Bank of Russia. The Group calculates its liquidity reserves as at the reporting date and for the next six monthly reporting dates (forecast). Liquidity buffer may be used to close the negative net position. As at 31 December 2016, the liquidity buffer amounts to EUR 75.9 mln (31 December 2015: EUR 65.1 mln).

The table below shows the contractual expiry by maturity of the Group'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.

	<u>2016</u>	<u>2015</u>
Less than 1 month	33,213	52,376
1 to 3 months	3,650	178
3 months to 1 year	6,138	7,254
1 to 5 years	4,934	3,920
Off-balance credit-related commitments	<u>47,935</u>	<u>63,728</u>

*(Thousands of euros)***23. 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. Quoted available-for-sale debt securities were included in “Less than 1 month” category as they are highly liquid investment securities, which the Group may sell in the short term on the arm-length basis. Available-for-sale investment securities pledged under repurchase agreements are presented on the basis of periods from the reporting date to the expiry date of respective contractual obligations of the Group.

	2016							2015							
	<i>Less than 1 month</i>	<i>1 to 3 months</i>	<i>3 months to 1 year</i>	<i>1 to 5 years</i>	<i>Over 5 years</i>	<i>Past due</i>	<i>Total</i>	<i>Less than 1 month</i>	<i>1 to 3 months</i>	<i>3 months to 1 year</i>	<i>1 to 5 years</i>	<i>Over 5 years</i>	<i>No stated maturity</i>	<i>Past due</i>	<i>Total</i>
Assets															
Cash and cash equivalents	93,031	–	–	–	–	–	93,031	59,519	–	–	–	–	–	–	59,519
Deposits with banks and other financial institutions	14,254	–	27,472	3,611	–	–	45,337	15,352	15,627	54,346	15,067	–	–	–	100,392
Derivative financial instruments	–	116	14,246	–	–	–	14,362	69	–	1,775	–	–	–	–	1,844
Available-for-sale investment securities	170,849	379	502	97,577	–	–	269,307	93,027	230	65	22,733	–	4	–	116,059
Held-to-maturity investment securities	–	–	–	–	–	–	–	64	972	2,981	76,728	42,483	–	–	123,228
Loans to banks	–	3,059	16,638	71,051	3,619	–	94,367	–	3,160	41,112	76,374	19,951	–	–	140,597
Loans to customers	2,066	10,139	59,833	133,047	63,951	–	271,290	982	1,872	26,573	85,268	45,944	–	5,103	165,742
Other financial assets	166	123	381	750	–	–	1,420	69	81	944	–	–	–	–	1,094
Total assets	280,366	13,816	119,072	306,036	67,570	–	786,860	169,082	21,942	127,796	276,170	108,378	4	5,103	708,475
Liabilities															
Due to banks and other financial institutions	(48,558)	–	–	(70,367)	–	–	(118,925)	(28,421)	–	(20,196)	(64,756)	–	–	–	(113,373)
Current customer accounts	(9,218)	–	–	–	–	–	(9,218)	(7,430)	–	–	–	–	–	–	(7,430)
Derivative financial instruments	(2,080)	–	(1,671)	(7,872)	–	–	(11,623)	–	–	(16,191)	(13,707)	–	–	–	(29,898)
Long-term loans of banks	–	–	(14,345)	(59,004)	–	–	(73,349)	(102)	–	(24,529)	(19,556)	–	–	–	(44,187)
Debt securities issued	–	–	(152,484)	(120,044)	–	–	(272,528)	–	–	(40,111)	(172,613)	–	–	–	(212,724)
Other financial liabilities	(348)	–	(933)	(582)	–	–	(1,863)	(43)	(988)	(32)	–	–	–	–	(1,063)
Total liabilities	(60,204)	–	(169,433)	(257,869)	–	–	(487,506)	(35,996)	(988)	(101,059)	(270,632)	–	–	–	(408,675)
Net position	220,162	13,816	(50,361)	48,167	67,570	–	299,354	133,086	20,954	26,737	5,538	108,378	4	5,103	299,800
Accumulated net position	220,162	233,978	183,617	231,784	299,354	299,354		133,086	154,040	180,777	186,315	294,693	294,697	298,800	

*(Thousands of euros)***23. Risk management (continued)****Analysis of financial liabilities by remaining contractual maturities**

The table below summarizes the maturity profile of the Group's financial liabilities at 31 December 2016 and 31 December 2015 based on contractual undiscounted repayment obligations except for gross settled derivatives that are shown by contractual maturity. Debt securities with put options (offers) are presented as if investors will exercise their options at the earliest possible date. The Group expects that it will have to make payment on current bond offers.

<i>At 31 December 2016</i>	<i>Less than 1 month</i>	<i>1 to 3 months</i>	<i>3 to 12 months</i>	<i>1 to 5 years</i>	<i>Total</i>
Financial liabilities					
Due to banks and other financial institutions	48,590	–	–	73,120	121,710
Current customer accounts	–	9,218	–	–	9,218
Net settled derivative liabilities	2,080	–	–	–	2,080
<i>Gross settled derivative financial instruments</i>					
- Contractual amounts payable	–	47,000	147,836	166,726	361,562
- Contractual amounts receivable	–	(47,089)	(173,371)	(173,625)	(394,085)
Long-term loans of banks	–	–	15,078	60,989	76,067
Debt securities issued	–	–	168,367	128,406	296,773
Other liabilities	348	–	933	582	1,863
Total undiscounted financial liabilities	51,018	9,129	158,843	256,198	475,188

<i>At 31 December 2015</i>	<i>Less than 1 month</i>	<i>1 to 3 months</i>	<i>3 to 12 months</i>	<i>1 to 5 years</i>	<i>Total</i>
Financial liabilities					
Due to banks and other financial institutions	–	28,443	20,293	69,386	118,122
Current customer accounts	–	7,430	–	–	7,430
Net settled derivative liabilities	(69)	–	–	–	(69)
<i>Gross settled derivative financial instruments</i>					
- Contractual amounts payable	–	–	118,408	160,641	279,049
- Contractual amounts receivable	–	–	(117,884)	(151,321)	(269,205)
Long-term loans of banks	–	–	23,473	22,303	45,776
Debt securities issued	–	–	50,936	201,220	252,156
Other liabilities	43	988	32	–	1,063
Total undiscounted financial liabilities	(26)	36,861	95,258	302,229	434,322

Market risk

Market risk is the risk that the Group 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 Group 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.

The Finance Committee coordinates the Group's market risk management policy and reviews and provides recommendations on management of market risks to the Management Board.

The Treasury Department performs strategic 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 Group's income on a daily basis.

*(Thousands of euros)***23. Risk management (continued)****Market risk (continued)***Currency risk and price risk*

Currency risk is the risk of loss resulting from adverse changes in exchange rates with respect to the Group'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 Group applies a VaR methodology to assess currency and equity risks. VaR is a method used in measuring maximum risk of the Group, 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 Group 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 Group is carried out in major currencies and financial instruments of the Group attributable to a securities portfolio.

At estimating value at risk, the Group 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 Group 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 Group 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 2016 and 31 December 2015, final data on value at risk assessment (VaR) in relation to currency and price risks assumed by the Group are represented as follows:

	<u>2016</u>	<u>2015</u>
Fixed income securities price risk	2,325	1,536
Currency risk	27	126

Despite the fact that 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.
- ▶ 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 Group'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)***23. Risk management (continued)****Market risk (continued)**

The Group has assets and liabilities denominated in several foreign currencies. The financial position and the cash flows of the Group are exposed to the effects of fluctuations in the prevailing foreign currency exchange rates. Non-monetary financial instruments and financial instruments denominated in functional currency are not exposed to currency risk.

The Group's exposure to currency risk as at 31 December 2016 and 31 December 2015 is presented below:

	2016					2015				
	EUR	USD	RUB	Other currencies	Total	EUR	USD	RUB	Other currencies	Total
Non-derivative financial										
Assets										
Cash and cash equivalents	66,125	19,969	6,778	159	93,031	37,363	20,147	1,907	102	59,519
Deposits with banks and other financial institutions	40,568	4,769	–	–	45,337	99,990	–	402	–	100,392
Available-for-sale investment securities	208,628	53,070	7,609	–	269,307	89,426	26,633	–	–	116,059
Held-to-maturity investment securities	–	–	–	–	–	55,416	63,636	4,176	–	123,228
Long-term loans to banks	53,574	40,793	–	–	94,367	106,063	34,534	–	–	140,597
Loans to customers	131,906	137,130	–	–	269,036	124,751	40,991	–	–	165,742
Other financial assets	225	14	927	254	1,420	483	–	171	440	1,094
Total non-derivative financial assets	501,026	255,745	15,314	413	772,498	513,492	185,941	6,656	542	706,631
Liabilities										
Due to banks and other financial institutions	(36,981)	(81,944)	–	–	(118,925)	(52,785)	(59,706)	(882)	–	(113,373)
Current customer accounts	(9,089)	(129)	–	–	(9,218)	(7,220)	(210)	–	–	(7,430)
Long-term loans of banks	(59,039)	(14,310)	–	–	(73,349)	(7,494)	(36,693)	–	–	(44,187)
Debt securities issued	(30,046)	–	(151,515)	(90,967)	(272,528)	(30,030)	–	(158,099)	(24,595)	(212,724)
Other financial liabilities	(529)	(49)	(1,106)	(179)	(1,863)	(212)	(1)	(818)	(32)	(1,063)
Total non-derivative financial liabilities	(135,684)	(96,432)	(152,621)	(91,146)	(475,883)	(97,741)	(96,610)	(159,799)	(24,627)	(378,777)
Net balance sheet position (excluding derivative financial instruments)	365,342	159,313	(137,307)	(90,733)	296,615	415,751	89,331	(153,143)	(24,085)	327,854
Derivative financial instruments										
Claims	125,117	–	145,832	90,318	361,267	61,068	–	156,879	24,108	242,055
Liabilities	(224,955)	(124,785)	(8,788)	–	(358,528)	(210,884)	(59,225)	–	–	(270,109)
Net balance sheet position including derivative financial instruments	265,504	34,528	(263)	(415)	299,354	265,935	30,106	3,736	23	299,800

*(Thousands of euros)***23. Risk management (continued)****Market risk (continued)*****Interest rate risk***

The Group 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 fluctuations but may also reduce or create losses in the event that unexpected movements arise.

The sensitivity of the consolidated income statement is the effect of the assumed changes in interest rates on net interest income for one year, based on financial assets and financial liabilities with floating rates. The sensitivity of equity is calculated by revaluing inactive traded available-for-sale financial assets with fixed rate as at 31 December 2016 for the effects of the assumed changes in interest rates based on the assumption that there are parallel shifts in the yield curve.

	<i>Increase in basis points</i>	<i>Sensitivity of the income statement</i>	<i>Sensitivity of equity</i>
	2016	2016	2016
RGBEY	1,00%	(956)	(233)
Libor EUR	0,12%	128	–
Libor USD	0,60%	405	–
3Y Swap-RON	0,50%	(1,148)	–
YTM 5Y USTreasuries	0,70%	973	–
YTM 5Y German Treasuries	0,40%	770	–

	<i>Decrease in basis points</i>	<i>Sensitivity of the income statement</i>	<i>Sensitivity of equity</i>
	2016	2016	2016
RGBEY	3,00%	2,868	699
Libor EUR	0,08%	(86)	–
Libor USD	0,08%	(54)	–
3Y Swap-RON	0,50%	1,148	–
YTM 5Y USTreasuries	0,50%	695	–
YTM 5Y German Treasuries	0,40%	(770)	–

	<i>Increase in basis points</i>	<i>Sensitivity of the income statement</i>	<i>Sensitivity of equity</i>
	2015	2015	2015
RGBEY	3,75%	(8,419)	–
Libor EUR	0,25%	367	–
Libor USD	0,50%	(49)	–
3Y Swap-RON	0,90%	(621)	–
YTM 5Y USTreasuries	1,00%	358	–
YTM 5Y German Treasuries	0,50%	1,554	–

	<i>Decrease in basis points</i>	<i>Sensitivity of the income statement</i>	<i>Sensitivity of equity</i>
	2015	2015	2015
RGBEY	3,75%	8,419	–
Libor EUR	0,25%	(367)	–
Libor USD	0,12%	12	–
3Y Swap-RON	0,90%	621	–
YTM 5Y USTreasuries	0,70%	(250)	–
YTM 5Y German Treasuries	0,50%	(1,554)	–

Indices listed in the tables above:

RGBEY – Russian Government Bonds Effective Yield until Redemption;

Libor EUR – London inter-bank EUR offer rate (3 and 6 months);

Libor USD – London inter-bank USD offer rate (1, 3 and 6 months);

3Y Swap-RON – three-year bid rate in Romanian leu on swap market

YTM 5Y USTreasuries – yield-to-maturity of five-year US Treasuries;

YTM 5Y German Treasuries – yield-to-maturity of five-year Germany Treasuries.

(Thousands of euros)

23. Risk management (continued)

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 Group'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 Group continuously seeks to enhance its business processes, operating structure and personnel incentives system in order to minimize the impact of operational risk.

24. Fair value measurements

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 Group 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 Group 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 that use inputs which have a significant effect on the recognized fair value that are not based on observable market data.

*(Thousands of euros)***24. Fair value measurements (continued)****Fair value hierarchy (continued)**

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

	<i>Valuation date</i>	<i>Level 1 2016</i>	<i>Level 2 2016</i>	<i>Level 3 2016</i>	<i>Total 2016</i>
Assets measured at fair value					
Derivative financial assets	31 December 2016	–	14,362	–	14,362
Government bonds of member countries	31 December 2016	70,561	–	–	70,561
Corporate bonds	31 December 2016	194,003	4,739	–	198,742
Quoted equity instruments	31 December 2016	–	4	–	4
Investment property	31 December 2016	–	–	21,840	21,840
Property and equipment – buildings	31 December 2016	–	–	67,527	67,527
Liabilities measured at fair value					
Derivative financial liabilities	31 December 2016	–	11,623	–	11,623
Assets for which fair values are disclosed					
Cash and cash equivalents	31 December 2016	104	92,927	–	93,031
Deposits with banks and other financial institutions	31 December 2016	–	–	45,337	45,337
Loans to banks	31 December 2016	–	–	88,558	88,558
Loans to customers	31 December 2016	–	–	270,243	270,243
Liabilities for which fair values are disclosed					
Due to banks and other financial institutions	31 December 2016	–	–	118,925	118,925
Current customer accounts	31 December 2016	–	–	9,218	9,218
Long-term loans of banks	31 December 2016	–	–	73,349	73,349
Debt securities issued	31 December 2016	–	279,181	–	279,181

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*(Thousands of euros)***24. Fair value measurements (continued)****Fair value hierarchy (continued)**

The following table shows an analysis of financial instruments recorded at fair value by level of the fair value hierarchy as at 31 December 2015:

	<i>Valuation date</i>	<i>Level 1 2015</i>	<i>Level 2 2015</i>	<i>Level 3 2015</i>	<i>Total 2015</i>
Assets measured at fair value					
Derivative financial assets	31 December 2015	–	1,844	–	1,844
Government bonds of member countries and bonds of regional governments	31 December 2015	114,673	–	–	114,673
Corporate bonds	31 December 2015	1,382	–	–	1,382
Quoted equity instruments	31 December 2015	–	4	–	4
Investment property	31 December 2015	–	–	33,819	33,819
Property and equipment – buildings	31 December 2015	–	–	62,807	62,807
Liabilities measured at fair value					
Derivative financial liabilities	31 December 2015	–	29,898	–	29,898
Assets for which fair values are disclosed					
Cash and cash equivalents	31 December 2015	66	59,453	–	59,519
Deposits with banks and other financial institutions	31 December 2015	–	–	100,392	100,392
Held-to-maturity investment securities	31 December 2015	114,876	–	–	114,876
Long-term loans to banks	31 December 2015	–	–	139,891	139,891
Loans to customers	31 December 2015	–	–	165,742	165,742
Liabilities for which fair values are disclosed					
Due to banks and other financial institutions	31 December 2015	–	–	113,373	113,373
Current customer accounts	31 December 2015	–	–	7,430	7,430
Long-term loans of banks	31 December 2015	–	–	44,187	44,187
Debt securities issued	31 December 2015	–	214,734	–	214,734

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(Thousands of euros)

24. Fair value measurements (continued)**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 Group's financial instruments that are recorded in the consolidated financial statements. The table does not include the fair values of non-financial assets and non-financial liabilities.

	<i>Carrying amount 2016</i>	<i>Fair value 2016</i>	<i>Unrecognized gain/(loss) 2016</i>	<i>Carrying amount 2015</i>	<i>Fair value 2015</i>	<i>Unrecognized gain/(loss) 2015</i>
Financial assets						
Cash and cash equivalents	93,031	93,031	–	59,519	59,519	–
Deposits with banks and other financial institutions	45,337	45,337	–	100,392	100,392	–
Held-to-maturity investment securities	–	–	–	123,228	114,876	(8,352)
Long-term loans to banks	94,367	88,558	(5,809)	140,597	139,891	(706)
Loans to customers	269,036	270,243	1,207	165,742	165,742	–
Financial liabilities						
Due to banks and other financial institutions	118,925	118,925	–	113,373	113,373	–
Current customer accounts	9,218	9,218	–	7,430	7,430	–
Long-term loans of banks	73,349	73,349	–	44,187	44,187	–
Debt securities issued	272,528	279,181	(6,653)	212,724	214,734	(2,010)
Total unrecognized change in unrealized fair value			(11,255)			(11,068)

Fair value measurements

The Group determines the policies and procedures for both recurring fair value measurement, such as unquoted derivatives, investment property and buildings, and for non-recurring measurement, such as inventories.

External appraisers are involved for valuation of significant assets, such as building and property. Involvement of external appraisers is decided upon by the Group's Finance Department. Unquoted derivatives are measured by the Finance Department.

Selection criteria include market knowledge, reputation, independence and compliance with professional standards.

Methodologies and assumptions

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

Assets for which fair value approximates their carrying amount

For financial assets and financial liabilities that are liquid or have 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 as at 31 December 2016 and 31 December 2015 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 existing practice of renegotiating interest rates to reflect current market conditions, and, therefore, a majority of balances carries interest at rates approximating market interest rates.

(Thousands of euros)

24. Fair value measurements (continued)

Methodologies and assumptions (continued)

Financial instruments with fixed and floating rate

The fair value of instruments with floating interest rates is approximately equal to their carrying amount. In case of significant changes of the market situation the interest rates on loans to customers and banks, and long-term loans of banks at a fixed interest rate may be revised. Consequently the interest rates on the financial instruments issued or received shortly before the balance sheet date are not significantly different from the current interest rates for new instruments with similar credit risk and a similar maturity. If the Group determines that the rates for loans issued or borrowings are significantly different from the current market rates, the Group determines the fair value of such loans issued and borrowings. The valuation is based on discounted cash flow method using current market interest rates for the financial instruments with similar credit risk and similar maturity. The discount rates depend on the currency, the maturity of the instrument and the credit risk of the counterparty. The Group determines that the fair value of due to banks and other financial institutions and long-term loans of banks did not differ significantly from their carrying amounts as at 31 December 2016 and 31 December 2015.

Investment property

The Group engages an independent appraiser for the investment property fair value measurement. As at the valuation date (31 December 2016), the fair values of investment property were based on the results of valuation performed by an accredited independent appraiser and the prices of market transactions using the market, cost and income approaches to fair value measurement.

The duration of the cash flows and the specific timing of inflows and outflows are determined by events such as rent reviews, lease renewal and related re-letting, redevelopment, or refurbishment. The appropriate duration is typically driven by market behavior that is a characteristic of the class of real property. Periodic cash flow is typically estimated as gross income less vacancy, non-recoverable expenses, collection losses, lease incentives, maintenance cost, agent and commission costs and other operating and management expenses. The series of periodic net operating income, along with an estimate of the terminal value anticipated at the end of the projection period, is then discounted.

Property and equipment - buildings

Fair value of the properties was determined using the market approach. This means that valuations performed by the appraiser are based on market transaction prices, significantly adjusted for difference in the nature, location or condition of the specific property. As at the valuation date (31 December 2016), the properties' fair values are based on valuations performed by an accredited independent appraiser and the prices of market transactions using the market, cost and income approaches to fair value measurement.

Significant unobservable inputs in determining the fair value of real estate properties

As at the valuation date (31 December 2016), the significant unobservable inputs used in determining the fair value of real estate properties included the average asking prices for sale of similar properties ranging from EUR 3,094 per sq. m (range minimum) to EUR 4,186 per sq. m (range maximum), and lease rates ranging from EUR 371 per sq. m. a year (minimum) to EUR 407 per sq. m. a year (maximum).

There were no transfers of financial instruments between level 1 and level 2 in 2016 and 2015.

(Thousands of euros)

24. Fair value measurements (continued)**Movements in level 3 assets and liabilities at fair value**

The following table shows a reconciliation of the opening and closing amount of Level 3 assets and liabilities that are recorded at fair value:

	<i>At 1 January 2016</i>	<i>Gains/(losses) recorded in profit or loss</i>	<i>Gains/(losses) recorded in comprehensive income</i>	<i>Purchases</i>	<i>Transfer in property and equipment</i>	<i>At 31 December 2016</i>
Assets						
Property and equipment – buildings	62,807	(1,174)	(18,508)	223	24,179	67,527
Investment property	33,819	(2,174)	–	14,374	(24,179)	21,840
Total	96,626	(3,348)	(18,508)	14,597	–	89,367
	<i>At 1 January 2015</i>	<i>Gains/(losses) recorded in profit or loss</i>	<i>Gains/(losses) recorded in comprehensive income</i>	<i>Purchases</i>	<i>Transfer in property and equipment</i>	<i>At 31 December 2015</i>
Assets						
Property and equipment – buildings	50,739	(935)	(3,642)	52	16,593	62,807
Investment property	52,879	(2,500)	–	33	(16,593)	33,819
Total	103,618	(3,435)	(3,642)	85	–	96,626

25. Transferred financial assets that are not derecognized

The table below provides a summary of the financial assets transferred by the Group in such a way that all the transferred financial assets do not qualify for derecognition:

	<i>Available-for-sale investment securities</i>		<i>Held-to-maturity investment securities</i>		<i>Total</i>
	<i>Government eurobonds</i>	<i>Corporate bonds</i>	<i>Government eurobonds</i>	<i>Corporate bonds</i>	
<i>Transferred financial asset</i>	<i>2016</i>	<i>2016</i>	<i>2016</i>	<i>2016</i>	<i>2016</i>
Carrying amount of assets	17,883	80,575	–	–	98,458
Carrying amount of associated liabilities	(13,485)	(52,584)	–	–	(66,069)
Net position	4,398	27,991	–	–	32,389
	<i>Available-for-sale investment securities</i>		<i>Held-to-maturity investment securities</i>		<i>Total</i>
	<i>Government bonds of member countries</i>	<i>Corporate bonds</i>	<i>Government bonds of member countries</i>	<i>Corporate bonds</i>	
<i>Transferred financial asset</i>	<i>2015</i>	<i>2015</i>	<i>2015</i>	<i>2015</i>	<i>2015</i>
Carrying amount of assets	21,646	1,382	10,489	62,705	96,222
Carrying amount of associated liabilities	(16,350)	(930)	(6,998)	(40,478)	(64,756)
Net position	5,296	452	3,491	22,227	31,466

(Thousands of euros)

25. Transferred financial assets that are not derecognized (continued)

Securities sold under repurchase agreements are transferred to a third party and the Group receives cash in exchange. If the securities increase or decrease in value, the Group may, in certain circumstances, require, or be required, to pay additional collateral in the form of cash and/or other securities. The Group has determined that it retains substantially all the risks and rewards of these securities, which include credit risk, market risk, country risk and operational risk, and therefore has not derecognized them. In addition, it recognizes a financial liability for cash received.

The fair value of investment securities available for sale sold under repurchase agreements is equal to their carrying amount (Note 24).

The related liabilities, which are recorded against the cash received for such transactions, are presented in amounts due to banks and other financial institutions in the consolidated statement of financial position as at 31 December 2016 (as at 31 December 2015: in amounts due to banks and other financial institutions).

26. Segment information

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

Credit investment activity	Investment banking services, including long-term corporate and interbank financing
Treasury	Operations in financial markets, transactions with securities, derivative financial instruments and foreign currency, and liquidity management
Other operations	Operational leasing services, 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 consolidated financial statements. The following table presents revenue, income, assets and liabilities of the Group's operating segments:

2016	<i>Credit investment activity</i>	<i>Treasury</i>	<i>Other operations</i>	<i>Total</i>
Income				
External customers				
Interest income	20,348	12,093	14	32,455
Net gains from trading in foreign currencies and operations with derivatives	–	9,068	–	9,068
Net gains from revaluation of derivative financial instruments	–	36,679	–	36,679
Net gains from available-for-sale investment securities	–	10,515	–	10,515
Net gains from held-to-maturity investment securities	–	616	–	616
Reversal of allowance for loan impairment	–	–	89	89
Income from lease of investment property	–	–	3,442	3,442
Reversal of allowance for impairment of other assets	–	–	67	67
Other segment income	241	–	430	671
Total income	20,589	68,971	4,042	93,602
Interest expenses	(11,250)	(16,401)	–	(27,651)
Net loss from revaluation of derivative financial instruments	–	(4,349)	–	(4,349)
Net losses from revaluation of assets and liabilities in foreign currencies	–	(31,119)	(54)	(31,173)
Net losses from revaluation of hedging instruments	–	(246)	–	(246)
Allowance for impairment of financial assets	(7,646)	–	–	(7,646)
Net losses from revaluation of investment property	–	–	(2,174)	(2,174)
Other segment expenses	(167)	(196)	(259)	(622)
Segment results	1,526	16,660	1,555	19,741
Other unallocated expenses				(18,939)
Profit for the period				802
Development Portfolio	363,403	68,349	–	431,752
Other segment assets	–	353,239	96,425	449,691
Total segment assets	363,403	421,588	96,425	881,443
Total segment liabilities	160,065	325,579	5,581	491,225
Other segment information				
Capital expenditures	–	–	1,065	1,065

The Group's management separates the "Development portfolio" assets allocated within operating segments. The criteria of separation is orientation of the assets on the fulfilling of the Group's mission. "Development Portfolio" includes loans to banks and loans to customers excluding impaired loan projects and the investments in debt securities purchased upon initial placement by the issuer..

(Thousands of euros)

26. Segment information (continued)

<i>2015</i>	<i>Credit investment activity</i>	<i>Treasury</i>	<i>Other operations</i>	<i>Total</i>
Income				
External customers				
Interest income	15,080	11,904	148	27,132
Net gains from revaluation of assets and liabilities in foreign currencies	–	22,614	369	22,983
Net gains from available-for-sale investment securities	–	3,204	–	3,204
Net gains from held-to-maturity investment securities	–	45	–	45
Income from lease of investment property	–	–	5,214	5,214
Recovery of provision	–	–	89	89
Other segment income	460	–	79	539
Total income	15,540	37,767	5,899	59,206
Interest expenses	(7,260)	(10,484)	–	(17,744)
Net losses from trading in foreign currencies	–	(5,302)	(25)	(5,327)
Net losses from revaluation of derivative financial instruments	–	(6,661)	–	(6,661)
Net loss from trading in foreign currencies and operations with derivatives	–	(5,302)	–	(5,302)
Allowance for loan impairment	(6,166)	–	–	(6,166)
Net losses from revaluation of investment property	–	–	(2,500)	(2,500)
Other segment expenses	–	(114)	(1,755)	(1,869)
Segment results	2,114	15,206	1,644	18,964
Other unallocated expenses				(16,908)
Profit for the year				2,056
Development Portfolio	301,236	–	–	301,236
Other segment assets	5,103	400,201	102,863	508,167
Total segment assets	306,339	400,201	102,863	809,403
Total segment liabilities	116,138	291,474	4,088	411,700
Other segment information				
Capital expenditures	–	–	85	85

In 2016, the Group's revenue from lease operations with two external counterparties (2015: one external counterparty) exceeded 20% of the Group's total revenue (2016: EUR 2,160 thousand; 2015: EUR 3,196 thousand).

Geographical information

Allocation of the Group's revenue from transactions with external customers and non-current assets based on the location of these customers and assets for the years ended 31 December 2016 and 31 December 2015 is presented in the table below:

	<i>2016</i>				<i>2015</i>			
	<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	7,760	16,095	8,600	32,455	12,147	11,721	3,264	27,132
Income from lease of investment property	3,442	–	–	3,442	5,214	–	–	5,214
Non-current assets	79,245	14,439	–	93,684	100,212	–	–	100,212

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

(Thousands of euros)

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

The geographical concentration of the Group's assets and liabilities based on the location of the Group's counterparties as at 31 December 2016 is presented below:

	2016									
	<i>Russian Federation</i>	<i>Republic of Bulgaria</i>	<i>Romania</i>	<i>Slovak Republic</i>	<i>Hungary</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	16,398	808	26	38	–	–	–	–	75,761	93,031
Deposits with banks and other financial institutions	7,159	–	–	–	–	–	–	–	38,178	45,337
Derivative financial instruments	2,980	–	–	–	–	–	–	–	11,382	14,362
Available-for-sale investment securities	44,688	49,482	36,713	10,286	3,475	–	–	–	124,663	269,307
Long-term loans to banks and trade financing loans less allowances for impairment	27,378	–	–	–	–	47,970	19,019	–	–	94,367
Loans to customers less allowances for impairment	61,213	58,967	37,981	308	–	5,683	–	22,930	81,954	269,036
Other financial assets	1,407	8	–	1	–	–	–	–	4	1,420
Assets	161,223	109,256	74,720	10,633	3,475	53,653	19,019	22,930	331,942	786,860
Liabilities										
Due to banks and other financial institutions	–	–	–	7,508	–	–	–	–	111,417	118,925
Derivative financial instruments	4,528	–	633	–	–	–	–	–	6,462	11,623
Long-term loans of banks	9,840	21,690	–	–	7,380	–	–	–	34,439	73,349
Long-term securities issued	151,434	–	90,967	30,127	–	–	–	–	–	272,528
Other financial liabilities	1,805	–	–	19	–	–	–	–	39	1,863
Liabilities	167,607	21,690	91,600	37,654	7,380	–	–	–	152,357	478,288

(Thousands of euros)

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

	<i>2015</i>									
	<i>Russian Federation</i>	<i>Republic of Bulgaria</i>	<i>Romania</i>	<i>Slovak Republic</i>	<i>Hungary</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	2,026	219	17	15	–	–	–	–	57,242	59,519
Deposits with banks and other financial institutions	6,049	–	–	–	–	30,539	–	–	63,804	100,392
Derivative financial instruments	669	–	–	–	–	–	–	–	1,175	1,844
Investment securities:										
- available-for-sale	–	26,889	31,150	13,208	12,056	13,746	11,506	6,118	1,386	116,059
- held-to-maturity	105,785	–	–	–	–	–	–	–	17,443	123,228
Long-term loans to banks less allowances for impairment	64,223	–	–	–	–	43,044	33,330	–	–	140,597
Loans to customers less allowances for impairment	28,160	51,162	25,844	20,437	–	21,890	–	–	18,249	165,742
Assets	206,912	78,270	57,011	33,660	12,056	109,219	44,836	6,118	159,299	707,381
Liabilities										
Due to banks and other financial institutions	992	–	–	7,508	–	–	–	20,086	84,787	113,373
Derivative financial instruments	18,723	–	864	–	–	–	–	–	10,311	29,898
Long-term loans of banks	22,953	13,740	–	7,494	–	–	–	–	–	44,187
Long-term securities issued	158,067	–	24,557	30,100	–	–	–	–	–	212,724
Liabilities	200,735	13,740	25,421	45,102	–	–	–	20,086	95,098	400,182

Other countries include non-member countries.

(Thousands of euros)

27. Offsetting of financial instruments

The table below shows the effect of enforceable master netting agreements and similar arrangements that do not result in an offset in the consolidated statement of financial position as at 31 December 2016:

	<i>Gross amount of recognized financial assets</i>	<i>Gross amount of recognized financial liabilities set off in the statement of financial position</i>	<i>Net amount of financial assets presented in the statement of financial position</i>	<i>Related amounts not set off in the statement of financial position</i>		<i>Net amount</i>
				<i>Financial instruments</i>	<i>Cash collateral received</i>	
2016						
Financial assets						
Financial assets pledged under repurchase agreements	98,458	–	98,458	(66,069)	–	32,389
Total	98,458	–	98,458	(66,069)	–	32,389
Financial liabilities						
Repurchase agreements with banks	66,069	–	66,069	(66,069)	–	–
Total	66,069	–	66,069	(66,069)	–	–

The table below shows financial assets offset against financial liabilities in the consolidated statement of financial position, as at 31 December 2015 as well as the effect of enforceable master netting agreements and similar arrangements that do not result in an offset in the consolidated statement of financial position:

	<i>Gross amount of recognized financial assets</i>	<i>Gross amount of recognized financial liabilities set off in the statement of financial position</i>	<i>Net amount of financial assets presented in the statement of financial position</i>	<i>Related amounts not set off in the statement of financial position</i>		<i>Net amount</i>
				<i>Financial instruments</i>	<i>Cash collateral received</i>	
2015						
Financial assets						
Financial assets pledged under repurchase agreements	96,222	–	96,222	(64,756)	–	31,466
Total	96,222	–	96,222	(64,756)	–	31,466
Financial liabilities						
Repurchase agreements with banks	64,756	–	64,756	(64,756)	–	–
Total	64,756	–	64,756	(64,756)	–	–

*(Thousands of euros)***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 expenses and income for 2016 and 2015 are as follows:

	<i>Related party</i>	<i>31 December 2016 Carrying amount</i>	<i>31 December 2015 Carrying amount</i>
Consolidated statement of financial position			
Current customer accounts	Key management personnel	1,783	1,897
Other non-financial liabilities	Key management personnel	416	493
	<i>Related party</i>	<i>2016 Income/ (expense)</i>	<i>2015 Income/ (expense)</i>
Consolidated income statement			
Interest expenses on current customer accounts	Key management personnel	(61)	(95)
Net interest expenses after allowance for impairment of loans		(61)	(95)
Operating expenses		(61)	(95)
Employee benefits	Key management personnel	(1,365)	(1,524)
Compensation for travel expenses and medical insurance	Key management personnel	(55)	(89)
Operating expenses		(1,420)	(1,613)
Net (loss)/profit for the year		(1,481)	(1,708)

29. Capital adequacy

Capital adequacy ratio is the most important financial indicator characterizing credibility of 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 Supervision recommends maintaining the ratio of capital to risk-weighted assets ("capital adequacy ratio") above the prescribed minimum level. As at 31 December 2016, this minimum level was 8% (2015: 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 for the Group at the level of not less than 25% as at 31 December 2016 (2015: 25%).

*(Thousands of euros)***29. Capital adequacy (continued)**

The following table shows the composition of the Group's capital position computed in accordance with the Basel Accord (Basel II) as at 31 December 2016 and 31 December 2015.

	<u>2016</u>	<u>2015</u>
Capital		
Tier 1 capital	378,034	365,978
Tier 2 capital	11,439	29,789
Total regulatory capital	<u>389,473</u>	<u>395,767</u>
Risk-weighted assets		
Credit risk	482,693	560,094
Market risk	186,588	70,461
Operational risk	57,999	55,548
Total risk-weighted assets	<u><u>727,280</u></u>	<u><u>686,103</u></u>
Total capital expressed as a percentage of risk-weighted assets, % ("capital adequacy ratio")	53.55%	57.68%
Total tier 1 capital expressed as a percentage of risk-weighted assets, % ("tier 1 capital adequacy ratio-")	51.98%	53.34%

(The end)

Independent auditor's report
on the consolidated financial statements of the
International Investment Bank
and its subsidiary
for 2017

February 2018

**Independent auditor's report
on the consolidated financial statements of the
International Investment Bank and its subsidiary**

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Independent auditor's report

To the Council of the International Investment Bank

Opinion

We have audited the consolidated financial statements of International Investment Bank (the "Bank") and its subsidiary (the "Group"), which comprise the consolidated statement of financial position as at 31 December 2017, and the consolidated income statement, consolidated statement of comprehensive income, consolidated statement of changes in equity and consolidated statement of cash flows for 2017, and notes to the consolidated financial statements, including a summary of significant accounting policies.

In our opinion, the accompanying consolidated financial statements present fairly, in all material respects, the financial position of the Group as at 31 December 2017 and its financial performance and its cash flows for 2017 in accordance with International Financial Reporting Standards (IFRSs).

Basis for opinion

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

Key audit matters

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

We have fulfilled the responsibilities described in the *Auditor's responsibilities for the audit of the consolidated financial statements* section of our report, including in relation to these matters. Accordingly, our audit included the performance of procedures designed to respond to our assessment of the risks of material misstatement of the consolidated financial statements. The results of our audit procedures, including the procedures performed to address the matters below, provide the basis for our audit opinion on the accompanying consolidated financial statements.

Key audit matter	How the relevant key audit matter was considered during our audit
<p><i>Provisions for impairment of loans to banks and loans to customers</i></p>	
<p>The assessment of provisions for impairment of loans to banks and loans to customers is a key area of judgement for management of the Group. The identification of impairment and the determination of the recoverable amount are processes involving significant use of judgements, various assumptions and factors including the financial standing of borrowers and expected future cash flows. Information on the impairment of loans to banks and customers is included in Note 9, Loans to banks, Note 10, Loans to customers and Note 23, Risk management, to the consolidated financial statements. The use of different models and assumptions could produce significantly different estimates of impairment of loans to banks and customers. Due to materiality of the loans to banks and customers represented 61% of the total assets and significant use of professional judgement the assessment of provisions for impairment was the key audit matter.</p>	<p>Our audit strategy for the impairment of loans to banks and loans to customers was founded on substantive procedures. Our audit procedures included an evaluation of the methodology of the assessment of provisions, testing of inputs, evaluation of the assumptions used by the Group in the calculation of the impairment and the assessment of the adequacy of provisions for loans to banks and customers with individual signs of impairment. We analyzed expected future cash flows in respect of significant individually impaired loans to banks and customers.</p> <p>We have also fulfilled the procedures for information on provisions for impairment of loans to banks and customers disclosed in Notes 9, 10 and 23 to the Group's consolidated financial statements.</p>

Other information included in the Group's Annual Report for 2017

Other information consists of the information included in the Annual Report of International Investment Bank for 2017 other than the consolidated financial statements and our auditor's report thereon. Management is responsible for the other information. The Annual Report of International Investment Bank for 2017 is expected to be made available to us after the date of this auditor's report.

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

In connection with our audit of the consolidated financial statements, our responsibility is to read the other information identified above when it becomes available and, in doing so, consider whether the other information is materially inconsistent with the consolidated financial statements or our knowledge obtained in the audit or otherwise appears to be materially misstated.

Responsibilities of management and Council of the International Investment Bank for the consolidated financial statements

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

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

Council of the International Investment Bank are responsible for overseeing the Group's financial reporting process.

Auditor's responsibilities for the audit of the consolidated financial statements

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

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

- ▶ Identify and assess the risks of material misstatement of the consolidated financial statements, whether due to fraud or error, design and perform audit procedures responsive to those risks, and obtain audit evidence that is sufficient and appropriate to provide a basis for our opinion. The risk of not detecting a material misstatement resulting from fraud is higher than for one resulting from error, as fraud may involve collusion, forgery, intentional omissions, misrepresentations, or the override of internal control.
- ▶ Obtain an understanding of internal control relevant to the audit in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Group's internal control.
- ▶ Evaluate the appropriateness of accounting policies used and the reasonableness of accounting estimates and related disclosures made by management.
- ▶ Conclude on the appropriateness of management's use of the going concern basis of accounting and, based on the audit evidence obtained, whether a material uncertainty exists related to events or conditions that may cast significant doubt on the Group's ability to continue as a going concern. If we conclude that a material uncertainty exists, we are required to draw attention in our auditor's report to the related disclosures in the consolidated financial statements or, if such disclosures are inadequate, to modify our opinion. Our conclusions are based on the audit evidence obtained up to the date of our auditor's report. However, future events or conditions may cause the Group to cease to continue as a going concern.



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Совершенство в бизнесе,
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- ▶ Evaluate the overall presentation, structure and content of the consolidated financial statements, including the disclosures, and whether the consolidated financial statements represent the underlying transactions and events in a manner that achieves fair presentation.

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

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

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

The partner in charge of the audit resulting in this independent auditor's report is O.V. Youshenkov.

O.V. Youshenkov
Partner
Ernst & Young Vneshaudit LLC

15 February 2018

Details of the audited entity

Name: International Investment Bank
Bank operates on the basis of the Agreement on the Establishment of the International Investment Bank dated 10 July 1970, registered in the UN Secretariat on 1 December 1971 under No. 11417.
Address: Russia 107078, Moscow, Mashk Poryvaevoy str., 7.

Details of the auditor

Name: Ernst & Young Vneshaudit LLC
Record made in the State Register of Legal Entities on 4 February 2016, State Registration Number 1167746123478.
Address: Russia 115035, Moscow, Sadovnicheskaya naberezhnaya, 77, building 1.
Ernst & Young Vneshaudit LLC is a member of Self-regulated organization of auditors "Russian Union of auditors" (Association) ("SRO RUA"). Ernst & Young Vneshaudit LLC is included in the control copy of the register of auditors and audit organizations, main registration number 11603050953.

CONSOLIDATED STATEMENT OF FINANCIAL POSITION**As at 31 December 2017***(Thousands of euros)*

	<i>Note</i>	<i>31 December 2017</i>	<i>31 December 2016</i>
Assets			
Cash and cash equivalents	5	66,097	93,031
Deposits with banks and other financial institutions	6	45,889	45,337
Derivative financial assets	7	7,761	14,362
Available-for-sale investment securities	8	138,704	170,849
Available-for-sale investment securities pledged under repurchase agreements	8	76,723	98,458
Loans to banks	9	201,635	94,367
Loans to customers	10	462,514	269,036
Investment property	11	21,853	21,840
Property, equipment and intangible assets	12	72,388	71,844
Other assets	13	2,476	2,319
Total assets		1,096,040	881,443
Liabilities			
Due to banks and other financial institutions	14	65,511	118,925
Derivative financial liabilities	7	15,073	11,623
Current customer accounts		8,593	9,218
Long-term loans of banks	15	95,592	73,349
Debt securities issued	16	509,213	272,528
Other liabilities	13	6,396	5,582
Total liabilities		700,378	491,225
Equity			
Subscribed capital	17	1,300,000	1,300,000
Callable capital		(985,038)	(986,947)
Paid-in capital		314,962	313,053
Revaluation reserve for available-for-sale investment securities		240	(1,506)
Revaluation reserve for property and equipment		13,748	12,945
Foreign currency translation reserve		(76)	(57)
Retained earnings less net income for the year		65,783	64,981
Net income for the year		1,005	802
Total equity		395,662	390,218
Total equity and liabilities		1,096,040	881,443

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

Nikolay Kosov



Chairman of the Board

Elena Minduksheva



Acting Deputy Director of the Finance Department

14 February 2018

The accompanying notes 1-30 are an integral part of these consolidated financial statements.

CONSOLIDATED INCOME STATEMENT**Year ended 31 December 2017***(Thousands of euros)*

	<i>Note</i>	<i>2017</i>	<i>2016</i>
Interest income	20	35,963	32,455
Interest expenses	20	(32,566)	(27,651)
Net interest income		3,397	4,804
Allowance for loan impairment	10, 11	(12,165)	(7,557)
Net interest expense after allowance for loan impairment		(8,768)	(2,753)
Fee and commission income		1,763	843
Fee and commission expense		(133)	(138)
Net fee and commission income		1,630	705
Net gains from operations in foreign currencies and with derivatives	21	15,949	9,979
Net gains from available-for-sale investment securities		7,399	10,515
Dividend income		123	–
Income from lease of investment property	19	4,034	3,442
Losses from revaluation of investment property	11	(26)	(2,174)
Other income		543	447
Net non-interest income		28,022	22,209
Operating income		20,884	20,161
Reversal of allowance for impairment of other assets	13	29	67
General and administrative expenses	22	(18,872)	(18,939)
Other operating expenses on banking operations		(1,036)	(487)
Operating expenses		(19,879)	(19,359)
Net income for the year		1,005	802

The accompanying notes 1-30 are an integral part of these consolidated financial statements.

CONSOLIDATED STATEMENT OF COMPREHENSIVE INCOME**Year ended 31 December 2017***(Thousands of euros)*

	<i>Note</i>	<i>2017</i>	<i>2016</i>
Net income for the year		1,005	802
Other comprehensive income			
<i>Other comprehensive income/(loss) to be reclassified to profit or loss in subsequent periods</i>			
Change in unrealized revaluation of available-for-sale investment securities	17	1,746	158
Translation differences		(19)	63
Net other comprehensive income to be reclassified to profit or loss in subsequent periods		1,727	221
<i>Other comprehensive income/(loss), not to be reclassified to profit or loss in subsequent periods</i>			
Revaluation of property and equipment	12	803	(18,508)
Net other comprehensive income/(loss) not to be reclassified to profit or loss in subsequent periods		803	(18,508)
Other comprehensive income/(loss)		2,530	(18,287)
Total income/(loss) for the year		3,535	(17,485)

The accompanying notes 1-30 are an integral part of these consolidated financial statements.

CONSOLIDATED STATEMENT OF CHANGES IN EQUITY**Year ended 31 December 2017***(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>Foreign currency translation reserve</i>	<i>Retained earnings</i>	<i>Total equity</i>
At 31 December 2015	1,300,000	(996,947)	(1,664)	31,453	(120)	64,981	397,703
Profit for the year	–	–	–	–	–	802	802
Other comprehensive income/(loss) for the year	–	–	158	(18,508)	63	–	(18,287)
Total comprehensive income/(loss)	–	–	158	(18,508)	63	802	(17,485)
Contributions to capital (Note 18)	–	10,000	–	–	–	–	10,000
At 31 December 2016	1,300,000	(986,947)	(1,506)	12,945	(57)	65,783	390,218
Profit for the year	–	–	–	–	–	1,005	1,005
Other comprehensive income/(loss) for the year	–	–	1,746	803	(19)	–	2,530
Total comprehensive income/(loss)	–	–	1,746	803	(19)	1,005	3,535
Contributions to capital (Note 18)	–	1,909	–	–	–	–	1,909
At 31 December 2017	1,300,000	(985,038)	240	13,748	(76)	66,788	395,662

The accompanying notes 1-30 are an integral part of these consolidated financial statements.

CONSOLIDATED STATEMENT OF CASH FLOWS**Year ended 31 December 2017***(Thousands of euros)*

	<i>Note</i>	2017	2016
Cash flows from operating activities			
Interest, fees and commissions received		28,578	24,092
Interest, fees and commissions paid		(3,327)	(3,364)
Realized gains less losses from dealing in foreign currencies and operations with derivatives		31,228	9,079
Cash flows from lease of investment property		4,034	3,442
General and administrative expenses		(15,638)	(16,094)
Other operating income/(expenses) on banking operations		36	(78)
Cash flows from operating activities before changes in operating assets and liabilities		44,911	17,077
<i>Net (increase)/decrease in operating assets</i>			
Deposits with banks and other financial institutions		(5,776)	54,498
Loans to banks		(118,882)	47,598
Loans to customers		(210,605)	(118,231)
Other assets		(15)	(5)
<i>Net increase/(decrease) in operating liabilities</i>			
Due to banks and other financial institutions		(47,426)	1,589
Current customer accounts		(1,227)	1,481
Other liabilities		1,016	68
Net cash flows from operating activities		(338,004)	4,075
Cash flows from investing activities			
Interest received		6,491	11,458
Purchase of available-for-sale investment securities		(426,482)	(668,584)
Proceeds from sale and redemption of available-for-sale investment securities		478,424	618,419
Proceeds from sale and redemption of held-to-maturity investment securities		–	30,373
Investments in investment property		(39)	(50)
Acquisition of property, equipment and intangible assets		(1,673)	(1,754)
Net cash flows from investing activities		56,721	(10,138)
Cash flows from financing activities			
Interest paid		(26,212)	(26,324)
Long-term interbank financing raised	29	36,185	60,000
Long-term interbank financing repaid	29	(13,451)	(29,569)
Placement of bonds	29	348,661	67,398
Redemption of bonds	29	(88,290)	(43,910)
Contributions to capital		1,909	10,000
Net cash flows from financing activities		258,802	37,595
Effect of exchange rate changes on cash and cash equivalents		(4,453)	1,980
Net increase/(decrease) in cash and cash equivalents		(26,934)	33,512
Cash and cash equivalents, beginning		93,031	59,519
Cash and cash equivalents, ending	5	66,097	93,031

The accompanying notes 1-30 are an integral part of these consolidated financial statements.

(Thousands of euros)

1. Principal activities

These consolidated financial statements include the financial statements of the International Investment Bank (the “Bank”, or “IIB”) and CJSC IIB Capital, the subsidiary of the Bank. The Bank and its subsidiary are hereinafter collectively referred to as the “Group”. The International Investment Bank is the parent company of the Group. Information on the subsidiary of the Bank is presented in Note 2.

The International Investment 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 Statute. 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 Group also performs transactions with securities and foreign currency. The Group operates from its office at 7 Mashki Poryvaevoy St., Moscow, Russia, and the European regional office in Bratislava (Eurovea Central 1, Pribinova 4, Bratislava, 81109, Slovak Republic).

The Group had an average of 220 staff employees during 2017 (2016: 230).

On 31 July 2014, the EU Council imposed sectoral sanctions against Russia. The preamble of the Decision of the EU Council of 31 July 2014 (paragraph 9) and Council Regulation (EU) No. 833/2014 of 31 July 2014 (paragraph 5), which was developed based on the Decision, emphasize that the sanctions do not cover Russia-based institutions with international status established by intergovernmental agreements in which Russia is one of the parties. Therefore, the IIB is directly excluded from the list of financial institutions to which restrictions apply.

The Group continues to expand its operations in accordance with its mandate and strategic objectives established by the member countries

- ▶ The Bank winds up the introduction of changes to its constituent documents and implementation of the three-level corporate governance structure. The Protocol on Introducing Changes to the Agreement on the Establishment of the International Investment Bank and the Statutes (hereinafter, the “Protocol”) signed at the end of 2015 is at the stage of ratification (internal state procedures) by member countries of the Bank. The Protocol will enter into force upon completion of those ratification procedures. As at the end of 2017, the Protocol was ratified by Hungary, the Socialist Republic of Vietnam, Romania, the Republic of Bulgaria, the Russian Federation, the Republic of Cuba, the Czech Republic and Mongolia (8 member countries out of 9).
- ▶ In March 2017, IIB granted observer status to the Republic of Belarus, a sovereign state, for the first time.
- ▶ At the 107th meeting of the Bank’s Council (Bucharest, Romania, June 2017), member countries unanimously approved the Group’s mid-term development strategy for 2018-2022.
- ▶ Taking into account the Group’s new development strategy for 2018-2022 approved by the member countries of the IIB, the Government of Mongolia decided to increase its interest in the paid-in portion of the share capital of the Bank to 1.077%. On 27 December 2017, Mongolia made an additional contribution exceeding EUR 1.9 million.
- ▶ In December 2017, the international rating agency Fitch Ratings upgraded its outlook on the Bank’s credit rating from stable to positive and confirmed its issuer credit rating and debt rating at BBB. Previously, in May 2017, Moody’s Investors Service also upgraded its outlook on the Bank’s credit rating from stable to positive and confirmed its issuer credit rating and debt rating at Baa1. Also, the Bank is assigned the following investment grade ratings: BBB (stable outlook) by Standard&Poor’s and A (stable outlook) by Dagong Global Credit Rating.
- ▶ In April 2017, the Group entered capital markets in Western Europe for the first time, with a debut issue of SSD debentures (Schuldscheindarlehen) – a traditional loan instrument of the German market.
- ▶ In September 2017, the Bank placed EUR- and RON-denominated bonds totaling EUR 125 million on the Romanian stock market. This became the first issue of debt instruments denominated in euro on the Romanian market. As a result, the Romanian Stockbrokers’ Association awarded the International Investment Bank for its support of the development of the national stock market in the *Contribution to the Development of the Romanian Corporate Bonds Market* category.
- ▶ In 2017, the Bank’s trade financing program was recognized the best among other international financial institutions’ programs by the Association of Development Financing Institutions in Asia and the Pacific (ADFIAP), and the Bank was the winner of ADFIAP Awards 2017 in the *Trade Development* category.

At the 107th meeting of the Bank’s Council (Bucharest, Romania), the Bank and the chambers of commerce and industry (the “CCIs”) of the member countries signed a multilateral Memorandum on Cooperation.

*(Thousands of euros)***1. Principal activities (continued)****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>	<i>2017, %</i>	<i>2016, %</i>
Russian Federation	47.633	47.923
Republic of Bulgaria	13.399	13.481
Hungary	12.700	12.777
Czech Republic	9.644	9.703
Slovak Republic	6.820	6.862
Romania	5.859	5.895
Republic of Cuba	1.702	1.713
Socialist Republic of Vietnam	1.165	1.172
Mongolia	1.077	0.474
	100.000	100.000

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

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

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

Business environment in the member countries

Economic and political development of the Bank's member countries affects the activities of enterprises operating in these countries. Considering this fact, the Group performs its operations with reference to the regional features of its member countries to ensure overall assessment and control of credit and operational risks.

The accompanying consolidated 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 Group. Future evolution of the conditions in which the Group operates may differ from the assessment made by the management for the purposes of these consolidated financial statements.

2. Basis of preparation**General**

These consolidated financial statements of the Group have been prepared in accordance with International Financial Reporting Standards ("IFRS") approved by the International Accounting Standards Board.

Subsidiary

As at 31 December 2017, the Bank is a parent company of the Group, which owns CJSC IIB Capital (the Bank's 100% subsidiary) established in 2012 to deal with issues related to IIB activities in Russia including provision of trustee services to the Bank. As at 31 December 2017, the authorized capital of the subsidiary is RUB 44.5 thousand (31 December 2016: RUB 44.5 thousand), which is equivalent to EUR 1.1 thousand at the historical exchange rate at the date of establishment.

Basis of measurement

These consolidated 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 in the property, equipment and investment property stated at revalued amounts.

(Thousands of euros)

2. Basis of preparation (continued)

Preparation and presentation of financial statements

The financial year of the Group begins on 1 January and ends on 31 December.

Functional and presentation currency

Euro (“EUR”) is the Group’s functional and presentation currency as it reflects the economic substance of the underlying operations conducted by the Group and circumstances affecting its operations, because most financial assets and financial liabilities as well as income and expenses of the Group are denominated in EUR.

These consolidated financial statements are presented in thousands of euros (“thousands of euros” or “EUR thousand”), unless otherwise indicated.

3. Summary of accounting policies

Changes in accounting policies

The Group has adopted the following amended IFRS which are effective for annual periods beginning on or after 1 January 2017. The Group has not early adopted standards, interpretations or amendments that have been issued but are not yet effective. The nature and the impact of each new amendment are described below:

Amendments to IAS 7 Statement of Cash Flows – Disclosure Initiative

The amendments require entities to provide disclosures about changes in their liabilities arising from financing activities, including both changes arising from cash flows and non-cash changes (such as foreign exchange gains or losses). The Group disclosed relevant information for both the current period and the comparative period in Note 29.

Amendments to IAS 12 Income Taxes – Recognition of Deferred Tax Assets for Unrealized Losses

The amendments clarify that an entity needs to consider whether tax law restricts the sources of taxable profits against which it may make deductions on the reversal of that deductible temporary difference related to unrealized losses. Furthermore, the amendments provide guidance on how an entity should determine future taxable profits and explain the circumstances in which taxable profit may include the recovery of some assets for more than their carrying amount. These amendments had no effect on the Group’s financial position and performance, since the Group has no deductible temporary differences or assets that are in the scope of the amendments.

Amendments to IFRS 12 Disclosure of Interests in Other Entities – Clarification of the scope of the disclosure requirements in IFRS 12

The amendments clarify that the disclosure requirements in IFRS 12 are applicable to an entity’s interest in a subsidiary, a joint venture or an associate (or a portion of its interest in a joint venture or an associate) that is classified (or included in a disposal group that is classified) as held for sale. These amendments had no impact on the Group’s financial position or performance.

Foreign currency transactions

The consolidated financial statements are presented in euro, which is the Group’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 consolidated income statement as “Net gains from operations in foreign currencies and with derivatives”. 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 Group’s exchange rate on the date of the transaction are included in “Net gains from operations in foreign currencies and with derivatives”.

(Thousands of euros)

3. Summary of accounting policies (continued)

Basis of consolidation

Subsidiaries, which are those entities in which the Group has an interest of more than one half of the voting rights, or otherwise has power to exercise control over their operations, are consolidated. Subsidiaries are consolidated from the date on which control is transferred to the Group and are no longer consolidated from the date that control ceases. All intra-group transactions, balances and unrealized gains on transactions between group companies are eliminated in full; unrealized losses are also eliminated unless the transaction provides evidence of an impairment of the asset transferred. Where necessary, accounting policies for subsidiaries have been changed to ensure consistency with the policies adopted by the Group.

A change in the ownership interest of a subsidiary, without a change of control, is accounted for as an equity transaction. Losses of the subsidiary are attributed to the non-controlling interests even if that results in a deficit balance.

If the Group loses control over a subsidiary, it derecognizes the assets (including goodwill) and liabilities of the subsidiary, the carrying amount of any non-controlling interests, the cumulative translation differences, recorded in equity; recognizes the fair value of the consideration received, the fair value of any investment retained and any surplus or deficit in profit or loss and reclassifies the parent's share of components previously recognized in other comprehensive income to profit or loss.

Investments in associates

Associates are entities in which the Group generally has between 20% and 50% of the voting rights (interest), or is otherwise able to exercise significant influence, but which it does not control or jointly control. Investments in associates are accounted for under the equity method and are initially recognized at cost, including goodwill. Subsequent changes in the carrying amount reflect the post-acquisition changes in the net assets of the associate attributable to the Group. The Group's share of its associates' profits or losses is recognized in the consolidated income statement, and its share of movements in reserves is recognized in other comprehensive income. However, when the Group's share of losses in an associate equals or exceeds its interest in the associate, the Group does not recognize further losses, unless the Group is obliged to make further payments to, or on behalf of, the associate.

Unrealized gains on transactions between Group and its associates are eliminated to the extent of the Group's interest in the associates; unrealized losses are also eliminated unless the transaction provides evidence of an impairment of the asset transferred.

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 Group measures financial instruments, such as trading and available-for-sale securities, derivatives and non-financial assets such as investment property, at fair value at each reporting date. Also, fair values of financial instruments measured at amortized cost are disclosed in Note 24.

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 Group. 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.

(Thousands of euros)

3. Summary of accounting policies (continued)

Fair value measurement (continued)

The Group 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 consolidated 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 consolidated financial statements on a recurring basis, the Group 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.

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 Group 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 Group 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 Group 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.

(Thousands of euros)

3. Summary of accounting policies (continued)

Financial assets (continued)

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 from change in fair value 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 consolidated 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 Group 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.

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 if the Group 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 gains or losses already recognized in profit or loss are 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 (“repo”) are treated as secured financing transactions. Securities sold under sale and repurchase agreements are retained in the consolidated statement of financial position and in case the transferee has the right by contract or custom to sell or repledge them, reclassified as investment securities pledged under sale and repurchase agreements.

The corresponding liabilities are presented within amounts due to credit institutions or customers. Securities purchased under agreements to resell (“reverse repo”) are recorded as cash equivalents, deposits with banks and other financial institutions as appropriate. The difference between sale and repurchase price is treated as interest and accrued over the life of repo agreements using the effective interest rate method.

Securities lent to counterparties are retained in the consolidated statement of financial position. Securities borrowed are not recorded in the consolidated 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 consolidated 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 Group enters into various derivative financial instruments including forwards and swaps in the foreign exchange market. Such financial instruments are held for trading and are initially 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 consolidated income statement as “Net gains from operations in foreign currencies and with derivatives”.

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 value on the trading portfolio with changes in fair value recognized in profit or loss.

(Thousands of euros)

3. Summary of accounting policies (continued)

Hedge accounting

To manage the risks associated with fluctuations in cash flows from receipt and payment of interest, as well as with fluctuations in the fair value of certain items, the Group uses derivative financial instruments. As a result, the Group applies hedge accounting for transactions that meet specified criteria.

At the inception of the hedge relationship, the Group documents the relationship between the hedged item and the hedging instrument, including the nature of the risk, the risk management objective and strategy for undertaking the hedge and the method that will be used to assess the effectiveness of the hedging relationship at the inception and on an ongoing basis.

At each hedge effectiveness assessment date, a hedge relationship must be expected to be highly effective on a prospective basis and demonstrate that it was highly effective (retrospective effectiveness) for the designated period in order to qualify for hedge accounting. A formal assessment is undertaken both at inception and at each month end on an ongoing basis. A hedge is expected to be highly effective if the changes in fair value or cash flows attributable to the hedged risk during the period for which the hedge is designated will be offset by the hedging instrument in a range of 80% to 125%.

Fair value hedges

For designated and qualifying fair value hedges, the change in the fair value of a hedging derivative is recognized in the consolidated income statement in “Net gains from operations in foreign currencies and with derivatives”.

Meanwhile, the cumulative change in the fair value of the hedged item attributable to the risk hedged is recorded as an adjustment of the carrying value of the hedged item in the consolidated income statement in “Net gains from operations in foreign currencies and with derivatives”.

If the hedging instrument expires or is sold, terminated or exercised, or where the hedge no longer meets the criteria for hedge accounting, the hedge relationship is discontinued prospectively. For hedged items recorded at amortized cost, using the effective interest rate method, when the hedge ceases, the adjustment of the carrying amount of the hedged financial instrument is amortized over the remaining period until date of maturity of the hedged financial instrument. If the hedged item is derecognized, the unamortized fair value adjustment is recognized in profit or loss.

Cash flow hedges

For designated and qualifying cash flow hedges, the effective portion of the cumulative gain or loss on the hedging instrument is initially recognized in consolidated other comprehensive income and is recorded through other comprehensive income. An ineffective portion of the gain or loss on the hedging instrument is recognized in the consolidated income statement.

When a hedging instrument expires, is sold, terminated, exercised, or when a hedge no longer meets the criteria for hedge accounting, the total amount of income or expense accumulated at that time in equity is transferred from equity and recognized in the consolidated income statement in the same period or periods during which hedged projected cash flows affect profit or loss.

When a forecast transaction is no longer expected, the cumulative gain or loss recognized in equity is immediately transferred to the consolidated income statement.

Borrowings

Issued financial instruments or their components are classified as liabilities, where the substance of the contractual arrangement results in the Group 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 banks and other financial institutions, long-term loans of banks and debt securities issued. 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.

(Thousands of euros)

3. Summary of accounting policies (continued)

Leases

Operating – Group 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.

Operating – Group as lessor

The Group presents assets subject to operating leases in the consolidated statement of financial position according to the nature of the asset.

Lease income from operating leases is recognized in the consolidated 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 Group 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 Group 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 Group 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 consolidated 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 consolidated statement of financial position.

Impairment of financial assets

The Group 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.

(Thousands of euros)

3. Summary of accounting policies (continued)

Impairment of financial assets (continued)

Deposits with banks and other financial institutions, long-term loans to banks, trade financing loans, and loans to customers

For deposits with banks and other financial institutions, long-term loans to banks, trade financing loans, and loans to customers carried at amortized cost, the Group 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 Group 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.

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 consolidated 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 consolidated statement of financial position is reduced through the use of an allowance account and the amount of the loss is recognized in the consolidated 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 Group. 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 consolidated 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 incurred by the Group and 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 Group 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 value 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 consolidated income statement.

(Thousands of euros)

3. Summary of accounting policies (continued)

Impairment of financial assets (continued)

Available-for-sale financial instruments

For available-for-sale financial instruments, the Group 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 consolidated income statement – is reclassified from other comprehensive income to the consolidated income statement. Impairment losses on equity investments are not reversed through the consolidated 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 consolidated 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 consolidated income statement, the impairment loss is reversed through the consolidated income statements.

Renegotiated loans

Where possible, the Group 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 consolidated statement of financial position.
- ▶ If the loan restructuring is not caused by the financial difficulties of the borrower, the Group 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 Group 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.

Once the terms have been renegotiated, the loan is no longer considered past due. The Group's 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 consolidated statement of financial position where:

- ▶ The rights to receive cash flows from the asset have expired.
- ▶ The Group 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.
- ▶ The Group 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.

(Thousands of euros)

3. Summary of accounting policies (continued)

Derecognition of financial assets and liabilities (continued)

Where the Group 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 Group'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 Group 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 Group's continuing involvement is the amount of the transferred asset that the Group 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 Group'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 consolidated income statement.

Financial guarantees

In the ordinary course of business, the Group gives financial guarantees, consisting of letters of credit, guarantees and acceptances. Financial guarantees are initially recognized in the consolidated financial statements at fair value, in "Other liabilities", being the premium received. Subsequent to initial recognition, the Group's liability under each guarantee is measured at the higher of the amortized premium and the best estimate of expenditure required to settle any financial obligation arising as a result of the guarantee.

Any increase in the liability relating to financial guarantees is taken to the consolidated statement of profit or loss. The premium received is recognized in profit or loss on a straight-line basis over the life of the guarantee.

Property and equipment

Property and equipment are carried in the consolidated 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 amount of property and equipment is reviewed for impairment when events or changes in circumstances indicate that the carrying amount 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 carried in other comprehensive income, except to the extent that it reverses a revaluation decrease of the same asset previously recognized in the consolidated income statement, in which case the increase is recognized in profit or loss. A revaluation deficit is recognized in the consolidated 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.

*(Thousands of euros)***3. Summary of accounting policies (continued)****Property and equipment (continued)**

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 consolidated 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 depreciation 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 includes a part of buildings held to earn rental income or for capital appreciation and which are not used by the Group 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 Group's investment property is determined on the basis 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.

Investment property that is being redeveloped for continuing use as investment property or for which the market has become less active continues to be measured at fair value. Earned rental income is recorded in the consolidated income statement within "Income from lease of investment property". Gains and losses resulting from changes in the fair value of investment property are recorded in the consolidated income statement and presented within gains/(losses) from revaluation of investment property.

Subsequent expenditure is subject to capitalization only when it is probable that future economic benefits associated with an asset will flow to the Group 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

The useful lives of intangible assets are assessed to be finite and include capitalized computer software. Intangible assets that have been acquired and recorded are capitalized based on costs incurred to acquire and bring to use these intangible assets. Following initial recognition, intangible assets are carried at acquisition cost less any accumulated amortization and any accumulated impairment losses. Intangible assets are amortized using the straight-line method and assessed for impairment whenever there is an indication that the intangible asset may be impaired. Depreciation is calculated on a straight-line basis over the following estimated useful lives:

	<u>Years</u>
Automated banking system	20
Other computer software	1-5

(Thousands of euros)

3. Summary of accounting policies (continued)

Assets classified as held for sale

The Group 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 Group'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 Group measures an asset classified as held for sale at the lower of its carrying amount and fair value less costs to sell.

The Group 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 Group 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 consolidated 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 consolidated statement of financial position but disclosed in the consolidated financial statements when an inflow of economic benefits is probable.

Recognition of income and expenses

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

(Thousands of euros)

3. Summary of accounting policies (continued)

Recognition of income and expenses (continued)

Fee and commission income

The Group 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. 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 consolidated 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

Dividend income is recognized when the Group's right to receive the payment is established.

Fiduciary assets

Fiduciary assets are not reported in the consolidated financial statements, as they are not owned by the Group.

Segment reporting

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

Standards issued but not yet effective

The standards and interpretations issued, but not yet effective, up to the date of issuance of the Group's consolidated financial statements are disclosed below. The Group intends to adopt these standards when they become effective.

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IFRS 9 Financial Instruments

In July 2014, the IASB issued the final version of IFRS 9 *Financial Instruments* which supersedes IAS 39 *Financial Instruments: Recognition and Measurement*. The standard introduces new requirements for classification and measurement, impairment, and hedge accounting. IFRS 9 is effective for annual periods beginning on or after 1 January 2018. Except for hedge accounting, retrospective application is required, but recalculation of comparative information is not compulsory, except for hedge accounting.

(Thousands of euros)

3. Summary of accounting policies (continued)

Standards issued but not yet effective (continued)

The Group plans to adopt the new standard and recognize the cumulative effect of transition in retained earnings as at 1 January 2018. The comparative information will not be restated. Based on data as at 31 December 2017 and the current adoption status, the Group is currently assessing, in quantitative terms, the impact of IFRS 9 adoption; however, the assessment has not been finalized yet.

The Group has developed a plan for the phase-by-phase transition to IFRS 9. The working group for the transition to the new standard comprises experts on methodology, data search and modeling, information technology and financial statements. The group was engaged in the assessment of financial instruments affected by classification and measurements requirements of IFRS 9, as well as in the development of the methodology to provide for expected credit losses.

(a) Classification and measurement

Pursuant to IFRS 9, all debt financial assets that do not meet the Solely Payments of Principal and Interest (SPPI) criterion are classified at initial recognition as financial assets at fair value through profit or loss (FVPL). According to this criterion, debt instruments that do not meet the definition of basic credit agreement (such as instruments with embedded conversion options or non-recourse loans) are measured at FVPL. Those debt financial instruments that meet the SPPI criterion are classified at initial recognition based on a business model for managing these instruments:

- ▶ Instruments held to receive the contractual cash flows are at amortized cost.
- ▶ Instruments held to receive the contractual cash flows and for sale are classified as at fair value through other comprehensive income (FVOCI).
- ▶ Instruments held for other purposes are classified as at FVPL.

Equity financial assets are to be classified at initial recognition as at FVPL, except when the entity decided to irrevocably designate such assets as at FVOCI. For equity financial instruments classified as at FVOCI, all realized and unrealized gains or losses (except for dividend income) are recognized in other comprehensive income, with no subsequent reclassification to profit or loss.

The classification and measurement of financial liabilities remain almost unchanged from the existing requirements of IAS 39. Derivative financial instruments continue to be measured at FVPL.

The Group does not expect any significant changes in classification and measurement of financial instruments recorded on its consolidated statement of financial position.

(b) Impairment

IFRS 9 sets requirements for assessing expected credit losses and providing for financial assets measured at amortized cost and at fair value through other comprehensive income, including loans, trade and lease receivables, debt securities, contractual assets per IFRS 15, as well as off-balance credit-related commitments (hereinafter, the “financial instruments”).

Key changes in the approach to assessing provisions for expected credit losses in IFRS 9:

- ▶ Expected credit losses are assessed for all financial instruments, including assets without any indications of impairment and/or deterioration of credit quality; provision is required from the date of acquisition of a financial instrument exposed to credit risk, which result in higher provisions.
- ▶ A more complex provisioning methodology was introduced. A provisioning model is to be developed using the following parameters: probability of default (PD) within 12 months and for the whole term of the financial instrument, loss given default (LGD), macroeconomic indicators.

The assessment of impairment losses is based on expected losses (IFRS 9) rather than on incurred losses (IAS 39). According to the new assessment model, an allowance should be created at initial recognition of a financial instrument (or at the date when the Group becomes a party to a loan agreement or a financial guarantee) based on expected potential credit losses.

(Thousands of euros)

3. Summary of accounting policies (continued)

Standards issued but not yet effective (continued)

Pursuant to IFRS 9, for financial instruments, either occurred or acquired, the Group will recognize an allowance for impairment in the amount of expected credit losses for 12 months, if there has been no significant increase in credit risk since origination (phase 1). This amount represents expected credit losses as a result of a default that may take place within the next 12 months. Interest income is calculated based on the gross carrying amount of a financial instrument at phase 1.

According to IFRS 9, credit losses shall be recognized over the remaining useful lives of financial instruments (“expected losses over the useful life”) that are considered to have a significantly increased credit risk exposure (phase 2), as well as for financial assets impaired at the reporting date (phase 3).

Expected losses for financial instruments are all possible events of default that may occur over the expected useful life of a financial instrument. The Group uses current risk management measures, changes in credit rating and relevant reasonable information to determine whether there is a significant increase in credit risk of a financial instrument. This includes considering prospective information, including macroeconomic factors. In addition, financial instruments will be transferred at phase 2, if they are 30 days overdue. Interest income is calculated based on the gross carrying amount of a financial instruments at phase 2.

IFRS 9 does not require separating individually significant financial instruments / borrowers in assessing expected credit losses and using a separate approach to such instruments/borrowers. Interest income is calculated only based on net carrying amount of these financial instruments at phase 3.

The Group decided to assess the provision for credit losses on an individual basis at phase 3. There is a number of criteria the Group analyses at transitions between phases 1, 2 and 3. At the same time, it analyses, on an individual basis, all factors that may provide evidences of changes in credit risk or impairment.

In order to assess expected credit losses, the Bank uses three basic components: the probability of default (PD) (point in time and lifetime), loss given default (LGD), macroeconomic indicators.

For the purpose of IFRS 9, provisions for credit losses are affected by such key characteristics as exposure at default (EAD), expected useful life of a financial asset, etc. As a result, the provision for credit losses for phase 2 financial instruments will be increased along with the expected useful life of a financial instrument.

According to estimates, IFRS 9 will result in higher provisions to cover credit losses, as mentioned above. This increase is a result of the requirement to fix a provision in the amount of expected credit losses for 12 months for instruments with no significant increase in credit risk since origination, and a larger number of financial instruments to which expected losses are applied over their useful lives.

(c) Changes in hedge accounting

IFRS 9 sets new hedge accounting rules that will align hedge accounting with risk management approach. The standard eliminated certain restrictions, so more instruments can qualify as hedging instruments for hedge accounting purposes.

Key changes: Modified approach to hedge effectiveness testing, risk component designated as the hedged item, hedging cannot be derecognized when the hedging purpose remains unchanged.

IFRS 9 provides possibility to postpone implementation of the standard in relation to hedge accounting and continue to apply IAS 39 requirements. The Group decided not to implement IFRS 9 in relation to hedge accounting at the date of IFRS 9 became effective.

(Thousands of euros)

3. Summary of accounting policies (continued)

Standards issued but not yet effective (continued)

IFRS 15 Revenue from Contracts with Customers

IFRS 15 was issued in May 2014 and amended in April 2016. The new standard will supersede all existing revenue recognition requirements under IFRS. Either a full retrospective application or a modified retrospective application will be required for annual periods beginning on or after 1 January 2018. The Group plans to adopt the new standard using the modified retrospective approach and recognize the cumulative effect of transition in retained earnings as at 1 January 2018. The comparative information will not be restated.

IFRS 15 establishes a new five-step model that will apply to revenue arising from contracts with customers. Under IFRS 15, revenue is recognized at an amount that reflects the consideration to which an entity expects to be entitled in exchange for transferring goods or services to a customer. However, interest and fee income integral to financial instruments and leases will continue to fall outside the scope of IFRS 15 and will be regulated by the other applicable standards (e.g., IFRS 9 and IFRS 16 *Leases*). As a result, this standard will have no impact on a significant portion of the Group's revenue.

The Group does not expect a significant impact of IFRS 15.

Amendments to IFRS 10 and IAS 28 – Sale or Contribution of Assets between an Investor and its Associate or Joint Venture

The amendments address the inconsistency between the requirements in IFRS 10 and IAS 28 in dealing with the loss of control of a subsidiary that is sold or contributed to an associate or a joint venture. The amendments clarify that gains or losses arising as a result of the sale or contribution of assets that constitute a business, as defined in IFRS 3, in a transaction between an investor and its associate or joint venture are recognized in full. However, gains or losses arising as a result of the sale or contribution of assets that do not constitute a business are recognized only to the extent of interests of investors, other than the entity, in an associate or a joint venture. The IASB has deferred the effective date of these amendments for an indefinite term, but an entity that early adopts the amendments must apply them prospectively. The Group does not expect any significant effect from these amendments.

Amendments to IFRS 2 – Classification and Measurement of Share-based Payments

The IASB issued amendments to IFRS 2 *Share-based Payments*, which cover the following three aspects: the effects of vesting conditions on the measurement of a cash-settled share-based payment; classification of share-based payments with settlement of the tax at source on a net basis; accounting for amended terms of share-based payments resulting in cease of classification as a cash-settled transaction and start of classification as equity-settled transaction.

When adopting the amendments, entities do not have to restate data for the prior periods, however retrospective application is possible if the entity applies all three aspects and if other criteria are met. The amendments are effective for annual periods beginning on or after 1 January 2018, with early adoption permitted. The Group does not expect any significant effect from these amendments.

IFRS 16 Leases

IFRS 16 was issued in January 2016 and replaces IAS 17 *Leases*, IFRIC 4 *Determining Whether an Arrangement Contains a Lease*, SIC 15 *Operating Leases – Incentives* and SIC 27 *Evaluating the Substance of Transactions Involving the Legal Form of a Lease*. IFRS 16 sets out the principles for the recognition, measurement, presentation and disclosure of leases, and requires that lessees account for all lease agreements using a single lessee accounting model, i.e. similarly to the accounting for finance leases in IAS 17. The standard provides for two types of disclosure exemptions for lessees: for leases of 'low-value' assets and 'short-term' leases (e.g. leases expiring in 12 months or less). At the inception of the lease, the lessee will recognize a liability to make lease payments (i.e. a lease liability) and an asset granting the right to use an underlying asset over the lease term (i.e. a right-of-use asset). The lessees will recognize the interest expense related to the lease liability separately from the amortization expense related to the right-of-use asset.

The lessees will also remeasure the lease liability on occurrence of a certain event (e.g. a change in lease terms or future lease payments resulting from a change in the index or rate used to determine those payments). In most cases, a lessee will account for the amount of the remeasured lease liability as an adjustment to the right-of-use asset.

(Thousands of euros)

3. Summary of accounting policies (continued)

Standards issued but not yet effective (continued)

The accounting treatment for the lessor under IFRS 16 remains almost unchanged from the existing requirements of IAS 17. Lessors will continue to classify leases as operating or finance leases using the same classification principles as in IAS 17.

In addition, IFRS 16 requires that lessors and lessees provide a more detailed disclosures as compared with IAS 17.

IFRS 16 is effective for annual periods beginning on or after 1 January 2019. Early application is permitted but not before the date on which the entity begins to apply IFRS 15. A lessee may apply this standard using either a full or modified retrospective approach. The transitional provisions of the standard contain certain exemptions. In 2018, the Group will continue to assess the potential impact of IFRS 16 on its consolidated financial statements.

IFRS 17 Insurance Contracts

In May 2017, the IASB issued IFRS 17 *Insurance Contracts*, a new comprehensive financial reporting standard related to insurance contracts, which addresses the issues of recognition, measurement, information presentation and disclosures.

When IFRS 17 is effective, it will replace IFRS 4 *Insurance Contracts*, which was issued in 2005. IFRS 17 applies to all insurance contracts (i.e., life insurance and insurance other than life insurance, direct insurance and reinsurance) regardless of the type of entity that issues them, as well as to certain guarantees and financial instruments with discretionary participation conditions.

There are several scope exceptions. The main objective of IFRS 17 is to provide a recognition model for insurance contracts, which is more effective and consistent for insurers. Unlike requirements of IFRS 4, which are based mostly on previous local accounting policies, IFRS 17 provides a comprehensive recognition model for insurance contracts covering all the relevant accounting considerations.

IFRS 17 is effective for reporting periods beginning on or after 1 January 2021. In addition, comparative information shall be provided. Earlier application is permitted on condition that the entity also applies IFRS 9 and IFRS 15. The Group does not expect that IFRS 15 will have a significant effect on the consolidated financial statements.

Amendments to IAS 40 – Transfers of Investment Property

Amendments clarify the cases when an entity is required to transfer real estate, including real estate under construction or development, into or from the category of investment property. The amendments state that a change in use occurs when property begins or ceases to comply with the definition of investment property and there is evidence of a change in use. Any change in management's intentions regarding the use of the property itself does not indicate a change in its use. Entities should apply these amendments prospectively with respect to changes in use, which occurred on or after the beginning of the annual reporting period, in which the entity applies these amendments for the first time, or after that date. The entity shall re-assess the classification of real estate held at that date and, if necessary, transfer real estate to reflect conditions that exist at that date. Retrospective application is permitted according to IAS 8 only if it is possible without more recent information. The amendments are effective for annual periods beginning on or after 1 January 2018. The Group does not expect any significant effect from these amendments.

Annual improvements 2014-2016 cycle (issued in December 2016)

They include:

IFRS 1 First-time Adoption of International Financial Reporting Standards – Elimination of Short-Term Exemptions for First-Time Adopters

Short-term exemptions stipulated by paragraphs E3-E7 of IFRS 1 were deleted since they had served their purpose. These amendments are effective from 1 January 2018. These amendments are not applicable to the Group.

(Thousands of euros)

3. Summary of accounting policies (continued)

Standards issued but not yet effective (continued)

IAS 28 Investments in Associates and Joint Ventures – Clarification that the Decision to Measure Investees at Fair Value through Profit or Loss Should Be Made Individually for Each Investment

The amendments clarify:

An entity that is a venture capital organization, or other similar entity may decide to measure investments in associates and joint ventures at fair value through profit or loss. This decision is made individually for each investment.

If the entity that is not an investment entity itself has an interest in an associate or joint venture that are investment entities, when applying the equity method, such entity can retain the fair value measurement applied by its investment associate or joint venture to its interests in subsidiaries. This decision is made individually for each investment associate or joint venture at the later of: (a) the date of initial recognition of an investment associate or joint venture; (b) the date when an associate or joint venture becomes an investment entity and (c) the date when an investment associate or joint venture first becomes a parent.

These amendments are applied retrospectively and are effective from 1 January 2018. The Group does not expect any significant effect from these amendments.

Amendments to IFRS 4 – Applying IFRS 9 Financial Instruments with IFRS 4 Insurance Contracts

These amendments eliminate concerns arising from implementing the new standard related to financial instruments, IFRS 9, before implementing IFRS 17 *Insurance Contracts*, which replaces IFRS 4. The amendments grant two options for entities issuing insurance contracts: a temporary exemption from applying IFRS 9 and an overlay approach. The temporary exemption is first applied for reporting periods beginning on or after 1 January 2018. An entity may elect the overlay approach when it first applies IFRS 9 and apply that approach retrospectively to financial assets designated at the entity's discretion on transition to IFRS 9. In addition, the entity restates comparative information to reflect the overlay application approach if, and only if, it restates comparative data while applying IFRS 9. These amendments are not applicable to the Group.

IFRIC 22 – Foreign Currency Transactions and Prepayment

It clarifies that for the purpose of determining exchange rate to be applied at initial recognition of the respective assets, expenses or revenues (or their part) at derecognition of a non-monetary asset or non-monetary liability related to making or receiving prepayment, the date of transaction should be considered the date when an entity initially recognizes non-monetary asset or non-monetary liability related to making or receiving prepayment. The clarification become effective for annual reporting periods beginning on or after 1 January 2018. However, since the current activities of the Group comply with the requirements of the clarification, the Group does not expect that it will have any impact on its consolidated financial statements.

IFRIC 23 – Uncertainty over Income Tax Treatments

The clarification addresses the treatment of income tax when there is uncertainty over tax interpretations, which affects the application of IAS 12. The clarification does not apply to taxes or fees that are not within the scope of IAS 12, nor does it contain specific requirements for interest and penalties related to uncertain tax interpretations.

The entity should decide whether to consider each uncertain tax interpretation separately or together with one or several other uncertain tax interpretations. It is necessary to use an approach that will allow predicting results of resolving uncertainty more accurately. The clarification also covers assumptions made to review interpretations of tax authorities and changes in facts and circumstances.

The clarification become effective for annual reporting periods beginning on or after 1 January 2019. The Bank is not subject to taxation, therefore application of these amendments has no effect on the Group's financial position and performance.

(Thousands of euros)

3. Summary of accounting policies (continued)

Standards issued but not yet effective (continued)

Annual improvements 2015-2017 cycle (issued in December 2017)

These improvements are applied for annual reporting periods beginning on or after 1 January 2019 and include:

IFRS 3 Business Combinations and IFRS 11 Joint Arrangements – previously held interest in a joint operation

- ▶ These amendments clarify whether the previously held interest in a joint operation (that is a business as defined in IFRS 3) should be remeasured to fair value, when: A party to a joint operation obtains control over the joint operation (IFRS 3);
- ▶ A party that participates in (but does not have joint control over a joint operation) obtains joint control over the joint operation (IFRS 11).

The Group does not expect any effect on its consolidated financial statements.

IAS 12 Income Taxes – income tax consequences of payments on financial instruments classified as equity

These amendments clarify that an entity must recognise all income tax consequences of dividends in profit or loss, other comprehensive income or equity, depending on where the entity recognised the originating transaction or event that generated the distributable profits giving rise to the dividend. Earlier application is permitted and must be disclosed. The amendments must first be applied to income tax consequences of dividends recognised on or after the beginning of the earliest comparative period. Since the Group's current practice is in line with the amendments, the Group does not expect any effect on its consolidated financial statements.

IAS 23 Borrowing Costs – borrowing costs eligible for capitalization

These amendments clarify that, when a qualifying asset is ready for its intended use or sale, and some of the specific borrowing related to that qualifying asset remains outstanding at that point, that borrowing is to be included in the funds that an entity borrows generally. Earlier application is permitted and should be disclosed. The Group does not expect any effect on its consolidated financial statements.

4. Significant accounting judgments and estimates

Assumptions and estimation uncertainty

In the process of applying the Group'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 consolidated financial statements, which have the most significant effect on the amounts recognized in the consolidated 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 Group's consolidated statement of financial position less allowances for impairment. The Group regularly reviews its financial assets to assess impairment. When assessing impairment losses, the Group 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 Group 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 consolidated 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 24.

Impairment of available-for-sale equity securities

The Group 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 Group 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 value of the buildings classified to “property and equipment” and “investment property”

As disclosed in Note 3, the Group applies the fair value model with regard to investment property. Buildings included in fixed assets are stated at revalued amount.

As for buildings within property and equipment, the Group 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 Group's building were carried out as at 31 October 2017 by an independent companies 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 technique may differ from the prices of actual transactions in the real estate market.

Management believes that during the period from the valuation date to the date of consolidated financial statements there were no significant changes in economy and technical parameters of the building that could affect its revalued cost. Starting from 31 October 2017, the revalued building is depreciated in accordance with the remaining useful life.

As for investment property, the Group 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 consolidated income statement. The most recent revaluation of the Group's investment properties were carried out as at 31 October 2017 by an independent company 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 technique may differ from the prices of actual transactions in the real estate market. Management believes that during the period from the valuation date to the date of consolidated financial statements there were no significant changes in economy and technical parameters of the investment properties that could affect its revalued cost.

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

- ▶ Note 7 – Derivative financial instruments;
- ▶ Note 8 – Available-for-sale investment securities;
- ▶ Note 9 – Loans to banks;
- ▶ Note 10 – Loans to customers;
- ▶ Note 11 – Investment property;
- ▶ Note 12 – Property, equipment and intangible assets;
- ▶ Note 18 – Commitments and contingencies.

(Thousands of euros)

4. Significant accounting judgments and estimates (continued)**Reclassification of comparative information**

The Group changed the presentation of line items in the consolidated income statement for the year ended 31 December 2016. The following adjustments were made to the data for 2016 to conform to the presentation of data for 2017:

	<i>In accordance with the previously issued report</i>	<i>Reclassification amount</i>	<i>After reclassification</i>
Article of the consolidated income statement			
Net gains from revaluation of derivative financial instruments	32,330	(32,330)	–
Net losses from fair value hedge operations	(246)	246	–
Net gains from dealing in foreign currencies and operations with derivatives	9,068	(9,068)	–
Net losses from revaluation of assets and liabilities in foreign currencies	(31,173)	31,173	–
Net gains from operations in foreign currencies and with derivatives	–	9,979	9,979

5. Cash and cash equivalents

Cash and cash equivalents comprise:

	<u>2017</u>	<u>2016</u>
Cash on hand	85	104
Nostro accounts with banks and other financial institutions		
<i>Credit rating from A- to A+</i>	49,120	62,548
<i>Credit rating from BBB- to BBB+</i>	4,167	4,526
<i>Credit rating from BB- to BB+</i>	274	551
Total nostro accounts with banks and other financial institutions	53,561	67,625
Short-term deposits with banks		
Term deposits with banks		
<i>Credit rating BBB-</i>	68	–
<i>Credit rating from BB- to BB+</i>	12,383	25,302
Total short-term deposits with banks	12,451	25,302
Cash and cash equivalents	66,097	93,031

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

6. Deposits with banks and other financial institutions

Deposits with banks and other financial institutions are presented based on contractual terms and include the following items:

	<u>2017</u>	<u>2016</u>
Term deposits up to 1 year		
<i>Credit rating from B- to B+</i>	37,157	37,126
Total term deposits up to 1 year	37,157	37,126
Term deposits over 1 year		
<i>Credit rating from A- to A+</i>	5,650	5,821
<i>Credit rating from BB- to BB+</i>	3,082	2,390
Total term deposits over 1 year	8,732	8,211
Total deposits with banks and other financial institutions	45,889	45,337

(Thousands of euros)

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

	<u>2017</u>	<u>2016</u>
Term deposits with the Central Bank of Cuba without credit rating	34,967	34,967
Less: allowance for impairment	<u>(34,967)</u>	<u>(34,967)</u>
Term deposits with the Central Bank of Cuba	<u><u>–</u></u>	<u><u>–</u></u>

Concentration of deposits with banks and other financial institutions

As at 31 December 2017, besides deposits with the Central Bank of Cuba, the Group had three counterparties (31 December 2016: three counterparties) accounting for over 10% of the Group's total deposits with banks and other financial institutions. As at 31 December 2017, deposits with these counterparties amounted to EUR 25,724 thousand (31 December 2016: EUR 37,125 thousand).

7. Derivative financial instruments

The Group performs the operations with currency and other derivative financial instruments which are generally traded in an over-the-counter market with professional market counterparties on standardized contractual terms and conditions. Derivative financial instruments have either potentially favorable terms (and are assets) or potentially unfavorable conditions (and are liabilities) as a result of fluctuations in exchange rates or other variable factors associated with these instruments. The fair value of derivative financial instruments can vary significantly depending on the potentially favorable and unfavorable conditions.

The table below shows the fair value of derivative financial instruments as at 31 December 2017 and 31 December 2016 and notional amounts of term contracts for the purchase and sale of foreign currency specifying contractual exchange rates.

	<u>31 December 2017</u>				
	<u>Notional amount</u>		<u>Weighted average exchange rate</u>	<u>Fair value</u>	
	<u>Purchase</u>	<u>Sale</u>		<u>Assets</u>	<u>Liabilities</u>
Derivative financial assets and liabilities at fair value through profit or loss					
Swaps	EUR 180,000 thousand	USD 209,572 thousand	1.16	5,203	89
	EUR 10,270 thousand	HUF 3,160,000 thousand	307.69	54	–
	RUB 9,997,998 thousand	EUR 158,232 thousand	63.20	–	8,603
	RUB 3,000,000 thousand	USD 52,910 thousand	56.70	638	–
	RON 319,800 thousand	EUR 70,544 thousand	4.53	931	1,212
Forwards	EUR 34,000 thousand	USD 39,527 thousand	1.16	935	–
Total derivative financial assets and liabilities at fair value through profit or loss				<u>7,761</u>	<u>9,904</u>
Derivative financial assets and liabilities designated as hedging instruments					
Swaps	RON 298,300 thousand	EUR 67,068 thousand	4.45	–	5,169
Total derivative financial assets and liabilities designated as hedging instruments				<u>–</u>	<u>5,169</u>
Derivative financial instruments				<u><u>7,761</u></u>	<u><u>15,073</u></u>

(Thousands of euros)

7. Derivative financial instruments (continued)

	31 December 2016				
	Notional amount		Weighted average exchange rate	Fair value	
	Purchase	Sale		Assets	Liabilities
Derivative financial assets and liabilities at fair value through profit or loss					
Swaps	RUB 9,136,720 thousand	EUR 132,150 thousand	69.42	14,246	883
	RON 110,300 thousand	EUR 24,971 thousand	4.44	–	632
	EUR 117,000 thousand	USD 128,825 thousand	1.10	116	5,704
	EUR 8,000 thousand	RUB 572,280 thousand	71.54	–	788
Forwards	EUR 34,000 thousand	USD 37,896 thousand	1.11	–	2,080
Total derivative financial assets and liabilities at fair value through profit or loss				14,362	10,087
Derivative financial assets and liabilities designated as hedging instruments					
Swaps	RON 298,300 thousand	EUR 67,068 thousand	4.45	–	1,536
Total derivative financial assets and liabilities designated as hedging instruments				–	1,536
Derivative financial instruments				14,362	11,623

Due to issue off bonds denominated in currencies other than the Group's functional currency (Note 16), the Group concluded cross currency interest rate swaps and currency forwards on an arm's length basis with large international and Russian credit institutions. These swaps are used to manage long-term currency risks of the Group. Payment netting is not applied to the parties' obligations in respect of interest and principal payments.

The Group applies hedge accounting for the fair value of the bond issue in Romanian lei placed on September 27, 2016 (Note 16).

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 end of the reporting period and are not indicative of the credit risk.

As at 31 December 2017 and 31 December 2016, the Group has positions in the following types of derivatives:

Forwards: Forward contracts are contractual agreements to buy or sell a specified financial instrument at a specific price and date in the future. Forwards are customized contracts transacted in the over-the-counter market.

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.

Fair value measurement is based on the corresponding forward curves that depend on exchange rates, interest rates and swap contract maturity. For the fair value of swaps, the discount rate was calculated on the basis of zero coupon yield curve and credit risk. Changes in the fair value of swaps were mainly due to the increase in the forward EUR to RUB exchange rates.

(Thousands of euros)

8. Available-for-sale investment securities

Available-for-sale investment securities comprise:

	<i>2017</i>	<i>2016</i>
Owned by the Group		
Quoted debt securities		
Government bonds		
Government bonds of member countries		
<i>Credit rating from BBB- to BBB+</i>	–	39,923
<i>Credit rating from BB- to BB+</i>	–	12,755
Government bonds of non-member countries		
<i>Credit rating AAA</i>	4,066	–
<i>Credit rating AA+</i>	5,396	–
<i>Credit rating B-</i>	18,552	–
Government bonds	28,014	52,678
Corporate bonds		
<i>Credit rating from A- to A+</i>	12,292	21,152
<i>Credit rating from BBB- to BBB+</i>	20,370	21,861
<i>Credit rating from BB- to BB+</i>	62,496	57,579
<i>Credit rating from B- to B+</i>	13,817	17,575
Corporate bonds	108,975	118,167
Total quoted debt securities	136,989	170,845
Quoted equity instruments		
<i>Credit rating A-</i>	633	–
<i>Credit rating BBB</i>	1,077	–
<i>No credit rating</i>	5	4
Total quoted equity instruments	1,715	4
Available-for-sale investment securities	138,704	170,849
Pledged under repurchase agreements		
Quoted debt securities		
Government bonds of member countries		
<i>Credit rating A+</i>	10,010	10,286
Government bonds of non-member countries		
<i>Credit rating A+</i>	7,867	7,597
Government bonds	17,877	17,883
Corporate bonds		
<i>Credit rating AAA</i>	19,991	22,486
<i>Credit rating from AA- to AA+</i>	7,466	4,688
<i>Credit rating from A- to A+</i>	18,544	32,521
<i>Credit rating from BBB- to BBB+</i>	5,995	4,994
<i>Credit rating from BB- to BB+</i>	6,850	15,886
Corporate bonds	58,846	80,575
Total quoted available-for-sale debt securities pledged under repurchase agreements	76,723	98,458

Government bonds represent EUR-denominated and USD-denominated securities issued and guaranteed by the Ministries of Finance of these countries, maturing in 2020-2027 (31 December 2016: maturing in 2018-2027). The annual coupon rate for these bonds varies from 0.4% to 7.6% (31 December 2016: from 0.4% to 7.9%).

Corporate bonds are represented by the bonds issued by large companies and banks of member countries of the Bank, as well as corporate international companies and development banks that have similar goals and missions with the Group, maturing in 2020-2026 (31 December 2016: maturing in 2018-2031). The annual coupon rate for these bonds varies from 0.4% to 7.9% (31 December 2016: from 0.6% to 10.3%).

Equity securities are represented by shares and depositary receipts issued by major international companies.

(Thousands of euros)

9. Loans to banks

During 2017, the Group continued its lending activities, being guided by the key priorities of the Development Strategy of the IIB. 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 Group considers national development institutes, export and import banks and agencies, international financial organizations and development banks as its key counterparties.

In 2017 and 2016, the Group provided trade financing loans and long-term loans to borrowers operating in the following countries:

	<i>2017</i>	<i>2016</i>
Trade financing loans		
Russian Federation	23,298	953
Republic of Belarus	3,239	–
Trade financing loans	26,537	953
Long-term loans to banks		
Russian Federation	75,401	26,425
Republic of Cuba	49,863	–
Mongolia	33,735	47,970
Socialist Republic of Vietnam	25,252	19,019
Long-term loans to banks	184,251	93,414
Less: allowance for impairment of loans to banks	(9,153)	–
Total loans to banks	201,635	94,367

The information on overdue loans as at 31 December 2017 and 31 December 2016 is provided below:

	<i>2017</i>	<i>2016</i>
Total loans with overdue principal and/or interest	15,254	–
Less: allowance for impairment of loans to banks	(9,153)	–
Overdue loans to banks	6,101	–

For the purposes of these consolidated financial statements, a loan to a bank is considered overdue if at least one of the loan-related payments is past due at the reporting date. In this case, the amount of the overdue loan is the total amount due from the borrower, including the accrued interest income.

Allowance for impairment of loans to banks

A reconciliation of the allowance for impairment of loans to banks by country is as follows:

	<i>Russian Federation</i>	<i>Total</i>
At 1 January 2017	–	–
Net charge for the period	9,153	9,153
At 31 December 2017	9,153	9,153
Individual impairment	9,153	9,153
Gross amount of loans to banks individually determined to be impaired, before deducting any individually assessed impairment allowance	15,254	15,254

During 2016 and as at 31 December 2016, there were no impaired loans, and no allowance for impairment was accrued.

*(Thousands of euros)***9. Loans to banks (continued)****Analysis of collateral for loans to banks**

The following table provides an analysis of the portfolio of trade financing loans and long-term loans to banks by type of collateral as at 31 December 2017 and 31 December 2016:

	<i>2017</i>		<i>2016</i>	
	<i>Loans to banks</i>	<i>Share in the total loans, %</i>	<i>Loans to banks</i>	<i>Share in the total loans, %</i>
State guarantees	49,863	24.7	–	–
Pledge of real property (mortgage) and title	–	–	7,247	7.7
Uncollateralized part of the loans	151,772	75.3	87,120	92.3
	201,635	100.0	94,367	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 2017, long-term loans and trade financing loans to two banks (31 December 2016: five banks) with a total amount of loans to each of them exceeding 10% of total loans to banks were recorded on the Group's balance sheet. As at 31 December 2017, the total amount of such major loans was EUR 70,100 thousand (31 December 2016: EUR 74,787 thousand) and no impairment allowances (31 December 2016: no allowances) were made for them.

10. Loans to customers

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

	<i>2017</i>	<i>2016</i>
Russian Federation	81,817	61,213
Romania	78,440	40,235
Slovak Republic	60,464	8,411
Republic of Bulgaria	57,995	65,922
Czech Republic	49,967	22,930
Hungary	42,910	–
Republic of Ecuador	34,763	39,570
Republic of Panama	29,775	36,276
Mongolia	24,425	5,683
Kingdom of the Netherlands	5,847	–
USA	1,666	6,108
Gross loans to customers	468,069	286,348
Less: allowance for impairment of loans to customers	(5,555)	(17,312)
Loans to customers	462,514	269,036

The information on overdue loans as at 31 December 2017 and 31 December 2016 is provided below:

	<i>2017</i>	<i>2016</i>
Total loans with overdue principal and/or interest	15,151	14,769
Less: allowance for impairment of loans to customers	(5,255)	(14,769)
Overdue loans to customers	9,896	–

For the purposes of these consolidated financial statements, a loan to a customer is considered overdue if at least one of the loan-related payments is past due at the reporting date. In this case, the amount of the overdue loan is the total amount due from the borrower, including the accrued interest income.

(Thousands of euros)

10. 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>Slovak Republic</i>	<i>Republic of Bulgaria</i>	<i>Romania</i>	<i>Total</i>
At 1 January 2017	8,103	6,955	2,254	17,312
Net charge for the period	–	11	3,001	3,012
Write off against previously accrued allowance	(8,103)	(6,666)	–	(14,769)
At 31 December 2017	–	300	5,255	5,555
Individual impairment	–	–	5,255	5,255
Gross amount of loans to customers, individually determined to be impaired, before deducting any individually assessed impairment allowance	–	–	15,151	15,151
	<i>Slovak Republic</i>	<i>Republic of Bulgaria</i>	<i>Romania</i>	<i>Total</i>
At 1 January 2016	3,000	6,755	–	9,755
Net charge for the period	5,103	200	2,254	7,557
At 31 December 2016	8,103	6,955	2,254	17,312
Individual impairment	8,103	6,666	–	14,769
Gross amount of loans to customers, individually determined to be impaired, before deducting any individually assessed impairment allowance	8,103	6,666	–	14,769

The following table provides an analysis of the customer loan portfolio, net of allowance for impairment, by types of collateral as at 31 December 2017 and 31 December 2016:

	<i>2017</i>		<i>2016</i>	
	<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	86,728	18.8	25,811	9.6
State guarantees	74,476	16.1	75,845	28.2
Corporate guarantees	70,599	15.3	22,930	8.5
Pledge of shares	42,504	9.2	21,579	8.0
Pledge of equipment and goods in turnover	15,292	3.3	22,641	8.4
Pledge of rights of claim	6,150	1.3	22,970	8.5
Pledge of vehicles	1,476	0.3	2,756	1.0
Uncollateralized part of the loans	165,289	35.7	74,504	27.8
Total loans to customers	462,514	100.0	269,036	100.0

Analysis of collateral for loans to customers

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.

*(Thousands of euros)***10. Loans to customers (continued)****Concentration of loans to customers**

As at 31 December 2017, loans to three borrowers (2016: three borrowers) with the total amount of loans to each of the three borrowers exceeding 10% of total loans to customers were recorded on the Group's balance sheet. As at 31 December 2017, these loans comprised EUR 181,256 thousand (31 December 2016: EUR 107,191 thousand) in total and no impairment allowances (31 December 2016: no allowances) were made for them.

Analysis of loans to customers by industry

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

	<u>2017</u>	<u>2016</u>
Leasing	116,910	85,897
Production and transmission of electricity	104,847	39,570
Metal working industry	49,967	22,930
Crude oil refining	30,099	10,002
Food and beverage	25,662	27,504
Communications	22,815	–
Manufacturing of electrical equipment	21,159	20,809
Mining	20,632	–
Real estate	19,722	308
Advisory services	19,543	–
Agriculture	13,408	14,295
Production of pharmaceutical products	11,319	6,645
Transport	11,248	13,752
Trading	738	6,036
Chemical production	–	23,831
Construction	–	14,769
	<u>468,069</u>	<u>286,348</u>
Less: allowance for impairment of loans to customers	(5,555)	(17,312)
Loans to customers	<u><u>462,514</u></u>	<u><u>269,036</u></u>

11. Investment property

In 2017 and 2016, the following changes occurred in the cost of property under operating lease:

	<u>2017</u>	<u>2016</u>
At 1 January	21,840	33,819
Additions	–	14,324
Inseparable improvements	39	50
Transfers to property and equipment	–	(24,179)
Effect of revaluation	(26)	(2,174)
Carrying amount at 31 December	<u><u>21,853</u></u>	<u><u>21,840</u></u>

The Group leases out investment properties under operating lease agreements. In 2017, the Group's income from lease of investment property amounted to EUR 4,034 thousand (2016: EUR 3,442 thousand).

As at 31 December 2017, the fair value of investment properties are determined based on the results of the valuation performed by independent companies of professional appraisers which have acknowledged qualification and relevant professional experience in appraising real property of a similar category and in a similar location.

The fair value is determined by reference to market-based evidence and ability to generate income. For further details on the fair value of investment property, refer to Note 24.

(Thousands of euros)

11. Investment property (continued)

If the investment property was measured using the cost method, the carrying amounts as at 31 December 2017 and 31 December 2016 would be as follows:

	<u>2017</u>	<u>2016</u>
Cost	20,141	20,091
Additions	49	50
Accumulated depreciation	<u>(2,611)</u>	<u>(2,370)</u>
Net book value	<u>17,579</u>	<u>17,771</u>

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

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*(Thousands of euros)***12. Property, equipment and intangible assets**

The movements in property, equipment and intangible assets for the years 2017 and 2016 were as follows:

	<i>Buildings</i>	<i>Equipment</i>	<i>Computers and software</i>	<i>Office furniture</i>	<i>Vehicles</i>	<i>Intangible assets</i>	<i>Other</i>	<i>Capital expenditure</i>	<i>Total</i>
Cost or revalued amount									
At 1 January 2017	67,644	7,500	3,361	307	808	2,472	183	427	82,702
Additions	–	–	–	–	–	–	–	1,749	1,749
Transfers	350	364	150	14	–	590	2	(1,470)	–
Disposals	–	(283)	(1,588)	(20)	(119)	(11)	(7)	–	(2,028)
Recovery of accumulated depreciation and amortization upon revaluation	(1,039)	–	–	–	–	–	–	–	(1,039)
Effect of revaluation	803	–	–	–	–	–	–	–	803
At 31 December 2017	67,758	7,581	1,923	301	689	3,051	178	706	82,187
Accumulated depreciation and amortization									
At 1 January 2017	(117)	(6,747)	(2,730)	(236)	(580)	(343)	(105)	–	(10,858)
Charge for the period	(1,108)	(250)	(284)	(21)	(102)	(237)	(6)	–	(2,008)
Disposals	–	283	1,587	18	119	14	7	–	2,028
Recovery of accumulated depreciation and amortization upon revaluation	1,039	–	–	–	–	–	–	–	1,039
At 31 December 2017	(186)	(6,714)	(1,427)	(239)	(563)	(566)	(104)	–	(9,799)
Net book value									
At 31 December 2016	67,527	753	631	71	228	2,129	78	427	71,844
At 31 December 2017	67,572	867	496	62	126	2,485	74	706	72,388

*(Thousands of euros)***12. Property, equipment and intangible assets (continued)**

	<i>Buildings</i>	<i>Equipment</i>	<i>Computers and software</i>	<i>Office furniture</i>	<i>Vehicles</i>	<i>Intangible assets</i>	<i>Other</i>	<i>Capital expenditure</i>	<i>Total</i>
Cost or revalued amount									
At 1 January 2016	62,807	7,073	3,278	296	808	325	176	1,591	76,354
Additions	–	–	–	–	–	–	–	1,754	1,754
Transfers from investment property	24,179	–	–	–	–	–	–	–	24,179
Transfers	223	436	83	22	–	2,147	7	(2,918)	–
Disposals	–	(9)	–	(11)	–	–	–	–	(20)
Recovery of accumulated depreciation and amortization upon revaluation	(1,057)	–	–	–	–	–	–	–	(1,057)
Effect of revaluation	(18,508)	–	–	–	–	–	–	–	(18,508)
At 31 December 2016	67,644	7,500	3,361	307	808	2,472	183	427	82,702
Accumulated depreciation and amortization									
At 1 January 2016	–	(6,547)	(2,445)	(228)	(477)	(165)	(99)	–	(9,961)
Charge for the period	(1,174)	(209)	(285)	(19)	(103)	(178)	(6)	–	(1,974)
Disposals	–	9	–	11	–	–	–	–	20
Recovery of accumulated depreciation and amortization upon revaluation	1,057	–	–	–	–	–	–	–	1,057
At 31 December 2016	(117)	(6,747)	(2,730)	(236)	(580)	(343)	(105)	–	(10,858)
Net book value									
At 31 December 2015	62,807	526	833	68	331	160	77	1,591	66,393
At 31 December 2016	67,527	753	631	71	228	2,129	78	427	71,844

As at 31 December 2017, the cost of fully depreciated property and equipment still used by the Group was EUR 5,217 thousand (31 December 2016: EUR 7,982 thousand).

*(Thousands of euros)***12. Property, equipment and intangible assets (continued)**

As at 31 December 2017, the fair value of buildings owned by the Group is determined based on the results of the valuation performed by an independent company of professional appraisers which have acknowledged qualification and relevant professional experience in appraising real property of a similar category and in a similar location.

The fair value is determined by reference to market-based evidence and ability to generate income. For further details on the fair value of property and equipment, refer to Note 24.

If the buildings were measured using the cost method, the carrying amounts as at 31 December 2017 and 31 December 2016 would be as follows:

	<u>2017</u>	<u>2016</u>
Cost	52,355	52,132
Additions	350	223
Accumulated depreciation and amortization	<u>(21,298)</u>	<u>(20,871)</u>
Net book value	<u>31,407</u>	<u>31,484</u>

13. Other assets and liabilities

Other assets comprise:

	<u>2017</u>	<u>2016</u>
Financial assets		
Settlements on bank transactions	2,007	1,814
Accounts receivable on business operations	73	1,352
Guarantee payments	26	42
Other financial assets	<u>363</u>	<u>136</u>
	2,469	3,344
Less: allowance for impairment	<u>(1,741)</u>	<u>(1,924)</u>
Total financial assets	<u>728</u>	<u>1,420</u>
Non-financial assets		
Advances issued	990	–
Assets held for sale – real estate	89	89
Inventories – real estate	50	55
Other non-financial assets	<u>619</u>	<u>755</u>
Total non-financial assets	<u>1,748</u>	<u>899</u>
Total other assets	<u>2,476</u>	<u>2,319</u>

The movements in other impairment allowance are as follows:

	<u>2017</u>	<u>2016</u>
Allowance at 1 January	1,924	1,633
Reversal charge for the year	(29)	(67)
Change in allowance resulting from changes in exchange rates	<u>(154)</u>	<u>358</u>
Allowance at 31 December	<u>1,741</u>	<u>1,924</u>

*(Thousands of euros)***13. Other assets and liabilities (continued)**

Other liabilities comprise:

	<u>2017</u>	<u>2016</u>
Financial liabilities		
Other accounts payable on bank transactions	1,125	662
Other accounts payable on business operations	1,015	1,182
Other financial liabilities	8	19
Total financial liabilities	<u>2,148</u>	<u>1,863</u>
Non-financial liabilities		
Settlements with employees	4,070	3,647
Other non-financial liabilities	178	72
Total non-financial liabilities	<u>4,248</u>	<u>3,719</u>
Total other liabilities	<u><u>6,396</u></u>	<u><u>5,582</u></u>

14. Due to banks and other financial institutions

Due to banks and other financial institutions are presented based on contractual terms and include the following items:

	<u>2017</u>	<u>2016</u>
Due to banks up to 1 year		
Term deposits of banks and other financial institutions	3,496	52,856
Total due to banks up to 1 year	<u>3,496</u>	<u>52,856</u>
Due to banks over 1 year		
Repurchase agreements	62,015	66,069
Total due to banks over 1 year	<u>62,015</u>	<u>66,069</u>
Total due to banks	<u><u>65,511</u></u>	<u><u>118,925</u></u>

The Group performs daily monitoring of repurchase agreements and the value of collateral when placing/returning additional collateral, if necessary.

Concentration of deposits from banks and other financial institutions

As at 31 December 2017, the Group has two counterparties (31 December 2016: two counterparties) accounting for over 10% of the Group's total deposits from banks and other financial institutions. As at 31 December 2017, deposits from these counterparties amounted to EUR 62,015 thousand (31 December 2016: EUR 111,418 thousand).

15. Long-term loans of banks

Long-term loans of banks comprise:

	<u>2017</u>	<u>2016</u>
Syndicated loans	59,755	59,039
SSD	22,939	–
Loans of banks	12,898	14,310
Total long-term loans of banks	<u><u>95,592</u></u>	<u><u>73,349</u></u>

In 2017, the Group issued SSD debentures (Schuldscheindarlehen) in the Western European market in the total amount of EUR 23,000 thousand.

On 3 August 2017, the Group raised bilateral financing in the Hungarian financial market in the amount of HUF 4.0 billion (EUR 13,185 thousand).

*(Thousands of euros)***16. Debt securities issued**

Debt securities issued comprise:

	<i>Interest rate, % p.a.</i>	<i>Maturity</i>	<i>2017</i>	<i>2016</i>
RUB-denominated bonds	0.01-9.5	2024-2027	267,112	151,516
RON-denominated bonds	3.4-4.1	2018-2020	152,084	90,885
EUR-denominated bonds	1.59-3.5	2019-2020	90,017	30,127
Total bonds			509,213	272,528

On 27 April 2017, the Group made a secondary placement of RUB-denominated bonds, series 02, in the amount of RUB 2,998.0 million (EUR 48,615 thousand) that had been repurchased in 2016 under the offer. A new coupon rate of 9.5% p.a. was set, with an offer planned for April 2019.

The Group redeemed RUB-denominated bonds, series 03, worth a total of RUB 3.99 billion (EUR 62,858 thousand) on 2 June 2017, as scheduled under the offer. A new coupon rate of 0.01% was set for the remaining bonds of this issue.

On 14 June 2017, the Group placed an issue of exchange-traded bonds at the Moscow Exchange under the Program to issue exchange-traded bonds registered in 2016. The issue totaled RUB 10 billion (EUR 156,579 thousand) and provides for an offer in March 2020. The coupon rate on the bonds was set at 8.75% payable on a quarterly basis with the first coupon payment to be made on 11 September 2017.

The Group placed a third issue of bonds in the Romanian stock market on 25 September 2017. The issue comprises two tranches of EUR 60 million and RON 300 million (EUR 65,199 thousand) maturing in three years. EUR-denominated bonds and RON-denominated bonds bear interest rates of 1.593% p.a. and 3m Robor + 1.50%, respectively.

The Group partially redeemed RUB-denominated bonds, series 01, worth a total of RUB 489,432 thousand (EUR 7,259 thousand) on 27 October 2017, as scheduled under the offer. A new coupon rate of 0.01% was set for the remaining bonds of this issue.

The Group redeemed and made a secondary placement of bonds, series 04, worth RUB 1.2 billion (EUR 18,271 thousand) on 21 November 2017, as scheduled under the offer. A new coupon rate of 8.15% was set.

On 27 September 2016, the Group issued bonds denominated in Romanian lei in the amount of RON 300.0 million (EUR 67,398 thousand) maturing in three years. The coupon rate on the bonds was set at 3.4% payable annually with the first coupon payment to be made on 27 September 2017.

On 31 October 2016, the Group offered to repurchase RUB-denominated bonds, series 02, and repurchased almost the total amount of those bonds (RUB 2,998.0 million, or EUR 43,327 thousand) from investors. A new coupon rate of 0.1% p.a. was set for the remaining bonds.

At the dates of placement of the RUB-denominated bonds, the Group entered into cross-currency interest rate swaps for the purpose of managing currency risks (Note 7) and exchanging interest expense from debt securities issued, denominated in RUB, RON, to the currency required by the Group (EUR, USD) to Finance credit projects in the required currency. The Group applies hedge accounting for the fair value of the bond issue in Romanian lei placed on 27 September 2016 (Note 16). The effects of using cross-currency interest rate swaps and fair value hedge operations are disclosed in Note 21.

Among other things, the Group used the proceeds from issuance of debt instruments and placement of bonds to expand its loan portfolio.

*(Thousands of euros)***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 2017, the unpaid portion of the Bank's subscribed capital in the amount of EUR 985,038 thousand (31 December 2016: EUR 986,947 thousand) is the amount of contributions that have not been made yet by the Bank's member countries and the amount of unallocated equity contributions totaling EUR 175,500 thousand (31 December 2016: EUR 175,500 thousand).

The Government of Mongolia made an additional contribution of EUR 1,909 thousand to the Bank's equity on 27 December 2017.

On 9 March 2016, in accordance with the Memorandum of Understanding signed at the 102nd meeting of the IIB's Council (20-21 November 2014), the Government of Hungary contributed EUR 10,000 thousand to the Bank's equity.

As a result, the paid-in capital of the International Investment Bank totaled EUR 314,962 thousand (31 December 2016: EUR 313,053 thousand).

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 2016	(1,664)	31,453
Net unrealized gains on available-for-sale investment securities	10,673	–
Realized gains on available-for-sale investment securities reclassified to the income statement	(10,515)	–
Revaluation of buildings	–	(18,508)
At 31 December 2016	(1,506)	12,945
Net unrealized gains on available-for-sale investment securities	9,145	–
Realized gains on available-for-sale investment securities reclassified to the income statement	(7,399)	–
Revaluation of buildings	–	803
At 31 December 2017	240	13,748

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. Commitments and contingencies****Legal**

In the ordinary course of business, the Group 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 Group. 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 Group 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 Group's further actions to collect bad debt and/or realize respective repossession rights is higher than the amount collected and also when the Group 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 Group 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 Group did not obtain insurance coverage related to temporarily discontinued operations or the Group's obligations to third parties.

Taxation

The IIB is an international institution operating on the basis of the Intergovernmental Agreement on the Establishment of the International Investment Bank (the "Agreement") and the Statute that constitutes an integral part of the Agreement. Pursuant to the Agreement, the Bank is exempt from any national or local direct taxes or duties effective in the territories of its member states. For taxation purposes, its subsidiaries are subject to the provisions of the effective Russian tax, currency and customs legislation.

Credit-related commitments

At any time, the Group may have outstanding commitments to extend loans. These commitments take the form of approved loan agreements.

As at 31 December 2017, credit-related commitments of the Group comprised off-balance credit-related commitments, in particular undrawn loan facilities, guarantees and reimbursement obligations.

The primary purpose of credit-related commitments is to ensure that funds are available to customers as required. Guarantees issued, which represent irrevocable assurances that the Group will make payments in the event that a customer cannot meet its obligations to third parties, carry the same credit risk as loans. Reimbursement obligations, which are irrevocable reimbursement obligations of the Group issued on behalf of banks issuing documentary letters of credit that are accepted and paid by foreign partner banks up to a stipulated amount under specific terms and conditions, are collateralized by the underlying shipments of goods to which they relate and therefore carry less risk than a direct borrowing. Undrawn loan facilities represent unused portions of funds to be issued as loans.

Off-balance credit-related commitments are presented in the table below as at 31 December 2017 and 31 December 2016.

	<u>2017</u>	<u>2016</u>
Undrawn loan facilities	116,161	33,103
Reimbursement obligations	32,812	9,898
Guarantees issued	15,425	4,934
Total credit-related commitments	<u>164,398</u>	<u>47,935</u>

19. Leases**Group as lessor**

The Group provides its investment property for operating leases. As at 31 December 2017, the Group's non-cancelable operating lease rentals amount to EUR 6,819 thousand (31 December 2016: EUR 4,752 thousand) and will be settled within 1-5 years.

*(Thousands of euros)***20. Interest income and interest expenses**

Net interest income comprises:

	<i>2017</i>	<i>2016</i>
Loans to customers	19,754	13,886
Loans to banks	6,908	6,462
Available-for-sale investment securities	6,006	5,091
Deposits with banks and other financial institutions, including cash and cash equivalents	3,252	4,041
Held-to-maturity investment securities	–	2,975
Other	43	–
Interest income	35,963	32,455
Debt securities issued	(27,851)	(22,511)
Long-term loans of banks	(2,377)	(1,798)
Funds raised under repurchase agreements	(1,940)	(1,839)
Current customer accounts	(237)	(305)
Due to banks and other financial institutions	(161)	(1,198)
Interest expenses	(32,566)	(27,651)
Net interest income	3,397	4,804

In 2017, interest income accrued on impaired loans issued amounted to EUR 122 thousand (2016: EUR 185 thousand).

21. Net gains from operations in foreign currencies and with derivatives

Gains less losses from operations in foreign currencies and with derivatives comprised:

	<i>2017</i>	<i>2016</i>
Derivative financial instruments and operations with foreign currencies		
Net gains from dealing in foreign currencies and operations with derivatives	29,915	9,068
Net (losses)/gains from revaluation of derivative financial instruments	(6,419)	32,330
Total derivative financial instruments and operations with foreign currencies	23,496	41,398
Fair value hedge operations		
Net gains from fair value hedge operations	1,016	–
Net losses from revaluation of fair value hedge operations	(3,633)	(1,536)
Net gains from revaluation of the hedged object	2,553	1,290
Total fair value hedge operations	(64)	(246)
Translation differences		
Net losses from revaluation of assets and liabilities in foreign currencies	(7,483)	(31,173)
Net gains from operations in foreign currencies and with derivatives	15,949	9,979

*(Thousands of euros)***22. General and administrative expenses**

General and administrative expenses comprise:

	<u>2017</u>	<u>2016</u>
Employee compensations and employment taxes	13,105	13,001
Depreciation of property, equipment and intangible assets (Note 12)	2,008	1,974
IT-expenses, inventory and occupancy expenses	1,842	1,715
Expenses related to business travel, representative and accommodation expenses	805	682
Professional services	559	1,019
Other	553	548
General and administrative expenses	<u>18,872</u>	<u>18,939</u>

23. Risk management**Risk management framework**

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

The Group's risk management activities are intended to:

- ▶ Identify, analyze and manage risks faced by the Group.
- ▶ 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 professional risk management for the bank transactions.

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

Risk management system

Integrated into the whole vertical organizational structure of the Group and all areas of the Group's activities, the risk management system makes it possible to identify in a timely manner and effectively manage different types of risks.

Risk management involves all of the Group's divisions in the evaluating, assuming, and controlling risks ("Three lines of defense"):

- ▶ Risk-taking (1st line of defense): the Group's divisions directly preparing and conducting transactions, are involved in the identification, assessment, and monitoring of risks and comply with internal regulations on risk management, as well as give due consideration to the risk level in the preparation of transactions.
- ▶ Risk management (2nd line of defense): the division responsible for risk management develops risk management tools and methodology, assesses and monitors the risk level, prepares reports on risks, carries out risk aggregation, and calculates the amount of total capital requirements.
- ▶ Internal audit (3rd line of defense): independent quality assessment for existing risk management processes, identification of violations, and proposals for the improvement of the risk management system.

The Group's operations are managed taking into account the level of the risk appetite approved by the Council and its integration into a system of limits and restrictions insuring the acceptable level of risk for aggregated positions, transparent distribution of total risk limit among the activities of the Group.

The Bank's Council, the Board, the Finance Committee, the Credit Committee and the Risk Management Department are responsible for managing the Group's risks.

(Thousands of euros)

23. Risk management (continued)

Risk management system (continued)

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 divisions and committees of the Bank.

The Finance Committee determines approaches to forming the optimal structure of the balance sheet, taking into account information of current and expected level of risks associated with assets and liabilities management within the established limits and other restrictions. It also ensures management and control over the credit risk, market risk, operational risk, reputational risk, legal risk and liquidity risk and reviews the limit-setting offers.

The Credit Committee manages the Group's loan portfolio in accordance with its effective lending policy, aligns operation of the Bank's divisions in terms of the credit risk management and reviews the offers for setting credit risk limits in respect of the certain counterparties.

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 Group's performance.

During 2017, further development of the risk management system started in 2013 was aimed at implementation of Basel standards and best practices of development banks within the Group.

In compliance with the existing procedures, twice a year the Group sets and reviews limits for counterparties for the purpose of performing financial transactions and assessing their creditworthiness. As part of the lending activity analysis, the Group continuously monitored the level of its loan assets risk. During the reporting period, the Group sent its specialists to certain borrowers in order to monitor the implementation of the projects and identify potential primary evidence of impairment of loan assets.

To control and monitor the compliance with limits, the Group 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 and stop-loss limits. In addition, the Group's management receives regular reports on the status of risks within the Group.

Risk appetite

The risk appetite is the aggregate amount of risk taken by the Group to achieve its strategic goals and objectives. By approving the level of risk appetite, the Bank's Council determines the willingness to accept a risk or the amount of equity and liquidity that the Bank is willing to risk in the implementation of this strategy.

Risk appetite consists of 4 main components:

- ▶ The allocation of capital and liquidity (if necessary).
- ▶ Target allocation of capital across the main types of risk.
- ▶ The level of risk and target risk appetite in the context of the main performance indicators of the Group and risks significant for the Group.
- ▶ Determining levels of tolerance.

The procedure for determining the Group's risk appetite shall be defined by the Risk Management Department and submitted for review by the Board and approval by the Council of the Bank.

The risk appetite shall be approved by the Council of the Bank on an annual basis for the next year and shall be a major factor of the Group's strategic limits determining the thresholds for the Group's key performance indicators and the Group's significant risks.

(Thousands of euros)

23. Risk management (continued)

Risk management system (continued)

In determining the risk appetite, the Group assesses whether the specified risk appetite is acceptable in the current time period and whether it will be acceptable in the future, taking into account:

- ▶ Expectations of the founders concerning the level of profitability.
- ▶ International regulatory standards.
- ▶ Current and expected future volume of transactions.
- ▶ Current and expected future structure of significant risks.
- ▶ Current and expected future level of aggregate capital.

Based on the risk appetite determined by the Council, the Board annually approves the Group's limits, sublimits, and risk indicators, which should not exceed the target values of the risk appetite.

Risk identification

The Group identifies and manages both external and internal risk factors throughout its organizational structure. As a result of regular analysis of the Group's exposure to different types of risks performed by the Risk Management Department, the Group 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 the Finance Committee and, if necessary, also communicated to the Board along with the recommendations on possible risk mitigation measures.

Risk assessment, management and control

The Group's risk exposure is primarily reduced by means of collective decision-making. Strict allocation of responsibilities between divisions and officers of the Group, 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, if necessary, updated by the Group in order to reflect changed market conditions and improve the risk management methodology.

The risk monitoring system comprises:

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

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

(Thousands of euros)

23. Risk management (continued)

Credit risk (continued)

System of credit risk management

The Group'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.

Pursuant to the established procedure, the Credit Committee establishes the limits per borrower/group of related borrowers. The Credit Committee structures the transaction to minimize credit risk. The Loan Operations Analysis Department, together with the Risk Management Department, is responsible for ongoing control over the quality of the Group's loan portfolio.

Upon preparation of a transaction by the initiating unit it is reviewed by the Credit Committee, and then it is approved by the Board. The Board is responsible for all direct credit risk exposures in the amount of up to 15% of the Group'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 Customer Relations Department. Based on the background information on the deal, the Customer Relations Department takes a decision whether to continue work with the client or not. In case of a positive decision, the Loan Operations Analysis Department makes full examination of the deal and sends the full set of required documents for reviewing the loan/credit application to the Legal Department, Risk Management Department, Security Department, Strategic Development and Analysis Department, Internal Control Department, Compliance Control Department, Operational Department, Financial Department, and Structured and Debt Financing Department. These departments prepare expert opinions in the framework of their competence. The loan/credit application is subject to review by the Credit Committee based on the Loan Operations Analysis Department's materials and expert opinions received from the departments. The procedure of making lending decisions comprises the following steps: Step 1 includes reviewing the application and making a decision by the Credit Committee (if such issue falls within its competence); Step 2 includes making a decision by the Board of the Group (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 country in order to obtain the final approval from the country of origin of the borrower or making a decision by the Council of the Bank (if such issue falls within its competence).

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

To mitigate credit risk, the Group limits concentrations of exposure by 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 of the borrowers and their ability to repay interest and principal, and on correspondent limits modification (if necessary).

The Group 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 Group. 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.

(Thousands of euros)

23. Risk management (continued)

Credit risk (continued)

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 Group 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 Group applies the following types of collateral for recovery of loans and fulfillment of obligations:

- ▶ Pledge of equipment and goods in turnover;
- ▶ Pledge of real estate (mortgage) and title;
- ▶ Pledge of construction investment agreements.

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

The Group assumes that the fair value of the collateral is its value estimate recognized by the Group 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 Group's internal expert estimate, or carrying amount of the collateral including adjustment coefficient (discount). Where the market value of the collateral is assessed as impaired, the borrowers are usually required to provide additional collateral.

Portfolio of loans to banks and customers (less allowance for impairment) by type of collateral is analyzed in Notes 9 and 10.

Maximum exposure to credit risk

The maximum exposure to credit risk for the components of the consolidated 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 the financial instruments are recorded at fair value, their carrying amounts represent the current credit risk exposure but not the maximum credit 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 10.

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

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 consolidated 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.

(Thousands of euros)

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

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 customer'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.

The following table provides information on the credit quality of long-term loans to banks and trade financing loans (Note 9) and loans to customers (Note 10) as at 31 December 2017 and 31 December 2016:

2017	Loan amount	Allowance for impairment	Loan amount, including allowance for impairment	Impairment to loan amount ratio, %
Trade financing loans without any signs of impairment identified				
Standard loans				
- Russian Federation	23,298	–	23,298	–
- Republic of Belarus	3,239	–	3,239	
Long-term loans to banks without any signs of impairment identified				
Standard loans				
- Russian Federation	60,147	–	60,147	–
- Republic of Cuba	49,863	–	49,863	–
- Mongolia	33,735	–	33,735	–
- Socialist Republic of Vietnam	25,252	–	25,252	–
Impaired loans				
- Russian Federation	15,254	(9,153)	6,101	60
	210,788	(9,153)	201,635	4.3
Loans to customers without any signs of impairment identified				
Standard loans				
- Russian Federation	81,817	–	81,817	–
- Romania	63,289	–	63,289	–
- Slovak Republic	60,464	–	60,464	–
- Republic of Bulgaria	51,987	–	51,987	–
- Czech Republic	49,967	–	49,967	–
- Hungary	42,910	–	42,910	–
- Republic of Ecuador	34,763	–	34,763	–
- Republic of Panama	29,775	–	29,775	–
- Mongolia	24,425	–	24,425	–
- Kingdom of the Netherlands	5,847	–	5,847	–
- USA	1,666	–	1,666	–
Restructured loans				
- Republic of Bulgaria	6,008	(300)	5,708	5.0
Impaired loans				
- Romania	15,151	(5,255)	9,896	34.7
	468,069	(5,555)	462,514	1.2
Total loans	678,857	(14,708)	664,149	2.2

(Thousands of euros)

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

2016	Loan amount	Allowance for impairment	Loan amount, including allowance for impairment	Impairment to loan amount ratio, %
Trade financing loans without any signs of impairment identified				
Standard loans				
- Russian Federation	953	–	953	–
Long-term loans to banks without any signs of impairment identified				
Standard loans				
- Mongolia	47,970	–	47,970	–
- Russian Federation	26,425	–	26,425	–
- Socialist Republic of Vietnam	19,019	–	19,019	–
	94,367	–	94,367	–
Loans to customers without any signs of impairment identified				
Standard loans				
- Russian Federation	61,213	–	61,213	–
- Republic of Bulgaria	53,477	–	53,477	–
- Republic of Ecuador	39,570	–	39,570	–
- Republic of Panama	36,276	–	36,276	–
- Romania	25,205	–	25,205	–
- Czech Republic	22,930	–	22,930	–
- USA	6,108	–	6,108	–
- Mongolia	5,683	–	5,683	–
- Slovak Republic	308	–	308	–
Watch loans to customers				
- Romania	15,030	(2,254)	12,776	15.0
Restructured loans				
- Republic of Bulgaria	5,779	(289)	5,490	5.0
Impaired loans				
- Slovak Republic	8,103	(8,103)	–	100
- Republic of Bulgaria	6,666	(6,666)	–	100
	286,348	(17,312)	269,036	6.0
Total loans	380,715	(17,312)	363,403	4.5

Where possible, the Group 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.

(Thousands of euros)

23. Risk management (continued)

Credit risk (continued)

Impairment assessment

The Group creates allowance for impairment of loans that represents its estimate of losses incurred in its loan portfolio. The Group writes off a loan balance against related allowances for impairment of loans 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 borrower'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 Group determines the allowances appropriate for each individually significant loan on an individual basis. Due to a limited number of borrowers, the Group 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 dividend 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, or more frequently, unless unforeseen circumstances require more careful attention.

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

Liquidity risk

Liquidity risk is the risk of loss resulting from the Group'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 Group'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 Group) and/or an unforeseen need of immediate and simultaneous discharge of its financial obligations.

Liquidity management is an integral part of general policy for the Group's assets and liabilities management (ALM) and operates within the established limits and restrictions related to management of risks (liquidity, interest rate and currency risk) and the Group's balance sheet items, and in accordance with the documents of strategic, tactical and operating planning.

Procedures for the Group's liquidity position management, ensuring the Group's ability to meet its obligations in full and on a timely basis and efficient resources management, are stipulated in the Regulations for IIB's Liquidity Position Management that enables the development of the liquidity position management function provided for by the IIB's Assets and Liabilities Management Policy, as an integral part of general function of the Group's management.

Decision making matrix related to liquidity management includes a strategic level of liquidity management (the Council), tactical level (the Board and special-purpose committees) and operational level (responsible structural divisions). Asset and Liability Management Department (DUAP or ALM Unit) is responsible for organizing and aligning management of the Group's liquidity position. The Group manages its liquidity position in accordance with planning horizons (up to 6 months) and possible scenarios of movements in liquidity position (stable, stressed).

Main instrument of liquidity position management under the stable scenario is a Plan of Cash Flows defining the cash flow by balance sheet products/instruments and taking into account the plan of future financial operations. The Group determines the balance sheet gaps, payment schedule and need in financing of future operations based on the Plan of Cash Flows. As a result of application of these instruments, DUAP issues appropriate recommendations to responsible structural divisions.

The Group has implemented a liquidity buffer to manage the Group's liquidity under the stressed scenario. Application of the liquidity buffer enables the Group to promptly monitor the sustainability and stability of the Group's balance sheet structure in case of liquidity shortage that is critical to the Group's solvency.

*(Thousands of euros)***23. Risk management (continued)****Liquidity risk (continued)**

The liquidity buffer is formed primarily due to liquidity reserves, namely securities recognized in the Group's balance sheet and included in the Lombard lists of the European Central Bank and Bank of Russia, and nostro accounts with banks and other financial institutions. The Group calculates its liquidity reserves as at the reporting date and for the next six monthly reporting dates (forecast). Liquidity buffer may be used to close the negative net position. As at 31 December 2017, the liquidity buffer amounts to EUR 83.5 million (31 December 2016: EUR 75.9 million).

Off-balance sheet credit related commitments of the Group are stated in accordance with contractual maturities in the table presented below. In case of absence of contractual schedule of the credit related commitments, these obligations are included into the earliest date, at which the client can demand their execution.

	<u>2017</u>	<u>2016</u>
Less than 1 month	25,835	33,213
1 to 3 months	72,744	3,650
3 months to 1 year	41,489	6,138
1 to 5 years	24,330	4,934
Off-balance credit-related commitments	<u>164,398</u>	<u>47,935</u>

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*(Thousands of euros)***23. 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. Quoted available-for-sale debt securities and equity instruments were included in “Less than 1 month” category as they are highly liquid investment securities, shares and depositary receipts which the Group may sell in the short term on the arm-length basis. Available-for-sale investment securities pledged under repurchase agreements are presented on the basis of periods from the reporting date to the expiry date of respective contractual obligations of the Group.

	2017							2016						
	<i>Less than 1 month</i>	<i>1 to 3 months</i>	<i>3 months to 1 year</i>	<i>1 to 5 years</i>	<i>Over 5 years</i>	<i>Past due</i>	<i>Total</i>	<i>Less than 1 month</i>	<i>1 to 3 months</i>	<i>3 months to 1 year</i>	<i>1 to 5 years</i>	<i>Over 5 years</i>	<i>Past due</i>	<i>Total</i>
Assets														
Cash and cash equivalents	65,445	652	–	–	–	–	66,097	93,031	–	–	–	–	–	93,031
Deposits with banks and other financial institutions	5,026	7,097	25,034	8,732	–	–	45,889	14,254	–	27,472	3,611	–	–	45,337
Derivative financial instruments	935	–	5,072	1,754	–	–	7,761	–	116	14,246	–	–	–	14,362
Available-for-sale investment securities	138,737	54,783	21,907	–	–	–	215,427	170,849	379	502	97,577	–	–	269,307
Loans to banks	1,322	53,491	49,786	90,935	–	6,101	201,635	–	3,059	16,638	71,051	3,619	–	94,367
Loans to customers	8,965	8,719	77,334	147,277	210,323	9,896	462,514	2,066	10,139	59,833	133,047	63,951	–	269,036
Other financial assets	489	57	19	163	–	–	728	166	123	381	750	–	–	1,420
Total assets	220,919	124,799	179,152	248,861	210,323	15,997	1,000,051	280,366	13,816	119,072	306,036	67,570	–	786,860
Liabilities														
Due to banks and other financial institutions	–	(30,982)	(34,059)	(470)	–	–	(65,511)	(48,558)	–	–	(70,367)	–	–	(118,925)
Current customer accounts	(8,593)	–	–	–	–	–	(8,593)	(9,218)	–	–	–	–	–	(9,218)
Derivative financial instruments	–	(89)	(1,213)	(13,771)	–	–	(15,073)	(2,080)	–	(1,671)	(7,872)	–	–	(11,623)
Long-term loans of banks	–	(24)	(59,967)	(18,819)	(16,782)	–	(95,592)	–	–	(14,345)	(59,004)	–	–	(73,349)
Debt securities issued	–	(3,906)	(26,519)	(478,788)	–	–	(509,213)	–	–	(152,484)	(120,044)	–	–	(272,528)
Other financial liabilities	(762)	(953)	(396)	(37)	–	–	(2,148)	(348)	–	(933)	(582)	–	–	(1,863)
Total liabilities	(9,355)	(35,954)	(122,154)	(511,885)	(16,782)	–	(696,130)	(60,204)	–	(169,433)	(257,869)	–	–	(487,506)
Net position	211,564	88,845	56,998	(263,024)	193,541	15,997	303,921	220,162	13,816	(50,361)	48,167	67,570	–	299,354
Accumulated net position	211,564	300,409	357,407	94,383	287,924	303,921		220,162	233,978	183,617	231,784	299,354	299,354	

*(Thousands of euros)***23. Risk management (continued)****Analysis of financial liabilities by remaining contractual maturities**

The table below summarizes the maturity profile of the Group's financial liabilities at 31 December 2017 and 31 December 2016 based on contractual undiscounted repayment obligations except for gross settled derivatives that are shown by contractual maturity. Debt securities with put options (offers) are presented as if investors will exercise their options at the earliest possible date. The Group expects that it will have to make payment on current bond offers.

<i>At 31 December 2017</i>	<i>Less than 1 month</i>	<i>1 to 3 months</i>	<i>3 to 12 months</i>	<i>1 to 5 years</i>	<i>Over 5 years</i>	<i>Total</i>
Financial liabilities						
Due to banks and other financial institutions	–	31,331	34,783	470	–	66,584
Current customer accounts	8,593	–	–	–	–	8,593
Net settled derivative liabilities	(904)	–	–	–	–	(904)
Gross settled derivative financial instruments						
- Contractual amounts payable	–	37,664	155,912	348,158	–	541,734
- Contractual amounts receivable	–	(42,735)	(169,034)	(350,742)	–	(562,511)
Long-term loans of banks	–	60,496	230	19,498	19,624	99,848
Debt securities issued	–	6,935	46,200	523,383	–	576,518
Other liabilities	762	953	396	37	–	2,148
Total undiscounted financial liabilities	8,451	94,644	68,487	540,804	19,624	732,010
<i>At 31 December 2016</i>	<i>Less than 1 month</i>	<i>1 to 3 months</i>	<i>3 to 12 months</i>	<i>1 to 5 years</i>	<i>Over 5 years</i>	<i>Total</i>
Financial liabilities						
Due to banks and other financial institutions	48,590	–	–	73,120	–	121,710
Current customer accounts	9,218	–	–	–	–	9,218
Net settled derivative liabilities	2,080	–	–	–	–	2,080
Gross settled derivative financial instruments						
- Contractual amounts payable	–	47,000	147,836	166,726	–	361,562
- Contractual amounts receivable	–	(47,089)	(173,371)	(173,625)	–	(394,085)
Long-term loans of banks	–	–	15,078	60,989	–	76,067
Debt securities issued	–	–	168,367	128,406	–	296,773
Other liabilities	348	–	933	582	–	1,863
Total undiscounted financial liabilities	60,236	(89)	158,843	256,198	–	475,188

*(Thousands of euros)***23. Risk management (continued)****Market risk**

Market risk is the risk that the Group 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 Group 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.

The Finance Committee coordinates the Group's market risk management policy and reviews and provides recommendations on management of market risks to the Management Board.

The Treasury Department performs strategic 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 Group'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 Group'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 Group applies a VaR methodology to assess currency and equity risks. VaR is a method used in measuring maximum risk of the Group, 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 Group 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 Group is carried out in major currencies and financial instruments of the Group attributable to a securities portfolio.

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

As at 31 December 2017 and 31 December 2016, final data on value at risk (VaR) assessment in relation to currency and price risks assumed by the Group are represented as follows:

	<u>2017</u>	<u>2016</u>
Fixed income securities price risk	1,005	2,325
Equity securities price risk	125	–
Currency risk	45	27

(Thousands of euros)

23. Risk management (continued)

Market risk (continued)

Despite the fact that 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.
- ▶ 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 Group'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.

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*(Thousands of euros)***23. Risk management (continued)****Market risk (continued)**

The Group has assets and liabilities denominated in several foreign currencies. The financial position and the cash flows are exposed to the effects of fluctuations in foreign currency exchange rates. Non-monetary financial instruments and financial instruments denominated in functional currency are not exposed to currency risk.

The Group's exposure to currency risk as at 31 December 2017 and 31 December 2016 is presented below:

	2017					2016				
	EUR	USD	RUB	Other currencies	Total	EUR	USD	RUB	Other currencies	Total
Non-derivative financial Assets										
Cash and cash equivalents	50,488	1,730	13,501	378	66,097	66,125	19,969	6,778	159	93,031
Deposits with banks and other financial institutions	28,936	16,953	–	–	45,889	40,568	4,769	–	–	45,337
Available-for-sale investment securities	111,516	102,202	–	1,709	215,427	208,628	53,070	7,609	–	269,307
Long-term loans to banks	147,253	54,382	–	–	201,635	53,574	40,793	–	–	94,367
Loans to customers	247,804	108,254	64,097	42,359	462,514	131,906	137,130	–	–	269,036
Other financial assets	186	323	214	5	728	225	14	927	254	1,420
Total non-derivative financial assets	586,183	283,844	77,812	44,451	992,290	501,026	255,745	15,314	413	772,498
Liabilities										
Due to banks and other financial institutions	(34,608)	(29,337)	–	(1,566)	(65,511)	(36,981)	(81,944)	–	–	(118,925)
Current customer accounts	(8,481)	(112)	–	–	(8,593)	(9,089)	(129)	–	–	(9,218)
Long-term loans of banks	(82,694)	–	–	(12,898)	(95,592)	(59,039)	(14,310)	–	–	(73,349)
Debt securities issued	(90,017)	–	(267,112)	(152,084)	(509,213)	(30,046)	–	(151,515)	(90,967)	(272,528)
Other financial liabilities	(546)	(175)	(1,427)	–	(2,148)	(529)	(49)	(1,106)	(179)	(1,863)
Total non-derivative financial liabilities	(216,346)	(29,624)	(268,539)	(166,548)	(681,057)	(135,684)	(96,432)	(152,621)	(91,146)	(475,883)
Net balance sheet position (excluding derivative financial instruments)	369,837	254,220	(190,727)	(122,097)	311,233	365,342	159,313	(137,307)	(90,733)	296,615
Derivative financial instruments										
Claims	190,457	–	197,443	132,639	520,539	125,117	–	145,832	90,318	361,267
Liabilities	(296,697)	(220,909)	–	(10,245)	(527,851)	(224,955)	(124,785)	(8,788)	–	(358,528)
Net balance sheet position including derivative financial instruments	263,597	33,311	6,716	297	303,921	265,504	34,528	(263)	(415)	299,354

*(Thousands of euros)***23. Risk management (continued)****Market risk (continued)*****Interest rate risk***

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

The sensitivity of the consolidated income statement is the effect of the assumed changes in interest rates on net interest income for one year, based on financial assets and financial liabilities with floating rates. The sensitivity of equity is calculated by revaluing inactive traded available-for-sale securities with fixed rates as at 31 December 2017 for the effects of the assumed changes in interest rates based on the assumption that there are parallel shifts in the yield curve.

	<i>Increase in basis points</i>	<i>Sensitivity of the income statement</i>	<i>Sensitivity of equity</i>
	<i>2017</i>	<i>2017</i>	<i>2017</i>
RGBEY	0.75%	(719)	–
Libor EUR	0.25%	792	–
Libor USD	0.70%	(214)	–
3Y Swap-RON	6.74%	(15,479)	–
YTM 5Y US Treasuries	1.30%	1,761	–
YTM 5Y German Treasuries	0.50%	962	–

	<i>Decrease in basis points</i>	<i>Sensitivity of the income statement</i>	<i>Sensitivity of equity</i>
	<i>2017</i>	<i>2017</i>	<i>2017</i>
RGBEY	1.75%	1,677	–
Libor EUR	0.01%	(32)	–
Libor USD	0.08%	24	–
3Y Swap-RON	4.47%	10,266	–
YTM 5Y US Treasuries	0.50%	(677)	–
YTM 5Y German Treasuries	0.40%	(192)	–

	<i>Increase in basis points</i>	<i>Sensitivity of the income statement</i>	<i>Sensitivity of equity</i>
	<i>2016</i>	<i>2016</i>	<i>2016</i>
RGBEY	1.00%	(956)	(233)
Libor EUR	0.12%	128	–
Libor USD	0.60%	405	–
3Y Swap-RON	0.50%	(1,148)	–
YTM 5Y US Treasuries	0.70%	973	–
YTM 5Y German Treasuries	0.40%	770	–

	<i>Decrease in basis points</i>	<i>Sensitivity of the income statement</i>	<i>Sensitivity of equity</i>
	<i>2016</i>	<i>2016</i>	<i>2016</i>
RGBEY	3.00%	2,868	699
Libor EUR	0.08%	(86)	–
Libor USD	0.08%	(54)	–
3Y Swap-RON	0.50%	1,148	–
YTM 5Y US Treasuries	0.50%	695	–
YTM 5Y German Treasuries	0.40%	(770)	–

(Thousands of euros)

23. Risk management (continued)

Market risk (continued)

Indices listed in the tables above:

RGBEY – Russian Government Bonds Effective Yield until Redemption;

Libor EUR – London inter-bank EUR offer rate (3 and 6 months);

Libor USD – London inter-bank USD offer rate (1, 3 and 6 months);

3Y Swap-RON – three-year bid rate in Romanian leu on swap market;

YTM 5Y US Treasuries – yield-to-maturity of five-year US Treasuries;

YTM 5Y German Treasuries – yield-to-maturity of five-year Germany Treasuries.

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 Group'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 Group continuously seeks to enhance its business processes, operating structure and personnel incentives system in order to minimize the impact of operational risk.

24. Fair value measurements

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 Group using available market information, where it exists, and appropriate valuation methodologies. However, judgment is necessarily required to interpret market data to determine the 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 Group 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 that use inputs which have a significant effect on the recognized fair value that are not based on observable market data.

*(Thousands of euros)***24. Fair value measurements (continued)****Fair value hierarchy (continued)**

For the purpose of fair value disclosures, the Group has determined classes of assets and liabilities on the basis of the nature, characteristics and risks of the asset or liability, and the level of the fair value hierarchy. The following table shows an analysis of financial instruments recorded at fair value by level of the fair value hierarchy as at 31 December 2017:

	<i>Level 1</i> <i>2017</i>	<i>Level 2</i> <i>2017</i>	<i>Level 3</i> <i>2017</i>	<i>Total</i> <i>2017</i>
Assets measured at fair value				
Derivative financial assets	–	7,761	–	7,761
Government bonds of member countries	45,891	–	–	45,891
Corporate bonds	149,277	18,544	–	167,821
Quoted equity instruments	1,710	5	–	1,715
Investment property	–	–	21,853	21,853
Property and equipment – buildings	–	–	67,572	67,572
Liabilities measured at fair value				
Derivative financial liabilities	–	15,073	–	15,073
Assets for which fair values are disclosed				
Cash and cash equivalents	85	66,012	–	66,097
Deposits with banks and other financial institutions	–	–	45,889	45,889
Loans to banks	–	–	201,743	201,743
Loans to customers	–	–	465,973	465,973
Liabilities for which fair values are disclosed				
Due to banks and other financial institutions	–	–	65,511	65,511
Current customer accounts	–	–	8,593	8,593
Long-term loans of banks	–	–	95,592	95,592
Debt securities issued	–	514,893	–	514,893

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*(Thousands of euros)***24. Fair value measurements (continued)****Fair value hierarchy (continued)**

The following table shows an analysis of financial instruments recorded at fair value by level of the fair value hierarchy as at 31 December 2016:

	<i>Level 1</i> <i>2016</i>	<i>Level 2</i> <i>2016</i>	<i>Level 3</i> <i>2016</i>	<i>Total</i> <i>2016</i>
Assets measured at fair value				
Derivative financial assets	–	14,362	–	14,362
Government bonds of member countries	70,561	–	–	70,561
Corporate bonds	194,003	4,739	–	198,742
Quoted equity instruments	–	4	–	4
Investment property	–	–	21,840	21,840
Property and equipment – buildings	–	–	67,527	67,527
Liabilities measured at fair value				
Derivative financial liabilities	–	11,623	–	11,623
Assets for which fair values are disclosed				
Cash and cash equivalents	104	92,927	–	93,031
Deposits with banks and other financial institutions	–	–	45,337	45,337
Loans to banks	–	–	88,558	88,558
Loans to customers	–	–	270,243	270,243
Liabilities for which fair values are disclosed				
Due to banks and other financial institutions	–	–	118,925	118,925
Current customer accounts	–	–	9,218	9,218
Long-term loans of banks	–	–	73,349	73,349
Debt securities issued	–	279,181	–	279,181

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 Group's financial instruments that are recorded in the consolidated financial statements. The table does not include the fair values of non-financial assets and non-financial liabilities.

	<i>Carrying amount</i> <i>2017</i>	<i>Fair value</i> <i>2017</i>	<i>Unrecognized gain/(loss)</i> <i>2017</i>	<i>Carrying amount</i> <i>2016</i>	<i>Fair value</i> <i>2016</i>	<i>Unrecognized gain/(loss)</i> <i>2016</i>
Financial assets						
Cash and cash equivalents	66,097	66,097	–	93,031	93,031	–
Deposits with banks and other financial institutions	45,889	45,889	–	45,337	45,337	–
Loans to banks	201,635	201,743	108	94,367	88,558	(5,809)
Loans to customers	462,514	465,973	3,459	269,036	270,243	1,207
Financial liabilities						
Due to banks and other financial institutions	65,511	65,511	–	118,925	118,925	–
Current customer accounts	8,593	8,593	–	9,218	9,218	–
Long-term loans of banks	95,592	95,592	–	73,349	73,349	–
Debt securities issued	509,213	514,893	(5,680)	272,528	279,181	(6,653)
Total unrecognized change in unrealized fair value			(2,113)			(11,255)

(Thousands of euros)

24. Fair value measurements (continued)

Fair value measurements

The Group determines the policies and procedures for both recurring fair value measurement, such as unquoted derivatives, investment property and buildings, and for non-recurring measurement, such as inventories.

External appraisers are involved for valuation of significant assets, such as buildings and real estate. Involvement of external appraisers is decided upon by the Bank's Finance Department. Unquoted derivatives are measured by the Finance Department.

Selection criteria include market knowledge, reputation, independence and compliance with professional standards.

Methodologies and assumptions

The following describes the methodologies and assumptions used to determine fair values of assets and liabilities recorded at fair value in the consolidated financial statements and of those items that are not measured at fair value in the consolidated statement of financial position, but their fair value is disclosed.

Assets for which fair value approximates their carrying amount

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

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

Management has estimated that as at 31 December 2017 and 31 December 2016 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 existing practice of renegotiating interest rates to reflect current market conditions, and, therefore, a majority of balances carries interest at rates approximating market interest rates.

Financial instruments with fixed and floating rates

The fair value of instruments with floating interest rates is approximately equal to their carrying amount. In case of significant changes of the market situation the interest rates on loans to customers and banks, and long-term loans of banks at a fixed interest rate may be revised. Consequently, the interest rates on the financial instruments issued or received shortly before the balance sheet date are not significantly different from the current interest rates for new instruments with similar credit risk and a similar maturity. If the Group determines that the rates for loans issued or borrowings are significantly different from the current market rates, the Group determines the fair value of such loans issued and borrowings. The valuation is based on the discounted cash flow method using current market interest rates for new financial instruments with similar credit risk and similar maturity. The discount rates depend on the currency, the maturity of the instrument and the credit risk of the counterparty. Management determines that the fair value of amounts due to banks and other financial institutions and long-term loans of banks did not differ significantly from their carrying amounts as at 31 December 2017 and 31 December 2016.

Investment property

The Group engages an independent appraiser for the investment property fair value measurement. As at the valuation date (31 December 2017), the fair values of investment property were based on the results of valuation performed by an accredited independent appraiser and the prices of market transactions using the market, cost and income approaches to fair value measurement.

The duration of the cash flows and the specific timing of inflows and outflows are determined by events such as rent reviews, lease renewal and related re-letting, redevelopment, or refurbishment. The appropriate duration is typically driven by market behavior that is a characteristic of the class of real property. Periodic cash flow is typically estimated as gross income less vacancy, non-recoverable expenses, collection losses, lease incentives, maintenance cost, agent and commission costs and other operating and management expenses. The series of periodic net operating income, along with an estimate of the terminal value anticipated at the end of the projection period, is then discounted.

*(Thousands of euros)***24. Fair value measurements (continued)****Methodologies and assumptions (continued)*****Property and equipment – buildings***

Fair value of the properties was determined using the market approach. This means that valuations performed by the appraiser are based on market transaction prices, significantly adjusted for difference in the nature, location or condition of the specific property. As at the valuation date (31 December 2017), the properties' fair values are based on valuations performed by an accredited independent appraiser and the prices of market transactions using the market, cost and income approaches to fair value measurement.

Significant unobservable inputs in determining the fair value of real estate properties

As at the valuation date (31 December 2017), the significant unobservable inputs used in determining the fair value of real estate properties included the average asking prices for sale of similar properties ranging from EUR 2,773 per sq. m (range minimum) to EUR 3,982 per sq. m (range maximum), and lease rates ranging from EUR 360 per sq. m. a year (minimum) to EUR 504 per sq. m. a year (maximum).

There were no transfers of financial instruments between Level 1 and Level 2 in 2017 and 2016.

Movements in Level 3 assets and liabilities at fair value

The following table shows a reconciliation of the opening and closing amount of Level 3 assets and liabilities that are recorded at fair value:

	<i>At 1 January 2017</i>	<i>Gains/(losses) recorded in profit or loss</i>	<i>Gains/(losses) recorded in comprehensive income</i>	<i>Purchases</i>	<i>Transfer to property and equipment</i>	<i>At 31 December 2017</i>
Assets						
Property and equipment – buildings	67,527	(1,108)	803	350	–	67,572
Investment property	21,840	(26)	–	39	–	21,853
Total	89,367	(1,134)	803	389	–	89,425

	<i>At 1 January 2016</i>	<i>Gains/(losses) recorded in profit or loss</i>	<i>Gains/(losses) recorded in comprehensive income</i>	<i>Purchases</i>	<i>Transfer to property and equipment</i>	<i>At 31 December 2016</i>
Assets						
Property and equipment – buildings	62,807	(1,174)	(18,508)	223	24,179	67,527
Investment property	33,819	(2,174)	–	14,374	(24,179)	21,840
Total	96,626	(3,348)	(18,508)	14,597	–	89,367

*(Thousands of euros)***25. Transferred financial assets that are not derecognized**

The table below provides a summary of the financial assets transferred by the Group in such a way that all the transferred financial assets do not qualify for derecognition:

<i>Transferred financial asset</i>	<i>Available-for-sale investment securities</i>		
	<i>Government</i>	<i>Corporate</i>	<i>Total</i>
	<i>bonds</i>	<i>bonds</i>	
	<i>2017</i>	<i>2017</i>	<i>2017</i>
Carrying amount of assets	17,877	58,846	76,723
Carrying amount of associated liabilities	(14,768)	(47,247)	(62,015)
Net position	3,109	11,599	14,708

<i>Transferred financial asset</i>	<i>Available-for-sale investment securities</i>		
	<i>Government</i>	<i>Corporate</i>	<i>Total</i>
	<i>bonds</i>	<i>bonds</i>	
	<i>2016</i>	<i>2016</i>	<i>2016</i>
Carrying amount of assets	17,883	80,575	98,458
Carrying amount of associated liabilities	(13,485)	(52,584)	(66,069)
Net position	4,398	27,991	32,389

Securities sold under repurchase agreements are transferred to a third party and the Group receives cash in exchange. If the securities increase or decrease in value, the Group may, in certain circumstances, require, or be required, to pay additional collateral in the form of cash and/or other securities. The Group has determined that it retains substantially all the risks and rewards of these securities, which include credit risk, market risk, country risk and operational risk, and therefore has not derecognized them. In addition, it recognizes a financial liability for cash received.

The fair value of investment securities available for sale sold under repurchase agreements is equal to their carrying amount (Note 24).

The related liabilities, which are recorded against the cash received for such transactions, are presented in amounts due to banks and other financial institutions in the consolidated statement of financial position as at 31 December 2017 (31 December 2016: in amounts due to banks and other financial institutions).

26. Segment information

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

Credit investment activity	Investment banking services, including long-term corporate and interbank financing
Treasury	Operations in financial markets, transactions with securities, derivative financial instruments and foreign currency, and liquidity management
Other operations	Operational leasing services, other operations

*(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 consolidated financial statements. The following table presents income, profit, assets and liabilities of the Group's operating segments:

2017	<i>Credit investment activity</i>	<i>Treasury</i>	<i>Other operations</i>	<i>Total</i>
Income				
<i>External customers</i>				
Interest income	26,662	9,263	38	35,963
Fee and commission income	1,763	–	–	1,763
Net gains from operations in foreign currencies and with derivatives	–	15,928	21	15,949
Net gains from available-for-sale investment securities	–	7,399	–	7,399
Dividend income	–	123	–	123
Income from lease of investment property	–	–	4,034	4,034
Reversal of allowance for impairment of other assets	–	–	29	29
Other segment income	329	–	214	543
Total income	28,754	32,713	4,336	65,803
Interest expenses	(18,656)	(13,910)	–	(32,566)
Fee and commission expense	(16)	(109)	(8)	(133)
Allowance for impairment of financial assets	(12,165)	–	–	(12,165)
Net losses from revaluation of investment property	–	–	(26)	(26)
Other segment expenses	(79)	(23)	(934)	(1,036)
Segment results	(2,162)	18,671	3,368	19,877
Other unallocated expenses				(18,872)
Profit for the period				1,005
Development portfolio	648,404	104,932	–	753,336
Other segment assets	15,997	229,906	96,801	342,704
Total segment assets	664,401	334,838	96,801	1,096,040
Total segment liabilities	359,918	334,477	5,983	700,378
Other segment information				
Capital expenditures	–	–	1,013	1,013

The Group's management separates the "Development portfolio" assets allocated within operating segments. The criteria of separation is orientation of the assets on the fulfilling of the Group's mission. "Development portfolio" includes loans to banks and loans to customers excluding impaired loan projects and the investments in debt securities purchased upon initial placement by the issuer.

(Thousands of euros)

26. Segment information (continued)

<i>2016</i>	<i>Credit investment activity</i>	<i>Treasury</i>	<i>Other operations</i>	<i>Total</i>
Income				
<i>External customers</i>				
Interest income	20,348	12,093	14	32,455
Fee and commission income	843	–	–	843
Net gains from operations in foreign currencies and with derivatives	–	10,033	(54)	9,979
Net gains from available-for-sale investment securities	–	10,515	–	10,515
Income from lease of investment property	–	–	3,442	3,442
Reversal of allowance for impairment of other assets	–	–	67	67
Other segment income	(331)	616	162	447
Total income	20,860	33,257	3,631	57,748
Interest expenses	(11,250)	(16,401)	–	(27,651)
Fee and commission expense	(5)	(128)	(5)	(138)
Allowance for impairment of financial assets	(7,646)	–	89	(7,557)
Net losses from revaluation of investment property	–	–	(2,174)	(2,174)
Other segment expenses	(162)	(68)	(257)	(487)
Segment results	1,797	16,660	1,284	19,741
Other unallocated expenses				(18,939)
Profit for the period				802
Development portfolio	363,403	68,349	–	431,752
Other segment assets	–	353,239	96,452	449,691
Total segment assets	363,403	421,588	96,452	881,443
Total segment liabilities	160,065	325,579	5,581	491,225
Other segment information				
Capital expenditures	–	–	1,065	1,065

In 2017, the Group's revenue from lease operations with two external counterparties (2016: two external counterparties) exceeded 20% of the Group's total revenue (2017: EUR 2,996 thousand; 2016: EUR 2,160 thousand).

Geographical information

Allocation of the Group's revenue from transactions with external customers and non-current assets based on the location of these customers and assets for the years ended 31 December 2017 and 31 December 2016 is presented in the table below:

	<i>2017</i>				<i>2016</i>			
	<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	9,346	17,417	9,200	35,963	7,755	16,095	8,600	32,450
Income from lease of investment property	3,860	174	–	4,034	3,442	–	–	3,442
Non-current assets	79,917	14,324	–	94,241	79,242	14,439	–	93,681

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

(Thousands of euros)

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

The geographical concentration of the Group's assets and liabilities based on the location of the Group's counterparties as at 31 December 2017 is presented below:

	<i>2017</i>										
	<i>Russian Federation</i>	<i>Republic of Bulgaria</i>	<i>Romania</i>	<i>Slovak Republic</i>	<i>Hungary</i>	<i>Mongolia</i>	<i>Socialist Republic of Vietnam</i>	<i>Czech Republic</i>	<i>Republic of Cuba</i>	<i>Other countries</i>	<i>Total</i>
Assets											
Cash and cash equivalents	1,209	792	226	35	–	–	–	36	–	63,799	66,097
Deposits with banks and other financial institutions	3,082	–	–	–	–	32,132	–	–	–	10,675	45,889
Derivative financial instruments	3,340	–	–	–	–	–	–	–	–	4,421	7,761
Available-for-sale investment securities	11,947	30,098	–	10,010	13,817	–	–	34,107	–	115,448	215,427
Loans to banks	89,545	–	–	–	–	33,735	25,252	–	49,863	3,240	201,635
Loans to customers	81,817	57,694	73,185	60,464	42,910	24,425	–	49,967	–	72,052	462,514
Other financial assets	382	6	–	–	5	5	–	1	–	329	728
Assets	191,322	88,590	73,411	70,509	56,732	90,297	25,252	84,111	49,863	269,964	1,000,051
Liabilities											
Due to banks and other financial institutions	1,460	–	–	7,508	–	–	–	1,566	–	54,977	65,511
Derivative financial instruments	4,480	–	1,213	–	–	–	–	–	–	9,380	15,073
Long-term loans of banks	9,959	7,470	–	–	20,367	–	–	–	–	57,796	95,592
Long-term securities issued	266,191	–	212,869	30,153	–	–	–	–	–	–	509,213
Other financial liabilities	1,658	33	15	8	–	237	–	–	–	197	2,148
Liabilities	283,748	7,503	214,097	37,669	20,367	237	–	1,566	–	122,350	687,537

*(Thousands of euros)***26. Segment information (continued)****Geographical information (continued)**

	2016									
	<i>Russian Federation</i>	<i>Republic of Bulgaria</i>	<i>Romania</i>	<i>Slovak Republic</i>	<i>Hungary</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	16,398	808	26	38	–	–	–	–	75,761	93,031
Deposits with banks and other financial institutions	7,159	–	–	–	–	–	–	–	38,178	45,337
Derivative financial instruments	2,980	–	–	–	–	–	–	–	11,382	14,362
Available-for-sale investment securities	44,688	49,482	36,713	10,286	3,475	–	–	–	124,663	269,307
Loans to banks	27,378	–	–	–	–	47,970	19,019	–	–	94,367
Loans to customers	61,213	58,967	37,981	308	–	5,683	–	22,930	81,954	269,036
Other financial assets	1,407	8	–	1	–	–	–	–	4	1,420
Assets	161,223	109,265	74,720	10,633	3,475	53,653	19,019	22,930	331,942	786,860
Liabilities										
Due to banks and other financial institutions	–	–	–	7,508	–	–	–	–	111,417	118,925
Derivative financial instruments	4,528	–	633	–	–	–	–	–	6,462	11,623
Long-term loans of banks	9,840	21,690	–	–	7,380	–	–	–	34,439	73,349
Long-term securities issued	151,434	–	90,967	30,127	–	–	–	–	–	272,528
Other financial liabilities	1,805	–	–	19	–	–	–	–	39	1,863
Liabilities	167,607	21,690	91,600	37,654	7,380	–	–	–	152,357	478,288

Other countries include non-member countries.

(Thousands of euros)

27. Offsetting of financial instruments

The table below shows the effect of enforceable master netting agreements and similar arrangements that do not result in an offset in the consolidated statement of financial position as at 31 December 2017:

	<i>Gross amount of recognized financial assets</i>	<i>Gross amount of recognized financial liabilities set off in the statement of financial position</i>	<i>Net amount of financial assets presented in the statement of financial position</i>	<i>Related amounts not set off in the statement of financial position</i>		<i>Net amount</i>
				<i>Financial instruments</i>	<i>Cash collateral received</i>	
2017						
Financial assets						
Financial assets pledged under repurchase agreements	76,723	–	76,723	(62,015)	–	14,708
Total	76,723	–	76,723	(62,015)	–	14,708
Financial liabilities						
Repurchase agreements	62,015	–	62,015	(62,015)	–	–
Total	62,015	–	62,015	(62,015)	–	–

The table below shows financial assets offset against financial liabilities in the consolidated statement of financial position as at 31 December 2016 as well as the effect of enforceable master netting agreements and similar arrangements that do not result in an offset in the consolidated statement of financial position:

	<i>Gross amount of recognized financial assets</i>	<i>Gross amount of recognized financial liabilities set off in the statement of financial position</i>	<i>Net amount of financial assets presented in the statement of financial position</i>	<i>Related amounts not set off in the statement of financial position</i>		<i>Net amount</i>
				<i>Financial instruments</i>	<i>Cash collateral received</i>	
2016						
Financial assets						
Financial assets pledged under repurchase agreements	98,458	–	98,458	(66,069)	–	32,389
Total	98,458	–	98,458	(66,069)	–	32,389
Financial liabilities						
Repurchase agreements	66,069	–	66,069	(66,069)	–	–
Total	66,069	–	66,069	(66,069)	–	–

(Thousands of euros)

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 expenses and income for 2017 and 2016 are as follows:

	<i>Related party</i>	<i>31 December 2017</i>	<i>31 December 2016</i>
		<i>Carrying amount</i>	<i>Carrying amount</i>
Consolidated statement of financial position			
Current customer accounts	Key management personnel	1,420	1,783
Other liabilities	Key management personnel	593	416
	<i>Related party</i>	<i>2017</i>	<i>2016</i>
		<i>Income/(expense)</i>	<i>Income/(expense)</i>
Consolidated income statement			
Interest expenses on current customer accounts	Key management personnel	(52)	(61)
Net interest expenses after allowance for impairment of loans		(52)	(61)
Expenses from operating activities		(52)	(61)
Employee benefits	Key management personnel	(1,398)	(1,365)
Compensation for travel expenses and medical insurance	Key management personnel	(32)	(55)
Operating expenses		(1,430)	(1,420)
Net loss for the year		(1,482)	(1,481)

29. Changes in liabilities arising from financing activities

	<i>Note</i>	<i>Debt securities issued</i>	<i>Long-term loans of banks</i>	<i>Total liabilities arising from financing activities</i>
Carrying amount at 31 December 2015		212,724	44,187	256,911
Additions		67,398	60,000	127,398
Repayment		(43,910)	(29,569)	(73,479)
Interest paid		(23,493)	(2,831)	(26,324)
Translation differences		37,380	(277)	37,103
Non-cash transactions		(82)	–	(82)
Interest accrued		22,511	1,839	24,350
Carrying amount at 31 December 2016		272,528	73,349	345,877
Additions		348,661	36,185	384,846
Repayment		(88,290)	(13,451)	(101,741)
Interest paid		(24,522)	(1,690)	(26,212)
Translation differences		(26,095)	(1,178)	(27,273)
Non-cash transactions		(920)	–	(920)
Interest accrued		27,851	2,377	30,228
Carrying amount at 31 December 2017		509,213	95,592	604,805

Translation differences represent a daily revaluation of liabilities denominated in a currency other than the euro. The Group uses derivatives to mitigate the currency risks (Note 7).

*(Thousands of euros)***30. Capital adequacy**

Capital adequacy ratio is the most important financial indicator characterizing credibility of credit institutions and is estimated as the 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 Supervision recommends maintaining the ratio of capital to risk-weighted assets ("capital adequacy ratio") above the prescribed minimum level. As at 31 December 2017, this minimum level was 8% (2016: 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 at 31 December 2017 (2016: 25%).

The following table shows the composition of the Group's capital position computed in accordance with the Basel Accord (Basel II) as at 31 December 2017 and 31 December 2016.

	<u>2017</u>	<u>2016</u>
Capital		
Tier 1 capital	380,745	378,034
Tier 2 capital	13,988	11,439
Total regulatory capital	<u>394,733</u>	<u>389,473</u>
Risk-weighted assets		
Credit risk	822,189	482,693
Market risk	177,273	186,588
Operational risk	43,411	57,999
Total risk-weighted assets	<u>1,042,873</u>	<u>727,280</u>
Total capital expressed as a percentage of risk-weighted assets, % ("capital adequacy ratio")	37.85%	53.55%
Total tier 1 capital expressed as a percentage of risk-weighted assets, % ("tier-1 capital adequacy ratio")	36.51%	51.98%

(The end)

Report on Review of Interim Financial Information of
International Investment Bank
for the six months ended 30 June 2017

July 2017

Report on Review of Interim Financial Information of International Investment Bank

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Report on Review of Interim Financial Information

To Council of International Investment Bank

Introduction

We have reviewed the accompanying interim condensed consolidated financial statements of International Investment Bank and its subsidiaries, which comprise the interim consolidated statement of financial position as at 30 June 2017, the interim consolidated income statement, interim consolidated statement of comprehensive income, interim consolidated statement of changes in equity and interim consolidated statement of cash flows for the six-month period then ended, and selected explanatory notes (interim financial information). Management of International Investment Bank is responsible for the preparation and presentation of this interim financial information in accordance with IAS 34, *Interim Financial Reporting*. Our responsibility is to express a conclusion on this interim financial information based on our review.

Scope of review

We conducted our review in accordance with International Standard on Review Engagements 2410, *Review of Interim Financial Information Performed by the Independent Auditor of the Entity*. A review of interim financial information consists of making inquiries, primarily of persons responsible for financial and accounting matters, and applying analytical and other review procedures. A review is substantially less in scope than an audit conducted in accordance with International Standards on Auditing and consequently does not enable us to obtain assurance that we would become aware of all significant matters that might be identified in an audit. Accordingly, we do not express an audit opinion.

Conclusion

Based on our review, nothing has come to our attention that causes us to believe that the accompanying interim financial information is not prepared, in all material respects, in accordance with IAS 34, *Interim Financial Reporting*.



O.V. Youshenkov
Partner
Ernst & Young Vneshaudit LLC

20 July 2017

Details of the entity

Name: International Investment Bank

Bank operates on the basis of the Agreement on the Establishment of the International Investment Bank dated 10 July 1970, registered in the UN Secretariat on 1 December 1971 under No. 11417.

Address: Russia 107078, Moscow, Mashi Poryvaevoy str., 7.

Details of the auditor

Name: Ernst & Young Vneshaudit LLC

Record made in the State Register of Legal Entities on 4 February 2016, State Registration Number 1167746123478. Address: Russia 115035, Moscow, Sadovnicheskaya naberezhnaya, 77, building 1.

Ernst & Young Vneshaudit LLC is a member of Self-regulated organization of auditors "Russian Union of auditors" (Association) ("SRO RUA"). Ernst & Young Vneshaudit LLC is included in the control copy of the register of auditors and audit organizations, main registration number 11603050953.

INTERIM CONSOLIDATED STATEMENT OF FINANCIAL POSITION**As at 30 June 2017***(Thousands of euros)*

	<i>Note</i>	<i>30 June 2017 (unaudited)</i>	<i>31 December 2016</i>
Assets			
Cash and cash equivalents	5	106,218	93,031
Deposits with banks and other financial institutions	6	55,341	45,337
Derivative financial assets	7	11,289	14,362
Available-for-sale investment securities	8	135,008	170,849
Available-for-sale investment securities pledged under repurchase agreements	8	98,667	98,458
Loans to banks	9	163,645	94,367
Loans to customers	10	337,166	269,036
Investment property		21,860	21,840
Property, equipment and intangible assets		71,671	71,844
Other assets	11	1,804	2,319
Total assets		1,002,669	881,443
Liabilities			
Due to banks and other financial institutions	12	108,355	118,925
Derivative financial liabilities	7	12,872	11,623
Current customer accounts		9,295	9,218
Long-term loans of banks	13	72,260	73,349
Debt securities issued	14	397,720	272,528
Other liabilities	11	9,403	5,582
Total liabilities		609,905	491,225
Equity			
Subscribed capital	15	1,300,000	1,300,000
Callable capital		(986,947)	(986,947)
Paid-in capital		313,053	313,053
Revaluation reserve for available-for-sale investment securities		(1,235)	(1,506)
Revaluation reserve for property and equipment		12,945	12,945
Foreign currency translation reserve		(69)	(57)
Retained earnings less net income for the period		65,783	64,981
Net income for the period		2,287	802
Total equity		392,764	390,218
Total equity and liabilities		1,002,669	881,443

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

Denis Ivanov



Acting Chairman of the Board

Elena Minduksheva



Acting Head of the Financial Department

20 July 2017

The accompanying notes 1-24 are an integral part of these interim condensed consolidated financial statements.

INTERIM CONSOLIDATED INCOME STATEMENT**For the six months ended 30 June 2017***(Thousands of euros)*

	<i>Note</i>	<i>For the six months ended 30 June (unaudited)</i>	
		<i>2017</i>	<i>2016</i>
Interest income	18	16,147	16,237
Interest expense	18	(14,364)	(13,184)
Net interest income		1,783	3,053
Allowance for loan impairment	9, 10	(3,781)	89
Net interest (expense)/income after allowance for loan impairment		(1,998)	3,142
Fee and commission income		302	525
Fee and commission expense		(71)	(66)
Net fee and commission income		231	459
Net (losses)/gains from revaluation of derivative financial instruments		(4,591)	14,198
Net gains from revaluation of hedging instruments		65	–
Net gains from dealing in foreign currencies and operations with derivatives		12,520	11,026
Net losses from revaluation of assets and liabilities in foreign currencies		(944)	(21,046)
Net gains from available-for-sale investment securities		4,553	3,186
Income from lease of investment property	17	2,049	1,782
Other income		85	627
Net non-interest income		13,737	9,773
Operating income		11,970	13,374
Reversal of allowance for impairment of other assets	11	27	14
General and administrative expenses	19	(9,061)	(8,174)
Other expenses		(649)	(184)
Operating expenses		(9,683)	(8,344)
Net income for the period		2,287	5,030

The accompanying notes 1-24 are an integral part of these interim condensed consolidated financial statements.

INTERIM CONSOLIDATED STATEMENT OF COMPREHENSIVE INCOME**For the six months ended 30 June 2017***(Thousands of euros)*

	<i>Note</i>	<i>For the six months ended 30 June (unaudited)</i>	
		<i>2017</i>	<i>2016</i>
Net income for the period		2,287	5,030
Other comprehensive income			
<i>Other comprehensive income to be reclassified to profit or loss in subsequent periods</i>			
Change in unrealized revaluation of available-for-sale investment securities	15	271	2,215
Translation differences		(12)	36
Net other comprehensive income to be reclassified to profit or loss in subsequent periods		259	2,251
Other comprehensive income		259	2,251
Total income for the period		2,546	7,281

The accompanying notes 1-24 are an integral part of these interim condensed consolidated financial statements.

INTERIM CONSOLIDATED STATEMENT OF CHANGES IN EQUITY**For the six months ended 30 June 2017***(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>Foreign currency translation reserve</i>	<i>Retained earnings</i>	<i>Total equity</i>
At 31 December 2015	1,300,000	(996,947)	(1,664)	31,453	(120)	64,981	397,703
Profit for the period	–	–	–	–	–	5,030	5,030
Other comprehensive income for the period	–	–	2,215	–	36	–	2,251
Total comprehensive income	–	–	2,215	–	36	5,030	7,281
Contributions to capital (Note 15)	–	10,000	–	–	–	–	10,000
At 30 June 2016 (unaudited)	1,300,000	(986,947)	551	31,453	(84)	70,011	414,984
At 31 December 2016	1,300,000	(986,947)	(1,506)	12,945	(57)	65,783	390,218
Profit for the period	–	–	–	–	–	2,287	2,287
Other comprehensive income/(loss) for the period	–	–	271	–	(12)	–	259
Total comprehensive income/(loss)	–	–	271	–	(12)	2,287	2,546
At 30 June 2017 (unaudited)	1,300,000	(986,947)	(1,235)	12,945	(69)	68,070	392,764

The accompanying notes 1-24 are an integral part of these interim condensed consolidated financial statements.

INTERIM CONSOLIDATED STATEMENT OF CASH FLOWS**For the six months ended 30 June 2017***(Thousands of euros)*

	<i>For the six months ended 30 June (unaudited)</i>		
	<i>Note</i>	<i>2017</i>	<i>2016</i>
Cash flows from operating activities			
Interest, fees and commissions received		11,641	11,602
Interest, fees and commissions paid		(2,097)	(1,521)
Realized gains less losses from dealing in foreign currencies and operations with derivatives		13,051	11,053
Cash flows from lease of investment property		2,049	1,782
General and administrative expenses		(7,364)	(4,498)
Other operating (expenses)/income from banking operations		(59)	5
Cash flows from operating activities before changes in operating assets and liabilities		17,221	18,423
<i>Net (increase)/decrease in operating assets</i>			
Due to banks and other financial institutions		(17,053)	29,022
Loans to banks		(69,609)	16,642
Loans to customers		(82,012)	(129,716)
Other assets		620	(501)
<i>Net (decrease)/increase in operating liabilities</i>			
Deposits from banks and other financial institutions		(4,037)	58,519
Current customer accounts		(543)	2,211
Other liabilities		4,397	227
Net cash flows from operating activities		(151,016)	(5,173)
Cash flows from investing activities			
Interest received		2,935	7,714
Purchase of available-for-sale investment securities		(193,404)	(308,150)
Proceeds from sale and redemption of available-for-sale investment securities		227,954	267,412
Proceeds from redemption of held-to-maturity securities		–	3,478
Investments in investment property		(20)	–
Purchase of property, equipment and intangible assets		(836)	(757)
Proceeds from sale of property, equipment and intangible assets		3	–
Net cash flows from investing activities		36,632	(30,303)
Cash flows from financing activities			
Interest paid		(10,533)	(10,978)
Long-term interbank financing raised		13,000	60,000
Long-term interbank financing repaid		(13,451)	(29,569)
Placement of bonds		205,194	–
Redemption and repurchase of bonds		(62,858)	–
Contributions to capital		–	10,000
Net cash flows from financing activities		131,352	29,453
Effect of exchange rate changes on cash and cash equivalents		(3,781)	623
Net decrease in cash and cash equivalents		13,187	(5,400)
Cash and cash equivalents, beginning		93,031	59,519
Cash and cash equivalents, ending	5	106,218	54,119

The accompanying notes 1-24 are an integral part of these interim condensed consolidated financial statements.

(Thousands of euros)

1. Principal activities

These interim condensed consolidated financial statements include the financial statements of the International Investment Bank (the “Bank”, or “IIB”) and its subsidiary. The Bank and its subsidiary are hereinafter collectively referred to as the “Group”. The International Investment Bank is the parent company of the Group. The Bank’s subsidiary is presented in Note 2.

The International Investment 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 Group and for other purposes defined by the Council of the Bank. The Group also performs transactions with securities and foreign currency. The Group operates from its office at 7 Mashki Poryvaevoi St., Moscow, Russia, and the European regional office in Bratislava (Europea Central 1, Pribinova 4, Bratislava, 81109, Slovak Republic).

On 31 July 2014, the EU Council imposed sectoral sanctions against Russia. The preamble of the Decision of the EU Council of 31 July 2014 (paragraph 9) and Council Regulation (EU) No. 833/2014 of 31 July 2014 (paragraph 5), which was developed based on the Decision, emphasize that the sanctions do not cover Russia-based institutions with international status established by intergovernmental agreements in which Russia is one of the parties. Therefore, the International Investment Bank is not subject to the restrictive measures.

The Bank continues to expand its operations despite the ongoing market volatility in member countries:

- ▶ The Bank winds up the introduction of changes to its constituent documents and implementation of the three-level corporate governance structure. The Protocol on Introducing Changes to the Agreement on the Establishment of the International Investment Bank and the Statutes (hereinafter, the “Protocol”) signed at the end of 2015 is at the stage of ratification (internal state procedures) by member countries of the Bank. The Protocol will enter into force upon completion of those ratification procedures. As at 30 June 2017, the Protocol was ratified by Hungary, Vietnam, Romania, Bulgaria, Russia and Cuba (6 countries out of 9).
- ▶ At the 107th meeting of the Bank’s Council (Bucharest, Romania, June 2017), member countries unanimously approved the Bank’s mid-term development strategy for 2018-2022.
- ▶ In May 2017, Moody’s Investors Service upgraded its outlook on the Bank’s credit rating from stable to positive and confirmed its issuer credit rating and debt rating at Baa1. Also, the Bank is assigned the following investment grade ratings: BBB with a stable outlook by Standard & Poor’s; BBB with a stable outlook by Fitch Ratings (upgraded in December 2016); A (stable outlook) by Dagong Global Credit Rating.
- ▶ The Group entered capital markets in Western Europe for the first time in April 2017 with a debut issue of SSD debentures (Schuldscheindarlehen) – a traditional loan instrument of the German market.
- ▶ In 2017, the Bank’s trade financing program was recognized the best among other IFOs’ programs by Association of Development Financing Institutions in Asia and the Pacific (ADFIAP), and the Bank was the winner of ADFIAP Awards 2017 in the Trade Development category.
- ▶ The Bank and chambers of commerce and industry (the “CCIs”) of the member countries signed a multilateral Memorandum on Cooperation at an international business forum timed to coincide with the 107th meeting of the Bank’s Council (Bucharest, Romania). The Memorandum established a framework for creating a “Project Exchange”, i.e. an integration platform under the aegis of the Bank aimed at facilitating development of investment activity both in member countries and in other countries. For this purpose, CCIs of other interested countries can also accede to the Memorandum in accordance with its provisions.

(Thousands of euros)

1. Principal activities (continued)

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>	<i>30 June 2017, % (unaudited)</i>	<i>31 December 2016, %</i>
Russian Federation	47.923	47.923
Republic of Bulgaria	13.481	13.481
Hungary	12.777	12.777
Czech Republic	9.703	9.703
Slovak Republic	6.862	6.862
Romania	5.895	5.895
Republic of Cuba	1.713	1.713
Socialist Republic of Vietnam	1.172	1.172
Mongolia	0.474	0.474
	100.000	100.000

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

In its 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

Economic and political development of the Bank's member countries affects the activities of enterprises operating in these countries. Considering this fact, the Bank performs its operations with reference to the local specifics of its member countries to ensure overall assessment and control of credit and operational risks.

The accompanying interim condensed consolidated 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 Group. Future evolution of the conditions in which the Group operates may differ from the assessment made by the management for the purposes of these interim condensed consolidated financial statements.

2. Basis of preparation

General

These interim condensed consolidated financial statements have been prepared for the six months ended 30 June 2017 in accordance with International Financial Reporting Standard ("IFRS") IAS 34, *Interim Financial Reporting*.

The interim condensed consolidated financial statements do not include all the information and disclosures required in the annual consolidated financial statements, and should be read in conjunction with the Group's annual consolidated financial statements as at 31 December 2016.

Subsidiary

The Bank is a parent company of the Group, which owns CJSC IIB Capital (a 100% subsidiary established in 2012 to deal with issues related to the Group's activities in Russia, in particular, for the property trust of the Group) as at 30 June 2017. The share capital of the subsidiary is RUB 44.5 thousand (EUR 1.1 thousand at the exchange rate effective at the date of incorporation).

(Thousands of euros)

2. Basis of preparation (continued)

Basis of measurement

These interim condensed consolidated 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 in the property and equipment and investment property are stated at revalued amounts.

Functional and presentation currency

Euro (“EUR”) is the Group’s functional and presentation currency as it reflects the economic substance of the underlying operations conducted by the Group and circumstances affecting its operations, because most financial assets and financial liabilities as well as income and expenses of the Group are denominated in EUR.

These interim condensed consolidated financial statements are presented in thousands of euros (“thousands of euros” or “EUR thousand”), unless otherwise indicated.

3. Changes in accounting policies

The accounting policies adopted in the preparation of the interim condensed consolidated financial statements are consistent with those followed in the preparation of the Group’s annual consolidated financial statements for the year ended 31 December 2016, except for the adoption of new standards effective as at 1 January 2017. The Group has not early adopted any other standard, interpretation or amendment that has been issued but is not yet effective.

The nature and effect of these changes are disclosed below. Although these new standards and amendments were applied for the first time in 2017, they do not have a material effect on the interim condensed consolidated financial statements of the Group. The nature and the impact of each new standard or amendment are described below:

Amendments to IAS 7 Statement of Cash Flows: Disclosure Initiative

The amendments require entities to provide disclosures about changes in their liabilities arising from financing activities, including both changes arising from cash flows and non-cash changes (such as foreign exchange gains or losses). On initial application of the amendments, entities are not required to provide comparative information for preceding periods. The Group is not required to provide additional disclosures in its condensed interim consolidated financial statements, but will disclose additional information in its annual consolidated financial statements for the year ended 31 December 2017.

Amendments to IAS 12 Income Taxes: Recognition of Deferred Tax Assets for Unrealized Losses

The amendments clarify that an entity needs to consider whether tax law restricts the sources of taxable profits against which it may make deductions on the reversal of that deductible temporary difference. Furthermore, the amendments provide guidance on how an entity should determine future taxable profits and explain the circumstances in which taxable profit may include the recovery of some assets for more than their carrying amount.

Entities are required to apply the amendments retrospectively. However, on initial application of the amendments, the change in the opening equity of the earliest comparative period may be recognized in opening retained earnings (or in another component of equity, as appropriate), without allocating the change between opening retained earnings and other components of equity. Entities applying this relief must disclose that fact.

The Bank is not subject to taxation, therefore application of these amendments has no effect on the Group’s financial position and performance.

*(Thousands of euros)***3. Changes in accounting policies (continued)*****Annual improvements cycle – 2014-2016******Amendments to IFRS 12 Disclosure of Interests in Other Entities: Clarification of the scope of disclosure requirements in IFRS 12***

The amendments clarify that the disclosure requirements in IFRS 12, other than those in paragraphs B10–B16, apply to an entity's interest in a subsidiary, a joint venture or an associate (or a portion of its interest in a joint venture or an associate) that is classified (or included in a disposal group that is classified) as held for sale. The amendment has no effect on the Group's interim condensed consolidated financial statements.

4. Significant accounting judgments and estimates**Assumptions and estimation uncertainty**

In the process of applying the Group'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 interim condensed consolidated financial statements, which have the effect on the amounts recognized in the interim condensed consolidated 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.

Assumptions and estimates adopted by management of the Group in the process of applying the accounting policies are consistent with those described in the consolidated financial statements for the year ended 31 December 2016.

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

- ▶ Note 7 – Derivative financial instruments.
- ▶ Note 8 – Available-for-sale investment securities.
- ▶ Note 9 – Loans to banks.
- ▶ Note 10 – Loans to customers.
- ▶ Note 16 – Contingencies and loan commitments.

5. Cash and cash equivalents

Cash and cash equivalents comprise:

	<i>30 June 2017</i> <i>(unaudited)</i>	<i>31 December</i> <i>2016</i>
Cash on hand	236	104
Nostro accounts with banks and other financial institutions:		
<i>Credit rating from A- to A+</i>	65,761	62,548
<i>Credit rating from BBB- to BBB+</i>	7,130	4,526
<i>Credit rating from BB- to BB+</i>	446	551
Total Nostro accounts with banks and other financial institutions	73,337	67,625
Short-term deposits with banks:		
Term deposits with banks		
<i>Credit rating from BBB- to BBB+</i>	10,332	–
<i>Credit rating from BB- to BB+</i>	–	25,302
<i>Credit rating from B- to B+</i>	22,313	–
Total short-term deposits with banks	32,645	25,302
Cash and cash equivalents	106,218	93,031

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

*(Thousands of euros)***6. Deposits with banks and other financial institutions**

Deposits with banks and other financial institutions are presented based on contractual terms and include the following items:

	<i>30 June 2017</i> <i>(unaudited)</i>	<i>31 December</i> <i>2016</i>
Term deposits up to 1 year:		
<i>Credit rating from B- to B+</i>	47,589	37,126
Total term deposits up to 1 year	47,589	37,126
Term deposits over 1 year:		
<i>Credit rating from A- to A+</i>	3,072	5,821
<i>Credit rating from BB- to BB+</i>	4,680	2,390
Total term deposits over 1 year	7,752	8,211
Total deposits with banks and other financial institutions	55,341	45,337

Amounts due from the Central Bank of the Republic of Cuba

	<i>30 June 2017</i> <i>(unaudited)</i>	<i>31 December</i> <i>2016</i>
Term deposits with the Central Bank of the Republic of Cuba without credit rating	34,967	34,967
Less: allowance for impairment	(34,967)	(34,967)
Term deposits with the Central Bank of the Republic of Cuba	–	–

Concentration of deposits with banks and other financial institutions

As at 30 June 2017, the Group had three counterparties (31 December 2016: three) accounting for over 10% of the Group's total deposits with banks and other financial institutions, except for deposits with the Central Bank of the Republic of Cuba.

7. Derivative financial instruments

The Group performs the operations with currency and other derivative financial instruments which are generally traded in an over-the-counter market with professional market counterparties on standardized contractual terms and conditions. Derivative financial instruments have either potentially favorable terms (and are assets) or potentially unfavorable conditions (and are liabilities) as a result of fluctuations in the exchange rates or other variable factors associated with these instruments. The fair value of derivative financial instruments may vary significantly depending on the potentially favorable or unfavorable conditions.

*(Thousands of euros)***7. Derivative financial instruments (continued)**

The table below shows the fair value of derivative financial instruments as at 30 June 2017 and 31 December 2016 and notional amounts of term contracts for the purchase and sale of foreign currency specifying weighted average contractual exchange rates.

	30 June 2017 (unaudited)				
	Notional amount		Weighted average exchange rate	Fair value	
	Purchase	Sale		Assets	Liabilities
Derivative financial assets and liabilities at fair value through profit or loss					
Swaps	EUR 170,500 thousand	USD 189,376 thousand	1.11	5,322	–
	EUR 16,500 thousand	RUB 1,051,741 thousand	63.74	1,222	–
	EUR 23,278 thousand	HUF 7,160,000 thousand	307.59	111	–
	EUR 16,514 thousand	RON 75,000 thousand	0.22	13	–
	RUB 15,417,998 thousand	EUR 236,382 thousand	65.36	2,616	9,442
	RON 110,300 thousand	EUR 24,971 thousand	4.42	–	596
	RUB 3,000,000 thousand	USD 52,910 thousand	56.70	–	1,567
Forwards					
- foreign currency	EUR 34,000 thousand	USD 36,641 thousand	1.08	2,002	–
- equity securities	16,780	EUR 250 thousand	14.91	3	–
Total derivative financial assets and liabilities at fair value through profit or loss				11,289	11,605
Derivative financial assets and liabilities designated as hedging instruments					
Swaps	RON 298,300 thousand	EUR 67,068 thousand	4.45	–	1,267
Total derivative financial assets and liabilities designated as hedging instruments				–	1,267
Derivative financial instruments				11,289	12,872

(Thousands of euros)

7. Derivative financial instruments (continued)

	31 December 2016				
	Notional amount		Weighted average exchange rate	Fair value	
	Purchase	Sale		Assets	Liabilities
Derivative financial assets and liabilities at fair value through profit or loss					
Swaps	RUB 9,136,720 thousand	EUR 132,150 thousand	69.42	14,246	883
	RON 110,300 thousand	EUR 24,971 thousand	4.44	–	632
	EUR 117,000 thousand	USD 128,825 thousand	1.10	116	5,704
	EUR 8,000 thousand	RUB 572,280 thousand	71.54	–	788
Forwards					
- foreign currency	EUR 34,000 thousand	USD 37,896 thousand	1.11	–	2,080
Total derivative financial assets and liabilities at fair value through profit or loss				14,362	10,087
Derivative financial assets and liabilities designated as hedging instruments					
Swaps	RON 298,300 thousand	EUR 67,068 thousand	4.45	–	1,536
Total derivative financial assets and liabilities designated as hedging instruments				–	1,536
Derivative financial instruments				14,362	11,623

Due to issuing debt securities denominated in currencies other than the functional currency of the Group (Note 14), the Group concluded cross currency interest rate swaps and currency forwards on an arm's length basis with large international and Russian credit institutions. These swaps are used to manage long-term currency risks of the Group. Payment netting is not applied to the parties' obligations in respect of interest and principal payments.

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 end of the reporting period and are not indicative of the credit risk.

As at 30 June 2017 and 31 December 2016, the Group has positions in the following types of derivatives:

Forwards: Forward contracts are contractual agreements to buy or sell a specified financial instrument at a specific price and date in the future. Forwards are customized contracts transacted in the over-the-counter market.

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.

Fair value measurement is based on the corresponding forward curves that depend on exchange rates, interest rates and swap contract maturity. For the fair value of swaps, the discount rate was calculated on the basis of zero coupon yield curve and credit risk. Changes in the fair value of swaps were mainly due to the increase in the forward exchange rate of EUR against the currencies of transactions.

(Thousands of euros)

8. Available-for-sale investment securities

Available-for-sale investment securities comprise:

	<i>30 June 2017</i> <i>(unaudited)</i>	<i>31 December</i> <i>2016</i>
Owned by the Group		
Quoted debt securities		
Government bonds:		
<i>Eurobonds issued by governments of member countries</i>	13,369	52,678
<i>Eurobonds issued by governments of other countries</i>	17,824	–
Government bonds	31,193	52,678
Corporate bonds		
<i>Credit rating AAA</i>	5,029	–
<i>Credit rating from AA- to AA+</i>	3,525	–
<i>Credit rating from A- to A+</i>	20,263	21,152
<i>Credit rating from BBB- to BBB+</i>	19,351	21,861
<i>Credit rating BB+</i>	51,632	57,579
<i>Credit rating B+</i>	1,024	17,575
Corporate bonds	100,824	118,167
Total quoted debt securities	132,017	170,845
Quoted equity instruments		
<i>Credit rating AA-</i>	248	–
<i>Credit rating A</i>	244	–
<i>Credit rating BBB-</i>	2,288	–
<i>Credit rating BB+</i>	207	–
<i>No credit rating</i>	4	4
Total quoted equity instruments	2,991	4
Available-for-sale investment securities	135,008	170,849
Pledged under repurchase agreements		
Quoted debt securities		
<i>Eurobonds issued by governments of member countries</i>	47,849	10,286
<i>Eurobonds issued by governments of other countries</i>	7,625	7,597
Government bonds	55,474	17,883
Corporate bonds		
<i>Credit rating AAA</i>	21,031	22,486
<i>Credit rating from AA- to AA+</i>	4,338	4,688
<i>Credit rating from A- to A+</i>	13,572	32,521
<i>Credit rating from BBB- to BBB+</i>	–	4,994
<i>Credit rating BB+</i>	4,252	15,886
Corporate bonds	43,193	80,575
Total quoted available-for-sale debt securities pledged under repurchase agreements	98,667	98,458

Government bonds represent EUR-denominated, USD-denominated and RUB-denominated securities issued and guaranteed by the Ministries of Finance of these countries, maturing in 2022-2027 (31 December 2016: maturing in 2018-2027). The annual coupon rate for these bonds varies from 0.4% to 8.8% (31 December 2016: from 0.4% to 7.9%).

Corporate bonds are represented by the bonds issued by large companies and banks of member countries of the Bank, as well as corporate international companies and Development Banks that have similar goals and missions with the Group, maturing in 2018-2031 (31 December 2016: maturing in 2018-2031). The annual coupon rate for these bonds varies from 2.1% to 10.3% (31 December 2016: from 0.6% to 10.35%).

Equity securities are represented by shares and depositary receipts issued by large international and Russian companies.

*(Thousands of euros)***9. Loans to banks**

During 2017, the Group continued its lending activities, being guided by the key priorities of the Development Strategy of the IIB Group. 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 Group considers national development institutes, export and import banks and agencies, international financial organizations and Development Banks as its key counterparties.

During the six-months ended 30 June 2017 and the year ended 31 December 2016, the Group provided trade financing loans and long-term loans to banks operating in the following countries:

	<i>30 June 2017 (unaudited)</i>	<i>31 December 2016</i>
Trade financing loans		
Russian Federation	29,256	953
Republic of Belarus	2,555	–
Trade financing loans	31,811	953
Long-term loans to banks		
Russian Federation	64,135	26,425
Mongolia	42,249	47,970
Socialist Republic of Vietnam	26,224	19,019
Long-term loans to banks	132,608	93,414
Total loans to banks	164,419	94,367
Less: allowance for loan impairment	(774)	–
Loans to banks	163,645	94,367

A summary of overdue loans as at 30 June 2017 and 31 December 2016 is presented below:

	<i>30 June 2017 (unaudited)</i>	<i>31 December 2016</i>
Loans with overdue principal and/or interest	15,478	–
Less: allowance for loan impairment	(774)	–
Overdue loans to banks	14,704	–

For the purposes of these interim condensed consolidated financial statements, a loan to banks is considered overdue if at least one of the loan-related payments is past due at the reporting date. In this case, the amount of the overdue loan is the total amount due from the borrower, including the principal amount and accrued interest income.

Allowance for impairment of loans to banks

A reconciliation of the allowance for impairment of loans to banks by country is as follows:

	<i>Russian Federation</i>	<i>Total</i>
At 1 January 2017	–	–
Net charge for the period	774	774
At 30 June 2017 (unaudited)	774	774
Individual impairment	774	774
Gross amount of loans to banks, individually determined to be impaired, before deducting any individually assessed impairment allowance	–	–

As at 31 December 2016, there were no impaired loans and allowance for impairment was not accrued.

*(Thousands of euros)***9. Loans to banks (continued)****Analysis of collateral for loans to banks**

The following table provides an analysis of the portfolio of trade financing loans and long-term loans to banks by type of collateral as at 30 June 2017 and 31 December 2016:

	<i>30 June 2017</i> <i>(unaudited)</i>		<i>31 December</i> <i>2016</i>	
	<i>Loans to banks</i>	<i>Share in the total loans, %</i>	<i>Loans to banks</i>	<i>Share in the total loans, %</i>
Pledge of the rights of claim	13,349	8.2	–	–
Pledge of real property (mortgage) and title	1,896	1.2	7,247	7.7
Uncollateralized part of the loans	148,400	90.6	87,120	92.3
Total loans to banks	163,645	100.0	94,367	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 loans to banks

As at 30 June 2017, long-term loans and trade financing loans to four banks (31 December 2016: five banks) with the total amount of loans to each of them exceeding 10% of total loans to banks were recorded on the Group's balance sheet. As at 30 June 2017, the total amount of such major loans was EUR 99,808 thousand (31 December 2016: EUR 74,787 thousand), and allowances for impairment of these loans were not made (31 December 2016: allowances were not made).

10. Loans to customers

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

	<i>30 June 2017</i> <i>(unaudited)</i>	<i>31 December</i> <i>2016</i>
Russian Federation	69,702	61,213
Republic of Bulgaria	59,774	65,922
Romania	56,602	40,235
Republic of Ecuador	36,273	39,570
Czech Republic	35,038	22,930
Republic of Panama	32,183	36,276
Hungary	22,865	–
Slovak Republic	20,016	8,411
USA	5,526	6,108
Mongolia	4,737	5,683
Gross loans to customers	342,716	286,348
Less: allowance for loan impairment	(5,550)	(17,312)
Loans to customers	337,166	269,036

A summary of overdue loans as at 30 June 2017 and 31 December 2016 is presented below:

	<i>30 June 2017</i> <i>(unaudited)</i>	<i>31 December</i> <i>2016</i>
Loans with overdue principal and/or interest	15,151	14,769
Less: allowance for loan impairment	(5,255)	(14,769)
Overdue loans to customers	9,896	–

(Thousands of euros)

10. Loans to customers (continued)

For the purposes of these interim condensed consolidated financial statements, a loan to customers is considered overdue if at least one of the loan-related payments is past due at the reporting date. In this case, the amount of the overdue loan is the total amount due from the borrower, including the principal amount and accrued interest income.

Allowance for impairment of loans to customers

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

	<i>Slovak Republic</i>	<i>Republic of Bulgaria</i>	<i>Romania</i>	<i>Total</i>
At 1 January 2017	8,103	6,955	2,254	17,312
Net charge for the period	–	6	3,001	3,007
Write off against previously accrued allowance	(8,103)	(6,666)	–	(14,769)
At 30 June 2017 (unaudited)	–	295	5,255	5,550
Individual impairment	–	–	5,255	5,255
Gross amount of loans to customers, individually determined to be impaired, before deducting any individually assessed impairment allowance	–	–	15,151	15,151
	<i>Slovak Republic</i>	<i>Republic of Bulgaria</i>	<i>Romania</i>	<i>Total</i>
At 1 January 2016	3,000	6,755	–	9,755
Net charge for the period	5,103	200	2,254	7,557
At 31 December 2016	8,103	6,955	2,254	17,312
Individual impairment	8,103	6,666	–	14,769
Gross amount of loans to customers, individually determined to be impaired, before deducting any individually assessed impairment allowance	8,103	6,666	–	14,769

The following table provides an analysis of the customer loan portfolio, net of allowance for impairment, by types of collateral as at 30 June 2017 and 31 December 2016:

	<i>30 June 2017 (unaudited)</i>		<i>31 December 2016</i>	
	<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	71,732	21.3	25,811	9.6
State guarantees	67,142	19.9	75,845	28.2
Corporate guarantees	43,038	12.7	22,930	8.5
Pledge of equipment and goods in turnover	35,916	10.7	22,641	8.4
Pledge of shares	14,942	4.4	21,579	8.0
Pledge of the rights of claim	9,023	2.7	22,970	8.5
Pledge of vehicles	1,970	0.6	2,756	1.0
Uncollateralized part of the loans	93,403	27.7	74,504	27.8
Total loans to customers	337,166	100.0	269,036	100.0

*(Thousands of euros)***10. Loans to customers (continued)****Analysis of collateral for loans to customers**

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.

Concentration of loans to customers

As at 30 June 2017, loans to three borrowers (31 December 2016: three) with the total amount of loans to each of the three borrowers exceeding 10% of total loans to customers were recorded on the Group's balance sheet. As at 30 June 2017, these loans totaled EUR 111,004 thousand (31 December 2016: EUR 107,191 thousand) and allowances were not created (31 December 2016: no allowances).

Analysis of loans to customers by industry

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

	30 June 2017 (unaudited)	31 December 2016
Leasing	76,259	85,897
Metal working industry	74,733	22,930
Production and transmission of electricity	55,976	39,570
Food and beverages	26,580	27,504
Communications	22,865	–
Manufacturing of electrical equipment	21,058	20,809
Consulting services	16,221	–
Agriculture	14,308	14,295
Transport	12,499	13,752
Crude oil refining	9,998	10,002
Production of pharmaceutical products	8,044	6,645
Trade	3,862	6,036
Other	313	308
Chemical production	–	23,831
Construction	–	14,769
	342,716	286,348
Less: allowance for loan impairment	(5,550)	(17,312)
Loans to customers	337,166	269,036

11. Other assets and liabilities

Other assets comprise:

	30 June 2017 (unaudited)	31 December 2016
Financial assets		
Settlements on bank transactions	1,686	1,814
Accounts receivable on business operations	93	1,352
Guarantee payments	26	42
Other financial assets	120	136
	1,925	3,344
Less: allowance for impairment	(1,766)	(1,924)
Total financial assets less allowance for impairment	159	1,420
Non-financial assets		
Advances issued	791	–
Assets held for sale – property	89	89
Inventories – real estate	51	55
Other non-financial assets	714	755
	1,645	899
Total non-financial assets	1,645	899
Total other assets	1,804	2,319

*(Thousands of euros)***11. Other assets and liabilities (continued)**

The movements in allowance for impairment of other financial assets are as follows:

	<i>30 June 2017</i> <i>(unaudited)</i>	<i>31 December</i> <i>2016</i>
Allowance at 1 January	1,924	1,633
Reversal for the period	(27)	(67)
Change in allowance resulting from changes in exchange rates	(131)	358
Allowance at the end of the period	1,766	1,924

Other liabilities comprise:

	<i>30 June 2017</i> <i>(unaudited)</i>	<i>31 December</i> <i>2016</i>
Financial liabilities		
Other accounts payable on bank transactions	3,140	662
Other accounts payable on business operations	679	1,182
Other financial liabilities	11	19
Total financial liabilities	3,830	1,863
Non-financial liabilities		
Settlements with employees	4,395	3,647
Other non-financial liabilities	1,178	72
Total non-financial liabilities	5,573	3,719
Total other liabilities	9,403	5,582

As at 30 June 2017, other accounts payable on bank transactions include EUR 3,000 thousand received by the Bank from one of its borrowers counting as loan repayment before its corresponding due date.

12. Deposits from banks and other financial institutions

Deposits from banks and other financial institutions are presented based on contractual terms and include the following items:

	<i>30 June 2017</i> <i>(unaudited)</i>	<i>31 December</i> <i>2016</i>
Deposits from banks up to 1 year		
Term deposits from banks and other financial institutions	45,060	52,856
Total deposits from banks up to 1 year	45,060	52,856
Deposits from banks over 1 year		
Repurchase agreements	63,295	66,069
Total deposits from banks over 1 year	63,295	66,069
Total deposits from banks	108,355	118,925

The Group performs daily monitoring of the repurchase agreements and the value of collateral when placing/returning additional collateral, if necessary.

Concentration of deposits from banks and other financial institutions

As at 30 June 2017, the Group has two counterparties (31 December 2016: two counterparties) accounting for over 10% of the Bank's total deposits from banks and other financial institutions in the amount of EUR 97,428 thousand (31 December 2016: EUR 111,418 thousand).

*(Thousands of euros)***13. Long-term loans from banks**

Long-term loans from banks comprise:

	<i>30 June 2017</i> <i>(unaudited)</i>	<i>31 December</i> <i>2016</i>
Syndicated loans	59,394	59,039
SSD debentures	12,866	–
Loans from banks	–	14,310
Total long-term loans from banks	72,260	73,349

On 6 April 2017 the Group made a debut issue of SSD debentures (Schuldscheindarlehen) on the capital market in Western Europe in the total amount of EUR 13,000 thousand.

14. Debt securities issued

Debt securities issued comprise:

	<i>Interest rate,</i> <i>% p.a.</i>	<i>Maturity</i>	<i>30 June 2017</i> <i>(unaudited)</i>	<i>31 December</i> <i>2016</i>
RUB-denominated bonds	0.01-11.9	2024-2027	274,458	151,516
RON-denominated bonds	3.4-4.1	2018-2019	92,602	90,885
EUR-denominated bonds	3.5	2019	30,660	30,127
Total debt securities issued			397,720	272,528

On 27 April 2017, the Group made a secondary placement of RUB-denominated bonds, series 02, in the amount of RUB 2,998.0 million (EUR 48,615 thousand) that had been repurchased under the offer. A new coupon rate of 9.5% p.a. was set. This issue provides for an offer in April 2019.

The Group redeemed RUB-denominated bonds, series 03, worth a total of RUB 3.99 billion (EUR 62,858 thousand) on 2 June 2017, as scheduled under the offer.

On 14 June 2017, the Group placed an issue of exchange-traded bonds at the Moscow Exchange under the Program to Issue Exchange-traded Bonds registered in 2016. The issue totaled RUB 10 billion (EUR 156,579 thousand); this issue provides for an offer in March 2020. The coupon rate on the bonds was set at 8.75% payable on a quarterly basis with the first coupon payment to be made on 11 September 2017.

On 27 September 2016, the Group issued RON-denominated bonds in the amount of RON 300.0 million (EUR 67,398 thousand) maturing in three years. The coupon rate on the bonds was set at 3.4% payable annually with the first coupon payment to be made on 27 September 2017.

On 31 October 2016, the Group offered to repurchase RUB-denominated bonds, series 02, and repurchased almost the total amount of those bonds (RUB 2,998.0 million, or EUR 43,327 thousand) from investors. A new coupon rate of 0.1% p.a. was set.

At the date of placement, the Group entered into cross-currency interest rate swaps for the purpose of managing currency risks (Note 7).

Among other things, the Group used the proceeds from issuance of debt instruments and placement of bonds to expand its loan portfolio.

*(Thousands of euros)***15. 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 30 June 2017, unpaid portion of the Bank's subscribed capital in the amount of EUR 986,947 thousand (31 December 2016: EUR 986,947 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 175,500 thousand (31 December 2016: EUR 175,500 thousand).

On 9 March 2016, in accordance with the Memorandum of Understanding signed at the 102nd meeting of the IIB's Council (20-21 November 2014), the Government of Hungary contributed EUR 10,000 thousand to the Bank's equity.

The paid-in capital of the International Investment Bank totals EUR 313,053 thousand (31 December 2016: EUR 313,053 thousand).

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

The movements in the revaluation reserve for available-for-sale 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 2016	(1,664)	31,453
Net unrealized gains on available-for-sale investment securities	5,401	–
Realized gains on available-for-sale investment securities reclassified to the income statement	(3,186)	–
At 30 June 2016 (unaudited)	551	31,453
At 1 January 2017	(1,506)	12,945
Net unrealized gains on available-for-sale investment securities	4,824	–
Realized gains on available-for-sale investment securities reclassified to the income statement	(4,553)	–
At 30 June 2017 (unaudited)	(1,235)	12,945

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.

16. Contingencies and loan commitments**Legal**

In the ordinary course of business, the Group 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 Group. 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.

*(Thousands of euros)***16. Contingencies and loan commitments (continued)****Legal (continued)**

The Group 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 Group's further actions to collect bad debt and/or realize respective repossession rights is higher than the amount collected and also when the Group 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 Group obtained insurance coverage for buildings, equipment and car park as well as liability insurance against damages caused by operating assets of a hazardous nature. However, the Group did not obtain insurance coverage related to temporarily discontinued operations or the Group's obligations to third parties.

Commitments and contingencies

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

As at 30 June 2017 and 31 December 2016, commitments and contingencies of the Group comprised off-balance credit-related commitments, in particular undrawn loan facilities and reimbursement obligations.

The primary purpose of credit-related commitments is to ensure that funds are available to customers as required. Guarantees issued, which represent irrevocable assurances that the Group will make payments in the event that a customer cannot meet its obligations to third parties, carry the same credit risk as loans. Reimbursement obligations, which are irrevocable reimbursement obligations of the Bank issued on behalf of banks issuing documentary letters of credit that are accepted and paid by partner foreign banks up to a stipulated amount under specific terms and conditions, are collateralized by the underlying shipments of goods to which they relate and therefore carry less risk than a direct borrowing. Undrawn loan facilities represent unused portions of funds to be issued as loans.

Off-balance credit-related commitments are presented in the table below as at 30 June 2017 and 31 December 2016.

	<i>30 June 2017</i> <i>(unaudited)</i>	<i>31 December</i> <i>2016</i>
Undrawn loan facilities	217,597	33,103
Reimbursement obligations	25,142	9,898
Guarantees issued	16,454	4,934
Total off-balance commitments	259,193	47,935

The total outstanding contractual amount of undrawn loan facilities, reimbursement obligations and guarantees issued does not necessarily represent future cash claims, as these commitments may expire or terminate without being funded.

17. Leases**Group as lessor**

The Group provides its investment property for operating leases. As at 30 June 2017, the Group's non-cancellable operating lease rentals amount to EUR 3,152 thousand (31 December 2016: EUR 4,752 thousand) and will be settled within 1 to 4 years (31 December 2016: 1 to 5 years).

*(Thousands of euros)***18. Interest income and interest expense**

Net interest income comprises:

	<i>30 June 2017</i> <i>(unaudited)</i>	<i>30 June 2016</i> <i>(unaudited)</i>
Loans to customers	8,313	6,279
Available-for-sale investment securities	3,120	1,705
Long-term loans to banks	2,906	3,398
Deposits with banks and other financial institutions, including cash and cash equivalents	1,637	2,092
Trade financing loans to banks	171	–
Held-to-maturity investment securities	–	2,763
Interest income	16,147	16,237
Debt securities issued	(11,932)	(10,833)
Long-term loans from banks	(1,235)	(632)
Funds raised under repurchase agreements	(971)	(904)
Current customer accounts	(120)	(179)
Correspondent accounts and deposits from banks and other financial institutions	(103)	(597)
Other	(3)	(39)
Interest expense	(14,364)	(13,184)
Net interest income	1,783	3,053

Interest income accrued on impaired loans issued for the six months of 2017 amounted to EUR 122 thousand (for the six months of 2016: EUR 0).

19. General and administrative expenses

General and administrative expenses comprise:

	<i>30 June 2017</i> <i>(unaudited)</i>	<i>30 June 2016</i> <i>(unaudited)</i>
Employee compensations and employment taxes	6,544	5,864
Depreciation of property and equipment and amortization of intangible assets	1,005	870
IT-expenses, inventory and occupancy expenses	845	731
Expenses related to business travel, representative and accommodation expenses	292	279
Professional fees	124	194
Other	251	236
General and administrative expenses	9,061	8,174

20. Risk management**Risk management framework**

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

(Thousands of euros)

20. Risk management (continued)

Risk management framework (continued)

The Group's risk management activities are intended to:

- ▶ Identify, analyze and manage risks faced by the Group.
- ▶ 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.

Risk management system

Integrated into the whole vertical organizational structure of the Group and all areas of the Group's activities, the risk management system makes it possible to identify in a timely manner and effectively manage different types of risks.

Risk management involves all of the Group's divisions in the evaluating, assuming, and controlling risks ("Three lines of defense"):

- ▶ Risk-taking (1st line of defense): the Group's divisions directly preparing and conducting transactions, involved in the identification, assessment, and monitoring of risks and comply with internal regulations on risk management, as well as give due consideration to the risk level in the preparation of transactions.
- ▶ Risk management (2nd line of defense): the division responsible for risk management develops risk management tools and methodology, assesses and monitors.
- ▶ The risk level, prepares reports on risks, carries out risk aggregation, and calculates the amount of total capital requirements.
- ▶ Internal audit (3rd line of defense): independent quality assessment for existing risk management processes, identification of violations, and proposals for the improvement of the risk management system.

The Group's operations are managed taking into account the level of the risk appetite approved by the Council and integrated into a system of limits and restrictions insuring the acceptable level of risk for aggregated positions, transparent distribution of total risk limit among the activities of the Group.

The Group 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 Group will incur a loss because its counterparty fails to discharge its contractual financial obligations to the Group, 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 Group considers and consolidates all elements of credit risk exposures such as consolidated borrower or counterparty default risk.

The credit quality assessment 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.

*(Thousands of euros)***20. Risk management (continued)****Credit risk (continued)**

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 customer'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.

The following table provides information on the credit quality of long-term loans to banks and trade financing loans (Note 9) and loans to customers (Note 10) as at 30 June 2017 and 31 December 2016:

<i>30 June 2017 (unaudited)</i>	<i>Loan amount</i>	<i>Allowance for impairment</i>	<i>Loan amount, including impairment</i>	<i>Impairment to loan amount ratio, %</i>
Trade financing loans to banks without any signs of impairment identified				
Standard loans				
- <i>Russian Federation</i>	29,256	–	29,256	–
- <i>Republic of Belarus</i>	2,555	–	2,555	–
Long-term loans to banks without any signs of impairment identified				
Standard loans				
- <i>Russian Federation</i>	48,657	–	48,657	–
- <i>Mongolia</i>	42,249	–	42,249	–
- <i>Socialist Republic of Vietnam</i>	26,224	–	26,224	–
Watch list loans				
- <i>Russian Federation</i>	15,478	(774)	14,704	5.0
	164,419	(774)	163,645	0.5
Loans to customers without any signs of impairment identified				
Standard loans				
- <i>Russian Federation</i>	69,702	–	69,702	–
- <i>Republic of Bulgaria</i>	53,867	–	53,867	–
- <i>Romania</i>	41,451	–	41,451	–
- <i>Republic of Ecuador</i>	36,273	–	36,273	–
- <i>Czech Republic</i>	35,038	–	35,038	–
- <i>Republic of Panama</i>	32,183	–	32,183	–
- <i>Hungary</i>	22,865	–	22,865	–
- <i>Slovak Republic</i>	20,016	–	20,016	–
- <i>USA</i>	5,526	–	5,526	–
- <i>Mongolia</i>	4,737	–	4,737	–
Renegotiated loans				
- <i>Republic of Bulgaria</i>	5,907	(295)	5,612	5.0
Impaired loans				
- <i>Romania</i>	15,151	(5,255)	9,896	34.7
	342,716	(5,550)	337,166	1.6
Total loans	507,135	(6,324)	500,811	1.2

(Thousands of euros)

20. Risk management (continued)

Credit risk (continued)

<i>31 December 2016</i>	<i>Loan amount</i>	<i>Allowance for impairment</i>	<i>Loan amount, including impairment</i>	<i>Impairment to loan amount ratio, %</i>
Trade financing loans to banks without any signs of impairment identified				
Standard loans				
- Russian Federation	953	–	953	–
Long-term loans to banks without any signs of impairment identified				
Standard loans				
- Mongolia	47,970	–	47,970	–
- Russian Federation	26,425	–	26,425	–
- Socialist Republic of Vietnam	19,019	–	19,019	–
	94,367	–	94,367	–
Loans to customers without any signs of impairment identified				
Standard loans				
- Russian Federation	61,213	–	61,213	–
- Republic of Bulgaria	53,477	–	53,477	–
- Republic of Ecuador	39,570	–	39,570	–
- Republic of Panama	36,276	–	36,276	–
- Romania	25,205	–	25,205	–
- Czech Republic	22,930	–	22,930	–
- USA	6,108	–	6,108	–
- Mongolia	5,683	–	5,683	–
- Slovak Republic	308	–	308	–
Watch list loans				
- Romania	15,030	(2,254)	12,776	15.0
Renegotiated loans				
- Republic of Bulgaria	5,779	(289)	5,490	5.0
Impaired loans				
- Slovak Republic	8,103	(8,103)	–	100
- Republic of Bulgaria	6,666	(6,666)	–	100
	286,348	(17,312)	269,036	6.0
Total loans	380,715	(17,312)	363,403	4.5

Where possible, the Group 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.

Liquidity risk

Liquidity risk is the risk of loss resulting from the Group'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 Group'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 Group) and/or an unforeseen need of immediate and simultaneous discharge of its financial obligations.

Liquidity management is an integral part of general policy for the Group's assets and liabilities management (ALM) and operates within the established limits and restrictions related to management of risks (liquidity, interest rate and currency risk) and the Group's balance sheet items, and in accordance with the documents of strategic, tactical and operating planning.

Procedures for the Group's liquidity position management, ensuring the Group's ability to meet its obligations in full and on a timely basis and efficient resources management, are stipulated in the Regulations for the IIB's Liquidity Position Management that enables the development of the liquidity position management function provided for by the IIB's Assets and Liabilities Management Policy, as an integral part of general function of the Group's management.

*(Thousands of euros)***20. Risk management (continued)****Liquidity risk (continued)**

Decision making matrix related to liquidity management includes a strategic level of liquidity management (the Council), tactical level (the Board and special-purpose committees) and operational level (responsible structural divisions). Asset and Liability Management Department (DUAP or ALM Unit) became responsible for organizing and aligning management of the Group's liquidity position. The Group manages its liquidity position in accordance with planning horizons (up to 6 months) and possible scenarios of movements in liquidity position (stable, stressed).

Main instrument of liquidity position management under the stable scenario is a Plan of Cash Flows defining the cash flow by balance sheet products/instruments and taking into account the plan of future financial operations. The Group determines the balance sheet gaps, payment schedule and need in financing of future operations based on the Plan of Cash Flows. As a result of application of these instruments, DUAP issues appropriate recommendations to responsible structural divisions.

The Group has implemented a liquidity buffer to manage the Group's liquidity under the stressed scenario. Application of the liquidity buffer enables the Group to promptly monitor the sustainability and stability of the Group's balance sheet structure in case of liquidity shortage that is critical to the Group's solvency.

The liquidity buffer is formed primarily by liquidity reverses, namely securities recognized on the Group's balance sheet and included in the Lombard lists of the European Central Bank and Bank of Russia, and nostro accounts with banks and other financial institutions. The Group calculates its liquidity reserves as at the reporting date and for the next six monthly reporting dates (forecast). Liquidity buffer may be used to close the negative net position. As at 30 June 2017, the liquidity buffer amounts to EUR 93.7 million (31 December 2016: EUR 75.9 million).

The table below shows the contractual expiry by maturity of the Group'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.

	<i>30 June 2017</i> <i>(unaudited)</i>	<i>31 December</i> <i>2016</i>
Less than 1 month	113,882	33,213
1 to 3 months	10,681	3,650
3 months to 1 year	89,712	6,138
1 to 5 years	44,918	4,934
Off-balance credit-related commitments	259,193	47,935

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(Thousands of euros)

20. Risk management (continued)

Liquidity risk (continued)

The following table provides an analysis of financial assets and liabilities on the basis of the remaining period from the reporting date to the contractual maturity date. Quoted available-for-sale debt securities were included in “Less than 1 month” category as they are highly liquid investment securities, which the Group may sell in the short-term on the arm-length basis. Available-for-sale investment securities pledged under repurchase agreements are presented on the basis of periods from the reporting date to the expiry date of respective contractual obligations of the Group.

	30 June 2017 (unaudited)							31 December 2016								
	Less than 1 month	1 to 3 months	3 months to 1 year	1 to 5 years	Over 5 years	No stated maturity	Past due	Total	Less than 1 month	1 to 3 months	3 months to 1 year	1 to 5 years	Over 5 years	Past due	Total	
Assets																
Cash and cash equivalents	83,831	22,387	–	–	–	–	–	106,218	93,031	–	–	–	–	–	–	93,031
Deposits with banks and other financial institutions	29,499	–	19,742	6,100	–	–	–	55,341	14,254	–	27,472	3,611	–	–	–	45,337
Derivative financial instruments	6,264	1,294	3,715	16	–	–	–	11,289	–	116	14,246	–	–	–	–	14,362
Available-for-sale investment securities	132,018	84	32,449	66,133	–	2,991	–	233,675	170,849	379	502	97,577	–	–	–	269,307
Loans to banks	885	9,398	78,900	57,943	1,815	–	14,704	163,645	–	3,059	16,638	71,051	3,619	–	–	94,367
Loans to customers	51,578	10,468	47,233	134,126	83,865	–	9,896	337,166	2,066	10,139	59,833	133,047	63,951	–	–	269,036
Other financial assets	67	23	69	–	–	–	–	159	166	123	381	750	–	–	–	1,420
Total assets	304,142	43,654	182,108	264,318	85,680	2,991	24,600	907,493	280,366	13,816	119,072	306,036	67,570	–	–	786,860
Liabilities																
Deposits from banks and other financial institutions	(40,351)	–	(38,193)	(29,811)	–	–	–	(108,355)	(48,558)	–	–	(70,367)	–	–	–	(118,925)
Current customer accounts	(9,295)	–	–	–	–	–	–	(9,295)	(9,218)	–	–	–	–	–	–	(9,218)
Derivative financial instruments	–	–	–	(12,872)	–	–	–	(12,872)	(2,080)	–	(1,671)	(7,872)	–	–	–	(11,623)
Long-term loans from banks	–	–	(59,459)	(5,933)	(6,868)	–	–	(72,260)	–	–	(14,345)	(59,004)	–	–	–	(73,349)
Debt securities issued	–	(2,258)	(84,094)	(311,368)	–	–	–	(397,720)	–	–	(152,484)	(120,044)	–	–	–	(272,528)
Other financial liabilities	(3,039)	–	(780)	(11)	–	–	–	(3,830)	(348)	–	(933)	(582)	–	–	–	(1,863)
Total liabilities	(52,685)	(2,258)	(182,526)	(359,995)	(6,868)	–	–	(604,332)	(60,204)	–	(169,433)	(257,869)	–	–	–	(487,506)
Net position	251,457	41,396	(418)	(95,677)	78,812	2,991	24,600	303,161	220,162	13,816	(50,361)	48,167	67,570	–	–	299,354
Accumulated net position	251,457	292,853	292,435	196,758	275,570	278,561	303,161		220,162	233,978	183,617	231,784	299,354	299,354		

*(Thousands of euros)***20. Risk management (continued)****Market risk**

Market risk is the risk that the Group 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 Group 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.

Currency risk

Currency risk is the risk of loss resulting from adverse changes in exchange rates with respect to the Group'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 Group applies a VaR methodology to assess currency and equity risks. VaR is a method used in measuring maximum risk of the Group, 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 Group assumes 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 Group is carried out for major currencies and financial instruments of the Group attributable to a securities portfolio.

At estimating value at risk, the Group 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 Group 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 Group 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 30 June 2017 and 31 December 2016, final data on value at risk assessment (VaR) in relation to currency and price risks assumed by the Group are represented as follows:

	<i>30 June 2017</i> <i>(unaudited)</i>	<i>31 December</i> <i>2016</i>
Fixed income securities price risk	1,870	2,325
Price risk on equity securities	256	–
Currency risk	59	27

Despite the fact that 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.
- ▶ 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 Group'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)

20. Risk management (continued)

Market risk (continued)

The Group has assets and liabilities denominated in several foreign currencies. The Bank's financial position and cash flows are exposed to the effects of fluctuations in the prevailing foreign currency exchange rates. Non-monetary financial instruments and financial instruments denominated in functional currency are not exposed to currency risk.

The Group's exposure to currency risk as at 30 June 2017 and 31 December 2016 is presented below:

	30 June 2017 (unaudited)					31 December 2016				
	EUR	USD	RUB	Other currencies	Total	EUR	USD	RUB	Other currencies	Total
Non-derivative financial Assets										
Cash and cash equivalents	72,388	21,768	11,173	889	106,218	66,125	19,969	6,778	159	93,031
Deposits with banks and other financial institutions	55,341	–	–	–	55,341	40,568	4,769	–	–	45,337
Available-for-sale investment securities	139,134	90,123	4,418	–	233,675	208,628	53,070	7,609	–	269,307
Loans to banks	98,126	65,519	–	–	163,645	53,574	40,793	–	–	94,367
Loans to customers	197,952	100,127	–	39,087	337,166	131,906	137,130	–	–	269,036
Other financial assets	72	1	84	2	159	225	14	927	254	1,420
Total non-derivative financial assets	563,013	277,538	15,675	39,978	896,204	501,026	255,745	15,314	413	772,498
Liabilities										
Deposits from banks and other financial institutions	(77,739)	(30,616)	–	–	(108,355)	(36,981)	(81,944)	–	–	(118,925)
Current customer accounts	(9,177)	(118)	–	–	(9,295)	(9,089)	(129)	–	–	(9,218)
Long-term loans from banks	(72,260)	–	–	–	(72,260)	(59,039)	(14,310)	–	–	(73,349)
Debt securities issued	(30,660)	–	(274,458)	(92,602)	(397,720)	(30,046)	–	(151,515)	(90,967)	(272,528)
Other financial liabilities	(3,112)	(30)	(572)	(116)	(3,830)	(529)	(49)	(1,106)	(179)	(1,863)
Total non-derivative financial liabilities	(192,948)	(30,764)	(275,030)	(92,718)	(591,460)	(135,684)	(96,432)	(152,621)	(91,146)	(475,883)
Net balance sheet position (excluding derivative financial instruments)	370,065	246,774	(259,355)	(52,740)	304,744	365,342	159,313	(137,307)	(90,733)	296,615
Derivative financial instruments										
Claims	227,181	–	281,409	91,542	600,132	125,117	–	145,832	90,318	361,267
Liabilities	(330,385)	(216,365)	(15,278)	(39,687)	(601,715)	(224,955)	(124,785)	(8,788)	–	(358,528)
Net balance sheet position including derivative financial instruments	266,861	30,409	6,776	(885)	303,161	265,504	34,528	(263)	(415)	299,354

*(Thousands of euros)***21. Fair value measurement**

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 Group 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 Group 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.

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

	<i>Level 1</i> <i>30 June 2017</i> <i>(unaudited)</i>	<i>Level 2</i> <i>30 June 2017</i> <i>(unaudited)</i>	<i>Level 3</i> <i>30 June 2017</i> <i>(unaudited)</i>	<i>Total</i> <i>30 June 2017</i> <i>(unaudited)</i>
Assets measured at fair value				
Derivative financial assets	–	11,289	–	11,289
Government bonds of countries	86,667	–	–	86,667
Corporate bonds	139,599	4,418	–	144,017
Quoted equity instruments	2,987	4	–	2,991
Investment property	–	–	21,860	21,860
Property and equipment – buildings	–	–	67,158	67,158
Liabilities measured at fair value				
Derivative financial liabilities	–	12,872	–	12,872
Assets for which fair values are disclosed				
Cash and cash equivalents	236	105,982	–	106,218
Deposits with banks and other financial institutions	–	–	55,341	55,341
Loans to banks	–	–	162,267	162,267
Loans to customers	–	–	338,052	338,052
Liabilities for which fair values are disclosed				
Deposits from banks and other financial institutions	–	–	108,355	108,355
Current customer accounts	–	–	9,295	9,295
Long-term loans from banks	–	–	72,260	72,260
Debt securities issued	–	403,323	–	403,323

*(Thousands of euros)***21. Fair value measurement (continued)****Fair value hierarchy (continued)**

The following table shows an analysis of financial instruments recorded at fair value by level of the fair value hierarchy as at 31 December 2016:

	<i>Level 1</i> <i>31 December</i> <i>2016</i>	<i>Level 2</i> <i>31 December</i> <i>2016</i>	<i>Level 3</i> <i>31 December</i> <i>2016</i>	<i>Total</i> <i>31 December</i> <i>2016</i>
Assets measured at fair value				
Derivative financial assets	–	14,362	–	14,362
Government bonds of countries	70,561	–	–	70,561
Corporate bonds	194,003	4,739	–	198,742
Quoted equity instruments	–	4	–	4
Investment property	–	–	21,840	21,840
Property and equipment – buildings	–	–	67,527	67,527
Liabilities measured at fair value				
Derivative financial liabilities	–	11,623	–	11,623
Assets for which fair values are disclosed				
Cash and cash equivalents	104	92,927	–	93,031
Deposits with banks and other financial institutions	–	–	45,337	45,337
Loans to banks	–	–	88,558	88,558
Loans to customers	–	–	270,243	270,243
Liabilities for which fair values are disclosed				
Deposits from banks and other financial institutions	–	–	118,925	118,925
Current customer accounts	–	–	9,218	9,218
Long-term loans from banks	–	–	73,349	73,349
Debt securities issued	–	279,181	–	279,181

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 Group's financial instruments that are carried in the interim condensed consolidated financial statements. The table does not include the fair values of non-financial assets and non-financial liabilities.

	<i>Carrying</i> <i>amount</i> <i>30 June 2017</i> <i>(unaudited)</i>	<i>Fair value</i> <i>30 June 2017</i> <i>(unaudited)</i>	<i>Unrecognized</i> <i>gain/(loss)</i> <i>30 June 2017</i> <i>(unaudited)</i>	<i>Carrying</i> <i>amount</i> <i>31 December</i> <i>2016</i>	<i>Fair value</i> <i>31 December</i> <i>2016</i>	<i>Unrecognized</i> <i>gain/(loss)</i> <i>31 December</i> <i>2016</i>
Financial assets						
Cash and cash equivalents	106,218	106,218	–	93,031	93,031	–
Deposits with banks and other financial institutions	55,341	55,341	–	45,337	45,337	–
Loans to banks	163,645	162,267	(1,378)	94,367	88,558	(5,809)
Loans to customers	337,166	338,052	886	269,036	270,243	1,207
Financial liabilities						
Deposits from banks and other financial institutions	108,355	108,355	–	118,925	118,925	–
Current customer accounts	9,295	9,295	–	9,218	9,218	–
Long-term loans from banks	72,260	72,260	–	73,349	73,349	–
Debt securities issued	397,720	403,323	(5,603)	272,528	279,181	(6,653)
Total unrecognized change in unrealized fair value			(6,095)			(11,255)

(Thousands of euros)

21. Fair value measurement (continued)

Methodologies and assumptions

The following describes the methodologies and assumptions used to determine fair values for those financial instruments that are not recorded at fair value in the interim condensed consolidated financial statements.

Assets for which fair value approximates their carrying amount

For financial assets and financial liabilities that are liquid or have a short-term maturity (less than three months) it is assumed that their carrying amount approximates their fair value.

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

Management has estimated that at 30 June 2017 and 31 December 2016 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 existing practice of renegotiating interest rates to reflect current market conditions and, therefore, a majority of balances carry interest at rates approximating market interest rates.

Fixed and floating rate financial instruments

The fair values of floating interest rate instruments generally approximate their carrying amount. In case of significant changes in the market situation interest rates on loans to customers and banks, and long-term loans to banks bearing a fixed interest rate may be renegotiated. Consequently, interest rates on the financial instruments issued or received shortly before the reporting date are not significantly different from the current interest rates applicable to new instruments with similar credit risk and maturity. If the Group determines that interest rates on previously issued loans or received borrowings differ materially from those applicable to similar instruments at the reporting date, the Group estimates the fair value of these loans and borrowings. The estimate is based on the discounted cash flow method using interest rates applicable to new instruments with similar credit risk and maturity. Discount rates used depend on currency, maturity of the instrument and credit risk of the counterparty. Management has estimated that at 30 June 2017 and 31 December 2016 the fair value of deposits from banks and long-term loans from banks was not significantly different from their respective carrying amount.

22. Segment information

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

Credit investment activity	Investment banking services, including long-term corporate and interbank financing, as well as financing through trade loans.
Treasury	Operations in financial markets, transactions with securities, derivative financial instruments and foreign currency, and liquidity management.
Other operations	Operational leasing services, other operations.

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*(Thousands of euros)***22. 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 interim condensed consolidated financial statements. The following table presents income, profit, assets and liabilities of the Group's operating segments:

30 June 2017 (unaudited)	Credit investment activity	Treasury	Other operations	Total
Income				
<i>External customers</i>				
Interest income	11,390	4,738	19	16,147
Fee and commission income	302	–	–	302
Net gains from dealing in foreign currencies and operations with derivatives	–	12,520	–	12,520
Net gains from revaluation of hedging instruments	–	65	–	65
Net gains from available-for-sale investment securities	–	4,553	–	4,553
Income from lease of investment property	–	–	2,049	2,049
Reversal of allowance for impairment of other assets	–	–	27	27
Other segment income	2	–	83	85
Total income	11,694	21,876	2,178	35,748
Interest expense	(7,313)	(7,051)	–	(14,364)
Fee and commission expense	(9)	(60)	(2)	(71)
Net loss from revaluation of derivative financial instruments	–	(4,591)	–	(4,591)
Net (losses)/gains from revaluation of assets and liabilities in foreign currencies	–	(955)	11	(944)
Allowance for impairment of financial assets	(3,781)	–	–	(3,781)
Other segment expenses	(89)	(83)	(477)	(649)
Segment results	502	9,136	1,710	11,348
Other unallocated expenses				(9,061)
Profit for the period				2,287
Development portfolio	490,923	65,631	–	556,554
Other segment assets	9,896	340,413	95,806	446,115
Total segment assets	500,819	406,044	95,806	1,002,669
Total segment liabilities	276,007	324,495	9,403	609,905
Other segment information				
Capital expenditures	–	–	70	70

When allocating resources managed by operating segments, the Group's management identifies the "Development portfolio" assets separately based on whether the investment purpose fulfills the Group's mission. "Development portfolio" includes loans to banks and loans to customers excluding impaired loan projects and the investments in debt securities purchased upon initial placement by the issuer.

(Thousands of euros)

22. Segment information (continued)

<i>30 June 2016 (unaudited)</i>	<i>Credit investment activity</i>	<i>Treasury</i>	<i>Other operations</i>	<i>Total</i>
Income				
External customers				
Interest income	9,677	6,560	–	16,237
Fee and commission income	369	–	156	525
Net gains from trading in foreign currencies	–	11,026	–	11,026
Net gains from revaluation of derivative financial instruments	–	14,198	–	14,198
Net gains from available-for-sale investment securities	–	3,186	–	3,186
Income from lease of investment property	–	–	1,782	1,782
Net gains from held-to-maturity investment securities	–	251	–	251
Reversal of allowance for impairment of financial assets	–	–	89	89
Reversal of allowance for impairment of other assets	–	–	14	14
Other segment income	102	–	274	376
Total income	10,148	35,221	2,315	47,684
Interest expense	(5,288)	(7,896)	–	(13,184)
Fee and commission expense	(2)	(60)	(4)	(66)
Net losses from revaluation of assets and liabilities in foreign currencies	–	(20,996)	(50)	(21,046)
Other segment expenses	–	–	(184)	(184)
Segment results	4,858	6,269	2,077	13,204
Other unallocated expenses				(8,174)
				5,030
Profit for the period				
Development portfolio	411,277	–	–	411,277
Other segment assets	5,103	403,401	101,836	510,340
Total segment assets	416,380	403,401	101,836	921,617
Total segment liabilities	141,326	361,182	4,125	506,633
Other segment information				
Capital expenditures	–	–	566	566

For the six months ended 30 June 2017, the Group's revenue from lease operations with two external counterparties (for the six months ended 30 June 2016: two counterparties) exceeded 20% of the Group's total revenue (for the six months ended 30 June 2017: EUR 1,511 thousand; for the six months ended 30 June 2016: EUR 1,443 thousand).

Geographical information

Allocation of the Group's revenue from transactions with external customers and non-current assets based on the location of these customers and assets for the periods ended 30 June 2017 and 30 June 2016 is presented in the table below:

	<i>30 June 2017 (unaudited)</i>				<i>30 June 2016 (unaudited)</i>			
	<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	4,135	7,035	4,977	16,147	4,677	7,961	3,599	16,237
Income from lease of investment property	1,942	107	–	2,049	1,782	–	–	1,782
Non-current assets	79,207	14,324	–	93,531	100,101	–	–	100,101

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

(Thousands of euros)

22. Segment information (continued)

Geographical information (continued)

Information on risk concentration by geographical region is based on geographical location of the Group's counterparties. The geographical concentration of the Group's assets and liabilities as at 30 June 2017 and 31 December 2016 is presented below:

	<i>30 June 2017 (unaudited)</i>									
	<i>Russian Federation</i>	<i>Republic of Bulgaria</i>	<i>Romania</i>	<i>Slovak Republic</i>	<i>Mongolia</i>	<i>Socialist Republic of Vietnam</i>	<i>Czech Republic</i>	<i>Hungary</i>	<i>Other countries</i>	<i>Total</i>
Assets										
Cash and cash equivalents	11,275	791	399	43	15,313	–	–	–	78,397	106,218
Deposits with banks and other financial institutions	4,680	–	–	–	–	–	–	–	50,661	55,341
Derivative financial instruments	3,577	–	–	–	–	–	–	–	7,712	11,289
Available-for-sale investment securities	17,336	48,971	37,875	9,974	11,293	2,076	–	1,024	105,126	233,675
Loans to banks less allowance for impairment	92,617	–	–	–	42,249	26,224	–	–	2,555	163,645
Loans to customers less allowance for impairment	69,702	59,479	51,347	20,016	4,737	–	35,038	22,865	73,982	337,166
Other financial assets	134	7	–	6	1	–	–	2	9	159
Assets	199,321	109,248	89,621	30,039	73,593	28,300	35,038	23,891	318,442	907,493
Liabilities										
Deposits from banks and other financial institutions	60	–	–	7,507	–	–	–	–	100,788	108,355
Derivative financial instruments	5,799	–	597	–	–	–	–	–	6,476	12,872
Long-term loans from banks	9,899	7,425	–	–	–	–	–	7,424	47,512	72,260
Debt securities issued	275,090	–	91,970	30,660	–	–	–	–	–	397,720
Other financial liabilities	759	–	–	11	–	–	3,000	–	60	3,830
Liabilities	291,607	7,425	92,567	38,178	–	–	3,000	7,424	154,836	595,037

International Investment Bank

(Thousands of euros)

22. Segment information (continued)

Geographical information (continued)

31 December 2016

	<i>Russian Federation</i>	<i>Republic of Bulgaria</i>	<i>Romania</i>	<i>Slovak Republic</i>	<i>Mongolia</i>	<i>Socialist Republic of Vietnam</i>	<i>Czech Republic</i>	<i>Hungary</i>	<i>Other countries</i>	<i>Total</i>
Assets										
Cash and cash equivalents	16,398	808	26	38	–	–	–	–	75,761	93,031
Deposits with banks and other financial institutions	7,159	–	–	–	–	–	–	–	38,178	45,337
Derivative financial instruments	2,980	–	–	–	–	–	–	–	11,382	14,362
Available-for-sale investment securities	44,688	49,482	36,713	10,286	3,475	–	–	–	124,663	269,307
Loans to banks less allowance for impairment	27,378	–	–	–	–	47,970	19,019	–	–	94,367
Loans to customers less allowance for impairment	61,213	58,967	37,981	308	–	5,683	–	22,930	81,954	269,036
Other financial assets	1,407	8	–	1	–	–	–	–	4	1,420
Assets	161,223	109,265	74,720	10,633	3,475	53,653	19,019	22,930	331,942	786,860
Liabilities										
Deposits from banks and other financial institutions	–	–	–	7,508	–	–	–	–	111,417	118,925
Derivative financial instruments	4,528	–	633	–	–	–	–	–	6,462	11,623
Long-term loans from banks	9,840	21,690	–	–	7,380	–	–	–	34,439	73,349
Debt securities issued	151,434	–	90,967	30,127	–	–	–	–	–	272,528
Other financial liabilities	1,805	–	–	19	–	–	–	–	39	1,863
Liabilities	167,607	21,690	91,600	37,654	7,380	–	–	–	152,357	478,288

Other countries include non-member countries.

*(Thousands of euros)***23. Related party transactions**

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 paid 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 as at 30 June 2017 and 31 December 2016, and related expense and income for the six months ended 30 June 2017 and 30 June 2016 are as follows:

	<i>Related party</i>	<u>30 June 2017 (unaudited) Carrying amount</u>	<u>31 December 2016 Carrying amount</u>
Consolidated statement of financial position			
Current customer accounts	Key management personnel	1,839	1,783
Other non-financial liabilities	Key management personnel	513	416
	<i>Related party</i>	<u>30 June 2017 (unaudited) Income/ (expense)</u>	<u>30 June 2016 (unaudited) Income/ (expense)</u>
Consolidated income statement			
Interest expense on current customer accounts	Key management personnel	(27)	(34)
Net interest expense after allowance for loan impairment		<u>(27)</u>	<u>(34)</u>
Operating losses		<u>(27)</u>	<u>(34)</u>
Employee benefits	Key management personnel	(669)	(572)
Compensation for travel expenses and medical insurance	Key management personnel	(32)	(55)
Operating expenses		<u>(701)</u>	<u>(627)</u>
Net loss for the period		<u>(728)</u>	<u>(661)</u>

24. Capital adequacy

Capital adequacy ratio is the most important financial indicator characterizing credibility of 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 Supervision recommends maintaining the ratio of capital to risk-weighted assets ("capital adequacy ratio") above the prescribed minimum level. As at 30 June 2017, this minimum level is 8% (31 December 2016: 8%).

Besides, taking into account the Bank's status as the multilateral development institution and the structure of the Bank's member countries, the capital adequacy ratio was set by the Council at the level of not less than 25% as at 30 June 2017 (31 December 2016: 25%).

*(Thousands of euros)***24. Capital adequacy (continued)**

The following table shows the composition of the Group's capital position computed in accordance with the Basel Accord (Basel II) as at 30 June 2017 and 31 December 2016.

	<i>30 June 2017</i> <i>(unaudited)</i>	<i>31 December</i> <i>2016</i>
Capital		
Tier 1 capital	378,836	378,034
Tier 2 capital	11,709	11,439
Total regulatory capital	390,545	389,473
Risk-weighted assets		
Credit risk	697,229	482,693
Market risk	179,730	186,588
Operational risk	48,623	57,999
Total risk weighted assets	925,582	727,280
Total capital expressed as a percentage of risk-weighted assets, % ("capital adequacy ratio")	42.19%	53.55%
Total tier 1 capital expressed as a percentage of risk-weighted assets, % ("tier 1 capital adequacy ratio")	40.93%	51.98%

(The end)

Report on Review of Interim Financial Information
International Investment Bank and its subsidiary
for the six-month period ended 30 June 2018

August 2018

Report on Review of Interim Financial Information of International Investment Bank and its subsidiary

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Report on Review of Interim Financial Information

To Council of International Investment Bank

Introduction

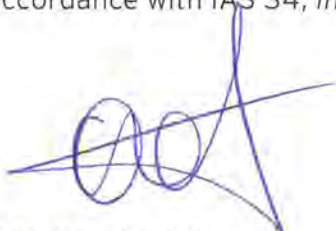
We have reviewed the accompanying interim condensed consolidated financial statements of International Investment Bank and its subsidiary, which comprise the interim consolidated statement of financial position as at 30 June 2018, the interim consolidated income statement, interim consolidated statement of comprehensive income, interim consolidated statement of changes in equity and interim consolidated statement of cash flows for the six-month period then ended, and selected explanatory notes (interim financial information). Management of International Investment Bank is responsible for the preparation and presentation of this interim financial information in accordance with IAS 34, *Interim Financial Reporting*. Our responsibility is to express a conclusion on this interim financial information based on our review.

Scope of review

We conducted our review in accordance with International Standard on Review Engagements 2410, *Review of Interim Financial Information Performed by the Independent Auditor of the Entity*. A review of interim financial information consists of making inquiries, primarily of persons responsible for financial and accounting matters, and applying analytical and other review procedures. A review is substantially less in scope than an audit conducted in accordance with International Standards on Auditing and consequently does not enable us to obtain assurance that we would become aware of all significant matters that might be identified in an audit. Accordingly, we do not express an audit opinion.

Conclusion

Based on our review, nothing has come to our attention that causes us to believe that the accompanying interim financial information is not prepared, in all material respects, in accordance with IAS 34, *Interim Financial Reporting*.



O.V. Youshenkov
Partner
Ernst & Young Vneshaudit LLC

3 August 2018

Details of the entity

Name: International Investment Bank

Bank operates on the basis of the Agreement on the Establishment of the International Investment Bank dated 10 July 1970, registered in the UN Secretariat on 1 December 1971 under No. 11417.

Address: Russia 107078, Moscow, Mashl Poryvaevoy str., 7.

Details of the auditor

Name: Ernst & Young Vneshaudit LLC

Record made in the State Register of Legal Entities on 4 February 2016, State Registration Number 1167746123478.

Address: Russia 115035, Moscow, Sadovnicheskaya naberezhnaya, 77, building 1.

Ernst & Young Vneshaudit LLC is a member of Self-regulated organization of auditors "Russian Union of auditors" (Association) ("SRO RUA"). Ernst & Young Vneshaudit LLC is included in the control copy of the register of auditors and audit organizations, main registration number 11603050953.

INTERIM CONSOLIDATED STATEMENT OF FINANCIAL POSITION**As at 30 June 2018***(Thousands of euros)*

	Note	30 June 2018 <i>(unaudited)</i>	31 December 2017
Assets			
Cash and cash equivalents	5	57,225	66,097
Deposits with banks and other financial institutions	6	34,296	45,889
Derivative financial assets	7	1,347	7,761
Available-for-sale securities	8	–	138,704
Available-for-sale securities pledged under repurchase agreements	8	–	76,723
Securities at fair value through other comprehensive income	8	174,808	–
Securities at fair value through other comprehensive income pledged under repurchase agreements	8	19,038	–
Securities at amortized cost	9	29,383	–
Securities at amortized cost pledged under repurchase agreements	9	12,039	–
Loans to banks	10	164,116	201,635
Loans to customers	11	545,627	462,514
Investment property		20,862	21,853
Property, equipment and intangible assets		71,570	72,388
Other assets	12	2,846	2,476
Total assets		1,133,157	1,096,040
Liabilities			
Due to banks and other financial institutions	14	84,941	65,511
Derivative financial liabilities	7	36,570	15,073
Current customer accounts		8,659	8,593
Long-term loans of banks	15	46,077	95,592
Debt securities issued	16	581,753	509,213
Other liabilities	12	7,555	6,396
Total liabilities		765,555	700,378
Equity			
Subscribed capital	17	1,300,000	1,300,000
Callable capital		(985,038)	(985,038)
Paid-in capital		314,962	314,962
Revaluation reserve for securities at fair value through other comprehensive income (2017: revaluation reserve for available-for-sale securities)		(4,239)	240
Revaluation reserve for property and equipment		13,748	13,748
Foreign currency translation reserve		(93)	(76)
Retained earnings less net income for the period		38,137	65,783
Net income for the period		5,087	1,005
Total equity		367,602	395,662
Total equity and liabilities		1,133,157	1,096,040

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

Nikolay Kosov



Chairman of the Board

Elena Minduksheva



Deputy Director of the Finance Department

3 August 2018

The accompanying notes 1-28 are an integral part of these interim condensed consolidated financial statements.

INTERIM CONSOLIDATED INCOME STATEMENT**Six months ended 30 June 2018***(Thousands of euros)*

	<i>Note</i>	<i>For the six months ended 30 June (unaudited)</i>	
		<i>2018</i>	<i>2017</i>
Interest income calculated using the EIR method	20	21,609	16,147
Other interest income	20	7,943	8,697
Interest expenses calculated using the EIR method	20	(17,476)	(14,364)
Other interest expenses	20	(908)	(806)
Net interest income		11,168	9,674
Net reversal/(charge) of allowance for credit losses on financial instruments	5-6, 8, 10-11, 13, 18	60	(3,781)
Net interest expense after allowance for loan impairment		11,228	5,893
Fee and commission income		870	302
Fee and commission expense		(115)	(71)
Net fee and commission income		755	231
Net losses from dealing in foreign currencies and operations with derivatives	21	(1,860)	(841)
Net gains from operations with securities at fair value through profit or loss		92	–
Net gains from operations with securities at fair value through other comprehensive income		2,238	4,553
Dividend income		6	–
Income from lease of investment property	19	2,032	2,049
Other income		532	85
Net non-interest income		3,040	5,846
Operating income		15,023	11,970
Net reversal of other allowances	12, 13	2	27
General and administrative expenses	22	(8,903)	(9,061)
Cost of inventories sold		(48)	–
Other operating expenses on banking operations		(987)	(649)
Operating expenses		(9,936)	(9,683)
Net income for the period		5,087	2,287

The accompanying notes 1-28 are an integral part of these interim condensed consolidated financial statements.

INTERIM CONSOLIDATED STATEMENT OF COMPREHENSIVE INCOME**Six months ended 30 June 2018***(Thousands of euros)*

	<i>Note</i>	<i>For the six months ended 30 June (unaudited)</i>	
		<i>2018</i>	<i>2017</i>
Net income for the period		5,087	2,287
Other comprehensive income			
<i>Other comprehensive income to be reclassified to profit or loss in subsequent periods</i>			
Impact of adopting IFRS 9		(2,043)	–
Change in unrealized revaluation of securities at fair value through other comprehensive income	17	(4,737)	271
Change in the allowance for expected credit losses related to securities at fair value through other comprehensive income	8	306	–
Translation differences		(17)	(12)
Net other comprehensive income to be reclassified to profit or loss in subsequent periods		(6,491)	259
<i>Other comprehensive loss not to be reclassified to profit or loss in subsequent periods</i>			
Losses from revaluation of equity instruments at fair value through other comprehensive income		(48)	–
Net other comprehensive loss not to be reclassified to profit or loss in subsequent periods		(48)	–
Other comprehensive (loss)/income		(6,539)	259
Total comprehensive (loss)/income for the period		(1,452)	2,546

The accompanying notes 1-28 are an integral part of these interim condensed consolidated financial statements.

INTERIM CONSOLIDATED STATEMENT OF CHANGES IN EQUITY**Six months ended 30 June 2018***(Thousands of euros)*

	<i>Subscribed capital</i>	<i>Callable capital</i>	<i>Revaluation reserve for securities</i>	<i>Revaluation reserve for property and equipment</i>	<i>Foreign currency translation reserve</i>	<i>Retained earnings</i>	<i>Total equity</i>
At 31 December 2016	1,300,000	(986,947)	(1,506)	12,945	(57)	65,783	390,218
Profit for the period	–	–	–	–	–	2,287	2,287
Other comprehensive income/(loss) for the period	–	–	271	–	(12)	–	259
Total comprehensive income/(loss)	–	–	271	–	(12)	2,287	2,546
At 30 June 2017 (unaudited)	1,300,000	(986,947)	(1,235)	12,945	(69)	68,070	392,764
At 31 December 2017	1,300,000	(985,038)	240	13,748	(76)	66,788	395,662
Impact of adopting IFRS 9	–	–	2,043	–	–	(28,903)	(26,860)
Balance at 1 January 2018 restated under IFRS 9	1,300,000	(985,038)	2,283	13,748	(76)	37,885	368,802
Profit for the period	–	–	–	–	–	5,087	5,087
Other comprehensive loss for the period	–	–	(6,522)	–	(17)	–	(6,539)
Total comprehensive (loss)/income	–	–	(6,522)	–	(17)	5,087	(1,452)
Reclassification of the net change in fair value of equity instruments at derecognition	–	–	–	–	–	252	252
At 30 June 2018 (unaudited)	1,300,000	(985,038)	(4,239)	13,748	(93)	43,224	367,602

The accompanying notes 1-28 are an integral part of these interim condensed consolidated financial statements.

INTERIM CONSOLIDATED STATEMENT OF CASH FLOWS**Six months ended 30 June 2018***(Thousands of euros)*

	<i>For the six months ended 30 June (unaudited)</i>		
	<i>Note</i>	<i>2018</i>	<i>2017</i>
Cash flows from operating activities			
Interest, fees and commissions received		30,120	22,261
Interest, fees and commissions paid		(5,226)	(6,052)
Realized gains less losses from dealing in foreign currencies and operations with derivatives		7,457	6,386
Cash flows from lease of investment property		2,032	2,049
General and administrative expenses		(7,750)	(7,364)
Other operating (expenses)/income on banking operations		(53)	(59)
Cash flows from operating activities before changes in operating assets and liabilities		26,580	17,221
<i>Net (increase)/decrease in operating assets</i>			
Deposits with banks and other financial institutions		20,255	(17,053)
Loans to banks		30,797	(69,609)
Loans to customers		(96,247)	(82,012)
Other assets		(280)	620
<i>Net increase/(decrease) in operating liabilities</i>			
Due to banks and other financial institutions		10,903	(4,037)
Current customer accounts		(570)	(543)
Other liabilities		(7,407)	4,397
Net cash flows from operating activities		(15,969)	(151,016)
Cash flows from investing activities			
Dividend income		6	–
Interest received		2,543	2,935
Purchase of securities at fair value through other comprehensive income		(189,836)	(193,404)
Proceeds from sale and redemption of securities at fair value through other comprehensive income		172,189	227,954
Proceeds from redemption of securities at amortized cost		253	–
Proceeds from sale of investment property/(investments) in investment property		1,074	(20)
Acquisition of property, equipment and intangible assets		(347)	(836)
Proceeds from sale of property, equipment and intangible assets		–	3
Net cash flows from investing activities		(14,118)	36,632
Cash flows from financing activities			
Interest paid		(12,150)	(10,533)
Long-term interbank financing raised		10,172	13,000
Long-term interbank financing repaid		(60,455)	(13,451)
Placement of debt securities issued		84,470	205,194
Redemption and repurchase of debt securities issued		–	(62,858)
Net cash flows from financing activities		22,037	131,352
Effect of exchange rate changes on cash and cash equivalents		(822)	(3,781)
Net increase/(decrease) in cash and cash equivalents		(8,872)	13,187
Cash and cash equivalents, beginning		66,097	93,031
Cash and cash equivalents, ending	5	57,225	106,218

The accompanying notes 1-28 are an integral part of these interim condensed consolidated financial statements.

(Thousands of euros)

1. Principal activities

These consolidated financial statements include the financial statements of the International Investment Bank (the “Bank”, or “IIB”) and CJSC IIB Capital, the subsidiary of the Bank. The Bank and its subsidiary are hereinafter collectively referred to as the “Group”. The International Investment Bank is the parent company of the Group. Information on the subsidiary of the Bank is presented in Note 2.

The International Investment 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 Statute. 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 Poryvaevoy St., Moscow, Russia, and the European regional office in Bratislava (Eurovea Central 1, Pribinova 4, Bratislava, 81109, Slovak Republic).

On 31 July 2014, the EU Council imposed sectoral sanctions against Russia. The preamble of the Decision of the EU Council of 31 July 2014 (paragraph 9) and Council Regulation (EU) No. 833/2014 of 31 July 2014 (paragraph 5), which was developed based on the Decision, emphasize that the sanctions do not cover Russia-based institutions with international status established by intergovernmental agreements in which Russia is one of the parties. Therefore, the IIB is directly excluded from the list of financial institutions to which the restrictions apply.

The Group continues to expand its operations in accordance with its mandate and strategic objectives established by the member countries:

- ▶ The Bank has wound up the introduction of changes to its constituent documents and implementation of the three level corporate governance structure. On 25 June 2018, the Protocol on Introducing Changes to the Agreement on the Establishment of the International Investment Bank and the Statutes (hereinafter, the “Protocol”) was ratified by the last remaining member country, the Slovak Republic. Accordingly, in August 2018, the Protocol will enter into force and new IIB corporate governance bodies (Board of Governors and Board of Directors) will be set up.
- ▶ In June 2018, the city of Yaroslavl, Russian Federation, hosted the 109th Meeting of the IIB Council. It was the first Council meeting in the new strategic cycle. Member countries unanimously supported the establishment of an IIB European Unit (Budapest) – a multifunctional front office, which also will perform middle and back office functions. To implement the decision, on 18 June 2018, the Government of Hungary and the IIB signed a Memorandum of Understanding, which provides legal foundation for the cooperation between the IIB and the Government of Hungary to open the IIB European Unit in Budapest, as well as formalizes intentions of both parties to finalize until the end of the year 2018 and sign the host-country agreement for the IIB European Unit, in order for the office to start operating in full at the beginning of 2019.
- ▶ As part of the 2013 Capitalization Program, the Government of Romania decided to make an additional contribution to the IIB’s paid-in capital of EUR 4 million. On 12 July 2018, the additional contribution was transferred to the Bank’s correspondent account.
- ▶ In June 2018, the Council of the Bank approved key approaches to the new IIB Capitalization Program for 2018-2022 (hereinafter, the “Program”). A detailed Program will be prepared in close cooperation with the member states until the year-end and submitted for approval to the IIB Council.
- ▶ On 12 April 2018, Standard & Poor’s international rating agency upgraded the IIB long-term credit rating to BBB+ with stable outlook. On 30 April 2018, Moody’s Investors Services international rating agency also upgraded the IIB long-term credit rating to A3 with stable outlook. In addition, the Bank was assigned the following investment grade ratings: BBB with positive outlook (Fitch Ratings) and A with positive outlook (Dagong Global Credit Rating).
- ▶ In April-June 2018, the IIB successfully placed its first CZK-denominated issue of bonds at the Vienna and Prague Stock Exchanges. The private placement issue totaled CZK 750 million.
- ▶ In October 2018, the Bank will become a full-fledged member of the International Development Finance Club (IDFC), a network of leading national and regional development banks.

*(Thousands of euros)***1. Principal activities (continued)****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>	<i>30 June 2018, % (unaudited)</i>	<i>31 December 2017, %</i>
Russian Federation	47.634	47.634
Republic of Bulgaria	13.399	13.399
Hungary	12.700	12.700
Czech Republic	9.644	9.644
Slovak Republic	6.820	6.820
Romania	5.859	5.859
Republic of Cuba	1.702	1.702
Socialist Republic of Vietnam	1.165	1.165
Mongolia	1.077	1.077
	100.000	100.000

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

In its 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

Economic and political development of the Bank's member countries affects the activities of enterprises operating in these countries. Considering this fact, the Group performs its operations with reference to the regional features of its member countries to ensure overall assessment and control of credit and operational risks.

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

2. Basis of preparation**General**

These interim condensed consolidated financial statements have been prepared for the six months ended 30 June 2018 in accordance with International Accounting Standard (IAS) 34 *Interim Financial Reporting* approved by the International Accounting Standards Board.

The interim condensed consolidated financial statements do not include all the information and disclosures required in the annual consolidated financial statements and should be read in conjunction with the Bank's annual consolidated financial statements as at 31 December 2017.

Subsidiary

As at 30 June 2018, the Bank is a parent company of the Group, which owns CJSC IIB Capital (the Bank's 100% subsidiary) established in 2012 to deal with issues related to IIB activities in Russia, including the provision of trustee services. As at 30 June 2018, the authorized capital of the subsidiary is RUB 44.5 thousand (31 December 2017: RUB 44.5 thousand), which is equivalent to EUR 1.1 thousand at the historical exchange rate at the date of establishment of the subsidiary.

(Thousands of euros)

2. Basis of preparation (continued)

Basis of measurement

These interim condensed consolidated 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 in the property, equipment and investment property stated at revalued amounts.

Functional and presentation currency

Euro (“EUR”) is the Group’s functional and presentation currency as it reflects the economic substance of the underlying operations conducted by the Group and circumstances affecting its operations, because most financial assets and financial liabilities as well as income and expenses of the Group are denominated in EUR.

These interim condensed consolidated financial statements are presented in thousands of euros (“thousands of euros” or “EUR thousand”), unless otherwise indicated.

3. Summary of accounting policies

Changes in accounting policies

The Group has adopted the following amended IFRS which are effective for annual periods beginning on or after 1 January 2018. The Group has not early adopted standards, interpretations or amendments that have been issued but are not yet effective. The nature and the impact of each new amendment are described below:

IFRS 9 Financial Instruments

IFRS 9 replaces IAS 39 *Financial Instruments: Recognition and Measurement* and is effective for annual periods beginning on or after 1 January 2018.

The Group has not restated comparative information for 2017 for financial instruments in the scope of IFRS 9. Therefore, the comparatives for 2017 are presented in accordance with IAS 39 and may not be consistent with the data for 2018. Differences arising from the adoption of IFRS 9 have been recognized directly in equity as at 1 January 2018 and are disclosed below.

(a) Classification and measurement

Pursuant to IFRS 9, all debt financial assets that do not meet the Solely Payments of Principal and Interest (“SPPI”) criterion are classified at initial recognition as financial assets at fair value through profit or loss (“FVPL”). According to this criterion, debt instruments that do not meet the definition of basic credit agreement (such as instruments with embedded conversion options or non-recourse loans) are measured at FVPL. Those debt financial instruments that meet the SPPI criterion are classified at initial recognition based on the business model used for managing such instruments:

- ▶ Instruments held to receive contractual cash flows are measured at amortized cost.
- ▶ Instruments held to receive the contractual cash flows and for sale are classified as at fair value through other comprehensive income (FVOCI).
- ▶ Instruments held for other purposes are classified as at FVPL.

Equity financial assets are classified at initial recognition at FVPL, except when the entity decided to irrevocably designate such assets at FVOCI. For equity financial instruments classified at FVOCI, all realized and unrealized gains or losses (except for dividend income) are recognized in other comprehensive income, with no subsequent reclassification to profit or loss.

The classification and measurement of financial liabilities remains almost unchanged from the existing requirements of IAS 39.

Derivative financial instruments continue to be measured at FVPL.

*(Thousands of euros)***3. Summary of accounting policies (continued)****Changes in accounting policies (continued)***(b) Impairment*

The adoption of IFRS 9 fundamentally changes the Group's accounting for allowances for expected credit losses by replacing the IAS 39 incurred loss approach with the forward-looking expected credit loss ("ECL") approach. Starting from 1 January 2018, the Group recognizes the allowance for ECL for all loans and other debt financial instruments not measured at FVPL, as well as for loan commitments and financial guarantee contracts, which are collectively referred to as financial instruments in this section. According to IFRS 9, requirements for impairment are not applicable to equity instruments.

The allowance for ECL is based on credit losses expected to be incurred over the life of the underlying asset (lifetime ECL), if there has been a significant increase in credit risk since the date of initial recognition. Otherwise, the allowance for ECL is based on 12-month expected credit losses. 12-month ECL are part of lifetime ECL and represent ECL arising from defaults on a financial instrument expected to occur 12 months after the reporting date.

The Group has established a policy to perform an assessment, at the end of each reporting period, of whether a financial instrument's credit risk has increased significantly since initial recognition, by considering the change in the risk of default occurring over the remaining life of the financial instrument. Based on the above, the Group classifies financial instruments issued and exposed to credit risk as follows:

- | | |
|----------|---|
| Stage 1: | At initial recognition of a financial instrument, the Group recognizes an impairment allowance in the amount equal to 12-month ECL. Stage 1 also includes loans and other financial instruments for which credit risk decreased to the extent they have been reclassified from Stage 2. |
| Stage 2: | If there has been a significant increase in credit risk for the financial instrument since its initial recognition, the Group recognizes an impairment allowance in the amount equal to lifetime ECL. Stage 2 also includes loans and other credit facilities for which credit risk decreased to the extent they have been reclassified from Stage 3. |
| Stage 3: | Credit-impaired financial instruments. The Group recognizes an impairment allowance in the amount equal to lifetime ECL. |

If the Group does not have reasonable expectations regarding recoverability of the financial asset in full or in part, the gross carrying amount of the asset should be decreased. Such a decrease is considered (a partial) derecognition of the financial asset.

Key inputs required for ECL calculation are as follows:

- | | |
|-----------------------------|--|
| Probability of default (PD) | <i>Probability of default</i> (PD) is an estimate of the probability of default within a specified period. Default may occur only at a certain point in time within the stated period unless the asset was derecognized or excluded from the portfolio. |
| Exposure at default (EAD) | <i>Exposure at default</i> (EAD) is an estimate of the exposure at default at a certain future date, adjusted to reflect its changes expected after the reporting date, including payments of interest or the principal amount due under a contract or otherwise, as well as repayment of loans issued and interest accrued on overdue payments. |
| Loss given default (LGD) | <i>Loss given default</i> (LGD) is an estimate of losses arising on default at a certain point in time. LGD is calculated as a difference between contractual cash flows and cash flows a creditor expects to receive, including from the sale of collateral. This estimate is usually expressed as EAD percentage. |

The Group uses a wide range of forecast information as economic inputs for its ECL assessment models. Impairment losses and their reversal are accounted for and recorded separately from gain or loss from modification recognized as an adjustment to the gross carrying amount of financial assets.

The Group considers an increase in the credit risk related to a financial asset since the date of its initial recognition to be significant, if credit quality of a counterparty has deteriorated significantly and there are grounds to believe that this deterioration can adversely affect the counterparty's ability to meet its liabilities to the Group. In addition, the Group applies a qualitative tool to identify a significant increase in credit risk associated with an asset, e.g. a list of defaulting customers / non-performing instruments or asset restructuring.

*(Thousands of euros)***3. Summary of accounting policies (continued)****Changes in accounting policies (continued)**

Regardless of changes in ratings, an increase in credit risk since the date of initial recognition is considered significant, if contractual payments are over 30 days past due.

For ECL calculation purposes, the Group considers the financial instrument to be in default, and, therefore, includes it in Stage 3 (credit-impaired assets) whenever a borrower is 90 days late with contractual payments. In case of treasury or interbank transactions, the Group considers that there is a default and takes prompt remedy measures whenever the counterparty fails to make intraday payments required by specific agreements before the end of an operating day and the Group has no grounds to believe that this non-payment was a technical delay.

The Group estimates on an individual basis the ECL for all assets included in Stage 3.

(c) Effect of transition to IFRS 9

The effect of transition to IFRS 9 on the interim statement of financial position and retained earnings, including the effect from replacing the IAS 39 incurred credit loss approach with the IFRS 9 ECL approach, is described below.

A reconciliation between carrying amounts under IAS 39 and IFRS 9 as at 1 January 2018 is as follows:

<i>Financial assets</i>	<i>Note</i>	<i>IAS 39 measurement</i>		<i>Reclas- sification</i>	<i>Difference (ECL)</i>	<i>Difference (other)</i>	<i>IFRS 9 measurement</i>	
		<i>Category</i>	<i>Amount</i>				<i>Amount</i>	<i>Category</i>
Cash and cash equivalents		L&R ¹	66,097	–	(8)	–	66,089	Amortized cost
Deposits with banks and other financial institutions		L&R	45,889	–	(241)	–	45,648	Amortized cost
Loans to banks – amortized cost		L&R	201,635	–	(8,848)	–	192,787	Amortized cost
Loans to customers – amortized cost		L&R	462,514	–	(18,542)	–	443,972	Amortized cost
<i>From: available-for-sale securities, including those pledged under repurchase agreements</i>		AFS ³	215,427	(215,427)	–	–	–	
<i>To:</i>								
Securities at fair value through other comprehensive income, including those pledged under repurchase agreements		AFS	–	175,065	(440)	440	175,065	FVOCI (debt instruments, investments)
Securities, including those pledged under repurchase agreements – equity securities at fair value through profit or loss	B	AFS	–	1,710	–	–	1,710	FVPL (equity instruments)
Securities at amortized cost	A	HTM	–	38,652	–	1,649	40,301	FVOCI (debt instruments)
Other financial assets		L&R	728	–	(6)	–	722	
Total assets			992,290	–	(28,085)	2,089	966,294	
Non-financial liabilities								
Allowances for expected credit losses on credit-related commitments and contingencies			–	–	864	–	864	
Total liabilities			–	–	864	–	864	

¹ L&R – loans and receivables.

² HTM – held to maturity.

³ AFS – available for sale.

A As at 1 January 2018, the Group reclassified a part of its assets previously classified as ‘available for sale’ to ‘debt instruments measured at amortized cost’. These instruments satisfied the SPPI criterion, were unquoted in an active market and held to collect related cash flows rather than for sale.

B The Group made an irrevocable election to reclassify certain investments in equity instruments previously classified as ‘available for sale’ to ‘investments in equity instruments at FVOCI’.

*(Thousands of euros)***3. Summary of accounting policies (continued)****Changes in accounting policies (continued)**

The impact of transition to IFRS 9 on reserves and retained earnings is as follows:

	<i>Reserves and retained earnings</i>
Revaluation reserve for securities at fair value through other comprehensive income (2017: revaluation reserve for available-for-sale securities)	
Balance at the end of the period as per IAS 39 (31 December 2017)	240
Reclassification of debt securities from 'available for sale' to 'measured at amortized cost'	1,603
ECL recognized on debt financial assets at FVOCI as per IFRS 9	440
Balance at the beginning of the period as per IFRS 9 (1 January 2018)	2,283
Retained earnings	
Balance at the end of the period as per IAS 39 (31 December 2017)	66,788
Revaluation on reclassification of debt securities from 'available for sale' to 'measured at amortized cost'	46
ECL recognized under IFRS 9, including on instruments at FVOCI	(28,949)
Balance at the beginning of the period as per IFRS 9 (1 January 2018)	37,885
Total changes in equity following the adoption of IFRS 9	(26,860)

The following table reconciles the allowance for impairment of financial assets and provisions for credit-related commitments, letters of credit and financial guarantees as defined by IAS 39 and IAS 37 as at 31 December 2017 with the allowances for expected credit losses as defined by IFRS 9 as at 1 January 2018.

	<i>31 December 2017 IAS 39 / IAS 37</i>	<i>Revaluation as per IFRS 9</i>	<i>1 January 2018 IFRS 9</i>
Allowance for impairment			
Cash and cash equivalents	–	8	8
Deposits with banks and other financial institutions	34,967	241	35,208
Securities at fair value through other comprehensive income (2017: available-for-sale securities)	–	440	440
Loans to banks	9,153	8,848	18,001
Loans to customers	5,555	18,542	24,097
Other financial assets	1,741	6	1,747
	51,416	28,085	79,501
Credit-related commitments	–	408	408
Letters of credit issued to customers	–	402	402
Financial guarantees	–	54	54
	–	864	864
	51,416	28,949	80,365

IFRS 15 Revenue from Contracts with Customers

IFRS 15, issued in May 2014 and amended in April 2016, establishes a five-step model that will apply to revenue arising from contracts with customers. Under IFRS 15, revenue is recognized at an amount that reflects the expectation of an entity regarding the compensation it would be entitled in exchange for transferring the goods or services to a customer. The standard, however, does not apply to income related to financial instruments or leases, and therefore does not impact most of the Group's income, including interest income, net gains/(losses) from securities, lease income regulated by IFRS 9 *Financial Instruments* and IAS 17 *Leases*. As a result, the Group's income is not affected by the adoption of this standard.

*(Thousands of euros)***4. Significant accounting judgments and estimates****Assumptions and estimation uncertainty**

In the process of applying the Group'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 interim condensed consolidated financial statements, which influence the amounts recognized in the interim condensed consolidated financial statements and the carrying amounts 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 considered as reasonable under the circumstances.

Assumptions and estimates adopted by management of the Group in the process of applying the accounting policies are consistent with those described in the consolidated financial statements for the year ended 31 December 2017.

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

- ▶ Note 7 – Derivative financial instruments;
- ▶ Note 8 – Available-for-sale securities;
- ▶ Note 10 – Loans to banks;
- ▶ Note 11 – Loans to customers;
- ▶ Note 18 – Commitments and contingencies.

Reclassification of comparative information

The Group changed the presentation of line items in the interim consolidated income statement and interim consolidated statement of cash flows for the six months ended 30 June 2017. The following adjustments were made to the data for 2017 in order to be consistent with the presentation of the data for 2018:

	<i>As previously reported</i>	<i>Reclassification amount</i>	<i>As reclassified</i>
Item of the interim consolidated income statement			
Net losses from revaluation of derivative financial instruments	(4,591)	4,591	–
Net gains from revaluation of hedging instruments	65	(65)	–
Net gains from dealing in foreign currencies and operations with derivatives	12,520	(12,520)	–
Net losses from revaluation of assets and liabilities in foreign currencies	(944)	944	–
Net gains from dealing in foreign currencies and operations with derivatives	–	(841)	(841)
Other interest income	–	8,697	8,697
Other interest expenses	–	(806)	(806)
Item of the interim consolidated statement of cash flows			
Interest, fees and commissions received	11,641	10,620	22,261
Interest, fees and commissions paid	(2,097)	(3,955)	(6,052)
Realized gains less losses from dealing in foreign currencies and operations with derivatives	13,051	(6,665)	6,386

*(Thousands of euros)***5. Cash and cash equivalents**

Cash and cash equivalents comprise:

	<i>30 June 2018</i> <i>(unaudited)</i>	<i>31 December</i> <i>2017</i>
Cash on hand	364	85
Nostro accounts with banks and other financial institutions		
<i>Credit rating from A- to A+</i>	40,639	49,120
<i>Credit rating from BBB- to BBB+</i>	4,126	4,167
<i>Credit rating from BB- to BB+</i>	370	274
Total nostro accounts with banks and other financial institutions	45,135	53,561
Short-term deposits with banks		
Term deposits with banks		
<i>Credit rating from A- to A+</i>	11,248	–
<i>Credit rating from BBB- to BBB+</i>	478	68
<i>Credit rating from BB- to BB+</i>	–	12,383
Total short-term deposits with banks	11,726	12,451
Less: allowance for impairment	(1)	–
Cash and cash equivalents	57,225	66,097

Cash and cash equivalents are neither impaired nor past due.

All balances of cash equivalents are included in Stage 1. The movements in the allowance for ECL for the six months ended 30 June 2018 were as follows:

Allowance for ECL at 1 January 2018	8
New purchased or originated assets	53
Assets derecognized or redeemed	(60)
Allowance for ECL at 30 June 2018 (unaudited)	1

6. Deposits with banks and other financial institutions

Deposits with banks and other financial institutions are presented based on contractual terms and include the following items:

	<i>30 June 2018</i> <i>(unaudited)</i>	<i>31 December</i> <i>2017</i>
Term deposits up to 1 year		
<i>Credit rating from B- to B+</i>	–	37,157
Total term deposits up to 1 year	–	37,157
Term deposits over 1 year		
<i>Credit rating from A- to A+</i>	22,090	5,650
<i>Credit rating from BBB- to BBB+</i>	9,046	–
<i>Credit rating from BB- to BB+</i>	3,160	3,082
Total term deposits over 1 year	34,296	8,732
Less: allowance for impairment	–	–
Total deposits with banks and other financial institutions	34,296	45,889

*(Thousands of euros)***6. Deposits with banks and other financial institutions (continued)**

All balances of deposits with banks and other financial institutions are included in Stage 1. The movements in the allowance for ECL for the six months ended 30 June 2018 were as follows:

Allowance for ECL at 1 January 2018	241
New purchased or originated assets	–
Assets derecognized or redeemed	(241)
Allowance for ECL at 30 June 2018 (unaudited)	–

As at 30 June 2018, EUR 34,967 thousand (31 December 2017: EUR 34,967 thousand) were due to the Group from the Central Bank of Cuba. This amount was 100% provisioned (31 December 2017: 100%).

Concentration of deposits with banks and other financial institutions

As at 30 June 2018, besides the deposits with the Central Bank of Cuba, the Group had three counterparties (31 December 2017: three counterparties) accounting for over 10% of the Group's total deposits with banks and other financial institutions. As at 30 June 2018, these deposits amounts to EUR 27,326 thousand (31 December 2017: EUR 25,724 thousand) and were not provisioned for (31 December 2017: the deposits were not provisioned).

7. Derivative financial instruments

The Group performs operations with currency and other derivative financial instruments which are generally traded in an over-the-counter market with professional market counterparties on standardized contractual terms and conditions. Derivative financial instruments have either potentially favorable terms (and are assets) or potentially unfavorable conditions (and are liabilities) as a result of fluctuations in exchange rates or other variable factors associated with these instruments. The fair value of derivative financial instruments can vary significantly depending on the potentially favorable and unfavorable conditions.

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*(Thousands of euros)***7. Derivative financial instruments (continued)**

The table below shows the fair value of derivative financial instruments as at 30 June 2018 and 31 December 2017 and notional amounts of term contracts for the purchase and sale of foreign currency specifying weighted average contractual exchange rates.

	30 June 2018 (unaudited)				
	Notional amount		Weighted average exchange rate	Fair value	
	Purchase	Sale		Assets	Liabilities
Derivative financial assets and liabilities at fair value through profit or loss					
Swaps	RUB 12,347,998 thousand	EUR 190,629 thousand	64.98	49	17,358
	RON 319,800 thousand	EUR 70,544 thousand	4.53	349	1,107
	EUR 166,500 thousand	USD 202,387 thousand	1.22	–	8,139
	EUR 15,139 thousand	HUF 4,760,000 thousand	314.42	643	5
	HUF 5,570,000 thousand	EUR 17,258 thousand	322.80	–	314
	CZK 750,000 thousand	EUR 29,503 thousand	25.42	306	–
	RUB 3,000,000 thousand	USD 52,910 thousand	56.70	–	3,286
Forwards	EUR 34,000 thousand	USD 42,040 thousand	1.24	–	2,317
Total derivative financial assets and liabilities at fair value through profit or loss				1,347	32,526
Derivative financial assets and liabilities designated as hedging instruments					
Swaps	RON 298,300 thousand	EUR 67,068 thousand	4.45	–	4,044
Total derivative financial assets and liabilities designated as hedging instruments				–	4,044
Derivative financial instruments				1,347	36,570

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*(Thousands of euros)***7. Derivative financial instruments (continued)**

	31 December 2017				
	Notional amount		Weighted average exchange rate	Fair value	
	Purchase	Sale		Assets	Liabilities
Derivative financial assets and liabilities at fair value through profit or loss					
Swaps	EUR 180,000 thousand	USD 209,572 thousand	1.16	5,203	89
	EUR 10,270 thousand	HUF 3,160,000 thousand	307.69	54	–
	RUB 9,997,998 thousand	EUR 158,232 thousand	63.20	–	8,603
	RUB 3,000,000 thousand	USD 52,910 thousand	56.70	638	–
	RON 319,800 thousand	EUR 70,544 thousand	4.53	931	1,212
Forwards	EUR 34,000 thousand	USD 39,527 thousand	1.16	935	–
Total derivative financial assets and liabilities at fair value through profit or loss				7,761	9,904
Derivative financial assets and liabilities designated as hedging instruments					
Swaps	RON 298,300 thousand	EUR 67,068 thousand	4.45	–	5,169
Total derivative financial assets and liabilities designated as hedging instruments				–	5,169
Derivative financial instruments				7,761	15,073

Following the issue of bonds denominated in currencies other than the Group's functional currency (Note 16), the Group entered into cross currency interest rate swaps and currency forwards on an arm's length basis with large international and Russian credit institutions. These swaps are used to manage long-term currency risks of the Group. Payment netting is not applied to the parties' obligations in respect of interest and principal payments.

The Group applies fair value hedge accounting for the RON-denominated bond issue placed on 27 September 2016 (Note 16).

The notional amount, stated at gross value, 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 end of the reporting period and are not an indication of the credit risk.

As at 30 June 2018 and 31 December 2017, the Group has positions in the following types of derivatives:

Forwards: Forward contracts are contractual agreements to buy or sell a specified financial instrument at a specific price and date in the future. Forwards are customized contracts transacted in the over-the-counter market.

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.

Fair value measurement is based on the corresponding forward curves that depend on exchange rates, interest rates and swap contract maturity. For the fair value of swaps, the discount rate was calculated on the basis of zero coupon yield curve and credit risk. Changes in the fair value of swaps were mainly due to the increase in the forward exchange rates of the euro to transaction currencies.

(Thousands of euros)

8. Securities at fair value through other comprehensive income

Securities at fair value through other comprehensive income comprise:

	<i>30 June 2018</i> <i>(unaudited)</i>	<i>31 December</i> <i>2017</i>
<i>Owned by the Bank</i>		
Quoted debt securities at fair value through other comprehensive income		
Government bonds of non-member countries		
<i>Credit rating AAA</i>	–	4,066
<i>Credit rating from AA- to AA+</i>	11,398	–
<i>Credit rating AA+</i>	–	5,396
<i>Credit rating from A- to A+</i>	3,790	–
<i>Credit rating B-</i>	18,168	18,552
Government bonds	33,356	28,014
Corporate bonds		
<i>Credit rating AAA</i>	17,434	–
<i>Credit rating from AA- to AA+</i>	3,441	–
<i>Credit rating from A- to A+</i>	30,103	12,292
<i>Credit rating from BBB- to BBB+</i>	30,489	20,370
<i>Credit rating from BB- to BB+</i>	59,478	62,496
<i>Credit rating from B- to B+</i>	–	13,817
Corporate bonds	140,945	108,975
Total quoted debt securities at fair value through other comprehensive income	174,301	136,989
Quoted equity instruments at fair value through other comprehensive income		
Corporate shares:		
<i>Credit rating A-</i>	–	633
<i>Credit rating BBB</i>	–	1,077
<i>No credit rating</i>	5	5
Corporate shares	5	1,715
Investments in equity instruments:		
<i>Investments in the Fund</i>	502	–
Investments in equity instruments	502	–
Total quoted equity instruments at fair value through other comprehensive income	507	1,715
Securities at fair value through other comprehensive income	174,808	138,704
<i>Pledged under repurchase agreements</i>		
Quoted debt securities at fair value through other comprehensive income		
Government bonds:		
Government bonds of member countries		
<i>Credit rating A+</i>	1,144	10,010
Government bonds of non-member countries		
<i>Credit rating A-</i>	7,676	7,867
Government bonds	8,820	17,877
Corporate bonds:		
<i>Credit rating AAA</i>	–	19,991
<i>Credit rating from AA- to AA+</i>	–	7,466
<i>Credit rating from A- to A+</i>	10,218	18,544
<i>Credit rating from BBB- to BBB+</i>	–	5,995
<i>Credit rating from BB- to BB+</i>	–	6,850
Corporate bonds	10,218	58,846
Total quoted debt securities at fair value through other comprehensive income pledged under repurchase agreements	19,038	76,723

(Thousands of euros)

8. Securities at fair value through other comprehensive income (continued)

All securities at fair value through other comprehensive income are included in Stage 1. The movements in the allowance for ECL for the six months ended 30 June 2018 were as follows:

Allowance for ECL at 1 January 2018	440
New purchased or originated assets	65
Assets derecognized or redeemed	(199)
Allowance for ECL at 30 June 2018 (unaudited)	306

Government bonds comprise EUR- and USD-denominated securities issued and guaranteed by the Ministries of Finance of these countries. The bonds mature in 2023-2027 (31 December 2017: 2020-2027). The coupon rate for these bonds varies from 0.4% to 7.6% (31 December 2017: from 0.4% to 7.6%).

Corporate bonds comprise bonds issued by large companies and banks of the member countries of the Bank, as well as international companies and development banks with goals and missions similar to those of the Group. The bonds mature in 2020-2028 (31 December 2017: 2020-2026). The coupon rate for these bonds varies from 0.1% to 7.8% (31 December 2017: from 0.4% to 7.9%).

Equity securities comprise shares issued by a major international company.

Investments in the Fund comprise investments in the Central Europe Fund of Funds (CEFoF, or the "Fund") established by the European Investment Fund (EIF), a member of the European Investment Bank (EIB), together with governments and national development banks of five countries, including the Republic of Austria, Hungary, the Slovak Republic, Slovenia and the Czech Republic. The Fund is primarily engaged in stimulating equity investments in SMEs and creating market infrastructure that would promote such investments, as well as attracting institutional investors and investment managers to the Central Europe.

9. Securities at amortized cost

As at 1 January 2018, the Group reclassified a part of its securities previously classified as 'available for sale' to 'debt instruments measured at amortized cost'. These instruments satisfy the SPPI criterion and are held to collect related cash flows rather than for sale.

	<i>30 June 2018</i> <i>(unaudited)</i>	<i>31 December</i> <i>2017</i>
Owned by the Bank		
Quoted debt securities at amortized cost		
Corporate bonds:		
<i>Credit rating AAA</i>	13,395	–
<i>Credit rating AA</i>	888	–
<i>Credit rating BBB-</i>	15,100	–
Corporate bonds	29,383	–
Total quoted debt securities at amortized cost	29,383	–
Pledged under repurchase agreements		
Quoted debt securities at amortized cost		
Corporate bonds:		
<i>Credit rating AAA</i>	8,487	–
<i>Credit rating AA</i>	3,552	–
Corporate bonds	12,039	–
Total quoted debt securities at amortized cost pledged under repurchase agreements	12,039	–

Corporate bonds comprise investment grade bonds issued by large companies and banks of the member countries of the Bank, as well as international companies and development banks with goals and missions similar to those of the Group. The bonds mature in 2021-2026 (31 December 2017: none). The coupon rate for these bonds varies from 1.8% to 2.1% (31 December 2017: none). No allowances for ECL were made.

*(Thousands of euros)***10. Loans to banks**

During 2018, the Group continued its lending activities, in accordance with the key priorities of the IIB Development Strategy. The principal lending activity is to participate in financing of socially important infrastructure projects in the member countries and to facilitate the development of small and medium-sized businesses in these countries. The Group considers national development institutes, export and import banks and agencies, international financial organizations and development banks as its key counterparties.

During the six months ended 30 June 2018 and in 2017, the Group provided trade financing loans and long-term loans to borrowers operating in the following countries:

	<i>30 June 2018</i> <i>(unaudited)</i>	<i>31 December</i> <i>2017</i>
Trade financing loans		
Republic of Belarus	34,866	3,239
Russian Federation	–	23,298
Trade financing loans	34,866	26,537
Long-term loans to banks		
Mongolia	56,470	33,735
Republic of Cuba	49,909	49,863
Socialist Republic of Vietnam	25,309	25,252
Russian Federation	14,377	75,401
Long-term loans to banks	146,065	184,251
Less: allowance for impairment of loans to banks	(16,815)	(9,153)
Total loans to banks	164,116	201,635

Changes in the allowances for ECL for the six months ended 30 June 2018 are presented in the table below:

<i>Trade financing loans</i>	<i>Stage 1</i>	<i>Stage 2</i>	<i>Stage 3</i>	<i>Total</i>
Allowance for ECL at 1 January 2018	114	–	–	114
New purchased or originated assets	586	–	–	586
Assets derecognized or redeemed (excluding write-offs)	(349)	–	–	(349)
Transfers to Stage 1	–	–	–	–
Transfers to Stage 2	–	–	–	–
Transfers to Stage 3	–	–	–	–
Effect on ECL at the year-end due to transfers between stages during the year	–	–	–	–
Amounts written off (against the allowance)	–	–	–	–
Translation differences	–	–	–	–
At 30 June 2018 (unaudited)	351	–	–	351
Long-term loans to banks	Stage 1	Stage 2	Stage 3	Total
Allowance for ECL at 1 January 2018	2,633	–	15,254	17,887
New purchased or originated assets	593	–	–	593
Assets derecognized or redeemed (excluding write-offs)	(789)	–	–	(789)
Transfers to Stage 1	–	–	–	–
Transfers to Stage 2	(350)	350	–	–
Transfers to Stage 3	–	–	–	–
Effect on ECL at the year-end due to transfers between stages during the year	–	1,486	–	1,486
Amounts written off (against the allowance)	–	(1,836)	–	(1,836)
Translation differences	–	–	(877)	(877)
At 30 June 2018 (unaudited)	2,087	–	14,377	16,464

*(Thousands of euros)***10. Loans to banks (continued)**

The information on overdue loans as at 30 June 2018 and 31 December 2017 is provided below:

	<i>30 June 2018</i> <i>(unaudited)</i>	<i>31 December</i> <i>2017</i>
Total loans with overdue principal and/or interest	14,377	15,254
Less: allowance for impairment of loans to banks	<u>(14,377)</u>	<u>(9,153)</u>
Overdue loans to banks	<u><u>–</u></u>	<u><u>6,101</u></u>

For the purpose of these interim condensed consolidated financial statements, a loan to a bank is considered overdue if at least one of the loan-related payments is past due at the reporting date. In this case, the amount of the overdue loan is the total amount due from the borrower, including the accrued interest income.

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*(Thousands of euros)***10. Loans to banks (continued)****Allowance for impairment of loans to banks**

A reconciliation of the allowance for impairment of loans to banks by country is as follows:

	<i>Russian Federation</i>	<i>Mongolia</i>	<i>Socialist Republic of Vietnam</i>	<i>Republic of Cuba</i>	<i>Other</i>	<i>Total</i>
At 31 December 2017	9,153	–	–	–	–	9,153
Impact of adopting IFRS 9	6,705	1,295	291	539	18	8,848
At 1 January 2018	15,858	1,295	291	539	18	18,001
Net (reversal)/charge for the period	(604)	(30)	(14)	5	2,170	1,527
Write off against previously accrued allowance	–	–	–	–	(1,836)	(1,836)
Change in allowance resulting from changes in exchange rates	(877)	–	–	–	–	(877)
At 30 June 2018 (unaudited)	14,377	1,265	277	544	352	16,815
Individual impairment	14,377	–	–	–	–	14,377
Gross amount of loans to banks individually determined to be impaired, before deducting any individually assessed impairment allowance	14,377	–	–	–	–	14,377
					<i>Russian Federation</i>	<i>Total</i>
At 1 January 2017					–	–
Net charge for the period					774	774
At 30 June 2017 (unaudited)					774	774
Individual impairment					774	774
Gross amount of loans to banks individually determined to be impaired, before deducting any individually assessed impairment allowance					–	–

*(Thousands of euros)***10. Loans to banks (continued)****Analysis of collateral for loans to banks**

The following table provides an analysis of the portfolio of trade financing loans and long-term loans to banks by type of collateral as at 30 June 2018 and 31 December 2017:

	30 June 2018 <i>(unaudited)</i>		31 December 2017	
	<i>Loans to banks net of allowance for impairment</i>	<i>Share in the total loans, %</i>	<i>Loans to banks net of allowance for impairment</i>	<i>Share in the total loans, %</i>
State guarantees	49,366	30.1	49,863	24.7
Uncollateralized part of the loans	114,750	69.9	151,772	75.3
Total loans to banks	164,116	100	201,635	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 30 June 2018, long-term loans and trade financing loans to five banks (31 December 2017: two banks) with a total amount of loans to each of them exceeding 10% of total loans to banks were recorded on the Group's balance sheet. As at 30 June 2018, the total amount of such major loans was EUR 132,496 thousand (31 December 2017: EUR 70,100 thousand) and allowances of EUR 1,577 thousand (31 December 2017: nil) were made for them.

11. Loans to customers

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

	30 June 2018 <i>(unaudited)</i>	31 December 2017
Republic of Bulgaria	116,712	57,995
Russian Federation	101,950	81,817
Slovak Republic	89,923	60,464
Romania	85,440	78,440
Czech Republic	50,053	49,967
Republic of Ecuador	33,066	34,763
Hungary	29,808	42,910
Republic of Panama	29,605	29,775
Mongolia	24,277	24,425
Kingdom of the Netherlands	5,693	5,847
United States of America	1,625	1,666
Gross loans to customers	568,152	468,069
Less: allowance for impairment of loans to customers	(22,525)	(5,555)
Loans to customers	545,627	462,514

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*(Thousands of euros)***11. Loans to customers (continued)**

Changes in the allowances for ECL for the six months ended 30 June 2018 are presented in the table below:

<i>Loans to customers</i>	<i>Stage 1</i>	<i>Stage 2</i>	<i>Stage 3</i>	<i>Total</i>
Allowance for ECL at				
1 January 2018	5,336	3,610	15,151	24,097
New purchased or originated assets	1,119	6	–	1,125
Assets derecognized or redeemed (excluding write-offs)	(4,014)	–	–	(4,014)
Transfers to Stage 1	–	–	–	–
Transfers to Stage 2	–	–	–	–
Transfers to Stage 3	–	–	–	–
Effect on ECL at the year-end due to transfers between stages during the year	–	–	–	–
Changes to models and inputs used for ECL calculations	–	1,317	–	1,317
Amounts written off (against the allowance)	–	–	–	–
Translation differences	–	–	–	–
At 30 June 2018 (unaudited)	2,441	4,933	15,151	22,525

A summary of overdue loans as at 30 June 2018 and 31 December 2017 is presented below:

	<i>30 June 2018 (unaudited)</i>	<i>31 December 2017</i>
Total loans with overdue principal and/or interest	15,151	15,151
Less: allowance for loan impairment	(15,151)	(5,255)
Overdue loans to customers	–	9,896

For the purposes of these interim condensed consolidated financial statements, a loan to a customer is considered overdue if at least one of the loan-related payments is past due at the reporting date. In this case, the amount of the overdue loan is the total amount due from the borrower, including the accrued interest income.

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

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

	<i>Russian Federation</i>	<i>Republic of Bulgaria</i>	<i>Romania</i>	<i>Slovak Republic</i>	<i>Hungary</i>	<i>Mongolia</i>	<i>Other</i>	<i>Total</i>
At 31 December 2017	–	300	5,255	–	–	–	–	5,555
Impact of adopting IFRS 9	64	3,752	10,261	454	3,333	370	308	18,542
At 1 January 2018	64	4,052	15,516	454	3,333	370	308	24,097
Net (reversal)/charge for the period	23	1,407	154	53	(3,040)	(21)	(148)	(1,572)
At 30 June 2018 (unaudited)	87	5,459	15,670	507	293	349	160	22,525
Individual impairment	–	–	15,151	–	–	–	–	15,151
Gross amount of loans to customers individually determined to be impaired, before deducting any individually assessed impairment allowance	–	–	15,151	–	–	–	–	15,151
						<i>Republic of Bulgaria</i>	<i>Romania</i>	<i>Total</i>
At 1 January 2017				8,103	6,955	2,254	17,312	
Net charge for the period				–	6	3,001	3,007	
Write off against previously accrued allowance				(8,103)	(6,666)	–	(14,769)	
At 30 June 2017 (unaudited)				–	295	5,255	5,550	
Individual impairment				–	–	5,255	5,255	
Gross amount of loans to customers, individually determined to be impaired, before deducting any individually assessed impairment allowance				–	–	15,151	15,151	

*(Thousands of euros)***11. Loans to customers (continued)****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 30 June 2018 and 31 December 2017:

	<i>30 June 2018</i> <i>(unaudited)</i>		<i>31 December</i> <i>2017</i>	
	<i>Loans to customers net of allowance for impairment</i>	<i>Share in the total loans, %</i>	<i>Loans to customers net of allowance for impairment</i>	<i>Share in the total loans %</i>
Pledge of real property (mortgage) and title	103,093	18.9	86,728	18.8
Corporate guarantees	98,393	18.0	70,599	15.3
Pledge of shares	96,507	17.7	42,504	9.2
State guarantees	62,535	11.5	74,476	16.1
Pledge of equipment and goods in turnover	15,115	2.8	15,292	3.3
Pledge of vehicles	9,830	1.8	1,476	0.3
Pledge of rights of claim	5,327	1.0	6,150	1.3
Uncollateralized part of the loans	154,827	28.3	165,289	35.7
Total loans to customers	545,627	100.0	462,514	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.

Concentration of loans to customers

As at 30 June 2018, loans to two borrowers (31 December 2017: three borrowers) with the total amount of loans to each of the two borrowers exceeding 10% of total loans to customers were recorded on the Group's balance sheet. As at 30 June 2018, these loans comprised EUR 164,368 thousand (31 December 2017: EUR 181,256 thousand) in total and impairment allowances of EUR 249 thousand (31 December 2017: nil) were made for them.

Analysis of loans to customers by industry

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

	<i>30 June 2018</i> <i>(unaudited)</i>	<i>31 December</i> <i>2017</i>
Production and transmission of electricity	149,597	104,847
Leasing	128,724	116,910
Metal working industry	50,053	49,967
Communications	49,897	22,815
Crude oil refining	30,097	30,099
Advisory services	29,431	19,543
Food and beverage	22,736	25,662
Mining	21,430	20,632
Manufacturing of electrical equipment	21,297	21,159
Real estate	19,267	19,722
Production of pharmaceutical products	13,182	11,319
Agriculture	11,970	13,408
Transport	10,757	11,248
Oil and gas production	9,714	–
Trading	–	738
	568,152	468,069
Less: allowance for impairment of loans to customers	(22,525)	(5,555)
Loans to customers	545,627	462,514

*(Thousands of euros)***12. Other assets and liabilities**

Other assets comprise:

	<i>30 June 2018</i> <i>(unaudited)</i>	<i>31 December</i> <i>2017</i>
Financial assets		
Settlements on bank transactions	2,006	2,007
Guarantee payments	25	26
Accounts receivable on business operations	40	73
Other financial assets	296	363
	2,367	2,469
Less: allowance for impairment of other financial assets	(1,657)	(1,741)
Total financial assets	710	728
Non-financial assets		
Advances issued	1,080	990
Assets held for sale – real estate	89	89
Inventories – real estate	–	50
Other non-financial assets	967	619
Total non-financial assets	2,136	1,748
Total other assets	2,846	2,476

The changes in the in allowance for impairment of other financial assets are as follows:

	<i>30 June 2018</i> <i>(unaudited)</i>	<i>31 December</i> <i>2017</i>
Allowance in accordance with IFRS 39	1,741	1,924
Impact of adopting IFRS 9	(6)	–
Allowance at 1 January	1,735	1,924
New purchased or originated assets	13	–
Assets derecognized or redeemed	(15)	(29)
Change in allowance resulting from changes in exchange rates	(76)	(154)
Allowance at the end of the period	1,657	1,741

Other liabilities comprise:

	<i>30 June 2018</i> <i>(unaudited)</i>	<i>31 December</i> <i>2017</i>
Financial liabilities		
Other accounts payable on business operations	929	1,015
Other accounts payable on bank transactions	880	1,125
Other financial liabilities	–	8
Total financial liabilities	1,809	2,148
Non-financial liabilities		
Settlements with employees	4,173	4,070
Allowances for expected credit losses on credit-related commitments	1,231	–
Other non-financial liabilities	342	178
Total non-financial liabilities	5,746	4,248
Total other liabilities	7,555	6,396

*(Thousands of euros)***13. Allowances for credit losses, other impairment losses and provisions**

The table below shows the allowances for ECL on financial instruments recorded in profit or loss for the six months ended 30 June 2018:

	<i>Note</i>	<i>Stage 1</i>	<i>Stage 2</i>	<i>Stage 3</i>	<i>Total</i>
Cash and cash equivalents	5	(7)	–	–	(7)
Deposits with banks and other financial institutions	6	(241)	–	–	(241)
Securities at fair value through other comprehensive income	8	(134)	–	–	(134)
Securities at amortized cost	9	–	–	–	–
Loans to banks	10	(309)	1,836	–	1,527
Loans to customers	11	(2,895)	1,323	–	(1,572)
Other financial assets	12	(2)	–	–	(2)
Other non-financial liabilities (credit-related commitments)	12, 18	368	(1)	–	367
Total (income)/loss on impairment		(3,220)	3,158	–	(62)

The changes in the allowance for ECL on financial instruments for the six months ended 30 June 2018 were as follows:

	<i>Stage 1</i>	<i>Stage 2</i>	<i>Stage 3</i>	<i>Total</i>
Allowance for ECL at 1 January 2018	9,574	3,678	67,000	80,252
New purchased or originated assets	3,811	6	–	3,817
Assets derecognized or redeemed (excluding write-offs)	(6,677)	(1)	–	(6,678)
Transfers to Stage 1	–	–	–	–
Transfers to Stage 2	(350)	350	–	–
Transfers to Stage 3	–	–	–	–
Effect on ECL at the year-end due to transfers between stages during the year	–	1,486	–	1,486
Changes to models and inputs used for ECL calculations	–	1,317	–	1,317
Amounts written off	–	(1,836)	–	(1,836)
Translation differences	–	–	(947)	(947)
At 30 June 2018	6,358	5,000	66,053	77,411

As at 30 June 2018 on the Group's balance sheet there were no other allowances except for those mentioned above.

14. Due to banks and other financial institutions

Due to banks and other financial institutions are presented based on contractual terms and include the following items:

	<i>30 June 2018 (unaudited)</i>	<i>31 December 2017</i>
Due to banks up to 1 year		
Term deposits of banks and other financial institutions	59,771	3,496
Total due to banks up to 1 year	59,771	3,496
Due to banks over 1 year		
Repurchase agreements	25,170	62,015
Total due to banks over 1 year	25,170	62,015
Total due to banks	84,941	65,511

The Group performs daily monitoring of repurchase agreements and the value of collateral when placing/returning additional collateral, if necessary.

*(Thousands of euros)***14. Due to banks and other financial institutions (continued)****Concentration of amounts due to banks and other financial institutions**

As at 30 June 2018, the Group has three counterparties (31 December 2017: two counterparties) accounting for over 10% of the Group's total amounts due to banks and other financial institutions. Resources raised from these counterparties amounted to EUR 75,062 thousand (31 December 2017: EUR 62,015 thousand).

15. Long-term loans of banks

Long-term loans of banks comprise:

	<i>30 June 2018</i> <i>(unaudited)</i>	<i>31 December</i> <i>2017</i>
Loans of banks	23,133	12,898
SSD	22,944	22,939
Syndicated loans	–	59,755
Total long-term loans of banks	46,077	95,592

On 19 March 2018, the Group received the first tranche from the BRICS New Development Bank in the amount of USD 12.5 million (EUR 10,237 thousand) under the loan agreement of USD 50 million.

In 2017, the Group issued SSD debentures (Schuldscheindarlehen) in the Western European market in the total amount of EUR 23,000 thousand.

On 3 August 2017, the Group raised bilateral financing in the Hungarian financial market in the amount of HUF 4.0 billion (EUR 13,185 thousand).

16. Debt securities issued

Debt securities issued comprise:

	<i>Interest rate,</i> <i>% p.a.</i>	<i>Maturity</i>	<i>30 June 2018</i> <i>(unaudited)</i>	<i>31 December</i> <i>2017</i>
RUB-denominated bonds	0.01-9.5	2024-2027	306,942	267,112
RON-denominated bonds	3.4-4.5	2018-2020	154,783	152,084
EUR-denominated bonds	1.59-3.5	2019-2020	91,092	90,017
CZK-denominated bonds	1.5	2021	28,936	–
Total bonds			581,753	509,213

On 26 April 2018, the Group placed bonds on the Czech market in the amount of CZK 501.1 million (EUR 19,832 thousand) maturing in three years. The interest rate on bonds was set at 3m Pribor + 0.55% p.a.

On 30 May 2018, the Group made a secondary placement of RUB-denominated bonds, series 03, in the amount of RUB 3.99 billion (EUR 55,120 thousand) that had been repurchased in 2017 under the offer. A new coupon rate of 7.6% p.a. was set, with an offer planned for November 2018.

The Group redeemed RUB-denominated bonds, series 03, worth a total of RUB 3.99 billion (EUR 62,858 thousand) on 2 June 2017, as scheduled under the offer. A new coupon rate of 0.01% was set for the remaining bonds of this issue.

On 04 June 2018, the Group additionally placed bonds on the Czech market in the amount of CZK 249.7 million (EUR 9,675 thousand) maturing in three years. The interest rate on bonds was set at 3m Pribor + 0.50% p.a.

(Thousands of euros)

16. Debt securities issued (continued)

On 14 June 2017, the Group placed an issue of exchange-traded bonds at the Moscow Exchange under the Program to issue exchange-traded bonds registered in 2016. The issue totaled RUB 10 billion (EUR 156,579 thousand) and provides for an offer in March 2020. The coupon rate on the bonds was set at 8.75% payable on a quarterly basis with the first coupon payment to be made on 11 September 2017.

The Group placed a third issue of bonds in the Romanian stock market on 25 September 2017. The issue comprises two tranches of EUR 60 million and RON 300 million (EUR 65,199 thousand) maturing in three years. EUR-denominated bonds and RON-denominated bonds bear interest rates of 1.593% p.a. and 3m Robor + 1.50%, respectively.

The Group partially redeemed RUB-denominated bonds, series 01, worth a total of RUB 489,432 thousand (EUR 7,259 thousand) on 27 October 2017, as scheduled under the offer. A new coupon rate of 0.01% was set for the remaining bonds of this issue.

The Group redeemed and made a secondary placement of bonds, series 04, worth RUB 1.2 billion (EUR 18,271 thousand) on 21 November 2017, as scheduled under the offer. A new coupon rate of 8.15% was set.

At the dates of placement of bonds, the Group entered into cross-currency interest rate swaps for the purpose of managing currency risks (Note 7) and exchanging interest expense from debt securities issued, denominated in RUB, RON, to the currency required by the Group (EUR, USD) to finance credit projects in the required currency. The Group applies hedge accounting for the fair value of the bond issue in Romanian lei placed on 27 September 2016. The effects of using cross-currency interest rate swaps and fair value hedge operations are disclosed in Note 20.

The Group primarily used the proceeds from issuance of debt instruments and placement of bonds to expand its loan portfolio.

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 30 June 2018, the unpaid portion of the Bank's subscribed capital in the amount of EUR 985,038 thousand (31 December 2017: EUR 985,038 thousand) is the amount of contributions that have not been made yet by the Bank's member countries and the amount of unallocated equity contributions totaling EUR 175,500 thousand (31 December 2017: EUR 175,500 thousand).

The Government of Mongolia made an additional contribution of EUR 1,909 thousand to the Bank's equity on 27 December 2017.

The paid-in capital of the International Investment Bank totaled EUR 314,962 thousand (31 December 2017: EUR 314,962 thousand).

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*(Thousands of euros)***17. Equity (continued)****Revaluation reserve for securities at fair value through other comprehensive income and revaluation reserve for property and equipment**

The changes in the revaluation reserve for securities at fair value through other comprehensive income and revaluation reserve for property and equipment were as follows:

	<i>Revaluation reserve for securities at fair value through other comprehensive income</i>	<i>Revaluation reserve for property and equipment</i>
At 1 January 2017	(1,506)	12,945
Net unrealized gains on available-for-sale securities	4,824	–
Realized gains on available-for-sale securities reclassified to the income statement	(4,553)	–
At 30 June 2017 (unaudited)	(1,235)	12,945
At 31 December 2017	240	13,748
Impact of adopting IFRS 9	2,043	–
At 1 January 2018	2,283	13,748
Net unrealized gains on securities at fair value through other comprehensive income	(4,542)	–
Change in the allowance for expected credit losses related to securities through other comprehensive income	306	–
Realized gains on securities at fair value through other comprehensive income, reclassified to the income statement	(2,238)	–
Losses from revaluation of equity securities at fair value through other comprehensive income	(48)	–
At 30 June 2018 (unaudited)	(4,239)	13,748

Revaluation reserve for securities at fair value through other comprehensive income

The revaluation reserve for securities at fair value through other comprehensive income 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.

18. Commitments and contingencies**Legal**

In the ordinary course of business, the Group 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 Group. 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 Group 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 Group's further actions to collect bad debt and/or realize respective repossession rights is higher than the amount collected and also when the Group 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.

*(Thousands of euros)***18. Commitments and contingencies (continued)****Insurance**

The Group 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 Group did not obtain insurance coverage related to temporarily discontinued operations or the Group's obligations to third parties.

Taxation

The IIB is an international institution operating on the basis of the Intergovernmental Agreement on the Establishment of the International Investment Bank (the "Agreement") and the Statute that constitutes an integral part of the Agreement. Pursuant to the Agreement, the Bank is exempt from any national or local direct taxes or duties effective in the territories of its member states. For taxation purposes, its subsidiaries are subject to the provisions of the effective Russian tax, currency and customs legislation.

Credit-related commitments

At any time, the Group may have outstanding commitments to extend loans. These commitments take the form of approved loan agreements. As at 30 June 2018, credit-related commitments of the Group comprised off-balance credit-related commitments, in particular undrawn loan facilities, guarantees and reimbursement obligations. The primary purpose of credit-related commitments is to ensure that funds are available to customers as required. Guarantees issued, which represent irrevocable assurances that the Group will make payments in the event that a customer cannot meet its obligations to third parties, carry the same credit risk as loans. Reimbursement obligations, which are irrevocable reimbursement obligations of the Group issued on behalf of banks issuing documentary letters of credit that are accepted and paid by foreign partner banks up to a stipulated amount under specific terms and conditions, are collateralized by the underlying shipments of goods to which they relate and therefore carry less risk than a direct borrowing. Undrawn loan facilities represent unused portions of funds to be issued as loans.

Off-balance credit-related commitments are presented in the table below as at 30 June 2018 and 31 December 2017.

	<i>30 June 2018</i> <i>(unaudited)</i>	<i>31 December</i> <i>2017</i>
Undrawn loan facilities	137,722	116,161
Guarantees issued	70,670	15,425
Reimbursement obligations	16,786	32,812
	225,178	164,398
Less: allowance for impairment of the off-balance sheet credit related commitments	(1,231)	–
Total credit-related commitments	223,947	164,398

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*(Thousands of euros)***18. Commitments and contingencies (continued)****Credit-related commitments (continued)**

The table below shows the analysis of changes in the allowances for ECL for the six months ended 30 June 2018:

<i>Guarantees issued</i>	<i>Stage 1</i>	<i>Stage 2</i>	<i>Stage 3</i>	<i>Total</i>
Allowance for ECL at 1 January 2018	54	–	–	54
New purchased or originated assets	849	–	–	849
Assets derecognized or redeemed (excluding write-offs)	(249)	–	–	(249)
Transfers to Stage 1	–	–	–	–
Transfers to Stage 2	–	–	–	–
Transfers to Stage 3	–	–	–	–
Effect on ECL at the year-end due to transfers between stages during the year	–	–	–	–
Amounts written off (against the allowance)	–	–	–	–
Translation differences	–	–	–	–
At 30 June 2018 (unaudited)	654	–	–	654
<i>Undrawn loan facilities</i>	<i>Stage 1</i>	<i>Stage 2</i>	<i>Stage 3</i>	<i>Total</i>
Allowance for ECL at 1 January 2018	340	68	–	408
New purchased or originated assets	253	–	–	253
Assets derecognized or redeemed (except for write-offs)	(328)	(1)	–	(329)
Transfers to Stage 1	–	–	–	–
Transfers to Stage 2	–	–	–	–
Transfers to Stage 3	–	–	–	–
Effect on ECL at the year-end due to transfers between stages during the year	–	–	–	–
Amounts written off (against the allowance)	–	–	–	–
Translation differences	–	–	–	–
At 30 June 2018 (unaudited)	265	67	–	332
<i>Reimbursement obligations</i>	<i>Stage 1</i>	<i>Stage 2</i>	<i>Stage 3</i>	<i>Total</i>
Allowance for ECL at 1 January 2018	402	–	–	402
New purchased or originated assets	272	–	–	272
Assets derecognized or redeemed (except for write-offs)	(429)	–	–	(429)
Transfers to Stage 1	–	–	–	–
Transfers to Stage 2	–	–	–	–
Transfers to Stage 3	–	–	–	–
Effect on ECL at the year-end due to transfers between stages during the year	–	–	–	–
Amounts written off (against the allowance)	–	–	–	–
Translation differences	–	–	–	–
At 30 June 2018 (unaudited)	245	–	–	245

19. Leases**Group as lessor**

The Group provides its investment property for operating leases. As at 30 June 2018, the Group's non-cancellable operating lease rentals amount to EUR 3,744 thousand (31 December 2017: EUR 6,819 thousand) and will be settled during the period from 1 month to 4.4 years (31 December 2017: 1 to 5 years).

*(Thousands of euros)***20. Interest income and interest expenses**

Net interest income comprises:

	<i>30 June 2018</i> <i>(unaudited)</i>	<i>30 June 2017</i> <i>(unaudited)</i>
Interest income		
<i>Interest income calculated using the EIR method</i>		
Loans to customers	12,947	8,313
Loans to banks	4,644	3,077
Securities at fair value through other comprehensive income	2,782	3,120
Deposits with banks and other financial institutions, including cash and cash equivalents	776	1,637
Securities at amortized cost	457	–
Other	3	–
<i>Other interest income</i>		
Cross-currency interest rate swaps to manage long-term currency risks	7,943	8,697
Total interest income	29,552	24,844
Interest expenses		
<i>Interest expenses calculated using the EIR method</i>		
Debt securities issued	(15,492)	(11,932)
Long-term loans of banks	(1,197)	(1,235)
Funds raised under repurchase agreements	(626)	(971)
Current customer accounts	(90)	(120)
Due to banks and other financial institutions	(56)	(103)
Other	(15)	(3)
<i>Other interest expenses</i>		
Cross-currency interest rate swaps to manage long-term currency risks	(908)	(806)
Total interest expense	(18,384)	(15,170)
Net interest income	11,168	9,674

There was no interest income accrued on impaired loans for the six months ended 30 June 2018 (2017: EUR 122 thousand).

21. Net gains from operations in foreign currencies and with derivatives

Gains less losses from operations in foreign currencies and with derivatives comprised:

	<i>30 June 2018</i> <i>(unaudited)</i>	<i>30 June 2017</i> <i>(unaudited)</i>
Derivative financial instruments and operations with foreign currencies		
Net gains from dealing in foreign currencies and operations with derivatives	13,560	12,520
Net losses from revaluation of derivative financial instruments	(28,583)	(4,064)
Total derivative financial instruments and operations with foreign currencies	(15,023)	8,456
Fair value hedge operations		
Net gains/(losses) from revaluation of fair value hedge operations	624	(258)
Net losses from revaluation of hedged object	(834)	(204)
Total fair value hedge operations	(210)	(462)
Translation differences		
Net gains/(losses) from revaluation of assets and liabilities in foreign currencies	13,373	(8,835)
Net losses from operations in foreign currencies and with derivatives	(1,860)	(841)

*(Thousands of euros)***22. General and administrative expenses**

General and administrative expenses comprise:

	<i>30 June 2018</i> <i>(unaudited)</i>	<i>30 June 2017</i> <i>(unaudited)</i>
Employee compensations and employment taxes	6,338	6,544
Depreciation of property, equipment and intangible assets	1,031	1,005
IT-expenses, inventory and occupancy expenses	897	845
Expenses related to business travel, representative and accommodation expenses	275	292
Professional services	148	124
Other	214	251
General and administrative expenses	8,903	9,061

23. Risk management**Risk management framework**

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

The Group's risk management activities are intended to:

- ▶ Identify, analyze and manage risks faced by the Group.
- ▶ 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 professional risk management for the bank transactions.

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

Risk management system

Integrated into the whole vertical organizational structure of the Group and all areas of the Group's activities, the risk management system makes it possible to identify in a timely manner and effectively manage different types of risks.

Risk management involves all of the Group's divisions in the evaluating, assuming, and controlling risks ("Three lines of defense"):

- ▶ Risk-taking (1st line of defense): the Group's divisions directly preparing and conducting transactions, involved in the identification, assessment, and monitoring of risks and comply with internal regulations on risk management, as well as give due consideration to the risk level in the preparation of transactions.
- ▶ Risk management (2nd line of defense): the division responsible for risk management develops risk management tools and methodology, assesses and monitors the risk level, prepares reports on risks, carries out risk aggregation, and calculates the amount of total capital requirements.
- ▶ Internal audit (3rd line of defense): independent quality assessment for existing risk management processes, identification of violations, and proposals for the improvement of the risk management system.

The Group's operations are managed taking into account the level of the risk appetite approved by the Council and its integration into a system of limits and restrictions insuring the acceptable level of risk for aggregated positions, transparent distribution of total risk limit among the activities of the Group.

*(Thousands of euros)***23. Risk management (continued)****Risk management system (continued)**

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

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 customer'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.

The following table provides information on the credit quality of long-term loans to banks and trade financing loans (Note 10) and loans to customers (Note 11) as at 30 June 2018 and 31 December 2017:

<i>30 June 2018 (unaudited)</i>	<i>Loan amount</i>	<i>Allowance for impairment</i>	<i>Loan amount, including allowance for impairment</i>	<i>Impairment to loan amount ratio, %</i>
Trade financing loans				
Standard loans	34,866	(351)	34,515	1.0
Total trade financing loans	34,866	(351)	34,515	1.0
Long-term loans to banks				
Standard loans	131,688	(2,087)	129,601	1.6
Loans more than 90 days past due	14,377	(14,377)	–	100.0
Total long-term loans to banks	146,065	(16,464)	129,601	11.3
Loans to customers				
Standard loans	546,856	(2,765)	544,091	0.5
Restructured loans	6,145	(4,609)	1,536	75.0
Loans more than 90 days past due	15,151	(15,151)	–	100.0
Total loans to customers	568,152	(22,525)	545,627	4.0
Total loans	749,083	(39,340)	709,743	5.3

*(Thousands of euros)***23. Risk management (continued)****Credit risk (continued)**

<i>31 December 2017</i>	<i>Loan amount</i>	<i>Allowance for impairment</i>	<i>Loan amount, including allowance for impairment</i>	<i>Impairment to loan amount ratio, %</i>
Trade financing loans				
Standard loans	26,537	–	26,537	–
Total trade financing loans	26,537	–	26,537	–
Long-term loans to banks				
Standard loans	168,997	–	168,997	–
Loans more than 90 days past due	15,254	(9,153)	6,101	60.0
Total long-term loans to banks	184,251	(9,153)	175,098	5.0
Loans to customers				
Standard loans	446,910	–	446,910	–
Restructured loans	6,008	(300)	5,708	5.0
Loans more than 90 days past due	15,151	(5,255)	9,896	34.7
Total loans to customers	468,069	(5,555)	462,514	1.2
Total loans	678,857	(14,708)	664,149	2.2

Where possible, the Group 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.

Liquidity risk

Liquidity risk is the risk of loss resulting from the Group'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 Group'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 Group) and/or an unforeseen need of immediate and simultaneous discharge of its financial obligations.

The Group manages its liquidity position in accordance with planning horizons (up to 12 months) and possible scenarios of movements in liquidity position (stable, stressed).

Main instrument of liquidity position management under the stable scenario is a Plan of Cash Flows defining the cash flow by balance sheet products/instruments and taking into account the plan of future financial operations. The Group determines the balance sheet gaps, payment schedule and need in financing of future operations based on the Plan of Cash Flows. As a result of application of these instruments, ALM Unit issues appropriate recommendations to responsible structural divisions.

The Group has implemented a liquidity buffer to manage the Group's liquidity under the stressed scenario. Application of the liquidity buffer enables the Group to promptly monitor the sustainability and stability of the Group's balance sheet structure in case of liquidity shortage that is critical to the Group's solvency.

The liquidity buffer is formed primarily due to liquidity reserves, namely securities recognized in the Group's balance sheet and included in the Lombard lists of the European Central Bank and Bank of Russia, and nostro accounts with banks and other financial institutions. The Group calculates its liquidity reserves as at the reporting date and for the next twelve monthly reporting dates (forecast). Liquidity buffer may be used to close the negative net position. As at 30 June 2018, the liquidity buffer amounts to EUR 72.9 million (31 December 2017: EUR 83.5 million).

*(Thousands of euros)***23. Risk management (continued)****Liquidity risk (continued)**

The table below shows the contractual maturities of the Group's off-balance credit-related commitments. In case of absence of contractual schedule of the credit related commitments, these obligations are included into the earliest date, at which the client can demand their execution.

	<i>30 June 2018</i> <i>(unaudited)</i>	<i>31 December</i> <i>2017</i>
Less than 1 month	137,390	25,835
1 to 3 months	5,054	72,744
3 months to 1 year	43,182	41,489
1 to 5 years	2,346	24,330
Over 5 years	35,975	–
Off-balance credit-related commitments	223,947	164,398

(intentionally blank)

(Thousands of euros)

23. 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. Quoted debt instruments at fair value through other comprehensive income and equity instruments were included in “Less than 1 month” category as they are highly liquid securities, shares and depositary receipts which the Group may sell in the short term on the arm-length basis. Securities at fair value through profit or loss pledged under repurchase agreements are presented on the basis of periods from the reporting date to the expiry date of respective contractual obligations of the Group.

	30 June 2018 (unaudited)							31 December 2017						
	Less than 1 month	1 to 3 months	3 months to 1 year	1 to 5 years	Over 5 years	Past due	Total	Less than 1 month	1 to 3 months	3 months to 1 year	1 to 5 years	Over 5 years	Past due	Total
Assets														
Cash and cash equivalents	56,746	479	–	–	–	–	57,225	65,445	652	–	–	–	–	66,097
Deposits with banks and other financial institutions	–	–	–	34,296	–	–	34,296	5,026	7,097	25,034	8,732	–	–	45,889
Derivative financial assets	49	–	–	1,298	–	–	1,347	935	–	5,072	1,754	–	–	7,761
Securities at fair value through other comprehensive income	174,808	19,038	–	–	–	–	193,846	138,737	54,783	21,907	–	–	–	215,427
Securities at amortized cost	–	83	216	4,404	36,719	–	41,422	–	–	–	–	–	–	–
Loans to banks	10,300	8,411	30,822	103,903	10,680	–	164,116	1,322	53,491	49,786	90,935	–	6,101	201,635
Loans to customers	11,904	17,798	70,627	151,801	293,497	–	545,627	8,965	8,719	77,334	147,277	210,323	9,896	462,514
Other financial assets	457	15	171	67	–	–	710	489	57	19	163	–	–	728
Total assets	254,264	45,824	101,836	295,769	340,896	–	1,038,589	220,919	124,799	179,152	248,861	210,323	15,997	1,000,051
Liabilities														
Due to banks and other financial institutions	(49,889)	(35,052)	–	–	–	–	(84,941)	–	(30,982)	(34,059)	(470)	–	–	(65,511)
Current customer accounts	(8,659)	–	–	–	–	–	(8,659)	(8,593)	–	–	–	–	–	(8,593)
Derivative financial liabilities	(2,489)	(2,783)	(11,139)	(20,159)	–	–	(36,570)	–	(89)	(1,213)	(13,771)	–	–	(15,073)
Long-term loans of banks	–	(280)	–	(28,948)	(16,849)	–	(46,077)	–	(24)	(59,967)	(18,819)	(16,782)	–	(95,592)
Debt securities issued	(76)	(6,047)	(123,234)	(452,396)	–	–	(581,753)	–	(3,906)	(26,519)	(478,788)	–	–	(509,213)
Other financial liabilities	(1,109)	–	(654)	(46)	–	–	(1,809)	(762)	(953)	(396)	(37)	–	–	(2,148)
Total liabilities	(62,222)	(44,162)	(135,027)	(501,549)	(16,849)	–	(759,809)	(9,355)	(35,954)	(122,154)	(511,885)	(16,782)	–	(696,130)
Net position	192,042	1,662	(33,191)	(205,780)	324,047	–	278,780	211,564	88,845	56,998	(263,024)	193,541	15,997	303,921
Accumulated net position	192,042	193,704	160,513	(45,267)	278,780	278,780		211,564	300,409	357,407	94,383	287,924	303,921	

*(Thousands of euros)***23. Risk management (continued)****Market risk**

Market risk is the risk that the Group may 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 Group 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.

Currency risk

Currency risk is the risk of loss resulting from adverse changes in exchange rates with respect to the Group'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 Group applies a VaR methodology to assess currency and equity risks. VaR is a method used in measuring maximum risk of the Group, 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 Group 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 Group is carried out in major currencies and financial instruments of the Group attributable to a securities portfolio.

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

As at 30 June 2018 and 31 December 2017, final data on value at risk (VaR) assessment in relation to currency and price risks assumed by the Group are represented as follows:

	<i>30 June 2018</i> <i>(unaudited)</i>	<i>31 December</i> <i>2017</i>
Fixed income securities price risk	936	1,005
Equity securities price risk	–	125
Currency risk	282	45

Despite the fact that 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.
- ▶ 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 Group'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)***23. Risk management (continued)****Market risk (continued)**

The Group has assets and liabilities denominated in several foreign currencies. The financial position and the cash flows are exposed to the effects of fluctuations in foreign currency exchange rates. Non-monetary financial instruments and financial instruments denominated in functional currency are not exposed to currency risk. The Group's exposure to currency risk as at 30 June 2018 and 31 December 2017 is presented below:

	<i>30 June 2018 (unaudited)</i>					<i>31 December 2017</i>				
	<i>EUR</i>	<i>USD</i>	<i>RUB</i>	<i>Other currencies</i>	<i>Total</i>	<i>EUR</i>	<i>USD</i>	<i>RUB</i>	<i>Other currencies</i>	<i>Total</i>
Non-derivative financial Assets										
Cash and cash equivalents	38,686	12,220	932	5,387	57,225	50,488	1,730	13,501	378	66,097
Deposits with banks and other financial institutions	34,296	–	–	–	34,296	28,936	16,953	–	–	45,889
Securities at fair value through other comprehensive income	95,184	90,083	8,579	–	193,846	111,516	102,202	–	1,709	215,427
Securities at amortized cost	15,101	26,321	–	–	41,422	–	–	–	–	–
Long-term loans to banks	129,426	34,690	–	–	164,116	147,253	54,382	–	–	201,635
Loans to customers	320,023	106,019	80,440	39,145	545,627	247,804	108,254	64,097	42,359	462,514
Other financial assets	154	334	220	2	710	186	323	214	5	728
Total non-derivative financial assets	632,870	269,667	90,171	44,534	1,037,242	586,183	283,844	77,812	44,451	992,290
Liabilities										
Due to banks and other financial institutions	(70,180)	–	–	(14,761)	(84,941)	(34,608)	(29,337)	–	(1,566)	(65,511)
Current customer accounts	(8,545)	(114)	–	–	(8,659)	(8,481)	(112)	–	–	(8,593)
Long-term loans of banks	(22,944)	(10,938)	–	(12,195)	(46,077)	(82,694)	–	–	(12,898)	(95,592)
Debt securities issued	(91,108)	–	(306,942)	(183,703)	(581,753)	(90,017)	–	(267,112)	(152,084)	(509,213)
Other financial liabilities	(873)	–	(925)	(11)	(1,809)	(546)	(175)	(1,427)	–	(2,148)
Total non-derivative financial liabilities	(193,650)	(11,052)	(307,867)	(210,670)	(723,239)	(216,346)	(29,624)	(268,539)	(166,548)	(681,057)
Net balance sheet position (excluding derivative financial instruments)	439,220	258,615	(217,696)	(166,136)	314,003	369,837	254,220	(190,727)	(122,097)	311,233
Derivative financial instruments										
Claims	181,750	–	217,908	176,151	575,809	190,457	–	197,443	132,639	520,539
Liabilities	(371,996)	(224,507)	–	(14,529)	(611,032)	(296,697)	(220,909)	–	(10,245)	(527,851)
Net balance sheet position including derivative financial instruments	248,974	34,108	212	(4,514)	278,780	263,597	33,311	6,716	297	303,921

*(Thousands of euros)***24. Fair value measurements**

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 Group using available market information, where it exists, and appropriate valuation methodologies. However, judgement is necessarily required to interpret market data to determine the 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 Group 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 that use inputs which have a significant effect on the recognized fair value that are not based on observable market data.

For the purpose of fair value disclosures, the Group has determined classes of assets and liabilities on the basis of the nature, characteristics and risks of the asset or liability and the level of the fair value hierarchy as explained above. The following table shows an analysis of financial instruments recorded at fair value by level of the fair value hierarchy as at 30 June 2018:

	<i>Level 1</i> <i>30 June</i> <i>2018</i> <i>(unaudited)</i>	<i>Level 2</i> <i>30 June</i> <i>2018</i> <i>(unaudited)</i>	<i>Level 3</i> <i>30 June</i> <i>2018</i> <i>(unaudited)</i>	<i>Total</i> <i>30 June</i> <i>2018</i> <i>(unaudited)</i>
Assets measured at fair value				
Derivative financial assets	–	1,347	–	1,347
Government bonds of member countries	41,919	–	–	41,919
Corporate bonds	151,114	–	–	151,114
Quoted equity instruments	–	5	–	5
Investment property	–	–	20,862	20,862
Property and equipment – buildings	–	–	67,054	67,054
Liabilities measured at fair value				
Derivative financial liabilities	–	36,570	–	36,570
Assets for which fair values are disclosed				
Cash and cash equivalents	364	56,861	–	57,225
Deposits with banks and other financial institutions	–	–	34,296	34,296
Securities at amortized cost	–	38,537	–	38,537
Loans to banks	–	–	161,448	161,448
Loans to customers	–	–	554,398	554,398
Liabilities for which fair values are disclosed				
Due to banks and other financial institutions	–	–	84,941	84,941
Current customer accounts	–	–	8,659	8,659
Long-term loans of banks	–	–	46,077	46,077
Debt securities issued	–	585,051	–	585,051

*(Thousands of euros)***24. Fair value measurements (continued)****Fair value hierarchy (continued)**

The following table shows an analysis of financial instruments recorded at fair value by level of the fair value hierarchy as at 31 December 2017:

	<i>Level 1</i> <i>2017</i>	<i>Level 2</i> <i>2017</i>	<i>Level 3</i> <i>2017</i>	<i>Total</i> <i>2017</i>
Assets measured at fair value				
Derivative financial assets	–	7,761	–	7,761
Government bonds of member countries	45,891	–	–	45,891
Corporate bonds	149,277	18,544	–	167,821
Quoted equity instruments	1,710	5	–	1,715
Investment property	–	–	21,853	21,853
Property and equipment – buildings	–	–	67,572	67,572
Liabilities measured at fair value				
Derivative financial liabilities	–	15,073	–	15,073
Assets for which fair values are disclosed				
Cash and cash equivalents	85	66,012	–	66,097
Deposits with banks and other financial institutions	–	–	45,889	45,889
Loans to banks	–	–	201,743	201,743
Loans to customers	–	–	465,973	465,973
Liabilities for which fair values are disclosed				
Due to banks and other financial institutions	–	–	65,511	65,511
Current customer accounts	–	–	8,593	8,593
Long-term loans of banks	–	–	95,592	95,592
Debt securities issued	–	514,893	–	514,893

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 Group's financial instruments that are recorded in the interim condensed consolidated financial statements. The table does not include the fair values of non-financial assets and non-financial liabilities.

	<i>Carrying amount 30 June 2018 (unaudited)</i>	<i>Fair value 30 June 2018 (unaudited)</i>	<i>Unrecognized gain/(loss) 30 June 2018 (unaudited)</i>	<i>Carrying amount 31 December 2017</i>	<i>Fair value 31 December 2017</i>	<i>Unrecognized gain/(loss) 31 December 2017</i>
Financial assets						
Cash and cash equivalents	57,225	57,225	–	66,097	66,097	–
Deposits with banks and other financial institutions	34,296	34,296	–	45,889	45,889	–
Securities at amortized cost	41,422	38,537	(2,885)	–	–	–
Loans to banks	164,116	161,448	(2,668)	201,635	201,743	108
Loans to customers	545,627	554,398	8,771	462,514	465,973	3,459
Financial liabilities						
Due to banks and other financial institutions	84,941	84,941	–	65,511	65,511	–
Current customer accounts	8,659	8,659	–	8,593	8,593	–
Long-term loans of banks	46,077	46,077	–	95,592	95,592	–
Debt securities issued	581,753	585,051	(3,298)	509,213	514,893	(5,680)
Total unrecognized change in unrealized fair value			(80)			(2,113)

*(Thousands of euros)***25. Segment information**

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

Credit investment activity	Investment banking services, including long-term corporate and interbank financing.
Treasury	Operations in financial markets, transactions with securities, derivative financial instruments and foreign currency, and liquidity management.
Other operations	Operational leasing services, other operations.

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 interim condensed consolidated financial statements. The following table presents income, profit, assets and liabilities of the Group's operating segments:

<i>30 June 2018 (unaudited)</i>	<i>Credit investment activity</i>	<i>Treasury</i>	<i>Other operations</i>	<i>Total</i>
Income				
External customers				
Interest income	17,592	11,943	17	29,552
Fee and commission income	870	–	–	870
Net gains from operations with securities at fair value through profit or loss	–	92	–	92
Net gains from operations with securities at fair value through other comprehensive income	–	2,238	–	2,238
Dividend income	–	6	–	6
Income from lease of investment property	–	–	2,032	2,032
Net reversal of allowance for impairment of financial instruments	(398)	382	76	60
Net reversal of allowance for credit losses from impairment of other financial assets	–	–	2	2
Other segment income	232	–	300	532
Total income	18,296	14,661	2,427	35,384
Interest expenses	(10,456)	(7,928)	–	(18,384)
Fee and commission expense	(31)	(82)	(2)	(115)
Net losses from dealing in foreign currencies and operations with derivatives	–	(1,844)	(16)	(1,860)
Cost of inventories sold	–	–	(48)	(48)
Other segment expenses	–	–	(987)	(987)
Segment results	7,809	4,807	1,374	13,990
Other unallocated expenses				(8,903)
Profit for the period				5,087
Development portfolio	711,276	100,379	–	811,655
Other segment assets	–	227,103	94,399	321,502
Total segment assets	711,276	327,482	94,399	1,133,157
Total segment liabilities	394,441	365,562	5,552	765,555
Other segment information				
Capital expenditures	–	–	683	683

The Group's management separates the "Development portfolio" assets allocated within operating segments. The criteria of separation is orientation of the assets on the fulfilling of the Group's mission. "Development portfolio" includes loans to banks and loans to customers excluding impaired loan projects and the investments in debt securities purchased upon initial placement by the issuer.

(Thousands of euros)

25. Segment information (continued)

<i>30 June 2017 (unaudited)</i>	<i>Credit investment activity</i>	<i>Treasury</i>	<i>Other operations</i>	<i>Total</i>
Income				
External customers				
Interest income	11,390	13,435	19	24,844
Fee and commission income	302	–	–	302
Net gains from available-for-sale investment securities	–	4,553	–	4,553
Income from lease of investment property	–	–	2,049	2,049
Reversal of allowance for impairment of other assets	–	–	27	27
Other segment income	2	–	83	85
Total income	11,694	17,988	2,178	31,860
Interest expenses	(7,313)	(7,857)	–	(15,170)
Fee and commission expense	(9)	(60)	(2)	(71)
Net losses from dealing in foreign currencies and operations with derivatives	–	(852)	11	(841)
Allowance for impairment of financial assets	(3,781)	–	–	(3,781)
Other segment expenses	(89)	(83)	(477)	(649)
Segment results	502	9,136	1,710	11,348
Other unallocated expenses				(9,061)
				2,287
Profit for the period				
Development portfolio	490,923	65,631	–	556,554
Other segment assets	9,896	340,413	95,806	446,115
Total segment assets	500,819	406,044	95,806	1,002,669
Total segment liabilities	276,007	324,495	9,403	609,905
Other segment information				
Capital expenditures	–	–	70	70

During the six months of 2018, the Group's revenue from lease operations with two external counterparties (30 June 2017: two external counterparties) exceeded 20% of the Group's total revenue (six months ended 30 June 2018: EUR 1,408 thousand; six months ended 30 June 2017: EUR 1,511 thousand).

Geographical information

Allocation of the Group's revenue from transactions with external customers and non-current assets based on the location of these customers and assets for the years ended 30 June 2018 and 30 June 2017 is presented in the table below:

	<i>30 June 2018 (unaudited)</i>				<i>30 June 2017 (unaudited)</i>			
	<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 calculated using the EIR method	4,567	12,326	4,700	21,593	4,130	7,035	4,977	16,142
Other interest income	3,756	161	4,026	7,943	330	175	8,192	8,697
Income from lease of investment property	1,947	85	–	2,032	1,942	107	–	2,049
Non-current assets (investment property)	7,534	13,328	–	20,862	7,536	14,324	–	21,860

(Thousands of euros)

25. Segment information (continued)

Geographical information (continued)

The geographical concentration of the Group's assets and liabilities based on the location of the Group's counterparties as at 30 June 2018 and 31 December 2017 is presented below:

	<i>30 June 2018 (unaudited)</i>										
	<i>Russian Federation</i>	<i>Republic of Bulgaria</i>	<i>Romania</i>	<i>Slovak Republic</i>	<i>Hungary</i>	<i>Mongolia</i>	<i>Socialist Republic of Vietnam</i>	<i>Czech Republic</i>	<i>Republic of Cuba</i>	<i>Other countries</i>	<i>Total</i>
Assets											
Cash and cash equivalents	1,092	805	329	11,255	–	–	–	5	–	43,739	57,225
Deposits with banks and other financial institutions	11,326	–	–	–	–	–	–	–	–	22,970	34,296
Derivative financial assets	49	–	–	–	–	–	–	–	–	1,298	1,347
Securities at fair value through other comprehensive income	12,476	14,980	10,002	1,144	–	–	–	34,495	–	120,749	193,846
Securities at amortized cost	–	–	–	–	–	–	–	–	–	41,422	41,422
Long-term loans to banks	–	–	–	–	–	55,205	25,031	–	49,366	34,514	164,116
Loans to customers	101,863	111,253	69,770	89,415	29,515	23,927	–	50,053	–	69,831	545,627
Other financial assets	369	–	–	–	2	6	–	–	–	333	710
Assets	127,175	127,038	80,101	101,814	29,517	79,138	25,031	84,553	49,366	334,856	1,038,589
Liabilities											
Due to banks and other financial institutions	–	5,000	9,882	–	4,878	–	–	40,010	–	25,171	84,941
Derivative financial liabilities	12,769	–	1,106	–	–	–	–	–	–	22,695	36,570
Long-term loans of banks	–	–	–	–	12,195	–	–	–	–	33,882	46,077
Long-term securities issued	306,957	–	215,174	30,686	–	–	–	28,936	–	–	581,753
Other financial liabilities	957	758	–	–	–	83	–	–	–	11	1,809
Liabilities	320,683	5,758	226,162	30,686	17,073	83	–	68,946	–	81,759	751,150

International Investment Bank

(Thousands of euros)

25. Segment information (continued)

Geographical information (continued)

	<i>31 December 2017</i>										
	<i>Russian Federation</i>	<i>Republic of Bulgaria</i>	<i>Romania</i>	<i>Slovak Republic</i>	<i>Hungary</i>	<i>Mongolia</i>	<i>Socialist Republic of Vietnam</i>	<i>Czech Republic</i>	<i>Republic of Cuba</i>	<i>Other countries</i>	<i>Total</i>
Assets											
Cash and cash equivalents	1,209	792	226	35	–	–	–	36	–	63,799	66,097
Deposits with banks and other financial institutions	3,082	–	–	–	–	32,132	–	–	–	10,675	45,889
Derivative financial assets Available-for-sale	3,340	–	–	–	–	–	–	–	–	4,421	7,761
investment securities	11,947	30,098	–	10,010	13,817	–	–	34,107	–	115,448	215,427
Loans to banks	89,545	–	–	–	–	33,735	25,252	–	49,863	3,240	201,635
Loans to customers	81,817	57,694	73,185	60,464	42,910	24,425	–	49,967	–	72,052	462,514
Other financial assets	382	6	–	–	5	5	–	1	–	329	728
Assets	191,322	88,590	73,411	70,509	56,732	90,297	25,252	84,111	49,863	269,964	1,000,051
Liabilities											
Due to banks and other financial institutions	1,460	–	–	7,508	–	–	–	1,566	–	54,977	65,511
Derivative financial liabilities	4,480	–	1,213	–	–	–	–	–	–	9,380	15,073
Long-term loans of banks	9,959	7,470	–	–	20,367	–	–	–	–	57,796	95,592
Long-term securities issued	266,191	–	212,869	30,153	–	–	–	–	–	–	509,213
Other financial liabilities	1,658	33	15	8	–	237	–	–	–	197	2,148
Liabilities	283,748	7,503	214,097	37,669	20,367	237	–	1,566	–	122,350	687,537

Other countries include non-member countries.

*(Thousands of euros)***26. 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 as at 30 June 2018 and 31 December 2017, and related expenses and income for the six months ended 30 June 2018 and 2017 are as follows:

		<i>30 June 2018</i> <i>(unaudited)</i>	<i>31 December</i> <i>2017</i>
	<i>Related party</i>	<i>Carrying amount</i>	<i>Carrying amount</i>
Interim consolidated statement of financial position			
Current customer accounts	Key management personnel	1,342	1,420
Other liabilities	Key management personnel	624	593
		<i>30 June 2018</i> <i>(unaudited)</i>	<i>30 June 2017</i> <i>(unaudited)</i>
	<i>Related party</i>	<i>Income/(expense)</i>	<i>Income/(expense)</i>
Interim consolidated income statement			
Interest expenses on current customer accounts	Key management personnel	(17)	(27)
Net interest expense after allowance for loan impairment		(17)	(27)
Expenses from operating activities		(17)	(27)
Employee benefits	Key management personnel	(836)	(669)
Compensation for travel expenses and medical insurance	Key management personnel	(36)	(32)
Operating expenses		(872)	(701)
Net loss for the period		(889)	(728)

27. Capital adequacy

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

The Basel Committee on Banking Supervision recommends maintaining the ratio of capital to risk-weighted assets ("capital adequacy ratio") above the prescribed minimum level. As of 30 June 2018, this minimum level was 8% (31 December 2017: 8%).

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 at 30 June 2018 (31 December 2017: 25%).

*(Thousands of euros)***27. Capital adequacy (continued)**

The following table shows the composition of the Group's capital position computed in accordance with the Basel Accord (Basel II) as at 30 June 2018 and 31 December 2017.

	<i>30 June 2018</i> <i>(unaudited)</i>	<i>31 December</i> <i>2017</i>
Capital		
Tier 1 capital	351,199	380,745
Tier 2 capital	9,257	13,988
Total regulatory capital	360,456	394,733
Risk-weighted assets		
Credit risk	896,578	822,189
Market risk	147,615	177,273
Operational risk	41,863	43,411
Total risk-weighted assets	1,086,056	1,042,873
Total capital expressed as a percentage of risk-weighted assets, % ("capital adequacy ratio")	33.19%	37.85%
Total tier 1 capital expressed as a percentage of risk-weighted assets, % ("tier 1 capital adequacy ratio")	32.34%	36.51%

28. Subsequent events

On 12 July, the Government of Romania made a contribution of EUR 4,000 thousand to the Bank's share capital. As a result, the paid-in capital of the International Investment Bank amounted to EUR 318,962 thousand, and Romania increased its share in the paid-in capital to 7.04%.

(The end).

Independent auditor's report
on the consolidated financial statements of
***the International Investment Bank
and its subsidiary***
for 2018

February 2019

**Independent auditor's report
on the consolidated financial statements of
the International Investment Bank and its subsidiary**

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Independent auditor's report

To the Board of Governors of
the International Investment Bank

Opinion

We have audited the consolidated financial statements of the International Investment Bank (the "Bank") and its subsidiary (the "Group"), which comprise the consolidated statement of financial position as at 31 December 2018, and the consolidated income statement, consolidated statement of comprehensive income, consolidated statement of changes in equity and consolidated statement of cash flows for 2018, and notes to the consolidated financial statements, including a summary of significant accounting policies.

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

Basis for opinion

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

Key audit matters

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

We have fulfilled the responsibilities described in the *Auditor's responsibilities for the audit of the consolidated financial statements* section of our report, including in relation to these matters. Accordingly, our audit included the performance of procedures designed to respond to our assessment of the risks of material misstatement of the consolidated financial statements. The results of our audit procedures, including the procedures performed to address the matters below, provide the basis for our audit opinion on the accompanying consolidated financial statements.

Key audit matter

How our audit addressed the key audit matter

Allowance for expected credit losses on loans to banks and loans to customers

Estimation of the allowance for expected credit losses on loans to banks and loans to customers in accordance with IFRS 9 is a key area of judgment for the Group's management. Identification of factors of significant credit risk increase, considering the change in the risk of default occurring over the remaining life of the financial instrument, estimation of default probability and loss given default involve significant use of judgments, assumptions and analysis of various factors, including financial and non-financial information by counterparty, macroeconomic projections and estimated future repayment proceeds.

The use of different models and assumptions can significantly affect the level of allowance for expected credit losses on loans to banks and loans to customers. Due to the significance of such loans, which account for 63% of the total assets, and the significant use of judgments, the assessment of the allowance for expected credit losses is a key audit matter.

The information on expected credit losses on loans to banks and loans to customers is provided in Note 10 Loans to banks, Note 11 Loans to customers, Note 15 Allowances for credit losses, other impairment losses and provisions and Note 25 Risk management to the consolidated financial statements.

Our audit procedures included an analysis of the methodology for assessing the allowance, a review of the financial and non-financial information by counterparty, debt servicing, internal credit ratings of counterparties and an assessment of default probability based on the Bank's methodology, monitoring reports and risk ratings, an analysis of macroeconomic projections, an estimation of future repayment proceeds on a sample basis, and analytical procedures with respect to the credit portfolio.

We have also analyzed information related to the allowance for expected credit losses on loans to banks and loans to customers disclosed in the notes to the consolidated financial statements of the Group.

Other information included in the Annual report of the Group for 2018

Other information comprises information included in the Annual report of the Group for 2018, other than the consolidated financial statements and our auditor's report thereon. Management is responsible for the other information. The Annual report of the Group for 2018 is expected to be made available to us after the date of this auditor's report.

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

In connection with our audit of the consolidated financial statements, our responsibility is to read the other information when it is provided to us and, in doing so, consider whether the other information is materially inconsistent with the consolidated financial statements or our knowledge obtained in the audit or otherwise appears to be materially misstated.

Responsibilities of management and the Board of Governors of the International Investment Bank for the consolidated financial statements

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

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

The Board of Governors of the International Investment Bank is responsible for overseeing the Group's financial reporting process.

Auditor's responsibilities for the audit of the consolidated financial statements

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

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

- ▶ Identify and assess the risks of material misstatement of the consolidated financial statements, whether due to fraud or error, design and perform audit procedures responsive to those risks, and obtain audit evidence that is sufficient and appropriate to provide a basis for our opinion. The risk of not detecting a material misstatement resulting from fraud is higher than for one resulting from error, as fraud may involve collusion, forgery, intentional omissions, misrepresentations, or the override of internal control.
- ▶ Obtain an understanding of internal control relevant to the audit in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Group's internal control.
- ▶ Evaluate the appropriateness of accounting policies used and the reasonableness of accounting estimates and related disclosures made by management.
- ▶ Conclude on the appropriateness of management's use of the going concern basis of accounting and, based on the audit evidence obtained, whether a material uncertainty exists related to events or conditions that may cast significant doubt on the Group's ability to continue as a going concern. If we conclude that a material uncertainty exists, we are required to draw attention in our auditor's report to the related disclosures in the consolidated financial statements or, if such disclosures are inadequate, to modify our opinion. Our conclusions are based on the audit evidence obtained up to the date of our audit report. However, future events or conditions may cause the Group to cease to continue as a going concern.
- ▶ Evaluate the overall presentation, structure and content of the consolidated financial statements, including the disclosures, and whether the consolidated financial statements represent the underlying transactions and events in a manner that achieves fair presentation.
- ▶ Obtain sufficient appropriate audit evidence regarding the financial information of the entities or business activities within the Group to express an opinion on the consolidated financial statements. We are responsible for the direction, supervision and performance of the group audit. We remain solely responsible for our audit opinion.

We communicate with the Board of Governors of the International Investment Bank regarding, among other things, the planned scope and timing of the audit and significant audit findings, including any significant deficiencies in internal control that we identify during our audit.

We also provide the Board of Governors of the International Investment Bank with a statement that we have complied with relevant ethical requirements regarding independence, and to communicate with it all relationships and other matters that may reasonably be thought to bear on our independence, and where applicable, related safeguards.

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

The partner in charge of the audit resulting in this independent auditor's report is O.V. Youshenkov.



O.V. Youshenkov
Partner
Ernst & Young Vneshaudit LLC

14 February 2019

Details of the audited entity

Name: International Investment Bank

The Bank operates on the basis of the Agreement on the Establishment of the International Investment Bank dated 10 July 1970, registered in the UN Secretariat on 1 December 1971 under No. 11417.

Address: Russia 107078, Moscow, Mashi Poryvaevoy str., 7.

Details of the auditor

Name: Ernst & Young Vneshaudit LLC

Record made in the State Register of Legal Entities on 4 February 2016, State Registration Number 1167746123478.

Address: Russia, 115035 Moscow, Sadovnicheskaya nab., 77, building 1.

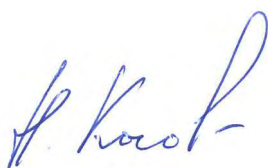
Ernst & Young Vneshaudit LLC is a member of Self-regulated organization of auditors "Russian Union of Auditors" (Association) ("SRO RUA"). Ernst & Young Vneshaudit LLC is included in the control copy of the register of auditors and audit organizations, main registration number 11603050953.

CONSOLIDATED STATEMENT OF FINANCIAL POSITION**At 31 December 2018***(Thousands of euros)*

	<i>Notes</i>	<i>31 December 2018</i>	<i>31 December 2017</i>
Assets			
Cash and cash equivalents	5	49,240	66,097
Deposits with banks and other financial institutions	6	47,396	45,889
Derivative financial assets	7	3,720	7,761
Securities at fair value through other comprehensive income	8	204,332	–
Available-for-sale investment securities		–	138,704
Available-for-sale investment securities pledged under repurchase agreements		–	76,723
Securities at amortized cost	9	41,465	–
Loans to banks	10	176,632	201,635
Loans to customers	11	576,203	462,514
Investment property	12	20,788	21,853
Property, equipment and intangible assets	13	71,266	72,388
Other assets	14	3,315	2,476
Total assets		1,194,357	1,096,040
Liabilities			
Due to banks and other financial institutions	16	67,872	65,511
Derivative financial liabilities	7	50,943	15,073
Current customer accounts		9,716	8,593
Long-term loans of banks	17	57,553	95,592
Debt securities issued	18	623,454	509,213
Other liabilities	14	8,820	6,396
Total liabilities		818,358	700,378
Equity			
Statutory capital	19	2,000,000	1,300,000
Unpaid capital		(1,674,038)	(985,038)
Paid-in capital		325,962	314,962
Revaluation reserve for securities at fair value through other comprehensive income (2017: Revaluation reserve for available-for-sale securities)		(7,366)	240
Revaluation reserve for property and equipment		13,748	13,748
Foreign currency translation reserve		(104)	(76)
Retained earnings less net income for the year		38,137	65,783
Net income for the year		5,622	1,005
Total equity		375,999	395,662
Total equity and liabilities		1,194,357	1,096,040

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

Nikolay Kosov



Chairperson of the Management Board

Elena Minduksheva



Deputy Director of the Finance Department

14 February 2019

The accompanying notes 1-30 are an integral part of these consolidated financial statements.

CONSOLIDATED INCOME STATEMENT**For the year ended 31 December 2018***(Thousands of euros)*

	<i>Notes</i>	2018	2017
Interest income calculated using the EIR method	22	45,929	35,963
Other interest income	22	16,874	19,932
Interest expenses calculated using the EIR method	22	(36,144)	(32,566)
Other interest expenses	22	(3,047)	(1,542)
Net interest income		23,612	21,787
Net allowance for credit losses on financial instruments	5-6, 8, 10-11, 14-15, 20	(161)	(12,136)
Net interest income after allowance for loan impairment		23,451	9,651
Fee and commission income		1,779	1,763
Fee and commission expense		(398)	(133)
Net fee and commission income		1,381	1,630
Net losses from operations with foreign currencies and derivatives	23	(5,042)	(2,441)
Net gains from operations with securities at fair value through profit or loss		92	–
Net gains from operations with securities at fair value through other comprehensive income		2,299	–
Net gains from available-for-sale investment securities		–	7,399
Dividend income		6	123
Income from lease of investment property	21	3,956	4,034
Loss on revaluation of investment property		–	(26)
Other income		1,200	543
Net non-interest income		2,511	9,632
Operating income		27,343	20,913
General and administrative expenses	24	(20,442)	(18,872)
Cost of inventories sold		(48)	–
Other operating expenses on banking operations		(1,231)	(1,036)
Operating expenses		(21,721)	(19,908)
Net profit for the year		5,622	1,005

CONSOLIDATED STATEMENT OF COMPREHENSIVE INCOME**For the year ended 31 December 2018***(Thousands of euros)*

	<i>Notes</i>	<i>2018</i>	<i>2017</i>
Net profit for the year		5,622	1,005
Other comprehensive income			
<i>Other comprehensive income to be reclassified to profit or loss in subsequent periods</i>			
Net change in the fair value of debt instruments at fair value through other comprehensive income	19	(9,624)	1,746
Translation differences		(28)	(19)
Change in the allowance for expected credit losses related to securities at fair value through other comprehensive income	8	300	–
Net other comprehensive (loss)/income to be reclassified to profit or loss in subsequent periods		(9,352)	1,727
<i>Other comprehensive loss not to be reclassified to profit or loss in subsequent periods</i>			
Revaluation of property and equipment	13	–	803
Losses on equity instruments at fair value through other comprehensive income		(73)	–
Net other comprehensive loss not to be reclassified to profit or loss in subsequent periods		(73)	803
Other comprehensive (loss)/income		(9,425)	2,530
Total comprehensive (loss)/income for the year		(3,803)	3,535

CONSOLIDATED STATEMENT OF CHANGES IN EQUITY**For the year ended 31 December 2018***(Thousands of euros)*

	<i>Statutory capital</i>	<i>Unpaid capital</i>	<i>Revaluation reserve for securities</i>	<i>Revaluation reserve for property and equipment</i>	<i>Foreign currency translation reserve</i>	<i>Retained earnings</i>	<i>Total equity</i>
At 31 December 2016	1,300,000	(986,947)	(1,506)	12,945	(57)	65,783	390,218
Profit for the year	–	–	–	–	–	1,005	1,005
Other comprehensive income for the year	–	–	1,746	803	(19)	–	2,530
Total comprehensive income	–	–	1,746	803	(19)	1,005	3,535
Contributions to capital (Note 19)	–	1,909	–	–	–	–	1,909
At 31 December 2017	1,300,000	(985,038)	240	13,748	(76)	66,788	395,662
At 31 December 2017	1,300,000	(985,038)	240	13,748	(76)	66,788	395,662
Impact of adopting IFRS 9	–	–	2,043	–	–	(28,903)	(26,860)
Balance at 1 January 2018 restated under IFRS 9	1,300,000	(985,038)	2,283	13,748	(76)	37,885	368,802
Profit for the year	–	–	–	–	–	5,622	5,622
Other comprehensive loss for the year	–	–	(9,397)	–	(28)	–	(9,425)
Total comprehensive (loss)/income	–	–	(9,397)	–	(28)	5,622	(3,803)
Statutory capital change (Note 19)	700,000	(700,000)	–	–	–	–	–
Contributions to capital (Note 19)	–	11,000	–	–	–	–	11,000
Transfer of accumulated revaluation reserve on disposal of equity instruments at fair value through other comprehensive income	–	–	(252)	–	–	252	–
At 31 December 2018	2,000,000	(1,674,038)	(7,366)	13,748	(104)	43,759	375,999

CONSOLIDATED STATEMENT OF CASH FLOWS**For the year ended 31 December 2018***(Thousands of euros)*

	<i>Notes</i>	2018	2017
Cash flows from operating activities			
Interest, fees and commissions received		34,612	28,578
Interest, fees and commissions paid		(1,174)	(3,327)
Realized gains less losses from operations with foreign currencies and derivatives		(1,577)	15,775
Cash flows from lease of investment property		3,956	4,034
General and administrative expenses		(16,221)	(15,761)
Other operating (expenses)/income on banking operations		(2)	36
Cash flows from operating activities before changes in operating assets and liabilities		19,594	29,335
<i>Net (increase)/decrease in operating assets</i>			
Deposits with banks and other financial institutions		6,350	(5,776)
Loans to banks		16,236	(118,882)
Loans to customers		(131,621)	(210,605)
Other assets		(493)	(15)
<i>Net increase/(decrease) in operating liabilities</i>			
Deposits from banks and other financial institutions		(6,057)	(47,426)
Current customer accounts		9	(1,227)
Other liabilities		(166)	1,016
Net cash flows from operating activities		(96,148)	(353,580)
Cash flows from investing activities			
Dividend income		6	123
Interest received		6,436	6,491
Purchase of securities at fair value through other comprehensive income (2017: Purchase of available-for-sale securities)		(208,498)	(426,482)
Proceeds from sale and redemption of securities at fair value through other comprehensive income (2017: Purchase of available-for-sale securities)		177,826	478,424
Proceeds from redemption of securities at amortized cost		729	–
Proceeds from sale of investment property/(investments in investment property)		1,065	(39)
Purchase of property, equipment and intangible assets		(1,259)	(1,673)
Net cash flows from investing activities		(23,695)	56,844
Cash flows from financing activities			
Interest paid		(18,469)	(10,759)
Long-term interbank financing raised		20,845	36,185
Long-term interbank financing repaid		(60,455)	(13,451)
Debt securities issued		228,798	348,661
Redemption and repurchase of debt securities		(76,792)	(88,290)
Contributions to capital		11,000	1,909
Net cash flows from financing activities		104,927	274,255
Effect of exchange rate changes on cash and cash equivalents		(1,941)	(4,453)
Net increase/(decrease) in cash and cash equivalents		(16,857)	(26,934)
Cash and cash equivalents, beginning		66,097	93,031
Cash and cash equivalents, ending	5	49,240	66,097

The accompanying notes 1-30 are an integral part of these consolidated financial statements.

(Thousands of euros)

1. Principal activities

These consolidated financial statements include the financial statements of the International Investment Bank (the “Bank”, or “IIB”) and CJSC IIB Capital, the subsidiary of the Bank. The Bank and its subsidiary are hereinafter collectively referred to as the “Group”. The International Investment Bank is the parent company of the Group. Information on the subsidiary of the Bank is presented in Note 2.

The International Investment Bank (the “Bank” or the “IIB”) 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 Statute. The Agreement was ratified by the member countries of the Bank and registered with the Secretariat of the United Nations in December 1971. On 18 August 2018, the revised Agreement and Statute, approved by the Protocol on Introducing Changes to the Agreement on the Establishment of the International Investment Bank and to the Statute of 8 May 2014, became effective and applicable. 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 Board of Governors of the IIB. The Bank also performs transactions with securities and foreign currency.

The Bank operates from its headquarters in Russia at 7 Mashi Poryvaevoy str., Moscow. In December 2018, the Board of Governors decided to close the European regional office in Bratislava (Eurovea Central 1, Pribinova 4, Bratislava, 81109, Slovak Republic) from 31 December 2018 and to transfer the IIB’s headquarters to Budapest, Hungary. In order to implement this decision, the Bank is working to draft agreements on the conditions of setting up the Bank’s headquarters in Budapest and the office in Moscow, which must be agreed with and signed by the Hungarian and Russian parties, respectively. The Bank’s headquarters in Budapest are expected to be officially opened in 2019.

The Group had an average of 213 staff employees during 2018 (2017: 220).

On 31 July 2014, the EU Council imposed sectoral sanctions against Russia. The preamble of the Decision of the EU Council of 31 July 2014 (paragraph 9) and Council Regulation (EU) No. 833/2014 of 31 July 2014 (paragraph 5), which was developed based on the Decision, emphasize that the sanctions do not cover Russia-based institutions with international status established by intergovernmental agreements in which Russia is one of the parties. Therefore, the IIB is directly excluded from the list of financial institutions to which the restrictions apply.

The Group continues to expand its operations in accordance with its mandate and strategic objectives established by the member countries:

- ▶ According to the Protocol on Introducing Changes to the Agreement on the Establishment of the International Investment Bank and the Statute:
 - ▶ The Bank implemented the three level corporate governance structure and established new bodies, the Board of Governors and the Board of Directors;
 - ▶ The IIB’s subscribed authorized capital increased from EUR 1.3 billion to EUR 2 billion;
 - ▶ A proportional voting system in accordance with the corresponding shares in the paid-in capital and double majority approach were introduced to the process of decision-making by the Bank’s supreme management bodies.
- ▶ In December 2018, in Varadero, Cuba, meetings of the Board of Governors and the Board of Directors were held for the first time in the Bank’s history, resulting in the adoption of several strategically important decisions, in particular:
 - ▶ The relocation of the Bank’s headquarters from Moscow to Budapest;
 - ▶ The opening of an IIB office in Moscow;
 - ▶ The new IIB capitalization program for 2020-2022 for the total amount of EUR 200 million was approved. Also, at least EUR 50 million of this amount is to be paid by the end of 2020.
- ▶ On 12 July 2018, as part of the Capitalization Program for 2013-2017 Romania made a contribution of EUR 4 million to the IIB authorized capital; on 20 December 2018, the Czech Republic contributed EUR 7 million.

*(Thousands of euros)***1. Principal activities (continued)**

- ▶ During 2018 four international rating agencies upgraded the long-term credit rating of the Bank: in February, Dagong Global Credit Rating upgraded IIB rating to A with a positive outlook; in April, Standard & Poor's and Moody's Investors Services upgraded IIB ratings – to BBB+ and A3, respectively, with a stable outlook; and in November, Fitch Ratings upgraded IIB rating to BBB+ with a stable outlook.
- ▶ In April-June 2018, the IIB successfully placed its first CZK-denominated bond issue the Vienna and Prague Stock Exchanges. The private placement issue totaled CZK 750 million. In October 2018, the IIB made a historically significant bond issue (the fourth by now) on the Bucharest Stock Exchange, which was the largest issue on the Romanian market (approx. EUR 145 million).
- ▶ In October 2018, the Bank became a full-fledged member of the International Development Finance Club (IDFC), a network of leading national and regional development banks.
- ▶ Following the results of 2018, the Bank won the award of Global Banking and Finance Review magazine in two categories: Fastest Growing Infrastructure Investment Bank Central Europe 2018, Fastest Growing Infrastructure Bank Eastern Europe 2018. Also, The European magazine awarded the title of Trade and Finance Bank of the Year CEE – 2019 to the Bank.

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>	<i>31 December 2018, %</i>	<i>31 December 2017, %</i>
Russian Federation	46.026	47.634
Republic of Bulgaria	12.947	13.399
Hungary	12.271	12.700
Czech Republic	11.466	9.644
Romania	6.889	5.859
Slovak Republic	6.590	6.820
Republic of Cuba	1.644	1.702
Socialist Republic of Vietnam	1.126	1.165
Mongolia	1.041	1.077
	100.000	100.000

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

In its 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

Economic and political development of the Bank's member countries affects the activities of enterprises operating in these countries. Considering this fact, the Group performs its operations with reference to the local specifics of its member countries to ensure overall assessment and control of credit and operational risks.

The accompanying consolidated 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 Group. Future evolution of the conditions in which the Group operates may differ from the assessment made by the management for the purposes of these consolidated financial statements.

(Thousands of euros)

2. Basis of preparation

General

These consolidated financial statements of the Group have been prepared in accordance with International Financial Reporting Standards (“IFRS”) approved by the International Accounting Standards Board.

Subsidiary

As at 31 December 2018, the Bank is a parent company of the Group, which owns CJSC IIB Capital (the Bank’s 100% subsidiary) established in 2012 to deal with issues related to the IIB activities in Russia, including the provision of trustee services to the Bank. As at 31 December 2018, the authorized capital of the subsidiary amounted to RUB 44.5 thousand (31 December 2017: RUB 44.5 thousand), which is equivalent to EUR 1.1 thousand at the historical exchange rate at the date of establishment.

Basis of measurement

These consolidated 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, financial instruments at fair value through other comprehensive income, and buildings in the property and equipment and investment property are stated at revalued amounts.

Preparation and presentation of financial statements

The financial year of the Bank begins on 1 January and ends on 31 December.

Functional and presentation currency

The euro (“EUR”) is the Group’s functional and presentation currency 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 Group are denominated in EUR.

These consolidated financial statements are presented in thousands of euros (“thousands of euros” or “EUR thousand”), unless otherwise indicated.

3. Summary of accounting policies

Changes in accounting policies

The Group applied IFRS 15 and IFRS 9 for the first time. The nature and the impact of new accounting standards are described below.

The Group applied for the first time certain amendments to the standards, which are effective for annual periods beginning on or after 1 January 2018. The Group has not early adopted standards, interpretations or amendments that have been issued but are not yet effective. The nature and the impact of each amendment is described below:

IFRS 9 Financial Instruments

IFRS 9 replaces IAS 39 *Financial Instruments: Recognition and Measurement* and is effective for annual periods beginning on or after 1 January 2018. The Group has not restated comparative information for 2017 for financial instruments in the scope of IFRS 9. Therefore, the comparative data for 2017 is presented in accordance with IAS 39 and is not comparable to the information presented for 2018. Differences arising from the adoption of IFRS 9 have been recognized directly in equity as at 1 January 2018 and are disclosed below.

(Thousands of euros)

3. Summary of accounting policies (continued)

Changes in accounting policies (continued)

(a) Classification and measurement

Under IFRS 9, all debt financial assets that do not meet a “solely payment of principal and interest” (SPPI) criterion, are classified at initial recognition as financial assets at fair value through profit or loss (FVPL). According to this criterion, debt instruments that do not meet the definition of basic credit agreement (such as instruments with embedded conversion options or non-recourse loans) are measured at FVPL. For debt financial assets that meet the SPPI criterion, classification at initial recognition is determined based on the business model, under which these instruments are managed:

- ▶ Instruments that are managed on a “hold to collect” basis are measured at amortized cost;
- ▶ Instruments that are managed on a “hold to collect and for sale” basis are measured at fair value through other comprehensive income (FVOCI);
- ▶ Instruments that are managed on other basis will be measured at FVPL.

Equity financial assets are required to be classified at initial recognition as FVPL unless an irrevocable designation is made to classify the instrument as FVOCI. For equity investments classified as at FVOCI, all realized and unrealized gains and losses, except for dividend income, are recognized in other comprehensive income with no subsequent reclassification to profit and loss.

The classification and measurement of financial liabilities remain largely unchanged from the current IAS 39 requirements.

Derivatives will continue to be measured at FVPL.

(b) Impairment

The adoption of IFRS 9 fundamentally changes the Group’s accounting for allowances for expected credit losses by replacing the IAS 39 incurred loss approach with the forward-looking expected credit loss (“ECL”) approach.

Starting from 1 January 2018, the Group recognizes the provision for ECL for all loans and other debt financial instruments not measured at FVPL, as well as for loan commitments and financial guarantee contracts, which are collectively referred to as financial instruments in this section. According to IFRS 9, requirements for impairment are not applicable to equity instruments.

The allowance for ECL is based on credit losses expected to be incurred over the life of the underlying asset (lifetime ECL), if there has been a significant increase in credit risk since the date of initial recognition. Otherwise, the allowance for ECL will be equal to 12-month expected credit losses (12-month ECL). The 12 month ECL are part of lifetime ECL and represent ECL arising from defaults on the financial instrument expected to occur 12 months after the reporting date. The impairment model applied by the Bank is detailed in Note 25.

Before 30 June 2018, the Group accounted for hedging instruments in accordance with IAS 39. As at 30 June 2018, the accumulated hedging adjustments of the fair value included in the carrying amount of the hedged item and recognized in the consolidated statement of financial position amounted to EUR 16 thousand. From 1 July 2018, the Group decided to cease hedge accounting, since accounting at the amortized cost of the hedged item until maturity (September 2019) and the market revaluation of the hedging derivative correctly reflect the effect of the hedged item and hedging instrument on the consolidated statement of financial position and the consolidated statement of comprehensive income. Thus, adjustments of the fair value of the hedged item are no longer required. As at 31 December 2018, the amount of hedging adjustments in the consolidated statement of financial position is equal to zero.

(Thousands of euros)

3. Summary of accounting policies (continued)**Changes in accounting policies (continued)***(c) Effect of transition to IFRS 9*

The effect of IFRS 9 on the consolidated statement of financial position and retained earnings, including the effect from the replacement of the incurred credit loss model under IAS 39 with the ECL model under IFRS 9, is described below.

A reconciliation between the carrying amount under IAS 39 with the carrying amount under IFRS 9 as at 1 January 2018 is as follows:

<i>Financial assets</i>	<i>Notes</i>	<i>IAS 39 measurement</i>		<i>Reclassifi- cation</i>	<i>Difference (ECL)</i>	<i>Difference (other)</i>	<i>IFRS 9 measurement</i>	
		<i>Category</i>	<i>Amount</i>				<i>Amount</i>	<i>Category</i>
Cash and cash equivalents		L&R ¹	66,097	–	(8)	–	66,089	Amortized cost
Deposits with banks and other financial institutions		L&R	45,889	–	(241)	–	45,648	Amortized cost
Loans to banks – amortized cost		L&R	201,635	–	(8,848)	–	192,787	Amortized cost
Loans to customers – amortized cost		L&R	462,514	–	(18,542)	–	443,972	Amortized cost
<i>From: available-for-sale securities, including those pledged under repurchase agreements</i>		AFS ³	215,427	(215,427)	–	–	–	
<i>To:</i>								
Securities at fair value through other comprehensive income, including those pledged under repurchase agreements		AFS	–	175,065	(440)	440	175,065	FVOCI (debt instruments, investments)
Securities, including those pledged under repurchase agreements – equity securities at fair value through other comprehensive income		AFS	–	1,710	–	–	1,710	FVOCI (equity instruments)
Securities at amortized cost	A	AFS	–	38,652	–	1,649	40,301	Amortized cost
Financial assets		L&R	728	–	(6)	–	722	
Total assets			992,290	–	(28,085)	2,089	966,294	
Non-financial liabilities								
Allowances for expected credit losses on credit-related commitments			–	–	(864)	–	(864)	
Total liabilities			–	–	(864)	–	(864)	

¹ L&R – loans and receivables² HTM – held to maturity³ AFS – available for sale.

A As at 1 January 2018, the Group reclassified a part of its assets previously classified as “available for sale” to “debt instruments measured at amortized cost”. These instruments satisfied the SPPI criterion, were unquoted in an active market and held to collect related cash flows rather than for sale.

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(Thousands of euros)

3. Summary of accounting policies (continued)**Changes in accounting policies (continued)**

The impact of transition to IFRS 9 on reserves and retained earnings is as follows:

	<i><u>Reserves and retained earnings</u></i>
Revaluation reserve for securities at fair value through other comprehensive income (2017: Revaluation reserve for available-for-sale securities)	
Balance at the end of the period as per IAS 39 (31 December 2017)	240
Reclassification of debt securities from “available for sale” to “measured at amortized cost”	1,603
ECL recognized on debt financial assets at FVOCI as per IFRS 9	440
Balance at the beginning of the period as per IFRS 9 (1 January 2018)	2,283
Retained earnings	
Balance at the end of the period as per IAS 39 (31 December 2017)	66,788
Revaluation on reclassification of debt securities from “available for sale” to “measured at amortized cost”	46
ECL recognition under IFRS 9, including with respect to instruments at FVOCI	(28,949)
Balance at the beginning of the period as per IFRS 9 (1 January 2018)	37,885
Total change in equity due to the adoption of IFRS 9	(26,860)

The following table reconciles the allowance for impairment of financial assets and provisions for credit-related commitments, letters of credit and financial guarantees as defined by IAS 39 and IAS 37 as at 31 December 2017 with the allowances for expected credit losses as defined by IFRS 9 as at 1 January 2018.

	<i>31 December 2017</i>	<i>Revaluation</i>	<i>Foreign exchange</i>	<i>1 January 2018</i>
	<i>IAS 39 / IAS 37</i>	<i>under IFRS 9</i>	<i>differences</i>	<i>IFRS 9</i>
Allowance for impairment				
Cash and cash equivalents	–	8	–	8
Deposits with banks and other financial institutions	34,967	241	–	35,208
Securities at fair value through other comprehensive income (2017: Available-for-sale securities)	–	440	–	440
Loans to banks	9,153	8,848	–	18,001
Loans to customers	5,555	18,542	–	24,097
Financial assets	1,741	6	(12)	1,735
	51,416	28,085	(12)	79,489
Loan commitments	–	408	–	408
Letters of credit issued to customers	–	402	–	402
Financial guarantees	–	54	–	54
	–	864	–	864
	51,416	28,949	(12)	80,353

IFRS 15 Revenue from Contracts with Customers

IFRS 15, issued in May 2014 and amended in April 2016, establishes a new five-step model that will apply to revenue arising from contracts with customers. Under IFRS 15, revenue is recognized at an amount that reflects the consideration to which an entity expects to be entitled in exchange for transferring goods or services to a customer. The standard, however, does not apply to income related to financial instruments or leases, and therefore does not impact most of the Bank’s revenue, including interest revenue, gains/(losses) from operations with securities, lease income regulated by IFRS 9 *Financial Instruments* and IAS 17 *Leases*. As a result, a major part of the Group’s income is not affected by the adoption of this standard.

(Thousands of euros)

3. Summary of accounting policies (continued)

Changes in accounting policies (continued)

IFRIC 22 Foreign Currency Transactions and Advance Consideration

IFRIC 22 clarifies that, in determining the spot exchange rate to use on initial recognition of the related asset, expense or income (or part of it) on the derecognition of a non-monetary asset or non-monetary liability relating to advance consideration, the date of the transaction is the date on which an entity initially recognizes the non-monetary asset or non-monetary liability arising from the advance consideration. If there are multiple payments or receipts in advance, the entity shall determine a date of the transaction for each payment or receipt of advance consideration. This interpretation had no impact on the Bank's consolidated financial statements.

Amendments to IAS 40 Transfers of Investment Property

These amendments clarify the cases when an entity is required to transfer real estate, including real estate under construction or development, into or from the category of investment property. The amendments state that a change in use occurs when property begins or ceases to comply with the definition of investment property and there is evidence of a change in use. Any change in management's intentions regarding the use of the property itself does not indicate a change in its use. These amendments did not have any impact on the Group's consolidated financial statements.

IAS 28 Investments in Associates and Joint Ventures – Clarification that the Decision to Measure Investees at Fair Value through Profit or Loss Should Be Made Individually for Each Investment

These amendments clarify that an entity that is a venture capital organization, or other similar entity may decide to measure investments in associates and joint ventures at fair value through profit or loss. This decision is made individually for each investment.

If the entity that is not an investment entity itself has an interest in an associate or joint venture that are investment entities, when applying the equity method, such entity can retain the fair value measurement applied by its investment associate or joint venture to its interests in subsidiaries. This decision is made separately for each investment entity associate or joint venture, at the later of the date on which: (a) the investment entity associate or joint venture is initially recognized; (b) the associate or joint venture becomes an investment entity; and (c) the investment entity associate or joint venture first becomes a parent. These amendments had no impact on the Group's consolidated financial statements.

Foreign currency transactions

The consolidated financial statements are presented in euro, which is the Group'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 translated 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 consolidated income statement as "Net losses from operations with foreign currencies and derivatives". 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 losses from operations with foreign currencies and derivatives".

Basis of consolidation

Subsidiaries, which are those entities in which the Group has an interest of more than one half of the voting rights, or otherwise has power to exercise control over their operations, are consolidated. Subsidiaries are consolidated from the date on which control was transferred to the Group and are no longer consolidated from the date when control ceased. All intra-group transactions, balances and unrealized gains on transactions between Group companies are eliminated in full; unrealized losses are also eliminated unless the transaction provides evidence of an impairment of the asset transferred. Where necessary, the accounting policies of subsidiaries have been changed to ensure consistency with the accounting policies adopted by the Group.

(Thousands of euros)

3. Summary of accounting policies (continued)

Basis of consolidation (continued)

A change in the ownership interest of a subsidiary, without a loss of control, is accounted for as an equity transaction. Losses within a subsidiary are attributed to the non-controlling interest even if that results in a deficit balance.

If the Group loses control over a subsidiary, it derecognizes the assets (including goodwill) and liabilities of the subsidiary, the carrying amount of any non-controlling interests, the cumulative translation differences recorded in equity; recognizes the fair value of the consideration received, the fair value of any investment retained and any surplus or deficit in profit or loss and reclassifies the parent's share of components previously recognized in other comprehensive income to profit or loss.

Investments in associates

Associates are entities in which the Group generally has between 20% and 50% of the voting rights (interest), or is otherwise able to exercise significant influence, but which it does not control or jointly control. Investments in associates are accounted for under the equity method and is initially recognized at cost, including goodwill. Subsequent changes in the carrying value reflect the post-acquisition changes in the Group's share of net assets of the associate. The Group's share of its associates' profits or losses is recognized in the consolidated profit or loss, and its share of movements in reserves is recognized in other comprehensive income. However, when the Group's share of losses in an associate equals or exceeds its interest in the associate, the Group does not recognize further losses, unless the Group is obliged to make further payments to, or on behalf of the associate.

Unrealized gains on transactions between the Group and its associates are eliminated to the extent of the Group's interest in the associates; unrealized losses are also eliminated unless the transaction provides evidence of an impairment.

Fair value measurement

The Group measures financial instruments through FVPL and FVOCI and non-financial assets such as investment property, at fair value at each reporting date. Fair values of financial instruments measured at amortized cost are disclosed in Note 26.

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. Also, 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 Group. 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 the best and most effective way or by selling it to another market participant that would use the asset in the best and most effective way.

The Group 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 consolidated 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.

(Thousands of euros)

3. Summary of accounting policies (continued)

Fair value measurement (continued)

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

Financial assets and liabilities

Initial recognition

Date of recognition

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

Initial measurement

Classification of financial instruments upon initial recognition depends on contractual terms and the business model used for managing financial instruments. Financial instruments are initially measured at fair value, including transaction costs, except when financial instruments are measured at fair value through profit and loss.

Categories of measurement of assets and liabilities

From 1 January 2018, the Bank has classified all its financial assets on the basis of the business model used for asset managing and asset contractual terms as measured at:

- ▶ Amortized cost;
- ▶ Fair value through other comprehensive income (FVOCI);
- ▶ Fair value through profit or loss (FVPL).

The Group classifies and measures the derivatives and instruments held for trading at FVPL. The Group may at its discretion designate the financial instruments as measured at FVPL, if doing so eliminates or significantly reduces a measurement or recognition inconsistency.

Prior to 1 January 2018 the Group classified the financial assets into the following categories: loans and receivables (measured at amortized cost), assets measured at FVPL, and assets available for sale or held to maturity (measured at amortized cost).

Financial liabilities, except for loan commitments, reimbursement obligations, and financial guarantees are measured at amortized cost or at FVPL, if they are held for trading or derivatives, or the entity may designate them as measured at fair value.

Deposits with banks and other financial institutions, loans to banks, loans to customers, securities at amortized cost

Prior to 1 January 2018, deposits with banks and other financial institutions, loans to banks, loans to customers items included non-derivative financial assets with fixed or determinable payments not quoted in an active market, other than:

- ▶ Those that the Group intended to sell immediately or in the near term;
- ▶ Those that the Group at its discretion designated as measured at FVPL or as available for sale at initial recognition;
- ▶ Those for which the Group could collect the amount substantially less than the amount of its initial investment for reasons other than deterioration of the asset's credit quality. Such assets were classified as available for sale.

(Thousands of euros)

3. Summary of accounting policies (continued)

Financial assets and liabilities (continued)

From 1 January 2018, the Group measures deposits with banks and other financial institutions, loans to banks, loans to customers, and other financial investments at amortized cost, only when both of the following conditions are met:

- ▶ The financial asset is held under a business model designed to hold financial assets in order to collect contractual cash flows; and
- ▶ Contractual terms of a financial asset provide for the receipt on specified dates of cash flows that are solely payments of principal and interest on the principal amount outstanding (SPPI).

These terms are detailed below.

Business model assessment

The Group determines the business model at the level that reflects the best way to manage the financial assets arranged in groups to accomplish a certain business objective.

The Group's business model is assessed at the higher level of aggregated portfolio, rather than the separate instrument level, and is based on the observable factors, such as:

- ▶ The method to assess the business model performance and the profitability of financial assets held within this business model, and the way this information is communicated to the key management personnel of the entity;
- ▶ Risks that influence the business model performance (and the profitability of financial assets held within this business model) and, in particular, the way to manage these risks;
- ▶ The procedure to reward business managers (for example, whether the remuneration is based on the fair value of the managed assets or on the obtained contractual cash flows);
- ▶ The expected frequency, scope and timing of sales are also important factors in assessing the Group's business model.

The business model assessment is based on scenarios, the occurrence of which is reasonably probable, without regard to the so-called worst case or stressed scenarios. If the cash flows following the initial recognition were realized in a way different from the Group's expectations, the Group won't change the classification of the rest of financial assets held within this business model, however, in future the Group will take such information into account when measuring recently created or recently purchased financial assets.

"Solely payments of principal and interest on the principal amount outstanding" test (SPPI test)

During the second stage of classification, the Group assesses contractual terms of a financial asset to determine whether the contractual cash flows of the asset are solely payments of principal and interest on the principal amount outstanding (the so-called SPPI test).

For the purpose of this test, principal is the fair value of a financial asset at initial recognition, and it can be changed over the life of this financial asset (for example, if there are payments of principal or the amortization of premium/discount).

The most significant elements of interest as part of the loan agreement are usually the compensation for the time value of money and the credit risk. To conduct the SPPI test, the Group applies judgments and analyzes relevant factors, for example, the currency, in which the financial asset is denominated, and the period, for which the interest rate is set.

Simultaneously, the contractual terms, which had a negligible effect on risk exposures or volatility of contractual cash flows not related to the base loan agreement, don't give rise to the contractual cash flows, which are solely payments of principal and interest on the principal amount outstanding. In such cases the financial asset should be measured at FVPL.

(Thousands of euros)

3. Summary of accounting policies (continued)

Financial assets and liabilities (continued)

Debt instruments at FVOCI

From 1 January 2018, according to IFRS 9, the Group applies a new category and measures debt instruments at FVOCI, if both of the following conditions are met:

- ▶ The instrument is held within a business model which objective is achieved by both collecting contractual cash flows and selling financial assets; and
- ▶ Contractual terms of the financial assets comply with the SPPI test.

Debt instruments at FVOCI are subsequently measured at fair value, and gains or losses from changes in the fair value are recognized in OCI. Interest revenue and gains or losses from the change in exchange rates are recognized in profit or loss in the same manner as in the case of financial assets at amortized cost. In the process of derecognition the cumulative gain or loss, previously recognized in OCI, are reclassified from OCI to profit or loss.

ECL on debt instruments at FVOCI won't decrease the carrying amount of these financial assets in the statement of financial position that continue to be measured at fair value. Instead, the amount equal to the allowance for expected losses that would be created when measuring the asset at amortized cost, is recognized in OCI as the cumulative amount of the impairment with the recognition of corresponding amounts in profit or loss. The cumulative amount of losses recognized in OCI is reclassified to profit or loss when the asset is derecognized.

Equity instruments at FVOCI

From 1 January 2018, the Group sometimes at initial recognition of some investments in equity instruments makes an irrevocable decision to reclassify investments in equity instruments at FVOCI if they meet the definition of an equity instrument according to IAS 32 *Financial Instruments: Presentation* and are not held for trading. Such classification decision is adopted for each instrument separately.

Gains and losses from such equity instruments are never reclassified to profit or loss. Dividends are recognized in profit or loss as other income, when the right for dividends is established, except where the Group obtains benefits from such receipts as the partial reimbursement of the instrument cost. In such case, the profit is recognized in OCI. Equity instruments at FVOCI are not tested for impairment. When such instruments are disposed, the accumulated revaluation reserve is transferred to retained earnings.

Financial guarantees, letters of credit and loan commitments

The Group issues guarantees, letters of credit and loan commitments.

Financial guarantees are initially recognized in the financial statements at fair value in the amount of the premium received. Subsequent to initial recognition, the Group measures its liability under each guarantee at the higher of the initially recognized amount less accumulated amortization recognized in the separate income statement, and, according to IAS 37 (prior to 1 January 2018), the best estimate of expenditure required to settle any financial obligation arising as a result of the guarantee, or, according to IFRS 9 (from 1 January 2018), of allowance for ECL.

Commitments to extend credit and letters of credit are contractual commitments, pursuant to which over the life of the commitment the Group undertakes to issue a loan to the client on previously specified terms. Similar to financial guarantees, in accordance with IAS 39, if such instruments were onerous, a reserve for them was made, however, from 1 January 2018 requirements related to measuring ECL are applied to such commitments.

Liability guarantees

Liability guarantees are agreements providing for a compensation if the other party to the agreement fails to fulfill its contractual liability. Liability guarantees do not transfer credit risk. Risk under the contract with a liability guarantee is the possibility that the other party fails to fulfill its contractual liability. Accordingly, liability guarantees are not financial instruments and, therefore, are outside the scope of IFRS 9.

(Thousands of euros)

3. Summary of accounting policies (continued)

Financial assets and liabilities (continued)

Held-to-maturity investments

Prior to 1 January 2018, non-derivative financial assets with fixed or determinable payments and fixed maturity are classified as held to maturity when the Group has the positive intention and ability to hold them to maturity. Investments intended to be held for an undefined period were not included in this category. Held-to-maturity investments were subsequently measured at amortized cost. Gains and losses were recognized in profit or loss when the investments are impaired, as well as through the amortization process.

Loans and receivables

Prior to 1 January 2018, loans and receivables were non-derivative financial assets with fixed or determinable payments that were not quoted in an active market. They were not entered into with the intention of immediate or short-term resale and were not classified as trading securities or designated as investment securities available for sale. Such assets were carried at amortized cost using the effective interest method. Gains and losses were recognized in profit or loss when such assets were derecognized or impaired, as well as through the amortization process.

Available-for-sale financial assets

Prior to 1 January 2018, available-for-sale financial assets were those non-derivative financial assets that were designated as available-for-sale or were not classified in any of the three preceding categories. After initial recognition available-for-sale financial assets were measured at fair value with gains or losses being recognized in other comprehensive income until the investment was derecognized or until the investment was determined to be impaired. In this case, the cumulative gain or loss previously reported in other comprehensive income was reclassified to the separate income statement. However, interest calculated using the effective interest method was recognized in profit or loss.

Reclassification of financial assets and liabilities

From 1 January 2018, the Group does not reclassify financial assets after the initial recognition, apart from exceptional cases, when the Group changes the business model for managing the financial assets. Financial liabilities are never reclassified. In 2017, the Group did not reclassify financial assets and liabilities.

Cash and cash equivalents

Cash and cash equivalents include cash in 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.

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 consolidated statement of financial position and in case the transferee has the right by contract or custom to sell or repledge them, reclassified as investment securities pledged under sale and repurchase agreements. The corresponding liabilities are presented within amounts due to credit institutions or customers. Securities purchased under agreements to resell (“reverse repo”) are recorded as cash equivalents, deposits with banks and other financial institutions as appropriate. The difference between sale and repurchase price is treated as interest and accrued over the life of repo agreements using the effective interest method.

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

(Thousands of euros)

3. Summary of accounting policies (continued)

Derivative financial instruments

In the normal course of business, the Group 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 from operations with these instruments are included in the consolidated income statement as “Net losses from operations with foreign currencies and derivatives”.

Embedded derivative is a part of a hybrid contract that also includes a non-derivative host contract, as a result of which some cash flows from the combined instrument change in the same manner as in the case of a separate derivative. An embedded derivative determines the change of some or all cash flows, which otherwise would have been determined by the contract, pursuant to the negotiated interest rate, financial instrument price, price of goods, foreign currency exchange rate, price or interest rate index, credit rating or credit index or other variables, provided that in case of a non-financial variable, such non-financial variable does not specifically relate to any of the contractual parties. A derivative, which is linked to the financial instrument, however, pursuant to contract can be transferred regardless of such instrument or entered into with another counterparty, is not embedded, but a separate financial instrument.

According to IAS 39 derivatives embedded in financial assets, liabilities and non-financial host contracts, were carried separately and recognized at fair value, if they met the definition of a derivative financial instrument (see above), their risks and characteristics were not closely linked to those of the host contracts and the host contracts were not held for sale and were not measured at FVPL. The embedded derivatives separated from the host contract were carried at fair value in the trading portfolio with changes in fair value recognized in the consolidated income statement.

From 1 January 2018, the date, when IFRS 9 became effective, the Bank carries derivatives embedded in financial liabilities and non-financial host contracts in the same manner. Financial assets are classified on the basis of the business model and SPPI test assessment.

Hedge accounting

To manage the risks associated with fluctuations in cash flows from receipt and payment of interest, as well as with fluctuations in the fair value of certain items, the Group uses derivative financial instruments. As a result, the Group applies hedge accounting for transactions that meet specified criteria.

At inception of the hedge relationship, the Group documents the relationship between the hedged item and the hedging instrument, including the nature of the risk, the objective and strategy for undertaking the hedge and the method that will be used to assess the effectiveness of the hedging relationship.

At each hedge effectiveness assessment date, a hedge relationship must be expected to be highly effective on a prospective basis and demonstrate that it was highly effective (retrospective effectiveness) for the designated period in order to qualify for hedge accounting. A formal assessment is undertaken both at inception and at each month end on an ongoing basis. A hedge is expected to be highly effective if the changes in fair value or cash flows attributable to the hedged risk during the period for which the hedge is designated will be offset by the hedging instrument in a range of 80% to 125%.

Fair value hedges

For designated and qualifying fair value hedges, the change in the fair value of a hedging derivative is recognized in the consolidated income statement in “Net losses from operations with foreign currencies and derivatives”. Meanwhile, the change in the fair value of the hedged item attributable to the risk hedged is recorded as an adjustment of the carrying value of the hedged item in the consolidated income statement in “Net losses from operations with foreign currencies and derivatives”.

If the hedging instrument expires or is sold, terminated or exercised, or where the hedge no longer meets the criteria for hedge accounting, the hedge relationship is terminated. For hedged items recorded at amortized cost, using the effective interest rate method, when the hedge ceases, the adjustment of the carrying amount of the hedged financial instrument is amortized over the remaining period until date of maturity of the hedged financial instrument. If the hedged item is derecognized, the unamortized fair value adjustment is recognized immediately in the consolidated statement of profit or loss.

(Thousands of euros)

3. Summary of accounting policies (continued)

Hedge accounting (continued)

Cash flow hedges

For designated and qualifying cash flow hedges, the effective portion of the cumulative gain or loss on the hedging instrument is initially recognized in consolidated other comprehensive income and is recorded through other comprehensive income. An ineffective portion of the gain or loss on the hedging instrument is recognized in the consolidated income statement.

When a hedging instrument expires, is sold, terminated, exercised, or when a hedge no longer meets the criteria for hedge accounting, the total amount of income or expense accumulated at that time in equity is transferred from equity and recognized in the consolidated income statement in the same period or periods during which hedged projected cash flows affect profit or loss.

When a forecast transaction is no longer expected, the cumulative gain or loss recognized in equity is immediately transferred to the income statement.

Borrowings

Issued financial instruments or their components are classified as liabilities, where the substance of the contractual arrangement results in the Group 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 banks and other financial institutions, long-term loans of banks and debt securities issued. 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 – Group as lessee

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

Operating lease – Group as lessor

The Group presents assets subject to operating leases in the consolidated statement of financial position according to the nature of the asset. Lease income from operating leases is recognized in the consolidated 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 value of the leased asset.

Offsetting of financial instruments

Financial assets and liabilities are offset and the net amount is reported in the consolidated 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. The right of offsetting must not be contingent on a future event and should be legally enforceable in all the following circumstances:

- ▶ In the normal course of business;
- ▶ In case of default; and
- ▶ In the event of insolvency or bankruptcy of the entity or any of its counterparties.

This is not generally the case with master netting agreements, and the related assets and liabilities are presented gross in the consolidated statement of financial position.

(Thousands of euros)

3. Summary of accounting policies (continued)

Renegotiated loans

Where possible, the Group 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.

From 1 January 2018, the Group derecognizes a financial asset, e.g. a loan to a customer, if the related contractual terms are renegotiated to the extent that it in fact becomes a new loan, and records the difference in gains or losses arising from derecognition before impairment loss is recognized. The newly recognized loans are classified as Stage 1 for ECL measurement purposes, unless the new loan is deemed to be POCL.

When assessing, whether the loan to customer should be derecognized, the Bank considers the following:

- ▶ The change in the currency of a loan;
- ▶ The change of a counterparty;
- ▶ Whether the modification results in the non-compliance of the instrument to the SPPPI test criteria.

If the modification does not imply a substantial change in cash flows, such modification does not result in a derecognition. Based on the changes in cash flows discounted at the original EIR, the Group recognizes gains or losses from the modification that are recorded within interest income calculated using the effective interest rate method in the consolidated income statement before impairment loss is recognized.

If the modification does not result in derecognition, the Group also reassesses the significant increase in credit risk or the need to classify assets as credit-impaired. After the designation of an asset as credit-impaired as a result of modification, it remains within Stage 3 for a probation period of at least 6 months. To transfer a renegotiated loan from Stage 3, regular payments of insignificant amounts of principal or interest are needed during at least half of the probation period in accordance with the modified payment schedule.

Impairment of financial assets

Prior to 1 January 2018, at each reporting date the Group individually assessed whether there is any objective evidence of impairment of a financial asset. A financial asset 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 might include indications that the debtor was experiencing significant financial difficulty, default or delinquency in interest or principal payments, the probability that they would enter bankruptcy or other financial reorganization and observable data indicating that there was a measurable decrease in the estimated future cash flows, such as changes in payment status or economic conditions that correlate with defaults. In case of available-for-sale financial instruments, a significant or prolonged decline in the fair value of the investment below its cost, was also the indicator of impairment.

If there was objective evidence that an impairment loss had been incurred, the amount of the loss was measured as the difference between the asset's carrying amount and the present value of estimated future cash flows (excluding future credit losses that had not been incurred) discounted at the financial asset's original effective interest rate or the difference between the original cost of the investment and its fair value in case of available-for-sale financial assets. The carrying value of the asset was reduced and the amount of the loss was recognized in profit or loss. Interest income continued to be accrued on the reduced carrying amount based on the original effective interest rate of the asset or at the interest rate used to discount the future cash flows for the purpose of measuring the impairment loss in case of available-for-sale financial assets. Assets together with the associated allowance were written off when there was no realistic prospect of future recovery and all collateral had been realized or had been transferred to the Group. If, in a subsequent year, the amount of the estimated impairment loss decreased because of an event occurring after the impairment had been recognized, the previously recognized impairment loss was credited to the separate income statement, except for increases in fair value of impaired available-for-sale equity investments, which were recognized in other comprehensive income.

Information on the impairment measurement according to IFRS 9 is provided in Note 25.

(Thousands of euros)

3. Summary of accounting policies (continued)

Derecognition of financial assets and liabilities

Financial assets

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

- ▶ The rights to receive cash flows from the asset have expired;
- ▶ The Group 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 Group 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 Group 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 Group’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 Group 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 Group’s continuing involvement is the amount of the transferred asset that the Group 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 Group’s continuing involvement is limited to the lower of the fair value of the transferred asset and the option exercise price.

Write-off

From 1 January 2018, financial assets are written off in part or in full, only when the Group does not expect to recover their value. If the amount to be written off is higher than the accumulated allowance for impairment, the difference is at first recorded as the increase in the allowance that is subsequently applied to the gross carrying amount. All the subsequent reversals are recognized as credit loss expenses. The write-off relates to the derecognition.

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 profit or loss.

Property and equipment

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

The carrying amount of property and equipment is reviewed for impairment when events or changes in circumstances indicate that the carrying amount 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.

*(Thousands of euros)***3. Summary of accounting policies (continued)****Property and equipment (continued)**

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 recognized in other comprehensive income, except to the extent that it reverses a revaluation decrease of the same asset previously recognized in the consolidated income statement, in which case the increase is taken to the financial result. A revaluation deficit is recognized in the consolidated 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 consolidated 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 depreciation 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 includes a part of building held to earn rental income or for capital appreciation and which is not used by the Group 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 Group'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.

Investment property that is being redeveloped for continuing use as investment property or for which the market has become less active continues to be measured at fair value.

Earned rental income is recorded in the consolidated income statement within "Income from lease of investment property". Gains and losses resulting from changes in the fair value of investment property are recorded in the consolidated income statement and presented within gains/losses from revaluation of investment property.

Subsequent expenditure is subject to capitalization only when it is probable that future economic benefits associated with an asset will flow to the Group 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.

*(Thousands of euros)***3. Summary of accounting policies (continued)****Intangible assets**

Intangible assets of the Group have definite useful life and mainly include capitalized computer software. Intangible assets that have been acquired and recorded are capitalized based on costs incurred to acquire and bring to use these intangible assets. Following initial recognition, intangible assets are carried at acquisition cost less any accumulated amortization and any accumulated impairment losses. Intangible assets are amortized using the straight-line method and assessed for impairment whenever there is an indication that the intangible asset may be impaired. Amortization is calculated on a straight-line basis over the following estimated useful lives:

	<u>Years</u>
Automated banking system	20
Other computer software	1-5

Assets classified as held for sale

The Group 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 Group'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.

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 assets as held for sale.

The Group measures an asset classified as held for sale at the lower of its carrying amount and fair value less costs to sell. The Group 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 Group 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.

Fiduciary assets

Assets held in a fiduciary capacity are not reported in the consolidated financial statements, as they are not the assets of the Bank.

Segment reporting

The Group's segment reporting is based on the following operating segments: credit and investment activity, treasury, other activities.

(Thousands of euros)

3. Summary of accounting policies (continued)

Contingencies

Contingent liabilities are not recognized in the consolidated 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 consolidated statement of financial position but disclosed when an inflow of economic benefits is probable.

Recognition of income and expenses

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

Interest and similar income and expense

From 1 January 2018, the Group calculates the interest revenue on debt financial assets at amortized cost or at FVOCI, applying the effective interest rate to the gross carrying amount of financial assets, except for credit-impaired assets (prior to 1 January 2018: applying the effective interest rate to the amortized cost of financial assets). Effective interest rate 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 Group 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 revenue or expenses.

In case of a credit-impaired financial asset, the Group calculates the interest revenue, applying the effective interest rate to the net amortized cost of this asset.

If the default on the financial asset is liquidated, and it is no longer a credit-impaired asset, the Group proceeds to calculate the income revenue on the basis of the gross carrying amount.

The interest revenue for all financial assets at FVPL is recognized with the use of a contractual interest rate in "Other interest income" in the consolidated income statement.

Fee and commission income

The Group 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. 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 expense comprises 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 consolidated 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.

(Thousands of euros)

3. Summary of accounting policies (continued)

Recognition of income and expenses (continued)

Dividend income

Dividend income is recognized when the Group's right to receive the payment is established.

Standards issued but not yet effective

The standards and interpretations that are issued, but not yet effective, up to the date of issuance of the Group's consolidated financial statements are disclosed below. The Group intends to adopt these standards when they become effective.

IFRS 16 Leases

IFRS 16 was issued in January 2016 and it replaces IAS 17 *Leases*, IFRIC 4 *Determining whether an Arrangement Contains a Lease*, SIC-15 *Operating Leases – Incentives* and SIC-27 *Evaluating the Substance of Transactions Involving the Legal Form of a Lease*. IFRS 16 sets out the principles for the recognition, measurement, presentation and disclosure of leases and requires lessees to account for all leases under a single on-balance sheet model similar to the accounting for finance leases under IAS 17. The standard includes two recognition exemptions for lessees – leases of 'low-value' assets (e.g., personal computers) and short-term leases (i.e., leases with a lease term of 12 months or less). At the commencement date of a lease, a lessee will recognise a liability to make lease payments (i.e., the lease liability) and an asset representing the right to use the underlying asset during the lease term (i.e., the right-of-use asset). Lessees will be required to separately recognise the interest expense on the lease liability and the depreciation expense on the right-of-use asset.

Lessees will be also required to remeasure the lease liability upon the occurrence of certain events (e.g., a change in the lease term, a change in future lease payments resulting from a change in an index or rate used to determine those payments). The lessee will generally recognise the amount of the remeasurement of the lease liability as an adjustment to the right-of-use asset.

Lessor accounting under IFRS 16 is substantially unchanged from today's accounting under IAS 17. The Group is a lessor only and will continue to classify all leases using the same classification principle as in IAS 17.

In addition, IFRS 16, which becomes effective for annual periods beginning on 1 January 2019, requires that lessors and lessees provide more detailed disclosures as compared with IAS 17.

IFRS 17 Insurance Contracts

In May 2017, the IASB issued IFRS 17 *Insurance Contracts* (IFRS 17), a comprehensive new accounting standard for insurance contracts covering recognition and measurement, presentation and disclosure. Once effective, IFRS 17 will replace IFRS 4 *Insurance Contracts* (IFRS 4) that was issued in 2005. IFRS 17 applies to all types of insurance contracts (i.e., life, non-life insurance, direct insurance and re-insurance) regardless of the type of entities that issues them, as well as to certain guarantees and financial instruments with discretionary participation features. A few scope exceptions will apply. The overall objective of IFRS 17 is to provide an accounting model for insurance contracts that is more useful and consistent for insurers. In contrast to the requirements in IFRS 4, which are largely based on grandfathering previous local accounting policies, IFRS 17 provides a comprehensive model for insurance contracts, covering all relevant accounting aspects. The core of IFRS 17 is the general model, supplemented by:

- ▶ Certain modifications related to insurance contracts with direct participation features (variable compensation method);
- ▶ A simplified approach (the premium allocation approach) mainly for short-duration contracts.

IFRS 17 is effective for reporting periods beginning on or after 1 January 2021, with comparative figures required. Early adoption is permitted, provided the entity also applies IFRS 9 and IFRS 15 on the date of the first application. This standard is not applicable to the Group.

(Thousands of euros)

3. Summary of accounting policies (continued)

Standards issued but not yet effective (continued)

IFRIC 23 Uncertainty over Income Tax Treatments

The interpretation addresses the accounting for income taxes when tax treatments involve uncertainty that affects the application of IAS 12 and does not apply to taxes or levies outside the scope of IAS 12, nor does it specifically include requirements relating to interest and penalties associated with uncertain tax treatments. In particular, the interpretation addresses the following issues:

- ▶ Whether the entity considers uncertain tax treatments separately;
- ▶ The assumptions that the entity makes with regard to the review of tax treatments by tax authorities;
- ▶ How the entity determines taxable profit (tax loss), tax base, unused tax losses, unused tax benefits and tax rates;
- ▶ How the entity considers changes in facts and circumstances.

An entity must determine whether to consider each uncertain tax treatment separately or together with one or more other uncertain tax treatments. The approach that better predicts the resolution of the uncertainty should be followed. The interpretation is effective for annual periods beginning on or after 1 January 2019. The Group will apply the interpretation from its effective date. Since the Bank is exempt from any national or local direct taxes or duties Pursuant to the Agreement on the Establishment, the interpretation will have no impact on the Group's consolidated financial statements.

Amendment to IFRS 9 Prepayment Features with Negative Compensation

Under IFRS 9, a debt instrument can be measured at amortized cost or at fair value through other comprehensive income, provided that the contractual cash flows are “solely payments of principal and interest on the principal amount outstanding” (the SPPI test) and the instrument is held within the appropriate business model for that classification. The amendments to IFRS 9 clarify that a financial asset passes the SPPI test regardless of the event or circumstance that causes the early termination of the contract and irrespective of which party pays or receives reasonable compensation for the early termination of the contract.

The amendments are applied retrospectively and become effective for annual periods beginning on 1 January 2019. Early adoption permitted. These amendments do not have any impact on the Group's consolidated financial statements.

Amendments to IFRS 10 and IAS 28 Sale or Contribution of Assets between an Investor and its Associate or Joint Venture

The amendments address the conflict between IFRS 10 and IAS 28 in dealing with the loss of control of a subsidiary that is sold or contributed to an associate or joint venture. The amendments clarify that the gain or loss resulting from the sale or contribution of assets that constitute a business, as defined in IFRS 3, between an investor and its associate or joint venture, is recognized in full. Any gain or loss resulting from the sale or contribution of assets that do not constitute a business, however, is recognized only to the extent of unrelated investors' interests in the associate or joint venture. The IASB has deferred the effective date of these amendments for an indefinite term, but an entity that early adopts the amendments must apply them prospectively.

The Group will apply these amendments when they become effective.

Amendments to IAS 19 Plan Amendment, Curtailment or Settlement

Amendments to IAS 19 address the accounting when a plan amendment, curtailment or settlement occurs during the reporting period. These amendments clarify that if a plan amendment, curtailment or settlement occurs during the reporting period, the entity is:

- ▶ To determine current service cost applicable to the remaining part of the period after the plan amendment, curtailment or settlement, based on the actuarial assumptions used for the revaluation of a net liability (asset) under the defined benefit plan, reflecting the consideration under the plan and assets of the plan after this event;
- ▶ To determine the net interest applicable to the remaining part of the period after the plan amendment, curtailment or settlement with the use of a net liability (asset) under the defined benefit plan, reflecting the consideration under the plan and assets of the plan after this event; and the discount rate used to remeasure this net liability (asset) under the defined benefit plan.

(Thousands of euros)

3. Summary of accounting policies (continued)

Standards issued but not yet effective (continued)

The amendments also clarify that the entity is to determine firstly the past service cost or gain/loss on settlement under this plan, not taking into consideration the impact of the asset ceiling. Such amount is recognized in profit or loss. Then the entity must determine the impact of the asset ceiling after the plan amendment, curtailment or settlement. Any change in this impact, except for amounts included in the net interest is recognized in other comprehensive income.

These amendments are applied to the plan amendment, curtailment or settlement, which occurred on the date of or after the beginning of the first annual period on or after 1 January 2019. Early adoption is permitted. These amendments will be applied to the Group's future plan amendment, curtailment or settlement.

Amendments to IAS 28 Long-Term Interests in Associates and Joint Ventures

The amendments clarify that an entity applies IFRS 9 to long-term investments in an associate or joint venture to which the equity method is not applied but that, in substance, form part of the net investment in the associate or joint venture (long-term investments). This clarification is important as it implies that the expected credit losses model is applied to such long-term investments in IFRS 9.

The amendments also clarify that, in applying IFRS 9, an entity does not take into account any losses of the associate or joint venture, or any impairment losses on the net investment, recognized as adjustments to the net investment in the associate or joint venture that arise from applying IAS 28 *Investments in Associates and Joint Ventures*.

These amendments are effective retrospectively for annual periods beginning on or after 1 January 2019. Early adoption is permitted. Since the Group does not have such long-term investments in an associate or a joint venture, these amendments will not have any impact on its consolidated financial statements.

Annual improvements 2015-2017 cycle (issued in December 2017)

IFRS improvements include the following amendments:

IFRS 3 Business Combinations

The amendments clarify that if the entity obtains control over the business that is a joint operation, it must apply requirements towards business combinations achieved in stages, including the revaluation of previously existing interests in assets and liabilities of a joint operations at fair value. Simultaneously, the acquirer must remeasure all the previously existing interest in joint operations.

The entity must apply these amendments to business combinations, the date of which coincides with or occurs after the beginning of the first annual period on or after 1 January 2019. Early adoption is permitted. These amendments will be applied to the Group's future business combinations.

IFRS 11 Joint Arrangements

A party that participates in (but does not have joint control over a joint operation) may obtain joint control over joint operations that comprise the activities defined as business in IFRS 3. The amendments clarify that in such cases the previously held interests in this joint operation are not remeasured.

The entity must apply these amendments to transactions, which provide for obtaining joint control, and the date of which coincides with or occurs after the beginning of the first annual period on or after 1 January 2019. Early adoption is permitted. Currently, these amendments are not applicable to the Group, however, they can be applicable to transactions in future.

IAS 12 Income Taxes

The amendments clarify that income tax consequences of dividends are to a greater extent related to past operations or events that generated the distributable profits than to distributions among owners. Therefore, an entity must recognize income tax consequences of dividends in profit or loss, other comprehensive income or equity, depending on where the entity recognized the originating past operations or events.

(Thousands of euros)

3. Summary of accounting policies (continued)

Standards issued but not yet effective (continued)

An entity must apply these amendments for annual periods beginning on or after 1 January 2019. Early adoption is permitted. On initial application of these amendments, an entity must apply them to income tax consequences of dividends recognized on or after the beginning of the earliest comparative period. Since pursuant to the Agreement on the Establishment, the Bank is exempt from any national or local direct taxes or duties, the clarification will have no impact on the Bank's consolidated financial statements.

IAS 23 Borrowing Costs

The amendments clarify that an entity must record specific borrowings related to the purchase of a qualifying asset, received as part of general borrowings, when almost all works required to prepare this asset for its intended use or sale are completed.

An entity must apply these amendments to borrowing costs incurred on or after the beginning of the annual reporting period in which an entity first applies these amendments. An entity must apply these amendments for annual periods beginning on or after 1 January 2019. Early adoption is permitted. Since the Group's current practice is in line with the requirements of the amendments, these amendments are not expected to have any impact on the Group's consolidated financial statements.

4. Significant accounting judgments and estimates

Assumptions and estimation uncertainty

In the process of applying the Group'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 consolidated financial statements, which have the most significant effect on the amounts recognized in the consolidated financial statements and the carrying amount of assets and liabilities in the following financial year. Estimates and assumptions are continuously assessed on the basis of management experience and other factors, including expectations of future events that are believed to be reasonable under the circumstances.

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

- ▶ Note 7 – Derivative financial instruments;
- ▶ Note 8 – Securities at fair value through other comprehensive income;
- ▶ Note 10 – Loans to banks;
- ▶ Note 11 – Loans to customers;
- ▶ Note 12 – Investment property;
- ▶ Note 13 – Property, equipment and intangible assets;
- ▶ Note 20 – Commitments and contingencies.

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(Thousands of euros)

4. Significant accounting judgments and estimates (continued)**Reclassification of comparative information**

The Group changed the presentation of line items in the consolidated income statement and the consolidated statement of cash flows for the year ended 31 December 2017. The following reclassifications have been made to 2017 balances to correspond to the 2018 presentation:

	<i>As previously reported</i>	<i>Reclassification amount</i>	<i>After reclassification</i>
Line item in the consolidated income statement			
Net gains/(losses) from operations with foreign currencies and derivatives	15,949	(18,390)	(2,441)
Other interest income	–	19,932	19,932
Other interest expenses	–	(1,542)	(1,542)
Reversal of allowance for impairment of other assets	27	(27)	–
Net charge of allowance for credit losses on financial instruments	(12,165)	27	(12,138)
Line item in the consolidated statement of cash flows			
Interest paid	(26,212)	15,453	(10,759)
Realized gains less losses from operations with foreign currencies and derivatives	31,228	(15,453)	15,775

5. Cash and cash equivalents

Cash and cash equivalents comprise:

	<i>31 December 2018</i>	<i>31 December 2017</i>
Cash on hand	276	85
Nostro accounts with banks and other financial institutions		
<i>Credit rating from A- to A+</i>	39,024	49,120
<i>Credit rating from BBB- to BBB+</i>	5,730	4,167
<i>Credit rating from BB- to BB+</i>	1,149	274
Total nostro accounts with banks and other financial institutions	45,903	53,561
Short-term deposits with banks		
Term deposits with banks		
<i>Credit rating from A- to A+</i>	3,061	–
<i>Credit rating BBB-</i>	–	68
<i>Credit rating from BB- to BB+</i>	–	12,383
Total short-term deposits with banks	3,061	12,451
Less: allowance for impairment	–	–
Cash and cash equivalents	49,240	66,097

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

(Thousands of euros)

5. Cash and cash equivalents (continued)

Movements in the gross carrying amount and respective ECL related to nostro accounts with banks and other financial institutions and short-term deposits with banks for the year ended 31 December 2018 are as follows:

<i>Cash equivalents</i>	<i>Stage 1</i>	<i>Total</i>
Carrying amount at 1 January 2018, gross	66,012	66,012
New assets purchased or originated	4,969,970	4,969,970
Assets derecognized or redeemed (excluding write-offs)	(4,985,091)	(4,985,091)
Foreign exchange differences	(1,927)	(1,927)
At 31 December 2018	48,964	48,964
Allowance for ECL at 1 January 2018		8
New assets purchased or originated		58
Assets derecognized or redeemed		(66)
Allowance for ECL at 31 December 2018		—

6. Deposits with banks and other financial institutions

Deposits with banks and other financial institutions are presented based on contractual terms and include the following items:

	<i>31 December 2018</i>	<i>31 December 2017</i>
Term deposits up to 1 year		
<i>Credit rating from B- to B+</i>	—	37,157
Total term deposits up to 1 year	—	37,157
Term deposits over 1 year		
<i>Credit rating from AA- to AA+</i>	900	—
<i>Credit rating from A- to A+</i>	24,180	5,650
<i>Credit rating from BBB- to BBB+</i>	16,876	—
<i>Credit rating from BB- to BB+</i>	5,440	3,082
Total term deposits over 1 year	47,396	8,732
Less: allowance for impairment	—	—
Deposits with banks and other financial institutions	47,396	45,889

Movements in the gross carrying amount and respective ECL related to deposits with banks and other financial institutions for the year ended 31 December 2018 are as follows:

<i>Deposits with banks and other financial institutions</i>	<i>Stage 1</i>	<i>Total</i>
Carrying amount at 1 January 2018, gross	45,889	45,889
New assets purchased or originated	131,413	131,413
Assets derecognized or redeemed (excluding write-offs)	(129,383)	(129,383)
Foreign exchange differences	(523)	(523)
At 31 December 2018	47,396	47,396
Allowance for ECL at 1 January 2018		241
New assets purchased or originated		—
Assets derecognized or redeemed		(241)
Allowance for ECL at 31 December 2018		—

As at 31 December 2018, EUR 34,967 thousand (31 December 2017: EUR 34,967 thousand) were due to the Group from the Central Bank of Cuba. This amount was fully provisioned (31 December 2017: EUR 34,967 thousand).

(Thousands of euros)

6. Deposits with banks and other financial institutions (continued)**Concentration of deposits with banks and other financial institutions**

As at 31 December 2018, besides deposits with the Central Bank of Cuba, the Group had four counterparties (31 December 2017: three counterparties) accounting for over 10% of the Group's total deposits with banks and other financial institutions. As at 31 December 2017, deposits with these counterparties amounted to EUR 42,956 thousand (31 December 2017: EUR 25,724 thousand); those deposits were not provisioned (31 December 2017: the deposits were not provisioned).

7. Derivative financial instruments

The Group performs operations with currency and other derivative financial instruments which are generally traded in an over-the-counter market with professional market counterparties on standardized contractual terms and conditions. Derivative financial instruments have either potentially favorable terms (and are assets) or potentially unfavorable conditions (and are liabilities) as a result of fluctuations in exchange rates or other variable factors associated with these instruments. The fair value of derivative financial instruments can vary significantly depending on the potentially favorable and unfavorable conditions. The table below shows the fair value of derivative financial instruments as at 31 December 2018 and 31 December 2017 and notional amounts of term contracts for the purchase and sale of foreign currency specifying contractual exchange rates.

	<i>31 December 2018</i>				
	<i>Nominal amount</i>		<i>Weighted average exchange rate</i>	<i>Fair value</i>	
	<i>Purchase</i>	<i>Sale</i>		<i>Assets</i>	<i>Liabilities</i>
Derivative financial assets and liabilities at fair value through profit or loss					
Swaps	RUB 11,997,998 thousand	EUR 185,875 thousand	64.73	–	32,810
	RON 757,800 thousand	EUR 166,289 thousand	4.56	2,091	3,925
	EUR 184,595 thousand	USD 216,924 thousand	1.18	28	5,049
	EUR 15,139 thousand	HUF 4,760,000 thousand	314.42	409	137
	EUR 4,512 thousand	RON 21,000 thousand	4.65	–	190
	EUR 53,833 thousand	RUB 4,116,000 thousand	76.46	561	–
	HUF 3,970,000 thousand	EUR 12,389 thousand	320.45	–	1
	CZK 750,000 thousand	EUR 29,503 thousand	25.42	631	–
	RUB 3,000,000 thousand	USD 52,910 thousand	56.70	–	7,779
Forwards	EUR 34,000 thousand	USD 40,140 thousand	1.18	–	1,052
Total derivative financial assets and liabilities at fair value through profit or loss				3,720	50,943
Derivative financial instruments				3,720	50,943

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(Thousands of euros)

7. Derivative financial instruments (continued)

	<i>31 December 2017</i>				
	<i>Nominal amount</i>		<i>Weighted average exchange rate</i>	<i>Fair value</i>	
	<i>Purchase</i>	<i>Sale</i>		<i>Assets</i>	<i>Liabilities</i>
Derivative financial assets and liabilities at fair value through profit or loss					
Swaps	EUR 180,000 thousand	USD 209,572 thousand	1.16	5,203	89
	EUR 10,270 thousand	HUF 3,160,000 thousand	307.69	54	–
	RUB 9,997,998 thousand	EUR 158,232 thousand	63.20	–	8,603
	RUB 3,000,000 thousand	USD 52,910 thousand	56.70	638	–
	RON 319,800 thousand	EUR 70,544 thousand	4.53	931	1,212
Forwards	EUR 34,000 thousand	USD 39,527 thousand	1.16	935	–
Total derivative financial assets and liabilities at fair value through profit or loss				7,761	9,904
Derivative financial assets and liabilities designated as hedging instruments					
Swaps	RON 298,300 thousand	EUR 67,068 thousand	4.45	–	5,169
Total derivative financial assets and liabilities designated as hedging instruments				–	5,169
Derivative financial instruments				7,761	15,073

Due to the issue of bonds denominated in currencies other than the Group's functional currency (Note 18), the Group concluded cross currency interest rate swaps and currency forwards on an arm's length basis with large international and Russian credit institutions. These swaps are used to manage long-term currency risks of the Group. Payment netting is not applied to the parties' obligations in respect of interest and principal payments.

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 nominal amounts indicate the volume of transactions outstanding at the end of the reporting period and are not indicative of the credit risk.

As at 31 December 2018 and 31 December 2017, the Group has positions in the following types of derivatives:

Forwards: Forward contracts are contractual agreements to buy or sell a specified financial instrument at a specific price and date in the future. Forwards are customized contracts transacted in the over-the-counter market.

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 nominal amounts.

Fair value measurement is based on the corresponding forward curves that depend on exchange rates, interest rates and swap contract maturity. For the fair value of swaps, the discount rate was calculated on the basis of zero coupon yield curve and credit risk. Changes in the fair value of swaps were mainly due to the increase in the forward exchange rates of the euro to transaction currencies.

(Thousands of euros)

8. Securities at fair value through other comprehensive income (2017: Available-for-sale investment securities)

Securities at fair value through other comprehensive income comprise:

	<i>31 December 2018</i>	<i>31 December 2017</i>
Owned by the Group		
Listed debt securities at fair value through other comprehensive income		
Government bonds of member countries		
<i>Credit rating A+</i>	1,149	–
Government bonds of non-member countries		
<i>Credit rating from AA- to AA+</i>	10,574	–
<i>Credit rating from A- to A+</i>	11,472	–
<i>Credit rating B-</i>	18,077	–
Government bonds	41,272	–
Corporate bonds		
<i>Credit rating AAA</i>	22,294	–
<i>Credit rating from AA- to AA+</i>	3,504	–
<i>Credit rating from A- to A+</i>	50,556	–
<i>Credit rating from BBB- to BBB+</i>	28,308	–
<i>Credit rating from BB- to BB+</i>	25,040	–
<i>Credit rating from B- to B+</i>	32,679	–
Corporate bonds	162,381	–
Total listed debt securities at fair value through other comprehensive income	203,653	–
Listed equity instruments at fair value through other comprehensive income		
Corporate shares:		
<i>No credit rating</i>	5	–
Corporate shares	5	–
Investments in equity instruments		
<i>Investments in the fund</i>	674	–
Investments in equity instruments	674	–
Total listed equity instruments at fair value through other comprehensive income	679	–
Securities at fair value through other comprehensive income	204,332	–

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(Thousands of euros)

8. Securities at fair value through other comprehensive income (2017: Available-for-sale investment securities) (continued)

	<i>31 December 2018</i>	<i>31 December 2017</i>
Owned by the Group		
Listed debt securities		
Government bonds of non-member countries		
<i>Credit rating AAA</i>	–	4,066
<i>Credit rating AA+</i>	–	5,396
<i>Credit rating B-</i>	–	18,552
Government bonds	–	28,014
Corporate bonds		
<i>Credit rating from A- to A+</i>	–	12,292
<i>Credit rating from BBB- to BBB+</i>	–	20,370
<i>Credit rating from BB- to BB+</i>	–	62,496
<i>Credit rating from B- to B+</i>	–	13,817
Corporate bonds	–	108,975
Total listed debt securities	–	136,989
Listed equity instruments		
<i>Credit rating A-</i>	–	633
<i>Credit rating BBB</i>	–	1,077
<i>No credit rating</i>	–	5
Total listed equity instruments	–	1,715
Available-for-sale investment securities	–	138,704
Pledged under repurchase agreements		
Listed debt securities		
Government bonds of member countries		
<i>Credit rating A+</i>	–	10,010
Government bonds of non-member countries		
<i>Credit rating A+</i>	–	7,867
Government bonds	–	17,877
Corporate bonds		
<i>Credit rating AAA</i>	–	19,991
<i>Credit rating from AA- to AA+</i>	–	7,466
<i>Credit rating from A- to A+</i>	–	18,544
<i>Credit rating from BBB- to BBB+</i>	–	5,995
<i>Credit rating from BB- to BB+</i>	–	6,850
Corporate bonds	–	58,846
Total listed available-for-sale debt securities pledged under repurchase agreements	–	76,723

Movements in the gross carrying amount and respective ECL related to securities at fair value through other comprehensive income for the year ended 31 December 2018:

<i>Securities at fair value through other comprehensive income</i>	<i>Stage 1</i>	<i>Total</i>
Carrying amount at 1 January 2018, gross	176,652	176,652
New assets purchased or originated	234,535	234,535
Assets derecognized or redeemed (excluding write-offs)	(210,382)	(210,382)
Foreign exchange differences	3,527	3,527
At 31 December 2018	204,332	204,332
Allowance for ECL at 1 January 2018		440
New assets purchased or originated		87
Assets derecognized or redeemed		(227)
Allowance for ECL at 31 December 2018		300

(Thousands of euros)

8. Securities at fair value through other comprehensive income (2017: Available-for-sale investment securities) (continued)

Government bonds comprise EUR- and USD-denominated securities issued and guaranteed by the Ministries of Finance of these countries. The bonds mature in 2023-2027 (31 December 2017: maturing in 2020-2027). The annual coupon rate for these bonds varies from 0.4% to 7.6% (31 December 2017: from 0.4% to 7.6%).

Corporate bonds comprise bonds issued by large companies and banks of the member countries of the Bank, as well as international companies and development banks with goals and missions similar to those of the Bank. The bonds mature in 2020-2028 (31 December 2017: maturing in 2020-2026). The annual coupon rate for these bonds varies from 0.4% to 7.8% (as at 31 December 2017: from 0.4% to 7.9%).

Equity securities are represented by shares issued by a major international company.

Investments in the fund comprise investments in the Central Europe Fund of Funds (CEFoF) established by the European Investment Fund (EIF), a member of the European Investment Bank (EIB), together with governments and national development banks of five countries, including the Republic of Austria, Hungary, the Slovak Republic, Slovenia, and the Czech Republic. The Fund is primarily engaged in encouraging investments in SMEs' equity and creating market infrastructure that would promote those investments, as well as attracting institutional investors and investment managers to Central Europe.

9. Securities at amortized cost

As at 1 January 2018, the Group reclassified a part of its securities previously classified as available for sale to debt instruments measured at amortized cost. These instruments satisfy the SPPI criteria and are held to collect related cash flows rather than for sale.

	<i>31 December 2018</i>	<i>31 December 2017</i>
Owned by the Bank		
Listed debt securities at amortized cost		
Corporate bonds:		
<i>Credit rating AAA</i>	22,053	–
<i>Credit rating AA</i>	4,455	–
<i>Credit rating BBB-</i>	14,957	–
Corporate bonds	41,465	–
Listed debt securities at amortized cost	41,465	–

Corporate bonds comprise investment grade bonds issued by large companies and banks of the member countries of the Bank, as well as international companies and development banks with goals and missions similar to those of the Bank. The bonds mature in 2021-2026(31 December 2017: none). The coupon rate for these bonds varies from 1.8% to 2.1% (31 December 2017: none).

Movements in the gross carrying amount related to securities at amortized cost for the year ended 31 December 2018:

<i>Investment securities at amortized cost</i>	<i>Stage 1</i>	<i>Total</i>
Carrying amount at 1 January 2018, gross	40,301	40,301
New assets purchased or originated	980	980
Assets derecognized or redeemed (excluding write-offs)	(922)	(922)
Foreign exchange differences	1,106	1,106
At 31 December 2018	41,465	41,465

No allowances for ECL for the year ended 31 December 2018 were made.

*(Thousands of euros)***10. Loans to banks**

In 2018, the Group continued its lending activities, being guided by the key priorities of the Development Strategy of the IIB. The principal lending activity is to participate in financing of socially important infrastructure projects in these countries and to facilitate the development of small and medium-sized businesses and foreign trade in the member countries. The Group considers national development institutes, export and import banks and agencies, international financial organizations and development banks as its key counterparties.

In 2018 and 2017, the Group provided trade financing loans and long-term loans to borrowers operating in the following countries:

	<i>31 December 2018</i>	<i>31 December 2017</i>
Trade financing loans		
Republic of Belarus	54,783	3,239
Mongolia	10,849	
Russian Federation	–	23,298
Trade financing loans	65,632	26,537
Long-term loans to banks		
Republic of Cuba	49,960	49,863
Mongolia	38,255	33,735
Socialist Republic of Vietnam	24,670	25,252
Russian Federation	–	75,401
Long-term loans to banks	112,885	184,251
Less: allowance for impairment of loans to banks	(1,885)	(9,153)
Loans to banks	176,632	201,635

Movements in the gross carrying amount and relevant ECL related to trade financing loans for the year ended 31 December 2018 are as follows:

<i>Trade financing loans</i>	<i>Stage 1</i>	<i>Total</i>
Carrying amount at 1 January 2018, gross	26,537	26,537
New assets purchased or originated	127,736	127,736
Assets derecognized or redeemed (excluding write-offs)	(88,977)	(88,977)
Foreign exchange differences	336	336
At 31 December 2018	65,632	65,632
Trade financing loans		
Allowance for ECL at 1 January 2018	114	114
New assets purchased or originated	1,320	1,320
Assets derecognized or redeemed (excluding write-offs)	(956)	(956)
At 31 December 2018	478	478

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*(Thousands of euros)***10. Loans to banks (continued)**

Movements in the gross carrying amount and respective ECL related to long-term loans to banks for the year ended 31 December 2018 are as follows:

<i>Long-term loans to banks</i>	<i>Stage 1</i>	<i>Stage 2</i>	<i>Stage 3</i>	<i>Total</i>
Carrying amount at 1 January 2018, gross	168,997	–	15,254	184,251
New assets purchased or originated	50,473	18	–	50,491
Assets derecognized or redeemed (excluding write-offs)	(87,798)	(118)	–	(87,916)
Transfers to Stage 2	(20,078)	20,078	–	–
Amounts written off	–	(19,978)	(14,377)	(34,355)
Foreign exchange differences	1,291	–	(877)	414
At 31 December 2018	112,885	–	–	112,885

<i>Long-term loans to banks</i>	<i>Stage 1</i>	<i>Stage 2</i>	<i>Stage 3</i>	<i>Total</i>
Allowance for ECL at 1 January 2018	2,633	–	15,254	17,887
New assets purchased or originated	1,117	–	–	1,117
Assets derecognized or redeemed (excluding write-offs)	(1,993)	–	–	(1,993)
Transfers to Stage 1	–	–	–	–
Transfers to Stage 2	(350)	350	–	–
Effect on ECL at the year-end due to transfers between stages during the year	–	1,486	–	1,486
Amounts written off (against the allowance)	–	(1,836)	(14,377)	(16,213)
Foreign exchange differences	–	–	(877)	(877)
At 31 December 2018	1,407	–	–	1,407

The information on overdue loans to banks as at 31 December 2018 and 31 December 2017 is provided below:

	<i>31 December 2018</i>	<i>31 December 2017</i>
Total loans with overdue principal and/or interest	–	15,254
Less: allowance for impairment of loans to banks	–	(9,153)
Overdue loans to banks	–	6,101

For the purposes of these consolidated financial statements, a loan to a bank is considered overdue if at least one of the loan-related payments is past due at the reporting date. In this case, the amount of the overdue loan is the total amount due from the borrower, including the accrued interest income.

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(Thousands of euros)

10. Loans to banks (continued)**Allowance for impairment of loans to banks**

A reconciliation of the allowance for ECL for impairment of loans to banks by country for the year ended 31 December 2018 is as follows:

	<i>Russian Federation</i>	<i>Mongolia</i>	<i>Socialist Republic of Vietnam</i>	<i>Republic of Cuba</i>	<i>Other</i>	<i>Total</i>
At 31 December 2017	9,153	–	–	–	–	9,153
Impact of adopting IFRS 9	6,705	1,295	291	539	18	8,848
At 1 January 2018	15,858	1,295	291	539	18	18,001
Net (reversal)/charge for an allowance for ECL during the period	(604)	(622)	(34)	4	2,230	974
Write off against previously accrued allowance	(14,377)	–	–	–	(1,836)	(16,213)
Change in allowance resulting from changes in exchange rates	(877)	–	–	–	–	(877)
At 31 December 2018	–	673	257	543	412	1,885

A reconciliation of the allowance for impairment of loans to banks by country for the year ended 31 December 2017 is as follows:

	<i>Russian Federation</i>	<i>Total</i>
At 1 January 2017	–	–
Net charge for the period	9,153	9,153
At 31 December 2017	9,153	9,153
Individual impairment	9,153	9,153
Loans to banks individually determined to be impaired, before deducting any individually assessed impairment allowance	15,254	15,254

(Thousands of euros)

10. Loans to banks (continued)**Analysis of collateral for loans to banks**

The following table provides an analysis of the portfolio of trade financing loans and long-term loans to banks by type of collateral as at 31 December 2018 and 31 December 2017:

	<i>31 December 2018</i>		<i>31 December 2017</i>	
	<i>Loans to banks net of allowance for impairment</i>	<i>Share in the total loans, %</i>	<i>Loans to banks net of allowance for impairment</i>	<i>Share in the total loans, %</i>
State guarantees	49,416	28.0	49,863	24.7
Uncollateralized part of the loans	127,215	72.0	151,772	75.3
Loans to banks	176,631	100.0	201,635	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 2018, long-term loans and trade financing loans to six banks (31 December 2017: two banks) with a total amount of loans to each of them exceeding 10% of total loans to banks were recorded on the Group's balance sheet. As at 31 December 2018, the total amount of such major loans was EUR 148,608 thousand (31 December 2017: EUR 70,100 thousand) and allowances of EUR 1,411 thousand (31 December 2017: no allowances) were made for them.

11. Loans to customers

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

	<i>31 December 2018</i>	<i>31 December 2017</i>
Loans to customers measured at amortized cost		
Republic of Bulgaria	105,161	57,995
Russian Federation	99,979	81,817
Slovak Republic	89,966	60,464
Romania	86,846	78,440
Kingdom of the Netherlands	35,075	5,847
Hungary	34,454	42,910
Republic of Ecuador	31,838	34,763
Republic of Panama	28,747	29,775
Mongolia	27,507	24,425
Socialist Republic of Vietnam	22,028	–
USA	1,580	1,666
Czech Republic	–	49,967
Total loans to customers at amortized cost	563,181	468,069
Loans to customers at fair value through other comprehensive income		
Republic of Bulgaria	30,073	–
Total loans to customers at fair value through other comprehensive income	30,073	–
Less: allowance for impairment of loans to customers	(17,051)	(5,555)
Loans to customers	576,203	462,514

*(Thousands of euros)***11. Loans to customers (continued)**

Movements in the gross carrying amount and respective ECL related to loans to customers for the year ended 31 December 2018 are as follows:

<i>Loans to customers</i>	<i>Stage 1</i>	<i>Stage 2</i>	<i>Stage 3</i>	<i>Total</i>
Carrying amount at 1 January 2018, gross	446,591	6,327	15,151	468,069
New assets purchased or originated	383,155	731	103	383,989
Assets derecognized or redeemed (excluding write-offs)	(194,676)	(51,013)	(1,014)	(246,703)
Transfers to Stage 2	(50,480)	50,480	–	–
Transfers to Stage 3	–	(6,190)	6,190	–
Amounts written off	–	–	(5,279)	(5,279)
Foreign exchange differences	(6,364)	–	(458)	(6,822)
At 31 December 2018	578,226	335	14,693	593,254

<i>Loans to customers</i>	<i>Stage 1</i>	<i>Stage 2</i>	<i>Stage 3</i>	<i>Total</i>
Allowance for ECL at 1 January 2018	5,336	3,610	15,151	24,097
New assets purchased or originated	2,399	11	640	3,050
Assets derecognized or redeemed (excluding write-offs)	(5,706)	–	–	(5,706)
Transfers to Stage 3	–	(4,639)	4,639	–
Changes to models and inputs used for ECL calculations	–	1,347	–	1,347
Amounts written off (against the allowance)	–	–	(5,279)	(5,279)
Foreign exchange differences	–	–	(458)	(458)
At 31 December 2018	2,029	329	14,693	17,051

The information on overdue loans to customers as at 31 December 2018 and 31 December 2017 is provided below:

	<i>31 December 2018</i>	<i>31 December 2017</i>
Total loans with overdue principal and/or interest	14,694	15,151
Less: allowance for impairment of loans to customers	(14,694)	(5,255)
Overdue loans to customers	–	9,896

For the purposes of these consolidated financial statements, a loan to a customer is considered overdue if at least one of the loan-related payments is past due at the reporting date. In this case, the amount of the overdue loan is the total amount due from the borrower, including the accrued interest income.

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(Thousands of euros)

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

A reconciliation of the allowance for ECL for impairment of loans to customers by country for the year ended 31 December 2018 is as follows:

	<i>Russian Federation</i>	<i>Republic of Bulgaria</i>	<i>Romania</i>	<i>Slovak Republic</i>	<i>Hungary</i>	<i>Mongolia</i>	<i>Socialist Republic of Vietnam</i>	<i>Other</i>	<i>Total</i>
At 31 December 2017	–	300	5,255	–	–	–	–	–	5,555
Impact of adopting IFRS 9	64	3,752	10,261	454	3,333	370	–	308	18,542
At 1 January 2018	64	4,052	15,516	454	3,333	370	–	308	24,097
Net (reversal)/charge for the period	6	1,919	(128)	(89)	(3,333)	331	93	(108)	(1,309)
Write off against previously accrued allowance	–	(5,279)	–	–	–	–	–	–	(5,279)
Change in allowance resulting from changes in exchange rates	–	–	(458)	–	–	–	–	–	(458)
At 31 December 2018	70	692	14,930	365	–	701	93	200	17,051

A reconciliation of the allowance for impairment of loans to customers by country for the year ended 31 December 2017 is as follows:

	<i>Slovak Republic</i>	<i>Republic of Bulgaria</i>	<i>Romania</i>	<i>Total</i>
At 1 January 2017	8,103	6,955	2,254	17,312
Net charge for the period	–	11	3,001	3,012
Write off against previously accrued allowance	(8,103)	(6,666)	–	(14,769)
At 31 December 2017	–	300	5,255	5,555
Individual impairment	–	–	5,255	5,255
Loans to customers, individually determined to be impaired, before deducting any individually assessed impairment allowance	–	–	15,151	15,151

(Thousands of euros)

11. Loans to customers (continued)**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 2018 and 31 December 2017:

	<i>31 December 2018</i>		<i>31 December 2017</i>	
	<i>Loans to customers net of allowance for impairment</i>	<i>Share in the total loans, %</i>	<i>Loans to customers net of allowance for impairment</i>	<i>Share in the total loans %</i>
Pledge of shares	113,532	19.7	42,504	9.2
Pledge of real property (mortgage) and title	103,128	17.9	86,728	18.8
Pledge of equipment and goods in turnover	74,607	12.9	15,292	3.3
State guarantees	60,462	10.5	74,476	16.1
Corporate guarantees	47,302	8.2	70,599	15.3
Pledge of rights of claim	24,888	4.3	6,150	1.3
Pledge of vehicles	16,567	2.9	1,476	0.3
Uncollateralized part of the loans	135,717	23.6	165,289	35.7
Loans to customers	576,203	100.0	462,514	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.

Concentration of loans to customers

As at 31 December 2018, loans to two borrowers (31 December 2017: three borrowers) with the total amount of loans to each of the two borrowers exceeding 10% of total loans to customers were recorded on the Group's balance sheet. As at 31 December 2018, these loans comprised EUR 159,485 thousand (31 December 2017: EUR 181,256 thousand) in total and impairment allowances of EUR 86 thousand (31 December 2017: no allowances) were made for them.

Analysis of loans to customers by industry

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

	<i>31 December 2018</i>	<i>31 December 2017</i>
Production and transmission of electricity	181,592	104,847
Leases	122,638	116,910
Communications	49,946	22,815
Manufacturing of refined oil products	30,101	30,099
Wholesale trade	29,538	738
Retail trade	29,506	–
Food and beverage	23,653	25,662
Finance	22,028	–
Mining	21,766	20,632
Real estate	18,863	19,722
Manufacturing of electrical equipment	14,694	21,159
Oil and gas production	14,361	–
Production of pharmaceutical products	10,771	11,319
Agriculture	10,527	13,408
Land transport	8,640	11,248
Postal activities	4,630	–
Metal working industry	–	49,967
Legal and advisory services, audit	–	19,543
	593,254	468,069
Less: allowance for impairment of loans to customers	(17,051)	(5,555)
Loans to customers	576,203	462,514

*(Thousands of euros)***12. Investment property**

In 2018 and 2017, the following changes occurred in the cost of investment property under operating lease:

	<u>2018</u>	<u>2017</u>
At 1 January	21,853	21,840
Leasehold improvements	13	39
Sales	(1,078)	(26)
Carrying amount at 31 December	<u>20,788</u>	<u>21,853</u>

The Group leases out investment properties under operating lease agreements. In 2018, the Group's income from lease of investment property amounted to EUR 3,956 thousand (2017: EUR 4,034 thousand).

The Group regularly remeasures the fair value of its investment property to ensure that the current value of the investment property does not significantly differ from its fair value. As at 31 December 2017, the investment properties were remeasured at market value based on the results of the valuation performed by independent companies of professional appraisers which have acknowledged qualification and relevant professional experience in appraising real property of a similar category and in a similar location. As at 31 December 2018, management of the Group believes that the fair value of the investment properties, determined by reference to market-based evidence and potential ability to generate income, does not significantly differ from their carrying amount at that date. For further details on the fair value of investment properties, refer to Note 26.

If the investment properties were measured using the cost method, the carrying amounts as at 31 December 2018 and 31 December 2017 would be as follows:

	<u>2018</u>	<u>2017</u>
Cost	20,190	20,141
Leasehold improvements	13	49
Sales	(1,078)	–
Accumulated depreciation	(2,822)	(2,611)
Net book value	<u>16,303</u>	<u>17,579</u>

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

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*(Thousands of euros)***13. Property, equipment and intangible assets**

The movements in property, equipment and intangible assets for the years 2018 and 2017 were as follows:

	<i>Buildings</i>	<i>Equipment</i>	<i>Computers and software</i>	<i>Office furniture</i>	<i>Vehicles</i>	<i>Intangible assets</i>	<i>Other</i>	<i>Capital expenditure</i>	<i>Total</i>
Cost or revalued amount									
At 1 January 2018	67,758	7,581	1,923	301	689	3,051	178	706	82,187
Additions	–	–	–	–	–	–	–	917	917
Transfers	121	251	158	7	–	945	4	(1,486)	–
Disposals	–	(31)	(2)	(2)	–	–	(6)	–	(41)
At 31 December 2018	67,879	7,801	2,079	306	689	3,996	176	137	83,063
Accumulated depreciation and amortization									
At 1 January 2018	(186)	(6,714)	(1,427)	(239)	(563)	(566)	(104)	–	(9,799)
Charge for the period	(1,124)	(241)	(267)	(19)	(81)	(296)	(6)	–	(2,034)
Disposals	–	31	–	1	–	–	4	–	36
At 31 December 2018	(1,310)	(6,924)	(1,694)	(257)	(644)	(862)	(106)	–	(11,797)
Net book value									
At 31 December 2017	67,572	867	496	62	126	2,485	74	706	72,388
At 31 December 2018	66,569	877	385	49	45	3,134	70	137	71,266

*(Thousands of euros)***13. Property, equipment and intangible assets (continued)**

	<i>Buildings</i>	<i>Equipment</i>	<i>Computers and software</i>	<i>Office furniture</i>	<i>Vehicles</i>	<i>Intangible assets</i>	<i>Other</i>	<i>Capital expenditure</i>	<i>Total</i>
Cost or revalued amount									
At 1 January 2017	67,644	7,500	3,361	307	808	2,472	183	427	82,702
Additions	–	–	–	–	–	–	–	1,749	1,749
Transfers	350	364	150	14	–	590	2	(1,470)	–
Disposals	–	(283)	(1,588)	(20)	(119)	(11)	(7)	–	(2,028)
Recovery of accumulated depreciation and amortization upon revaluation	(1,039)	–	–	–	–	–	–	–	(1,039)
Revaluation	803	–	–	–	–	–	–	–	803
At 31 December 2017	67,758	7,581	1,923	301	689	3,051	178	706	82,187
Accumulated depreciation and amortization									
At 1 January 2017	(117)	(6,747)	(2,730)	(236)	(580)	(343)	(105)	–	(10,858)
Charge for the period	(1,108)	(250)	(284)	(21)	(102)	(237)	(6)	–	(2,008)
Disposals	–	283	1,587	18	119	14	7	–	2,028
Recovery of accumulated depreciation and amortization upon revaluation	1,039	–	–	–	–	–	–	–	1,039
At 31 December 2017	(186)	(6,714)	(1,427)	(239)	(563)	(566)	(104)	–	(9,799)
Net book value									
At 31 December 2016	67,527	753	631	71	228	2,129	78	427	71,844
At 31 December 2017	67,572	867	496	62	126	2,485	74	706	72,388

As at 31 December 2018, the cost of fully depreciated property and equipment still used by the Bank was EUR 6,082 thousand (31 December 2017: EUR 5,217 thousand).

*(Thousands of euros)***13. Property, equipment and intangible assets (continued)**

As at 31 December 2018, the fair value of buildings owned by the Group is determined based on the results of the valuation performed by an independent company 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, the Group's management believes that the fair value of buildings owned by the Bank as at 31 December 2018 does not significantly differ from their carrying amount at that date.

The fair value is determined by reference to market-based evidence and ability to generate income. For further details on the fair value of property and equipment, refer to Note 26.

The Group regularly performs revaluation of the fair value of its buildings to ensure that the current book value of buildings owned by the Group does not differ significantly from their fair value. Revaluation of buildings owned by the Group at market value was performed as at 31 December 2017 based on the results of the valuation performed by an independent firm of professional appraisers who have acknowledged qualification and relevant professional experience in appraising real property of a similar category and in a similar location. As at 31 December 2018, management of the Group believes that by reference to market-based evidence the fair value of buildings owned by the Group does not significantly differ from their carrying amount at that date. For further details on the fair value of buildings owned by the Group, refer to Note 26.

If the buildings were measured using the cost method, the carrying amounts as at 31 December 2018 and 31 December 2017 would be as follows:

	<i>2018</i>	<i>2017</i>
Cost	52,705	52,355
Additions	121	350
Accumulated depreciation and amortization	(22,331)	(21,298)
Net book value	30,495	31,407

14. Other assets and liabilities

Other assets comprise:

	<i>31 December 2018</i>	<i>31 December 2017</i>
Financial assets		
Settlements on bank transactions	1,970	2,007
Accounts receivable on business operations	108	73
Guarantee payments	26	26
Other financial assets	316	363
	2,420	2,469
Less allowance for impairment of financial assets	(1,527)	(1,741)
Total financial assets	893	728
Non-financial assets		
Advances issued	1,585	990
Assets held for sale – real estate	89	89
Inventories – real estate	–	50
Other non-financial assets	748	619
Total non-financial assets	2,422	1,748
Other assets	3,315	2,476

(Thousands of euros)

14. Other assets and liabilities (continued)

Movements in the gross carrying amount and relevant ECL related to financial assets for the year ended 31 December 2018 were as follows:

<i>Financial assets</i>	<i>Stage 1</i>	<i>Stage 2</i>	<i>Stage 3</i>	<i>Total</i>
Carrying amount at 1 January 2018, gross	729	–	1,740	2,469
New assets purchased or originated	1,823,655	1	–	1,823,656
Assets derecognized or redeemed (excluding write-offs)	(1,824,294)	(1)	–	(1,824,295)
Foreign exchange differences	806	–	(216)	590
At 31 December 2018	896	–	1,524	2,420

Significant amounts in “New purchased or originated assets” and “Assets derecognized or redeemed (excluding write-offs)” comprise, among others, cash paid to arrangers of the debt securities issue to fulfil the Bank’s obligations (Note 18).

	<i>Stage 1</i>	<i>Stage 3</i>	<i>Total</i>
Allowance under IFRS 39	5	1,736	1,741
Impact of adopting IFRS 9	–	(6)	(6)
Allowance at 1 January	5	1,730	1,735
New purchased or originated assets	19	–	–
Assets derecognized or redeemed (excluding write-offs)	(22)	–	(22)
Change in allowance resulting from changes in exchange rates	–	(205)	(205)
Allowance at the end of the reporting period	2	1,525	1,527

Other liabilities comprise the following:

	<i>31 December 2018</i>	<i>31 December 2017</i>
Financial liabilities		
Other accounts payable on bank transactions	163	1,125
Other accounts payable on business operations	1,606	1,015
Other financial liabilities.	–	8
Total financial liabilities	1,769	2,148
Non-financial liabilities		
Settlements with employees	4,812	4,070
Allowance for ECL on credit-related commitments	1,752	–
Other non-financial liabilities	487	178
Total non-financial liabilities	7,051	4,248
Other liabilities	8,820	6,396

(Thousands of euros)

15. Allowances for credit losses, other impairment and provisions

The table below shows allowances for ECL on financial instruments recorded in profit or loss for the year ended 31 December 2018:

	<i>Notes</i>	<i>Stage 1</i>	<i>Stage 2</i>	<i>Stage 3</i>	<i>Total</i>
Cash and cash equivalents	5	(8)	–	–	(8)
Deposits with banks and other financial institutions	6	(241)	–	–	(241)
Securities at fair value through other comprehensive income	8	(140)	–	–	(140)
Loans to banks	10	(862)	1,836	–	974
Loans to customers	11	(3,307)	1,358	640	(1,309)
Financial assets	14	(3)	–	–	(3)
Non-financial liabilities (allowance for ECL on credit-related commitments)	14, 20	889	(1)	–	888
Total (income)/expenses on impairment		(3,672)	3,193	640	161

Movements in allowances for ECL on financial instruments for the year ended 31 December 2018 were as follows:

	<i>Stage 1</i>	<i>Stage 2</i>	<i>Stage 3</i>	<i>Total</i>
Allowance for ECL at 1 January 2018	9,573	3,678	67,102	80,353
New assets purchased or originated	8,570	11	640	9,221
Assets derecognized or redeemed (excluding write-offs)	(11,892)	(1)	–	(11,893)
Transfers to Stage 2	(350)	350	–	–
Transfers to Stage 3	–	(4,639)	4,639	–
Effect on ECL at the year-end due to transfers between stages during the year	–	1,486	–	1,486
Changes to models and inputs used for ECL calculations	–	1,347	–	1,347
Amounts written off	–	(1,836)	(19,656)	(21,492)
Foreign exchange differences	–	–	(1,540)	(1,540)
At 31 December 2018	5,901	396	51,185	57,482

As at 31 June 2018, there were no other allowances other than those mentioned above on the Group's balance sheet.

16. Due to banks and other financial institutions

Due to banks and other financial institutions are presented based on contractual terms and include the following items:

	<i>31 December 2018</i>	<i>31 December 2017</i>
Due to banks up to 1 year		
Term deposits of banks and other financial institutions	67,872	3,496
Total due to banks up to 1 year	67,872	3,496
Due to banks over 1 year		
Repurchase agreements	–	62,015
Total due to banks over 1 year	–	62,015
Due to banks and other financial institutions	67,872	65,511

The Group performs daily monitoring of repurchase agreements and the value of collateral when placing/returning additional collateral, if necessary.

(Thousands of euros)

16. Due to banks and other financial institutions (continued)**Concentration of deposits from banks and other financial institutions**

As at 31 December 2018, the Group has four counterparties (31 December 2017: two counterparties) accounting for over 10% of the Group's total deposits from banks and other financial institutions in the amount of EUR 67,872 thousand (31 December 2017: EUR 62,015 thousand).

17. Long-term loans of banks

Long-term loans of banks comprise:

	<i>31 December 2018</i>	<i>31 December 2017</i>
Loans of banks	34,559	12,898
SSD	22,994	22,939
Syndicated loans	–	59,755
Long-term loans of banks	57,553	95,592

On 19 March 2018, the Group received the first tranche from the BRICS New Development Bank in the amount of USD 12.5 thousand (EUR 10,273 thousand) under the loan agreement of USD 50 mln. On 17 July 2018, the Bank received the second tranche in the amount of USD 12.5 million (EUR 10,674 thousand).

In 2017, the Group issued SSD debentures (Schuldscheindarlehen) in the Western European market in the total amount of EUR 23,000 thousand.

On 3 August 2017, the Group raised bilateral financing in the Hungarian financial market in the amount of HUF 4.0 billion (EUR 13,185 thousand).

18. Debt securities issued

Debt securities issued comprise:

	<i>Interest rate, % p.a.</i>	<i>Maturity</i>	<i>31 December 2018</i>	<i>31 December 2017</i>
RUB-denominated bonds	0.01-9.50	2024-2027	230,032	267,112
RON-denominated bonds	3.40-4.57	2019-2021	194,071	152,084
EUR-denominated bonds	1.50-3.50	2019-2021	170,085	90,017
CZK-denominated bonds	2.33	2021	29,266	–
Debt securities issued			623,454	509,213

On 15 October 2018, the Group placed bonds of the fourth issue on the Bucharest Stock Exchange structured in two tranches of EUR 80 million and RON 300 million (EUR 64,364 thousand). Both tranches mature in three years. EUR-denominated bonds and RON-denominated bonds bear interest rates of 1.5026% p.a. and 3m Robor + 1.40%, respectively.

On 15 October 2018, the Bank fully repaid the first issue of bonds placed in Romania in the amount of RON 111 million (EUR 23,801 thousand).

On 26 April 2018, the Group placed in the amount of CZK 501.1 million (EUR 19,832 thousand) maturing in three years. On 4 June 2018, the Group made an additional placement of bonds worth a total of CZK 249.7 million (EUR 9,675 thousand). The coupon rate was set at 3m Pribor + 0.55% p.a.

(Thousands of euros)

18. Debt securities issued (continued)

On 30 May 2018, the Group made a secondary placement of RUB-denominated bonds, series 03, in the amount of RUB 3.99 billion (EUR 55,120 thousand) that had been repurchased in 2017 under the offer. A new coupon rate of 7.6% p.a. was set for one coupon period before the offer in November 2018. The Group repurchased the full issue from investors under the offer in November 2018.

The Group redeemed and made a secondary placement of bonds, series 04, worth RUB 1.2 billion (EUR 18,271 thousand) on 21 November 2017, as scheduled under the offer. A new coupon rate of 8.15% was set.

The Group partially redeemed RUB-denominated bonds, series 01, worth a total of RUB 489,432 thousand (EUR 7,259 thousand) on 27 October 2017, as scheduled under the offer. A new coupon rate of 0.01% was set for the remaining bonds of this issue.

The Group placed a third issue of bonds in the Romanian capital market on 25 September 2017. The issue comprises two tranches of EUR 60 million and RON 300 million (EUR 65,199 thousand) maturing in three years. EUR-denominated bonds and RON-denominated bonds bear interest rates of 1.593% p.a. and 3m Robor + 1.50%, respectively.

On 14 June 2017, the Group placed an issue of exchange-traded bonds at the Moscow Exchange under the Program to issue exchange-traded bonds registered in 2016. The issue totaled RUB 10 billion (EUR 156,579 thousand) and provides for an offer in March 2020. The coupon rate of the bonds was set at 8.75% payable on a semi-annual basis with the first coupon payment to be made on 11 September 2017.

The Group redeemed RUB-denominated bonds, series 03, worth a total of RUB 3.99 billion (EUR 62,858 thousand) on 2 June 2017, as scheduled under the offer. A new coupon rate of 0.01% was set for the remaining bonds of this issue.

At the issue dates of bonds, the Group entered into cross-currency interest rate swaps for the purpose of managing currency risks (Note 7) and exchanging interest expense from debt securities issued, denominated in RUB, RON, to the currency required by the Group (EUR, USD) to finance credit projects in the required currency. The effects of using cross-currency interest rate swaps and fair value hedge operations are disclosed in Notes 22 and 23.

The Group primarily used the proceeds from issuance of debt instruments and placement of bonds to expand its loan portfolio.

19. Equity

Subscribed and paid-in capital

On 18 August 2018, new statutory documents of the International Investment Bank entered into force. Pursuant to the amended statutory documents, the Bank's statutory capital amounts to EUR 2,000,000 thousand (31 December 2017: 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 2018, the unpaid portion of the Bank's statutory capital in the amount of EUR 1,674,038 thousand (31 December 2017: EUR 985,038 thousand) is the amount of contributions that have not been made yet by the Bank's member countries and the amount of unallocated equity contributions totaling EUR 875,500 thousand (31 December 2017: EUR 175,500 thousand).

The Government of the Czech Republic made an additional contribution of EUR 7,000 thousand to the Bank's equity on 20 December 2018.

The Government of Romania made an additional contribution of EUR 4,000 thousand to the Bank's equity on 12 July 2018.

The Government of Mongolia made an additional contribution of EUR 1,909 thousand to the Bank's equity on 27 December 2017.

The paid-in capital of the International Investment Bank totaled EUR 325,962 thousand (31 December 2017: EUR 314,962 thousand).

(Thousands of euros)

19. Equity (continued)**Revaluation reserve for securities at fair value through other comprehensive income and revaluation reserve for property and equipment**

Changes in the revaluation reserve for securities at fair value through other comprehensive income and revaluation reserve for property and equipment were as follows:

	<i>Revaluation reserve for securities</i>	<i>Revaluation reserve for property and equipment</i>
At 1 January 2017	(1,506)	12,945
Net unrealized gains on available-for-sale securities	9,145	–
Realized gains on available-for-sale securities reclassified to the income statement	(7,399)	–
Revaluation of buildings	–	803
At 31 December 2017	240	13,748
Effect of adopting IFRS 9	2,043	–
At 1 January 2018	2,283	13,748
Net change in the fair value of securities at fair value through other comprehensive income	(7,398)	–
Change in the allowance for ECL on securities at fair value through other comprehensive income	300	–
Reclassification of accumulated gains from disposal of debt securities at fair value through other comprehensive income to the consolidated income statement	(2,299)	–
Reclassification of accumulated profit from disposal of equity instruments at fair value through other comprehensive income to retained earnings	(252)	–
At 31 December 2018	(7,366)	13,748

Revaluation reserve for securities

The revaluation reserve for securities records fair value changes of available-for-sale (before 1 January 2018) and financial assets through FVOCI (after 1 January 2018).

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.

20. Commitments and contingencies**Legal**

In the ordinary course of business, the Group 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 Group. 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 Group 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 Group's further actions to collect bad debt and/or realize respective repossession rights is higher than the amount collected and also when the Group 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.

*(Thousands of euros)***20. Commitments and contingencies (continued)****Insurance**

The Group 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 Group did not obtain insurance coverage related to temporarily discontinued operations or the Group's obligations to third parties.

Taxation

The IIB is an international institution operating on the basis of the Intergovernmental Agreement on the Establishment of the International Investment Bank (the "Agreement") and the Statute that constitutes an integral part of the Agreement. Pursuant to the Agreement, the Bank is exempt from any national or local direct taxes or duties effective in the territories of its member states. For taxation purposes, its subsidiaries are subject to the provisions of the effective Russian tax, currency and customs legislation.

Credit-related commitments

At any time, the Group may have outstanding commitments to extend loans. These commitments take the form of approved loan agreements.

As at 31 December 2018, credit-related commitments of the Bank comprised credit-related commitments such as undrawn loan facilities, guarantees and reimbursement obligations, including under the Trade Financing Program.

The primary purpose of credit-related commitments is to ensure that funds are available to customers as required. Guarantees issued, which represent irrevocable assurances that the Group will make payments in the event that a customer cannot meet its obligations to third parties, carry the same credit risk as loans. Reimbursement obligations, which are irrevocable reimbursement obligations of the Group issued on behalf of banks issuing documentary letters of credit that are accepted and paid by foreign partner banks up to a stipulated amount under specific terms and conditions, are collateralized by the underlying shipments of goods to which they relate and therefore carry less risk than a direct borrowing. Undrawn loan facilities represent unused portions of funds to be issued as loans.

Credit-related commitments are presented in the table below as at 31 December 2018 and 31 December 2017.

	<i>31 December 2018</i>	<i>31 December 2017</i>
Undrawn loan facilities	108,601	116,161
Guarantees issued	63,987	15,425
Reimbursement obligations	17,021	32,812
	189,609	164,398
Less: allowance for impairment of credit-related commitments	(1,752)	–
Credit-related commitments	187,857	164,398

Changes in the gross carrying amount and relevant ECL related to guarantees issued for the year ended 31 December 2018 were as follows:

<i>Guarantees issued</i>	<i>Stage 1</i>	<i>Total</i>
Carrying amount at 1 January 2018, gross	15,425	15,425
New purchased or originated credit-related commitments	69,606	69,606
Credit-related commitments derecognized or redeemed (excluding write-offs)	(17,094)	(17,094)
Translation differences	(3,950)	(3,950)
At 31 December 2018	63,987	63,987

(Thousands of euros)

20. Commitments and contingencies (continued)**Credit-related commitments (continued)**

<i>Guarantees issued</i>	<i>Stage 1</i>	<i>Total</i>
Allowance for ECL at 1 January 2018	54	54
New purchased or originated credit-related commitments	2,083	2,083
Credit-related commitments derecognized or redeemed (excluding write-offs)	(1,209)	(1,209)
At 31 December 2018	928	928

Changes in the gross carrying amount and relevant ECL related to the undrawn loan facilities for the year ended 31 December 2018 were as follows:

<i>Undrawn loan facilities</i>	<i>Stage 1</i>	<i>Stage 2</i>	<i>Total</i>
Carrying amount at 1 January 2018, gross	116,094	68	116,162
New purchased or originated credit-related commitments	497,819	15,067	512,886
Credit-related commitments derecognized or redeemed (excluding write-offs)	(494,547)	(15,068)	(509,615)
Translation differences	(10,832)	–	(10,832)
At 31 December 2018	108,534	67	108,601

<i>Undrawn loan facilities</i>	<i>Stage 1</i>	<i>Stage 2</i>	<i>Total</i>
Allowance for ECL at 1 January 2018	340	68	408
New purchased or originated credit-related commitments	760	–	760
Credit-related commitments derecognized or redeemed (excluding write-offs)	(741)	(1)	(742)
At 31 December 2018	359	67	426

Changes in the gross carrying amount and relevant ECL related to reimbursement obligations for the year ended 31 December 2018 were as follows:

<i>Reimbursement obligations</i>	<i>Stage 1</i>	<i>Total</i>
Carrying amount at 1 January 2018, gross	32,812	32,812
New purchased or originated credit-related commitments	20,745	20,745
Credit-related commitments derecognized or redeemed (excluding write-offs)	(36,766)	(36,766)
Translation differences	230	230
At 31 December 2018	17,021	17,021

<i>Reimbursement obligations</i>	<i>Stage 1</i>	<i>Total</i>
Allowance for ECL at 1 January 2018	402	402
New purchased or originated credit-related commitments	727	727
Credit-related commitments derecognized or redeemed (excluding write-offs)	(731)	(731)
At 31 December 2018	398	398

*(Thousands of euros)***21. Leases****Group as lessor**

The Group provides its investment property for operating leases. As at 31 December 2018, the Group's non-cancelable operating lease rentals amount to EUR 3,326 thousand (31 December 2017: EUR 6,819 thousand) and will be settled within 1 month-4 years (31 December 2017: 1-5 years).

22. Interest income and interest expenses

Net interest income comprises:

	<u>2018</u>	<u>2017</u>
Interest income		
<i>Interest income calculated using the EIR method</i>		
Loans to customers	28,311	19,754
Loans to banks	8,896	6,908
Securities at fair value through other comprehensive income	6,528	–
Available-for-sale securities	–	6,006
Deposits with banks and other financial institutions, including cash and cash equivalents	1,492	3,252
Securities at amortized cost	697	–
Other	5	43
<i>Other interest income</i>		
Cross-currency interest rate swaps covering long-term currency risks	16,874	19,932
Total interest income	<u>62,803</u>	<u>55,895</u>
Interest expense		
<i>Interest expenses calculated using the EIR method</i>		
Debt securities issued	(32,875)	(27,851)
Long-term loans of banks	(2,044)	(2,377)
Funds raised under repurchase agreements	(772)	(1,940)
Due to banks and other financial institutions	(207)	(161)
Current customer accounts	(181)	(237)
Other	(65)	–
<i>Other interest expenses</i>		
Cross-currency interest rate swaps covering long-term currency risks	(3,047)	(1,542)
Total interest expenses	<u>(39,191)</u>	<u>(34,108)</u>
Net interest income	<u><u>23,612</u></u>	<u><u>21,787</u></u>

There was no interest income accrued on impaired loans issued for the year ended 31 December 2018 (2017: EUR 122 thousand).

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*(Thousands of euros)***23. Net losses from operations with foreign currencies and derivatives**

Net losses from operations with foreign currencies and derivatives comprise:

	<u>2018</u>	<u>2017</u>
Derivatives and operations with foreign currencies		
Net gains from operations with foreign currencies and derivatives	11,132	29,915
Net losses from revaluation of derivatives	(54,862)	(24,809)
Total derivatives and operations with foreign currencies	<u>(43,730)</u>	<u>5,106</u>
Fair value hedge operations		
Net gains from fair value hedge operations	–	1,016
Net gains/(losses) from revaluation of fair value hedge operations	1,125	(3,633)
Net losses from revaluation of the hedged object	(834)	2,553
Total fair value hedge operations	<u>291</u>	<u>(64)</u>
Translation differences		
Net gains/(losses) from revaluation of assets and liabilities in foreign currencies	38,397	(7,483)
Net losses from operations in foreign currencies and with derivatives	<u>(5,042)</u>	<u>(2,441)</u>

24. General and administrative expenses

General and administrative expenses comprise:

	<u>2018</u>	<u>2017</u>
Employee compensations and employment taxes	14,432	13,105
Depreciation of property, equipment and intangible assets	2,034	2,008
IT expenses, inventory and occupancy expenses	1,938	1,842
Expenses related to business travel, representative and accommodation expenses	790	805
Professional services	764	559
Other	484	553
General and administrative expenses	<u>20,442</u>	<u>18,872</u>

25. Risk management**Risk management framework**

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

The Group's risk management activities are intended to:

- ▶ Identify, analyze and manage risks faced by the Group;
- ▶ 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 professional risk management for the bank transactions.

Risk management policies and procedures are reviewed regularly to reflect changing circumstances on global financial markets.

(Thousands of euros)

25. Risk management (continued)

Risk management system

Integrated into the whole vertical organizational structure of the Group and all areas of the Group's activities, the risk management system makes it possible to identify in a timely manner and effectively manage different types of risks.

Risk management involves all of the Group's divisions in the evaluating, assuming, and controlling risks ("Three lines of defense"):

- ▶ Risk-taking (1st line of defense): the Group's divisions directly preparing and conducting transactions, are involved in the identification, assessment, and monitoring of risks and comply with internal regulations on risk management, as well as give due consideration to the risk level in the preparation of transactions;
- ▶ Risk management (2nd line of defense): the division responsible for risk management develops risk management tools and methodology, assesses and monitors the risk level, prepares reports on risks, carries out risk aggregation, and calculates the amount of total capital requirements;
- ▶ Internal audit (3rd line of defense): independent quality assessment for existing risk management processes, identification of violations, and proposals for the improvement of the risk management system.

The Group's operations are managed taking into account the level of the risk appetite approved by the Board of Directors and its integration into a system of limits and restrictions insuring the acceptable level of risk for aggregated positions, transparent distribution of total risk limit among the activities of the Group.

The Board of Governors, the Board of Directors, the Audit Commission, the Management Board, the Finance Committee, the Credit Committee and the Risk Management Department are responsible for managing the Group's risks.

The Board of Governors, within its powers, decides on lending transactions.

The Board of Directors, within its powers, decides on lending transactions, is responsible for the general control over the risk management system, determines its development strategy and risk profile, and sets strategic limits and risk appetite.

The Audit Commission appointed by the Board of Governors audits the Group's activities with all risk factors taken into account.

The Management 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 Board of Directors. The Board ensures co-operation among all divisions and committees of the Bank.

The Finance Committee determines approaches to forming the optimal structure of the balance sheet, taking into account information of the current and expected level of risks associated with assets and liabilities management within the established limits and other restrictions.

It also ensures management and control over the credit risk, market risk, operational risk, reputational risk, legal risk and liquidity risk and reviews the limit-setting offers. The Credit Committee manages the Group's loan portfolio in accordance with its effective lending policy, aligns operation of the Group's divisions in terms of the credit risk management and reviews the offers for setting credit risk limits in respect of the certain counterparties.

Committees meet on a regular basis and provide the Management Board with 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 Group's performance.

During 2018, further development of the risk management system was aimed at implementation of Basel standards and best practices of development banks within the Group.

(Thousands of euros)

25. Risk management (continued)

Risk management system (continued)

In compliance with the existing procedures, the Group annually reviews limits for counterparties for the purpose of performing financial transactions and assessing their creditworthiness. As part of the lending activity analysis, the Group continuously monitors the level of its loan assets risk. During the reporting period, the Group sent its specialists to certain borrowers in order to monitor the implementation of the projects and identify potential primary evidence of impairment of loan assets.

To control and monitor the compliance with limits, the Group 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 and stop-loss limits. In addition, the Group's management receives regular reports on the status of risks within the Group.

Risk appetite

The risk appetite is the aggregate amount of risk taken by the Group to achieve its strategic goals and objectives. By approving the level of risk appetite, the Bank's Board of Directors determines the willingness to accept a risk or the amount of equity and liquidity that the Bank is willing to risk in the implementation of this strategy.

Risk appetite consists of 4 main components:

- ▶ The allocation of capital and liquidity (if necessary);
- ▶ Target allocation of capital across the main types of risk;
- ▶ The level of risk and target risk appetite in the context of the main performance indicators of the Group and risks significant for the Group;
- ▶ Determining levels of tolerance.

The procedure for determining the Group's risk appetite shall be defined by the Risk Management Department and submitted for review by the Management Board and approval by the Board of Directors of the Bank.

The risk appetite shall be approved by the Board of Directors of the Bank on an annual basis for the next year and shall be a major factor of the Group's strategic limits determining the thresholds for the Group's key performance indicators and the Group's significant risks.

In determining the risk appetite, the Group assesses whether the specified risk appetite is acceptable in the current time period and whether it will be acceptable in the future, taking into account:

- ▶ Expectations of the founders concerning the level of profitability;
- ▶ International regulatory standards;
- ▶ Current and expected future volume of transactions;
- ▶ Current and expected future structure of significant risks;
- ▶ Current and expected future level of aggregate capital.

Based on the risk appetite determined by the Board of Directors, the Management Board annually approves the Group's limits, sublimits, and risk indicators, which should not exceed the target values of the risk appetite.

Risk identification

The Group identifies and manages both external and internal risk factors throughout its organizational structure. As a result of regular analysis of the Group's exposure to different types of risks performed by the Risk Management Department, the Group 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 in the course of funds placement, 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 the Finance Committee and, if necessary, also communicated to the Management Board along with the recommendations on possible risk mitigation measures.

(Thousands of euros)

25. Risk management (continued)

Risk management system (continued)

Risk assessment, management and control

The Group's risk exposure is primarily reduced by means of collective decision-making. Strict allocation of responsibilities between divisions and officers of the Group, 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, if necessary, updated by the Group in order to reflect changed market conditions and improve the risk management methodology.

The risk monitoring system comprises:

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

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

System of credit risk management

The Group'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.

Pursuant to the established procedure, the Credit Committee establishes the limits per borrower/group of related borrowers. The Credit Committee structures the transaction to minimize credit risk. The Loan Operations Analysis Department, together with the Risk Management Department, is responsible for ongoing control over the quality of the Group's loan portfolio.

Upon preparation of a transaction by the initiating unit, it must be approved by the Credit Committee and, subsequently, by the Management Board and/or the Board of Directors/Board of Governors, within their powers.

(Thousands of euros)

25. Risk management (continued)

Credit risk (continued)

The corporate loan/credit application and appropriate project documents are reviewed by the Customer Relations Department. Based on the background information on the deal, the Customer Relations Department takes a decision whether to continue work with the client. In case of a positive decision, the Loan Operations Analysis Department makes full examination of the deal and sends the full set of required documents for reviewing the loan/credit application to the Legal Department, Risk Management Department, Security Department, Strategic Development and Analysis Department, Internal Control Department, Compliance Control Department, and Structured and Debt Financing Department. These departments prepare expert opinions in the framework of their competence. The loan/credit application is subject to review by the Credit Committee based on the Loan Operations Analysis Department's materials and expert opinions received from the departments. The procedure of making lending decisions comprises the following steps: Step 1 includes reviewing the application and making a decision by the Credit Committee (if such issue falls within its competence); Step 2 includes making a decision by the Management Board of the Bank (if such issue falls within its competence); Step 3 includes sending a set of respective documents approved by the Management Board of the Bank to the member country in order to obtain the final approval from the country of origin of the borrower or making a decision by the Board of Directors/Board of Governors, within their powers.

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

To mitigate credit risk, the Group limits concentrations of exposure by 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 of the borrowers and their ability to repay interest and principal, and on correspondent limits modification (if necessary).

The Group 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 Group. 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 Group 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 Group applies the following types of collateral for recovery of loans and fulfillment of obligations:

- ▶ Pledge of equipment and goods in turnover;
- ▶ Pledge of real estate (mortgage) and title;
- ▶ Pledge of construction investment agreements.

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

The Group assumes that the fair value of the collateral is its value estimate recognized by the Group 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 Group's internal expert estimate, or carrying amount of the collateral including adjustment coefficient (discount). Where the market value of the collateral is assessed as impaired, the borrowers are usually required to provide additional collateral.

Portfolio of loans to banks and customers (less allowance for impairment) by type of collateral is analyzed in Notes 9 and 10.

(Thousands of euros)

25. Risk management (continued)**Credit risk (continued)***Maximum exposure to credit risk*

The maximum exposure to credit risk for the components of the consolidated 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 the financial instruments are recorded at fair value, their carrying amounts represent the current credit risk exposure but not the maximum credit 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 10.

Maximum credit risk exposure by credit related commitments represents the whole amount of these commitments (Note 20).

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 consolidated statement of financial position.

Credit quality per class of financial assets

The Group assesses credit quality of financial instruments in accordance with IFRS 9 and based on 3 quality categories: – quality category I – standards financial instruments, quality category II – financial instruments with significant increase in credit risk, quality category III – impaired financial instruments. The credit quality is based on the assessment of the customer's financial position, payment discipline, credit history, compliance with its 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, and other available information.

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 (Note 6).

The following table provides information on the credit quality of long-term loans to banks and trade financing loans (Note 10) and loans to customers (Note 11) as at 31 December 2018 and 31 December 2017:

<i>31 December 2018</i>	<i>Loan amount</i>	<i>Allowance for impairment</i>	<i>Loan amount, including allowance for impairment</i>	<i>Impairment to loan amount ratio, %</i>
Trade financing loans				
Not past due (Stage 1)	65,632	(478)	65,154	0.7
Total trade financing loans	65,632	(478)	65,154	0.7
Long-term loans to banks				
Not past due (Stage 1)	112,885	(1,407)	111,478	1.2
Total long-term loans to banks	112,885	(1,407)	111,478	1.2
Loans to customers at amortized cost				
Not past due (Stage 1, 2)	548,487	(2,357)	546,130	0.4
Loans more than 90 days past due (Stage 3)	14,694	(14,694)	–	100.0
Total loans to customers at amortized cost	563,181	(17,051)	546,130	3.03
Loans to customers at fair value through other comprehensive income				
Not past due (Stage 1)	30,073	–	30,073	–
Total loans to customers at fair value through other comprehensive income	30,073	–	30,073	–
Total loans	771,771	(18,936)	752,835	2.5

*(Thousands of euros)***25. Risk management (continued)****Credit risk (continued)**

<i>31 December 2017</i>	<i>Loan amount</i>	<i>Allowance for impairment</i>	<i>Loan amount, including allowance for impairment</i>	<i>Impairment to loan amount ratio, %</i>
Trade financing loans				
Not past due	26,537	–	26,537	–
Total trade financing loans	26,537	–	26,537	–
Long-term loans to banks				
Not past due	168,997	–	168,997	–
Loans more than 90 days past due	15,254	(9,153)	6,101	60.0
Total long-term loans to banks	184,251	(9,153)	175,098	5.0
Loans to customers				
Not past due	446,910	–	446,910	–
Restructured loans	6,008	(300)	5,708	5.0
Loans more than 90 days past due	15,151	(5,255)	9,896	34.7
Total loans to customers	468,069	(5,555)	462,514	1.2
Total loans	678,857	(14,708)	664,149	2.2

Impairment assessment

The adoption of IFRS 9 fundamentally changes the Group's accounting for allowances for expected credit losses by replacing the IAS 39 incurred loss approach with the forward-looking expected credit loss ("ECL") approach. Starting from 1 January 2018, the Group recognizes the provision for ECL for all loans and other debt financial instruments not measured at FVPL, as well as for loan commitments and financial guarantee contracts, which are collectively referred to as financial instruments in this section. According to IFRS 9, requirements for impairment are not applicable to equity instruments. The allowance for ECL is based on the credit losses expected to be incurred over the life of the underlying asset (lifetime ECL), if there has been a significant increase in credit risk on this asset since the date of initial recognition. Otherwise, the allowance for ECL will be equal to 12-month expected credit losses (12-month ECL). 12-months ECL are part of lifetime ECL and represent ECL arising from defaults on the financial instrument expected to occur 12 months after the reporting date.

The Group has established a policy to perform an assessment, at the end of each reporting period, of whether a financial instrument's credit risk has increased significantly since initial recognition by considering the change in the risk of default occurring over the remaining life of the financial instrument. Based on the above, the Group classifies financial instruments exposed to credit risk as follows:

- ▶ Stage 1: At initial recognition of a financial instrument, the Group recognizes an impairment allowance in the amount equal to 12-month ECL. Stage 1 also includes loans and other financial instruments for which credit risk decreased to the extent that they have been reclassified from Stage 2.
- ▶ Stage 2: If there has been a significant increase in credit risk for the financial instrument since its initial recognition, the Group recognizes an impairment allowance in the amount equal to lifetime ECL. Financial instruments overdue more than 30 calendar days are always included in Stage 2 or Stage 3, unless the Group has reasonable and supportable information not to consider this delay a significant deterioration in the counterparty's credit quality. Stage 2 also includes loans and other credit facilities, for which credit risk has decreased to such an extent that they have been reclassified from Stage 3.
- ▶ Stage 3: Credit-impaired financial instruments. The Group recognizes an impairment allowance in the amount equal to lifetime ECL. If the Group does not have reasonable expectations regarding recoverability of the financial asset in full or in part, the gross carrying amount of the asset should be decreased. Such a decrease is considered (partial) derecognition of the financial asset. Financial instruments overdue more than 90 calendar days are always included in Stage 3, unless the Group has reasonable and supportable information not to consider this delay a significant deterioration in the counterparty's credit quality. The loan overdue less than 90 days can be included in Stage 3, if the Group has reasonable and supportable information that this loan will not be repaid and there is significant indicators of the decrease in the counterparty's credit quality.

(Thousands of euros)

25. Risk management (continued)

Credit risk (continued)

Key inputs required for ECL calculation are as follows:

- ▶ Probability of default (PD) is an estimate of the probability of default within a specified period. A default may only happen at a certain time over the assessed period, if the facility has not been previously derecognized and is still in the portfolio.
- ▶ Exposure at default (EAD) is an estimate of the exposure at default at a certain future date, adjusted to reflect its changes expected after the reporting date, including payments of interest or the principal amount due under a contract or otherwise, as well as repayment of loans issued and interest accrued on overdue payments.
- ▶ Loss given default (LGD) is an estimate of losses arising on default at a certain point of time. LGD is calculated as a difference between contractual cash flows and cash flows a creditor expects to receive, including from the sale of collateral. This estimate is usually expressed as a percentage of EAD.

To calculate the macroeconomic adjustment for ECL the Group uses a wide range of forecast information as economic inputs for its models, including:

- GDP growth rates
- Debt to GDP ratio
- Unemployment rate
- Inflation rate
- Base rates
- Exchange rates

The macroeconomic adjustment is calculated using developed and tested macroeconomic models (functions) and two macroeconomic annual forecasts of the corresponding parameters (optimistic and pessimistic scenarios). Forecast data on parameters are taken from open sources, such as Bloomberg, IMF, BMI, World Bank, central banks, and national statistical agencies.

Impairment losses and their reversal are accounted for and disclosed separately from gain or loss from modification recognized as an adjustment to the gross carrying amount of financial assets. The Group believes an increase in the credit risk related to a financial asset since the date of its initial recognition to be significant, if credit quality of a counterparty has deteriorated significantly and there are grounds to believe that this deterioration can adversely affect the counterparty's ability to meet its liabilities to the Group. In addition, the Group applies a qualitative method to identify a significant increase in credit risk associated with an asset, e.g. a list of non-performing customers / instruments or asset restructuring. Regardless of changes in ratings, an increase in credit risk since the date of initial recognition is considered significant, if contractual payments are over 30 days past due.

For ECL calculation purposes, the Group considers the financial instrument to be in default and, therefore, includes it in Stage 3 (credit-impaired assets) whenever a borrower is 90 days late with contractual payments. In case of treasury or interbank transactions, the Group considers that there is a default and takes prompt remedy measures whenever the counterparty fails to make intraday payments required by specific agreements before the end of an operating day and the Group has no grounds to believe that this non-payment was a technical delay. The Group estimates ECL on all assets included in Stage 3 on an individual basis.

The Group creates an allowance for a financial instrument in accordance with IFRS 9 that represents its estimates of losses on such a financial instrument. A financial instrument can be written off against the related allowance for expected credit losses only upon permission of the IIB's Board of Governors and where the financial instrument is determined as uncollectable and all necessary steps to collect the financial instrument are completed. Such decision is made after consideration of the information on significant changes in counterparty's financial position such as inability to repay the financial instrument and when proceedings from disposal of the collateral are insufficient to cover the debt amount in full.

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

*(Thousands of euros)***25. Risk management (continued)****Liquidity risk**

Liquidity risk is the risk of loss resulting from the Group's inability to meet its payment obligations in full when they fall due under normal and stress circumstances. Liquidity risk results from an improper balance between the Group'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 Group) and/or an unforeseen need of immediate and simultaneous discharge of its financial obligations.

Liquidity management is an integral part of the general policy for the Group's assets and liabilities management (ALM) and operates within the established limits and restrictions related to the management of risks (liquidity, interest rate and currency risk) and the Group's balance sheet items, and in accordance with the documents of planning.

Procedures for the Group's liquidity position management, ensuring the Group's ability to meet its obligations in full and on a timely basis and efficient resources management, are stipulated in the Regulations for IIB's Liquidity Position Management that enables the development of the liquidity position management function provided for by IIB's Assets and Liabilities Management Policy, as an integral part of the general function of the Group's management.

The decision making matrix related to liquidity management includes a strategic level of liquidity management (the Council), tactical level (the Management Board and special-purpose committees) and operational level (responsible structural divisions). The Asset and Liability Management Department (DUAP or ALM Unit) is responsible for organizing and aligning management of the Group's liquidity position. The Group manages its liquidity position in accordance with planning horizons (up to 12 months) and possible scenarios of movements in the liquidity position (stable, stressed).

The main instrument of liquidity position management under the stable scenario is a Plan of Cash Flows defining the cash flow by balance sheet product/instrument and taking into account the plan of future financial operations. The Group determines the balance sheet gaps, payment schedule and need for financing of future operations based on the Plan of Cash Flows. As a result of applying these instruments, DUAP issues appropriate recommendations to responsible structural divisions.

The Group has implemented a liquidity buffer to manage the Group's liquidity under the stressed scenario. Application of the liquidity buffer enables the Group to promptly monitor the sustainability and stability of the Group's balance sheet structure in case of a liquidity shortage that is critical to the Group's solvency.

The liquidity buffer is formed primarily due to liquidity reserves, namely securities recognized in the Group's balance sheet and included in the Lombard lists of the European Central Bank and Bank of Russia, and nostro accounts with banks and other financial institutions. The Group calculates its liquidity reserves as at the reporting date and for the next twelve monthly reporting dates (forecast). The liquidity buffer may be used to close the negative net position. As at 31 December 2018, the liquidity buffer amounts to EUR 135.1 million (31 December 2017: EUR 83.5 million).

Credit-related commitments of the Group are stated in accordance with contractual maturities in the table presented below. Where there is no contractual schedule of credit-related commitments, these obligations are included into the earliest date on which the client can demand their execution.

	<u>2018</u>	<u>2017</u>
Less than 1 month	17,303	25,835
1 to 3 months	34,126	72,744
3 months to 1 year	40,539	41,489
1 to 5 years	59,984	24,330
Over 5 years	35,905	–
Credit-related commitments	<u>187,857</u>	<u>164,398</u>

*(Thousands of euros)***25. 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. Quoted debt securities at fair value through other comprehensive income and equity instruments were included in the “Less than 1 month” category as they are highly liquid securities, shares and depositary receipts which the Group may sell in the short term on the arm-length basis. Securities at fair value through other comprehensive income pledged under repurchase agreements are presented on the basis of periods from the reporting date to the expiry date of the respective contractual obligations of the Group.

	31 December 2018						31 December 2017							
	<i>Less than 1 month</i>	<i>1 to 3 months</i>	<i>3 months to 1 year</i>	<i>1 to 5 years</i>	<i>Over 5 years</i>	<i>Past due</i>	<i>Total</i>	<i>Less than 1 month</i>	<i>1 to 3 months</i>	<i>3 months to 1 year</i>	<i>1 to 5 years</i>	<i>Over 5 years</i>	<i>Past due</i>	<i>Total</i>
Assets														
Cash and cash equivalents	49,214	26	–	–	–	–	49,240	65,445	652	–	–	–	–	66,097
Deposits with banks and other financial institutions	–	–	–	47,396	–	–	47,396	5,026	7,097	25,034	8,732	–	–	45,889
Derivative financial assets	–	28	65	3,627	–	–	3,720	935	–	5,072	1,754	–	–	7,761
Securities at fair value through other comprehensive income	204,332	–	–	–	–	–	204,332	–	–	–	–	–	–	–
Available-for-sale securities	–	–	–	–	–	–	–	138,737	54,783	21,907	–	–	–	215,427
Securities at amortized cost	–	84	86	4,420	36,875	–	41,465	–	–	–	–	–	–	–
Loans to banks	465	34,531	42,227	91,380	8,029	–	176,632	–	53,491	49,786	90,935	–	6,101	201,635
Loans to customers	6,751	11,986	42,185	215,571	299,710	–	576,203	8,965	8,719	77,334	147,277	210,323	9,896	462,514
Other financial assets	581	310	2	–	–	–	893	489	57	19	163	–	–	728
Total assets	261,343	46,965	84,565	362,394	344,614	–	1,099,881	220,919	124,799	179,152	248,861	210,323	15,997	1,000,051
Liabilities														
Due to banks and other financial institutions	(35,001)	(32,871)	–	–	–	–	(67,872)	–	(30,982)	(34,059)	(470)	–	–	(65,511)
Current customer accounts	(9,716)	–	–	–	–	–	(9,716)	(8,593)	–	–	–	–	–	(8,593)
Derivative financial liabilities	(1,052)	(1,380)	(14,954)	(33,557)	–	–	(50,943)	–	(89)	(1,213)	(13,771)	–	–	(15,073)
Long-term loans of banks	–	(279)	(212)	(18,391)	(38,671)	–	(57,553)	–	(24)	(59,967)	(18,819)	(16,782)	–	(95,592)
Debt securities issued	(732)	(3,406)	(134,648)	(484,668)	–	–	(623,454)	–	(3,906)	(26,519)	(478,788)	–	–	(509,213)
Other financial liabilities	(116)	(849)	(156)	(119)	(529)	–	(1,769)	(762)	(953)	(396)	(37)	–	–	(2,148)
Total liabilities	(46,617)	(38,785)	(149,970)	(536,735)	(39,200)	–	(811,307)	(9,355)	(35,954)	(122,154)	(511,885)	(16,782)	–	(696,130)
Net position	214,726	8,180	(65,405)	(174,341)	305,414	–	288,574	211,564	88,845	56,998	(263,024)	193,541	15,997	303,921
Accumulated net position	214,726	222,906	157,501	(16,840)	288,574	288,574	211,564	300,409	357,407	94,383	287,924	303,921	303,921	303,921

(Thousands of euros)

25. Risk management (continued)**Analysis of financial liabilities by remaining contractual maturities**

The table below summarizes the maturity profile of the Group's financial liabilities at 31 December 2018 and 31 December 2017 based on contractual undiscounted repayment obligations except for gross settled derivatives that are shown by contractual maturity. Debt securities issued with put options (offers) are presented as if investors will exercise their options at the earliest possible date. The Group expects that it will have to make payment on current bond offers.

<i>At 31 December 2018</i>	<i>Less than 1 month</i>	<i>1 to 3 months</i>	<i>3 to 12 months</i>	<i>1 to 5 years</i>	<i>Over 5 years</i>	<i>Total</i>
Financial liabilities						
Due to banks and other financial institutions	35,001	32,871	–	–	–	67,872
Current customer accounts	9,716	–	–	–	–	9,716
Net settled derivative financial instruments	1,097	–	–	–	–	1,097
Gross settled derivative financial instruments						
- Contractual amounts payable	596	50,905	175,068	504,272	–	730,841
- Contractual amounts receivable	(1,216)	(53,047)	(165,872)	(474,441)	–	(694,576)
Long-term loans of banks	–	565	1,155	24,540	45,897	72,157
Debt securities issued	907	6,199	154,542	510,187	–	671,835
Other liabilities	116	849	156	119	529	1,769
Total undiscounted financial liabilities	46,217	38,342	165,049	564,677	46,426	860,711

<i>At 31 December 2017</i>	<i>Less than 1 month</i>	<i>1 to 3 months</i>	<i>3 to 12 months</i>	<i>1 to 5 years</i>	<i>Over 5 years</i>	<i>Total</i>
Financial liabilities						
Due to banks and other financial institutions	–	31,331	34,783	470	–	66,584
Current customer accounts	8,593	–	–	–	–	8,593
Net settled derivative financial instruments	(904)	–	–	–	–	(904)
Gross settled derivative financial instruments						
- Contractual amounts payable	–	37,664	155,912	348,158	–	541,734
- Contractual amounts receivable	–	(42,735)	(169,034)	(350,742)	–	(562,511)
Long-term loans of banks	–	60,496	230	19,498	19,624	99,848
Debt securities issued	–	6,935	46,200	523,383	–	576,518
Other liabilities	762	953	396	37	–	2,148
Total undiscounted financial liabilities	8,451	94,644	68,487	540,804	19,624	732,010

Market risk

Market risk is the risk that the Group may incur losses due to adverse fluctuations in the 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.

Analysis of financial liabilities by remaining contractual maturities

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

The Finance Committee coordinates the Group's market risk management policy, and reviews and provides recommendations on management of market risks to the Management Board.

*(Thousands of euros)***25. Risk management (continued)****Market risk (continued)**

The Treasury Department performs day-to-day 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 Group'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 Group's open positions in foreign currencies. Price risk is the risk that the fair values of securities decrease as a result of changes in the levels of indices and the value of individual securities.

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

The Group 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 the currency position of the Group is carried out in major currencies and financial instruments of the Group attributable to a securities portfolio.

In estimating value at risk, the Group 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.

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

As at 31 December 2018 and 31 December 2017, final data on the value at risk (VaR) assessment in relation to currency and price risks assumed by the Group are represented as follows:

	<u>2018</u>	<u>2017</u>
Fixed income securities price risk	1,341	1,005
Currency risk	75	45
Equity securities price risk	–	125

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

- ▶ Analysis based on the value at risk assessment is correct in case current market conditions remain unchanged;
- ▶ 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;
- ▶ The 10-day time horizon implies the entire Group's position over this period could have been closed or hedged. The results of the 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)***25. Risk management (continued)****Market risk (continued)**

The Group has assets and liabilities denominated in several foreign currencies. The financial position and the cash flows are exposed to the effects of fluctuations in foreign currency exchange rates. Non-monetary financial instruments and financial instruments denominated in functional currency are not exposed to currency risk. The Group's exposure to currency risk as at 31 December 2018 and 31 December 2017 is presented below:

	31 December 2018					31 December 2017				
	EUR	USD	RUB	Other currencies	Total	EUR	USD	RUB	Other currencies	Total
Non-derivative financial assets										
Cash and cash equivalents	41,332	4,912	927	2,069	49,240	50,488	1,730	13,501	378	66,097
Deposits with banks and other financial institutions	47,396	–	–	–	47,396	28,936	16,953	–	–	45,889
Securities at fair value through other comprehensive income	99,347	97,401	7,584	–	204,332	–	–	–	–	–
Available-for-sale securities	–	–	–	–	–	111,516	102,202	–	1,709	215,427
Securities at amortized cost	14,957	26,508	–	–	41,465	–	–	–	–	–
Long-term loans to banks	133,242	43,390	–	–	176,632	147,253	54,382	–	–	201,635
Loans to customers	323,348	123,807	80,551	48,497	576,203	247,804	108,254	64,097	42,359	462,514
Other financial assets	445	377	71	–	893	186	323	214	5	728
Total non-derivative financial assets	660,067	296,395	89,133	50,566	1,096,161	586,183	283,844	77,812	44,451	992,290
Liabilities										
Due to banks and other financial institutions	(67,872)	–	–	–	(67,872)	(34,608)	(29,337)	–	(1,566)	(65,511)
Current customer accounts	(9,602)	(114)	–	–	(9,716)	(8,481)	(112)	–	–	(8,593)
Long-term loans of banks	(22,994)	(22,113)	–	(12,446)	(57,553)	(82,694)	–	–	(12,898)	(95,592)
Debt securities issued	(170,085)	–	(230,032)	(223,337)	(623,454)	(90,017)	–	(267,112)	(152,084)	(509,213)
Other financial liabilities	(652)	(227)	(870)	(20)	(1,769)	(546)	(175)	(1,427)	–	(2,148)
Total non-derivative financial liabilities	(271,205)	(22,454)	(230,902)	(235,803)	(760,364)	(216,346)	(29,624)	(268,539)	(166,548)	(681,057)
Net balance sheet position (excluding derivative financial instruments)	388,862	273,941	(141,769)	(185,237)	335,797	369,837	254,220	(190,727)	(122,097)	311,233
Derivative financial instruments										
Claims	258,078	–	192,297	206,977	657,352	190,457	–	197,443	132,639	520,539
Liabilities	(394,056)	(237,679)	(53,272)	(19,568)	(704,575)	(296,697)	(220,909)	–	(10,245)	(527,851)
Net balance sheet position, including derivative financial instruments	252,884	36,262	(2,744)	2,172	288,574	263,597	33,311	6,716	297	303,921

*(Thousands of euros)***25. Risk management (continued)****Market risk (continued)*****Interest rate risk***

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

The sensitivity of the consolidated income statement is the effect of the assumed changes in interest rates on net interest income for one year, based on financial assets and financial liabilities with floating rates. The sensitivity of equity is calculated by revaluing inactive traded available-for-sale securities with fixed rates as at 31 December 2018 for the effects of the assumed changes in interest rates based on the assumption that there are parallel shifts in the yield curve.

	<i>Increase in basis points</i>	<i>Sensitivity of the income statement</i>	<i>Sensitivity of equity</i>
	<i>2018</i>	<i>2018</i>	<i>2018</i>
BUBOR	0.20%	5	–
EURIBOR	0.20%	872	–
Ger Gov (Average)	0.75%	(2,049)	(3,448)
LIBOR USD	0.50%	344	–
LEONIA	0.10%	9	–
MOSPRIME	0.75%	699	–
PRIBOR	0.80%	(256)	–
ROBOR	0.80%	(1,274)	–
US Treasuries (Average)	1.00%	2,884	(4,024)
OFZ (federal loan bonds) (Average)	1.25%	(2,590)	(210)

	<i>Decrease in basis points</i>	<i>Sensitivity of the income statement</i>	<i>Sensitivity of equity</i>
	<i>2018</i>	<i>2018</i>	<i>2018</i>
BUBOR	0.05%	(1)	–
EURIBOR	0.01%	(44)	–
Ger Gov (Average)	0.40%	1,093	1,839
LIBOR USD	0.15%	(103)	–
LEONIA	0.05%	(4)	–
MOSPRIME	1.00%	(933)	–
PRIBOR	0.15%	48	–
ROBOR	0.40%	637	–
US Treasuries (Average)	0.50%	(1,442)	2,012
OFZ (federal loan bonds) (Average)	1.40%	2,897	236

	<i>Increase in basis points</i>	<i>Sensitivity of the income statement</i>	<i>Sensitivity of equity</i>
	<i>2017</i>	<i>2017</i>	<i>2017</i>
RGBEY	0.75%	(719)	–
LIBOREUR	0.25%	792	–
LIBOR USD	0.70%	(214)	–
3Y Swap-RON	6.74%	(15,479)	–
YTM 5Y USTreasuries	1.30%	1,761	–
YTM 5Y German Treasuries	0.50%	962	–

	<i>Decrease in basis points</i>	<i>Sensitivity of the income statement</i>	<i>Sensitivity of equity</i>
	<i>2017</i>	<i>2017</i>	<i>2017</i>
RGBEY	1.75%	1,677	–
LIBOR EUR	0.01%	(32)	–
LIBOR USD	0.08%	24	–
3Y Swap-RON	4.47%	10,266	–
YTM 5Y USTreasuries	0.50%	(677)	–
YTM 5Y German Treasuries	0.40%	(192)	–

(Thousands of euros)

25. Risk management (continued)

Market risk (continued)

Indices listed in the tables above:

BUBOR - Budapest Interbank HUF Offered Rate (1 and 3 months)

EURIBOR - Europe Interbank EUR Offered Rate (3 and 6 months)

Ger Gov (Average) - German Government Bonds Aggregate Effective Yield Until Redemption

RGBEY – Russian Government Bonds Effective Yield Until Redemption

LIBOR EUR – London Interbank EUR Offered Rate (3 and 6 months)

LIBOR USD – London Interbank USD Offered Rate (1, 3 and 6 months)

LEONIA - LEv OverNight Index Average

MOSPRIME - indicative rate of issuing RUB-denominated loans (deposits) on Moscow market (3 months)

PRIBOR - Prague Interbank CZK Offered Rate (3 months)

ROBOR - Romanian Interbank RON Offered Rate (3 months)

US Treasuries (Average) - US Government Bonds Aggregate Effective Yield Until Redemption

OFZ (Average) - Russian Federal Loan Bonds Aggregate Effective Yield Until Redemption

3Y Swap-RON – three-year bid rate in Romanian leu on the swap market

YTM 5Y US Treasuries – yield-to-maturity of five-year US Treasuries

YTM 5Y German Treasuries – yield-to-maturity of five-year Germany Treasuries.

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 Group's property.

Generally, the Management 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 Management 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 Group continuously seeks to enhance its business processes, operating structure and personnel incentives system in order to minimize the impact of operational risk.

26. Fair value measurements

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 Group using available market information, where it exists, and appropriate valuation methodologies. However, professional judgment is necessarily required to interpret market data to determine the 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.

*(Thousands of euros)***26. Fair value measurements (continued)****Fair value hierarchy**

The Group 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 that use inputs which have a significant effect on the recognized fair value that are not based on observable market data.

For the purpose of fair value disclosures, the Group 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. The following table shows an analysis of financial instruments recorded at fair value by level of the fair value hierarchy as at 31 December 2018:

	<i>Level 1</i> <i>31 December</i> <i>2018</i>	<i>Level 2</i> <i>31 December</i> <i>2018</i>	<i>Level 3</i> <i>31 December</i> <i>2018</i>	<i>Total</i> <i>31 December</i> <i>2018</i>
Assets measured at fair value				
Derivative financial assets	–	3,720	–	3,720
Government bonds of member countries	41,272	–	–	41,272
Corporate bonds	115,960	46,421	–	162,381
Quoted equity instruments	–	5	–	5
Loans to customers at fair value through other comprehensive income	30,073	–	–	30,073
Investment property	–	–	20,788	20,788
Property and equipment – buildings	–	–	66,569	66,569
Liabilities measured at fair value				
Derivative financial liabilities	–	50,943	–	50,943
Assets for which fair values are disclosed				
Cash and cash equivalents	276	48,964	–	49,240
Deposits with banks and other financial institutions	–	–	47,396	47,396
Securities at amortized cost	–	37,347	–	37,347
Loans to banks at amortized cost	–	–	177,186	177,186
Loans to customers	–	–	564,178	564,178
Liabilities for which fair values are disclosed				
Due to banks and other financial institutions	–	–	67,872	67,872
Current customer accounts	–	–	9,716	9,716
Long-term loans of banks	–	–	57,553	57,553
Debt securities issued	–	627,394	–	627,394

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(Thousands of euros)

26. Fair value measurements (continued)**Fair value hierarchy (continued)**

The following table shows an analysis of financial instruments recorded at fair value by level of the fair value hierarchy as at 31 December 2017:

	<i>Level 1</i> 2017	<i>Level 2</i> 2017	<i>Level 3</i> 2017	<i>Total</i> 2017
Assets measured at fair value				
Derivative financial assets	–	7,761	–	7,761
Government bonds of member countries	45,891	–	–	45,891
Corporate bonds	149,277	18,544	–	167,821
Quoted equity instruments	1,710	5	–	1,715
Investment property	–	–	21,853	21,853
Property and equipment – buildings	–	–	67,572	67,572
Liabilities measured at fair value				
Derivative financial liabilities	–	15,073	–	15,073
Assets for which fair values are disclosed				
Cash and cash equivalents	85	66,012	–	66,097
Deposits with banks and other financial institutions	–	–	45,889	45,889
Loans to banks	–	–	201,743	201,743
Loans to customers	–	–	465,973	465,973
Liabilities for which fair values are disclosed				
Due to banks and other financial institutions	–	–	65,511	65,511
Current customer accounts	–	–	8,593	8,593
Long-term loans of banks	–	–	95,592	95,592
Debt securities issued	–	514,893	–	514,893

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 Group's financial instruments that are recorded in the consolidated financial statements. The table does not include the fair values of non-financial assets and non-financial liabilities.

	<i>Carrying amount</i> 31 December 2018	<i>Fair value</i> 31 December 2018	<i>Unrecognized gain/(loss)</i> 31 December 2018	<i>Carrying amount</i> 31 December 2017	<i>Fair value</i> 31 December 2017	<i>Unrecognized gain/(loss)</i> 31 December 2017
Financial assets						
Cash and cash equivalents	49,240	49,240	–	66,097	66,097	–
Deposits with banks and other financial institutions	47,396	47,396	–	45,889	45,889	–
Securities at amortized cost	41,465	37,347	(4,118)	–	–	–
Loans to banks	176,632	177,186	554	201,635	201,743	108
Loans to customers at amortized cost	546,130	564,178	18,048	462,514	465,973	3,459
Financial liabilities						
Due to banks and other financial institutions	67,872	67,872	–	65,511	65,511	–
Current customer accounts	9,716	9,716	–	8,593	8,593	–
Long-term loans of banks	57,553	57,553	–	95,592	95,592	–
Debt securities issued	623,454	627,394	(3,940)	509,213	514,893	(5,680)
Total unrecognized change in unrealized fair value			10,544			(2,113)

(Thousands of euros)

26. Fair value measurements (continued)

Fair value measurements

The Group determines the policies and procedures for both recurring fair value measurement, such as unlisted derivatives, investment property and buildings, and for non-recurring measurement, such as inventories. Unlisted derivatives are measured by the Finance Department.

External appraisers are involved for valuation of significant assets, such as buildings and real estate. Involvement of external appraisers is decided upon by the Bank's Finance Department.

Selection criteria include market knowledge, reputation, independence and compliance with professional standards.

Methodologies and assumptions

The following describes the methodologies and assumptions used to determine fair values of assets and liabilities recorded at fair value in the consolidated financial statements and of those items that are not measured at fair value in the consolidated statement of financial position, but their fair value is disclosed.

Assets for which fair value approximates their carrying amount

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

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

Management has estimated that as at 31 December 2018 and 31 December 2017 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 existing practice of renegotiating interest rates to reflect current market conditions, and, therefore, the majority of balances carries interest at rates approximating market interest rates.

Financial instruments with fixed and floating rates

The fair value of instruments with floating interest rates is approximately equal to their carrying amount. In case of significant changes of the market situation interest rates on loans to customers and banks, and long-term loans of banks at a fixed interest rate may be revised. Consequently, interest rates on the financial instruments issued or received shortly before the balance sheet date are not significantly different from the current interest rates for new instruments with a similar credit risk and a similar maturity. If the Group determines that the rates for loans issued or borrowings are significantly different from the current market rates, the Group determines the fair value of such loans issued and borrowings. The valuation is based on the discounted cash flow method using current market interest rates for new financial instruments with a similar credit risk and a similar maturity. The discount rates depend on the currency, the maturity of the instrument and the credit risk of the counterparty. Management determines that the fair value of amounts due to banks and long-term loans of banks did not differ significantly from their carrying amounts as at 31 December 2018 and 31 December 2017.

Investment property

The Group engages an independent appraiser for the investment property fair value measurement. Fair values of investment properties are determined using the market approach and the discounted cash flow method.

Under the market approach, measurements are based on market transaction prices, significantly adjusted for difference in the nature, location or condition of a specific property. Under the discounted cash flow method, the duration of the cash flows is typically driven by market behavior that is a characteristic of the class of real property. Periodic cash flow is typically estimated as gross income less vacancy, non-recoverable expenses, collection losses, lease incentives, maintenance cost, agent and commission costs and other operating and management expenses. The series of periodic net operating income, along with an estimate of the terminal value anticipated at the end of the projection period, is then discounted.

Management believes that at 31 December 2018 fair values of investment properties do not differ significantly from their carrying amounts at the above date.

(Thousands of euros)

26. Fair value measurements (continued)**Methodologies and assumptions (continued)****Property and equipment – buildings**

The Group engages an independent appraiser for the real estate property fair value measurement. Fair values of real estate properties are determined using the market approach. This means that valuations are based on market transaction prices, significantly adjusted for differences in the nature, location or condition of a specific property.

Management believes that at 31 December 2018 fair values of real estate properties do not differ significantly from their carrying amounts at the above date.

There were no transfers of financial instruments between Level 1 and Level 2 in 2018 and 2017.

Changes in Level 3 assets and liabilities at fair value

The following table shows a reconciliation of the opening and closing amounts of Level 3 assets and liabilities that are recorded at fair value:

	<i>At 1 January 2018</i>	<i>Gains/(losses) recorded in profit or loss</i>	<i>Gains/(losses) recorded in comprehen- sive income</i>	<i>Additions/ (disposals)</i>	<i>Transfer to property and equipment</i>	<i>At 31 December 2018</i>
Assets						
Property and equipment – buildings	67,572	(1,124)	–	121	–	66,569
Investment property	21,853	–	–	(1,065)	–	20,788
Total	89,425	(1,124)	–	(944)	–	87,357

	<i>At 1 January 2017</i>	<i>Gains/(losses) recorded in profit or loss</i>	<i>Gains/(losses) recorded in comprehen- sive income</i>	<i>Additions</i>	<i>Transfer to property and equipment</i>	<i>At 31 December 2017</i>
Assets						
Property and equipment – buildings	67,527	(1,108)	803	350	–	67,572
Investment property	21,840	(26)	–	39	–	21,853
Total	89,367	(1,134)	803	389	–	89,425

27. Segment information

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

Credit investment activity	Investment banking services, including long-term corporate and interbank financing
Treasury	Operations in financial markets, transactions with securities, derivative financial instruments and foreign currency, and liquidity management
Other operations	Operational leasing services, other operations

(Thousands of euros)

27. 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 consolidated financial statements. The following table presents income, profit, assets and liabilities of the Group's operating segments:

<i>31 December 2018</i>	<i>Credit investment activity</i>	<i>Treasury</i>	<i>Other operations</i>	<i>Total</i>
Income				
<i>External customers</i>				
Interest income calculated using the EIR method	37,647	8,248	34	45,929
Other interest income	–	16,874	–	16,874
Fee and commission income	1,779	–	–	1,779
Net gains from operations with securities at fair value through profit or loss	–	92	–	92
Net gains from operations with securities at fair value through other comprehensive income	–	2,299	–	2,299
Dividend income	–	6	–	6
Income from lease of investment property	–	–	3,956	3,956
Other segment income	306	–	894	1,200
Total income	39,732	27,519	4,884	72,135
Interest expenses calculated using the EIR method	(23,035)	(13,109)	–	(36,144)
Other interest expenses	–	(3,047)	–	(3,047)
Fee and commission expense	(115)	(193)	(90)	(398)
Net losses from operations with foreign currencies and derivatives	–	(5,062)	20	(5,042)
Allowance for credit losses from impairment of financial instruments	(553)	389	3	(161)
Cost of inventories sold	–	–	(48)	(48)
Other segment expenses	(698)	(1)	(532)	(1,231)
Segment results	15,331	6,496	4,237	26,064
Other unallocated expenses				(20,442)
Profit for the period				5,622
Development portfolio	754,236	107,726	–	861,962
Other segment assets	–	238,242	94,153	332,395
Total segment assets	754,236	345,968	94,153	1,194,357
Total segment liabilities	450,949	360,930	6,479	818,358
Other segment information				
Capital expenditures	–	–	572	572

(Thousands of euros)

27. Segment information (continued)

The Group's management separates the "Development portfolio" assets allocated within operating segments. The criterion for the separation is whether the investment corresponds the Bank's mission. The "Development portfolio" includes loans to banks and loans to customers excluding impaired loan projects and investments in debt securities purchased upon the initial placement by the issuer.

<i>31 December 2017</i>	<i>Credit investment activity</i>	<i>Treasury</i>	<i>Other operations</i>	<i>Total</i>
Income				
<i>External customers</i>				
Interest income calculated using the EIR method	26,662	9,263	38	35,963
Other interest income	–	19,932	–	19,932
Fee and commission income	1,763	–	–	1,763
Net gains from available-for-sale investment securities	–	7,399	–	7,399
Dividend income	–	123	–	123
Income from lease of investment property	–	–	4,034	4,034
Other segment income	329	–	214	543
Total income	28,754	36,717	4,286	69,757
Interest expenses calculated using the EIR method	(18,656)	(13,910)	–	(32,566)
Other interest expenses	–	(1,542)	–	(1,542)
Fee and commission expense	(16)	(109)	(8)	(133)
Net losses from operations with foreign currencies and derivatives	–	(2,462)	21	(2,441)
Allowance for impairment of financial assets	(12,165)	–	29	(12,136)
Net losses from revaluation of investment property	–	–	(26)	(26)
Other segment expenses	(79)	(23)	(934)	(1,036)
Segment results	(2,162)	18,671	3,368	19,877
Other unallocated expenses				(18,872)
Profit for the period				1,005
Development portfolio	648,404	104,932	–	753,336
Other segment assets	15,997	229,906	96,801	342,704
Total segment assets	664,401	334,838	96,801	1,096,040
Total segment liabilities	359,914	334,477	5,983	700,378
Other segment information				
Capital expenditures	–	–	1,013	1,013

In 2018, the Group's revenue from lease operations with two external counterparties (31 December 2017: two external counterparties) exceeded 20% of the Group's total revenue (2018: EUR 2,674 thousand; 2017: EUR 2,996 thousand).

*(Thousands of euros)***27. Segment information (continued)****Geographical information**

Allocation of the Group's revenue from transactions with external customers and non-current assets based on the location of these customers and assets for the years ended 31 December 2018 and 31 December 2017 is presented in the table below:

	<i>31 December 2018</i>				<i>31 December 2017</i>			
	<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 calculated using the EIR method	10,361	25,239	10,329	45,929	9,346	17,417	9,200	35,963
Other interest income	8,174	269	8,431	16,874	5,376	346	14,210	19,932
Income from lease of investment property	3,731	225	–	3,956	3,860	174	–	4,034

Non-current assets include investment property.

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(Thousands of euros)

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

Information on risk concentration by geographical region is based on the geographical location of the Group's counterparties. The geographical concentration of the Group's assets and liabilities as at 31 December 2018 and 31 December 2017 is presented below:

	<i>31 December 2018</i>										
	<i>Russian Federation</i>	<i>Republic of Bulgaria</i>	<i>Romania</i>	<i>Slovak Republic</i>	<i>Hungary</i>	<i>Mongolia</i>	<i>Socialist Republic of Vietnam</i>	<i>Czech Republic</i>	<i>Republic of Cuba</i>	<i>Other countries</i>	<i>Total</i>
Assets											
Cash and cash equivalents	1,098	734	1,108	3,073	808	–	–	4	–	42,415	49,240
Deposits with banks and other financial institutions	18,776	–	–	–	–	–	–	–	–	28,620	47,396
Derivative financial assets	65	–	–	–	–	–	–	–	–	3,655	3,720
Securities at fair value through other comprehensive income	12,429	15,037	10,003	1,149	–	–	–	42,711	–	123,003	204,332
Securities at amortized cost	–	–	–	–	–	–	–	–	–	41,465	41,465
Long-term loans to banks	–	–	–	–	–	48,431	24,412	–	49,416	54,373	176,632
Loans to customers	99,908	134,543	71,916	89,601	34,454	26,805	21,935	–	–	97,041	576,203
Other financial assets	320	–	191	–	–	43	–	–	–	339	893
Assets	132,596	150,314	83,218	93,823	35,262	75,279	46,347	42,715	49,416	390,911	1,099,881
Liabilities											
Due to banks and other financial institutions	–	47,871	–	–	–	–	–	–	–	20,001	67,872
Derivative financial liabilities	20,796	–	–	–	–	–	–	–	–	30,147	50,943
Long-term loans of banks	–	–	–	–	12,446	–	–	–	–	45,107	57,553
Long-term securities issued	230,032	–	333,977	30,179	–	–	–	29,266	–	–	623,454
Other financial liabilities	1,606	–	–	–	–	–	–	–	–	163	1,769
Liabilities	252,434	47,871	333,977	30,179	12,446	–	–	29,266	–	95,418	801,591

(Thousands of euros)

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

	<i>31 December 2017</i>										
	<i>Russian Federation</i>	<i>Republic of Bulgaria</i>	<i>Romania</i>	<i>Slovak Republic</i>	<i>Hungary</i>	<i>Mongolia</i>	<i>Socialist Republic of Vietnam</i>	<i>Czech Republic</i>	<i>Republic of Cuba</i>	<i>Other countries</i>	<i>Total</i>
Assets											
Cash and cash equivalents	1,209	792	226	35	–	–	–	36	–	63,799	66,097
Deposits with banks and other financial institutions	3,082	–	–	–	–	32,132	–	–	–	10,675	45,889
Derivative financial assets	3,340	–	–	–	–	–	–	–	–	4,421	7,761
Available-for-sale investment securities	11,947	30,098	–	10,010	13,817	–	–	34,107	–	115,448	215,427
Loans to banks	89,545	–	–	–	–	33,735	25,252	–	49,863	3,240	201,635
Loans to customers	81,817	57,694	73,185	60,464	42,910	24,425	–	49,967	–	72,052	462,514
Other financial assets	382	6	–	–	5	5	–	1	–	329	728
Assets	191,322	88,590	73,411	70,509	56,732	90,297	25,252	84,111	49,863	269,964	1,000,051
Liabilities											
Due to banks and other financial institutions	1,460	–	–	7,508	–	–	–	1,566	–	54,977	65,511
Derivative financial liabilities	4,480	–	1,213	–	–	–	–	–	–	9,380	15,073
Long-term loans of banks	9,959	7,470	–	–	20,367	–	–	–	–	57,796	95,592
Long-term securities issued	266,191	–	212,869	30,153	–	–	–	–	–	–	509,213
Other financial liabilities	1,658	33	15	8	–	237	–	–	–	197	2,148
Liabilities	283,748	7,503	214,097	37,669	20,367	237	–	1,566	–	122,350	687,537

Other countries include non-member countries.

*(Thousands of euros)***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.

Volumes of related party transactions, outstanding balances at 31 December 2018 and 31 December 2017, and related expenses and income for the year ended 31 December 2018 and 31 December 2017 are as follows:

		<i>31 December 2018</i>	<i>31 December 2017</i>
	<i>Related party</i>	<i>Carrying amount</i>	<i>Carrying amount</i>
Consolidated statement of financial position			
Current customer accounts	Key management personnel	1,577	1,420
Other assets	Key management personnel	21	–
Other liabilities	Key management personnel	769	593
		<i>2018</i>	<i>2017</i>
	<i>Related party</i>	<i>Income/ (expense)</i>	<i>Income/ (expense)</i>
Consolidated income statement			
Interest expenses on current customer accounts	Key management personnel	(33)	(52)
Net interest expense after allowance for loan impairment		(33)	(52)
Expenses from operating activities		(33)	(52)
Employee benefits	Key management personnel	(1,687)	(1,398)
Compensation for travel expenses and medical insurance	Key management personnel	(36)	(32)
Operating expenses		(1,723)	(1,430)
Net loss for the period		(1,756)	(1,482)

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*(Thousands of euros)***29. Changes in liabilities arising from financing activities**

<i>Notes</i>	<i>Debt securities issued</i>	<i>Long-term loans of banks</i>	<i>Total liabilities arising from financing activities</i>
Carrying amount at 31 December 2016	272,528	73,349	345,877
Additions	348,661	36,185	384,846
Repayment	(88,290)	(13,451)	(101,741)
Interest paid	(24,522)	(1,690)	(26,212)
Translation differences	(26,095)	(1,178)	(27,273)
Non-cash transactions	(920)	–	(920)
Interest accrued	27,851	2,377	30,228
Carrying amount at 31 December 2017	509,213	95,592	604,805
Additions	228,798	20,845	249,643
Repayment	(76,792)	(60,455)	(137,247)
Interest paid	(31,371)	(734)	(32,105)
Translation differences	(39,269)	1,094	(38,175)
Interest accrued	32,875	1,211	34,086
Carrying amount at 31 December 2018	623,454	57,553	681,007

Translation differences represent a daily revaluation of liabilities denominated in a currency other than the euro. The Group uses derivatives to mitigate currency risks (Note 7). As at 31 December 2018, interest of RUB 13,636 thousand (31 December 2017: EUR 15,453 thousand) received under cross-currency interest rate swap agreements, shifting interest expenses on issued debt securities denominated in currencies other than the euro, is recorded in the “Interest paid” line of the consolidated statement of cash flows.

30. Capital adequacy

The capital adequacy ratio is the most important financial indicator characterizing credibility of credit institutions and is estimated as the ratio of the capital base to risk-weighted assets expressed as a percentage. Approval of the capital adequacy ratio is the exclusive competency of the IIB’s Board of Governors.

The Basel Committee on Banking Supervision recommends maintaining the ratio of capital to risk-weighted assets (“capital adequacy ratio”) above the prescribed minimum level. As at 31 December 2018, this minimum level was 8% (31 December 2017: 8%).

Besides, taking into account the Bank’s status as a multilateral development institution and the structure of the Bank’s member countries, the IIB’s Board of Governors set the capital adequacy ratio at the level of not less than 25% as at 31 December 2018 (31 December 2017: 25%).

The following table shows the composition of the Group’s capital position calculated in accordance with the Basel Accord (Basel II) as at 31 December 2018 and 31 December 2017.

	<i>31 December 2018</i>	<i>31 December 2017</i>
Capital		
Tier 1 capital	368,749	380,443
Tier 2 capital	6,381	13,988
Total regulatory capital	375,130	394,431
Risk-weighted assets		
Credit risk	863,716	821,863
Market risk	188,040	177,273
Operational risk	41,472	43,411
Total risk-weighted assets	1,093,228	1,042,547
Total capital expressed as a percentage of risk-weighted assets, % (“capital adequacy ratio”)	34.39%	37.83%
Total tier 1 capital expressed as a percentage of risk-weighted assets, % (“tier 1 capital adequacy ratio”)	33.73%	36.49%