CEB

COUNCIL OF EUROPE DEVELOPMENT BANK

REPORT OF THE GOVERNOR 2005





CEB 50th anniversary

KEY FIGURES

in million euros

	2005	2004		2003	2002
	In accordance with IFRS	*Restated in accordance with IFRS*			
Loans disbursed during the year	**1 559**	**1 530**	**1 530**	**1 589**	**1 537**
Projects approved during the year	**2 517**	**1 751**	**1 751**	**2 149**	**1 605**
Loans outstanding	**11 483**	**10 765**	**10 765**	**9 903**	**9 350**
Shareholders' equity (after allocation of profit)	**4 610**	**4 529**	**4 522**	**4 358**	**4 254**
Usable capital (after allocation of profit)	**1 685**	**1 604**	**1 581**	**1 470**	**1 384**
Total assets	**17 675**	**16 396**	**16 390**	**14 786**	**14 217**
Net profit	**88.5**	**121.0**	**115.2**	**86.9**	**95.2**
Selective Trust Account					
Social dividends cumulated since the STA's inception	**82.4**	**74.4**	**74.4**	**64.4**	**63.5**
Balance available (after allocation of profit)	**24.8**	**37.7**	**37.7**	**33.7**	**24.5**

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REPORT OF THE GOVERNOR

Financial year 2005



CEB 50th anniversary



THE BANK'S MEMBER STATES Year of accession

ALBANIA	1999	HOLY SEE	1973	POLAND	1998
BELGIUM	1956	HUNGARY	1998	PORTUGAL	1976
BOSNIA AND HERZEGOVINA	2003	ICELAND	1956	ROMANIA	1996
BULGARIA	1994	IRELAND	2004	SAN MARINO	1989
CROATIA	1997	ITALY	1956	SERBIA AND MONTENEGRO	2004
CYPRUS	1962	LATVIA	1998	SLOVAK REPUBLIC	1998
CZECH REPUBLIC	1999	LIECHTENSTEIN	1976	SLOVENIA	1994
DENMARK	1978	LITHUANIA	1996	SPAIN	1978
ESTONIA	1998	LUXEMBOURG	1956	SWEDEN	1977
FINLAND	1991	MALTA	1973	SWITZERLAND	1974
FRANCE	1956	MOLDOVA	1998	"THE FORMER YUGOSLAV REPUBLIC OF MACEDONIA"	1997
GERMANY	1956	NETHERLANDS	1978	TURKEY	1956
GREECE	1956	NORWAY	1978		





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MEMBERSHIP OF THE BANK'S ORGANS as at 31 December 2005*

GOVERNING BOARD		ADMINISTRATIVE COUNCIL
LARS KOLTE Managing Director, Eksport Kredit Fonden, Copenhagen	Chairmen	RAINER STECKHAN Former Director of the World Bank
CHARLES GHISLAIN Ambassador Extraordinary and Plenipotentiary, Permanent Representative of Belgium to the Council of Europe, Strasbourg	Vice-Chairs	RENALDO MÄNDMETS Deputy Secretary General for Foreign Relations, Ministry of Finance, Tallinn
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CHARLES GHISLAIN Ambassador Extraordinary and Plenipotentiary, Permanent Representative of Belgium to the Council of Europe, Strasbourg	Belgium	FRANCISCUS GODTS Administrator, International and European Financial Affairs, Federal Public Service Finance, Brussels
BORISLAV MARIĆ Ambassador Extraordinary and Plenipotentiary, Permanent Representative of Bosnia and Herzegovina to the Council of Europe, Strasbourg	Bosnia and Herzegovina	LJERKA MARIĆ Minister of Finances and Treasury, Sarajevo
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DANIEL BUČAN Ambassador Extraordinary and Plenipotentiary, Permanent Representative of Croatia to the Council of Europe, Strasbourg	Croatia	ANA HRASTOVIĆ Assistant Minister of Finance, Directorate for European Integration and International Financial Relations, Ministry of Finance, Zagreb
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ALAR STREIMANN Ambassador Extraordinary and Plenipotentiary, Permanent Representative of Estonia to the Council of Europe, Strasbourg	Estonia	RENALDO MÄNDMETS Deputy Secretary General for Foreign Relations, Ministry of Finance, Tallinn

*The Bank's organs are: the Governing Board, the Administrative Council, the Governor and the Auditing Board. In accordance with Article XIII, the secretariat of the Bank's organs is provided by the "Secretariat of the Partial Agreement on the Development Bank" at the Council of Europe in Strasbourg (Head of the Secretariat of the Partial Agreement: MS GIUSI PAJARDI; Executive Secretary to the organs: Mr GYÖRGY BERGOU).

GOVERNING BOARD

ADMINISTRATIVE COUNCIL

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Holy See

Mgr Vito RALLO

Special Envoy of the Holy See to the Council of Europe, Strasbourg

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Liechtenstein

Daniel OSPELT

Ambassador Extraordinary and Plenipotentiary, Permanent Representative of Liechtenstein to the Council of Europe, Strasbourg

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Ronald MAYER Ambassador Extraordinary and Plenipotentiary, Permanent Representative of Luxembourg to the Council of Europe, Strasbourg	Luxembourg	**Jérôme HAMILIUS** Government Adviser, Ministry of Finance, Luxembourg
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Joaquim DUARTE Ambassador Extraordinary and Plenipotentiary, Permanent Representative of Portugal to the Council of Europe, Strasbourg	Portugal	**Lina NETO** Deputy Director General, General Directorate for European Affairs and International Relations, Ministry of Finance, Lisbon
Gheorghe MAGHERU Ambassador Extraordinary and Plenipotentiary, Permanent Representative of Romania to the Council of Europe, Strasbourg	Romania	**Claudiu DOLTU** Secretary of State, Ministry of Public Finance, Bucharest
Guido BELLATTI CECCOLI Ambassador, Permanent Representative of San Marino to the Council of Europe, Strasbourg	San Marino	**Raffaele GIARDI** Counsellor, Ministry of Finance, Republic of San Marino
Sladjana PRICA Ambassador Extraordinary and Plenipotentiary, Permanent Representative of Serbia and Montenegro to the Council of Europe, Strasbourg	Serbia and Montenegro	**Miroslav IVANICŠEVIĆ** Deputy Prime Minister for Financial Sector and Public Expenditure, Podgorica
Anna LAMPEROVÁ Ambassador Extraordinary and Plenipotentiary, Permanent Representative of Slovak Republic to the Council of Europe, Strasbourg	Slovak Republic	**Mária KOMPIŠOVÁ** Director General of the European Affairs Section, Ministry of Finance, Bratislava

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ESTANISLAO DE GRANDES PASCUAL Ambassador Extraordinary and Plenipotentiary, Permanent Representative of Spain to the Council of Europe, Strasbourg	Spain	RAMÓN GUZMÁN ZAPATER Director General of International Finance, Ministry of Economy, Madrid
PER SJÖGREN Ambassador Extraordinary and Plenipotentiary, Permanent Representative of Sweden to the Council of Europe, Strasbourg	Sweden	BJÖRN FRITJOFSSON Director, International Financial Institutions, Ministry of Finance, Stockholm
JEAN-CLAUDE JOSEPH Ambassador Extraordinary and Plenipotentiary, Permanent Representative of Switzerland to the Council of Europe, Strasbourg	Switzerland	MARTIN ROHNER Head of Division, Multilateral Financial Institutions, State Secretariat for Economic Affairs, Bern LUKAS SIEGENTHALER (since 9-1-2006) Head of Division, Multilateral Financial Institutions, State Secretariat for Economic Affairs, Bern
ELEONORA PETROVA-MITEVSKA Ambassador Extraordinary and Plenipotentiary, Permanent Representative of "the former Yugoslav Republic of Macedonia" to the Council of Europe, Strasbourg	"the former Yugoslav Republic of Macedonia"	MELAIM ADEMI State Secretary, Ministry of Finance, Skopje
DARYAL BATIBAY Ambassador Extraordinary and Plenipotentiary, Permanent Representative of Turkey to the Council of Europe, Strasbourg	Turkey	MEMDUH ASLAN AKÇAY Director General, General Directorate of Foreign Economic Relations, Undersecretariat of the Treasury, Ankara

GOVERNOR

RAPHAËL ALOMAR

VICE-GOVERNORS

NUNZIO GUGLIELMINO (Vice-Governor Delegate)
KRZYSZTOF J. NERS
APOLONIO RUIZ LIGERO

AUDITING BOARD

Bulgaria: NADEZHDA SANDOLOVA, Head of the Audit Department, National Audit Office, Sofia
Liechtenstein: RENÉ H. MELLIGER, Chairman of the Financial Market Authority, Vaduz
Switzerland: PAUL BRÜGGER, Head of the Control of Federal Finances Legal Service, Bern

2006 will mark the fiftieth anniversary of the institution's creation. This date provides an opportunity to recall that the CEB is the oldest of the international financial institutions in Europe; it is also an opportunity to consider the ambitions underpinning its creation and how the institution has evolved during its half century of history.

The institution's origins in war-scarred Europe

Immediately following the Second World War, the brutal installation of non democratic regimes to the East of the Iron Curtain triggered a flood of political refugees into Western Europe and, in particular, of so-called *national* refugees in Germany. In the face of this tragic problem, Pierre Schneiter, Special Representative of the Council of Europe for National Refugees and Over-population, was entrusted with a mission of reflection.

He proposed a flexible financial technique: the creation, by members of the Council of Europe, of an autonomous social institution with the legal capacity to borrow and to contribute to the financing of projects providing for the resettlement of refugees. Thus was born the "*Council of Europe Resettlement Fund for National Refugees and Over-Population in Europe*", the first of the Council of Europe's Partial Agreements, signed by eight countries on 16 April 1956.

Steady consolidation

Endowed from the start with an exclusively social purpose, this new organisation had only very modest beginnings since, in addition to the limited number of its founding member countries, its initial capital was under seven million dollars. From this, the institution's first years saw the steady development of its geographical scope and financial capacity.

When the Resettlement Fund reached its twentieth anniversary, Pierre Schneiter could congratulate himself on having welcomed the fourteenth member state and could observe that the Fund's own assets represented three times the initial subscribed capital. Moreover, the Fund had extended its action to include populations and regions victims of natural disasters, thereby enhancing its original vocation to respond to emergency situations.

New momentum since the fall of the Berlin wall

The return to democracy in the Central and Eastern European countries and the widening of the social concept in Europe have led to a profound transformation of the institution in the last decade, implemented by the new management team in place since 1994, within the policies decided by the Administrative Council and the Governing Board.

The wave of new accessions has been considerable, with the number of member states increasing from 21 to today's 38. Both the geographical and the sectoral scopes of action have been radically changed, transforming the institution into a fully-fledged modern development bank, an indispensable complement to the other European supranational actors. An overall review of the institution's means and objectives led to a capital increase in 1999 and then, in 2004, to the adoption of a new Development Plan with the unanimous backing of the member states.

In a concrete but also symbolic way, the institution's name was changed in 1999 in order to show its full and exclusively banking status: since then it has been known as the **CEB - Council of Europe Development Bank.** Today it enjoys a unique and original position among the European institutions, characterised by a capacity for action tailored to financing social projects, a maximum AAA rating and a very favourable intermediation cost.

Moreover, it is this whole policy of developing and transforming the institution into a development bank in the full sense of the term that was acknowledged by all the member states in 2004 and 2005 when they renewed the mandates of the entire elected management: Governor Raphaël ALOMAR, Vice-Governor Delegate Nunzio GUGLIELMINO and Vice-Governors Krzysztof J. NERS and Apolonio RUIZ LIGERO.

***

In conclusion, the CEB was founded in 1956 with a mission to finance social projects, essentially focussed on problems of migratory flows, then on aid to victims of natural disasters. Given the boost provided by the new management team since 1994, it is today a development bank that is celebrating its anniversary, still fully faithful to its original vocation but also endowed with the means with which to envisage its future growth.

CEB
COUNCIL OF EUROPE DEVELOPMENT BANK

MESSAGE FROM THE GOVERNOR



2005 saw significant new impetus given to the CEB's contribution to promoting social cohesion in Europe.

By the end of the first year of its implementation**, the course set by the Bank's medium-term Development Plan** for the period 2005 - 2009 had been **fully respected**. To achieve this, the CEB mobilised around one priority objective: to further intensify the institution's action in the social field, in particular in Central and South Eastern Europe.

Respect for the objectives of the new Development Plan…

In concrete terms, the overall volume of activity was adjusted so as to enable the Bank, for the duration of the Plan, to devote **50% of its lending to a target group of countries**, which together represent less than 17% of the CEB's subscribed capital to date.

At the expense of a substantial effort, the Bank moderated its overall volume of disbursements, which increased only very slightly to 1.56 billion euros, in order to further concentrate on the target group countries, whose share reached almost 800 million euros, representing 51% of the total amount. **As at 31 December 2005, the loans outstanding stood at 11.5 billion euros**, which constitutes the highest level since the CEB's inception.

…through considerable growth in the Bank's operations in Central and South Eastern Europe…

The **42 new projects** approved amounted to a total of 2.52 billion euros, including **56% in favour of the target group countries** for an amount of almost 1.4 billion euros, up 65% on the previous year. In all, at end 2005, the accumulated volume of projects approved for the Central and South Eastern European countries alone stood at over 4 billion euros, more than half of which had already been disbursed.

…accompanied by an ever deeper commitment to its sectoral priorities,…

The **breakdown of the loans and projects activity** was made **according to the three major sectoral lines of action**, namely: **social integration**, accounting for 56% of total approvals in 2005, **environmental management** (31%) and **human capital development** (13%). The CEB's disbursements were spread over 66 projects in 21 of its member states, thus reflecting a diversified loans portfolio.

This intensification of the CEB's social contribution went hand in hand with continued strengthening of its financial base.

...the continued strengthening of the institution's financial base...

Following the application of IFRS standards to the CEB's accounts for the first time in 2005, **the net profit for the year stood at 88.5 million euros.** By maintaining a sustained level of profitability, excluding extraordinary items, the Bank was able to make an allocation to the reserves, thereby further increasing its own funds which now stand at a total 4.6 billion euros. At the same time, **the quality of the CEB's counterparties improved**, with 83.5% of them rated A or more as at 31 December 2005. **The new prudential framework**, set up within the context of the Bank's medium-term Development Plan, was successfully implemented and **has resulted in increasingly efficient risk monitoring.**

...confirmed by it triple AAA rating,...

Confirmation of the **triple AAA rating** by the agencies Moody's, Standard & Poor's and Fitch Ratings attests to the Bank's excellent level of solvency and the quality of its signature on the international financial markets.

Ever attentive to the value added of its contribution to promoting social development, the CEB took a number of important initiatives in 2005 in order to meet the challenges of a rapidly changing environment.

...an active policy of partnerships with the other international organisations,...

First of all, **emphasis was placed on the policy of cooperation with the other international organisations, both financial and non financial.** To this effect, close contacts were established with the **European Commission**, with a view to facilitating sustainable efforts in favour of social convergence in Europe: together with the European Investment Bank, the CEB was thus invited by the Commission to enter into a privileged partnership for the financing of social housing. Moreover, the very year in which the UN World Summit was held, the CEB strengthened its ties with several **United Nations specialised agencies**, as evidenced by the signing of a framework agreement with the United Nations High Commissioner for Refugees (UNHCR) on 14 March 2005 - and very shortly with the United Nations Development Programme (UNDP) and with the United Nations Children's Fund (UNICEF). In conjunction with the World Health Organisation (WHO) and the Council of Europe, the CEB also organised, in Skopje, the 2nd Forum of Ministers of Health [and of Finance] from the countries of South Eastern Europe.

...emphasis on the value added of its contribution...

In addition to this, **the Bank continued to adapt its instruments for action in favour of its priority member states.** This involved increased recourse to the resources of its trust accounts, notably in favour of the less advantaged Balkan countries, and the intensification of the institution's assistance and monitoring missions: upstream, through the boost given to policy dialogue and accompanying sectoral reforms; downstream, through the increased role given over to ex post evaluation, which is part of the constant quest for project quality.

The CEB naturally encourages the most **innovative solutions** in order to meet the needs of its borrowers: thus, in 2005, with the full agreement of the managers of the five agencies concerned, it proposed **to promote the Nordic experience in local authority financing** among interested target group countries.

For reasons of efficiency, and to follow up on the enhanced mandate decided on for the CEB by the Third Summit of Heads of State and Government of the Council of Europe, the Bank has also undertaken to **adapt** the rules and provisions pertaining to **its loans and project financing policies**. At the outcome of this process, which will be continuing throughout the first half of 2006, the coherence and readability of the institution's framework for action will be further enhanced for the benefit of its borrowers.

…and the updating of its framework for action, for the benefit of its borrowers,…

The funding policy has remained in continuity with the objectives established over the past few years, while adjusting to orientations in the activity.

In 2005, the volume of issues reached almost 2.6 billion euros, up 600 million in relation to 2004, taking into account a markedly higher volume of debt to be repaid than for the previous year. These borrowings were 81% denominated in US dollars because of the opportunities offered by that market. In particular, this policy led to the launch of a 1 billion US dollar issue, which was subsequently increased to 1.25 billion dollars following a re-opening operation. The Bank was also very active on the **Australian dollar market** which represented the CEB's second issuance currency, making up 13% of total borrowings, more than half of which were carried out on the domestic "kangaroo" market. All these funding operations, with an average maturity of 5 years, were systematically combined with hedging swaps in variable rate euros, with the swaps themselves over 99% collateralised. As at 31 December 2005, the tightened liquidity ratio stood at 76% for a minimum requirement of 50%.

…a dynamic funding policy tailored to the activity…

*

In all, 2005 thus fully met the priority objective fixed by the medium-term Development Plan: to redeploy the loans and projects activity in favour of the Central and South Eastern European countries. This result is the fruit of exemplary commitment on the part of the Bank's teams and of the confidence of its shareholders, which was evidenced once again in 2005 by the renewed mandate given to the same elected management team.

Strengthened by these achievements, by its close collaboration with the Council of Europe and by constant consolidation of its sound financial base, the CEB, Europe's oldest multilateral financial institution, will be celebrating its fiftieth anniversary in 2006. This event will provide an opportunity to measure just how much ground has been covered in order to better affirm the CEB's ambition to be the social development bank in Europe.

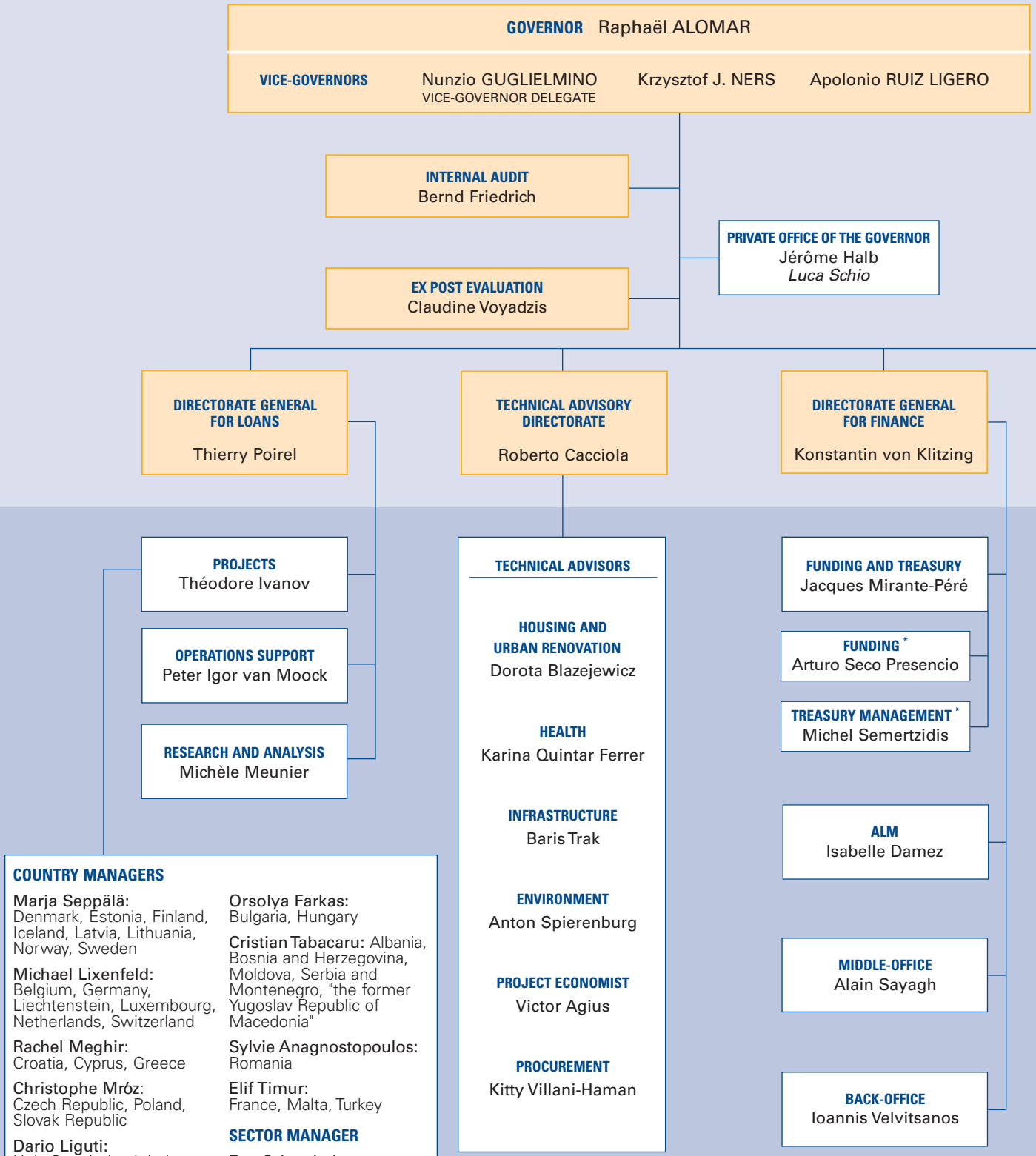
…all confirm the CEB in its ambition: to be the social development Bank in Europe.

Paris, 27 February 2006



Raphaël ALOMAR

ORGANISATION CHART



* Since 22-3-2006

GENERAL MANAGEMENT COMMITTEE



In front
Raphaël ALOMAR
Governor

First row, centre
Nunzio GUGLIELMINO
Vice-Governor Delegate

left, **Krzysztof J. NERS**
Vice-Governor

right, **Apolonio RUIZ LIGERO**
Vice-Governor

Second row, from left to right
Roberto CACCIOLA
Director of Technical Advisors

Arnaud VIOLETTE
Central Director for Information Systems and Control

Thierry POIREL
Director General for Loans

Christos GIAKOUMOPOULOS
Central Director for Legal and Administrative Affairs

Konstantin von KLITZING
Director General for Finance

Richard VENEAU
Director for Corporate Affairs and Human Resources

CENTRAL DIRECTORATE FOR INFORMATION SYSTEMS AND CONTROL
Arnaud Violette

- **GLOBAL RISK MANAGEMENT** — Martin Weigand, *Rafael Ruisanchez*
- **ACCOUNTING** — José Limet
- **INFORMATION TECHNOLOGY** — Frédéric Lardinois
- **ORGANISATION** — Ahmet Kizil

DIRECTORATE FOR CORPORATE AFFAIRS AND HUMAN RESOURCES
Richard Veneau

- **HUMAN RESOURCES** — Maria Lucia Oristanio
- **CONTROLLING** — Patrick Radhauer
- **CORPORATE AFFAIRS** — Sébastien Relland
- **COMMUNICATION AND DOCUMENTATION** — Armelle de la Jugannière

CENTRAL DIRECTORATE FOR LEGAL AND ADMINISTRATIVE AFFAIRS
Christos Giakoumopoulos

- **LEGAL AFFAIRS I** — Heikki Cantell
- **LEGAL AFFAIRS II** — Jan De Bel
- **SPECIAL ADVISOR** — Nicola Catalano
- **GENERAL SERVICES** — Gilles Coron

COMMITTEES

General Management Committee

Treasury Committee
Risk Committee
Projects and Development Committee
Funding Committee
ALM Committee
Information Technology Steering Committee
Committee for Operational Risks and Organisation

February 2006



THE THIRD SUMMIT OF HEADS OF STATE AND GOVERNMENT OF THE COUNCIL OF EUROPE AND THE CEB

Background

The Summit of Heads of State and Government of the Council of Europe was held in Warsaw, Poland, on 16 and 17 May 2005. Following on from the Vienna Summit in 1993 and the Strasbourg Summit in 1997, it was the third meeting to be held since the Council of Europe's creation in 1949. The Warsaw Summit provided an opportunity to reaffirm the institution's pre-eminent role in defending human rights in the broadest sense (rule of law, human rights, democracy, security, etc.) and to emphasise the importance of cooperation agreements with other international institutions.

Thus, at the end of that Summit, the Heads of State and Government adopted the Warsaw Declaration, paving the way for *"strengthened cooperation and solidarity at pan-European level"*. They also adopted an Action Plan focussed around five guidelines:

- promoting common fundamental values: human rights, rule of law, democracy
- strengthening the security of European citizens
- building a more humane and inclusive Europe
- fostering cooperation with other international and European organisations and institutions
- implementing the Action Plan: a transparent and efficient Council of Europe

Consequences of the 3rd Summit for the CEB

The conclusions of the Warsaw Summit not only provide confirmation of the importance accorded by the Heads of State and Government to the sectors of action that are traditionally those of the CEB, but also mark the broadening of the Bank's role within the context of its social purpose.

In effect, the Action plan invites the CEB to enhance its role, stating (Point I-5):

> *"We request the Council of Europe Development Bank (CEB), while confirming its traditional role on behalf of populations in distress and of social cohesion, also to facilitate, through its own means of action, the implementation of policies which aim at the consolidation of democracy, the promotion of the rule of law and respect for human rights, notably in the field of training of magistrates, civil servants and other participants in public life, as well as in the organisation, operation and infrastructure of administrative and judicial public services".*

Without making any substantial modifications to the CEB's mandate, this request will enable the institution to progressively integrate new themes such as the training of magistrates and the financing of infrastructure of administrative and judicial public services.

In more general terms, it will be recalled that the CEB's traditional action in the social field is fully in unison with the policy expressed by the Heads of State and Government within the framework of the Action Plan. Part III of the Plan includes numerous points to which the Bank already contributes within the framework of its current sectors of activity.

Lastly, by stipulating that any broadening of its mandate would have to be carried out *"through its own means of action"*, the Warsaw Summit explicitly invited the Bank to consider its means of action as intangible, whether in terms of the strictly banking nature of its operations or of the beneficiaries of those operations. This naturally strengthens the institution it its quest for a fair balance between financial profitability and social purpose.



PROJECTS AND LOANS

I - OPERATIONAL CONTEXT IN 2005

2005 represented a decisive stage in the CEB's development marked by the launch of a new strategy (Development Plan 2005-2009), which sets the guidelines for the Bank's activities in a rapidly changing Europe.

It will be recalled that the institution's **action logic** for the period 2005-2009 is centred around one priority objective: to further intensify the CEB's action in the social field, particularly in Central and South Eastern Europe. In concrete terms, at least 50% of the Bank's annual disbursements must be in favour of a **target group** of 19 countries*. It is also important to emphasise the need for the CEB to enhance its development bank status by highlighting its internal expertise, intensifying its policy of partnerships with the other development actors and by giving greater readability to its contribution focused around three **sectoral lines of action** (see next page, Means of Action).

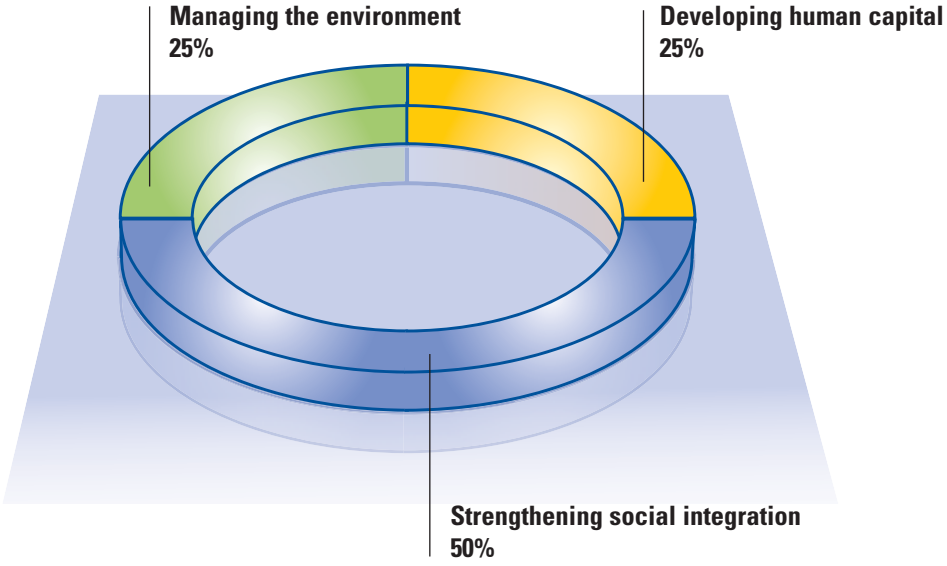
**Albania, Bosnia and Herzegovina, Bulgaria, Croatia, Cyprus, Czech Republic, Estonia, Hungary, Latvia, Lithuania, Malta, Moldova, Poland, Romania, Serbia and Montenegro, Slovak Republic, Slovenia, "the former Yugoslav Republic of Macedonia" and Turkey.*

It is within this context that the CEB this year pursued its policy of **cooperation and close partnerships** with the other international organisations, both financial and non financial, thereby providing good leverage for strengthening its capacity for action and for highlighting its own particular expertise:

- relations with the European Commission were strengthened in order to facilitate complementarity of action with the European Union's Structural and Cohesion Funds and with the European Investment Bank (EIB), particularly in the key fields of social housing and urban renewal (see box on page 24).
- efforts were continued towards closer cooperation with the European Bank for Reconstruction and Development (EBRD), in order to facilitate co-financings in favour of the Central and Eastern European countries in the forthcoming years.

Loans disbursed from 2001 to 2005

Breakdown by sectoral line of action





CEB PARTNERSHIPS WITH THE UNITED NATIONS INSTITUTIONS

Within the framework of the CEB's policy of cooperation and collaboration with numerous international institutions, and in particular with the United Nations specialised agencies, a number of partnerships have been set up. These partnerships respond to a threefold requirement: to widen the Bank's capacity for action, to enhance its expertise and to highlight its specific status as a social development bank in Europe.

*

On 14 March 2005, the CEB signed a Memorandum of Understanding with the **United Nations High Commissioner for Refugees (UNHCR)**, involving a total amount of € 3 million over 5 years.

It should be recalled that one of the CEB's statutory priority objectives is to help in solving the social problems with which European countries are or may be faced as a result of the presence of refugees and displaced persons. To achieve this, the CEB's partnership with the UNHCR appears both natural and necessary. The Memorandum of Understanding establishes a framework for structured cooperation between the two institutions, and is the result of their long experience of successful one-off joint projects.

This cooperation, targeted solely to the sector of housing for refugees and displaced persons, has two lines of focus. On the one hand, through the Selective Trust Account, the CEB can make donations, in particular for displaced populations in South Eastern Europe. It will be recalled that the CEB's Administrative Council has already approved donations of this kind for an amount of USD 2 million, including 1 million in 2005. On the other hand, the Memorandum recognises the facilitating role played by the UNHCR in the identification of project beneficiaries and in project monitoring. As early as 2004, the UNHCR was particularly effective in helping to set up a project worth € 8 million in Bosnia and Herzegovina and, in 2005, a project worth € 20 million for Serbia and Montenegro.

*

In the same spirit, cooperation has been developed with **UNICEF** and the **United Nations Development Programme (UNDP)** over the last few years. Thus,

- in April 1999, at the time of the Kosovo crisis, the CEB financed, through the UNDP, the extension of the drinking water and waste water networks in several villages (€ 1.1 million).

- in 2001, the CEB contributed € 1 million to financing projects implemented by the UNDP involving, on the one hand, emergency food aid and, on the other hand, the reconstruction of water and electricity supply infrastructure for the benefit of 14 000 displaced families in "the former Yugoslav Republic of Macedonia", following the Kosovo crisis.

- in 2003, the CEB approved an amount of USD 450 000, including a disbursed amount of USD 360 000, for projects implemented by UNICEF concerning infrastructure linked to health, education and vocational training for the Roma community in "the former Yugoslav Republic of Macedonia".

- lastly, in June 2004, the CEB approved an amount of USD 200 000 to finance a project implemented by UNICEF in Moldova, involving the conversion of an orphanage into a reception centre for abandoned children and young mothers in difficulty.

On the basis of this experience, the CEB envisages institutionalising the framework of its cooperation with UNICEF and the UNDP through the signing of cooperation agreements in the near future.



- a framework agreement was signed in March 2005 with the United Nations High Commissioner for Refugees (UNHCR), establishing a framework for cooperation for a period of 5 years (see box on page 16).

- in conjunction with the World Health Organisation (WHO) and the Council of Europe, the CEB organised another ministerial conference that was held in Skopje on 25 and 26 November 2005 (see box page 32).

- Lastly, the trust accounts set up in conjunction with certain member states this year proved to be of major importance for the Bank in the appraisal and preparation phases of increasingly complex projects (see box on page 18, The Norwegian Trust Account).



BOSNIA AND HERZEGOVINA
Rebuilding the Mostar Gymnasium

II - MEANS OF ACTION

Acknowledged for its expertise and know-how in financing social projects, the CEB enjoys a unique and original position in Europe, both by the nature of the projects it finances, the sectors in which it undertakes its action and the geographical scope of its shareholder base.

1. Sectoral lines of action

The Bank's original mandate was to respond to emergency situations. Because of this, aid for refugees and migrants as well as for projects in the field of natural or ecological disasters are statutory priorities. The CEB's capacity for action has steadily widened to include other sectors of activity contributing either directly or indirectly to strengthening social cohesion in Europe.

The structure of its projects and loans activity, comprising three major action lines, namely **strengthening social integration, managing the environment** and **developing human capital**, reflect the Bank's commitment to social development:

- to contribute to **strengthening social integration** and thus to attack the roots of exclusion at operational level means acting in favour of refugees, migrants, displaced persons and minorities, improving the social habitat, facilitating employment, and fighting against the marginalisation of the most needy.

- to participate in **responsible management of the environment** involves systematically responding to emergency situations in the event of natural or ecological disasters, and taking sustainable action in favour of risk prevention, protection of the environment and preservation of historic and cultural heritage.

- lastly, to support the **development of human capital** in the key fields of health, education and vocational training, in the long term means facilitating more dynamic and equitable economic and social growth, thereby promoting individual fulfilment and collective well-being.

2. Methods of financing

The CEB proposes a whole range of financial products in order to respond to the specific nature of each project to which it contributes, according to sector and category.

The CEB can therefore grant long-term loans, more often than not combined with a franchise period. The duration of this period, ranging between 10 and 20 years, is all the more necessary in that it is targeted to social investments with deferred profitability. The Bank's action thus makes it possible to do away with the constraints that weigh upon access to long-term credit for projects generating positive externalities.



THE NORWEGIAN TRUST ACCOUNT: AN ESSENTIAL TOOL FOR ENHANCING THE CEB'S ACTION

On the initiative of the Norwegian Authorities, as of 2003 the CEB set up the Norwegian Trust Account, an original mechanism with which to implement diverse initiatives in favour of the Western Balkan countries.

These resources facilitate the financing of a significant amount of technical assistance activity, thereby broadening the scope of the CEB's action since this notably involves preparing pre-feasibility and feasibility studies, setting up pilot projects, accompanying projects financed by the Bank as well as organising conferences and publishing reports. The resources are also used to promote the development of interregional cooperation and best practices.

Among the sectors eligible for support through the Norwegian Trust Account are:

- aid for the return and reinsertion of refugees, displaced persons and minorities
- support for job creation in SMEs and for micro credit instruments
- activities linked to reform of the security sector
- local institution and capacity building.

Originally endowed with an amount of € 1 million, in 2005 the total contribution by the Norwegian Authorities was increased to € 2 million. By end 2005, the Norwegian Trust Account had provided support for 19 projects in the different eligible sectors, with funds essentially being used to prepare and implement high quality, socially sustainable projects in the region concerned.

All these activities have contributed to promoting regional stabilisation and to accompanying the efforts of the countries in the region in the transition process.

To illustrate what has been achieved, several actions implemented thanks to the resources of the Norwegian Trust Account are indicated in the table below.

Country/Region	Description of actions undertaken
Albania	Feasibility study for a pilot project involving **housing for migrants**
Bosnia and Herzegovina	Feasibility study for a project involving **job creation** through the offer of micro credits in Srebrenica
	Technical assistance in preparing a feasibility study for a project involving - **housing for refugees**
	Technical assistance in preparing the implementation of a project for **housing reconstruction**
Serbia and Montenegro	Technical assistance in preparing a feasibility study for a project involving the construction of 1000 **social housing units** in Montenegro
	Technical assistance in preparing the implementation of a project involving **housing for refugees** in Serbia
	Equipment for **training centres** concerned with the reinsertion of demobilised military personnel into civilian life
"the former Yugoslav Republic of Macedonia"	Investments in small-scale infrastructure in favour of Roma communities and aid for **job creation** through the granting of micro-loans involving **support for entrepreneurship** among Roma women
	Aid for **job creation** and for the **economic and social stabilisation** of vulnerable populations in border areas
Projects with regional coverage (Western Balkans)	Report "Trends and progress in social housing reforms in South Eastern Europe", published in November 2005
	Programme of **grants** for **public health students**



The CEB pays particular attention to **the quality of the projects** that it finances in order to optimise their social impact. To achieve this, the Bank has increasingly strengthened its **assistance** and **monitoring** roles throughout the project cycle (see diagram on page 22).

Thus, for each project, the Bank carefully evaluates the socio-economic impact, the technical aspects, the costs, the institutional capacity for managing the project, as well as ensuring that there are no negative consequences for the environment.

Once the project has been approved by the Administrative Council, through on-site missions carried out within the framework of a regular monitoring process, the Bank's services check the physical progress of the works, compliance with costs and procurement procedures, and the achievement of the anticipated social objectives.

On completion of the project, the Bank checks that the use of funds has been in conformity with the objectives and forecasts and evaluates the physical and social results that have been obtained.

It is also the role of the Bank's services to sound the alarm in respect of any difficulties that could jeopardise the success of a project and to give advice on how to solve them. Underpinning this approach is the quest for effectiveness - namely to what extent the objectives have been met - and efficiency, that is to say the use of the resources deployed in order to achieve those objectives.

Moreover, the Bank has continued to enhance its contribution:

- *upstream of projects* through increased recourse to country strategies, prepared in close collaboration with the authorities concerned, and the definition of sectoral policies within the framework of sustainable development and social cohesion,

- and *downstream,* by putting emphasis on ex post evaluation, which makes it possible to measure the short-term social impact of the projects and programmes following their completion, while at the same time improving the quality of both ongoing and future projects through the learning effect.



CROATIA
Building and renovating housing for refugees

III - PROJECTS AND LOANS ACTIVITIES IN 2005

Through its action, the Bank's intention is to facilitate improvements in living conditions and social cohesion. The sectoral breakdown of the projects approved and loans disbursed in 2005 reflects this determination.

The amount of **projects approved in 2005** reached **€ 2 517 million**, representing the highest amount ever approved by the Bank in one year. This overall amount is spread over **42 projects** in favour of 20 countries of operations, including 14 target group countries.

In terms of loans disbursed, the deliberate moderation in volumes resulted in an overall amount that was markedly comparable to that of the previous year. The **loans disbursed in 2005** thus represented **€ 1 559 million**, including € 798 million for the target group countries (representing 51% of the total volume of disbursements). They were spread over **66 projects** in 21 countries of operations.

As at 31 December 2005, the **loans outstanding** stood at **€ 11 483 million**, spread among 32 countries.

1. Strengthening social integration

For the period 2001-2005, this sectoral action line represented an accumulated amount of € 4.8 billion in terms of **projects approved** (representing almost 50% of all projects approved since 2001). For 2005 alone, project approvals amounted to over **€ 1.4 billion.**



PROJECTS APPROVED

per country and per sectoral line of action, from 2001 to 2005

In thousand euros

	2005		Accumulated total 2001-2005	
COUNTRIES	**Amounts**	**%**	**Amounts**	**%**
Albania	23 169	0.9	29 645	0.3
Bosnia and Herzegovina	11 834	0.5	19 834	0.2
Bulgaria	15 000	0.6	75 400	0.8
Croatia	22 662	0.9	152 898	1.6
Cyprus	-	-	390 641	4.0
Czech Republic	20 000	0.8	40 000	0.4
Denmark	100 000	4.0	200 000	2.1
Estonia	-	-	1 000	<0.1
Finland	225 000	8.9	575 000	5.9
France	-	-	500 000	5.2
Germany*	458 500	18.2	953 500	9.8
Hungary	185 000	7.3	777 634	8.0
Iceland	-	-	26 591	0.3
Ireland	-	-	100 000	1.0
Italy**	160 000	6.4	1 499 200	15.5
Latvia	100 000	4.0	125 800	1.3
Lithuania	2 500	0.1	13 032	0.1
Malta	-	-	152 182	1.6
Moldova	-	-	6 000	0.1
Norway	-	-	241 600	2.5
Poland	326 000	13.0	871 415	9.0
Portugal	70 000	2.8	524 660	5.4
Romania	200 000	7.9	475 491	4.9
Serbia and Montenegro	29 600	1.2	29 600	0.3
Slovak Republic	-	-	9 535	0.1
Slovenia	30 000	1.2	64 277	0.7
Spain	327 500	13.0	896 423	9.3
Sweden	-	-	108 256	1.1
"the former Yugoslav Republic of Macedonia"	10 000	0.4	10 000	0.1
Turkey	200 000	7.9	815 028	8.4
TOTAL	**2 516 765**	**100.0**	**9 684 642**	**100.0**

* *including € 62.5 million for projects approved in favour of target group countries (2005)*

** *for the benefit of target group countries (2005)*

	2005		Accumulated total 2001-2005	
SECTORAL LINES OF ACTION* **	**Amounts**	**%**	**Amounts**	**%**
STRENGTHENING SOCIAL INTEGRATION	1 411 000	56.1	4 784 876	49.4
Aid to refugees, migrants and displaced populations	325 000	12.9	389 676	4.0
Social housing	310 000	12.3	1 822 441	18.8
Job creation and preservation in SMEs	552 000	22.0	1 575 200	16.3
Urban and rural modernisation	224 000	8.9	997 559	10.3
MANAGING THE ENVIRONMENT	768 012	30.5	2 881 875	29.8
Natural or ecological disasters and preventive action	320 600	12.7	1 569 515	16.2
Protection of the environment	412 250	16.4	1 054 279	10.9
Protection of historic and cultural heritage	35 162	1.4	258 081	2.7
DEVELOPING HUMAN CAPITAL	337 753	13.4	2 017 891	20.8
Education and vocational training	80 435	3.2	993 025	10.2
Health	257 318	10.2	1 024 866	10.6
TOTAL	**2 516 765**	**100.0**	**9 684 642**	**100.0**

**** For these programmes, the indicative breakdown per sector is provided by the borrower; it is updated as disbursements are made.*

NB: It will be noted that the amounts approved by the CEB represent on average 40% of the total volume of the actual investments. The impact of the CEB's financings thus actually corresponds to 2.5 times the amounts indicated in the table.



PROJECTS APPROVED

per counterparty, in 2005

In million euros

COUNTRIES	COUNTERPARTIES	SECTORS	AMOUNTS
Albania	Government	Education	12.4
	Government	Health	10.8
Bosnia and Herzegovina	Government	Health	10.8
	Government	Education	1.0
Bulgaria	Raiffeisen Leasing Bulgaria	SMEs	10.0
	ProCredit Bank	Multi-sector	5.0
Croatia	Government	Historic heritage	22.7
Czech Republic	Czech Moravian Guarantee and Development Bank	Protection of the environment	20.0
Denmark	KommuneKredit	Social housing	100.0
Finland	OKO Bank	Multi-sector	100.0
	Municipality Finance	Multi-sector	75.0
	Finnvera	Multi-sector	50.0
Germany	KfW Bankengruppe	Protection of the environment	200.0
	Investitionsbank des Landes Brandenburg	Health	196.0
	KfW Bankengruppe*	SMEs	50.0
	KfW Bankengruppe*	Multi-sector	12.5
Hungary	Magyar Fejlesztési Bank	Urban and rural modernisation	100.0
	Magyar Fejlesztési Bank	SMEs	50.0
	Erste Bank Hungary	SMEs	30.0
	Government	Refugees, migrants and displaced populations	5.0
Italy	Unicredito Italiano*	SMEs	100.0
	Banca Intesa*	Multi-sector	40.0
	Banca Intesa*	SMEs	20.0
Latvia	Latvenergo JSC	Protection of the environment	100.0
Lithuania	Siauliu Bankas	SMEs	2.5
Poland	Government	Natural disasters	251.0
	Municipality of Warsaw	Urban modernisation	75.0
Portugal	Banco Espirito Santo	Protection of the environment	70.0
Romania	Government	Social housing	140.0
	Government	Natural disasters	60.0
Serbia and Montenegro	Government	Refugees, migrants and displaced populations / Housing	20.0
	Government	Natural disasters	9.6
Slovenia	Raiffeisen Krekova Banka	SMEs	30.0
Spain	Caja Madrid	Refugees, migrants and displaced populations / Housing	150.0
	La Caixa	Refugees, migrants and displaced populations / Housing	150.0
	IBISEC	Education	27.5
"the former Yugoslav Republic of Macedonia"	Macedonian Bank for Development Promotion	SMEs	10.0
Turkey	Turkiye Sinai Kalkinma Bankasi (TSKB)	SMEs	100.0
	Turkiye Vakiflar Bankasi (Vakifbank)	SMEs	100.0
TOTAL			**2 516.8**

** for the benefit of target group countries*



THE DIFFERENT STAGES IN THE PROJECT CYCLE

Identification	During this stage, a file is drawn up bringing together all the elements needed to define the project's objectives and the means with which to achieve them.
Appraisal	Evaluation of the project, its social objectives and its financial and technical feasibility, with a view to its submission to the Administrative Council.
Approval by the Administrative Council	After examination, the project is approved by the Administrative Council.
Monitoring and Disbursements	Evaluation of the project's correct implementation and of the appropriate use of the funds disbursed.
Completion	Presentation of a report giving a full description of the works carried out and the objectives achieved within the framework of the project.
Ex Post Evaluation	Evaluation of the impact and sustainability of the project in order to assess performance and quality.

In parallel, during the past five years, **loans disbursed** in favour of strengthening social integration represented an accumulated total of almost **€ 4 billion**, representing 50% of all disbursements made since 2001.

In 2005, the Bank disbursed **€ 1 031 million**, including € 638 million for the benefit of the target group countries.

Aid to refugees, migrants and displaced populations

Aid to refugees and migrants is one of the CEB's statutory priorities. Projects financed in this sector are essentially concerned with the construction or rehabilitation of reception centres, social housing (both temporary and permanent), programmes for preventive health, education, and vocational training, as well as the basic infrastructure required to meet the immediate needs of populations victims of exceptional situations.

In 2005, the CEB responded to requests from several of its member states for the implementation of projects targeted to refugees and displaced persons, for a total amount of € 325 million.

Two new operations were approved in **Spain**, in favour of Caja Madrid and La Caixa, for a total amount of € 300 million. These programmes are aimed at strengthening social cohesion by facilitating access to housing credit for immigrant populations in a regular situation.

In **Hungary**, a new project amounting to € 5 million was approved this year in favour of Roma populations. This operation aims to facilitate their social integration through the financing of investments in the social housing, education and vocational training sectors.

Lastly, a project worth € 20 million was also approved this year in **Serbia and Montenegro**. This project will provide for the construction and rehabilitation of housing units for refugee populations and vulnerable persons living in Serbia.

For loans disbursed involving aid for refugees, migrants and displaced populations, in 2005, the Bank paid out a total of € 174 million, representing 11% of all disbursements made during the year.

*

Within the framework of the collaboration between the CEB and the United Nations High Commissioner for Refugees (UNHCR), the CEB this year approved two donations in favour of refugee populations and displaced persons. A donation of USD 500 000 in favour of **Bosnia and Herzegovina** to fund a project aimed at facilitating the return of displaced persons, victims of the war, living in collective centres. Another donation amounting to USD 500 000 in **Serbia and Montenegro** will go towards financing a project for refugees who have opted for integration in Serbia.

The Bank also approved a grant of € 150 000 to finance a project aiming to improve access to formal education for Roma children in **Bulgaria**. The grant will be channelled through and monitored by the St. Cyril and St. Methodius International Foundation.



ROMANIA
Social housing in Constanta



DENMARK
Social housing for the elderly

Social housing

Since its inception, the Bank has always considered action in favour of social housing to be essential in contributing to improving living conditions in urban and rural areas (see box on next page).

Over the past five years, the CEB has approved projects for the financing of social housing for an accumulated amount of € 1 822 million, representing almost 19% of all approvals for the period 2001-2005 (€ 9.7 billion).

In 2005, the CEB approved 3 new operations in this sector, amounting to a total of € 310 million (representing 12% of all projects approved).

In **Denmark**, a project worth € 100 million with KommuneKredit will involve the part-financing of projects for the construction or renovation of some 1 500 housing units for the elderly, subsidised by the local authorities in several towns and counties.

The CEB this year also approved a new programme for **Finland** with OKO Bank. This operation will provide approximately € 70 million to finance the construction or renovation of housing units and related infrastructure in favour of low-income persons.

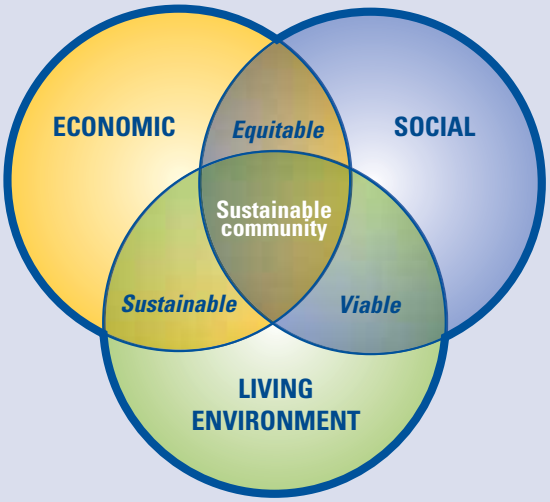
In **Romania**, a project amounting to € 140 million was approved. This operation will allow for the construction and renovation of almost 9 500 social housing units intended for low-income persons. These housing units will be rented in priority to young adults (between the ages of 18 and 35).



AN INTEGRATED APPROACH IN FAVOUR OF SOCIAL HOUSING AND IMPROVED LIVING ENVIRONMENT

Initially limited to financing housing in favour of refugee populations and victims of natural disasters, the CEB has steadily widened its scope of action in this sector, while constantly seeking to ensure its contribution to the social development of individuals and to their living conditions in general.

Operations financed in this sector are concerned with projects for the construction and rehabilitation of social housing. Projects may also be aimed at access to ownership or rental of new housing, renovation or rehabilitation of housing, or the conversion of buildings into housing. The Bank also finances projects involving housing-related municipal infrastructure such as drinking water supplies and waste water treatment, electricity and gas installations, the creation of play areas and local shops.



During the past five years, the CEB's operations in the housing sector have amounted to a total of € 1.8 billion, representing almost 19% of the total volume of projects approved since 2001. Through its financings, the CEB has thus continued to provide its contribution and its technical expertise for the implementation of sustainable housing policies in close collaboration with national and local authorities and with other international organisations.

In 2005, the CEB published a report on trends and progress in housing reforms in South Eastern Europe, in cooperation with the United Nations Economic Commission for Europe (UNECE) and the Council of Europe. This publication *(Trends and Progress in Housing Reforms in South Eastern Europe)* follows up on the Ministerial Conference on housing policies in the Balkans, organised in 2003 with the World Bank under the auspices of the Stability Pact for South Eastern Europe. The objective of the conference was to give fresh impetus to the reform process in a sector in great difficulty.

One of the main challenges linked to the financing of social housing and to improving living conditions stems from the diversity of social problems and from the multitude of forces, actors and factors that impact on the quality of life in urban and rural areas.

Because actions at economic, social, and environmental level in favour of employment are mutually strengthening, the Bank encourages a multi-sector, integrated approach targeted to meeting all the challenges involved in strengthening social cohesion in Europe and to creating the necessary conditions for establishing sustainable communities in both urban and rural environments.

It is in this perspective that the Bank this year strengthened its contacts with the European Commission and the managers of the European Union's Structural and Cohesion Funds, with a view to putting into operational effect actions in favour of social housing and improved living environment in general, in particular in the new European Union member countries.



In terms of loans disbursed in favour of social housing, in 2005, the Bank financed operations worth a total € 166 million, representing 11% of all disbursements made during the year.

Job creation and preservation in SMEs

The CEB gives priority to investment in small and medium-sized businesses (SMEs), as a principal source of new jobs.

The Bank's action to promote the creation and preservation of permanent or seasonal jobs involves financing projects in favour of SMEs in disadvantaged regions.

During the past five years (2001-2005), the Bank has approved projects in this sector for a total amount of € 1 575 million. For 2005 alone, the amount of projects approved reached € 552 million (representing 22% of all projects approved in the year).



SLOVENIA
SME making tennis nets

The Bank this year approved new amounts (€ 50 million) in favour of KfW Bankengruppe for the continuation of two programmes concerned with the financing of productive investment projects, with a view to the creation and preservation of jobs in SMEs located in different **target group countries**. The first programme (€ 40 million) comes within the framework of the *SME Finance Facility* (Phase 2), set up under the auspices of and with a contribution from the European Union; the second programme (€ 10 million) comes within the framework of the *Preparatory Action Programme*, a new programme launched by the European Union in 2004 as a complement to the *SME Finance Facility* which particularly focuses on offering micro-credits to SMEs and is aimed at helping credit institutions in **eight of the new EU member states** to develop their loan operations to SMEs.

Among the operations approved this year in favour of job creation and preservation in SMEs are two new programmes in **Bulgaria** with ProCredit Bank (€ 4.5 million) and Raiffeisen Leasing Bulgaria (€ 10 million).

Furthermore, the Bank is to contribute to financing projects providing support for productive investments undertaken by SMEs in order to strengthen their competitivity and to enable jobs to be preserved or created in several countries: in **Finland**, with Finnvera (€ 50 million) and Municipality Finance (€ 10 million); in **Hungary**, with Erste Bank Hungary (€ 15 million) and MFB (€ 50 million); in **"the former Yugoslav Republic of Macedonia"** with the Macedonian Bank for Development Promotion (€ 10 million); in **Lithuania** with Siauliu Bankas (€ 2.5 million) for the continuation of programmes implemented by the Bank in previous years in support of women's entrepreneurship in the country; and in **Slovenia** with Raiffeisen Krekova Banka (€ 30 million).

The Bank also approved two new loan programmes, through Italian banks, in favour of several target group countries. The first, with Banca Intesa (€ 20 million), will involve job creation and preservation in SMEs located in **Serbia and Montenegro**; the second, implemented with Unicredito Italiano (€ 100 million), will contribute to job creation and preservation in SMEs situated in **Bosnia and Herzegovina, Bulgaria, Croatia, Czech Republic, Poland, Romania, Slovak Republic** and **Turkey**.

Lastly, two other programmes were also approved this year in **Turkey**: € 100 million with Turkiye Sinai Kalkinma Bankasi (TSKB), and another € 100 million with Turkiye Vakiflar Bankasi (Vakifbank). The purpose of these new programmes is to help local SMEs to develop and grow, thus contributing to job creation and preservation in the country.

In 2005, loans disbursed for projects involving job creation and preservation in SMEs amounted to € 476 million, representing 31% of all disbursements.



LOANS DISBURSED

per country and per sectoral line of action, from 2001 to 2005

In thousand euros

COUNTRIES	2005 Amounts	2005 %	Accumulated total 2001-2005 Amounts	Accumulated total 2001-2005 %
Albania	6 193	0.4	9 194	0.1
Belgium	-	-	160 000	2.0
Bulgaria	5 259	0.3	50 069	0.6
Croatia	41 563	2.6	135 108	1.7
Cyprus	15 000	1.0	334 978	4.2
Czech Republic	12 000	0.8	12 000	0.2
Denmark	100 000	6.4	200 000	2.5
Estonia	-	-	8 541	0.1
Finland	142 500	9.1	477 500	6.0
France	-	-	513 357	6.5
Germany*	261 250	16.8	682 297	8.6
Greece	-	-	245 518	3.1
Hungary	144 737	9.3	486 031	6.1
Iceland	5 975	0.4	32 406	0.4
Ireland	-	-	50 000	0.6
Italy**	200 000	12.8	1 267 186	15.9
Latvia	500	<0.1	17 423	0.2
Lithuania	4 233	0.3	15 612	0.2
Malta	-	-	118 000	1.5
Norway	-	-	128 788	1.6
Poland	132 230	8.5	537 878	6.8
Portugal	22 500	1.4	471 180	5.9
Romania	37 410	2.4	222 407	2.8
San Marino	-	-	1 162	<0.1
Slovak Republic	7 307	0.5	33 966	0.4
Slovenia	20 000	1.3	47 533	0.6
Spain	186 475	12.0	1 033 915	13.0
Sweden	52 807	3.4	163 058	2.1
"the former Yugoslav Republic of Macedonia"	-	-	11 556	0.1
Turkey	160 596	10.3	496 720	6.2
TOTAL	**1 558 535**	**100.0**	**7 963 383**	**100.0**

* *including € 61.3 million for loans disbursed in favour of target group countries (2005)*

** *including € 150 million for the benefit of target group countries (2005)*

SECTORAL LINES OF ACTION***	2005 Amounts	2005 %	Accumulated total 2001-2005 Amounts	Accumulated total 2001-2005 %
STRENGTHENING SOCIAL INTEGRATION	1 030 653	66.2	3 973 960	49.9
Aid to refugees, migrants and displaced populations	173 556	11.1	249 798	3.1
Social housing	166 159	10.7	1 511 260	19.0
Job creation and preservation in SMEs	476 141	30.6	1 305 310	16.4
Urban and rural modernisation	214 797	13.8	907 592	11.4
MANAGING THE ENVIRONMENT	265 612	17.0	2 006 647	25.2
Natural or ecological disasters and preventive action	41 936	2.7	1 193 985	15.0
Protection of the environment	158 015	10.1	639 088	8.0
Protection of historic and cultural heritage	65 661	4.2	173 574	2.2
DEVELOPING HUMAN CAPITAL	262 270	16.8	1 982 776	24.9
Education and vocational training	97 329	6.2	990 008	12.4
Health	164 941	10.6	992 768	12.5
TOTAL	**1 558 535**	**100.0**	**7 963 383**	**100.0**

*** *For these programmes, the indicative breakdown per sector is provided by the borrower; it is updated as disbursements are made.*



LOANS DISBURSED

per counterparty, in 2005

In million euros

COUNTRIES	COUNTERPARTIES	SECTORS	AMOUNTS
Albania	Government	Health	4.2
	Government	Education	2.0
Bulgaria	ProCredit Bank	Multi-sector	2.5
	Government	Natural disasters	2.3
	Municipality of Sofia	Housing / Roma	0.5
Croatia	Government	Education	20.7
	Government	Housing / Refugees	14.3
	Government	Rural modernisation	6.5
Cyprus	Nicosia Sewerage Board	Environment	15.0
Czech Republic	VB Leasing CZ	SMEs	10.0
	Czech Moravian Guarantee and Development Bank	Protection of the environment	2.0
Denmark	KommuneKredit, Copenhagen	Housing	100.0
Finland	Finnvera plc, Kuopio	SMEs	50.0
	OKO Bank, Helsinki	Multi-sector	50.0
	Municipality Finance Ltd.,Helsinki	Multi-sector	37.5
	OKO Bank, Helsinki	SMEs	5.0
Germany	Investitionsbank des Landes Brandenburg	Health	100.0
	KfW Bankengruppe	Protection of the environment	100.0
	KfW Bankengruppe *	SMEs	43.8
	KfW Bankengruppe *	Multi-sector	17.5
Hungary	Magyar Fejlesztési Bank	SMEs	60.0
	Magyar Fejlesztési Bank	Urban and rural modernisation	50.0
	Government	Natural disasters	20.5
	Erste Bank Hungary	Multi-sector	14.2
Iceland	Municipality of Reykjavik	Education	6.0
Italy	Banca Intesa *	Multi-sector	70.0
	Dexia Crediop	Historic heritage	50.0
	Unicredito Italiano *	SMEs	50.0
	Banca Intesa *	SMEs	30.0
Latvia	Mortgage and Land Bank of Latvia	SMEs	0.5
Lithuania	Government	Education	1.5
	Government	Housing / Refugees	1.4
	Siauliu Bankas	SMEs	1.3
Poland	City of Warsaw	Urban modernisation	69.9
	Europejski Fundusz Leasingowy	SMEs	51.2
	Government	SMEs / Urban modernisation	7.5
	University of Warsaw	Education	3.6
Portugal	Instituto Nacional de Habitação	Housing	12.5
	Banco Português de Investimento	Housing	10.0
Romania	Government	Natural disasters	15.9
	Government	Education	14.0
	Government	Housing	5.5
	Government	Protection of the environment	1.0
	Government	Health	1.0
Slovak Republic	Government	Health	3.6
	Slovak Water Management Enterprise	Natural disasters	3.3
	Government	Historic heritage	0.4
Slovenia	Nova Kreditna Banka Maribor	SMEs	20.0
Spain	La Caixa	Housing / Migrants	75.0
	Caja Madrid	Housing / Migrants	75.0
	Caixa Cataluña	Multi-sector	22.5
	IBISEC	Education	6.9
	Institut Catalá de Finances	Health	4.0
	Gicaman S.A., Toledo	Health	2.2
	Gicaman S.A., Toledo	Education	0.6
	Gicaman S.A., Toledo	Historic heritage	0.3
Sweden	Kommuninvest i Sverige	Multi-sector	52.8
Turkey	Government	SMEs	138.3
	Government	Rural modernisation	22.3
TOTAL			**1 558.5**

** for the benefit of target group countries*



Urban and rural modernisation

The CEB undertakes actions that contribute to improving the quality of life in urban and rural areas in disadvantaged regions.

The projects financed by the CEB in matters of urban modernisation concern run-down towns or neighbourhoods where there is an obvious lack of infrastructure or of any social or cultural amenities. These projects are concerned with the improvement or creation of service infrastructure such as drinking water, electricity and gas supplies, roads and sewers. They also serve to improve social and cultural amenities such as basic medical services, primary and secondary schools, socio-cultural centres, sports centres, exhibition areas and the development of green spaces.

In parallel, the Bank focuses its actions in favour of rural modernisation on regions where the active population in the agricultural sector is equal or inferior to 10% of the total active population of the region, and incomes are below the national average. The operations financed may concern infrastructure projects such as drinking water, electricity and gas supplies, the creation of roads, irrigation infrastructure and social and cultural amenities.

During the period 2001-2005, the Bank took action in favour of urban and rural modernisation for a total amount of projects approved that reached almost € 1 billion.



HUNGARY
Terracing works for flood prevention in Tivadar (Vásárhelyi Plan)

For 2005 alone, new operations in this sector represented a total of € 224 million.

The new operations approved this year included a loan programme submitted by KfW Bankengruppe (Germany) that will enable € 4 million to be devoted to financing projects involving urban and rural infrastructure, to be implemented in towns situated in **Bulgaria, Croatia, Romania** and **Turkey**.

Similarly, a new loan programme was approved in **Finland** with Municipality Finance. This will provide € 20 million to finance various investments in municipal infrastructure, carried out by municipalities or federations of municipalities and businesses under municipal control.

The Bank also approved two new programmes in **Hungary**. The first, with Erste Bank Hungary, will provide € 15 million to finance investments in municipal infrastructure (wastewater drainage networks, water treatment plants). The second programme, with Magyar Fejlesztési Bank (MFB), will allow € 100 million to be spent on financing municipal investments, within the framework of the *MFB Loans Programme for the development of municipal infrastructure.* These investments, with a high social value, will contribute to improving the quality of life for the inhabitants of the big and small towns and the villages concerned by creating conditions conducive to a healthy, safe and sustainable environment.

Similarly, a new loan programme, with Banca Intesa (Italy), will provide € 10 million to part-finance municipal investments in social infrastructure in **Serbia and Montenegro**.

Lastly, the Bank this year approved an operation in **Poland** with the Municipality of Warsaw. This project, worth a total € 75 million, will contribute to improving the living conditions of the inhabitants of Warsaw and its 18 districts, through the construction and/or rehabilitation of urban public infrastructure.

In 2005, the loans disbursed in favour of projects involving urban and rural modernisation amounted to a total of € 215 million, representing 14% of all disbursements.



2. Managing the environment

The CEB's action in matters of environmental management is clearly acknowledged through its projects in favour of regions hit by natural or ecological disasters (one of the Bank's two statutory priorities) and actions to safeguard historic heritage.

For the period 2001-2005, this sectoral action line represented an accumulated amount of projects approved totalling almost **€ 3 billion**. For 2005 alone, **project approvals** amounted to **€ 768 million**.

In parallel, **loans disbursed** in favour of environmental management since 2001 reached an accumulated total of over **€ 2 billion**, representing 25% of all disbursements over the same period.

In 2005, the Bank disbursed **€ 266 million**, including € 91 million in favour of the target group countries.



SERBIA AND MONTENEGRO
Flooding in Vojvodina

Natural or ecological disasters: reconstruction and preventive action

The purpose of the operations carried out by the Bank is, on the one hand, to provide national and local authorities with assistance involving immediate financial support for the reconstruction of the affected areas and, on the other hand, to develop means for the prevention of natural or ecological disasters, along the lines of the Hyogo Action Plan for the period 2005-2015, adopted at the World Conference on Natural Disaster Reduction held in Kobe (Japan) in January 2005. The action plan places emphasis on strengthening the local and national capacities of countries at risk and on the need to invest financial resources for the purpose of reducing both the incidence and the gravity of natural disasters.

In the first case, accelerated procedures are put in place for the appraisal and approval of such projects. Actions typically involve the reconstruction or rehabilitation of destroyed or damaged public structures and, more particularly, basic infrastructure such as water supply, waste water and solid waste treatment, electricity and gas supplies.

Over the period 2001-2005, the Bank undertook action in this sector for an amount of projects approved totalling almost € 1.6 billion.

In 2005, the total amount of approvals for new operations in this sector reached € 321 million, spread among 3 countries (Poland, Romania, Serbia and Montenegro), representing almost 13% of the total amount of approvals.

Thus, in matters of natural disaster prevention, the Bank approved a large-scale project in **Poland** (for a maximum amount of € 251 million) involving financing for flood prevention works and for the losses incurred in terms of property and production capacity in the Oder River Basin.

In **Romania**, the Bank also approved two new projects for a total amount of € 60 million to finance reconstruction work following the torrential rains that hit the country in spring 2005. The rains caused substantial flooding in several regions, damaging arable land, real estate property and infrastructure, and severely affecting the local populations.

Lastly, another project was approved in **Serbia and Montenegro** (€ 9.6 million) providing financing for works to rehabilitate housing damaged by the April 2005 floods in the Vojvodina region.

Loans disbursed in favour of projects concerned with natural or ecological disasters (reconstruction and preventive action) in 2005 amounted to € 42 million, representing 3% of the total amount of disbursements.



Protection of the environment

The initiatives taken in this sector today represent a wide geographical diversity. In parallel to its specific action in this field, it should be remembered that the Bank systematically takes into account the environmental aspects of all the projects it appraises.



CZECH REPUBLIC
Water treatment plant in Moravské Budějovice

During the past 5 years (2001-2005), the Bank has approved new projects in this sector for an accumulated total of over € 1 billion. In 2005, new operations were approved for a total of € 412 million.

Among these, in **Germany**, a large-scale project was approved in favour of KfW Bankengruppe (€ 200 million) to finance investments coming within the framework of the *KfW Environmental Protection Programme (EPP)*, aimed at promoting energy saving and reductions in harmful emissions in the new Länder.

In **Latvia**, the Bank this year approved a first operation with Latvenergo, a public energy producing company, for an amount of € 100 million aimed at financing the reconstruction of a power station located in the Riga district. The project's overall objective is to contribute to the protection of the environment through a reduction in atmospheric pollution made possible by cogeneration.

The Bank also approved a project in **Portugal** with Banco Espirito Santo (€ 70 million), whose prime objective is to contribute to the protection of the environment through the production of electricity by means of wind power. This project should thus lead to a reduction in harmful gas emissions through recourse to renewable energies.

Lastly, a new project in matters of environmental protection was approved this year in the **Czech Republic** for an amount of € 20 million. This operation will provide financing for municipal investments in environmental infrastructure.

Loans disbursed in favour of projects for the protection of the environment in 2005 reached a total of € 158 million, representing 10% of all disbursements.

Protection of historic and cultural heritage

Historical and cultural heritage, whose restructuring and rehabilitation may be financed by the Bank, must be classified as such by UNESCO or by the country concerned.

Over the period 2001-2005, the Bank approved a total amount of € 258 million in this sector. In 2005, approvals in favour of projects involving the protection and rehabilitation of elements of historic and cultural heritage amounted to over € 35 million.



PORTUGAL
Renovating the Convento do Espinheiro chapel in Evora



In **Croatia**, the Bank this year approved a project worth € 22.7 million in order to finance reconstruction work on three historic sites in Eastern Slavonia.

Similarly, in **Finland**, a loan programme with Municipality Finance will provide € 10 million to finance projects involving the restoration of elements of Finnish historic and cultural heritage.

Lastly, a new loan programme with Banca Intesa (Italy) will devote € 2.5 million to financing projects in **Serbia and Montenegro**, for the restructuring and rehabilitation of classified historic and cultural heritage sites.

In terms of the loans disbursed in 2005, a total of € 66 million was paid out this year in favour of projects in this sector, representing 4% of the total amount of loans disbursed during the year.

3. Developing human capital

The CEB contributes to the development of human capital through its financings in favour of education and health. The Bank undertakes actions in these two sectors not only by financing the construction or rehabilitation of infrastructure but also by providing fittings and equipment.

It will be recalled that these two sectors play a vital role in the quest for balanced development and greater social cohesion in Europe. Indeed, modern education and health services are essential in promoting economic growth, development at both regional and national level in Europe, and the reduction of inequalities.

For the period 2001-2005, this sectoral action line represented an accumulated total of **over € 2 billion** in terms of **projects approved**. In 2005, project approvals reached a total of **€ 338 million** (representing 13.4% of the total amount of projects approved in the year).

In parallel, since 2001, the accumulated amount of **loans disbursed** in favour of human capital development is **€ 2 billion**, representing 25% of all disbursements made in the last five years. The figure for 2005 was **€ 262 million**, including € 68 million in favour of the target group countries.

Education and vocational training

The CEB undertakes action at different levels in the education system, either in primary schools, secondary schools or universities. The Bank thus finances both the construction and modernisation of school infrastructure and supplies of pedagogical equipment.

As regards vocational training, alternating theoretical training and hands-on work experience constitutes an appropriate response both to the needs of businesses, in particular SMEs, and to the expectations of those preparing to enter the world of work.

During the past five years, the CEB has approved operations for an accumulated amount of almost € 1 billion. In 2005, new operations were approved in this sector for a total amount of € 80 million.

Among these operations, the Bank this year approved a project worth € 12.4 million in **Albania**. This project will provide for improvements in teaching conditions in the city of Tirana, through the construction of seven schools and the rehabilitation of twelve others. The investments involved will improve conditions of study and work for 17 000 pupils and 1 000 teachers. The new schools should generate approximately 100 teaching posts and 250 jobs in the building sector. The rehabilitation of existing schools will involve the elimination of dangerous materials such as asbestos, which will also have a positive impact on the environment.



ITALY
Renovating the Il Carignano Theatre in Turin



HEALTH AND ECONOMIC DEVELOPMENT IN SOUTH EASTERN EUROPE
Second Forum of Health Ministers
Skopje, 25-26 November 2005

The countries of South Eastern Europe have made health policies one of their priorities.

The reforms already undertaken must be completed by policies and measures of encouragement that will enable Governments to invest further in matters of public health in order to guarantee quality healthcare for their populations and to improve health services in this region of Europe.

With this in mind, the CEB, the Council of Europe and the World Health Organisation jointly organised the Second Forum of Health Ministers on the theme of health and economic development in South Eastern Europe. The Forum, which took place on 25-26 November 2005 in Skopje, in "the former Yugoslav Republic of Macedonia", brought together not only the Ministers of Health and Finance from the South Eastern European countries, but also donor countries and representatives from the European Commission, the World Bank, the European Investment Bank and UNICEF.

All the exchanges that took place evidenced the participants' great interest in seeing the CEB intensify its activity in the region not only in the health sector but also in other fields linked to social and economic development.

In preparation for this meeting, the CEB asked a group of experts to draw up a report on the role of health in economic development in South Eastern Europe, which emphasised the close link that exists between economic performance and the situation in matters of public health, in particular in terms of job market participation, productivity and income levels.

The report, whose preliminary conclusions were presented and discussed at the Forum, was published in cooperation with the World Health Organisation. It recalls the efforts that still need to be made to improve the state of health of the populations in South Eastern Europe in order to promote sustainable economic and social development.

The *Skopje Commitment*, signed by Health Ministers at the end of the Forum, constitutes a major stage in the innovative process initiated in 2001 with the *Dubrovnik Commitment,* the first political document to define regional cooperation in the health sector in South Eastern Europe.





GERMANY
Kindergarten in Gadebusch

Another project, implemented with the Government in **Bosnia and Herzegovina** (€ 1 million), will be devoted to financing reconstruction work on the prestigious school, the Mostar Gymnasium. The specific objective of this project is to complete repairs on the building, thereby making it possible to bring the 200 students together under one roof, whereas, in the meantime, they have to receive their schooling on other premises.

Lastly, in **Spain**, a project (€ 27.5 million) with the Institut Balear d'Infraestructuras i Serveis Educatius i Culturals (IBISEC) will provide financing for the construction or renovation of educational infrastructure situated in the Autonomous Community of the Balearic Islands, as well as for the provision and installation of pedagogical and computer equipment.

The amounts disbursed in favour of education projects in 2005 reached a total of € 97 million, representing 6% of all disbursements.

Health

In the health sector, the CEB contributes to financing the construction, renovation and modernisation of medical infrastructure such as neighbourhood health centres, hospitals, university hospitals or centres catering especially for the elderly and the handicapped.

During the past five years, the CEB has approved new operations for an accumulated amount of over € 1 billion. In 2005, the total amount of projects approved in this sector reached over € 257 million, representing 10% of the total amount of approvals.

Among the operations approved this year is a new project to be financed by the Bank for a total € 10.8 million in **Albania**. This project will provide financing for works in the first phase of the reform programme for the Tirana University Hospital: the construction of a new building and rehabilitation of three others, in order to improve the quality of the healthcare services dispensed each year to some 6 000 patients.

The Bank also approved two new operations in **Germany** with Investitionsbank des Landes Brandenburg, for a total amount of € 196 million. The first will allow for the financing of investments in the field of health aimed at improving the quality of the healthcare services and living conditions for the elderly, handicapped or chronically ill. The second will involve the financing of works in three hospitals for the construction and/or renovation of healthcare structures for the elderly.

Lastly, in **Bosnia and Herzegovina**, a new project worth € 10.8 million is to provide financing for the Programme for the Development of the Healthcare System, which will set up an efficient system of primary healthcare to meet the everyday needs of the local populations. This



LATVIA
Kindergarten in Riga





ALBANIA
Renovating Shkodra Hospital

programme will provide for the construction, renovation and refurbishing of medical centres throughout the country.

In 2005, the Bank paid out a total of € 165 million in loans for the health sector, representing 11% of all disbursements made during the year.

***

In 2005, additional impetus was given to the Bank's action in favour of social development, as evidenced by a number of key facts and results:

- the increasing role of **ex post evaluation** in assessing the sustainability of the social impact of the projects financed by the Bank (global programme for the evaluation of 11 projects concerning natural or ecological disasters),

- the constant efforts made to improve the **performance indicators** of operations throughout the project life cycle (from identification to completion) combined with enhanced **technical assistance**,

- the promotion of **policy making dialogue** through the organisation of conferences (see box on page 32) and the publication of sectoral and analytical studies applied to the Western Balkans, a priority geographical area for the CEB (publications in 2005: *Social Challenges in South Eastern Europe* and *Trends and Progress in housing reforms in South Eastern Europe).*

Financings carried out this year brought the **loans outstanding** to **€ 11.5 billion** and the **stock of projects** awaiting financing reached **€ 3.2 billion.** For the CEB, this stock of projects naturally constitutes a solid reserve for action for the years to come.

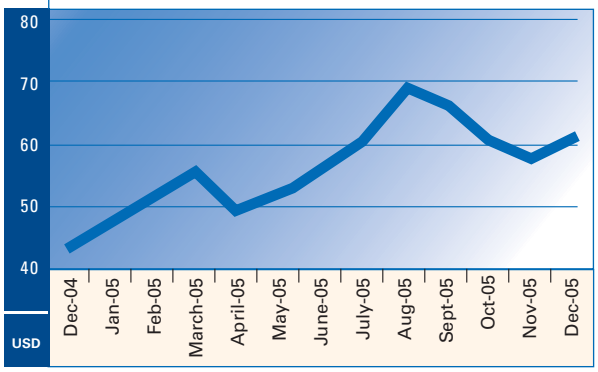
I - ECONOMIC ENVIRONMENT IN 2005

The year 2005 began on an optimistic note, in the hope of a consolidation of the resumption in growth after the encouraging signs observed during the course of 2004.

The general financial position for the year 2005 indicates that the global economy has maintained relatively high growth rates. On the other hand, the rise in short-term interest rates, the accelerating increase in raw material prices and the termination of certain budget incentives are all factors that could lead to a slowdown. One should note in particular the volatility of oil prices, the impact of which on world growth is becoming increasingly high.

Finally, geopolitical risks remain, especially in the Middle East, and are liable to heighten a certain climate of instability that appears currently prevalent in the economic world.

TREND IN OIL PRICES (CRUDE)

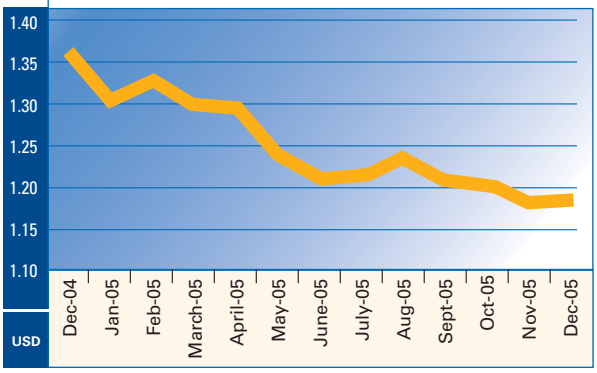


The United States: rise in short-term and long-term interest rates

The US economy recorded strong growth due to higher employment. Capital investment remained at a high level thanks to the growth in earnings and despite consecutive increases in Fed key rates. But there are still uncertainties regarding the strength of this recovery as it was achieved at the cost of a deterioration in budget and current account balance deficits which are worrying the markets.

In this context, long-term US dollar interest rates have started to rise again in an environment marked by concern at the widening US budget and trade deficits.

EURO VERSUS US DOLLAR

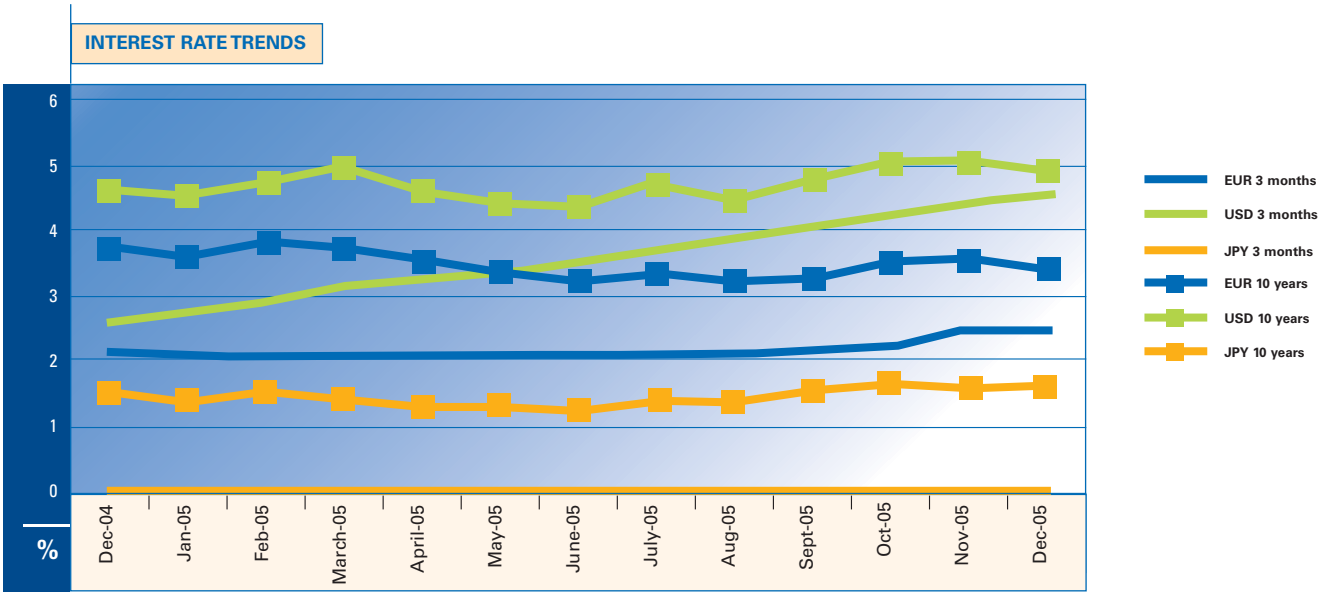


Europe: rise in short-term rates and fall in long-term rates

Europe has slowed down its integration process following the votes in referendums on the European Constitution, which has relaunched temporarily criticisms against the euro. Nevertheless, a number of voices were raised in defence of the euro, including that of Rodrigo Rato, IMF Managing Director, who stated that *"the euro was a success and that it would be inadvisable to abandon it"*. The signs of a pickup in growth glimpsed in 2003, except in the Eurozone, were confirmed this year; inflation has stayed moderate, but the unemployment rate remains high.

The continuing depreciation of the euro against the US dollar during the course of 2005 may assist recovery in Europe by facilitating exports.

At the end of the year, the European Central Bank increased its key rates by 25 bp to 2.25%. The last time it cut interest rates, by 0.50% in June 2003, was to thwart the risk of inflation rekindling due to

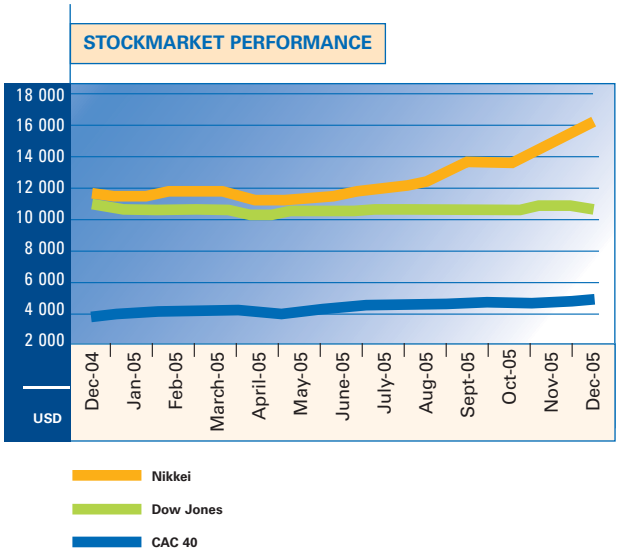


higher raw material prices and an accumulation of liquid assets. In 2005, inflation is expected to remain around the 2% mark in line with the European Central Bank's targets.

Ten-year rates on the euro market remained at a very low level, lower than in 2004, fluctuating in a bracket of 3.90% to 3.10%.

Central banks in Central and Eastern Europe continue on their path towards convergence with the European Central Bank by lowering their key rates at a rapid pace.

For its part, the Bank of England lowered its key rates by 25 bp in August.



Asia: China abolishes the dollar peg

China breaks the fixed link between the yuan and the US dollar and thus authorises a low appreciation of the yuan, following pressure from different western countries. The four currencies dominating the new renmibi basket are the US dollar, the euro, the yen and the South Korean won; The very sharp growths recorded in China and India continue to fuel the increase in raw material and oil prices.

Rising stock markets

In 2005, the major stock markets rose sharply in Europe (more than 20%), and in Japan (35%). On the other hand, the US stockmarket index only rose very slightly compared to 2004.

II - BOND PORTFOLIOS

Two securities portfolios appear on the asset side of the Bank's balance sheet: the available-for-sale financial assets and the financial assets held to maturity.

- The **available-for-sale financial assets** consists of securities with a maximum maturity of seven years. In order to limit exposure to interest rate risk, securities of maturities greater than one year are floating-rate, through asset swaps where

applicable. Short-term instruments, of maturities less than one year, also include Euro Commercial Paper (ECP), as an alternative to bank deposits.

Longer-term securities, of maturities greater than one year, must have a minimum rating of AA or Aa2, and shall not exceed a € 1 billion ceiling. For instruments maturing in less than one year, the prerequisite minimum rating is A-1 or P-1.

As at 31 December 2005, the total value of securities in this portfolio with a maturity of more than one year stood at € 1 billion.

- The **financial assets held to maturity** consists of euro-denominated plain vanilla fixed-rate bonds with a maximum maturity of 30 years. To be eligible for this portfolio, securities must have a minimum rating of AA or Aa2. However, securitised products and other special-purpose instruments, must have an AAA/Aaa rating and not exceed a total limit of € 500 million. The size of the portfolio of financial assets held to maturity is limited to the amount of usable capital (paid-in capital, reserves) plus the provision for post employment staff benefits.

The strategic objective is for these resources to be remunerated by a satisfactory long-term return. This portfolio is accounted for at amortised cost. By nature, the securities contained in it can be neither exchanged nor sold, except under exceptional circumstances.

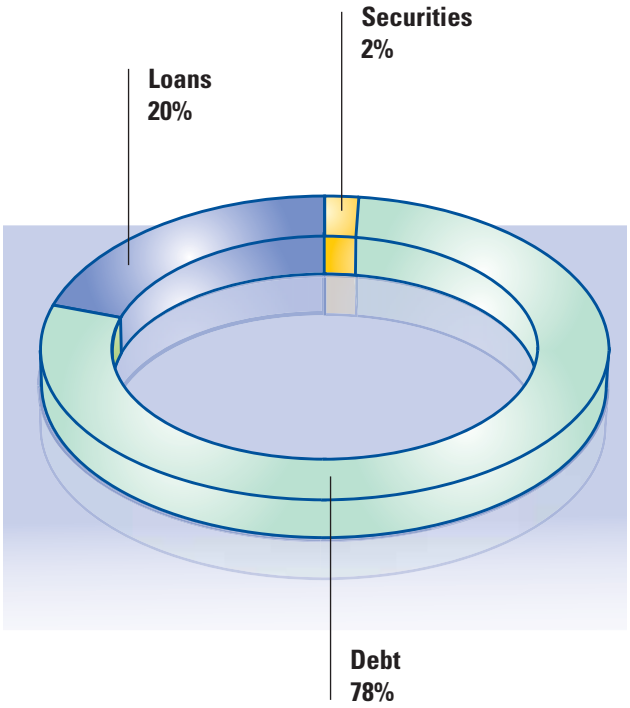
As at 31 December 2005, the total value of this portfolio stood at € 1.7 billion.

In practice, the CEB implements an annual purchasing programme under which the cash generated by bonds maturing and the current year's profits are re-invested.

III - DERIVATIVES

The market risks resulting from loan, financing and investment transactions are systematically hedged by using derivatives, in accordance with the policy adopted by the directing bodies. As an end user, the Bank employs derivatives solely for hedging purposes.

As at 31 December 2005, the breakdown of derivatives by type of hedge was as follows:



To guard against the risks inherent in the use of these financial instruments, the Bank follows a strict derivatives management policy, the principles of which are outlined in the section entitled "Integrated Risk Management" (see page 42).

To limit its credit risk, the Bank has signed collaterals contracts with nearly all its counterparties. Thus, as at 31 December 2005, almost all of the CEB's swaps contracts are collateralised. The residual credit risk, calculated as the sum of the positive market values not covered by collaterals received, remains very low.

IV - FUNDING IN 2005

1. Borrowings

Within the framework of the annual borrowing authorisation set by the Administrative Council, the CEB makes issues in the international capital markets. In 2005, the Bank borrowed a total amount of € 2.6 billion, broken down into 14 funding operations, with maturities of 1 year or more, including six reopenings of existing issues.

This amount, superior to the funding volume in 2004 meets two main objectives:

- to cover lending needs, similar to those in 2004, and
- to meet the Bank's repayment of maturing debt, which in 2005 was noticeably more important than in 2004.

The volume of resources raised in 2005 also enabled the Bank to maintain a liquidity level in accordance with the rules set by the Administrative Council. It is the CEB's policy to include its stock of projects in projected cash requirements. In accordance with prudential liquidity policy, the CEB's reinforced liquidity ratio states that at least 50% of projected cash requirements for the next three years should be available in liquidity. These projected requirements include the funding of approved projects and additional liquidity requirements covering the risk of default over three years.

To ensure constant access to the resources needed to fund its activities, the Bank continues to combine benchmark borrowings in major currencies targeting a broad range of institutional investors and opportunistic borrowings in various currencies or with a more specific structure meeting special investor demand.

In 2005, 81% of the funds raised by the Bank were denominated in US dollars, versus 93% in 2004. The remaining 19% were raised in Australian dollar (13%), euro (2.5%), South-African rand (2.5%) and new Turkish lira (1%).

The preponderant role of the US dollar, swapped for floating euros, can be explained by the attractive funding conditions on this market. In that aspect, it should be underlined that the CEB launched benchmark issue denominated in US dollars, with a maturity of three years, for an initial amount of USD 1 billion, increased to USD 1.25 billion after conclusion of a reopening operation. At the start of the year, the CEB also launched a new tranche of USD 600 million on its benchmark issue arriving to maturity in 2010, bringing the total of this line to USD 2 billion. The reopening of USD 250 million on the 2013 benchmark issue brings its outstanding amount to USD 1 billion. A new five years transaction has been launched for a total of USD 500 million.

In 2005, the CEB launched a new ten-year issue on the Australian domestic market via its "kangaroo" programme. This operation, with increases in existing transactions with various maturities, in both "kangaroo" and EMTN formats, has made the Australian dollar the second currency in terms of funding volume.

An *"Uridashi"* issue in ZAR was launched on the Japanese domestic market with a maturity of four years. In addition, it should be noted that the CEB participated in the creation of the *"Eurolira"* market at the start of 2005 by launching a 1.5-year issue in the new Turkish lira market and it also launched a 20-year issue on the Italian domestic market.

All these borrowing operations were combined with hedging swaps, which eliminated both the interest rate risk and the currency risk. After swaps, the resources borrowed were fully converted into euros.

The average maturity of the issues launched in 2005 was five years, as against seven years and seven months in 2004, which reflects the adaptation of the funding activity to market demand conditions. The table on page 39 gives details of the funds raised in their original currencies.

Over 50% of the issues launched under the programme had a maturity of four years or more, to enable refinancing of the Bank's loans and avoid cash gaps over the coming financial years.

The multi-currency EMTN programme was updated in October 2005 to adapt the legal framework of the Bank's issues to new capital market features. The Bank makes priority use of this programme whenever possible.

2. Trend in debt position

As at 31 December 2005, the total outstanding debt represented by securities, excluding interest payable, stood at € 13 billion, up from the previous financial year (€ 11.2 billion).

The Bank bought back a total € 13.3 million worth of its own debt and made an early repayment of € 8 million. The breakdown of debt per maturity, taking into account these operations and new issues launched, is shown in the diagram on page 39.

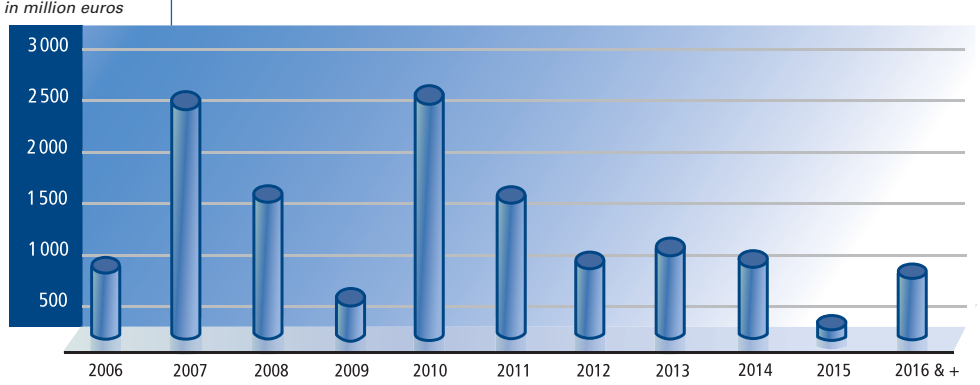
2005 BORROWINGS

Date of payment	Date of maturity	Currency	Term (in millions)	Nominal amount	Lead manager
26/01/2005	20/01/2010	USD	5 years*	600	Mitsubishi Securities International
04/02/2005	18/01/2012	AUD	7 years*	50	The Toronto-Dominion Bank
24/02/2005	24/02/2015	USD	10 years**	10	Mizuho
07/03/2005	08/09/2006	TRY	1 year 6 months	50	The Toronto-Dominion Bank
01/04/2005	01/12/2010	USD	5 years 8 months	500	Royal Bank of Canada / Daiwa Securities
12/07/2005	18/01/2012	AUD	6 years 6 months*	50	The Toronto-Dominion Bank
01/08/2005	01/08/2035	EUR	30 years	10	Deutsche Bank
15/09/2005	15/09/2008	USD	3 years	1 000	Royal Bank of Canada / BNP Paribas / Credit Suisse First Boston
17/10/2005	17/10/2025	EUR	20 years	50	Merrill Lynch
28/10/2005	15/09/2008	USD	2 years 11 months*	250	Royal Bank of Canada
23/11/2005	22/04/2013	USD	7 years 5 months*	250	Dresdner Bank
01/12/2005	01/12/2009	ZAR	4 years	511	Mitsubishi Securities International
14/12/2005	14/12/2015	AUD	10 years	200	The Toronto-Dominion Bank
15/12/2005	15/08/2008	AUD	2 years 8 months*	250	Royal Bank of Canada

* *re-opening of existing issues*

** *issue with a 1-year redemption call*

ISSUES BY MATURITY AT 31 DECEMBER 2005



V - PROFIT AND BALANCE SHEET

The Bank applied IFRS standards for the first time in 2005. In compliance with IFRS 1, the Bank presents its restated 2004 accounts, with the exception of application of IAS 32 and 39 relative to financial instruments, according to an option stated in the legal texts.

1. Trend in profits

Net profit for the financial year 2005 was € 88.5 million compared to € 121 million in 2004. This significant variation in the net profit was due to a reversal in 2004, totalling + € 32.3 million, for the remaining provisions for arrears concerning Bosnia and Herzegovina, and Serbia and Montenegro, countries which became members of the CEB.

The profit before extraordinary items for 2005, i.e. € 88.5 million, is on a par with that of 2004 after restatement: € 88.7 million, i.e. a variation of only - 0.2%.

This stability of profit encompasses the following developments:

- The increase of the net operating income rose by € 1.2 million, i.e. + 1% after an adjustment of - € 1.0 million following application of IAS 39. The higher volume of interest-bearing assets (cash, loans) was offset by a relative contraction in the financial margin due to a general drop on return on assets in 2005.

- The controlled increase of general operating expenses: + € 1.4 million, i.e. + 5%, mainly due to a rise in payroll, including a technical adjustment linked to application of IAS 19 relative to pension benefits and other benefit entitlements (tax adjustment and health insurance), i.e. - € 4 million in 2005 and - € 3.8 million in 2004.

Consequently, after application of IFRS, the cost/income ratio (general expenses/net operating income), remained stable at 25.1% in 2005 compared to 24.1% in 2004.

2. Trend in the balance sheet

At 31 December 2005, the total assets stood at € 17 675 million, representing an increase of 7.8% compared to the 2004 balance sheet after restatements.

- On the **assets** side, outstanding loans rose by € 878 million, i.e. + 8.1%, partly under the effect of an adjustment linked to application of IAS 39

TREND IN PROFITS

in million euros

	2005 IFRS	2004 IFRS	Variation	%	2004 reported
Net operating income	**118.1**	**116.9**	**+ 1.2**	**+ 1.0%**	**115.0**
General expenses	*- 29.6*	*- 28.2*	*+ 1.4*	*+ 5.0%*	*- 24.5*
Profit before extraordinary items	**88.5**	**88.7**	**- 0.2**	**- 0.2%**	**90.5**
Extraordinary items	*-*	*32.3*	*- 32.3*	*-*	*24.7*
NET PROFIT	**88.5**	**121.0**	**- 32.5**	**- 26.9%**	**115.2**

TREND IN THE BALANCE SHEET

in million euros

	2005 IFRS	2004 IFRS	Variation	%
ASSETS				
Financial assets at fair value through profit/loss and hedging derivatives	1 253	-	+ 1 253	-
Loans	11 714	10 836	+ 878	+ 8.1%
Employment of cash	2 904	3 225	- 322	- 10.0%
Financial assets held to maturity	1 750	1 663	+ 87	+ 5.2%
Other assets	54	672	- 618	- 92.0%
TOTAL	**17 675**	**16 396**	**+ 1 279**	**7.8%**

in million euros

	2005 IFRS	2004 IFRS	Variation	%
LIABILITIES				
Financial liabilities at fair value through profit/loss and hedging derivatives	1 909	-	+ 1 909	-
Debts represented by a security	13 725	11 777	+ 1 948	+ 16.5%
Cash resources	79	68	+ 11	+ 16.2%
Shareholders' equity	1 693	1 614	+ 79	+ 4.9%
Other liabilities	269	2 937	- 2 668	- 90.8%
TOTAL	**17 675**	**16 396**	**+ 1 279**	**7.8%**

totalling + € 160 million, i.e. + 1.5%. This rise was due to a significant volume of new loan disbursements totalling € 1 559 million of which 51% in favour of counterparties in a target group countries*, i.e. + 23.5% compared to 2004, despite substantial repayment by borrowers from Western European countries. In compliance with IAS 39, the 2005 balance sheet shows the positive value of swaps recognised as hedging instruments or not (loans, securities and debts), i.e. € 1 253 million. On the other hand, the interests accrued on derivatives, which represented most of the "other assets" item, have disappeared.

- On the **liabilities** side, debt represented by a security rose by € 1 948 million, i.e. + 16.5%, thus ensuring refinancing of the loan portfolio and liquidity reserves. In compliance with IAS 39, the 2005 balance sheet shows the negative value of swaps recognised as hedging instruments or not (loans, securities and debts), i.e. € 1 909 million. On the other hand, the foreign currency adjustment account and the interest accrued on derivatives, which represented most of the "other liabilities" item, have disappeared. Finally, shareholders'equity before allocation of profit rose by 4.9% under the combined effect of 2004 profit allocation and profit made in 2005.

**Albania, Bosnia and Herzegovina, Bulgaria, Croatia, Cyprus, Czech Republic, Estonia, Hungary, Latvia, Lithuania, Malta, Moldova, Poland, Romania, Serbia and Montenegro, Slovak Republic, Slovenia, "the former Yugoslav Republic of Macedonia" and Turkey.*

INTEGRATED RISK MANAGEMENT

Risk management and control are decisive factors in maintaining the financial soundness of a lending institution. Consequently, the CEB is constantly revising its risk management and monitoring systems so as to comply with best practices in the profession, the Basle Committee Recommendations and European Union Directives.

I - A STRUCTURED, DYNAMIC FUNCTION

Dedicated departments

- The **Risk Management Department** identifies, assesses and manages all the risks inherent in the CEB's operations, as a result of both on- and off-balance sheet transactions. For each new loan, the department analyses the transaction, taking into account the standing of the counterparty, the transactions already in progress with it and the country risk, and, if necessary, recommends that guarantees be obtained. The department also keeps constant watch on the application of portfolio management rules (loans, securities, derivatives) and monitors the Bank's situation with regard to large exposure.

- The **ALM Department** monitors market risk on a regular basis (interest rate risk, currency risk) and liquidity risk incurred by the Bank. Its conclusions are presented in a quarterly report submitted to the ALM Committee. This report analyses, through a number of stress tests, various scenarios of interest rate variations and their impact on the Bank's profitability and presents the projected liquidity situation based on various borrower default assumptions. It reports, where applicable, actual or foreseeable cases of limits being exceeded and proposes recommendations to the ALM Committee so as to reduce the detected risks.

- The **Organisation Department** is in charge of activities designed to protect the bank from operational risks. It identifies all the events that could cause operating losses. It manages the business continuity plan (updating and tests with retreat to the back-up site), the archiving framework and reviews the internal procedures covering all activities within the scope of operational risks. In concrete terms, the department is implementing the operational risk policy of the CEB and, for this purpose, is establishing a complete map of processes and associated operational risks. In addition, in order to increase security awareness among the personnel, various training courses are provided during the year.

Decision-making committees

- The **Risk Committee** is the keystone of the Bank's risk management system. Each week, decisions concerning counterparty and country limits are made on the basis of analyses and recommendations made by the Risk Management Department.

- The **Assets and Liabilities (ALM) Committee** decides on assets and liabilities management strategy. It takes the necessary decisions with regard to financial risks in light of the ALM report and on the basis of the financial policies approved by the Administrative Council.

- The **Funding Committee** decides on borrowing strategy (amounts, currencies, conditions and timing) taking into account the Bank's projected liquidity needs and within the framework of the annual borrowing authorisation set by the Administrative Council.

- The **Committee for Operational Risks and Organisation** validates the Bank's security policy and takes decisions relating to operational risk prevention.

Controlling bodies

- **Internal control**: each directorate controls the risks specific to its activity (self-assessment). Prior to signature, the *Central Directorate for Legal and Administrative Affairs* validates all contracts binding the CEB (loans, issues, derivatives, etc.) so as to control all the legal risks inherent in the banking business and more specifically those faced by a multilateral development bank.

Reporting directly to the Governor, the *Internal Audit Department* completes the Bank's control system through regular reviews of all activities, thus ensuring that the procedures are systematically complied with.

Finally, the *Auditing Board* consisting of three members chosen from shareholder countries and appointed by the Governing Board for a three-year term, examines the Bank's accounts and checks their accuracy in accordance with the Articles of Agreement. The Auditing Board's report, an excerpt of which is included in the Financial statements, is presented to the Bank's Boards at the time of annual approval of the accounts for the financial year.

- **External control**: as a multilateral development bank, the CEB is not subject to any national or international regulatory authority. However, in accordance with its statutory provisions and with banking best practices, it undergoes control by the following external entities:

- The *External Auditor*: appointed for a three-year term, upon the decision of the Governing Board, on the basis of an opinion given by the Auditing Board and a recommendation by the Administrative Council, following an invitation to tender, its task is to audit the Bank's financial statements and carry out a review of internal control and risks. At the end of each financial year, the External Auditor certifies the accounts and issues a report setting out his opinion (see Financial statements). It also prepares, for the directing bodies, an interim report bringing together its conclusions on procedures and internal control, a detailed report on the accounts for the financial year and the situation in matters of risks.

- The Bank undergoes strict assessment by the *international rating agencies*, Moody's, Standard & Poor's and Fitch Ratings which, each year, carry out an in-depth analysis of the Bank's financial structure to check its long-term creditworthiness and assign it a rating. In 2005, they all confirmed the maximum rating (AAA/Aaa) that they have been assigning to the CEB for several years now.

II - SITUATION AT 31 DECEMBER 2005

Within the context of its project and treasury financing activities, the CEB is exposed to three different types of risk: credit risk, market risk and operational risk.

1. Credit risk

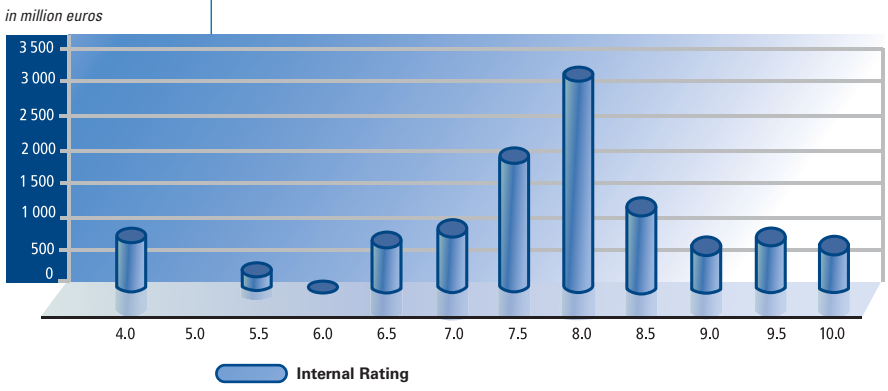
Credit risk can be defined as the risk of loan losses in the event of counterparty default. The credit risk on the loan portfolio is measured on the basis of a rating system. In accordance with the Basle Committee Recommendations, when a counterparty has various ratings, the second best rating is adopted. In the case of a guarantee with risk transferred to the guarantor, the CEB takes into account the latter's rating. In the absence of a rating, an internal rating is applied.

During 2005, CEB continued developing and improving its risk management methods.

In line with international best banking standards, the Risk Management Department provides an internal rating for all counterparties based on an adequate due diligence (on or off site). The common unified risk classification system consists of categories from 1 to 10, of which 10 is the best and 1 is the worst in terms of risk. Each internal grade corresponds to the rating agencies' scale. The internal rating system is reviewed periodically by both the internal and external auditors.

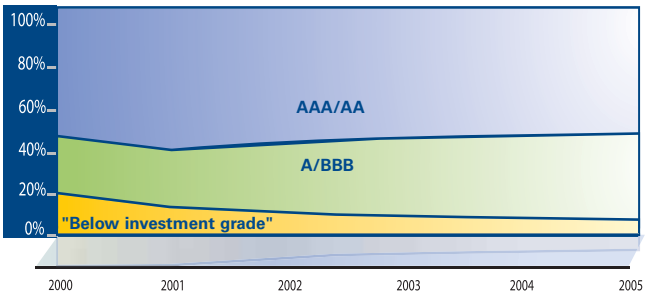
Furthermore the Bank introduced and further developed a methodology for establishing credit risk limits for regional and local government counterparties.

LOANS OUSTANDING BY INTERNAL RATING AT END 2005



Loans portfolio

In 2005, loans outstanding increased by 8.1% relative to 2004, reaching a total of € 11.5 billion. Loans rated "investment grade" represented 92.5% of the total portfolio compared to 91.6% at the end of 2004. The relative weight of loans classified "below investment grade" dropped from 8.4% in 2004 to 7.5%. This improvement resulted from the upgrading of some of Central and Eastern European countries.



As for the risk allocation per type of counterparty, in 2005, 46.1% of loans were allocated to financial institutions and 53.9% to states or government administrations.

Credit risk profile of the stock of projects

The credit risk quality of the stock "committed" remained outstanding with 91.4% on counterparties rated "investment grade", compared to 83.1% at year-end 2004. This improvement resulted from the upgrading of some of Central and Eastern European countries.

	2002	2003	2004	2005
Stock committed *(in million euros)*	1 906.5	2 171.0	2 199.7	2 290.9
AAA/AA	25.3%	30.2%	26.4%	29.6%
A/BBB	57.5%	52.8%	56.7%	61.8%
"Below investment grade"	17.2%	17.0%	16.9%	8.6%

Credit enhancement

At end of December 2005, the amount of credit enhancement in the loan portfolio ensuring a 100% risk transfer totalled € 1.8 billion (against € 1.6 billion at end of 2004), of which € 0.3 billion in collateral and € 1.5 billion in guarantees.

At 31 December 2005, the overall impact of these credit enhancements on the risk profile is shown in the following table:

	Before credit enhancement	After credit enhancement	Variation
AAA/AA	46.1%	51.7%	12.1%
A/BBB	46.0%	40.8%	-11.3%
"Below investment grade"	7.9%	7.5%	-4.6%
TOTAL	**100.0%**	**100.0%**	

In practical terms, the credit risk mitigation techniques allowed for the transfer of € 639.8 million from the A/BBB to the AAA/AA category.

Bond portfolios

The CEB manages two categories of bond portfolios: a portfolio of financial assets held to maturity and a portfolio of available-for-sale financial assets (see Financial Activities, p. 35). The breakdown, per rating, of the outstanding value of each of these portfolios at 31 December 2005, is given in the table below:

in million euros

	AAA	AA	A	Total
Available-for-sale financial assets	515	587	42	1 144
Financial assets held to maturity	1 435	211	8	1 654
TOTAL	**1 950**	**798**	**50**	**2 798**

Derivatives

The Bank uses derivatives to hedge the interest rate and currency risks on its lending and borrowing operations (see Derivatives, p. 37).

Derivative transactions, in all cases, require prior credit clearance of the issuing counterparty by the Risk Committee and prior signing of a framework agreement (for example, the ISDA Master Agreement). In addition, for transactions with a maturity of over five years, the counterparty must have a minimum AA rating or have signed a CSA (Credit Support Annex) collateral agreement with the CEB.

All swap operations are valued at their net present value and the positions per counterparty are monitored daily so that additional collateral can be requested where necessary.

The CEB has pursued and extended its active policy of collateral agreement management in order to further reduce the credit risk entailed in the use of derivatives. Moreover, 82% of the notional outstanding and 100% of the value at risk concern counterparties with ratings of at least AA.

Large exposure

Large exposure is the total exposure in regard to a single counterparty (or group of counterparties) exceeding 10% of shareholders' equity. In this respect, the CEB adopts as the definition of shareholders' equity, paid-in capital, reserves, profits plus uncalled capital of shareholder countries with an AAA or AA rating (according to Moody's, Standard & Poor's and Fitch Ratings).

In accordance with the Basle Committee Recommendations and European Union directives, the CEB ensures that no counterparty (or group of counterparties) exceeds the limit of 25% of shareholders' equity as defined above, and that the cumulative total of large exposure does not exceed 800% of said shareholders' equity.

At the end of 2005, no counterparty exceeded the limit of 25% of the CEB's shareholders' equity, and only five counterparties exceeded 10%. The total outstanding exposure to these five counterparties amounts to € 3 billion, i.e. 73.9% of the CEB's shareholders' equity, within a limit of 800%.

2. Market risk

Interest-rate and currency risks

Market risk includes, in particular, the risk of a loss being incurred as a result of an adverse fluctuation in interest or exchange rates.

The strategy adopted by the directing bodies with regard to interest-rate risks is based on systematic hedging of positions, so as to reduce the interest-rate risk to a minimum.

The Bank uses derivatives to protect itself against interest and currency risks on its lending and borrowing operations. Macro-hedging can also be considered if necessary. Moreover, since the Bank performs no trading operations, there is no credit risk which requires matching with part of its own funds, all in accordance with the Basle Committee Recommendations. In conclusion, the interest rate risk in the CEB's balance sheet is limited to the portfolio of fixed-rate financial assets held to maturity, backed by the Bank's usable capital.

As regards the currency risk, the CEB's strategy is not to take any position and to finance assets and liabilities in a single currency. The residual risk arising from gains and losses in currencies other than the euro is systematically monitored and hedged on a monthly basis. The net open position is limited to the countervalue of € 1 million per currency. As at 31 December 2005, the net open position was almost nil.

Liquidity risk

The projected liquidity situation is covered by a weekly report submitted to the Treasury Committee. This is supplemented by stress tests presented to the ALM Committee, based on borrower default assumptions.

The liquidity ratio has been reinforced (see page 46).

3. Operational risk

The operational risk represents the risk of direct or indirect loss resulting from inadequate or failed structures, procedures, people or systems as well as from external events.

By deliberately choosing to operate within the framework of the Basle Committee Recommendations, the CEB has undertaken to assess constantly its operational risks and to put in place the appropriate preventive measures. The Basic Indicator Approach method (BIA) is adopted to calculate the operational risk charge against the Bank's shareholders' equity, namely € 17 million as at 31 December 2005.

III - PRUDENTIAL FRAMEWORK

Whilst establishing its Development Plan 2005-2009 and in order to define a precise framework for the new strategic guidelines which characterise it, the Bank has defined a new prudential framework inspired by the Basle Committee Recommendations, especially with regard to capital adequacy.

This new prudential framework, approved by the CEB's Administrative Council in June 2004 took effect as of 1 January 2005, and is mainly organised around three ratios:

1. The capital adequacy ratio

This limits the default risk to usable capital.

CAPITAL ADEQUACY RATIO =

$$\frac{\text{Risk Weighted Loan Portfolio}}{\text{Usable Capital}}$$

- *Risk Weighted Loan Portfolio: ∑ [(Capital + Interest) x Default Probability]*
- *Usable capital: total of paid-in capital and reserves*

The absolute limit of the capital adequacy ratio is set at 100%. At the end of 2005, this ratio stood at 17% against 29% at end 2004.

2. The risk asset coverage ratio

This ratio constitutes an additional limit on the volume of loans outstanding. In accordance with the analysis methodology already applied by the rating agencies, it limits the fraction of the loan portfolio rated "below investment grade" to the "usable capital" plus uncalled AAA/AA capital.

RISK ASSET COVERAGE RATIO =

$$\frac{\text{Portfolio of loans rated "below investment grade"}}{\text{Usable Capital + Uncalled AAA/AA capital}}$$

The limit is set at 66%, i.e. € 2.6 billion. At the end of December 2005, this ratio was 21.8%, compared to 24.4% at end-2004.

3. The reinforced liquidity ratio

The CEB's cash position must not be less than 50% of the net liquidity requirement for the next three years, including the additional liquidity requirement equal to the risk of default of counterparties rated "below investment grade" for the same period. At end 2005, the reinforced liquidity ratio was 75.8% against 91.7% at end 2004.

4. Other statutory ratios

- **Indebtness ratio:** this is the ratio of total debt outstanding against total equity in the broadest sense (subscribed capital and reserves). At 31 December 2005, this ratio was 3.11 compared to a maximum limit of 4.

- **Portfolio ratio:** this is the ratio of the total outstanding of the securities portfolio plus cash transactions not represented by securities (bank deposits, repos) against the amount of equity in the broadest sense. At 31 December 2005, this ratio was 0.99 compared with a maximum limit of 1.5.



HUMAN RESOURCES MANAGEMENT

In order to meet extremely rigorous commitments in matters of risk and quality and to accompany the enhancing of its scope of action, the CEB has steadily increased its staff numbers over the past few years.

Since 1994, the Bank's staff has thus increased by an average of 7% per year. In all, the number of Appointed Officials and permanent staff members doubled over the period to reach 139 by end 2005. This nevertheless remains a very reasonable figure given the volumes of activity recorded by the Bank.

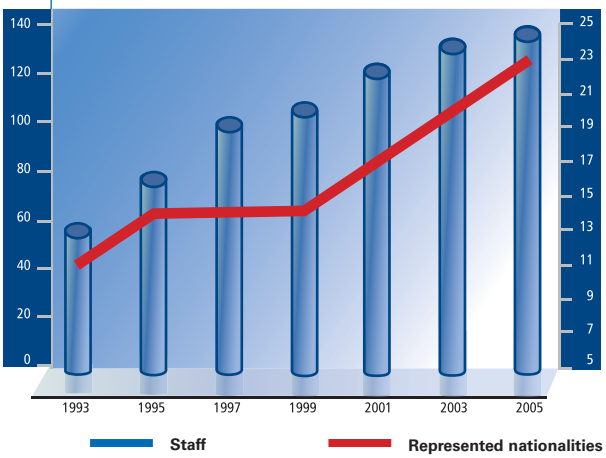
During 2005, the Bank pursued the very significant recruitment effort underway since the approval of the Development Plan 2005-2009 in June 2004. It thus has proceeded with the recruitment of 9 permanent staff members.

As was the case in previous years, this recruitment policy went hand in hand with continued diversification of the nationalities represented among the Bank's teams.

The number of nationalities present among the Bank's staff thus increased by 15% in the past year and has increased by over 100% since 1994, reaching a total of 23 by end 2005 (see graph). This increase has been even more marked among the CEB's management staff where, between 1994 and 2005, the number of represented nationalities increased threefold to reach 21 by end 2005.

This effort to diversify the nationalities has been particularly targeted to the countries that have just recently joined the Bank. Over half the permanent staff members recruited in 2005 are from countries that have joined the Bank since 1994. In all, at end 2005, these countries comprised over one third of all the nationalities represented on the Bank's staff.

TREND IN STAFF NUMBERS AND REPRESENTED NATIONALITIES



At the same time, the CEB strove throughout the year to further improve the organisation of its various departments. Thus, the budget piloting functions have been brought together with those of human resources in order to enhance their respective efficiency.

Lastly, in 2005 the CEB pursued a policy of staff evaluation and capacity building based, notably, on training programmes tailored to the specific nature of its activity. In all, more than 90% of the staff received either technical, linguistic or computer training during the year.

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FINANCIAL STATEMENTS PREPARED IN COMPLIANCE WITH IFRS STANDARDS ADOPTED BY THE EUROPEAN UNION

THE BANK'S OBJECTIVES

"The primary purpose of the Bank is to help in solving the social problems with which European countries are or may be faced as a result of the presence of refugees, displaced persons or migrants consequent upon movements of refugees or other forced movements of populations and as a result of the presence of victims of natural or ecological disasters.

The investment projects to which the Bank contributes may be intended either to help such people in the country in which they find themselves or to enable them to return to their countries of origin when the conditions for return are met or, where applicable, to settle in another host country. These projects must be approved by a member of the Bank.

The Bank may also contribute to the realisation of investment projects approved by a member of the Bank which enable jobs to be created in disadvantaged regions, people in low income groups to be housed or social infrastructure to be created".

(Articles of Agreement, Article II).

In furtherance of the Bank's objective of strengthening its actions in favour of social cohesion, in conformity with the provisions of Resolution 1424 (1997), and as revised in 2003, the Bank's fields of action have been broadened. Since 2001, the Bank may, beyond its initial statutory priorities, contribute to the financing of social infrastructures related to the protection of the environment and the rehabilitation of the historical heritage. Financing investment plans in small and medium-sized enterprises and small industrial firms, which contribute to job creation, is also one of the Bank's major fields of action.

The Bank's activities with respect to project-financing can be presented under 3 main areas of intervention: strengthening social integration, managing the environment and developing human capital. Within this context, the Bank has undertaken to redefine certain eligibility criteria concerning projects for the improvement of quality of life in disadvantaged urban areas, social housing, as well as those applicable to sector-based multi-project programmes (SMPs), and this with a view to better adapting itself to the social and economic realities of its members.

The Bank's policy, similar to that of other multilateral financial institutions, is not to reschedule interest or capital payments on its loans and not to participate in debt rescheduling agreements.

APPLICABLE ACCOUNTING STANDARDS

Up to 31 December 2004, the Bank's financial statements have been prepared in accordance with the general principles of the European Parliament and European Union Council Directive on the annual accounts and consolidated accounts of banks and other financial institutions (Directive 86/635 EC amended by Directive 2001/65/EC and by Directive 2003/51/EC).

Although the Bank is under no legal or statutory obligation to adopt IFRS standards (International Financial Reporting Standards) as from the 2005 financial year, the Administrative Council decided, on 15 November 2005 that, as from 31 December 2005, the Bank's non-consolidated accounts would for the first time and thereafter be prepared in compliance with IFRS standards as adopted by the European Union. This decision was taken in order to improve comparability with the other multilateral financial institutions.

Consequently, the accounts as at 31 December 2005 are prepared in accordance with IFRS standards as adopted by the European Union at that date.

Accounts for the 2004 financial year, presented for comparison purposes, are prepared in compliance with the same IFRS standards except for IAS 32 and IAS 39. In fact, the Bank decided to use the option provided under IFRS 1 to maintain unchanged in the opening balance sheet at 1 January 2004 transactions arising from IAS 32 and IAS 39 and to apply these standards for the first time as of 1 January 2005. Transactions arising from these standards will thus continue to be accounted for and presented in accordance with the accounting policies provided under the above-mentioned European Union Directive.

The following are the norms employed in drawing the financial statements:

- **Balance sheet**

  The balance sheet as at 31 December 2005 is prepared in compliance with IFRS standards as adopted by the European Union at that date. In the financial statements, these standards are referred to as "IFRS 2005". Figures for the financial year 2004, presented for comparison purposes, are accounted for and presented in accordance with these same standards, except for IAS 32 and IAS 39. These standards are referred to as "IFRS 2004".

- **Profit and loss account**

  The profit and loss account for the 2005 financial year is presented in compliance with the new denominations and classifications of IFRS standards. The main reclassifications and restatements, resulting from the application of the standards referred to as "IFRS 2004" applied to the profit and loss account for the 2004 financial year, prepared in accordance with the previous standards, are specifically presented under Note 2.3: "Effects of the first application of IFRS standards - Transition of the 2004 profit and loss account".

- **Shareholders' equity**

  The statement of changes in shareholders' equity, between 31 December 2003 and 31 December 2005, incorporates the impact of the adjustments carried out in applying IFRS standards in force on 1 January 2004, on 31 December 2004 and on 1 January 2005 respectively.

- **Accounting policies**

  The accounting policies employed by the Bank, within the framework of IFRS 2004 and IFRS 2005, are described under Note 1 - Accounting policies and valuation methods.

BALANCE SHEET

In thousand euros

	Notes	31/12/05 IFRS 2005	31/12/04 IFRS 2004
Assets			
Cash in hand, balances with central banks		65	49
Fair value financial assets through profit or loss	A	384 778	
Hedging derivatives	B	868 587	
Available-for-sale financial assets	C	1 168 179	
Loans and advances to credit institutions and to customers			
Loans	D	11 713 728	10 836 308
Advances	D	1 734 690	1 467 395
Securities portfolio	C		3 419 873
Financial assets held to maturity	C	1 750 402	
Fixed assets	E	29 251	26 583
Other assets	F	25 164	645 582
Total assets		**17 674 844**	**16 395 790**
Liabilities			
Fair value financial liabilities through profit or loss	A	1 278 289	
Hedging derivatives	B	630 997	
Amounts owed to credit institutions and to customers	G	79 084	68 263
Debt securities	G	13 724 837	11 776 777
Other liabilities	F	155 056	2 835 546
Selective Trust Account (STA)	H	64 740	57 431
Provision for financial risks	I	48 609	43 302
Total liabilities		**15 981 612**	**14 781 319**
Capital	J		
Subscribed		3 293 570	3 293 570
Uncalled		(2 924 922)	(2 924 922)
Called		368 648	368 648
General reserve		1 235 820	1 124 811
Unrealised or deferred gains or losses	C	225	
Profit for the year		88 539	121 012
Total shareholders' equity		**1 693 232**	**1 614 471**
Total liabilities		**17 674 844**	**16 395 790**

The Bank decided to use the option provided under IFRS 1 to maintain unchanged the opening balance sheet at 1 January 2004 in conformity with the provisions of IAS 32 and IAS 39 as adopted by the European Union and to apply these two standards for the first time on 1 January 2005. In this respect, for the 2004 comparative figures, financial instruments and transactions arising from IAS 32 and IAS 39 are accounted for and presented according to the accounting policies in conformity with the general principles as provided under the European Parliament and European Union Council Directive on the annual accounts and consolidated accounts of banks and other financial institutions. Note 2 specifies the overall effects of the first application of the IFRS standards as adopted by the Bank.

PROFIT AND LOSS ACCOUNT

In thousand euros

	Notes	31/12/05 IFRS 2005	31/12/04 IFRS 2004
Interest receivable and similar income			
Available-for-sale financial assets		30 319	
Loans and advances to credit institutions and to customers		299 786	241 539
Financial assets held to maturity		84 038	
Treasury assets			62 834
Investment portfolio			83 012
Interest expenses and similar charges			(270 446)
Amounts owed to credit institutions and to customers		(5 524)	
Debt securities		(292 258)	
Interest margin	K	**116 361**	**116 939**
Net commissions		28	
Net gains or losses on fair value financial instruments through profit or loss	L	1 576	
Net gains or losses on available-for-sale financial assets		143	
Income from shares and other variable-yield securities			55
Foreign exchange			(161)
Held-for-sale securities			8
Commissions and other net operating expenses			90
Total operating income		**118 108**	**116 931**
General operating expenses	M	(27 874)	(26 454)
Net depreciation charges of fixed assets	E	(1 695)	(1 721)
Operating profit before provisions		**88 539**	**88 756**
Risk cost	N		32 256
Profit for the year		**88 539**	**121 012**

STATEMENT OF CHANGES IN SHAREHOLDERS' EQUITY

In thousand euros

	Called capital	Reserves and result	Unrealised or deferred gains/losses	Total shareholders' equity
Shareholders' equity as at 31 December 2003 (in conformity with the previous standards)	**363 735**	**878 991**		**1 242 726**
Appropriation of profit for the 2003 financial year		86 000		86 000
Shareholders' equity as at 1 January 2004 (in conformity with the previous standards)	**363 735**	**964 991**		**1 328 726**
Impact of the adoption of IAS/IFRS standards applied in 2004		145 574		145 574
Shareholders' equity as at 1 January 2004 in conformity with IAS/IFRS standards applied in 2004	**363 735**	**1 110 565**		**1 474 300**
Increase during the financial year	4 913	14 246		19 159
Sub-total of movements in relation to member states	**4 913**	**14 246**		**19 159**
Reported profit for financial year 2004		115 166		115 166
Impact of the adoption of IAS/IFRS standards on reported profit for 2004		5 846		5 846
Profit for financial year 2004 in IAS/IFRS standards applied in 2004		**121 012**		**121 012**
Shareholders' equity as at 31 December 2004 in conformity with IAS/IFRS standards applied in 2004	**368 648**	**1 245 823**		**1 614 471**
Impact of the adoption of IAS 32 and IAS 39		(3)	(96)	(99)
Shareholders' equity as at 1 January 2005 in conformity with IAS/IFRS standards applied in 2005 before appropriation of 2004 profit	**368 648**	**1 245 820**	**(96)**	**1 614 372**
Appropriation of profit for the 2004 financial year		(10 000)		(10 000)
Shareholders' equity as at 1 January 2005 in conformity with IAS/IFRS standards applied in 2005 after appropriation of 2004 profit	**368 648**	**1 235 820**	**(96)**	**1 604 372**
Profit for the 2005 financial year		88 539		88 539
Other movements			321	321
Shareholders' equity as at 31 December 2005 in conformity with IAS/IFRS standards applied in 2005	**368 648**	**1 324 359**	**225**	**1 693 232**

The main restatements carried out in application of IFRS standards are presented in the transition tables under paragraph 2.

The Bank recorded definitively the impacts on the general reserve following the adoption of IFRS standards. It should be noted that the general reserve is the only type of reserve included in the Bank's shareholders' equity.

STATEMENT OF CASH FLOWS

In thousand euros

For the year ended 31 December	Notes	31/12/05 IFRS 2005	31/12/04 IFRS 2004
Profit for the year		**88 539**	**121 012**
+/- Net depreciation charges of tangible and intangible fixed assets	E	1 695	1 843
+/- Net provision charges	N		(32 256)
+/- Net losses/net profits from investment operations		2 456	2 352
+/- Other movements		9 413	6 891
Total of non-monetary items included in the result		**13 564**	**(21 170)**
+/- Cash flows related to operations with credit institutions and customers		(578 455)	(859 244)
+/- Cash flows related to other operations affecting financial assets or liabilities		480 938	(502)
+/- Cash flows related to operations affecting non-financial assets or liabilities		112 155	(12 653)
Net decrease /(increase) of assets and liabilities resulting from operational activities		**14 638**	**(872 399)**
Total net cash flows generated by operational activities (a)		**116 741**	**(772 557)**
+/- Cash flows related to financial assets		(88 084)	(101 733)
+/- Cash flows related to tangible and intangible fixed assets	E	(4 320)	(792)
Total net cash flows related to investment operations (b)		**(92 404)**	**(102 525)**
+/- Cash flows from/to member states		11 039	6 831
+/- Net cash flows from financing operations		219 628	1 385 370
Total net cash flows related to financing operations (c)		**230 667**	**1 392 201**
Effects of exchange rate variations on cash and cash equivalents (d)		**12 624**	**(6 450)**
Net increase/(decrease) in cash and cash equivalents (a)+(b)+(c)+(d)		**267 628**	**510 669**
Cash and cash equivalents at the beginning of the financial year		**1 463 682**	**953 013**
Cash in hand, central banks		*49*	*52*
Accounts assets and loans repayable on demand with credit institutions	D	*1 464 734*	*952 961*
Accounts liabilities and issues repayable on demand with credit institutions		*(1 101)*	
Cash and cash equivalents at the end of the financial year		**1 731 310**	**1 463 682**
Cash in hand, central banks		*65*	*49*
Accounts assets and loans repayable on demand with credit institutions	D	*1 731 245*	*1 464 734*
Accounts liabilities and issues repayable on demand with credit institutions	G		*(1 101)*
Net cash flows variations		**267 628**	**510 669**

Financing activities consist of cash flows deriving from debt securities.

NOTES TO THE FINANCIAL STATEMENTS

1 - ACCOUNTING POLICIES AND VALUATION METHODS

The principal norms with respect to the valuation and presentation employed in preparing the Bank's financial statements as at 31 December 2004 and 31 December 2005 are specified hereafter. The Bank did not use any of the optional exceptions authorised under IFRS 1.

1.1 Accounting policies applied to the financial statements as from 1 January 2005 ("IFRS 2005")

Foreign currency transactions

In conformity with Article IV (Section 1) of the Bank's Articles of Agreement, the financial statements are presented in euros.

Monetary assets and liabilities denominated in foreign currencies other than the euro are translated into euros at the exchange rate applicable at the end-date of the accounting period. Exchange adjustments resulting from this foreign currency translation are accounted for in the profit and loss account.

Non-monetary assets denominated in foreign currencies, particularly shares and other variable-yield securities which are classified as "available-for-sale financial assets" are translated into euros at the exchange rate applicable at end-date. Resulting exchange variations recorded under shareholders' equity are accounted for in the profit and loss account only at their disposal, or at an eventual reduction in market value, as well as in the case of fair value hedge of exchange risk.

Forward currency transactions are valued at market value by using the forward exchange rate applicable for the remaining period for the currency concerned. Cash positions are valued at the spot exchange rate at the end of the period. Any resulting exchange differences are recorded in the profit and loss account.

Non-derivative financial assets and liabilities

The purchase of financial assets held to maturity and the purchase and sale of available-for-sale financial assets are accounted for in the balance sheet at transaction settlement date whereas derivatives are recorded at trade date.

Financial assets and liabilities are valued at their fair value when first recorded and are classified under one of the following four categories:

- **Loans and advances**

Loans and advances are first recorded at their market value, which in general is the equivalent of the net amount disbursed by the Bank. Thereafter, loans and advances are valued at the amortised cost on the basis of the effective interest rate, and could be subject to depreciation. This depreciation is accounted for when there is an objective indication that an event occurred after loan approval that might lead to a measurable loss.

Financing commitments are recorded in the off-balance sheet for the amount not yet used.

- **Financial assets held to maturity**

This category includes securities at fixed income and fixed maturity which the Bank has the intention and the means to hold to maturity. They are accounted for at the amortised cost in accordance with the effective interest rate method, which includes the amortisation of the premium or discount as well as purchase charges. Securities' depreciation is recorded under the profit and loss account in cases of an objective indication of durable depreciation resulting from events subsequent to the purchase.

• Available-for-sale financial assets

These are non-derivative financial assets held for an unspecified duration and which the Bank may have to dispose of at any time. Consequently, these are financial assets which do not fall under any of the two preceding categories. The value recorded when they are first accounted for is the trade price (i.e. the value of the consideration paid). These financial assets are valued at their market value. This is equivalent to the amount for which an asset could be exchanged, or a liability settled, between knowledgeable, willing parties in an arm's length transaction. The fair value used is the quoted market price in cases where the security is quoted in an active market. In absence of an active market, the fair value is the one determined by the company managing the security. Accrued or acquired income from fixed income securities is recorded in the profit and loss account on the basis of the effective interest rate, whilst fair value changes, excluding income earned, are presented in a specific line item under shareholders' equity ("unrealised or deferred gains or losses"). Income from variable-yield securities is equally recorded under the profit and loss account. Securities' depreciation is recorded under the profit and loss account in cases of an objective indication of durable depreciation resulting from events subsequent to the purchase.

In case of a subsequent improvement, depreciation of fixed income securities is recorded under the profit and loss account. In the case of variable-yield securities, this depreciation is recorded under shareholders' equity and transferred to the profit and loss account at the date of disposal of the security.

• Debt securities

Debt securities are first recorded at their issuance value, net of transaction charges, and are subsequently valued at their amortised cost by using the effective interest rate method including issue or reimbursement premium.

Derivatives

Derivatives are classified under two categories:

• Transaction derivatives

Derivatives are considered to be transaction instruments, except that they can be qualified as hedging instruments. They are recorded in the balance sheet under the item "fair value financial assets through profit or loss" in cases of positive market value and under "fair value financial liabilities through profit or loss" when the market value is negative. Profits or losses are recorded in the profit and loss account as "net profits or losses on market value financial instruments through profit or loss".

• Hedging derivatives

Value hedging is used by the Bank as interest rate risk cover of fixed-rate assets and liabilities for identified financial instruments (loans, securities, debt).

In order to qualify a hedging derivative, the Bank keeps a report on the hedge from its initial application. This report specifies the asset, the liability, the hedged risk, the type of derivative used and the evaluation method which will be employed in assessing the retrospective and prospective effectiveness of the hedge. The hedging derivative has to be highly effective in order to compensate for the value variations resulting from the hedged risk; this effectiveness has to be ensured from the hedge's initial application and subsequently throughout its life.

In the case of fair value hedging, derivatives are revalued in the balance sheet at their fair value, whilst fair value variations are recorded in the profit and loss account under "net profits or losses on market value financial instruments through profit or loss", symmetrically to the revaluation of the instruments hedged for the estimated risk. In the balance sheet, in the case of hedging of identified assets or liabilities, the revaluation of the hedged item is accounted for in conformity with the classification of the hedged instrument. The impact recorded in the profit and loss account represents the eventual ineffectiveness of the hedge.

In cases where a hedge is interrupted or it no longer satisfies the effectiveness tests, hedging derivatives are transferred to the trading portfolio and accounted for in accordance with the policies applicable to this category. In the case of initially hedged identified interest rate instruments, the revaluation amount with respect to these instruments recorded in the balance sheet is amortised at the effective interest rate for its residual life duration. If the hedged items no longer figure in the balance sheet, particularly due to early redemption, this amount is immediately recorded in the profit and loss account.

Fixed assets

Fixed assets recorded under the Bank's balance sheet include tangible and intangible fixed assets.

Fixed assets are recorded at their purchase price, to which, expenses directly connected are added.

Depreciation is calculated according to the estimated useful life of the asset expected by the Bank using the straight-line method, the residual value of the asset being deducted from its depreciable basis.

At every end-date, fixed assets are valued at their amortised cost (cost less depreciation and any eventual impairment) and in which case, an accounting adjustment is carried out with respect to the duration of the useful life and the residual value.

• Tangible fixed assets

The following is the breakdown of the "building" part of the operational premises, every element being depreciated according to its own useful life:

• Main works	50 years
• *Façade* and roofing	50 years
• General and technical installations	10 years
• Fixtures and fittings	10 years

Land is not depreciated. The other tangible fixed assets are depreciated according to the following durations:

• Fittings and furniture	10 years
• Vehicles	4 years
• Office and IT equipment	3 years

• Intangible assets

Intangible assets (IT software) are amortised by using the straight-line method over either 1 year (office software) or 5 years (application software).

Post-employment staff benefits

The Bank's pension scheme is a defined benefit scheme, funded by contributions made partly by the Bank and partly by the employees. Benefits are calculated on the number of years of service and a percentage of the basis remuneration of the last year of service.

The other two post-employment benefits schemes (possibility for retired staff to maintain the medical insurance if they would wish to, fiscal adjustment) are likewise defined benefit schemes.

These schemes, which are valued and for which provisions are set up, represent a commitment on the part of the Bank.

In conformity with IAS 19, actuarial valuations are carried out on these commitments, taking into account both financial and demographic assumptions.

The amount of the provision in relation to these commitments is determined by an independent actuary in accordance with the projected unit credit method.

The Bank applies the "corridor" method to calculate changes in the level of its actuarial variations relating to the staff pension scheme. This method leads to the amortisation, in the profit and loss account, of the actuarial variances over the average number of expected remaining working years of the beneficiaries to the pension scheme when such changes represent over 10% of the discounted value of the commitment relative to the defined benefits.

Selective Trust Account (STA)

The Selective Trust Account (STA) is the Bank's special instrument enabling it to accentuate the impact of its action in social priority sectors (natural disasters, refugees, minorities and disadvantaged persons, as well as migrants), whose main features are defined in Resolution CA 1380 (1995) and revised by Resolution CA 1437 (1999, revised in 2001).

The purpose of this account is to provide interest rate subsidies for loans granted by the Bank for projects of high social value, concerning low-income countries particularly Central and Eastern European countries. The STA can also be used in granting donations in aid of victims of natural disasters, refugees, minorities and disadvantaged persons.

The account is funded by contributions received from the Bank's member states through dividends of a social nature allocated at the time of the Bank's appropriation of profits. It is also funded by voluntary contributions from member states of the Bank and the Council of Europe.

Interest rate subsidies and donations are subject to approval by the Bank's Administrative Council.

Donations are granted to the beneficiaries and interest rate subsidies are recorded in the profit and loss account under "Interest receivable and similar income" and are spread over the life of the relative loans.

This account is detailed under a note to the financial statements (see Note H).

Provision for financial risks

Provisions recorded on the liabilities side of the Bank's balance sheet concern exclusively social commitments - post-employment staff benefits.

Related parties

With respect to IAS 24, the Bank does not control any entity and has no share investments. Moreover, the Bank is not a subsidiary of any entity. The financial statements are not affected by related party relationships.

Taxation

The Third Protocol to the General Agreement on Privileges and Immunities of the Council of Europe states that the Bank's assets, income and other property are exempt from all direct taxes.

1.2 Accounting policies applied to the 2004 financial statements presented for comparative purposes ("IFRS 2004")

The Bank decided to use the option provided under IFRS 1 not to restate the opening balance sheet at 1 January 2004 in conformity with the provisions of IAS 32 and IAS 39 as adopted by the European Union, but to apply these standards for the first time as of 1 January 2005.

In this respect, financial instruments and transactions arising from IAS 32 and IAS 39 are accounted for and presented in accordance with the following accounting principles, which are in conformity with the European Union Directive 86/635 EC as amended:

Foreign currency transactions

Monetary assets and liabilities, as well as financing commitments, denominated in foreign currencies other than the euro are translated into euros at the exchange rate applicable at the balance sheet date. Revenue and charges are translated into euros at the exchange rate applicable at the end of the month during which they occurred. Exchange profits or losses resulting from the conversion of assets, liabilities and commitments relative to forward currency transactions are accounted for in the profit and loss account.

Loans and advances

Loans and advances issued by the Bank are recorded under the historical cost convention. Provisions are set up for risks of non-recovery of a part or the total amount of the loan granted.

Securities portfolio

Securities are classified as follows:

- by nature: treasury bills and similar securities, debt securities and other fixed income securities, shares and other variable-yield securities;
- by destination (held-for-sale, investment) corresponding to the economic purpose of their holding.

Investment securities

These securities are purchased with the intention of holding them until maturity date. They are accounted for at their purchase price, and adjusted up to maturity by the amortisation of the premium or discount at the time of purchase, using the straight-line method. These securities may be subject to depreciation in cases of a default risk on the part of the issuer.

Held-for-sale securities

Securities other than investment securities are considered as held-for-sale securities. They are first recorded at their historical cost, and are valued thereafter at market value. A provision is set up for losses whilst profits are not recorded.

Debt securities

These borrowings are recorded at their nominal value. Issue premiums and issuance fees are amortised using the straight-line method over the life of the issue.

Derivatives

Derivatives include interest rate derivatives and foreign currency derivatives. The notional of these instruments is recorded in the off-balance sheet, and these operations are valued thereafter according to the objective sought.

- **Hedging activities**

Profits and losses on hedging instruments are recorded in the profit and loss account in the same way as profits and losses on the hedged item. Premiums paid or received are amortised over the life of the hedged instrument.

- **Other activities**

Trading positions are marked to market and the resulting realised and unrealised gains or losses are recorded in the profit and loss account.

2 - EFFECTS OF THE FIRST APPLICATION OF IFRS STANDARDS AS ADOPTED BY THE EUROPEAN UNION

The main effects of the transition of the shareholders' equity, of the balance sheet and the profit and loss account between the financial statements published in accordance with the Bank's previous accounting standards and the financial statements in IFRS standards, as well as reclassifications carried out between certain headings, are shown hereafter.

2.1 Transition of the balance sheet at 31 December 2004

In thousand euros

	31/12/04 previous standards	Reclassifications and restatements	31/12/04 IFRS 2004
Assets			
Cash in hand, balances with Central Banks	49		49
Loans and advances to credit institutions and to customers			
Loans	10 836 308		10 836 308
Advances	1 467 395		1 467 395
Securities portfolio	3 419 873		3 419 873
Fixed assets [1]	20 571	6 012	26 583
Other assets	645 582		645 582
Total assets	**16 389 778**	**6 012**	**16 395 790**
Liabilities			
Amounts owed to credit institutions and to customers	68 263		68 263
Debt securities	11 776 777		11 776 777
Other liabilities	2 835 546		2 835 546
Selective Trust Account (STA)	57 431		57 431
Provision for financial risks [2]	44 710	(1 408)	43 302
Fund for General Banking Risks [3]	144 000	(144 000)	
Total liabilities	**14 926 727**	**(145 408)**	**14 781 319**
Shareholders' equity			
Capital			
Subscribed	3 293 570		3 293 570
Uncalled	(2 924 922)		(2 924 922)
Called	368 648		368 648
General reserve	979 237	145 574	1 124 811
Profit for the year	115 166	5 846	121 012
Total shareholders' equity	**1 463 051**	**151 420**	**1 614 471**
Total liabilities	**16 389 778**	**6 012**	**16 395 790**

Comments on the main impacts of the transition to IFRS 2004:

1) Fixed assets

The application of IAS 16 and IAS 36 as from 1 January 2004 increased the net book value in the balance sheet by 6.01 million euros as a result of the increase of 5.89 million euros in the reserves and 0.12 million euros in the 2004 profit and loss account.

2) Social commitments

The application of IAS 19 as from 1 January 2004 has generated an increase of 5.72 million euros in the 2004 result, a reduction of 4.32 million euros in the opening reserves and 1.40 million euros in the provision for financial risks in connection with social commitments.

3) Fund for General Banking Risks (FGBR)

Given that the FGBR does not meet the eligibility criteria set by IAS 30 and IAS 37 to qualify these liability items, its reclassification increases the shareholders' equity by 144 million euros.

2.2 Transition of the 2004 profit and loss account

In thousand euros

	31/12/04 previous standards	Reclassifications and restatements	31/12/04 IFRS 2004
Interest receivable and similar income			
Loans	241 539		241 539
Treasury assets	62 834		62 834
Investment portfolio	83 012		83 012
Interest expenses and similar charges [1]	(272 352)	1 906	(270 446)
Interest margin	**115 033**	**1 906**	**116 939**
Income from shares and other variable-yield securities	55		55
Foreign exchange	(161)		(161)
Held-for-sale securities	8		8
Other income and charges	90		90
Total operating income	**115 025**	**1 906**	**116 931**
General operating expenses [1]	(22 696)	(3 758)	(26 454)
Depreciation [2]	(1 843)	122	(1 721)
Operating profit before risk cost	**90 486**	**(1 730)**	**88 756**
Risk cost [1]	24 680	7 576	32 256
Profit for the year	**115 166**	**5 846**	**121 012**

1) Social commitments

The application of IAS 19 as from 1 January 2004 has generated an increase of 5.72 million euros in the 2004 result, and 1.90 million euros following the reclassification of interest paid by the Bank with respect to the pension scheme.

2) Fixed assets

The application of IAS 16 and IAS 36 as from 1 January 2004, has led to a net release of depreciation amounting to 0.12 million euros.

2.3 Transition of the balance sheet at 1 January 2005

In thousand euros

	31/12/04 IFRS 2004	Reclassifications and restatements	01/01/05 IFRS 2005
Assets			
Cash in hand, balances with central banks	49		49
Fair value financial assets through profit or loss		118 649	118 649
Hedging derivatives		971 190	971 190
Available-for-sale financial assets		1 809 028	1 809 028
Loans and advances to credit institutions and to customers			
Loans	10 836 308	219 685	11 055 993
Other advances	1 467 395		1 467 395
Securities portfolio	3 419 873	(3 419 873)	
Financial assets held to maturity		1 636 459	1 636 459
Fixed assets	26 583		26 583
Other assets	645 582	(603 710)	41 872
Total assets	**16 395 790**	**731 428**	**17 127 218**
Liabilities			
Fair value financial liabilities through profit or loss		2 596 439	2 596 439
Hedging derivatives		545 453	545 453
Amounts owed to credit institutions and to customers	68 263	2 610	70 873
Debt securities	11 776 777	380 039	12 156 816
Other liabilities	2 835 546	(2 793 014)	42 532
Selective Trust Account (STA)	57 431		57 431
Provision for financial risks	43 302		43 302
Total liabilities	**14 781 319**	**731 527**	**15 512 846**
Shareholders' equity			
Capital			
Subscribed	3 293 570		3 293 570
Uncalled	(2 924 922)		(2 924 922)
Called	368 648		368 648
General reserve	1 124 811	(3)	1 124 808
Profit for the year	121 012		121 012
Unrealised or deferred gains or losses		(96)	(96)
Total shareholders' equity	**1 614 471**	**(99)**	**1 614 372**
Total liabilities	**16 395 790**	**731 428**	**17 127 218**

Restatements and reclassifications in application of IAS 32 and IAS 39

The application of IAS 32 and 39 has a minor impact (-99 thousand euros), on the Bank's shareholders' equity as at 1 January 2005.

Fair value hedge financial instruments

Fair value hedged financial instruments (loans, securities, issues) are revalued at their fair value with respect to the hedged risk, symmetrically to the hedging derivative.

Derecognition of hedging derivatives and revaluation of other financial instruments

Certain hedging operations, particularly certain interest rate swaps and currency interest rate swaps (CIRS), carried out by the Bank in order to diminish the interest rate risk, do not meet the hedging accounting criteria in terms of IAS 39. These transactions have been recorded as fair value financial assets through profit or loss.

In conformity with the provisions of IAS 39 and IFRS 1, hedging swaps of investment securities classified under "securities held to maturity" in IFRS are no longer eligible to qualify as hedging transactions. Consequently, these securities have been classified as available-for-sale financial assets.

Unrealised gains or losses on the securities portfolio

Held-for-sale securities have been classified as "available-for-sale financial assets".

In the case of securities not hedged for interest rate risk, unrealised gains relative to these securities, not recognised under the previous accounting framework, are now recognised and accounted for in the shareholders' equity under "unrealised or deferred gains or losses". Unrealised losses previously recorded in the profit and loss account are also accounted for under "unrealised or deferred gains or losses".

In the case of securities whose interest rate risk is hedged by a derivative, the unrealised gains or losses compensate for the variations of the hedging instrument in the profit and loss account.

Reclassification of fees and premium

Fees and premium concerning financial debts and relative hedging derivatives already recorded in the balance sheet initially under "accrued income and other assets or liabilities", have been reclassified under "financial debts or hedging derivatives".

2.4 Transition of shareholders' equity at 1 January 2005

In thousand euros

	Called capital	Reserves and result	Unrealised or deferred gains/losses	Total shareholders' equity
Shareholders' equity as at 31 December 2003 (in conformity with the previous standards)	**363 735**	**878 991**		**1 242 726**
Appropriation of profit for the 2003 financial year		86 000		86 000
Shareholders' equity as at 1 January 2004 (in conformity with the previous standards)	**363 735**	**964 991**		**1 328 726**
Impact of the adoption of IAS 19 (social commitments)		(4 316)		(4 316)
Impact of the adoption of IAS 16 (fixed assets)		5 890		5 890
Impact of the adoption of IAS 30 and 37 (Fund for General Banking Risks)		144 000		144 000
Impact of the adoption of IFRS standards applied on 1 January 2004		**145 574**		**145 574**
Shareholders' equity as at 1 January 2004 in conformity with IAS/IFRS standards applied in 2004	**363 735**	**1 110 565**		**1 474 300**
Increase during the financial year	4 913	14 246		19 159
Sub-total of movements in relation to member states	**4 913**	**14 246**		**19 159**
Reported profit for financial year 2004		115 166		115 166
Impact of the adoption of IAS 19 on the 2004 profit (social commitments)		5 724		5 724
Impact of the adoption of IAS 16 on the 2004 profit (fixed assets)		122		122
Profit for financial year 2004 in IAS/IFRS standards applied in 2004		**121 012**		**121 012**
Shareholders' equity as at 31 December 2004 in conformity with IAS/IFRS standards applied in 2004	**368 648**	**1 245 823**		**1 614 471**
Impact of the adoption of IAS 39 applied on 1 January 2005		(3)	(96)	(99)
Shareholders' equity as at 1 Januar 2005 in conformity with IAS/IFRS standards applied in 2005 before appropriation of 2004 profit	**368 648**	**1 245 820**	**(96)**	**1 614 372**
Appropriation of profit for the 2004 financial year		(10 000)		(10 000)
Shareholders' equity as at 1 January 2005 in conformity with IAS/IFRS standards applied in 2005 after appropriation of 2004 profit	**368 648**	**1 235 820**	**(96)**	**1 604 372**

The main restatements carried out in application of IFRS standards are presented in the previous notes.

3 - NOTES TO THE 2005 FINANCIAL STATEMENTS

3.1 Notes relative to the balance sheet

Note A - Fair value financial assets and liabilities through profit or loss

As from 1 January 2005, this item shows the value (inclusive of interest) of the Bank's hedging derivatives but whose hedge is not recognised under IAS 39. These operations are composed of interest rate swaps, currency interest rate swaps and FX swaps. The following table shows the notional amount and the market value of these derivatives.

In thousand euros

	31/12/2005 in IFRS 2005		
	Notional	**Positive market value**	**Negative market value**
Interest rate derivatives	150 056	157	(866)
Exchange rate derivatives	432 809	2 007	(4 891)
Revaluation of exchange postitions		382 614	(1 272 532)
Total	**582 865**	**384 778**	**(1 278 289)**

Note B - Hedging derivatives

The following table shows the notional amount and the market value (inclusive of interest) of derivatives used for fair value hedging purposes and whose hedge is in conformity with IAS 39. These operations are composed of interest rate swaps, currency interest rate swaps and FX swaps.

In thousand euros

	31/12/2005 in IFRS 2005		
	Notional	**Positive market value**	**Negative market value**
Interest rate derivatives	4 872 838	289 216	(303 287)
Exchange rate derivatives	12 488 857	579 371	(327 710)
Total	**17 361 695**	**868 587**	**(630 997)**

Note C - Securities portfolio

Under the previous standards, securities were classified according to their destination (held-for-sale or investment). As from 1 January 2005, the Bank designates held-for-sale securities as available-for-sale financial assets, and investment securities as financial assets held to maturity. In application of IAS 39, within the ambit of fair value hedging transactions, the book value (inclusive of interest) of available-for-sale financial assets is adjusted for the profits or losses relative to the hedged risk.

In thousand euros

	31/12/2005 in IFRS 2005		31/12/2004 in IFRS 2004	
	Balance sheet value(*)	***of which unrealised gains or losses***	**Balance sheet value(*)**	***Market value***
Available-for-sale financial assets				
Treasury bills and similar securities	100 429		100 539	
Debt securities and other fixed income securities	1 052 559	14	1 656 585	
Shares and other variable-yield securities	735	211	1 380	
Sub-total	**1 153 723**	**225**	**1 758 504**	**1 757 425**
Fair value adjustment of securities hedged by hedging derivatives	14 456			
Provisions for depreciation			(1 170)	
Total available-for-sale financial assets	**1 168 179**	**225**	**1 757 334**	**1 757 425**
Assets held to maturity				
Treasury bills and similar securities	772 570		703 078	
Debt securities and other fixed income securities	977 832		959 461	
Sub-total	**1 750 402**		**1 662 539**	**1 769 397**
Provisions for depreciation				
Total assets held to maturity	**1 750 402**		**1 662 539**	**1 769 397**
Total securities portfolio	**2 918 581**	**225**	**3 419 873**	**3 526 822**

(*) including interest receivable

Financial assets held to maturity comprise bonds issued by countries or similar institutions holding at least an AA rating at the time of the purchase. None of the securities under these financial assets has been disposed of, or transferred to another category of assets during the last two financial years.

Moreover, none of the securities classified under the categories of financial assets available for sale or held to maturity has been given as guarantee during 2005.

At 31 December 2005, unlisted securities under financial assets available for sale or held to maturity amount to 16.57 million euros.

The amount of net profits transferred to the 2005 profit and loss account after disposals or maturity dates with respect to available-for-sale financial assets amounts to 94 thousand euros.

Transactions with respect to securities during the 2005 financial year are shown below:

In thousand euros

	31/12/2005 IFRS 2005
Available-for-sale financial assets	
At 1 January	1 737 056
Purchase	452 616
Sale or with maturity dates	(1 071 886)
Foreign exchange movements	18 144
Sub-total	**1 135 930**
Fair value adjustment of securities hedged by hedging derivatives	14 456
Interest receivable	17 793
Total available-for-sale financial assets	**1 168 179**
Assets held to maturity	
At 1 January	1 609 642
Purchase	152 058
With maturity dates	(66 304)
Foreign exchange movements	1 086
Sub-total	**1 696 482**
Interest receivable	53 920
Total assets held to maturity	**1 750 402**
Total securities portfolio	**2 918 581**

Note D - Loans and advances to credit institutions and to customers

This heading covers loans and deposits to credit institutions and to customers. As from 1 January 2005 and in application of IAS 39, within the context of fair value hedging transactions, the loan book value includes the profit or loss adjustment relative to the hedged risk.

In thousand euros

Breakdown by category of borrower	31/12/2005 IFRS 2005	31/12/2004 IFRS 2004
Loans to credit institutions		
Loans	7 597 038	7 104 849
Interest receivable	39 764	40 755
Sub-total	**7 636 802**	**7 145 604**
Loans to customers		
Loans	3 885 718	3 659 973
Interest receivable	31 692	30 731
Unpaid receivables		
Provisions		
Sub-total	**3 917 410**	**3 690 704**
Value adjustment of loans hedged by derivatives	159 516	
Total loans	**11 713 728**	**10 836 308**
Other loans and advances		
Advances repayable on demand	8 147	9 010
Advances with agreed maturity dates or periods of notice	1 723 098	1 455 724
Sub-total	**1 731 245**	**1 464 734**
Interest receivable	3 445	2 661
Total other advances	**1 734 690**	**1 467 395**

At 31 December 2005, outstanding subsidised loans benefiting from the Selective Trust Account amounted to 490 875 thousand euros (2004: 422 157 thousand euros).

Loans are guaranteed up to the amount of 1 784 518 thousand euros (2004: 1 212 298 thousand euros). These guarantees could be either in the form of securities or financial commitments.

Loan disbursements and reimbursements during the 2005 financial year are indicated below:

In thousand euros

	31/12/2005 IFRS 2005	31/12/2004 IFRS 2004
At 1 January	10 764 822	9 902 568
Disbursements	1 558 535	1 529 938
Reimbursements	(969 749)	(649 017)
Foreign exchange movements	129 147	(50 923)
Provision release		32 256
At 31 December	**11 482 755**	**10 764 822**
Interest receivable	71 457	71 486
Value adjustment of loans hedged by derivatives	159 516	
Total	**11 713 728**	**10 836 308**

Breakdown of outstanding loans and financing commitments by borrower country as at 31 December 2005:

In thousand euros

	Outstanding				Financing commitments	
Breakdown by country	IFRS 2005	%	IFRS 2004	%	IFRS 2005	IFRS 2004
Spain	2 167 511	18.88	2 002 235	18.60	182 607	166 582
Italy [1]	1 337 017	11.64	1 241 409	11.53	160 000	181 200
Germany [2]	1 272 979	11.09	1 460 503	13.57	213 750	104 417
France	1 097 332	9.55	1 142 601	10.61		
Turkey	791 361	6.89	635 905	5.91	138 926	280 327
Poland	613 651	5.34	481 277	4.47	116 387	143 129
Greece	577 821	5.03	667 424	6.20	57 947	84 208
Finland	550 004	4.79	438 942	4.08	97 500	15 000
Portugal	540 571	4.71	521 281	4.84	17 334	39 834
Hungary	523 802	4.56	390 625	3.63	313 183	277 688
Cyprus	447 728	3.90	464 031	4.31	292 714	306 223
Romania	234 806	2.04	186 205	1.73	113 000	86 353
Belgium	227 972	1.99	270 614	2.51		
Denmark	190 000	1.65	100 000	0.93		
Sweden	163 058	1.42	110 251	1.02		55 398
Croatia	155 864	1.36	116 574	1.08	97 048	111 941
Norway	128 788	1.12	128 788	1.20	125 235	121 411
Malta	120 170	1.05	120 819	1.12	79 503	78 588
Bulgaria	55 076	0.48	48 929	0.45	16 175	16 308
Slovenia	54 496	0.47	31 773	0.30		20 000
Ireland [3]	50 000	0.44	50 000	0.46	50 000	50 000
Slovak Republic	39 118	0.34	32 409	0.30	7 107	14 257
Iceland	33 942	0.30	30 528	0.28	27 956	30 259
Serbia and Montenegro	21 084	0.18	24 598	0.23		
Lithuania	19 146	0.17	15 313	0.14	7 853	9 586
Latvia	17 150	0.15	15 561	0.14	100 000	500
"the former Yugoslav Republic of Macedonia"	16 785	0.15	16 913	0.16	13 200	3 200
Czech Republic	11 386	0.10			28 000	
Albania	9 602	0.08	2 953	0.03	19 408	1 203
Estonia	8 145	0.07	8 343	0.08	2 046	2 046
Bosnia and Herzegovina	4 182	0.04	5 694	0.05	8 000	
San Marino	2 208	0.02	2 324	0.02		
Moldova					6 000	
Total	**11 482 755**	**100.00**	**10 764 822**	**100.00**	**2 290 879**	**2 199 658**

(1) of which 169 000 thousand euros outstanding in favour of Central and Eastern European countries as at 31 December 2005 (31 December 2004: 70 000 thousand euros)

(2) of which 209 133 thousand euros outstanding in favour of Central and Eastern European countries as at 31 December 2005 (31 December 2004: 178 139 thousand euros)

(3) of which 25 000 thousand euros outstanding in favour of Central and Eastern European countries as at 31 December 2005 (31 December 2004: 25 000 thousand euros)

Loans outstanding and financing commitments benefiting from the Selective Trust Account included in the table above are presented under Note H.

In thousand euros

Breakdown by sector-based activities	Outstanding				Financing commitments	
	IFRS 2005	%	IFRS 2004	%	IFRS 2005	IFRS 2004
Strengthening social integration						
Aid to refugees, migrants and displaced populations	296 457		143 974		183 677	44 997
Social housing	2 327 937		2 189 648		90 514	83 515
Job creation and preservation in SMEs, and vocational training	1 703 639		1 601 336		256 540	353 846
Urban and rural modernisation	1 152 230		999 882		292 590	291 838
Sub-total	**5 480 263**	**48**	**4 934 840**	**46**	**823 321**	**774 196**
Managing the environment						
Natural or ecological disasters and preventive actions	1 626 007		1 611 970		276 443	320 378
Protection of the environment	1 406 077		1 345 697		391 701	239 285
Protection of historic and cultural heritage	176 177		132 102		92 333	117 460
Infrastructure	90 374		116 747			
Sub-total	**3 298 635**	**29**	**3 206 516**	**30**	**760 477**	**677 123**
Developing human capital						
Education	1 362 927		1 363 275		457 984	484 066
Health	1 340 930		1 260 191		249 097	264 273
Sub-total	**2 703 857**	**23**	**2 623 466**	**24**	**707 081**	**748 339**
Total	**11 482 755**	**100**	**10 764 822**	**100**	**2 290 879**	**2 199 658**

Financing commitments

Financing commitments comprise projects for which a framework agreement has been signed, or projects which have been granted at least one financing.

In thousand euros

Breakdown by year of approval	2003 and before	2004	2005	Total
Projects				
With signed framework loan agreements	692 636	540 548	836 671	**2 069 855**
With at least one financing	206 829	14 195		**221 024**
Total	**899 465**	**554 743**	**836 671**	**2 290 879**

Note E - Tangible and intangible fixed assets

In thousand euros

	Land	Buildings	Fixtures and equipment	Other	Intangible assets	Total
Gross book value						
At 1 January 2005	11 321	9 057	10 449	4 522	3 308	**38 657**
Additions	1 725	1 380	737	753	369	**4 964**
Disposals				(43)		**(43)**
Other movements			(104)	(317)	(180)	**(601)**
At 31 December 2005	**13 046**	**10 437**	**11 082**	**4 915**	**3 497**	**42 977**
Depreciation						
At 1 January 2005			(6 178)	(3 149)	(2 747)	**(12 074)**
Charge for the year			(809)	(648)	(238)	**(1 695)**
Disposals				43		**43**
At 31 December 2005			**(6 987)**	**(3 754)**	**(2 985)**	**(13 726)**
Net book value						
At 31 December 2005	**13 046**	**10 437**	**4 095**	**1 161**	**512**	**29 251**
At 31 December 2004	11 321	10 099	3 230	1 372	561	26 583

Note F - Other assets and other liabilities

In thousand euros

	31/12/2005 IFRS 2005	31/12/2004 IFRS 2004
Subscribed, called and unpaid capital and reserves to be paid(*)	10 715	16 073
Other accrued income and sundry debtors	10 341	20 806
Sundry debtors	2 950	3 759
Prepaid expenses	1 072	59 788
Accrued interest receivable	86	469 017
Other expenses to be amortised		76 139
Total other assets	**25 164**	**645 582**
Deposits of guarantees received	140 462	23 804
Other accruals and sundry creditors	14 594	18 729
Foreign currencies adjustment account		2 478 344
Accrued expenses		181 296
Deferred income		133 373
Total other liabilities	**155 056**	**2 835 546**

(*) See detail under Note J

The balance of the foreign currencies adjustment account at 31 December 2004 (IFRS 2004) represents exchange unrealised losses on currency swaps maturity flows.

Note G - Amounts owed to credit institutions, to customers and debt securities

In thousand euros

	31/12/2005 in IFRS 2005	31/12/2004 in IFRS 2004
Amounts owed to credit institutions		
Issues		1 101
Interest payable		1
Total amounts owed to credit institutions		**1 102**
Amounts owed to customers		
Interest bearing accounts	40 760	30 829
of which European Community	*39 371*	*29 626*
Issues	35 997	35 804
Interest payable	531	528
Value adjustment of issues hedged by derivatives	1 796	
Total amounts owed to customers	**79 084**	**67 161**
Debt securities		
Bonds	12 699 967	11 209 681
Euro Commercial paper	335 955	
Perpetual debt	130 889	131 924
Interest payable	468 156	435 172
Value adjustment of securities hedged by derivatives	89 870	
Total debt securities	**13 724 837**	**11 776 777**

Development of customers' interest-bearing accounts

The Bank opened interest-bearing accounts funded by contributions from the European Community:

- Five accounts to receive the European Community contributions ("Contribution Arrangement in respect of a SME Finance Facility Phase 2 Special Fund") for partial financing of productive investment projects designed to create or safeguard jobs in SMEs located in transition countries.

  - In 2001, setting-up of "EC-Contribution Fund Phare Account"
  - In 2002, contribution to Turkey "EC-Contribution Fund MEDA Account"
  - In 2004, increase "SME Finance Facility (SMEFF) 2002 Special Account"
  - In 2004, contribution to Cyprus "SME Finance Facility (SMEFF) Cyprus Special Account"
  - In 2005, increase "SME Finance Facility (SMEFF) 2003 Special Account"

At 31 December 2005, the balance of these accounts amounts to 24 361 thousand euros.

- Two accounts to partially finance local infrastructural projects in favour of the municipalities of six Central and Eastern European countries, also applicant countries at the time of the project (Czech Republic, Estonia, Latvia, Lithuania, Poland and Slovak Republic), within the ambit of the EU Programme "EU Municipal Finance Facility".

  - In 2004, setting-up of "EU Municipal Finance Facility Special Account"
  - In 2005, increase with respect to geographical extension to the programme "EU Municipal Finance Facility 2003 Special Account"

At 31 December 2005, the balance of these accounts amounts to 13 012 thousand euros.

- An account for the partial financing of productive investment projects of small and medium-sized enterprises and in particular micro-enterprises, known as the "Preparatory Action Programme" aimed at creating or safeguarding jobs, in eight new EU member states in Central and Eastern Europe.

  - In 2005, setting-up of "Preparatory Action Special Account 04"

The balance of this account amounts to 1 998 thousand euros as at 31 December 2005.

Contributions made by member states are transferred to the following funds:

- In 2001, an account to receive the Finnish government's contributions for the financing of technical assistance within the ambit of projects in Estonia, Latvia and Lithuania
- In 2004, the Swiss government effected a payment for the setting-up of a fund for the education of the Roma community

These two funds were closed in 2005, and corresponding funds were disbursed in favour of the Roma Education Fund.

- In 2004, an account to receive the Norwegian government's contributions for the financing of technical assistance within the ambit of projects in support of economic and social reforms in the western Balkans.

Debt securities

Debt transactions carried out during the 2005 and 2004 financial years are indicated hereunder:

In thousand euros

	31/12/2005 in IFRS 2005	31/12/2004 in IFRS 2004
At 1 January	11 341 605	10 456 627
New issues	3 049 732	1 831 762
Maturities	(2 479 554)	(441 267)
Repurchases	(13 316)	(16 484)
Foreign exchange movements	1 268 344	(489 033)
At 31 December	**13 166 811**	**11 341 605**
Interest payable	468 156	435 172
Value adjustment of issues hedged by derivatives	89 870	
Total	**13 724 837**	**11 776 777**

The table below shows the outstanding debt securities after breakdown of currency swaps:

In thousand euros

Breakdown by currency	Outstanding	Currency swap	Net value 2005	Net value 2004
Euro	1 393 074	11 547 478	12 940 552	13 031 183
US Dollar	9 837 316	(8 861 119)	976 197	707 285
Swiss Franc	259 498	(128 609)	130 889	131 924
Japanese Yen	256 123	(210 767)	45 356	45 113
Taiwan Dollar	258 372	(258 372)		
Australian Dollar	682 848	(682 848)		
Pound sterling	218 882	(218 882)		
Canadian Dollar	109 290	(109 290)		
South African Rand	120 009	(120 009)		
Turkey New Lira	31 399	(31 399)		
Total	**13 166 811**	**926 183**	**14 092 994**	**13 915 505**

Note H - Selective Trust Account (STA)

1 - General operating principle

Interest rate subsidies and granting of donations are the basis of the underlying operating principle of this account. Within the framework of the Bank's financing of high social value projects, the Selective Trust Account covers the interest rate differential between the rate usually applied by the Bank and the rate proposed to the borrower. Any proposal for an interest rate subsidy is specified in the loan application submitted by the Governor to the Administrative Council for approval.

2 - Funding

The STA is supplied, although not automatically, with grants received from the Bank's member states through dividends of a social nature allocated at the time of the Bank's appropriation of annual profits.

Voluntary contributions from member states of the Bank and the Council of Europe are also recorded on the credit side of the STA.

The Bank remunerates the STA funds in conformity with the provisions of Resolution 1437 (1999) as revised in 2001.

3 - Accounting within the framework of IAS/IFRS standards

The STA is divided into two sub-accounts:

- Member states sub-account recording the amount of available funds: contributions received from member states as well as interest on the STA's funds are recorded on the credit side; donations granted and total interest rate subsidies granted on the day of payment of every loan concerned are recorded on the debit side.

- Subsidised projects sub-account recording interest rate subsidies: the amount of interest rate subsidies recorded under credit in the Bank's profit and loss account is recorded on the debit side simultaneously with interest payments made by the borrower; interest rate subsidies granted on the day of disbursement of the subsidised loan are recorded on the credit side.

In thousand euros

1) Member states sub-account	Debit	Credit
Sub-account balance as at 1 January 2004		**40 612**
Payment by member states for the financial year 2003		895
Resale of securities guaranteeing a subsidised loan		3 225
Credit interest paid into the STA		1 088
Subsidies on disbursed loans	2 920	
Donations granted	816	
Sub-account balance as at 31 December 2004 [a]		**42 084**
Payment by member states for the financial year 2004		10 000
Credit interest paid into the STA		1 317
Subsidies on disbursed loans	4 356	
Donations granted	1 279	
Sub-account balance as at 31 December 2005 [b]		**47 766**
2) Subsidised projects sub-account		
Sub-account balance at 31 December 2004 [c]		**15 347**
Sub-account balance at 31 December 2005 [d]		**16 974**
STA balance as at 31 December 2004 [a] + [c]		**57 431**
STA balance as at 31 December 2005 [b] + [d]		**64 740**

Donations

Since it was set up in 1995, donations for a total amount of 10.4 million euros have been granted from the STA.

The following is the breakdown of donations granted during the last two financial years:

In thousand euros

Payments	2005	2004
Roma Education Fund: CEB's contribution to the implementation of the Fund	500	
Serbia and Montenegro (UNHCR): help for refugees having opted for local integration in Serbia	420	572
Bosnia and Herzegovina (UNHCR): provision of permanent housing for displaced persons	420	244
Estonia: creation of the Sillamäe Rehabilitation Centre	150	
Moldova (UNICEF): creation of the Mother and Child Temporary Placement Centre in Balti	78	
Joint programme CEB/Council of Europe - Reimbursement of an unused balance	(289)	
Total	**1 279**	**816**

Loans outstanding and financing commitments by country with STA interest rate subsidies

In thousand euros

	Outstanding		Financing commitments	
Breakdown by country	2005	2004	2005	2004
Croatia	142 813	109 688	49 137	81 485
Hungary	136 300	124 800	197 968	218 006
Poland	93 160	96 977		
Romania	53 800	39 000	77 400	31 000
Slovak Republic	30 000	26 714		3 286
Bulgaria	9 269	6 294	13 675	16 308
Albania	8 142	2 423	18 952	74
Lithuania	6 658	5 394	5 068	6 517
Slovenia	6 168	6 734		
Bosnia and Herzegovina	4 182	3 622	8 000	
Germany	383	511		1 917
Moldova			6 000	
Total	**490 875**	**422 157**	**376 200**	**358 593**

These loans outstanding are included in the Bank's loan portfolio (Note D).

Note I - Provision for financial risks

The Bank set up the following provisions for financial risks with respect to its social commitments:

In thousand euros

	31/12/2005 IFRS 2005	31/12/2004 IFRS 2004
Provision for pension commitments	38 424	34 470
Provision for other post-employment benefits	10 185	8 832
Total	**48 609**	**43 302**

The Bank administers a pension scheme. It also provides for certain related benefits (particularly medical insurance) in favour of its retired staff. The cost of benefits in relation to the different social staff entitlements is determined separately, in accordance with the actuarial valuation using the projected unit credit method. The last actuarial valuation was carried out on 30 June 2005 and projected as at 31 December 2005.

Pension scheme

The following is the pension scheme financial situation:

In thousand euros

	31/12/2005 IFRS 2005	31/12/2004 IFRS 2004
Financial situation as at 31 December		
Actuarial liability	(46 201)	(34 321)
Actuarial surplus / (deficit)	(46 201)	(34 321)
Stock of unrealised actuarial gains / (losses)	7 777	(149)
Provision as at 31 December	**(38 424)**	**(34 470)**
Provision development as at 31 December		
Provision as at 1 January	**(34 470)**	**(30 462)**
Book charge for the year [(1)]	(4 976)	(4 657)
Benefits paid	1 022	649
Provision as at 31 December	**(38 424)**	**(34 470)**

(1) The book charge is divided into 3 195 thousand euros for the cost of services rendered and 1 781 thousand euros with respect to the financial cost (3 075 thousand euros and 1 582 thousand euros for 2004 respectively).

Other information	2005	2004
Interest rate	4.50%	5.25%
Inflation rate	1.75%	1.75%
Pension revaluation rate	1.75%	1.75%
Salary increase rate	5.00%	5.00%
Staff average number of residual working years as at 31 December	15	16

Pension scheme-related commitments

The following is the financial situation with respect to pension scheme-related commitments:

In thousand euros

	31/12/2005 in IFRS 2005	31/12/2004 in IFRS 2004
Pension scheme financial situation as at 31 December		
Actuarial liability	(9 337)	(8 846)
Actuarial surplus / (deficit)	(9 337)	(8 846)
Stock of unrealised actuarial (gains) / losses	(848)	14
(Provision) / Surplus as at 31 December	**(10 185)**	**(8 832)**
Provision development as at 31 December		
(Provision) / Surplus as at 1 January	**(8 832)**	**(7 576)**
Book charge for the year [1]	(1 451)	(1 335)
Benefits paid	98	79
(Provision) / Surplus as at 31 December	**(10 185)**	**(8 832)**

(1) The book charge is divided into 989 thousand euros with respect to services rendered and 462 thousand euros for financial costs (940 thousand euros and 395 thousand euros for 2004 respectively).

The economic assumptions with respect to related commitments are similar to those within the ambit of the pension scheme. Moreover, the rate of the increase in contributions is of 7.50% up to 2010 and 6.00% thereafter.

Note J - Subscribed capital

The capital is composed of participating certificates of 1 000 euros. Each participating certificate represents one vote. All member states of the Council of Europe or other states, upon authorisation by the Governing Board, may subscribe to the capital. This subscription is effective upon acceptance of the Articles of Agreement. Earnings per participating certificate for 2005 amount to 8 853.93 euros.

In thousand euros

Members	Subscribed capital	Uncalled capital	Called capital
Germany	549 692	489 000	60 692
France	549 692	489 000	60 692
Italy	549 692	489 000	60 692
Spain	358 504	318 922	39 582
Turkey	233 077	207 344	25 733
Netherlands	119 338	106 161	13 177
Belgium	98 634	87 746	10 888
Greece	98 634	87 746	10 888
Portugal	83 538	74 315	9 223
Sweden	83 538	74 315	9 223
Poland	76 988	68 488	8 500
Switzerland	53 824	43 229	10 595
Denmark	53 823	47 879	5 944
Finland	41 889	37 264	4 625
Norway	41 889	37 264	4 625
Bulgaria	37 491	33 352	4 139
Romania	35 963	31 993	3 970
Ireland	28 998	25 797	3 201
Hungary	26 884	23 916	2 968
Czech Republic	25 833	22 981	2 852
Luxembourg	20 849	18 547	2 302
Serbia and Montenegro	15 511	13 799	1 712
Croatia	12 831	11 414	1 417
Cyprus	11 934	10 617	1 317
Slovak Republic	11 380	10 123	1 257
Albania	8 034	7 147	887
Latvia	7 688	6 840	848
Estonia	7 637	6 794	843
"the former Yugoslav Republic of Macedonia"	7 637	6 794	843
Lithuania	7 556	6 722	834
Slovenia	7 380	6 565	815
Iceland	6 089	5 417	672
Malta	6 089	5 417	672
Bosnia and Herzegovina	5 816	5 174	642
Moldova	3 294	2 930	364
Liechtenstein	2 921	2 374	547
San Marino	2 921	2 478	443
Holy See	82	58	24
TOTAL 2005	**3 293 570**	**2 924 922**	**368 648**
TOTAL 2004	**3 293 570**	**2 924 922**	**368 648**

Subscribed, called and unpaid capital as well as reserves to be paid are detailed below:

Members	Capital	Reserves	Total
Ireland	1 601	4 949	6 550
Serbia and Montenegro	856	2 174	3 030
Bosnia and Herzegovina	321	815	1 136
TOTAL	**2 778**	**7 938**	**10 716**

3.2 Notes relative to the profit and loss account

Note K - Interest margin

Within the framework of IFRS 2005, under this heading the Bank includes the remuneration determined in accordance with the effective interest rate method (interest, commissions and expenses). Income and interest charges on fair value hedging derivatives are shown alongside the income derived from items to which they are providing risk hedging.

In thousand euros

	31/12/2005 in IFRS 2005	31/12/2004 in IFRS 2004
Available-for-sale financial assets [1]		
Securities transactions	40 370	50 322
Hedging derivatives	(10 051)	(13 689)
Sub-total	**30 319**	**36 633**
Loans and advances to credit institutions and to customers		
Loans (exclusive of interbanking)	356 022	343 025
Other loans and advances [1]	38 828	26 201
Hedging derivatives	(95 064)	(101 486)
Sub-total	**299 786**	**267 740**
Financial assets held to maturity		
Securities transactions	84 038	85 187
Hedging derivatives		(2 175)
Sub-total	**84 038**	**83 012**
Amounts owed to credit institutions and to customers		
Issues	(1 224)	(1 197)
Interest-bearing accounts	(3 856)	(2 042)
Hedging derivatives	(444)	443
Sub-total [2]	**(5 524)**	**(2 796)**
Debt securities		
Issues	(581 951)	(570 013)
Hedging derivatives	289 693	293 930
Sub-total [2]	**(292 258)**	**(276 083)**
Macro-hedging derivatives [2]		8 433
Interest margin	**116 361**	**116 939**

(1) In 2004, these headings were presented under "Treasury assets".
(2) In 2004, these headings were presented under "Interest expenses and similar charges".

The following is the breakdown of interest received on loans relative to the financial year:

In thousand euros

Breakdown by country	2005	2004
Spain	48 689	45 869
Germany	48 242	49 452
Turkey	43 494	44 243
Italy	32 364	30 985
Greece	31 256	36 419
France	29 809	34 313
Poland	26 037	24 240
Cyprus	14 904	14 732
Finland	13 888	12 439
Hungary	12 648	8 447
Portugal	11 608	6 964
Belgium	7 337	6 941
Romania	6 731	3 383
Croatia	6 277	5 176
Malta	5 747	5 928
Norway	2 695	2 644
Sweden	2 686	2 249
Denmark	2 044	1 256
Slovenia	1 774	1 232
Bulgaria	1 486	958
Ireland	1 077	212
Slovak Republic	988	892
Serbia and Montenegro	834	1 037
Lithuania	773	716
Iceland	706	717
Latvia	506	292
"the former Yugoslav Republic of Macedonia"	477	407
Estonia	399	406
Bosnia and Herzegovina	303	290
San Marino	114	117
Czech Republic	83	
Albania	46	69
Total	**356 022**	**343 025**

Note L - Net profits on fair value financial instruments through profit or loss

As from 1 January 2005, this heading covers profits relative to the Bank's hedging derivatives whose hedging is not recognised under IAS 39, as well as realised and unrealised exchange profits. Income and interest charges in relation to these derivatives are presented under "interest margin" (Note K).

In thousand euros

	31/12/05
Derivatives	1 364
Revaluation of exchange positions	212
Total	**1 576**

Note M - General operating expenses

In thousand euros

	2005	2004
Staff costs		
Wages and salaries	13 349	12 981
Social Security and pension costs [1]	6 617	6 110
Other general operating expenses	7 908	7 363
Total	**27 874**	**26 454**

(1) The impact on social security and pension costs resulting from the application of IAS 19 amounts to 4.0 million euros in 2005 (2004: 3.8 million euros).

At 31 December 2005, the Bank's staff was composed of 139 agents: 4 appointed officials (Governor, Vice-Governor Delegate and Vice-Governors) and 135 professional staff.

At 31 December 2004, the Bank's staff was composed of 133 agents: 4 appointed officials (Governor, Vice-Governor Delegate and Vice-Governors) and 129 professional staff.

Note N - Risk cost

The risk cost covers nety charges constitued with respect to credit risk relative to the Bank's loan activity:

In thousand euros

	2005	2004
Provision releases for risks on loans		32 256
Total provision variations		**32 256**

3.3 Complementary notes

Note O - Currency position

The net exchange rate risks are the result of margins from banking transactions and general operating expenses. Exchange market transactions are conducted so as to minimise these risks.

In thousand euros

Breakdown by currency	Assets	Liabilities	Derivative instruments	**Net position 2005**	**Net position 2004**
Euro	14 221 430	4 421 337	(10 692 331)	(892 238)	(2 477 754)
Swiss Franc	193 744	268 788	74 117	(927)	(1 452)
Pound Sterling	5 409	224 272	218 882	19	52
Other currencies	406 569	1 305 582	899 186	173	153
US Dollar	1 922 371	10 391 673	8 470 316	1 014	267
Japanese Yen	159 891	297 762	139 025	1 154	977
Total	**16 909 414**	**16 909 414**	**(890 805)**	**(890 805)**	**(2 477 757)**

Note P - Liquidity position

The liquidity risk is a measure which defines the projected situation of the Bank's treasury.

The table below provides an analysis of assets and liabilities grouped on the basis of the remaining period between the balance sheet end-date and the operations' contractual maturity date.

Those assets and liabilities that do not have a contractual maturity date are grouped under the column "Undefined".

The valuation of derivatives and operations related thereto is classified under the column "Undefined". In fact, except for the eventual ineffectiveness of the derivative, the balance of these valuations has no impact on the liquidity position.

In thousand euros

	Undefined	Up to 1 month	1 to 3 months	More than 3 months up to 1 year	More than 1 year up to 5 years	More than 5 years	**Total**
ASSETS							
Cash in hand, balances with central banks	65						65
Fair value financial assets through profit or loss	384 778						384 778
Hedging derivatives	868 587						868 587
Available-for-sale financial assets	15 404	3 024	3 128	169 232	805 874	171 517	1 168 179
Loans and advances to credit institutions and to customers	159 516	1 139 738	772 475	775 117	6 158 971	4 442 601	13 448 418
Financial assets held to maturity		14 158	18 618	20 927	572 496	1 124 203	1 750 402
Fixed assets	29 251						29 251
Other assets	25 164						25 164
Total assets	**1 482 765**	**1 156 920**	**794 221**	**965 276**	**7 537 341**	**5 738 321**	**17 674 844**
LIABILITIES							
Fair value financial liabilities through profit or loss	1 278 289						1 278 289
Hedging derivatives	630 997						630 997
Amounts owed to credit institutions and to customers	1 796	40 760			36 528		79 084
Debt securities	89 869	294 757	273 292	593 915	7 181 415	5 291 589	13 724 837
Other liabilities	155 056						155 056
Selective Trust Account (STA)	64 740						64 740
Provision for financial risks	48 609						48 609
Shareholders' equity	1 693 232						1 693 232
Total liabilities	**3 962 588**	**335 517**	**273 292**	**593 915**	**7 217 943**	**5 291 589**	**17 674 844**
Liquidity position 2005	**(2 479 823)**	**821 403**	**520 929**	**371 361**	**319 398**	**446 732**	
Liquidity position 2004	(3 877 838)	392 126	539 923	(376 953)	1 674 704	(829 719)	

Note Q - Market value of financial instruments accounted for at the amortised cost

The given information is an estimate which is based on Bank's own valuation models.

It represents the day value as at 31 December 2005.

In thousand euros

	31/12/2005 in IFRS 2005	
	Balance sheet value	***Market value***
Financial assets		
Loans and advances to credit institutions and to customers	11 713 728	11 787 470
Financial assets held to maturity	1 750 402	1 928 804
Financial liabilities		
Amounts owed to credit institutions and to customers	79 084	78 820
Debt securities	13 724 837	13 395 784

Note R - Notional of derivatives

In thousand euros

	31/12/2005 IFRS 2005	**31/12/2004 IFRS 2004**
Type of instruments:		
Currency interest rate swaps	12 823 034	12 329 145
Interest rate swaps	5 022 894	6 102 806
FX swaps	98 632	102 442
Total	**17 944 560**	**18 534 393**
Hedging instruments recognised under IAS 39 (1)	17 361 695	
Hedging instruments not recognised under IAS 39 (2)	582 865	
Total	**17 944 560**	

(1) See detail under Note A
(2) See detail under Note B

Note S - Risk management policy and hedging activity

1 - CENTRAL ORGANISATION FRAMEWORK

1.1 Dedicated departments

The **Risk Management Department** identifies, assesses and manages all the risks inherent in the Bank's operations, as a result of both on- and off-balance sheet transactions. For each new loan, the department analyses the transaction, taking into account the standing of the counterparty, the transactions already in progress with it and the country risk, and, if necessary, recommends obtaining guarantees/credit enhancement. The department also keeps constant watch on the application of portfolio management rules (loans, securities, derivatives) and monitors the Bank's situation with regard to large exposures.

The **ALM Department** monitors market risk on a regular basis (interest rate risk, currency risk) and liquidity risk incurred by the Bank. Its conclusions are presented in a quarterly report submitted to the ALM Committee. This report analyses, through a number of stress tests, various scenarios of interest rate variations and their impact on the Bank's profitability as well as the projected liquidity situation based on various borrower default assumptions. It reports, where applicable, actual or foreseeable cases of limits being exceeded and proposes recommendations to the ALM Committee so as to limit the detected risks.

The **Organisation Department** is in charge of activities designed to protect the Bank from operational risks; it identifies all the events that could cause operating losses; it manages the business continuity plan (updating and tests with retreat to the back-up site) and reviews the internal procedures covering all activities within the scope of operational risks. In concrete terms, the department is implementing the operational risk policy of the Bank and, for this purpose, is establishing a complete map of processes and associated operational risks. Also, various training courses are provided during the year in order to increase security awareness among the personnel.

1.2 Decision-making committees

The **Risk Committee** is the keystone of the Bank's risk management system. Each week, decisions on this matter are taken here (counterparty and country limits, etc.), based on the recommendations made by the Risk Management Department.

The **Assets and Liabilities (ALM) Committee** decides on assets and liabilities management strategy. It takes the necessary decisions with regard to financial risks in light of the ALM report and on the basis of the financial policies approved by the Administrative Council.

The **Funding Committee** decides on borrowing strategy (amounts, currencies, conditions and timing) taking into account the Bank's projected liquidity needs and within the framework of the annual borrowing authorisation set by the Administrative Council.

The **Committee for Operational Risks and Organisation** validates the Bank's security policy and takes decisions relating to operational risk prevention.

2 - RISK MANAGEMENT AND HEDGING ACTIVITY

Within the context of its project and treasury financing activities, the Bank is exposed to three different types of risk: credit risk, market risk and operational risk.

2.1 Credit risk

Credit risk can be defined as the risk of loan losses in the event of counterparty default. The credit risk on the loan portfolio is measured on the basis of a rating system. In accordance with the Basle Committee Recommendations, when a counterparty has various ratings, the second best rating is adopted. In the case of a guarantee with risk transferred to the guarantor, the Bank takes into account the latter's rating. In the absence of a rating, an internal rating is applied.

Loan portfolio

In 2005, loans notional outstanding increased by 6.7% relative to 2004 and stood at € 11.5 billion. Loans rated "investment grade" account for 92.5% of the total portfolio, against 91.6% at end of 2004. The proportion of loans ranked "below investment grade" went down from 8.4% in 2004 to 7.5%. This improvement results from the upgrading of some Central and Eastern Europe countries.

As far as breakdown by nature of counterparties, in 2005, 46.1% of the loans were allocated to financial institutions and 53.9% to states or government administrations.

Credit enhancement

At end of December 2005, the amount of credit enhancement in the loan portfolio ensuring a 100% risk transfer totalled € 1.8 billion (against € 1.6 billion at end of 2004); thereof € 0.3 billion collaterals and € 1.5 billion guarantees.

The overall impact of these types of credit enhancement on risk transfer is presented below.

More specifically, the credit risk mitigation techniques have allowed transferring € 639.8 million from the A/BBB category to the AA/AAA.

	Before guarantee	After guarantee	Variance
AAA/AA	46.1%	51.7%	12.1%
A/BBB	46.0%	40.8%	-11.3%
"Below investment grade"	7.9%	7.5%	-4.6%
Total	**100.0%**	**100.0%**	

Bond portfolios

The Bank manages two categories of bond portfolios: a financial assets portfolio held to maturity and a portfolio of financial assets available-for-sale.

The financial assets portfolio held to maturity consists of euro-denominated plain vanilla fixed-rate bonds with a maximum maturity of 30 years. To be eligible to this portfolio, securities must have a rating of at least AA or Aa2. However, securitised products and other special-purpose vehicles must have an AAA/Aaa rating and not exceed a total limit of € 500 million. The size of the financial assets portfolio held to maturity is limited to the amount of own funds available (paid-in capital, reserves) plus the provision for personnel benefits.

The strategic objective is for these resources to be remunerated by a satisfactory long-term return. This portfolio is accounted for at historical cost. By nature, the securities contained in it can be neither exchanged nor sold, except under exceptional circumstances.

As at 31 December 2005, the total value of financial assets portfolio held to maturity stood at € 1.7 billion.

In practice, the Bank implements an annual purchasing programme under which the cash generated by bonds maturing and the current year's profits are re-invested.

The portfolio of financial assets available-for-sale consists of securities with a maximum maturity of seven years. In order to limit exposure to interest rate risk, securities of maturities greater than one year are floating-rate, through asset swaps where applicable. Short-term instruments, of maturities less than one year, also include Euro Commercial Paper (ECP), as an alternative to bank deposits.

Longer-term securities, of maturities greater than one year, must have an AA or Aa2 rating, and shall not exceed a € 1 billion ceiling. For instruments maturing in less than one year, the prerequisite minimum rating is A-1 or P-1.

As at 31 December 2005, the total value of the portfolio of financial assets available-for-sale maturing in more than one year stood at € 1 billion. Changes in values are recorded in equity, except for securities backed by a derivative, which variations are recognised in profit and loss account. The securities in this portfolio are accounted for at historical cost.

The table below shows the outstanding value exclusive of accrued interest of each of these portfolios at 31 December 2005 classified by rating:

In million euros

	AAA	AA	A	Total
Available-for-sale financial assets	515	587	42	1 144
Financial assets held to maturity	1 435	211	8	1 654
Total	1 950	798	50	2 798

Derivatives

The market risks resulting from loan, financing and investment transactions are systematically hedged by using derivatives, in accordance with the policy adopted by the directing bodies. As an end user, the Bank employs derivatives solely for hedging purposes.

Derivative transactions in any case necessitate prior credit clearance of the issuing counterparty by the Risk Committee and prior signing of a framework agreement (for example, the ISDA Master Agreement). In addition, for transactions with a maturity of over five years, the counterparty must have a minimum AA rating or have signed a CSA (Credit Support Annex) collateralization agreement with the Bank. All swap operations are valued at their net present value and daily monitoring of the positions by counterparty is carried out in order to be able to make a request for additional collateral if needed. The Bank has pursued and extended its active policy of collateral agreement management in order to further reduce the credit risk entailed in the use of derivatives. At today, almost the entire notional value of derivative outstanding is collateralised. Furthermore, 82% of the notional value of loans outstanding and 100% of the value at risk are with counterparties rated AA or above.

Distribution of derivatives according to hedging as at 31 December 2005 is the following: loans 78%, debt 20%, securities 2%.

Large exposure

Large exposure is an aggregate exposure to a single counterparty (or group of counterparties) exceeding 10% of own funds. In this respect, the Bank adopts as the definition of own funds paid-in capital, reserves, profits plus uncalled capital of shareholder countries with an AAA or AA rating (according to Moody's, Standard & Poor's and Fitch Ratings).

In accordance with the Basle Committee Recommendations and European Union Directives, the Bank ensures that no counterparty (or group of counterparties) exceeds the limit of 25% of own funds as defined above, and that the cumulative total of large exposures does not exceed 800% of said own funds.

At the end of 2005, no counterparty exceeded the limit of 25% of the Bank's own funds, and only five counterparties exceeded 10%. The total outstanding exposure to these five counterparties amounts to € 3 billion, i.e. 73.9% of the Bank's own funds, versus a limit of 800%.

2.2 Market risk

Interest rate and currency risks

Market risk includes, in particular, the risk of a loss being incurred as a result of an adverse fluctuation in interest or exchange rates.

The strategy adopted by the directing bodies with regard to interest rate risks is based on systematic hedging of positions, so as to reduce the Bank's interest rate exposure to a minimum.

The Bank uses derivatives to protect itself against interest and currency risks on its lending and borrowing operations. Macro-hedging can also be considered if necessary. Moreover, since the Bank performs no trading operations, there is no credit risk which requires matching with part of its own funds, all in accordance with the Basle Committee Recommendations. In conclusion, the interest rate risk in the Bank's balance sheet is confined to the fixed-rate investment portfolio, matched by all the Bank's own funds.

As regards currency risk, the Bank's strategy is not to take any position and to finance assets and liabilities in a single currency. The residual risk arising from gains and losses in currencies other than the euro is systematically monitored and hedged on a monthly basis. The net open position is limited to the equivalent of € 1 million per currency. As at 31 December 2005, the net open position was next to nil.

Liquidity risk

The projected liquidity situation is covered by a weekly report submitted to the Treasury Committee. This is supplemented by stress tests presented to the ALM Committee, based on borrower default assumptions.

2.3 Operational risk

Operational risk represents the risk of direct or indirect loss resulting from inadequate or failed structures, procedures, people or systems as well as from external events.

By deliberately choosing to operate within the framework of the Basle Committee Recommendations, the Bank has undertaken to assess constantly its operational risks and to put in place the appropriate preventive measures. The Basic Indicator Approach method (BIA) is adopted to calculate the operational risk charge against the Bank's own funds, namely € 17 million as at 31 December 2005.

3 - PRUDENTIAL FRAMEWORK

This new prudential framework, approved by the Bank's Administrative Council in June 2004 took effect as of 1 January 2005.

The Capital Adequacy Ratio

Its enables the default risk to be limited to usable capital.

$$\text{Capital Adequacy Ratio} = \frac{\text{Risk Weighted Loan Portfolio}}{\text{Usable Capital}}$$

- Risk Weighted Loan Portfolio: ∑ [(Capital + Interest) x Default Probability]

- Usable capital: total of paid-in capital and reserves

The absolute limit of the Capital Adequacy Ratio is fixed at 100%. At end 2005, this ratio stood at 17% against 29% at end 2004.

The Risk Asset Coverage Ratio

It is an additional limitation on the volume of loans outstanding. In accordance with the analysis methodology already applied by the rating agencies, it limits the value of the loan portfolio rated below investment grade to the "usable capital" plus uncalled AAA/AA capital.

The ceiling is fixed at 66% or currently € 2.6 billion. At end 2005, this ratio stood at 21.8%, against 24.4% at end 2004.

$$\text{"Risk Asset Coverage Ratio"} = \frac{\text{Loan Portfolio rated "below investment grade"}}{\text{Usable Capital + Uncalled AAA/AA capital}}$$

The Reinforced Liquidity Ratio

The Bank's cash position must not be less than 50% of the net liquidity needs on a three-year horizon, including the additional liquidity needs equal to the risk of default of "below investment grade" counterparties within this timeframe. The Bank's liquidity must not be less than 50% of the net requirements for the next 3 years. At end 2005, the strengthened liquidity ratio stood at 76% against 91.7% at end 2004.

Other Statutory Ratios

Indebtedness ratio sets total debt outstanding against total own funds in the broadest sense. As at 31 December 2005, the ratio stood at 3.11 compared with a maximum limit of 4.

Portfolio ratio sets the total value of the securities portfolio plus cash transactions not evidenced by securities (bank deposits, repos) against the amount of own funds in the broadest sense. As at 31 December 2005, the ratio stood at 0.99 compared with a maximum limit of 1.5.

Note T - Post-balance sheet events

There have been no material post-balance sheet events that would require disclosure or adjustment to these financial statements since the closing of the accounts by the Governor on 23 February, 2006.

EXTERNAL AUDITOR'S REPORT

PRICEWATERHOUSECOOPERS

PricewaterhouseCoopers Audit
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EXTERNAL AUDITOR'S REPORT
ON THE FINANCIAL STATEMENTS
Year ended 31 December, 2005

Council of Europe Development Bank
55, Avenue Kléber
75116 Paris

To the Members of the Governing Board and the Administrative Council,

In compliance with the assignment entrusted to us by the Governing Board, we have audited the accompanying financial statements of the Council of Europe Development Bank for the year ended 31 December, 2005. These financial statements, presented in euros, include a balance sheet, a profit and loss account, a statement of cash flows, a statement of changes in shareholders'equity and notes to the financial statements.

The financial statements are the responsibility of the Governor. Our responsibility is to express an opinion on these financial statements based on our audit.

The financial statements have been prepared for the first time in accordance with International Financial Reporting Standards (IFRS) as adopted for use by the European Union. They include comparative information in respect of financial year 2004 restated in accordance with the same standards, except for IAS 32 and IAS 39 which have only been applied as from 1 January 2005, as authorised by IFRS 1.

We conducted our audit in accordance with the international standards on auditing as prescribed by the International Federation of Accountants (IFAC). These standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by the Governor, as well as evaluating the overall financial statements presentation. We believe that our audit provides a reasonable basis for our opinion.

In our opinion, the financial statements give a true and fair view of the financial position of the Bank at 31 December 2005, and of the results of its operations and cash flows for the year then ended, in accordance with IFRSs as adopted for use by the European Union.

Paris, 23 February, 2006

PricewaterhouseCoopers Audit

Dominique Paul

AUDITING BOARD'S REPORT ON THE BALANCE SHEET AND THE PROFIT AND LOSS ACCOUNT AND THE NOTES TO THE FINANCIAL STATEMENTS FOR 2005

In pursuance of its terms of reference under Article XII of the Articles of Agreement of the Council of Europe Development Bank and Article I of its Rules of Procedure, the Auditing Board met in Paris on four occasions in 2005 and from 20-24 February in order to audit the CEB's balance sheet and profit and loss account and the Notes to the financial statements for the year ended 31 December 2005.

Based on Resolution 343 (2002) of the Governing Board clarified by its decision taken at its meeting of 10 December 2004, following the Administrative Council's recommendation on this issue and on the Auditing Board's previous years' findings, the External Auditor, PricewaterhouseCoopers (Paris), presented his statement and gave, when needed, evidence in detail of the performance of the audit.

The Auditing Board carried out the audit of the CEB for the year 2005 as follows:

- Consulting the Governor, the Vice-Governors, the Directors and other pertinent staff;
- Examining the financial statements of the CEB for the year 2005, including the balance sheet at 31 December 2005, the profit and loss account and the Notes to the financial statements, which had been prepared by the Accounting Department of the CEB and signed by the Governor on 23 February 2006;
- Consulting the Internal Audit Department and examining its reports;
- Consulting the External Auditor of the CEB and examining his interim report and his detailed report for the year 2005;
- Obtaining the opinion signed by the External Auditor on 23 February 2006;
- Obtaining all necessary documents, information and explanations which the Auditing Board deemed necessary. These were readily given by the Governor, the Vice-Governors, the Internal Auditor, the Directors and other pertinent staff.

The Auditing Board certifies, on the basis of the information which was made available to it and to the best of its understanding, that the CEB's balance sheet and profit and loss account including the Notes to the financial statements are in agreement with the books and other records and give a true and fair picture, in all material respects, of the state of the CEB's affairs as at 31 December 2005 and the results of its operations and its cash flows for the year then ended, in accordance with International Financial Reporting Standards (IFRS) set out by EC Regulation N° 1606/2002 of 19 July 2002.

Paris, 24 February 2006

Paul BRÜGGER
Nadejda SANDOLOVA
René H. MELLIGER

EXTRACT FROM THE MINUTES OF THE 241ST MEETING OF THE ADMINISTRATIVE COUNCIL OF THE CEB

Resolution 1494 (2006) **CA/PV 241 (2006)**

Paris, 15 March 2006

The Administrative Council,

Having regard to Article XI, Section 2 of the Bank's Articles of Agreement,
Having regard to the balance sheet, profit and loss account and Notes to the financial statements as at 31 December 2005
Having taken note of the External Auditor's report dated 23 February 2006
Having taken note of the Auditing Board's report dated 24 February 2006
Having taken note of the Governor's Memorandum dated 27 February 2006

1. recommends that the Governing Board approve the balance sheet, the profit and loss account and the Notes to the financial statements as at 31 December 2005
2. discharges the Governor from his responsibility for financial management in respect of the financial year 2005
3. resolves to allocate the net profit for 2005 (+ € 88 539 366) as follows:
   - € 80 539 366 to the General reserve
   - € 8 000 000 as social dividend to fund the Selective Trust Account
4. recommends that the Governing Board approves point 3 above.

EXTRACT FROM THE MINUTES OF THE 182ND MEETING OF THE GOVERNING BOARD OF THE CEB

Resolution 363 (2006) **CD/PV 182 (2006)**

Paris, 24 March 2006

The Governing Board,

Having regard to Article IX, Section 3, paragraph 1, litt.e of the Articles of Agreement
Having regard to the balance sheet, the profit and loss account and the Notes to the financial statements as at 31 December 2005
Having taken note of the certification by the External Auditor, dated 23 February 2006
Having regard to the reports of the Bank's statutory organs viz:
- the Report of the Governor for the financial year 2005
- the Auditing Board's report dated 24 February 2006

Having regard to Resolution 1494 (2006) of the Administrative Council
Having heard the Auditing Board

Decides:
- to approve the Bank's annual report, accounts and other financial statements for 2005
- to discharge the Administrative Council from its responsibility for the financial year 2005
- to endorse point 3 of Resolution 1494 (2006) of the Administrative Council of 15 March 2006, by which the Administrative Council agreed to allocate the net profit for 2005, amounting to € 88 539 366, as follows:
  - € 80 539 366 to the General reserve
  - € 8 000 000 as social dividend to fund the Selective Trust Account.

BALANCE SHEET AS AT 31 DECEMBER 2005 AFTER ALLOCATION OF PROFIT

In thousand euros

	Notes	31/12/05 IFRS 2005	31/12/04 IFRS 2004
Assets			
Cash in hand, balances with central banks		65	49
Fair value financial assets through profit or loss	A	384 778	
Hedging derivatives	B	868 587	
Available-for-sale financial assets	C	1 168 179	
Loans and advances to credit institutions and to customers			
Loans	D	11 713 728	10 836 308
Advances	D	1 734 690	1 467 395
Securities portfolio	C		3 419 873
Financial assets held to maturity	C	1 750 402	
Fixed assets	E	29 251	26 583
Other assets	F	25 164	645 582
Total assets		**17 674 844**	**16 395 790**
Liabilities			
Fair value financial liabilities through profit or loss	A	1 278 289	
Hedging derivatives	B	630 997	
Amounts owed to credit institutions and to customers	G	79 084	68 263
Debt securities	G	13 724 837	11 776 777
Other liabilities	F	155 056	2 835 546
Selective Trust Account (STA)	H	72 740	67 431
Provision for financial risks	I	48 609	43 302
Total liabilities		**15 989 612**	**14 791 319**
Capital	J		
Subscribed		3 293 570	3 293 570
Uncalled		(2 924 922)	(2 924 922)
Called		368 648	368 648
General reserve		1 316 359	1 235 823
Unrealised or deferred gains or losses	C	225	
Total shareholders' equity		**1 685 232**	**1 604 471**
Total liabilities		**17 674 844**	**16 395 790**

NOTES FOR THE READER

Title:
Since its creation in 1956, the Bank has been known successively under three different titles. Since 1 November 1999, it has been known as the CEB - Council of Europe Development Bank.

Member states:
As at 31 December 2005, the Bank had 38 member states: Albania, Belgium, Bosnia and Herzegovina, Bulgaria, Croatia, Cyprus, Czech Republic, Denmark, Estonia, Finland, France, Germany, Greece, Holy See, Hungary, Iceland, Ireland, Italy, Latvia, Liechtenstein, Lithuania, Luxembourg, Malta, Moldova, Netherlands, Norway, Poland, Portugal, Romania, San Marino, Serbia and Montenegro, Slovak Republic, Slovenia, Spain, Sweden, Switzerland, "the former Yugoslav Republic of Macedonia" and Turkey. From 1989 to 1991, a contract of association linked the former Yugoslavia to the Bank as an Associate Member.

Articles of Agreement:
The first Articles of Agreement were adopted by the Committee of Ministers of the Council of Europe on 16 April 1956 under Resolution (56)9. New Articles of Agreement, adopted by the Committee of Ministers on 16 June 1993 under Resolution (93)22, came into force on 18 March 1997 following their ratification by all the member states.

Target group countries:
Albania, Bosnia and Herzegovina, Bulgaria, Croatia, Cyprus, Czech Republic, Estonia, Hungary, Latvia, Lithuania, Malta, Moldova, Poland, Romania, Serbia and Montenegro, Slovak Republic, Slovenia, "the former Yugoslav Republic of Macedonia" and Turkey.

Project approved:
A project which has been submitted to the Administrative Council and approved for funding.

Loan disbursed:
A loan which has actually been paid to the beneficiary.

Loan tranche:
Loans are paid in several tranches, depending on the progress of the work, up to the maximum amount approved by the Administrative Council.

Awaiting financing:
Total amount of signed master agreements to be disbursed and of individual projects (not within master agreements) for which at least one disbursement has already been made.

Selective Trust Account (STA):
A special account set up in 1995 to provide interest rate subsidies for projects that comply with the Bank's priority objectives and have a high social value. The account is fed with allocations from the Bank's profits and voluntary contributions from member states. This account may also be used to make donations, granted by the Administrative Council.

Loans outstanding:
Total amount of loans disbursed and not yet repaid.

Subscribed capital:
Participating certificates issued by the CEB and subscribed by its members.

Called capital:
Total capital paid in and to be paid in.

Uncalled capital:
Difference between the subscribed capital and the called capital.

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