Independent auditor's report
on the consolidated financial statements of
International Investment Bank and its subsidiaries
for 2016

March 2017

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Independent auditor's report

To the Council of the International Investment Bank

Opinion

We have audited the consolidated financial statements of International Investment Bank (the "Bank") and its subsidiaries (the "Group"), which comprise the consolidated statement of financial position as at 31 December 2016, and the consolidated income statement, consolidated statement of comprehensive income, consolidated statement of changes in equity and consolidated statement of cash flows for 2016 , and notes to the consolidated financial statements, including a summary of significant accounting policies.

In our opinion, the accompanying consolidated financial statements present fairly, in all material respects, the financial position of the Group as at 31 December 2016 and its financial performance and its cash flows for 2016 in accordance with International Financial Reporting Standards (IFRSs).

Basis for opinion

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

Key audit matters

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

We have fulfilled the responsibilities described in the *Auditor's responsibilities for the audit of the consolidated financial statements* section of our report, including in relation to these matters. Accordingly, our audit included the performance of procedures designed to respond to our assessment of the risks of material misstatement of the consolidated financial statements. The results of our audit procedures, including the procedures performed to address the matters below, provide the basis for our audit opinion on the accompanying consolidated financial statements.

Provisions for impairment of loans to customers

The assessment of provisions for impairment of loans to customers is a key area of judgement for management of the Group. The identification of impairment and the determination of the recoverable amount are inherently uncertain processes involving significant judgements, various assumptions and factors including the financial standing of borrowers and expected future cash flows. Information on the impairment of loans to customers is included in Note 11, *Loans to customers*, Note 23, *Risk management*, to the consolidated financial statements. The use of different models and assumptions could produce significantly different estimates of impairment of loans to customers. Due to materiality of the loans to customers represented 31% of the total assets and significant judgements the assessment of provisions for impairment was one of the key audit matters.

Our audit procedures included an evaluation of the methodology of the assessment of provisions, testing of inputs, evaluation of the assumptions used by the Group in the calculation of the impairment and the assessment of the adequacy of provisions for loans to customers with individual signs of impairment. We analysed expected future cash flows in respect of significant individually impaired loans to customers.

We also assessed whether the disclosures in the consolidated financial statements about the Group's provision for impairment of loans to customers are compliant with applicable IFRS requirements.

Valuation of the buildings classified to "property and equipment" and "investment property"

The Group's aggregate value of the buildings classified to "property and equipment" and "investment property" was 10% of the total Group's assets. Group's management measured the value the buildings classified to "property and equipment" and "investment property" with involvement of the independent appraiser.

The valuation of the assets utilises unobservable inputs and assumptions. Changes of these inputs and assumptions may have a significant impact on the valuation. The significance and subjectivity of these valuations make them a key audit matter. Information of the valuation of the buildings classified to "property and equipment" and "investment property" is included in Note 12, *Investment property*, Note 13, *Property, equipment and intangible assets*, and Note 24, *Fair value measurements,* to the consolidated financial statements.

Our audit procedures in respect of the buildings classified to "property and equipment" and "investment property" included evaluation of competence and objectivity of the Group's independent appraiser involved, examination of the significant assumptions applied and comparison of inputs used to available market prices and other observable information. We involved our real estate valuation specialists to evaluate the methodology and assumptions used. We also assessed whether the Group's disclosures in relation to the valuation of the buildings classified to "property and equipment" and "investment property", in particular, the sensitivity of fair value to changes to key assumptions, are compliant with applicable IFRS requirements.

Other information included in the Group's Annual Report for 2016

Other information consists of the information included in the Annual Report of International Investment Bank for 2016 other than the consolidated financial statements and our auditor's report thereon. Management is responsible for the other information. The Annual Report of International Investment Bank for 2016 is expected to be made available to us after the date of this auditor's report.

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

In connection with our audit of the consolidated financial statements, our responsibility is to read the other information identified above when it becomes available and, in doing so, consider whether the other information is materially inconsistent with the consolidated financial statements or our knowledge obtained in the audit or otherwise appears to be materially misstated.

Responsibilities of management and Council of the International Investment Bank for the consolidated financial statements

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

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

Council of the International Investment Bank are responsible for overseeing the Group's financial reporting process.

Auditor's responsibilities for the audit of the consolidated financial statements

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

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

- Identify and assess the risks of material misstatement of the consolidated financial statements, whether due to fraud or error, design and perform audit procedures responsive to those risks, and obtain audit evidence that is sufficient and appropriate to provide a basis for our opinion. The risk of not detecting a material misstatement resulting from fraud is higher than for one resulting from error, as fraud may involve collusion, forgery, intentional omissions, misrepresentations, or the override of internal control.
- Obtain an understanding of internal control relevant to the audit in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Group's internal control.
- Evaluate the appropriateness of accounting policies used and the reasonableness of accounting estimates and related disclosures made by management.
- Conclude on the appropriateness of management's use of the going concern basis of accounting and, based on the audit evidence obtained, whether a material uncertainty exists related to events or conditions that may cast significant doubt on the Group's ability to continue as a going concern. If we conclude that a material uncertainty exists, we are required to draw attention in our auditor's report to the related disclosures in the consolidated financial statements or, if such disclosures are inadequate, to modify our opinion. Our conclusions are based on the audit evidence obtained up to the date of our auditor's report. However, future events or conditions may cause the Group to cease to continue as a going concern.
- Evaluate the overall presentation, structure and content of the consolidated financial statements, including the disclosures, and whether the consolidated financial statements represent the underlying transactions and events in a manner that achieves fair presentation.
- Obtain sufficient appropriate audit evidence regarding the financial information of the entities or business activities within the Group to express an opinion on the consolidated financial statements. We are responsible for the direction, supervision and performance of the group audit. We remain solely responsible for our audit opinion.

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

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

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

The partner in charge of the audit resulting in this independent auditor's report is O.V. Youshenkov.

O.V. Youshenkov
Partner
Ernst & Young Vneshaudit LLC

15 March 2017

Details of the audited entity

Name: International Investment Bank
Bank operates on the basis of the Agreement on the Establishment of the International Investment Bank dated 10 July 1970, registered in the UN Secretariat on 1 December 1971 under No 11417.
Address: Russia 107078, Moscow, Mashi Poryvaevoy str., 7.

Details of the auditor

Name: Ernst & Young Vneshaudit LLC
Record made in the State Register of Legal Entities on 4 February 2016, State Registration Number 1167746123478.
Address: Russia 115035, Moscow, Sadovnicheskaya naberezhnaya, 77, building 1.
Ernst & Young Vneshaudit LLC is a member of Self-regulated organization of auditors "Russian Union of auditors" (Association) ("SRO RUA"). Ernst & Young Vneshaudit LLC is included in the control copy of the register of auditors and audit organizations, main registration number 11603050953.

CONSOLIDATED STATEMENT OF FINANCIAL POSITION

As at 31 December 2016

(Thousands of euros)

	Note	*31 December 2016*	*31 December 2015*
Assets			
Cash and cash equivalents	5	93,031	59,519
Deposits with banks and other financial institutions	6	45,337	100,392
Derivative financial assets	7	14,362	1,844
Available-for-sale investment securities	8	170,849	93,031
Available-for-sale investment securities pledged under repurchase agreements	8	98,458	23,028
Held-to-maturity investment securities	9	–	50,034
Held-to-maturity investment securities pledged under repurchase agreements	9	–	73,194
Loans to banks	10	94,367	140,597
Loans to customers	11	269,036	165,742
Investment property	12	21,840	33,819
Property, equipment and intangible assets	13	71,844	66,393
Other assets	14	2,319	1,810
Total assets		**881,443**	**809,403**
Liabilities			
Due to banks and other financial institutions	15	118,925	113,373
Derivative financial liabilities	7	11,623	29,898
Current customer accounts		9,218	7,430
Long-term loans of banks	16	73,349	44,187
Debt securities issued	17	272,528	212,724
Other liabilities	14	5,582	4,088
Total liabilities		**491,225**	**411,700**
Equity	18		
Subscribed capital		1,300,000	1,300,000
Callable capital		(986,947)	(996,947)
Paid-in capital		**313,053**	**303,053**
Revaluation reserve for available-for-sale investment securities		(1,506)	(1,664)
Revaluation reserve for property and equipment		12,945	31,453
Foreign currency translation reserve		(57)	(120)
Retained earnings less net income for the year		64,981	62,925
Net income for the year		802	2,056
Total equity		**390,218**	**397,703**
Total equity and liabilities		**881,443**	**809,403**

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

Alexandru Florescu — Acting Chairman of the Board

Eugeny Atanasov — Head of the Financial Department

15 March 2017

The accompanying notes 1-29 are an integral part of these consolidated financial statements.

CONSOLIDATED INCOME STATEMENT

Year ended 31 December 2016

(Thousands of euros)

	Note	*2016*	*2015*
Interest income	21	32,455	27,132
Interest expenses	21	(27,651)	(17,744)
Net interest income		**4,804**	**9,388**
Allowance for loan impairment	11	(7,557)	(6,166)
Net interest income after allowance for loan impairment		**(2,753)**	**3,222**
Fee and commission income		843	548
Fee and commission expense		(138)	(133)
Net fee and commission income		**705**	**415**
Net gains/(losses) from revaluation of derivative financial instruments		32,330	(6,661)
Net losses from revaluation of hedging instruments		(246)	–
Net gains/(losses) from dealing in foreign currencies and operations with derivatives		9,068	(5,302)
Net (losses)/gains from revaluation of assets and liabilities in foreign currencies		(31,173)	22,983
Net gains from available-for-sale investment securities		10,515	3,204
Income from lease of investment property	12	3,442	5,214
Losses from revaluation of investment property	12	(2,174)	(2,500)
Other income/(expenses)		447	(296)
Net non-interest income		**22,209**	**16,642**
Operating income		**20,161**	**20,279**
Reversal of allowance for impairment of other assets	14	67	89
General and administrative expenses	22	(18,939)	(16,908)
Other operating expenses on banking operations		(487)	(1,404)
Operating expenses		**(19,359)**	**(18,223)**
Net income for the year		**802**	**2,056**

The accompanying notes 1-29 are an integral part of these consolidated financial statements.

CONSOLIDATED STATEMENT OF COMPREHENSIVE INCOME

Year ended 31 December 2016

(Thousands of euros)

	Note	*2016*	*2015*
Net income for the year		**802**	**2,056**
Other comprehensive loss			
Other comprehensive income/(loss) to be reclassified to profit or loss in subsequent periods:			
Change in unrealized revaluation of available-for-sale investment securities	18	158	(665)
Translation differences		63	104
Net other comprehensive income/(loss) to be reclassified to profit or loss in subsequent periods		**221**	**(561)**
Other comprehensive loss not to be reclassified to profit or loss in subsequent periods:			
Revaluation of property and equipment	13	(18,508)	(3,642)
Net other comprehensive loss not to be reclassified to profit or loss in subsequent periods		**(18,508)**	**(3,642)**
Other comprehensive loss		**(18,287)**	**(4,203)**
Total loss for the year		**(17,485)**	**(2,147)**

The accompanying notes 1-29 are an integral part of these consolidated financial statements.

CONSOLIDATED STATEMENT OF CHANGES IN EQUITY

Year ended 31 December 2016

(Thousands of euros)

	Subscribed capital	*Callable capital*	*Revaluation reserve for available-for-sale investment securities*	*Revaluation reserve for property and equipment*	*Foreign currency translation reserve*	*Retained earnings*	*Total equity*
At 31 December 2014	**1,300,000**	**(1,027,382)**	**(999)**	**35,095**	**(224)**	**82,925**	**389,415**
Profit for the year	–	–	–	–	–	2,056	**2,056**
Other comprehensive (loss)/income for the year	–	–	(665)	(3,642)	104	–	**(4,203)**
Total comprehensive (loss)/income	**–**	**–**	**(665)**	**(3,642)**	**104**	**2,056**	**(2,147)**
Contributions to capital (Note 18)	–	30,435	–	–	–	(20,000)	**10,435**
At 31 December 2015	**1,300,000**	**(996,947)**	**(1,664)**	**31,453**	**(120)**	**64,981**	**397,703**
Profit for the year	–	–	–	–	–	802	**802**
Other comprehensive income/(loss) for the year	–	–	158	(18,508)	63	–	**(18,287)**
Total comprehensive income/(loss)	**–**	**–**	**158**	**(18,508)**	**63**	**802**	**(17,485)**
Contributions to capital (Note 18)	–	10,000	–	–	–	–	**10,000**
At 31 December 2016	**1,300,000**	**(986,947)**	**(1,506)**	**12,945**	**(57)**	**65,783**	**390,218**

The accompanying notes 1-29 are an integral part of these consolidated financial statements.

CONSOLIDATED STATEMENT OF CASH FLOWS

Year ended 31 December 2016

(Thousands of euros)

	Note	*2016*	*2015*
Cash flows from operating activities			
Interest, fees and commissions received		24,092	17,498
Interest, fees and commissions paid		(3,364)	(1,497)
Realized gains less losses from dealing in foreign currencies and operations with derivatives		9,079	(5,420)
Cash flows from lease of investment property		3,442	5,214
General and administrative expenses		(16,094)	(15,814)
Other operating expenses on banking operations		(78)	(932)
Cash flows from operating activities before changes in operating assets and liabilities		**17,077**	**(951)**
Net (increase)/decrease in operating assets			
Deposits with banks and other financial institutions		54,498	(76,379)
Loans to banks		47,598	(5,904)
Loans to customers		(118,231)	(61,048)
Other assets		(5)	401
Net increase/(decrease) in operating liabilities			
Due to banks and other financial institutions		1,589	60,572
Current customer accounts		1,481	2,618
Other liabilities		68	135
Net cash flows from operating activities		**4,075**	**(80,556)**
Cash flows from investing activities			
Interest received		11,458	10,805
Purchase of available-for-sale investment securities		(668,584)	(245,442)
Proceeds from sale and redemption of available-for-sale investment securities		618,419	161,597
Proceeds from sale and redemption of held-to-maturity investment securities		30,373	15,268
Investments in investment property		(50)	(33)
Acquisition of property, equipment and intangible assets		(1,754)	(2,764)
Net cash flows from investing activities		**(10,138)**	**(60,569)**
Cash flows from financing activities			
Interest paid		(26,324)	(14,759)
Long-term interbank financing raised		60,000	21,448
Long-term interbank financing repaid		(29,569)	–
Placement of bonds		67,398	184,399
Redemption of bonds		(43,910)	(65,089)
Contributions to capital		10,000	10,435
Net cash flows from financing activities		**37,595**	**136,434**
Effect of exchange rate changes on cash and cash equivalents		1,980	(1,708)
Net increase/(decrease) in cash and cash equivalents		**33,512**	**(6,399)**
Cash and cash equivalents, beginning		**59,519**	**65,918**
Cash and cash equivalents, ending	5	**93,031**	**59,519**

The accompanying notes 1-29 are an integral part of these consolidated financial statements.

(Thousands of euros)

1. Principal activities

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

The Bank is an international institution operating on the basis of the Intergovernmental Agreement on the Establishment of the International Investment Bank (the "Agreement") and the Statutes. The Agreement was ratified by the member countries of the Bank and registered with the Secretariat of the United Nations in December 1971. The Group is primarily engaged in commercial lending for the benefit of national investment projects in the member countries of the Group and for other purposes defined by the Council of the Bank. The Group also performs transactions with securities and foreign currency. The Group operates from its office at 7 Mashi Poryvaevoi St., Moscow, Russia, and the European regional office in Bratislava (Eurovea Central 1, Pribinova 4, Bratislava, 81109, Slovak Republic).

The Group had an average of 230 staff employees during 2016 (2015: 237).

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

The Group continues to expand its operations despite the ongoing market volatility in member countries:

- Hungary re-entered the Bank in 2015 and in 2016 made an ahead-of-schedule final contribution to the Group's equity. As at the end of 2016, Hungary's share in the Bank's paid-in capital was EUR 40 million or 12.78%.
- As a result of the Hungary's re-entering, the respective share of the EU countries in the Bank's paid-in capital grew up to 48.72% exceeding the share of the Russian Federation, which decreased to 47.92%.
- The Banks winds up the introduction of changes to its constituent documents and implementation of the three-level corporate governance structure. The Protocol on Introducing Changes to the Agreement on the Establishment of the International Investment Bank and the Statutes (hereinafter, the "Protocol") signed at the end of 2015 is at the stage of ratification (internal state procedures) by member countries of the Bank. The Protocol will enter into force upon completion of those ratification procedures. As at the end of 2016, the Protocol was ratified by Hungary, Vietnam, Romania, and Russia (4 countries out of 9).
- In December 2016, Fitch Ratings upgraded the rating of the Group to BBB with a stable outlook, for the first time since rating in 2013. Also, the Bank is assigned the following investment grade ratings: Baa1 (stable outlook) by Moody's and A (stable outlook) by Dagong Global Credit Rating. In June 2016, the Bank was assigned the BBB rating (stable outlook) by Standard & Poor's.
- In June 2016, the Group concluded a cooperation agreement on fund raising with the Central Bank of Cuba. The agreement confirms the special status of the International Investment Bank in Cuba, which implies that the Cuban party shall fulfill its liabilities to the IIB under the projects in Cuba financed by the Group.
- The IIB completed a large-scale IT-project to upgrade its core banking system (CBS) – a digital platform to manage, process and protect the Bank's data. A data-processing center was launched in the IIB European Regional Office in Bratislava to ensure security and uninterrupted service of the new CBS.
- In April 2016 the Group signed an agreement with the Ministry of Finance of Slovakia concerning the creation of a Technical Assistance Fund, which will be a new instrument supporting the activities of the IIB in country shareholders. The aim of the Fund is to finance the consulting services and technical assistance rendered, for projects in which the IIB is investing in fulfilling its mission. The countries in scope are Mongolia, Vietnam and Cuba. Within this given scope the Group is undertaking consultation and negotiations with CAF (The Development Bank of Latin America) in order to identify potential projects in which to invest or to finance.

(Thousands of euros)

1. Principal activities (continued)

Member countries of the Group

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

Member countries	***2016, %***	***2015, %***
Russian Federation	47.923	49.505
Republic of Bulgaria	13.481	13.926
Hungary	12.777	9.899
Czech Republic	9.703	10.023
Slovak Republic	6.862	7.088
Romania	5.895	6.089
Republic of Cuba	1.713	1.769
Socialist Republic of Vietnam	1.172	1.211
Mongolia	0.474	0.490
	100.000	**100.000**

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

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

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

Business environment in the member countries

Economic and political development of the Bank's member countries affects the activities of enterprises operating in these countries. Considering this fact, the Bank performs its operations with reference to the regional features of its member countries to ensure overall assessment and control of credit and operational risks.

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

2. Basis of preparation

General

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

Subsidiary

The Bank is a parent company of the Group, which owns CJSC IIB Capital (a 100% subsidiary established in 2012 for the purpose of the acting of the Bank, in particular, for the property trust of the Bank) as at 31 December 2016. The authorized capital of the subsidiary is 44.5 thousand rubles (1.1 thousand of euros at the historical exchange rate at the date of established).

Basis of measurement

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

(Thousands of euros)

2. Basis of preparation (continued)

Preparation and presentation of financial statements

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

Functional and presentation currency

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

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

3. Summary of accounting policies

Changes in accounting policies

The Group has adopted the following amended IFRS which are effective for annual periods beginning on or after 1 January 2016:

Amendments to IAS 1 Disclosure Initiative

The amendments to IAS 1 clarify, rather than significantly change, existing IAS 1 requirements. The amendments clarify:

- The materiality requirements in IAS 1;
- That specific line items in the statements of profit or loss and OCI and the statement of financial position may be disaggregated;
- That entities have flexibility as to the order in which they present the notes to financial statements;
- That the share of OCI of associates and joint ventures accounted for using the equity method must be presented in aggregate as a single line item, and classified between those items that will or will not be subsequently reclassified to profit or loss.

Furthermore, the amendments clarify the requirements that apply when additional subtotals are presented in the statement of financial position and the statements of profit or loss and OCI. These amendments are effective for annual periods beginning on or after 1 January 2016. These amendments do not have any impact on the Group and presentation of other comprehensive income in consolidated financial statements of the Group.

Amendments to IFRS 10, IFRS 12 and IAS 28 Investment Entities: Applying the Consolidation Exception

The amendments address issues that have arisen in applying the investment entities exception under IFRS 10 *Consolidated Financial Statements*. The amendments to IFRS 10 clarify that the exemption from presenting consolidated financial statements applies to a parent entity that is a subsidiary of an investment entity, when the investment entity measures all of its subsidiaries at fair value.

Furthermore, the amendments to IFRS 10 clarify that only a subsidiary of an investment entity that is not an investment entity itself and that provides support services to the investment entity is consolidated. All other subsidiaries of an investment entity are measured at fair value. The amendments to IAS 28 *Investments in Associates and Joint Ventures* allow the investor, when applying the equity method, to retain the fair value measurement applied by the investment entity associate or joint venture to its interests in subsidiaries.

These amendments must be applied retrospectively and are effective for annual periods beginning on or after 1 January 2016. These amendments do not have any impact on the Group as the Group does not apply the consolidation exception.

(Thousands of euros)

3. Summary of accounting policies (continued)

Changes in accounting policies (continued)

Annual improvements 2012-2014 cycle

These improvements are effective for annual periods beginning on or after 1 January 2016. They include, in particular:

IFRS 5 Non-current Assets Held for Sale and Discontinued Operations

Assets (or disposal groups) are generally disposed of either through sale or distribution to owners. The amendment clarifies that changing from one of these disposal methods to the other would not be considered a new plan of disposal, rather it is a continuation of the original plan. There is, therefore, no interruption of the application of the requirements in IFRS 5. This amendment must be applied prospectively.

IFRS 7 Financial Instruments: Disclosures

The amendment clarifies that a servicing contract that includes a fee can constitute continuing involvement in a financial asset. An entity must assess the nature of the fee and the arrangement against the guidance for continuing involvement in IFRS 7 in order to assess whether the disclosures are required. The assessment of which servicing contracts constitute continuing involvement must be done retrospectively. However, the required disclosures would not need to be provided for any period beginning before the annual period in which the entity first applies the amendments.

Foreign currency transactions

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

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

Basis of consolidation

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

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

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

(Thousands of euros)

3. Summary of accounting policies (continued)

Investments in associates

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

Unrealized gains on transactions between Group and its associates are eliminated to the extent of the Group's interest in the associates; unrealized losses are also eliminated unless the transaction provides evidence of an impairment of the asset transferred.

Cash and cash equivalents

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

Fair value measurement

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

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

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

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

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

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

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

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

(Thousands of euros)

3. Summary of accounting policies (continued)

Financial assets

Initial recognition

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

Date of recognition

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

Financial assets at fair value through profit or loss

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

Held-to-maturity investments

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

Loans and receivables

Loans and receivables are non-derivative financial assets with fixed or determinable payments that are not quoted in an active market. They are not entered into with the intention of immediate or short-term resale and are not classified as trading securities or designated as investment securities available-for-sale. Such assets are carried at amortized cost using the effective interest method.

Gains and losses are recognized in profit or loss when the loans and receivables are derecognized or impaired, as well as through the amortization process.

Available-for-sale financial assets

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

Reclassification of financial assets

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

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

(Thousands of euros)

3. Summary of accounting policies (continued)

Financial assets (continued)

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

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

Repurchase and reverse repurchase agreements and securities lending

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

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

Derivative financial instruments

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

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

Hedge accounting

To manage the risks associated with fluctuations in cash flows from receipt and payment of interest, as well as with fluctuations in the fair value of certain items, the Group uses derivative financial instruments. As a result, the Group applies hedge accounting for transactions that meet specified criteria.

At inception of the hedge accounting relationship, the Group formally documents the relationship between the hedged item and the hedging instrument, including the nature of the risk, the risk management objective and strategy for undertaking the hedge and the method that will be used to assess the effectiveness of the hedging relationship at inception and on an ongoing basis.

At each hedge effectiveness assessment date, a hedge relationship must be expected to be highly effective on a prospective basis and demonstrate that it was highly effective (retrospective effectiveness) for the designated period in order to qualify for hedge accounting. A formal assessment is undertaken both at inception and at each month end on an ongoing basis. A hedge is expected to be highly effective if the changes in fair value or cash flows attributable to the hedged risk during the period for which the hedge is designated were offset by the hedging instrument in a range of 80% to 125% during the hedging period.

(Thousands of euros)

3. Summary of accounting policies (continued)

Hedge accounting (continued)

Fair value hedges

For designated and qualifying fair value hedges, the cumulative change in the fair value of a hedging derivative is recognised in the consolidated income statement in Net gains (losses) from revaluation of hedging instruments. Meanwhile, the cumulative change in the fair value of the hedged item attributable to the risk hedged is recorded as part of the carrying value of the hedged item in the consolidated statement of financial position and is also recognised in the consolidated income statement in Net gains (losses) from revaluation of hedging instruments.

If the hedging instrument expires or is sold, terminated or exercised, or where the hedge no longer meets the criteria for hedge accounting, or the Group decides to voluntarily discontinue the hedging relationship, the hedge relationship is discontinued prospectively. When the hedge ceases, the adjustment of the carrying amount of the hedged financial instrument is amortized over the remaining period until date of maturity of the hedged financial instrument. If the hedged item is derecognised, the unamortized amount of the adjustment is recognized in profit or loss.

Cash flow hedges

For designated and qualifying cash flow hedges, the effective portion of the cumulative gain or loss on the hedging instrument is initially recognized in consolidated other comprehensive income and is recorded through other comprehensive income. An ineffective portion of the gain or loss on the hedging instrument is recognized in the consolidated income statement.

When a hedging instrument expires, is sold, terminated, exercised, or when a hedge no longer meets the criteria for hedge accounting, the total amount of income or expense accumulated at that time in equity is transferred from equity and recognized in the consolidated statement of income in the same period or periods during which hedged projected cash flows affect profit or loss. When a forecast transaction is no longer expected, the cumulative gain or loss recognized in equity is immediately transferred to the consolidated income statement.

Borrowings

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

Leases

Operating – Group as lessee

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

Operating – Group as lessor

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

(Thousands of euros)

3. Summary of accounting policies (continued)

Measurement of financial instruments at initial recognition

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

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

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

Offsetting of financial instruments

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

Impairment of financial assets

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

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

Deposits with banks and other financial institutions, long-term loans to banks, trade financing loans, and loans to customers

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

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

(Thousands of euros)

3. Summary of accounting policies (continued)

Impairment of financial assets (continued)

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

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

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

Held-to-maturity financial investments

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

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

Available-for-sale financial investments

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

In the case of equity investments classified as available-for-sale, objective evidence would include a significant or prolonged decline in the fair value of the investment below its acquisition cost.

Where there is evidence of impairment, the cumulative loss – measured as the difference between the acquisition coast and the current fair value, less any impairment loss on that investment previously recognized in the consolidated income statement – is reclassified from other comprehensive income to the consolidated income statement. Impairment losses on equity investments are not reversed through the consolidate income statement; increases in their fair value after impairment are recognized in other comprehensive income.

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

(Thousands of euros)

3. Summary of accounting policies (continued)

Impairment of financial assets (continued)

Renegotiated loans

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

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

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

Derecognition of financial assets and liabilities

Financial assets

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

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

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

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

Financial liabilities

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

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

(Thousands of euros)

3. Summary of accounting policies (continued)

Financial guarantees

In the ordinary course of business, the Group gives financial guarantees, consisting of letters of credit, guarantees and acceptances. Financial guarantees are initially recognised in the consolidated financial statements at fair value, in "Other liabilities", being the premium received. Subsequent to initial recognition, the Group's liability under each guarantee is measured at the higher of the amortised premium and the best estimate of expenditure required to settle any financial obligation arising as a result of the guarantee.

Any increase in the liability relating to financial guarantees is taken to the consolidated statement of profit or loss. The premium received is recognised in profit or loss on a straight-line basis over the life of the guarantee.

Property and equipment

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

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

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

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

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

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

Depreciation of property and equipment (including self-constructed property and equipment) begins when it is available for use and is recognized in the consolidated income statement. Depreciation is calculated on a straight-line basis over the following estimated useful lives:

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

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

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

(Thousands of euros)

3. Summary of accounting policies (continued)

Investment property

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

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

Investment property that is being redeveloped for continuing use as investment property or for which the market has become less active continues to be measured at fair value. Earned rental income is recorded in the consolidated income statement within Income from lease of investment property. Gains and losses resulting from changes in the fair value of investment property are recorded in the consolidated income statement and presented within gains/(losses) from revaluation of investment property.

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

Intangible assets

The useful lives of intangible assets are assessed to be finite and include the value of computer software. Intangible assets acquired are measured on initial recognition at cost. Following initial recognition, intangible assets are carried at cost less any accumulated amortisation and any accumulated impairment losses. Amortisation is calculated using the straight–line method. Intangible assets are tested for impairment if any indication of impairment exists. The amortisation period and the amortisation method for an intangible asset with a indefinite useful life are reviewed at least at each financial year-end. Amortisation is calculated using the straight–line method to write down the cost of intangible assets to their residual values over their estimated useful lives, as follows:

	Years
Automated banking system	20
Other computer software	1-5

Intangible assets with finite lives are amortized over the useful economic lives and assessed for impairment whenever there is an indication that the intangible asset may be impaired. Amortization periods and methods for intangible assets with indefinite useful lives are reviewed at least at each financial year-end.

Assets classified as held for sale

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

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

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

(Thousands of euros)

3. Summary of accounting policies (continued)

Provisions

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

Equity

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

Contingencies

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

Recognition of income and expenses

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

Interest and similar income and expense

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

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

Fee and commission income

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

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

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

- *Other fee and commission income*

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

(Thousands of euros)

3. Summary of accounting policies (continued)

Recognition of income and expenses (continued)

Fee and commission expense

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

Dividend income

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

Assets under trust

Assets under trust management are not reported in consolidate financial statements, as they are not assets of the Group.

Segment reporting

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

Standards issued but not yet effective

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

IFRS 9 Financial Instruments

In July 2014, the IASB issued the final version of IFRS 9 *Financial Instruments* which reflects all phases of the financial instruments project and replaces IAS 39 *Financial Instruments: Recognition and Measurement* and all previous versions of IFRS 9. The standard introduces new requirements for classification and measurement, impairment, and hedge accounting.

From a classification and measurement perspective, the new standard will require all financial assets, except equity instruments and derivatives, to be assessed based on a combination of the entity's business model for managing the assets and the instruments' contractual cash flow characteristics. The IAS 39 measurement categories will be replaced by: fair value through profit or loss (FVPL), fair value through other comprehensive income (FVOCI), and amortized cost categories. IFRS 9 will also allow entities to continue to irrevocably designate instruments that qualify for amortized cost or FVOCI instruments as FVPL, if doing so eliminates or significantly reduces a measurement or recognition inconsistency. Equity instruments that are not held for trading may be irrevocably designated as FVOCI, with no subsequent reclassification of gains or losses to the income statement. The accounting for financial liabilities will largely be the same as the requirements of IAS 39.

IFRS 9 will also fundamentally change the approach to loan impairment. The standard will replace IAS 39's incurred loss approach with a forward-looking expected credit loss (ECL) approach. The Group will be required to record an allowance for expected losses for all loans and other debt financial assets not carried at FVPL, as well as for loan commitments and financial guarantee contracts. The allowance is based on the expected credit losses associated with the probability of default in the next twelve months unless there has been a significant increase in credit risk since origination, in which case the allowance would be based on the probability of default over the life of the asset.

(Thousands of euros)

3. Summary of accounting policies (continued)

Standards issued but not yet effective (continued)

IFRS 9 is effective for annual periods beginning on or after 1 January 2018, with early application permitted. Retrospective application is required, but restatement of comparative information is not required; the effect on the transition date – 1 January 2018 – would be recorded in retained earnings. The adoption of IFRS 9 is not expected to have a significant effect on the classification and measurement of the Group's financial assets and will have no impact on the classification and measurement of the Group's financial liabilities. The Group expects to measure investment securities at fair value through OCI as the Group expects not only to hold the assets to collect contractual cash flows but also to sell a significant amount on a relatively frequent basis. Deposits with banks and other financial institutions, loans to banks and loans to customers are held to collect contractual cash flows and are expected to give rise to cash flows representing solely payments of principal and interest. Thus, the Group expects to continue measuring those financial assets at amortized cost under IFRS 9. The Group plans to adopt the new standard on the required effective date. In 2016, the Group made a general assessment of the impact of all three phases of IFRS 9. This preliminary assessment is based on currently available information and may be subject to changes arising from further detailed analyses or additional reasonable and supportable information that will become available to the Group in the future. On the whole, the Group does not expect the adoption of the new requirements to have a significant impact on its balance sheet or equity, except for the effect of adoption of IFRS 9 impairment requirements. The Group expects increase in level of provisions which will influence an equity, and will perform a detailed assessment to determine the amount of such increase. The Group believes that all existing hedge relationships currently designated at the discretion of the Group in effective hedging relationships will still qualify for hedge accounting under IFRS 9. As IFRS 9 does not change the general principles of how an entity accounts for effective hedges, the Group does not expect a significant impact as a result of adoption of IFRS 9. The Group will assess possible changes related to the accounting for the time value of options, forward points or the currency basis spread in more detail in the future.

IFRS 15 Revenue from Contracts with Customers

In May 2014, the IASB issued IFRS 15 *Revenue from Contracts with Customers*, effective for periods beginning on 1 January 2018 with early adoption permitted. IFRS 15 defines principles for recognizing revenue and will be applicable to all contracts with customers. However, interest and fee income integral to financial instruments and leases will continue to fall outside the scope of IFRS 15 and will be regulated by the other applicable standards (e.g., IFRS 9, and IFRS 16 *Leases*).

Revenue under IFRS 15 will need to be recognized as goods and services are transferred, to the extent that the transferor anticipates entitlement to goods and services.

The standard will also specify a comprehensive set of disclosure requirements regarding the nature, extent and timing as well as any uncertainty of revenue and corresponding cash flows with customers.

The Group does not anticipate early adopting IFRS 15 and is currently evaluating its impact.

IFRS 16 Leases

The IASB issued the new standard for accounting for leases – IFRS 16 *Leases* in January 2016. The new standard does not significantly change the accounting for leases for lessors. However, it does require lessees to recognize most leases on their balance sheets as lease liabilities, with the corresponding right of-use assets. Lessees must apply a single model for all recognized leases, but will have the option not to recognize 'short-term' leases and leases of 'low-value' assets. Generally, the profit or loss recognition pattern for recognized leases will be similar to today's finance lease accounting, with interest and depreciation expense recognized separately in the consolidated statement of profit or loss.

IFRS 16 is effective for annual periods beginning on or after 1 January 2019. Early application is permitted provided the new revenue standard, IFRS 15, is applied on the same date.

The Group does not anticipate early adopting IFRS 16 and is currently evaluating its impact.

(Thousands of euros)

3. Summary of accounting policies (continued)

Standards issued but not yet effective (continued)

Amendments to IAS 12 Income Taxes

In January 2016, through issuing amendments to IAS 12, the IASB clarified the accounting treatment of deferred tax assets of debt instruments measured at fair value for accounting, but measured at cost for tax purposes. The Group does not anticipate that adopting the amendments would have a material impact on its consolidated financial statements.

Amendments to IAS 7 Statement of Cash Flows

In January 2016, the IASB issued amendments to IAS 7 *Statement of Cash Flows* with the intention to improve disclosures of financing activities and help users to better understand the reporting entities' liquidity positions. Under the new requirements, entities will need to disclose changes in their financial liabilities as a result of financing activities such as changes from cash flows and non-cash items (e.g., gains and losses due to foreign currency movements). The amendment is effective from 1 January 2017. The Group is currently studying the application of these amendments.

Amendments to IFRS 2 Share-based Payment

The IASB issued amendments to IFRS 2 *Share-based Payment* in relation to the classification and measurement of share-based payment transactions. The amendments are intended to eliminate diversity in practice, but are narrow in scope and address specific areas of classification and measurement. The amendments address three main areas:

- The effects of vesting conditions on the measurement of a cash-settled share-based payment transaction.
- The classification of a share-based payment transaction with net settlement features for withholding tax obligations.
- The accounting where a modification to the terms and conditions of a share-based payment transaction changes its classification from cash-settled to equity-settled.

These amendments are effective for annual periods beginning on or after 1 January 2018. On adoption, entities are required to apply the amendments without restating prior periods, but retrospective application is permitted if elected for all three amendments and other criteria are met. Early application is permitted. The amendments are not expected to have any impact on the Group.

Applying IFRS 9 Financial Instruments with IFRS 4 Insurance Contracts – Amendments to IFRS 4

The amendments address concerns arising from implementing the new financial instruments Standard, IFRS 9, before implementing the new insurance contracts standard that the Board is developing to replace IFRS 4. The amendments introduce two options for entities issuing insurance contracts: a temporary exemption from applying IFRS 9 and an overlay approach. The optional temporary exemption from IFRS 9 is available to entities whose activities are predominantly connected with insurance. The temporary exemption permits such entities to continue to apply IAS 39 *Financial Instruments: Recognition and Measurement* while they defer the application of IFRS 9 until 1 January 2021 at the latest. The overlay approach requires an entity to remove from profit or loss additional volatility that may arise if IFRS 9 is applied with IFRS 4.

The temporary exemption is first applied for reporting periods beginning on or after 1 January 2018. An entity may elect the overlay approach when it first applies IFRS 9 and apply that approach retrospectively to financial assets designated on transition to IFRS 9. The amendments are not expected to have any impact on the Group.

Applying IFRS 10 and IAS 28 – Sale or transfer of assets between an investor and its associate or joint venture

The amendments eliminate a known discrepancy between the requirements of IFRS 10 and IAS 28 for the loss of control of a subsidiary that is transferred to an associate or a joint venture as a contribution to equity. The amendments clarify that the income or loss arising from the sale or transfer by an investor of assets that are business in accordance with the definition in IFRS 3 in favor of its associate or joint venture should be fully reflected. In December 2015, the IASB decided to postpone the effective date of these amendments indefinitely.

(Thousands of euros)

3. Summary of accounting policies (continued)

Standards issued but not yet effective (continued)

Transfers of investment property (amendments to IAS 40).

The amendments clarify when an entity should transfer property, including property under construction or development into, or out of investment property. The amendments state that a change in use occurs when the property meets, or ceases to meet, the definition of investment property and there is evidence of the change in use.

Entities should apply the amendments prospectively to changes in use that occur on or after the beginning of the annual reporting period in which the entity first applies the amendments. An entity should reassess the classification of property held at that date and, if applicable, reclassify property to reflect the conditions that exist at that date. The amendments effective for annual periods beginning on or after 1 January 2018. Early application of the amendments is permitted and must be disclosed.

IFRIC Interpretation 22 Foreign Currency Transactions and Advance Consideration

The interpretation clarifies that in determining the spot exchange rate to use on initial recognition of the related asset, expense or income (or part of it) on the derecognition of a non-monetary asset or non-monetary liability relating to advance consideration, the date of the transaction is the date on which an entity initially recognises the non-monetary asset or non-monetary liability arising from the advance consideration. If there are multiple payments or receipts in advance, then the entity must determine a date of the transactions for each payment or receipt of advance consideration. Entities may apply the amendments on a fully retrospective basis. Early application of interpretation is permitted and must be disclosed. The Group does not anticipate early adopting of interpretation and is currently evaluating its impact. The interpretation is effective for annual periods beginning on or after 1 January 2018.

4. Significant accounting judgments and estimates

Assumptions and estimation uncertainty

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

The most significant uses of judgments and estimates are as follows:

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

Financial assets are recorded in the Group's consolidated statement of financial position less allowances for impairment. The Group regularly reviews its financial assets to assess impairment. When assessing impairment losses, the Group uses its professional judgment in relation to objective evidences that future contractual cash flows on financial asset shall decrease.

These evidences may include information on financial difficulties of the borrower or other observable data on adverse changes in the payment status of borrowers, or national or local economic conditions that correlate with defaults on assets. The Group uses its professional judgment to adjust observable data for financial assets to reflect current circumstances. Impairment loss may be reversed only if a subsequent increase of estimated contractual cash flows can be objectively related to an event occurring after the impairment loss was recognized.

Fair value of financial instruments

Where the fair values of financial assets and financial liabilities recorded in the consolidated statement of financial position cannot be derived from active markets, they are determined using a variety of valuation techniques that include the use of mathematical models. The input to these models is taken from observable markets where possible, but where this is not feasible, a degree of judgment is required in establishing fair values. More details are provided in Note 24.

(Thousands of euros)

4. Significant accounting judgments and estimates (continued)

Assumptions and estimation uncertainty (continued)

Impairment of available-for-sale equity securities

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

Fair values of buildings and investment property

As disclosed in Note 3, the Group applies the fair value model with regard to investment property. Buildings included in fixed assets are stated at revalued amount.

As for buildings within property and equipment, the Group monitors the compliance of the present value of buildings with their fair value and performs revaluation to ensure that there are no significant differences. Changes in the fair value are recognized in other comprehensive income. The most recent revaluation of the Group's building was carried out as at 31 December 2016 by an independent firm of professional appraisers applying an appropriate valuation methodology and information on transactions with similar real estate objects on the local market. However, valuation results based on the above valuation technique may differ from the prices of actual transactions in the real estate market. Starting from 31 December 2016, the revalued building is depreciated in accordance with the remaining useful life.

As for investment property, the Group monitors changes in its fair value at each reporting date to ensure that the present value of investment property does not differ materially from its fair value. Changes in the fair value of investment property are recognized in the consolidated income statement. The most recent revaluation of the Group's investment property was carried out as at 31 December 2016 by an independent firm of professional appraisers applying an appropriate valuation methodology and information on transactions with similar real estate objects on the local market.

However, valuation results based on the above valuation technique may differ from the prices of actual transactions in the real estate market.

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

- Note 7 – Derivative financial instruments.
- Note 8 – Available-for-sale investment securities.
- Note 10 – Loans to banks.
- Note 11 – Loans to customers.
- Note 12 – Investment property.
- Note 13 – Property, equipment and intangible assets.
- Note 19 – Contingencies and lending commitments.

(Thousands of euros)

5. Cash and cash equivalents

Cash and cash equivalents comprise:

	2016	*2015*
Cash on hand	**104**	**66**
Nostro accounts with banks and other financial institutions		
Credit rating from A- to A+	62,548	21,106
Credit rating from BBB- to BBB+	4,526	3,059
Credit rating from BB- to BB+	551	350
Total nostro accounts with banks and other financial institutions	**67,625**	**24,515**
Short-term deposits with banks		
Term deposits with banks		
Credit rating from BBB- to BBB+	–	18,304
Credit rating from BB- to BB+	25,302	16,634
Total short-term deposits with banks	**25,302**	**34,938**
Cash and cash equivalents	**93,031**	**59,519**

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

6. Deposits with banks and other financial institutions

Deposits with banks and other financial institutions are presented based on contractual terms and include the following items:

	2016	*2015*
Term deposits up to 1 year		
Credit rating from BB- to BB+	–	6,049
Credit rating from B- to B+	37,126	79,276
Total term deposits up to 1 year	**37,126**	**85,325**
Term deposits over 1 year		
Credit rating from A- to A+	5,821	15,067
Credit rating from BB- to BB+	2,390	–
Total term deposits over 1 year	**8,211**	**15,067**
Total deposits with banks and other financial institutions	**45,337**	**100,392**

Amounts due from the National Bank of the Republic of Cuba

	2016	*2015*
Term deposits with the National Bank of the Republic of Cuba without credit rating	34,967	34,967
Less: allowance for impairment	(34,967)	(34,967)
Term deposits with the National Bank of the Republic of Cuba	–	–

Concentration of deposits with banks and other financial institutions

As at 31 December 2016, the Group had three counterparties (31 December 2015: five counterparty) accounting for over 10% of the Group's total deposits with banks and other financial institutions, except for deposits with the National Bank of the Republic of Cuba.

(Thousands of euros)

7. Derivative financial instruments

The Group performs the operations with currency and other derivative financial instruments which are generally traded in an over-the-counter market with professional market counterparties on standardized contractual terms and conditions. Derivative financial instruments have either potentially favorable terms (and are assets) or potentially unfavorable conditions (and are liabilities) as a result of fluctuations in the exchange rates or other variable factors associated with these instruments. The fair value of derivative financial instruments can vary significantly depending on the potentially favorable and unfavorable conditions.

The table below shows the fair value of derivative financial instruments as at 31 December 2016 and 31 December 2015 and notional amounts of term contracts for the purchase and sale of foreign currency specifying contractual exchange rates.

	31 December 2016				
	Notional amount		***Weighted average***	***Fair value***	
	Purchase	***Sale***	***exchange rate***	***Assets***	***Liabilities***
Derivative financial assets and liabilities at fair value through profit or loss					
Swaps	RUB 9,136,720 thousand	EUR 132,150 thousand	69.42	14,246	883
	RON 110,300 thousand	EUR 24,971 thousand	4.44	–	632
	EUR 117,000 thousand	USD 128,825 thousand	1.10	116	5,704
	EUR 8,000 thousand	RUB 572,280 thousand	71.54	–	788
Forwards	EUR 34,000 thousand	USD 37,896 thousand	1.11	–	2,080
Total derivative financial assets and liabilities at fair value through profit or loss				**14,362**	**10,087**
Derivative financial assets and liabilities designated as hedging instruments					
Swaps	RON 298,300 thousand	EUR 67,068 thousand	4.45	–	1,536
Total derivative financial assets and liabilities designated as hedging instruments				**–**	**1,536**
Derivative financial instruments				**14,362**	**11,623**

	31 December 2015				
	Notional amount		***Weighted average***	***Fair value***	
	Purchase	***Sale***	***exchange rate***	***Assets***	***Liabilities***
Derivative financial assets and liabilities at fair value through profit or loss					
Swaps	RUB 12,136,720 thousand	EUR 185,914 thousand	65.28	–	29,034
	RON 110,300 thousand	EUR 24,972 thousand	4.42	–	864
	EUR 61,000 thousand	USD 64,982 thousand	1.07	1,775	–
Forwards	EUR 30,000 thousand	USD 32,721 thousand	1.09	69	–
Total derivative financial assets and liabilities at fair value through profit or loss				**1,844**	**29,898**
Derivative financial instruments				**1,844**	**29,898**

(Thousands of euros)

7. Derivative financial instruments (continued)

Due to issuing bond loans denominated in currencies other than the Group's functional currency (Note 17), the Group concluded cross currency interest rate swaps and currency forwards on an arm's length basis with large international and Russian credit institutions. These swaps are used to manage long-term currency risks of the Group. Payment netting is not applied to the parties' obligations in respect of interest and principal payments.

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

As at 31 December 2016 and 31 December 2015, the Group has positions in the following types of derivatives:

Forwards: Forward contracts are contractual agreements to buy or sell a specified financial instrument at a specific price and date in the future. Forwards are customized contracts transacted in the over-the-counter market.

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

Fair value measurement is based on the corresponding forward curves that depend on exchange rates, interest rates and swap contract maturity. For the fair value of swaps, the discount rate was calculated on the basis of zero coupon yield curve and credit risk. Changes in the fair value of swaps were mainly due to the increase in the forward EUR to RUB exchange rates.

8. Available-for-sale investment securities

Available-for-sale investment securities comprise:

	2016	*2015*
Owned by the Group		
Quoted debt securities		
Government bonds:		
Eurobonds issued by governments of member countries	52,678	93,027
Government bonds	**52,678**	**93,027**
Corporate bonds		
Credit rating from A- to A+	21,152	–
Credit rating from BBB- to BBB+	21,861	–
Credit rating from BB- to BB+	57,579	–
Credit rating from B- to B+	17,575	–
Corporate bonds	**118,167**	**–**
Total quoted debt securities	**170,845**	**93,027**
Quoted equity instruments		
No credit rating	4	4
Total quoted equity instruments	**4**	**4**
Available-for-sale investment securities	**170,849**	**93,031**
Pledged under repurchase agreements		
Quoted debt securities		
Eurobonds issued by governments of member countries	10,286	21,646
Eurobonds issued by governments of non-member countries	7,597	–
Government bonds	**17,883**	**21,646**
Corporate bonds		
Credit rating AAA	22,486	–
Credit rating from AA- to AA+	4,688	–
Credit rating from A- to A+	32,521	–
Credit rating from BBB- to BBB+	4,994	1,382
Credit rating from BB- to BB+	15,886	–
Corporate bonds	**80,575**	**1,382**
Total quoted available-for-sale debt securities pledged under repurchase agreements	**98,458**	**23,028**

(Thousands of euros)

8. Available-for-sale investment securities (continued)

Government bonds represent EUR-denominated, USD-denominated and RUB-denominated securities issued and guaranteed by the Ministries of Finance of these countries, maturing in 2018-2027 (31 December 2015: maturing in 2018-2027). The annual coupon rate for these bonds varies from 0.4% to 7.9% (31 December 2015: from 2.0% to 6.0%).

Corporate bonds are represented by the bonds issued by large companies and banks of member countries of the Bank, as well as corporate international companies and Development Banks that have similar goals and missions with the Group, maturing in 2018-2031 (31 December 2015: maturing in 2020). The annual coupon rate for these bonds varies from 0.6% to 10.25% (31 December 2015: 5.0%).

9. Held-to-maturity investment securities

In July 2016, due to changes in the Bank's management's intent to withhold investment securities to maturity, the Bank reclassified these securities into investment securities available for sale. At the date of reclassification, the amortized cost of securities amounted to 92,105 thousand euros.

Held-to-maturity investment securities comprise:

	2016	***2015***
Owned by the Bank		
Quoted debt securities		
Eurobonds issued by governments of member countries	–	1,272
Government bonds of member countries	**–**	**1,272**
Corporate bonds		
Credit rating from BBB- to BBB+	–	17,442
Credit rating from BB- to BB+	–	31,320
Corporate bonds	**–**	**48,762**
Total quoted held-to-maturity debt securities	**–**	**50,034**
Held-to-maturity investment securities pledged under repurchase agreements		
Quoted debt securities		
Eurobonds issued by governments of member countries	–	10,489
Government bonds of member countries	**–**	**10,489**
Corporate bonds		
Credit rating from BB- to BB+	–	62,705
Corporate bonds	**–**	**62,705**
Total held-to-maturity investment securities pledged under repurchase agreements	**–**	**73,194**

Government bonds of member countries represent EUR-denominated and RUB-denominated securities issued and guaranteed by the Ministries of Finance of these countries maturing as at 31 December 2015 in 2018-2020. The annual coupon rate for these bonds as at 31 December 2015 varies from 3.6% to 7.9%.

Corporate bonds are represented by the bonds issued by major companies and banks of member countries and EU countries, maturing as at 31 December 2015 in 2016-2023. The annual coupon rate for these bonds as at 31 December 2015 varies from 3.0% to 7.9%.

(Thousands of euros)

10. Loans to banks

During 2016, the Group continued its lending activities, being guided by the key priorities of the Development Strategy of the IIB. The principal lending activity is to facilitate the development of small and medium-sized businesses in the member countries and participate in financing of socially important infrastructure projects in these countries. The Group considers national development institutes, export and import banks and agencies, international financial organizations and development banks as its key counterparties.

In 2016 and 2015, the Group provided trade financing loans and long-term loans to banks operating in the following countries:

	2016	*2015*
Trade financing loans:		
Russian Federation	953	–
Trade financing loans	**953**	**–**
Long-term loans to banks		
Mongolia	47,970	43,044
Russian Federation	26,425	64,223
Socialist Republic of Vietnam	19,019	33,330
Long-term loans to banks	**93,414**	**140,597**
Total loans to banks	**94,367**	**140,597**

As at 31 December 2016 and 31 December 2015, outstanding trade financing loans and long-term loans to banks are neither past due nor impaired, and no allowances for impairment of these loans were made.

Analysis of collateral for loans to banks

The following table provides an analysis of the portfolio of trade financing loans and long-term loans to banks by type of collateral as at 31 December 2016 and 31 December 2015:

	2016		*2015*	
	Loans to banks	*Share in the total loans, %*	*Loans to banks*	*Share in the total loans, %*
Pledge of real property (mortgage) and title	7,247	7.7	6,933	4.9
Uncollateralized part of the loans	87,120	92.3	133,664	95.1
	94,367	**100.0**	**140,597**	**100.0**

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

Concentration of long-term loans to banks

As at 31 December 2016, long-term loans and trade financing loans to five banks (31 December 2015: five banks) with the total amount of loans to each of them exceeding 10% of total loans to banks were recorded on the Group's balance sheet. As at 31 December 2016, the total amount of such major loans was EUR 74,787 thousand (31 December 2015: EUR 85,238 thousand) and no impairment allowances (31 December 2015: no allowances) have been made for them.

(Thousands of euros)

11. Loans to customers

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

	2016	*2015*
Republic of Bulgaria	65,922	57,917
Russian Federation	61,213	28,160
Romania	40,235	25,844
Republic of Ecuador	39,570	18,249
Republic of Panama	36,276	–
Czech Republic	22,930	–
Slovak Republic	8,411	23,437
USA	6,108	–
Mongolia	5,683	21,890
Gross loans to customers	**286,348**	**175,497**
Less: allowance for loan impairment	(17,312)	(9,755)
Loans to customers	**269,036**	**165,742**

The information on the overdue loans as at 31 December 2016 and 31 December 2015 is stated below:

	2016	*2015*
Loans with overdue principal and/or interest	14,769	14,858
Less: allowance for loan impairment	(14,769)	(9,755)
Overdue loans to customers	**–**	**5,103**

As at 31 December 2016 and 31 December 2015, there were no overdue but not impaired loans.

Allowance for impairment of loans to customers

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

	Slovak Republic	*Republic of Bulgaria*	*Romania*	*Total*
At 1 January 2016	**3,000**	**6,755**	**–**	**9,755**
Net charge for the period	5,103	200	2,254	**7,557**
At 31 December 2016	**8,103**	**6,955**	**2,254**	**17,312**
Individual impairment	**8,103**	**6,666**	**–**	**14,769**
Gross amount of loans, individually determined to be impaired, before deducting any individually assessed impairment allowance	**8,103**	**6,666**	**–**	**14,769**

	Slovak Republic	*Republic of Bulgaria*	*Total*
At 1 January 2015	**3,589**	**–**	**3,589**
Net (reversal)/charge for the period	(589)	6,755	**6,166**
At 31 December 2015	**3,000**	**6,755**	**9,755**
Individual impairment	**3,000**	**6,755**	**9,755**
Gross amount of loans, individually determined to be impaired, before deducting any individually assessed impairment allowance	**8,103**	**6,755**	**14,858**

(Thousands of euros)

11. Loans to customers (continued)

The following table provides an analysis of the customer loan portfolio, net of allowance for impairment, by types of collateral as at 31 December 2016 and 31 December 2015:

	2016		*2015*	
	Loans net of allowance for impairment	***Share in the total loans, %***	***Loans net of allowance for impairment***	***Share in the total loans, %***
State guarantees	75,845	28.2	18,249	11.0
Pledge of real property (mortgage) and title	25,811	9.6	35,896	21.6
Pledge of right of claim	22,970	8.5	18,492	11.2
Corporate guarantees	22,930	8.5	–	–
Pledge of equipment and goods in turnover	22,641	8.4	13,281	8.0
Pledge of shares	21,579	8.0	29,952	18.1
Pledge of vehicles	2,756	1.0	–	–
Uncollateralized part of the loans	74,504	27.8	49,872	30.1
Total loans to customers	**269,036**	**100.0**	**165,742**	**100.0**

Analysis of collateral for loans to customers

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

Concentration of loans to customers

As at 31 December 2016, loans to three borrowers (2015: two) with the total amount of loans to each of the two borrowers exceeding 10% of total loans to customers were recorded on the Group's balance sheet. As at 31 December 2016, these loans comprised EUR 107,191 thousand (2015: EUR 40,991 thousand) in total and no impairment allowances (2015: no allowances) have been made for them.

Analysis of loans to customers by industry

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

	2016	*2015*
Leasing	85,897	44,114
Production and transmission of electricity	39,570	14,688
Food and beverage	27,504	7,569
Chemical production	23,831	22,743
Metal working industry	22,930	–
Manufacturing of electrical equipment	20,809	21,208
Construction	14,769	29,179
Agriculture	14,295	4,942
Transport	13,752	15,001
Crude oil refining	10,002	9,989
Production of pharmaceutical products	6,645	–
Trading	6,036	5,418
Other	308	646
	286,348	**175,497**
Less: allowance for loan impairment	(17,312)	(9,755)
Loans to customers	**269,036**	**165,742**

(Thousands of euros)

12. Investment property

In 2016 and 2015, the following changes occurred in the cost of property under operating lease:

	2016	*2015*
At 1 January	**33,819**	**52,879**
Additions	14,324	–
Inseparable improvements	50	33
Transfers in the property and equipment	(24,179)	(16,593)
Effect of revaluation	(2,174)	(2,500)
Carrying amount at 31 December	**21,840**	**33,819**

In 2016, the Group received collateral in the form of an administrative building in the city of Ulan Bator, Mongolia.

The Group rents buildings under operating lease agreements. In 2016, the Group's income from lease of investment property amounted to EUR 3,442 thousand (2015: EUR 5,214 thousand).

As at 31 December 2016, the fair value of investment property is determined based on the results of valuation performed on 31 December 2016. The valuation services were performed by an independent firm of professional appraisers which have acknowledged qualification and relevant professional experience in appraising real property of a similar category and in a similar location.

The fair value is determined by reference to market-based evidence. For further details on the fair value of investment property refer to Note 24.

If the investment property was measured using the cost method, the carrying amounts as at 31 December 2016 and 31 December 2015 would be as follows:

	2016	*2015*
Cost	20,091	20,264
Additions	50	–
Accumulated depreciation	(2,370)	(8,092)
Net book value	**17,771**	**12,172**

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

(Thousands of euros)

13. Property, equipment and intangible assets

The movements in property, equipment and intangible assets for the years 2016 and 2015 were as follows:

	Buildings	*Equipment*	*Computers and software*	*Office furniture*	*Vehicles*	*Intangible assets*	*Other*	*Capital expenditure*	*Total*
Cost or revalued amount									
At 1 January 2016	**62,807**	**7,073**	**3,278**	**296**	**808**	**325**	**176**	**1,591**	**76,354**
Additions	–	–	–	–	–	–	–	1,754	**1,754**
Transfers from the investment property	24,179	–	–	–	–	–	–	–	**24,179**
Transfers	223	436	83	22	–	2,147	7	(2,918)	**–**
Disposals	–	(9)	–	(11)	–	–	–	–	**(20)**
Recovery of accumulated depreciation upon revaluation	(1,057)	–	–	–	–	–	–	–	**(1,057)**
Effect of revaluation	(18,508)	–	–	–	–	–	–	–	**(18,508)**
At 31 December 2016	**67,644**	**7,500**	**3,361**	**307**	**808**	**2,472**	**183**	**427**	**82,702**
Accumulated depreciation									
At 1 January 2016	–	**(6,547)**	**(2,445)**	**(228)**	**(477)**	**(165)**	**(99)**	**–**	**(9,961)**
Charge for the period	(1,174)	(209)	(285)	(19)	(103)	(178)	(6)	–	**(1,974)**
Disposals	–	9	–	11	–	–	–	–	**20**
Recovery of accumulated depreciation upon revaluation	1,057	–	–	–	–	–	–	–	**1,057**
At 31 December 2016	**(117)**	**(6,747)**	**(2,730)**	**(236)**	**(580)**	**(343)**	**(105)**	**–**	**(10,858)**
Net book value									
At 31 December 2015	**62,807**	**526**	**833**	**68**	**331**	**160**	**77**	**1,591**	**66,393**
At 31 December 2016	**67,527**	**753**	**631**	**71**	**228**	**2,129**	**78**	**427**	**71,844**

(Thousands of euros)

13. Property, equipment and intangible assets (continued)

	Buildings	*Equipment*	*Computers and software*	*Office furniture*	*Vehicles*	*Intangible assets*	*Other*	*Capital expenditure*	*Total*
Cost or revalued amount									
At 1 January 2015	**50,806**	**7,069**	**3,095**	**298**	**923**	**160**	**188**	**766**	**63,305**
Inseparable improvements	52	–	–	–	–	–	–	–	**52**
Additions	–	–	–	–	–	–	–	1,780	**1,780**
Transfers from the investment property	16,593	–	–	–	–	–	–	–	**16,593**
Transfers	–	179	505	4	102	165	–	(955)	**–**
Disposals	–	(175)	(322)	(6)	(217)	–	(12)	–	**(732)**
Recovery of accumulated depreciation upon revaluation	(1,002)	–	–	–	–	–	–	–	**(1,002)**
Effect of revaluation	(3,642)	–	–	–	–	–	–	–	**(3,642)**
At 31 December 2015	**62,807**	**7,073**	**3,278**	**296**	**808**	**325**	**176**	**1 591**	**76,354**
Accumulated depreciation									
At 1 January 2015	**(67)**	**(6,523)**	**(2,537)**	**(214)**	**(598)**	**(53)**	**(106)**	**–**	**(10,098)**
Charge for the period	(935)	(176)	(229)	(18)	(96)	(112)	(6)	–	**(1,572)**
Disposals	–	152	321	4	217	–	13	–	**707**
Recovery of accumulated depreciation upon revaluation	1,002	–	–	–	–	–	–	–	**1,002**
At 31 December 2015	**–**	**(6,547)**	**(2,445)**	**(228)**	**(477)**	**(165)**	**(99)**	**–**	**(9,961)**
Net book value									
At 31 December 2014	**50,739**	**546**	**558**	**84**	**325**	**107**	**82**	**766**	**53,207**
At 31 December 2015	**62,807**	**526**	**833**	**68**	**331**	**160**	**77**	**1,591**	**66,393**

As at 31 December 2016, the cost of fully depreciated property and equipment still used by the Group was EUR 7,982 thousand (31 December 2015: EUR 7,977 thousand).

(Thousands of euros)

13. Property, equipment and intangible assets (continued)

As at 31 December 2016, the fair value of a group of buildings owned by the Group is determined based on the results of valuation performed on 31 December 2016. The valuation services were performed by an independent firm of professional appraisers which have acknowledged qualification and relevant professional experience in appraising real property of a similar category and in a similar location.

The fair value is determined by reference to market-based evidence. For further details on the fair value of property and equipment refer to Note 24.

If the buildings were measured using the cost method, the carrying amounts as at 31 December 2016 and 31 December 2015 would be as follows:

	2016	*2015*
Cost	52,132	37,583
Additions	223	52
Accumulated depreciation	(20,871)	(15,029)
Net book value	**31,484**	**22,606**

14. Other assets and liabilities

Other assets comprise:

	2016	*2015*
Financial assets		
Settlements on bank transactions	1,814	1,525
Accounts receivable on business operations	1,394	1,202
Other financial assets	136	–
	3,344	**2,727**
Less: allowance for impairment	(1,924)	(1,633)
Total financial assets less allowance	**1,420**	**094**
Non-financial assets		
Assets held-for-sale – real estate	89	–
Inventories – real estate	55	43
Other non-financial assets	755	673
Total non-financial assets	**899**	**716**
Total other assets	**2,319**	**1,810**

The movements in other impairment allowance are as follows:

	2016	*2015*
Allowance at 1 January	**1,633**	**1,763**
Reversal charge for the year	(67)	(89)
Change in allowance resulting from changes in exchange rates	358	(41)
Allowance at 31 December	**1,924**	**1,633**

(Thousands of euros)

14. Other assets and liabilities (continued)

Other liabilities comprise:

	2016	*2015*
Financial liabilities		
Other accounts payable on business operations	1,182	1,063
Other accounts payable on bank transactions	662	–
Other financial liabilities	19	–
Total financial liabilities	**1,863**	**1,063**
Non-financial liabilities		
Settlements with employees	3,647	2,975
Other non-financial liabilities	72	50
Total non-financial liabilities	**3,719**	**3,025**
Total other liabilities	**5,582**	**4,088**

15. Due to banks and other financial institutions

Due to banks and other financial institutions are presented based on contractual terms and include the following items:

	2016	*2015*
Due to banks up to 1 year		
Term deposits of banks and other financial institutions	52,856	48,617
Total due to banks up to 1 year	**52,856**	**48,617**
Due to banks over 1 year		
Repurchase agreements	66,069	64,756
Total due to banks over 1 year	**66,069**	**64,756**
Total due to banks	**118,925**	**113,373**

The Group performs daily monitoring of the repurchase agreements and the value of collateral when placing/returning additional collateral, if necessary.

Concentration of deposits from banks and other financial institutions

As at 31 December 2016, the Group has two counterparties (31 December 2015: three counterparties) accounting for over 10% of the Group's total deposits from banks and other financial institutions in the amount of EUR 111,418 thousand (31 December 2015: EUR 104,873 thousand).

16. Long-term loans of banks

Long-term loans of banks comprise:

	2016	*2015*
Syndicated loans	59,039	–
Loans of banks	14,310	44,187
Total long-term loans of banks	**73,349**	**44,187**

In June 2016 the Group received a syndicated loan in the amount of EUR 60,000 thousand with a floating rate of EURIBOR (6 months) + 1.75% p. a. and maturing in May 2018.

(Thousands of euros)

17. Debt securities issued

Debt securities issued comprise:

	Interest rate, % p.a.	*Maturity*	*2016*	*2015*
RUB-denominated bonds	0.1-12.3	2024-2025	151,516	158,067
EUR-denominated bonds	3.5	2019	30,127	30,100
RON-denominated bonds	3.4-4.1	2018-2019	90,885	24,557
Total bonds			**272,528**	**212,724**

On 27 September 2016, the Group issued bonds denominated in Romanian lei in the amount of RON 300 million (EUR 67,398 thousand) maturing in three years. The coupon rate on the bonds was set at 3.4% payable annually with the first coupon payment to be made on 27 September 2017.

Among other things, the Group used the proceeds from the offerings to expand its loan portfolio.

At the dates of placement of the RUB-denominated bonds, the Group entered into cross-currency interest rate swaps for the purpose of managing currency risks (Note 7).

On 31 October 2016, the Bank offered to repurchase RUB-denominated bonds, series 02, and repurchased almost the total amount of those bonds RUB 2 998,0 thousand (EUR 43,327 thousand) from investors. A new coupon rate of 0.1% p.a. was set.

18. Equity

Subscribed and paid-in capital

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

As at 31 December 2016, the unpaid portion of the Bank’s subscribed capital in the amount of EUR 986,947 thousand (31 December 2015: EUR 996,947 thousand) is the amount of contributions that have not been made yet by the Bank’s member countries and the amount of unallocated equity contributions totaling EUR 175,500 thousand (31 December 2015: EUR 175,500 thousand).

On 9 March 2016, in accordance with the Memorandum of Understanding singed at the 102nd meeting of the IIB’s Council (20-21 November 2014), the Government of Hungary contributed EUR 10,000 thousand to the Bank’s equity. On 18 May 2015, the Government of Hungary contributed EUR 10,000 thousand to the Bank's equity to resume its full membership. In accordance with the Memorandum of Understanding singed at the 102nd meeting of the IIB's Council (20-21 November 2014), the Bank added EUR 10,000 thousand to the contribution of Hungary out of retained earnings for the previous years. On 29 July in accordance with the Memorandum of Understanding singed at the 102nd meeting of the IIB's Council (20-21 November 2014), the Bank fulfilled its obligations to transfer the second payment in the amount of EUR 10,000 thousand out of retained earnings for the previous years as Hungary's additional contribution to the Bank's share capital.

As a result, the paid-in capital of the International Investment Bank totaled EUR 313,053 thousand (31 December 2015: EUR 303,053 thousand).

(Thousands of euros)

18. Equity (continued)

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

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

	Revaluation reserve for available-for-sale investment securities	***Revaluation reserve for property and equipment***
At 1 January 2015	**(999)**	**35,095**
Net unrealized gains on available-for-sale investment securities	2,539	–
Realized gains on available-for-sale investment securities reclassified to the income statement	(3,204)	–
Revaluation of buildings	–	(3,642)
At 31 December 2015	**(1,664)**	**31,453**
Net unrealized gains on available-for-sale investment securities	10,673	–
Realized gains on available-for-sale investment securities reclassified to the income statement	(10,515)	–
Revaluation of buildings	–	(18,508)
At 31 December 2016	**(1,506)**	**12,945**

Revaluation reserve for available-for-sale investment securities

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

Revaluation reserve for property and equipment

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

19. Contingencies and loan commitments

Legal

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

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

Insurance

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

(Thousands of euros)

19. Contingencies and loan commitments (continued)

Commitments and contingencies

At any time the Group may have outstanding commitments to extend loans. These commitments take the form of approved loan agreements.

As at 31 December 2016, commitments and contingencies of the Group comprised off-balance credit-related commitments, in particular undrawn loan facilities and reimbursement obligations.

Off-balance credit-related commitments are presented in the table below as at 31 December 2016 and 31 December 2015.

	2016	*2015*
Undrawn loan facilities	33,103	52,376
Reimbursement obligations	9,898	6,796
Guarantees issued	4,934	4,556
Total off-balance commitments	**47,935**	**63,728**

20. Leases

Group as lessor

The Group provides its investment property for operating leases. As at 31 December 2016, the Group's non-cancelable operating lease rentals amount to EUR 4,752 thousand (31 December 2015: EUR 5,938 thousand) and will be settled within 1-5 years.

21. Interest income and interest expense

Net interest income comprises:

	2016	*2015*
Loans to customers	13,886	8,022
Loans to banks	6,462	7,058
Available-for-sale investment securities	5,091	2,165
Held-to-maturity investment securities	2,975	5,944
Deposits with banks and other financial institutions, including cash and cash equivalents	4,041	3,943
Interest income	**32,455**	**27,132**
Debt securities issued	(22,511)	(14,812)
Funds raised under repurchase agreements	(1,839)	(819)
Long-term loans of banks	(1,798)	(1,247)
Due to banks and other financial institutions	(1,198)	(609)
Current customer accounts	(305)	(257)
Interest expenses	**(27,651)**	**(17,744)**
Net interest income	**4,804**	**9,388**

In 2016, there was no interest income accrued on impaired loans issued (2015: EUR 185 thousand).

(Thousands of euros)

22. General and administrative expenses

General and administrative expenses comprise:

	2016	*2015*
Employee compensations and employment taxes	13,001	11,471
Depreciation of property, equipment and intangible assets (Note 13)	1,974	1,572
IT-expenses, inventory and occupancy expenses	1,715	1,293
Professional services	1,019	466
Expenses related to business travel, representative and accommodation expenses	682	1,277
Other	548	829
General and administrative expenses	**18,939**	**16,908**

23. Risk management

Risk management framework

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

The Group's risk management activities are intended to:

- Identify, analyze and manage risks faced by the Group.
- Establish ratios and limits that restrict level of the appropriate types of risks.
- Monitor the level of the risk and its compliance with established limits.
- Develop and implement regulative and methodological documents as well as software applications that ensure professional risk management for the bank transactions.

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

Integrated into the whole vertical organizational structure of the Group and all areas of the Group's activities, the risk management system makes it possible to identify in a timely manner and effectively manage different types of risks.

Risk management involves all of the Group's divisions in the evaluating, assuming, and controlling risks ("Three lines of defense"):

- Risk-taking (1st line of defense): the Group's divisions directly preparing and conducting transactions, involved in the identification, assessment, and monitoring of risks and comply with internal regulations on risk management, as well as give due consideration to the risk level in the preparation of transactions.
- Risk management (2nd line of defense): the division responsible for risk management develops risk management tools and methodology, assesses and monitors the risk level, prepares reports on risks, carries out risk aggregation, and calculates the amount of total capital requirements.
- Internal audit (3rd line of defense): independent quality assessment for existing risk management processes, identification of violations, and proposals for the improvement of the risk management system.

The Group's operations are managed taking into account the level of the risk appetite approved by the Council and its integration into a system of limits and restrictions insuring the acceptable level of risk for aggregated positions, transparent distribution of total risk limit among the activities of the Group.

The Bank's Council, the Board, the Finance Committee, the Credit Committee and the Risk Management Department are responsible for managing the Group's risks.

(Thousands of euros)

23. Risk management (continued)

Risk management framework (continued)

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

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

The Finance Committee determines the Bank's approaches to forming the optimal structure of the Bank's balance sheet, taking into account information of current and expected level of risks associated with assets and liabilities management within the established limits and other restrictions. It also ensures management and control over the credit risk, market risk, operational risk, reputational risk, legal risk and liquidity risk and reviews the limit-setting offers.

The Credit Committee manages the Bank's loan portfolio in accordance with its effective lending policy, aligns operation of the Group's divisions in terms of the credit risk management and reviews the offers for setting credit risk limits in respect of the certain counterparties.

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

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

During 2016, further development of the risk management system started in 2013 was aimed at implementation of Basel standards and best practices of development banks within the Group:

- New methodological and regulatory documents relating to credit and operational risk management have been elaborated.
- The Group continued to implement the target model of the risk management system, based on requirements of the leading rating agencies.

In compliance with the existing procedures, twice a year the Group sets and reviews limits for counterparties for the purpose of performing financial transactions and assessing their creditworthiness. As part of the lending activity analysis, the Group continuously monitored the level of its loan assets risk. During the reporting period, the Group sent its specialists to certain borrowers in order to monitor the implementation of the projects and identify potential primary evidence of impairment of loan assets.

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

Risk appetite

The risk appetite is the aggregate amount of risk taken by the Group to achieve its strategic goals and objectives. By approving the level of risk appetite, the Bank's Council determines the willingness to accept a risk or the amount of equity and liquidity that the Bank is willing to risk in the implementation of this strategy.

Risk appetite consists of 4 main components:

- The allocation of capital and liquidity (if necessary).
- Target allocation of capital across the main types of risk.
- The level of risk and target risk appetite in the context of the main performance indicators of the Group and risks significant for the Group.
- Determining levels of tolerance.

(Thousands of euros)

23. Risk management (continued)

Risk management framework (continued)

The procedure for determining the Group's risk appetite shall be defined by the Credit Risk Management Department and submitted for review by the Board and approval by the Council of the Bank.

The risk appetite shall be approved by the Council of the Bank on an annual basis for the next year and shall be a major factor of the Group's strategic limits determining the thresholds for the Group's key performance indicators and the Group's significant risks.

In determining the risk appetite, the Group assesses whether the specified risk appetite is acceptable in the current time period and whether it will be acceptable in the future, taking into account:

- Expectations of the founders concerning the level of profitability.
- International regulatory standards.
- Current and expected future volume of transactions.
- Current and expected future structure of significant risks.
- Current and expected future level of aggregate capital.

Based on the risk appetite determined by the Council, the Board annually approves the Group's limits, sublimits, and risk indicators, which should not exceed the target values of the risk appetite.

Risk identification

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

Risk assessment, management and control

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

The risk monitoring system comprises:

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

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

- Credit risk;
- Liquidity risk;
- Market risk;
- Operational risk.

(Thousands of euros)

23. Risk management (continued)

Credit risk

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

System of credit risk management

The Group's regulatory documents establish the following:

- Procedures to review and approve loan/credit applications.
- Methodology for the credit assessment of borrowers, counterparties, issuers and insurance companies.
- Requirements to the credit documentation.
- Procedures for the ongoing monitoring of loans and other credit exposures.

The Credit Committee establishes the limits per borrower/group of related borrowers. The Credit Committee structures the transaction to minimize credit risk. The Loan Operations Analysis Department is responsible for ongoing control over the quality of the Group's loan portfolio.

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

The corporate loan/credit application and appropriate project documents are reviewed by the Customer Relations Department. Customer Relations Department takes a decision on the preliminary of starting information on the deal whether to continue work with the client or not. In case of a positive decision, Credit Department makes full examination of the deal and sends the full set of required documents for reviewing the loan/credit application to Legal Department, Risk Management Department, Security Department, Strategic Development and Analysis Department, Internal Control Department, Compliance Control Department, Operational Department, Financial Department, Structured and Debt financing Department. These departments prepare expert opinions in the framework of their competence. The loan/credit application is subject to review by the Credit Committee based on the Credit Department's Description of the Investment Transaction and expert opinions received form the departments. The procedure of making lending decisions comprises the following steps: Step 1 includes reviewing application and making decision by the Credit Committee (if such issue falls within its competence); Step 2 includes making decision by the Board of the Group (if such issue falls within its competence); Step 3 includes sending a set of respective documents approved by the Board of the Group to the member country in order to obtain the final approval from the country of origin of the borrower or making decision by the Council of the Group (if such issue falls within its competence).

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

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

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

(Thousands of euros)

23. Risk management (continued)

Credit risk (continued)

Collateral and other credit enhancements

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

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

- Pledge of equipment and goods in turnover;
- Pledge of real estate (mortgage) and title;
- Pledge of rights of demand and construction.

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

The Group assumes that the fair value of the collateral is its value estimate recognized by the Group to calculate the discounted impairment allowance based on its liquidity and possibility of selling such property in the event of borrower's default considering the time needed for such sale, litigation and other costs. Current market value of the collateral, if necessary, is assessed by accredited appraisers or based on the Group's internal expert estimate, or carrying amount of the collateral including adjustment coefficient (discount). Where the market value of the collateral is assessed as impaired, the borrowers are usually required to provide additional collateral.

Portfolio of loans to banks and customers (less allowance for impairment) by type of collateral is analyzed in Notes 10 and 11.

Maximum exposure to credit risk

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

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

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

Maximum credit risk exposure by credit related commitment represents the whole amount of these commitments (Note 19).

Derivative financial instruments

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

Credit quality per class of financial assets

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

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

(Thousands of euros)

23. Risk management (continued)

Credit risk (continued)

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

The following table provides information on the credit quality of long-term loans to banks and trade financing loans (Note 10) and loans to customers (Note 11) as at 31 December 2016 and 31 December 2015:

2016	*Loan amount*	*Allowance for impairment*	*Loan amount, including allowance for impairment*	*Impairment to loan amount ratio, %*
Trade financing loans without any signs of impairment identified				
Standard loans				
- *Russian Federation*	953	–	953	–
Long-term loans to banks without any signs of impairment identified				
Standard loans				
- *Mongolia*	47,970	–	47,970	–
- *Russian Federation*	26,425	–	26,425	–
- *Socialist Republic of Vietnam*	19,019	–	19,019	–
	94,367	**–**	**94,367**	**–**
Loans to customers without any signs of impairment identified				
Standard loans				
- *Russian Federation*	61,213	–	61,213	–
- *Republic of Bulgaria*	53,477	–	53,477	–
- *Republic of Ecuador*	39,570	–	39,570	–
- *Republic of Panama*	36,276	–	36,276	–
- *Romania*	25,205	–	25,205	–
- *Czech Republic*	22,930	–	22,930	–
- *USA*	6,108	–	6,108	–
- *Mongolia*	5,683	–	5,683	–
- *Slovak Republic*	308	–	308	–
Watch loans to customers				
- *Romania*	15,030	(2,254)	12,776	15.0
Restructured loans				
- *Republic of Bulgaria*	5,779	(289)	5,490	5.0
Uncollectible loans				
- *Slovak Republic*	8,103	(8,103)	–	100
- *Republic of Bulgaria*	6,666	(6,666)	–	100
	286,348	**(17,312)**	**269,036**	**6.0**
Total loans	**380,715**	**(17,312)**	**363,403**	**4.5**

(Thousands of euros)

23. Risk management (continued)

Credit risk (continued)

2015	*Loan amount*	*Allowance for impairment*	*Loan amount, including allowance for impairment*	*Impairment to loan amount ratio, %*
Long-term loans to banks without any signs of impairment identified				
Standard loans				
- *Russian Federation*	64,223	–	64,223	–
- *Mongolia*	43,044	–	43,044	–
- *Socialist Republic of Vietnam*	33,330	–	33,330	–
	140,597	**–**	**140,597**	**–**
Loans to customers without any signs of impairment identified				
Standard loans				
- *Republic of Bulgaria*	51,162	–	51,162	–
- *Russian Federation*	28,160	–	28,160	–
- *Romania*	25,844	–	25,844	–
- *Mongolia*	21,890	–	21,890	–
- *Republic of Ecuador*	18,249	–	18,249	–
- *Slovak Republic*	15,334	–	15,334	–
Uncollectible loans				
- *Slovak Republic*	8,103	(3,000)	5,103	37
- *Republic of Bulgaria*	6,755	(6,755)	–	100
	175,497	**(9,755)**	**165,742**	**5.6**
Total loans	**316,094**	**(9,755)**	**306,339**	**3.1**

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

Impairment assessment

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

Individually assessed allowances

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

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

(Thousands of euros)

23. Risk management (continued)

Liquidity risk

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

Liquidity management is an integral part of general policy for the Group's assets and liabilities management (ALM) and operates within the established limits and restrictions related to management of risks (liquidity, interest rate and currency risk) and the Group's balance sheet items, and in accordance with the documents of strategic, tactical and operating planning.

Procedures for the Group's liquidity position management, ensuring the Group's ability to meet its obligations in full and on a timely basis and efficient resources management, are stipulated in the *Regulations for IIB's Liquidity Position Management* that enables the development of the liquidity position management function provided for by the *IIB's Assets and Liabilities Management Policy*, as an integral part of general function of the Group's management.

Decision making matrix related to liquidity management includes a strategic level of liquidity management (the Council), tactical level (the Board and special-purpose committees) and operational level (responsible structural divisions). In 2015, the Group updated its approaches to the assets and liabilities management.). Asset and Liability Management Department (DUAP or ALM Unit) became responsible for organizing and aligning management of the Group's liquidity position. The Group manages its liquidity position in accordance with planning horizons (up to 6 months) and possible scenarios of movements in liquidity position (stable, stressed).

Main instrument of liquidity position management under the stable scenario is a Plan of cash flows defining the cash flow by balance sheet products/instruments and taking into account the plan of future financial operations. The Group determines the balance sheet gaps, payment schedule and need in financing of future operations based on the Plan of cash flows. As a result of application of these instruments, DUAP issues appropriate recommendations to responsible structural divisions.

The Group has implemented a liquidity buffer to manage the Group's liquidity under the stressed scenario. Application of the liquidity buffer enables the Group to promptly monitor the sustainability and stability of the Group's balance sheet structure in case of liquidity shortage that is critical to the Group's solvency.

The liquidity buffer is formed primarily due to liquidity reserves, namely securities recognized in the Group's balance sheet and included in the Lombard lists of the European Central Bank and Bank of Russia. The Group calculates its liquidity reserves as at the reporting date and for the next six monthly reporting dates (forecast). Liquidity buffer may be used to close the negative net position. As at 31 December 2016, the liquidity buffer amounts to EUR 75.9 mln (31 December 2015: EUR 65.1 mln).

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

	2016	***2015***
Less than 1 month	33,213	52,376
1 to 3 months	3,650	178
3 months to 1 year	6,138	7,254
1 to 5 years	4,934	3,920
Off-balance credit-related commitments	**47,935**	**63,728**

(Thousands of euros)

23. Risk management (continued)

Liquidity risk (continued)

The following table provides an analysis of assets and liabilities on the basis of the remaining period from the reporting date to the contractual maturity date. Quoted available-for-sale debt securities were included in "Less than 1 month" category as they are highly liquid investment securities, which the Group may sell in the short term on the arm-length basis. Available-for-sale investment securities pledged under repurchase agreements are presented on the basis of periods from the reporting date to the expiry date of respective contractual obligations of the Group.

	2016							*2015*							
	Less than 1 month	*1 to 3 months*	*3 months to 1 year*	*1 to 5 years*	*Over 5 years*	*Past due*	*Total*	*Less than 1 month*	*1 to 3 months*	*3 months to 1 year*	*1 to 5 years*	*Over 5 years*	*No stated maturity*	*Past due*	*Total*
Assets															
Cash and cash equivalents	93,031	–	–	–	–	–	**93,031**	59,519	–	–	–	–	–	–	**59,519**
Deposits with banks and other financial institutions	14,254	–	27,472	3,611	–	–	**45,337**	15,352	15,627	54,346	15,067	–	–	–	**100,392**
Derivative financial instruments	–	116	14,246	–	–	–	**14,362**	69	–	1,775	–	–	–	–	**1,844**
Available-for-sale investment securities	170,849	379	502	97,577	–	–	**269,307**	93,027	230	65	22,733	–	4	–	**116,059**
Held-to-maturity investment securities	–	–	–	–	–	–	–	64	972	2,981	76,728	42,483	–	–	**123,228**
Loans to banks	–	3,059	16,638	71,051	3,619	–	**94,367**	–	3,160	41,112	76,374	19,951	–	–	**140,597**
Loans to customers	2,066	10,139	59,833	133,047	63,951	–	**271,290**	982	1,872	26,573	85,268	45,944	–	5,103	**165,742**
Other financial assets	166	123	381	750	–	–	**1,420**	69	81	944	–	–	–	–	**1,094**
Total assets	**280,366**	**13,816**	**119,072**	**306,036**	**67,570**	**–**	**786,860**	**169,082**	**21,942**	**127,796**	**276,170**	**108,378**	**4**	**5,103**	**708,475**
Liabilities															
Due to banks and other financial institutions	(48,558)	–	–	(70,367)	–	–	**(118,925)**	(28,421)	–	(20,196)	(64,756)	–	–	–	**(113,373)**
Current customer accounts	(9,218)	–	–	–	–	–	**(9,218)**	(7,430)	–	–	–	–	–	–	**(7,430)**
Derivative financial instruments	(2,080)	–	(1,671)	(7,872)	–	–	**(11,623)**	–	–	(16,191)	(13,707)	–	–	–	**(29,898)**
Long-term loans of banks	–	–	(14,345)	(59,004)	–	–	**(73,349)**	(102)	–	(24,529)	(19,556)	–	–	–	**(44,187)**
Debt securities issued	–	–	(152,484)	(120,044)	–	–	**(272,528)**	–	–	(40,111)	(172,613)	–	–	–	**(212,724)**
Other financial liabilities	(348)	–	(933)	(582)	–	–	**(1,863)**	(43)	(988)	(32)	–	–	–	–	**(1,063)**
Total liabilities	**(60,204)**	**–**	**(169,433)**	**(257,869)**	**–**	**–**	**(487,506)**	**(35,996)**	**(988)**	**(101,059)**	**(270,632)**	**–**	**–**	**–**	**(408,675)**
Net position	**220,162**	**13,816**	**(50,361)**	**48,167**	**67,570**	**–**	**299,354**	**133,086**	**20,954**	**26,737**	**5,538**	**108,378**	**4**	**5,103**	**299,800**
Accumulated net position	**220,162**	**233,978**	**183,617**	**231,784**	**299,354**	**299,354**		**133,086**	**154,040**	**180,777**	**186,315**	**294,693**	**294,697**	**298,800**	

(Thousands of euros)

23. Risk management (continued)

Analysis of financial liabilities by remaining contractual maturities

The table below summarizes the maturity profile of the Group's financial liabilities at 31 December 2016 and 31 December 2015 based on contractual undiscounted repayment obligations except for gross settled derivatives that are shown by contractual maturity. Debt securities with put options (offers) are presented as if investors will exercise their options at the earliest possible date. The Group expects that it will have to make payment on current bond offers.

At 31 December 2016	*Less than 1 month*	*1 to 3 months*	*3 to 12 months*	*1 to 5 years*	*Total*
Financial liabilities					
Due to banks and other financial institutions	48,590	–	–	73,120	**121,710**
Current customer accounts	–	9,218	–	–	**9,218**
Net settled derivative liabilities	2,080	–	–	–	**2,080**
Gross settled derivative financial instruments					
- Contractual amounts payable	–	47,000	147,836	166,726	**361,562**
- Contractual amounts receivable	–	(47,089)	(173,371)	(173,625)	**(394,085)**
Long-term loans of banks	–	–	15,078	60,989	**76,067**
Debt securities issued	–	–	168,367	128,406	**296,773**
Other liabilities	348	–	933	582	**1,863**
Total undiscounted financial liabilities	**51,018**	**9,129**	**158,843**	**256,198**	**475,188**

At 31 December 2015	*Less than 1 month*	*1 to 3 months*	*3 to 12 months*	*1 to 5 years*	*Total*
Financial liabilities					
Due to banks and other financial institutions	–	28,443	20,293	69,386	**118,122**
Current customer accounts	–	7,430	–	–	**7,430**
Net settled derivative liabilities	(69)	–	–	–	**(69)**
Gross settled derivative financial instruments					
- Contractual amounts payable	–	–	118,408	160,641	**279,049**
- Contractual amounts receivable	–	–	(117,884)	(151,321)	**(269,205)**
Long-term loans of banks	–	–	23,473	22,303	**45,776**
Debt securities issued	–	–	50,936	201,220	**252,156**
Other liabilities	43	988	32	–	**1,063**
Total undiscounted financial liabilities	**(26)**	**36,861**	**95,258**	**302,229**	**434,322**

Market risk

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

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

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

The Finance Committee coordinates the Group's market risk management policy and reviews and provides recommendations on management of market risks to the Management Board.

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

(Thousands of euros)

23. Risk management (continued)

Market risk (continued)

Currency risk and price risk

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

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

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

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

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

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

As at 31 December 2016 and 31 December 2015, final data on value at risk assessment (VaR) in relation to currency and price risks assumed by the Group are represented as follows:

	2016	***2015***
Fixed income securities price risk	2,325	1,536
Currency risk	27	126

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

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

Fluctuations that may occur in the course of the day are not taken into account at calculating value at risk on the basis of the results of a business day.

(Thousands of euros)

23. Risk management (continued)

Market risk (continued)

The Group has assets and liabilities denominated in several foreign currencies. The financial position and the cash flows of the Group are exposed to the effects of fluctuations in the prevailing foreign currency exchange rates. Non-monetary financial instruments and financial instruments denominated in functional currency are not exposed to currency risk.

The Group's exposure to currency risk as at 31 December 2016 and 31 December 2015 is presented below:

	2016					*2015*				
	EUR	***USD***	***RUB***	***Other currencies***	***Total***	***EUR***	***USD***	***RUB***	***Other currencies***	***Total***
Non-derivative financial										
Assets										
Cash and cash equivalents	66,125	19,969	6,778	159	**93,031**	37,363	20,147	1,907	102	**59,519**
Deposits with banks and other financial institutions	40,568	4,769	–	–	**45,337**	99,990	–	402	–	**100,392**
Available-for-sale investment securities	208,628	53,070	7,609	–	**269,307**	89,426	26,633	–	–	**116,059**
Held-to-maturity investment securities	–	–	–	–	–	55,416	63,636	4,176	–	**123,228**
Long-term loans to banks	53,574	40,793	–	–	**94,367**	106,063	34,534	–	–	**140,597**
Loans to customers	131,906	137,130	–	–	**269,036**	124,751	40,991	–	–	**165,742**
Other financial assets	225	14	927	254	**1,420**	483	–	171	440	**1,094**
Total non-derivative financial assets	**501,026**	**255,745**	**15,314**	**413**	**772,498**	**513,492**	**185,941**	**6,656**	**542**	**706,631**
Liabilities										
Due to banks and other financial institutions	(36,981)	(81,944)	–	–	**(118,925)**	(52,785)	(59,706)	(882)	–	**(113,373)**
Current customer accounts	(9,089)	(129)	–	–	**(9,218)**	(7,220)	(210)	–	–	**(7,430)**
Long-term loans of banks	(59,039)	(14,310)	–	–	**(73,349)**	(7,494)	(36,693)	–	–	**(44,187)**
Debt securities issued	(30,046)	–	(151,515)	(90,967)	**(272,528)**	(30,030)	–	(158,099)	(24,595)	**(212,724)**
Other financial liabilities	(529)	(49)	(1,106)	(179)	**(1,863)**	(212)	(1)	(818)	(32)	**(1,063)**
Total non-derivative financial liabilities	**(135,684)**	**(96,432)**	**(152,621)**	**(91,146)**	**(475,883)**	**(97,741)**	**(96,610)**	**(159,799)**	**(24,627)**	**(378,777)**
Net balance sheet position (excluding derivative financial instruments)	**365,342**	**159,313**	**(137,307)**	**(90,733)**	**296,615**	**415,751**	**89,331**	**(153,143)**	**(24,085)**	**327,854**
Derivative financial instruments										
Claims	125,117	–	145,832	90,318	**361,267**	61,068	–	156,879	24,108	**242,055**
Liabilities	(224,955)	(124,785)	(8,788)	–	**(358,528)**	(210,884)	(59,225)	–	–	**(270,109)**
Net balance sheet position including derivative financial instruments	**265,504**	**34,528**	**(263)**	**(415)**	**299,354**	**265,935**	**30,106**	**3,736**	**23**	**299,800**

(Thousands of euros)

23. Risk management (continued)

Market risk (continued)

Interest rate risk

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

The sensitivity of the consolidated income statement is the effect of the assumed changes in interest rates on net interest income for one year, based on financial assets and financial liabilities with floating rates. The sensitivity of equity is calculated by revaluing inactive traded available-for-sale financial assets with fixed rate as at 31 December 2016 for the effects of the assumed changes in interest rates based on the assumption that there are parallel shifts in the yield curve.

	Increase in basis points	***Sensitivity of the income statement***	***Sensitivity of equity***
	2016	***2016***	***2016***
RGBEY	1,00%	(956)	(233)
Libor EUR	0,12%	128	–
Libor USD	0,60%	405	–
3Y Swap-RON	0,50%	(1,148)	–
YTM 5Y USTreasuries	0,70%	973	–
YTM 5Y German Treasuries	0,40%	770	–

	Decrease in basis points	***Sensitivity of the income statement***	***Sensitivity of equity***
	2016	***2016***	***2016***
RGBEY	3,00%	2,868	699
Libor EUR	0,08%	(86)	–
Libor USD	0,08%	(54)	–
3Y Swap-RON	0,50%	1,148	–
YTM 5Y USTreasuries	0,50%	695	–
YTM 5Y German Treasuries	0,40%	(770)	–

	Increase in basis points	***Sensitivity of the income statement***	***Sensitivity of equity***
	2015	***2015***	***2015***
RGBEY	3,75%	(8,419)	–
Libor EUR	0,25%	367	–
Libor USD	0,50%	(49)	–
3Y Swap-RON	0,90%	(621)	–
YTM 5Y USTreasuries	1,00%	358	–
YTM 5Y German Treasuries	0,50%	1,554	–

	Decrease in basis points	***Sensitivity of the income statement***	***Sensitivity of equity***
	2015	***2015***	***2015***
RGBEY	3,75%	8,419	–
Libor EUR	0,25%	(367)	–
Libor USD	0,12%	12	–
3Y Swap-RON	0,90%	621	–
YTM 5Y USTreasuries	0,70%	(250)	–
YTM 5Y German Treasuries	0,50%	(1,554)	–

Indices listed in the tables above:
RGBEY – Russian Government Bonds Effective Yield until Redemption;
Libor EUR –London inter-bank EUR offer rate (3 and 6 months);
Libor USD – London inter-bank USD offer rate (1, 3 and 6 months);
3Y Swap-RON – three-year bid rate in Romanian leu on swap market
YTM 5Y USTreasuries – yield-to-maturity of five-year US Treasuries;
YTM 5Y German Treasuries – yield-to-maturity of five-year Germany Treasuries.

(Thousands of euros)

23. Risk management (continued)

Operational risk

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

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

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

24. Fair value measurements

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

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

Fair value hierarchy

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

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

(Thousands of euros)

24. Fair value measurements (continued)

Fair value hierarchy (continued)

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

	Valuation date	*Level 1 2016*	*Level 2 2016*	*Level 3 2016*	*Total 2016*
Assets measured at fair value					
Derivative financial assets	31 December 2016	–	14,362	–	**14,362**
Government bonds of member countries	31 December 2016	70,561	–	–	**70,561**
Corporate bonds	31 December 2016	194,003	4,739	–	**198,742**
Quoted equity instruments	31 December 2016	–	4	–	**4**
Investment property	31 December 2016	–	–	21,840	**21,840**
Property and equipment – buildings	31 December 2016	–	–	67,527	**67,527**
Liabilities measured at fair value					
Derivative financial liabilities	31 December 2016	–	11,623	–	**11,623**
Assets for which fair values are disclosed					
Cash and cash equivalents	31 December 2016	104	92,927	–	**93,031**
Deposits with banks and other financial institutions	31 December 2016	–	–	45,337	**45,337**
Loans to banks	31 December 2016	–	–	88,558	**88,558**
Loans to customers	31 December 2016	–	–	270,243	**270,243**
Liabilities for which fair values are disclosed					
Due to banks and other financial institutions	31 December 2016	–	–	118,925	**118,925**
Current customer accounts	31 December 2016	–	–	9,218	**9,218**
Long-term loans of banks	31 December 2016	–	–	73,349	**73,349**
Debt securities issued	31 December 2016	–	279,181	–	**279,181**

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(Thousands of euros)

24. Fair value measurements (continued)

Fair value hierarchy (continued)

The following table shows an analysis of financial instruments recorded at fair value by level of the fair value hierarchy as at 31 December 2015:

	Valuation date	*Level 1 2015*	*Level 2 2015*	*Level 3 2015*	*Total 2015*
Assets measured at fair value					
Derivative financial assets	31 December 2015	–	1,844	–	**1,844**
Government bonds of member countries and bonds of regional governments	31 December 2015	114,673	–	–	**114,673**
Corporate bonds	31 December 2015	1,382	–	–	**1,382**
Quoted equity instruments	31 December 2015	–	4	–	**4**
Investment property	31 December 2015	–	–	33,819	**33,819**
Property and equipment – buildings	31 December 2015	–	–	62,807	**62,807**
Liabilities measured at fair value					
Derivative financial liabilities	31 December 2015	–	29,898	–	**29,898**
Assets for which fair values are disclosed					
Cash and cash equivalents	31 December 2015	66	59,453	–	**59,519**
Deposits with banks and other financial institutions	31 December 2015	–	–	100,392	**100,392**
Held-to-maturity investment securities	31 December 2015	114,876	–	–	**114,876**
Long-term loans to banks	31 December 2015	–	–	139,891	**139,891**
Loans to customers	31 December 2015	–	–	165,742	**165,742**
Liabilities for which fair values are disclosed					
Due to banks and other financial institutions	31 December 2015	–	–	113,373	**113,373**
Current customer accounts	31 December 2015	–	–	7,430	**7,430**
Long-term loans of banks	31 December 2015	–	–	44,187	**44,187**
Debt securities issued	31 December 2015	–	214,734	–	**214,734**

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(Thousands of euros)

24. Fair value measurements (continued)

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

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

	Carrying amount 2016	*Fair value 2016*	*Unrecognized gain/(loss) 2016*	*Carrying amount 2015*	*Fair value 2015*	*Unrecognized gain/(loss) 2015*
Financial assets						
Cash and cash equivalents	93,031	93,031	–	59,519	59,519	–
Deposits with banks and other financial institutions	45,337	45,337	–	100,392	100,392	–
Held-to-maturity investment securities	–	–	–	123,228	114,876	(8,352)
Long-term loans to banks	94,367	88,558	(5,809)	140,597	139,891	(706)
Loans to customers	269,036	270,243	1,207	165,742	165,742	–
Financial liabilities						
Due to banks and other financial institutions	118,925	118,925	–	113,373	113,373	–
Current customer accounts	9,218	9,218	–	7,430	7,430	–
Long-term loans of banks	73,349	73,349	–	44,187	44,187	–
Debt securities issued	272,528	279,181	(6,653)	212,724	214,734	(2,010)
Total unrecognized change in unrealized fair value			**(11,255)**			**(11,068)**

Fair value measurements

The Group determines the policies and procedures for both recurring fair value measurement, such as unquoted derivatives, investment property and buildings, and for non-recurring measurement, such as inventories.

External appraisers are involved for valuation of significant assets, such as building and property. Involvement of external appraisers is decided upon by the Group's Finance Department. Unquoted derivatives are measured by the Finance Department.

Selection criteria include market knowledge, reputation, independence and compliance with professional standards.

Methodologies and assumptions

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

Assets for which fair value approximates their carrying amount

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

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

Management has estimated that as at 31 December 2016 and 31 December 2015 the fair value of deposits with banks and other financial institutions, and cash and cash equivalents was not significantly different from their respective carrying amount. This is due to the existing practice of renegotiating interest rates to reflect current market conditions, and, therefore, a majority of balances carries interest at rates approximating market interest rates.

(Thousands of euros)

24. Fair value measurements (continued)

Methodologies and assumptions (continued)

Financial instruments with fixed and floating rate

The fair value of instruments with floating interest rates is approximately equal to their carrying amount. In case of significant changes of the market situation the interest rates on loans to customers and banks, and long-term loans of banks at a fixed interest rate may be revised. Consequently the interest rates on the financial instruments issued or received shortly before the balance sheet date are not significantly different from the current interest rates for new instruments with similar credit risk and a similar maturity. If the Group determines that the rates for loans issued or borrowings are significantly different from the current market rates, the Group determines the fair value of such loans issued and borrowings. The valuation is based on discounted cash flow method using current market interest rates for the financial instruments with similar credit risk and similar maturity. The discount rates depend on the currency, the maturity of the instrument and the credit risk of the counterparty. The Group determines that the fair value of due to banks and other financial institutions and long-term loans of banks did not differ significantly from their carrying amounts as at 31 December 2016 and 31 December 2015.

Investment property

The Group engages an independent appraiser for the investment property fair value measurement. As at the valuation date (31 December 2016), the fair values of investment property were based on the results of valuation performed by an accredited independent appraiser and the prices of market transactions using the market, cost and income approaches to fair value measurement.

The duration of the cash flows and the specific timing of inflows and outflows are determined by events such as rent reviews, lease renewal and related re-letting, redevelopment, or refurbishment. The appropriate duration is typically driven by market behavior that is a characteristic of the class of real property. Periodic cash flow is typically estimated as gross income less vacancy, non-recoverable expenses, collection losses, lease incentives, maintenance cost, agent and commission costs and other operating and management expenses. The series of periodic net operating income, along with an estimate of the terminal value anticipated at the end of the projection period, is then discounted.

Property and equipment - buildings

Fair value of the properties was determined using the market approach. This means that valuations performed by the appraiser are based on market transaction prices, significantly adjusted for difference in the nature, location or condition of the specific property. As at the valuation date (31 December 2016), the properties' fair values are based on valuations performed by an accredited independent appraiser and the prices of market transactions using the market, cost and income approaches to fair value measurement.

Significant unobservable inputs in determining the fair value of real estate properties

As at the valuation date (31 December 2016), the significant unobservable inputs used in determining the fair value of real estate properties included the average asking prices for sale of similar properties ranging from EUR 3,094 per. sq. m (range minimum) to EUR 4,186 per sq. m (range maximum), and lease rates ranging from EUR 371 per sq. m. a year (minimum) to EUR 407 per sq. m. a year (maximum).

There were no transfers of financial instruments between level 1 and level 2 in 2016 and 2015.

(Thousands of euros)

24. Fair value measurements (continued)

Movements in level 3 assets and liabilities at fair value

The following table shows a reconciliation of the opening and closing amount of Level 3 assets and liabilities that are recorded at fair value:

	At 1 January 2016	*Gains/(losses) recorded in profit or loss*	*Gains/(losses) recorded in comprehensive income*	*Purchases*	*Transfer in property and equipment*	*At 31 December 2016*
Assets						
Property and equipment – buildings	62,807	(1,174)	(18,508)	223	24,179	67,527
Investment property	33,819	(2,174)	–	14,374	(24,179)	21,840
Total	**96,626**	**(3,348)**	**(18,508)**	**14,597**	**–**	**89,367**

	At 1 January 2015	*Gains/(losses) recorded in profit or loss*	*Gains/(losses) recorded in comprehensive income*	*Purchases*	*Transfer in property and equipment*	*At 31 December 2015*
Assets						
Property and equipment – buildings	50,739	(935)	(3,642)	52	16,593	62,807
Investment property	52,879	(2,500)	–	33	(16,593)	33,819
Total	**103,618**	**(3,435)**	**(3,642)**	**85**	**–**	**96,626**

25. Transferred financial assets that are not derecognized

The table below provides a summary of the financial assets transferred by the Group in such a way that all the transferred financial assets do not qualify for derecognition:

	Available-for-sale investment securities		*Held-to-maturity investment securities*		
	Government eurobonds	*Corporate bonds*	*Government eurobonds*	*Corporate bonds*	*Total*
Transferred financial asset	***2016***	***2016***	***2016***	***2016***	***2016***
Carrying amount of assets	17,883	80,575	–	–	**98,458**
Carrying amount of associated liabilities	(13,485)	(52,584)	–	–	**(66,069)**
Net position	**4,398**	**27,991**	**–**	**–**	**32,389**

	Available-for-sale investment securities		*Held-to-maturity investment securities*		
	Government bonds of member countries	*Corporate bonds*	*Government bonds of member countries*	*Corporate bonds*	*Total*
Transferred financial asset	***2015***	***2015***	***2015***	***2015***	***2015***
Carrying amount of assets	21,646	1,382	10,489	62,705	**96,222**
Carrying amount of associated liabilities	(16,350)	(930)	(6,998)	(40,478)	**(64,756)**
Net position	**5,296**	**452**	**3,491**	**22,227**	**31,466**

(Thousands of euros)

25. Transferred financial assets that are not derecognized (continued)

Securities sold under repurchase agreements are transferred to a third party and the Group receives cash in exchange. If the securities increase or decrease in value, the Group may, in certain circumstances, require, or be required, to pay additional collateral in the form of cash and/or other securities. The Group has determined that it retains substantially all the risks and rewards of these securities, which include credit risk, market risk, country risk and operational risk, and therefore has not derecognized them. In addition, it recognizes a financial liability for cash received.

The fair value of investment securities available for sale sold under repurchase agreements is equal to their carrying amount (Note 24).

The related liabilities, which are recorded against the cash received for such transactions, are presented in amounts due to banks and other financial institutions in the consolidated statement of financial position as at 31 December 2016 (as at 31 December 2015: in amounts due to banks and other financial institutions).

26. Segment information

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

Credit investment activity	Investment banking services, including long-term corporate and interbank financing
Treasury	Operations in financial markets, transactions with securities, derivative financial instruments and foreign currency, and liquidity management
Other operations	Operational leasing services, other operations

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(Thousands of euros)

26. Segment information (continued)

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

2016	*Credit investment activity*	*Treasury*	*Other operations*	*Total*
Income				
External customers				
Interest income	20,348	12,093	14	**32,455**
Net gains from trading in foreign currencies and operations with derivatives	–	9,068	–	**9,068**
Net gains from revaluation of derivative financial instruments	–	36,679	–	**36,679**
Net gains from available-for-sale investment securities	–	10,515	–	**10,515**
Net gains from held-to-maturity investment securities	–	616	–	**616**
Reversal of allowance for loan impairment	–	–	89	**89**
Income from lease of investment property	–	–	3,442	**3,442**
Reversal of allowance for impairment of other assets	–	–	67	**67**
Other segment income	241	–	430	**671**
Total income	**20,589**	**68,971**	**4,042**	**93,602**
Interest expenses	(11,250)	(16,401)	–	**(27,651)**
Net loss from revaluation of derivative financial instruments	–	(4,349)	–	**(4,349)**
Net losses from revaluation of assets and liabilities in foreign currencies	–	(31,119)	(54)	**(31,173)**
Net losses from revaluation of hedging instruments	–	(246)	–	**(246)**
Allowance for impairment of financial assets	(7,646)	–	–	**(7,646)**
Net losses from revaluation of investment property	–	–	(2,174)	**(2,174)**
Other segment expenses	(167)	(196)	(259)	**(622)**
Segment results	**1,526**	**16,660**	**1,555**	**19,741**
Other unallocated expenses				**(18,939)**
Profit for the period				**802**
Development Portfolio	363,403	68,349	–	**431,752**
Other segment assets	–	353,239	96,425	**449,691**
Total segment assets	**363,403**	**421,588**	**96,425**	**881,443**
Total segment liabilities	**160,065**	**325,579**	**5,581**	**491,225**
Other segment information				
Capital expenditures	–	–	1,065	**1,065**

The Group's management separates the "Development portfolio" assets allocated within operating segments. The criteria of separation is orientation of the assets on the fulfilling of the Group's mission. "Development Portfolio" includes loans to banks and loans to customers excluding impaired loan projects and the investments in debt securities purchased upon initial placement by the issuer..

(Thousands of euros)

26. Segment information (continued)

2015	*Credit investment activity*	*Treasury*	*Other operations*	*Total*
Income				
External customers				
Interest income	15,080	11,904	148	**27,132**
Net gains from revaluation of assets and liabilities in foreign currencies	–	22,614	369	**22,983**
Net gains from available-for-sale investment securities	–	3,204	–	**3,204**
Net gains from held-to-maturity investment securities	–	45	–	**45**
Income from lease of investment property	–	–	5,214	**5,214**
Recovery of provision	–	–	89	**89**
Other segment income	460	–	79	**539**
Total income	**15,540**	**37,767**	**5,899**	**59,206**
Interest expenses	(7,260)	(10,484)	–	**(17,744)**
Net losses from trading in foreign currencies	–	(5,302)	(25)	**(5,327)**
Net losses from revaluation of derivative financial instruments	–	(6,661)	–	**(6,661)**
Net loss from trading in foreign currencies and operations with derivatives	–	(5,302)	–	**(5,302)**
Allowance for loan impairment	(6,166)	–	–	**(6,166)**
Net losses from revaluation of investment property	–	–	(2,500)	**(2,500)**
Other segment expenses	–	(114)	(1,755)	**(1,869)**
Segment results	**2,114**	**15,206**	**1,644**	**18,964**
Other unallocated expenses				**(16,908)**
Profit for the year				**2,056**
Development Portfolio	301,236	–	–	**301,236**
Other segment assets	5,103	400,201	102,863	**508,167**
Total segment assets	**306,339**	**400,201**	**102,863**	**809,403**
Total segment liabilities	**116,138**	**291,474**	**4,088**	**411,700**
Other segment information				
Capital expenditures	–	–	85	**85**

In 2016, the Group's revenue from lease operations with two external counterparties (2015: one external counterparty) exceeded 20% of the Group's total revenue (2016: EUR 2,160 thousand; 2015: EUR 3,196 thousand).

Geographical information

Allocation of the Group's revenue from transactions with external customers and non-current assets based on the location of these customers and assets for the years ended 31 December 2016 and 31 December 2015 is presented in the table below:

	2016				*2015*			
	Russia	*Other member countries*	*Other countries*	*Total*	*Russia*	*Other member countries*	*Other countries*	*Total*
Interest income	7,760	16,095	8,600	**32,455**	12,147	11,721	3,264	**27,132**
Income from lease of investment property	3,442	–	–	**3,442**	5,214	–	–	**5,214**
Non-current assets	79,245	14,439	–	**93,684**	100,212	–	–	**100,212**

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

(Thousands of euros)

26. Segment information (continued)

Geographical information (continued)

The geographical concentration of the Group's assets and liabilities based on the location of the Group's counterparties as at 31 December 2016 is presented below:

	2016									
	Russian Federation	***Republic of Bulgaria***	***Romania***	***Slovak Republic***	***Hungary***	***Mongolia***	***Socialist Republic of Vietnam***	***Czech Republic***	***Other countries***	***Total***
Assets										
Cash and cash equivalents	16,398	808	26	38	–	–	–	–	75,761	**93,031**
Deposits with banks and other financial institutions	7,159	–	–	–	–	–	–	–	38,178	**45,337**
Derivative financial instruments	2,980	–	–	–	–	–	–	–	11,382	**14,362**
Available-for-sale investment securities	44,688	49,482	36,713	10,286	3,475	–	–	–	124,663	**269,307**
Long-term loans to banks and trade financing loans less allowances for impairment	27,378	–	–	–	–	47,970	19,019	–	–	**94,367**
Loans to customers less allowances for impairment	61,213	58,967	37,981	308	–	5,683	–	22,930	81,954	**269,036**
Other financial assets	1,407	8	–	1	–	–	–	–	4	**1,420**
Assets	**161,223**	**109,256**	**74,720**	**10,633**	**3,475**	**53,653**	**19,019**	**22,930**	**331,942**	**786,860**
Liabilities										
Due to banks and other financial institutions	–	–	–	7,508	–	–	–	–	111,417	**118,925**
Derivative financial instruments	4,528	–	633	–	–	–	–	–	6,462	**11,623**
Long-term loans of banks	9,840	21,690	–	–	7,380	–	–	–	34,439	**73,349**
Long-term securities issued	151,434	–	90,967	30,127	–	–	–	–	–	**272,528**
Other financial liabilities	1,805	–	–	19	–	–	–	–	39	**1,863**
Liabilities	**167,607**	**21,690**	**91,600**	**37,654**	**7,380**	**–**	**–**	**–**	**152,357**	**478,288**

(Thousands of euros)

26. Segment information (continued)

Geographical information (continued)

	2015									
	Russian Federation	***Republic of Bulgaria***	***Romania***	***Slovak Republic***	***Hungary***	***Mongolia***	***Socialist Republic of Vietnam***	***Czech Republic***	***Other countries***	***Total***
Assets										
Cash and cash equivalents	2,026	219	17	15	–	–	–	–	57,242	**59,519**
Deposits with banks and other financial institutions	6,049	–	–	–	–	30,539	–	–	63,804	**100,392**
Derivative financial instruments	669	–	–	–	–	–	–	–	1,175	**1,844**
Investment securities:										
- available-for-sale	–	26,889	31,150	13,208	12,056	13,746	11,506	6,118	1,386	**116,059**
- held-to-maturity	105,785	–	–	–	–	–	–	–	17,443	**123,228**
Long-term loans to banks less allowances for impairment	64,223	–	–	–	–	43,044	33,330	–	–	**140,597**
Loans to customers less allowances for impairment	28,160	51,162	25,844	20,437	–	21,890	–	–	18,249	**165,742**
Assets	**206,912**	**78,270**	**57,011**	**33,660**	**12,056**	**109,219**	**44,836**	**6,118**	**159,299**	**707,381**
Liabilities										
Due to banks and other financial institutions	992	–	–	7,508	–	–	–	20,086	84,787	**113,373**
Derivative financial instruments	18,723	–	864	–	–	–	–	–	10,311	**29,898**
Long-term loans of banks	22,953	13,740	–	7,494	–	–	–	–	–	**44,187**
Long-term securities issued	158,067	–	24,557	30,100	–	–	–	–	–	**212,724**
Liabilities	**200,735**	**13,740**	**25,421**	**45,102**	**–**	**–**	**–**	**20,086**	**95,098**	**400,182**

Other countries include non-member countries.

(Thousands of euros)

27. Offsetting of financial instruments

The table below shows the effect of enforceable master netting agreements and similar arrangements that do not result in an offset in the consolidated statement of financial position as at 31 December 2016:

2016	*Gross amount of recognized financial assets*	*Gross amount of recognized financial liabilities set off in the statement of financial position*	*Net amount of financial assets presented in the statement of financial position*	*Related amounts not set off in the statement of financial position*		*Net amount*
				Financial instruments	*Cash collateral received*	
Financial assets						
Financial assets pledged under repurchase agreements	98,458	–	98,458	(66,069)	–	**32,389**
Total	**98,458**	**–**	**98,458**	**(66,069)**	**–**	**32,389**
Financial liabilities						
Repurchase agreements with banks	66,069	–	66,069	(66,069)	–	**–**
Total	**66,069**	**–**	**66,069**	**(66,069)**	**–**	**–**

The table below shows financial assets offset against financial liabilities in the consolidated statement of financial position, as at 31 December 2015 as well as the effect of enforceable master netting agreements and similar arrangements that do not result in an offset in the consolidated statement of financial position:

2015	*Gross amount of recognized financial assets*	*Gross amount of recognized financial liabilities set off in the statement of financial position*	*Net amount of financial assets presented in the statement of financial position*	*Related amounts not set off in the statement of financial position*		*Net amount*
				Financial instruments	*Cash collateral received*	
Financial assets						
Financial assets pledged under repurchase agreements	96,222	–	96,222	(64,756)	–	**31,466**
Total	**96,222**	**–**	**96,222**	**(64,756)**	**–**	**31,466**
Financial liabilities						
Repurchase agreements with banks	64,756	–	64,756	(64,756)	–	**–**
Total	**64,756**	**–**	**64,756**	**(64,756)**	**–**	**–**

(Thousands of euros)

28. Related party disclosures

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

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

The volumes of related party transactions, outstanding balances at the year end, and related expenses and income for 2016 and 2015 are as follows:

		31 December 2016	***31 December 2015***
	Related party	***Carrying amount***	***Carrying amount***
Consolidated statement of financial position			
Current customer accounts	Key management personnel	1,783	1,897
Other non-financial liabilities	Key management personnel	416	493

		2016	***2015***
	Related party	***Income/ (expense)***	***Income/ (expense)***
Consolidated income statement			
Interest expenses on current customer accounts	Key management personnel	(61)	(95)
Net interest expenses after allowance for impairment of loans		**(61)**	**(95)**
Operating expenses		**(61)**	**(95)**
Employee benefits	Key management personnel	(1,365)	(1,524)
Compensation for travel expenses and medical insurance	Key management personnel	(55)	(89)
Operating expenses		**(1,420)**	**(1,613)**
Net (loss)/profit for the year		**(1,481)**	**(1,708)**

29. Capital adequacy

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

The Basel Committee on Banking Supervision recommends maintaining the ratio of capital to risk-weighted assets ("capital adequacy ratio") above the prescribed minimum level. As at 31 December 2016, this minimum level was 8% (2015: 8%).

Besides, taking into account the Bank's status as the multilateral development institution and the structure of the Bank's member countries and respective decision of the Council, the capital adequacy ratio was set for the Group at the level of not less than 25% as at 31 December 2016 (2015: 25%).

(Thousands of euros)

29. Capital adequacy (continued)

The following table shows the composition of the Group's capital position computed in accordance with the Basel Accord (Basel II) as at 31 December 2016 and 31 December 2015.

	2016	*2015*
Capital		
Tier 1 capital	378,034	365,978
Tier 2 capital	11,439	29,789
Total regulatory capital	**389,473**	**395,767**
Risk-weighted assets		
Credit risk	482,693	560,094
Market risk	186,588	70,461
Operational risk	57,999	55,548
Total risk-weighted assets	**727,280**	**686,103**
Total capital expressed as a percentage of risk-weighted assets, % ("capital adequacy ratio")	53.55%	57.68%
Total tier 1 capital expressed as a percentage of risk-weighted assets, % ("tier 1 capital adequacy ratio-")	51.98%	53.34%

(The end)