

**European Bank
for Reconstruction and Development**

The Italian Investment Special Fund

**Annual Financial Report
31 December 2006**

European Bank for Reconstruction and Development

The Italian Investment Special Fund

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Income statement For the year ended 31 December 2006	Note	Year to 31 December 2006 €000	Year to 31 December 2005 €000
Interest and similar income			
From loans		248	321
Other interest		605	395
Net (losses)/gains from share investments at fair value through profit or loss	4	(29)	714
Foreign exchange (loss)/gain		(328)	834
Other operating expenses	5	(7)	(7)
Operating profit before provisions		489	2,257
Provisions for impairment of loan investments and guarantees	6	217	158
Net profit for the year		706	2,415

Balance sheet At 31 December 2006	Note	31 December 2006 €000	31 December 2005 €000
Assets			
Placements with credit institutions		22,414	19,412
Other assets	7	179	150
Loan investments			
Loans	8	2,105	4,510
Less: Provisions for impairment	6	(569)	(1,372)
		1,536	3,138
Share investments			
Share investments at fair value through profit or loss	9	522	733
Total assets		24,651	23,433
Liabilities and contributor's resources			
Other liabilities	10	7	7
Provisions for impairment of guaranteed parallel investments	6	2,306	1,794
Total liabilities		2,313	1,801
Contributions	11	21,915	21,915
Reserves and retained earnings		423	(283)
Total contributor's resources		22,338	21,632
Total liabilities and contributor's resources		24,651	23,433

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Statement of changes in contributor's resources For the year ended 31 December 2006

	Contributions	General reserve	Accumulated loss	Total
	€000	€000	€000	€000
At 31 December 2004	21,935	-	(3,353)	18,582
Transitional restatement of opening balances for fair value of share investments	-	655	-	655
At 1 January 2005	21,935	655	(3,353)	19,237
Contributions refunded	(20)	-	-	(20)
Profit for the year	-	-	2,415	2,415
At 31 December 2005	21,915	655	(938)	21,632
Profit for the year	-	-	706	706
At 31 December 2006	21,915	655	(232)	22,338

Statement of cash flows For the year ended 31 December 2006

	Year to 31 December 2006	Year to 31 December 2005
	€000	€000
Cash flows from operating activities		
Net profit for the year	706	2,415
Adjustment for:		
Net losses/(gains) from share investments at fair value through profit or loss	29	(714)
Provisions for impairment of loan investments and guarantees	(217)	(158)
Foreign exchange	328	(834)
Net profit before changes in operating assets	846	709
(Increase)/decrease in operating assets:		
Interest receivable	(29)	10
Funds advanced for loans	(1,632)	(1,482)
Proceeds from repayment of loans	4,037	4,635
Proceeds from sale of share investments	182	636
Decrease in operating liabilities		
Accrued expenses	-	(128)
Net cash from operating activities	3,404	4,380
Cash flows from financing activities		
Contributions refunded	-	(20)
Net cash from financing activities	-	(20)
Net increase in cash and cash equivalents	3,404	4,360
Cash and cash equivalents at beginning of year	19,412	14,218
Effect of foreign exchange rate changes	(402)	834
Cash and cash equivalents at 31 December	22,414	19,412

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Notes to the financial statements

1 Creation of the Special Fund

The creation of The Italian Investment Special Fund ("the Fund") was approved by the Board of Directors ("the Board") of the European Bank for Reconstruction and Development ("the Bank") at its meeting of 15/16 September 1998 and is administered, *inter alia*, under the terms of Rules and Regulations of such Special Fund approved by the Board on that date. The Fund became operational on 19 January 2000 following the receipt of the first contribution.

The Fund was established in accordance with Article 18 of the agreement establishing the Bank. The objective of the Fund is to assist the modernisation, restructuring, expansion and development of small and medium size enterprises in certain countries of operations of the Bank.

The Fund is separated into five Sub-Accounts: The Albania Reconstruction Equity Fund Sub-Account ("AREF"), The Bosnia and Herzegovina SME Framework Sub-Account ("BiH SME"), The Kosovo Reconstruction Equity Fund Sub-Account ("KREF"), The Serbia and Montenegro Risk Sharing Facility ("S&M RSF") and The Western Balkans Local Enterprise Facility ("WB LEF").

2 President's responsibilities

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

3 Accounting policies

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

i Basis of preparation

These financial statements have been prepared in accordance with International Financial Reporting Standards (IFRS) as issued by the International Accounting Standards Board (IASB) and the overall principles of the European Community's Council Directive on Annual Accounts and Consolidated Accounts of Banks and Other Financial Institutions. The financial statements have been prepared under the historical cost convention, as modified by the revaluation of financial assets held at fair value through profit or loss.

The preparation of financial statements in conformity with IFRS requires the use of certain critical accounting estimates. It also requires management to exercise its judgement in the process of applying the Fund's policies. The areas involving a higher degree of judgement or complexity, or areas where assumptions and estimates are significant to the financial statements are disclosed below in "critical accounting estimates and judgements".

ii Significant changes in the financial statements

Amendments to published standards effective in 2006

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

This amendment requires issued financial guarantees to be initially recognised at their fair value, and subsequently measured at the higher of the unamortised balance of the related fees received and deferred, and the expenditure required to settle the commitment at the balance sheet date. The Fund resources are used to guarantee the principal losses of the Bank's investments in which the Fund makes a parallel investment. In the case of share investments, the Fund also guarantees a preferential rate of return to the Bank up to a particular hurdle rate. The Fund receives no benefit for being a party to these guarantees, i.e. no fees are received and there are no preferential lending arrangements on behalf of the Fund where parallel lending exists. As there is no implied value of these guarantees to the Fund, they are deemed outside of the scope of IAS 39. Any subsequent provisioning is determined under IAS 37 Provisions, Contingent Liabilities and Contingent Assets.

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Notes to the financial statements (continued)

3 Accounting policies (continued)

IAS 39 (Amendment), The Fair Value Option

This amendment permits the irrevocable designation on initial recognition of financial instruments that meet certain conditions as ones to be measured at fair value through profit or loss. The conditions that are required to be met under the amendment are where such designation eliminates or significantly reduces an accounting mismatch, when a group of financial assets, financial liabilities or both are managed and their performance is evaluated on a fair value basis in accordance with a documented risk management or investment strategy, and when an instrument contains an embedded derivative that meets particular conditions. From 1 January 2005 the Fund has designated its associate share investments and high-risk equity funds at fair value through profit or loss as the performance of these assets is managed on a fair value basis in accordance with the Bank's risk management and accounting policies.

Standards early adopted by the Fund

No standards were early adopted by the Fund in 2006.

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

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

- IAS 19 (Amendment), Employee Benefits;
- IAS 21 (Amendment), Net Investment in a Foreign Operation;
- IAS 39 (Amendment), Cash Flow Hedge Accounting for Forecast Intragroup Transactions;
- IFRS 1 (Amendment), First-Time Adoption of International Financial Reporting Standards;
- IFRS 6, Exploration for and Evaluation of Mineral Resources;
- IFRIC 4, Determining whether an Arrangement contains a Lease;
- IFRIC 5, Rights to Interests arising from Decommissioning, Restoration and Environmental Rehabilitation Funds; and
- IFRIC 6, Liabilities arising from Participating in a Specific Market – Waste Electrical and Electronic Equipment.

Standards that are not yet effective and have not been early adopted by the Fund

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

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

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

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Notes to the financial statements (continued)

3 Accounting policies (continued)

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

IFRS 8 requires an entity to report financial and descriptive information about its reportable segments. Reportable segments are operating segments or aggregations of operating segments that meet specified criteria. Operating segments are components of an entity about which separate financial information is available that is evaluated regularly by the chief operating decision maker in deciding how to allocate resources and in assessing performance. Generally, financial information is required to be reported on the basis that it is used internally for evaluating operating segment performance and deciding how to allocate resources to operating segments. The Fund has assessed the impact of IFRS 8 and concluded that it is not expected to impact the operating segments of the Fund and that the main additional disclosures will be in relation to the determination and measurement of the Fund's operating segments. The Fund will apply IFRS 8 from its annual period beginning 1 January 2009.

Interpretations to existing standards that are not yet effective and not relevant for the Fund's operations

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

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

Changes in critical accounting policies, accounting estimates and judgements in the prior period

International Accounting Standard 28, Investments in Associates (IAS 28 Revised 2005)

Prior to 2005 all share investments were accounted for as available-for-sale financial assets as the Fund did not issue consolidated financial statements under the requirements of the previous IAS 28. As of 1 January 2005, the Fund applied the exemption for venture capital organisations under IAS 28 Revised 2005. This permitted the Fund to designate share investments, previously held as available-for-sale, as financial assets at fair value through profit or loss. The Fund has chosen to designate all high risk equity fund share investments as financial assets at fair value through profit or loss with changes in fair value included in the income statement.

Prior to 2005 the Bank could not reliably measure the fair value of the Fund's unlisted share investments and as such it was impracticable to restate 2004 comparatives for unlisted associate share investments.

Fair valuation of unlisted share investments

Prior to 2005, the Bank valued the Fund's unlisted share investments at historic cost, less any provisions for impairment. In 2005 the Bank performed an assessment of the fair value of the share investment portfolio as at 1 January 2005 and 31 December 2005. As a result of the assessment the Bank enhanced its valuation techniques so that unlisted equity could be measured at fair value.

As fair value could not be reliably measured prior to 2005 it was impracticable to restate 2004 comparatives for unlisted share investments. At 1 January 2005 the Fund released specific provisions for the identified impairment of share investments, totalling €2,031,000, to reserves. In addition the Fund restated all unlisted share investments to fair value resulting in a reduction to the Fund's reserves of €1,376,000. The total impact on the Fund's opening reserves was a net increase of €655,000.

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Notes to the financial statements (continued)

3 Accounting policies (continued)

iii Significant accounting policies

Financial assets

Loan investments

Loans originated by the Fund are measured at amortised cost using the effective yield method less any provision for impairment or uncollectibility. Loans are recognised at settlement date.

Financial assets at fair value through profit or loss

This category comprises the Fund's high risk equity fund share investments. Such assets are measured at fair value on the balance sheet with changes in fair value recorded in the income statement. The basis of fair value for unlisted share investments is determined using valuation techniques appropriate to the market and industry of each investment. Purchases and sales of share investments are recorded at trade date. Note 10 analyses unlisted share investments.

Provisions for impairment of loan investments

Where there is objective evidence that an identified loan is impaired, specific provisions for impairment are recognised in the income statement. Impairment is defined as the difference between the carrying value of the asset and the net present value of expected future cash flows, determined using the instrument's original effective interest rate where applicable. The Bank's Risk Management Vice Presidency normally reviews assets for impairment every six months, and sometimes more frequently. Resulting adjustments include the unwinding of the discount in the income statement over the life of the asset, and any adjustments required in respect of a reassessment of the initial impairment.

Provisions for impairment of classes of similar assets that are not individually identified as impaired are calculated on a portfolio basis. The methodology used for assessing such impairment is based on a risk-rated approach for non-sovereign assets applied in the month of disbursement. The effect of applying the Fund's methodology is considered to approximate to the calculation of impairment on an incurred loss basis, being the difference between the carrying value of the groups of similar assets and the net present value of their expected future cash flows. Impairment, as determined above, is deducted from the asset categories on the balance sheet.

Impairment, less any amounts reversed during the year, is charged to the income statement under the caption "provisions for impairment of loan investments", as summarised in note 6. When a loan is deemed uncollectable the principal is written off against the related estimated impairment. Subsequent recoveries are credited to the income statement if previously written off.

Financial guarantees

The Fund resources are used to guarantee the principal losses of the Bank's investments in which the Fund makes a parallel investment. In the case of share investments, the Fund also guarantees a preferential rate of return to the Bank up to a particular hurdle rate. The Fund receives no benefit for being a party to these guarantees, i.e. no fees are received and there are no preferential lending arrangements on behalf of the Fund where parallel lending exists. As there is no implied value of these guarantees to the Fund, they are deemed outside of the scope of IAS 39.

Any subsequent provisioning is determined under IAS 37 Provisions, Contingent Liabilities and Contingent Assets upon consideration of objective evidence that the guarantee is impaired and is recognised when it is both probable that the guarantee will require to be settled and that the settlement amount can be reliably estimated. Such provisions are included in "provisions for impairment of guaranteed parallel investments" on the balance sheet.

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Notes to the financial statements (continued)

3 Accounting policies (continued)

iv Critical accounting estimates and judgements

Estimates and judgements are continually evaluated and are based on historical experience and other factors, including expectations of future events that are believed to be reasonable under the circumstances. Preparing financial statements in conformity with IFRS requires the Fund to make estimates and assumptions that affect the reported amounts of assets and liabilities at the date of the financial statements and the reported amounts included in the income statement during the reporting period.

The estimates and assumptions that have a significant risk of causing a material adjustment to the carrying amounts of assets and liabilities within the next financial year are as follows:

- fair value of available-for-sale share investments and share investments at fair value through profit or loss; and
- provisions for impairment of loan investments.

These estimates are highly dependent on a number of variables which reflect the economic environment and financial markets of the Fund's countries of operations but which are not directly correlated to market risks such as interest rate and foreign exchange risk. The resultant volatility, combined with a lack of comparable information in relation to the Fund's banking portfolio, limits the Fund's ability to apply traditional sensitivity analysis methods.

The methodology and assumptions used for estimating provisions for the impairment of loan investments are reviewed regularly to reduce any differences between loss estimates and actual experience.

v Foreign currencies

The unit of measurement for the presentation of the financial statements of the Fund is euro (€). Monetary assets and liabilities denominated in foreign currencies are translated into euro at spot rates as at 31 December 2006. Non-monetary items are expressed in euro at the exchange rates ruling at the time of the transaction. Revenue and expense items are translated into euro at the exchange rate on the date on which they occurred. Exchange gains or losses arising from the translation of assets, liabilities and transactions during the year are taken to the income statement.

vi Interest, fees, commissions and dividends

Interest is recorded on an accruals basis using the effective yield method. Interest is recognised on impaired loans through unwinding the discount used in the present value calculations applied to expected future cash flows.

Commitment fees are deferred in accordance with IAS 18, together with the related direct costs of originating and maintaining the commitment, and are recognised in interest income over the period from disbursement to repayment of the related loan. If the commitment expires without the loan being drawn down, the fee is recognised as income on expiry.

Dividends relating to share investments are recognised when received.

vii Contributions

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

viii Cash and cash equivalents

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

ix Taxation

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

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Notes to the financial statements (continued)

3 Accounting policies (continued)

x Comparatives

Where necessary, comparative figures have been adjusted to conform with changes in presentation in the current year.

4 Net (losses)/gains from share investments at fair value through profit or loss

	2006	2005
	€000	€000
Net unrealised (losses)/gains from associate share investments	(29)	714
Net (losses)/gains from share investments at fair value through profit or loss	(29)	714

5 Other operating expenses

Other operating expenses comprise administrative expenses directly related to the Fund and includes external auditors' remuneration of €7,400 (2005: €7,100).

6 Provisions for impairment of loan investments and guarantees

	Loans	Guarantees	Total	Loans	Guarantees	Total
	€000	€000	€000	€000	€000	€000
(Release)/charge for the year						
Portfolio provisions for the unidentified impairment of assets						
Non-sovereign risk assets	(803)	-	(803)	447	-	447
Specific provisions for the identified impairment of assets:						
Non-sovereign risk assets	-	586	586	-	(605)	(605)
Provisions for impairment of loan investments and guarantees	(803)	586	(217)	447	(605)	(158)

	Loans	Guarantees	Total	Loans	Guarantees	Total
	€000	€000	€000	€000	€000	€000
Movement in provisions						
At 1 January	1,372	1,794	3,166	925	2,399	3,324
(Release)/charge for the year	(803)	586	(217)	447	(605)	(158)
Effect of foreign exchange rate changes	-	(74)	(74)	-	-	-
At 31 December	569	2,306	2,875	1,372	1,794	3,166

Analysed between:

Portfolio provision for the unidentified impairment of assets:						
Non-sovereign risk assets	569	-	569	1,372	-	1,372
Deducted from assets	569	-	569	1,372	-	1,372
Provisions for impairment of guaranteed parallel investments	-	2,306	2,306	-	1,794	1,794
At 31 December	569	2,306	2,875	1,372	1,794	3,166

7 Other assets

	2006	2005
	€000	€000
Interest receivable on placements	166	88
Interest receivable on loans	13	62
At 31 Decemeber	179	150

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Notes to the financial statements (continued)

8 Loan investments

	2006	2005
	€000	€000
At 1 January	4,510	7,663
Disbursements	1,632	1,482
Repayments and prepayments	(4,037)	(4,635)
At 31 December	2,105	4,510
Impairment at 31 December (note 6)	(569)	(1,372)
Total loan investments net of impairment at 31 December	1,536	3,138
Undrawn commitments		
At 31 December	1,080	1,613

Loans are for projects in Bosnia and Herzegovina, Serbia, Montenegro and the Western Balkans.

9 Share investments at fair value through profit or loss

Operating assets	€000
At 1 January 2005	2,031
Disposals at cost	(636)
At 1 January 2006	1,395
Disposals at cost	(182)
At 31 December 2006	1,213
Fair value adjustment	€000
At 1 January 2005	(1,376)
Movement in fair value revaluation	714
At 1 January 2006	(662)
Movement in fair value revaluation	(29)
At 31 December 2006	(691)
Fair value at 31 December 2006	522
Fair value at 31 December 2005	733
Undrawn commitments	
At 31 December 2006	-
At 31 December 2005	2

Share investments are for projects in Albania and Kosovo.

10 Other liabilities

	2006	2005
	€000	€000
Audit fees payable	7	7
At 31 December	7	7

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Notes to the financial statements (continued)

11 Contributions

Contributions received from the Italian Government are set out below:

	2006	2005
Sub-Account	€000	€000
AREF	701	6,035
BiH SME	5,400	5,400
KREF	1,980	1,980
S&M RSF	4,500	8,500
WB LEF	9,334	-
At 31 December	21,915	21,915

On 5 April 2006 the Contributor pledged €10,000,000 to be financed from the resources of the S&M RSF and AREF subaccounts when they become available. As at 31 December 2006 contributions of €4,000,000 and €5,334,000 had been transferred to the WB LEF from S&M RSF and AREF respectively.

12 Net currency position

	Euro	United States dollars	Other currencies	Total
	€000	€000	€000	€000
Net currency position at 31 December 2006				
Assets				
Placements with credit institutions	20,755	1,659	-	22,414
Other assets	172	7	-	179
Loans	2,105	-	-	2,105
Provisions for impairment of loan investments	(569)	-	-	(569)
Share investments at fair value through profit or loss	-	-	522	522
Total assets	22,463	1,666	522	24,651
Liabilities and contributor's resources				
Other liabilities	(7)	-	-	(7)
Provisions for impairment of guaranteed parallel investments	(1,480)	(826)	-	(2,306)
Total contributor's resources	(21,427)	(911)	-	(22,338)
Total liabilities and contributor's resources	(22,914)	(1,737)	-	(24,651)
Net currency position at 31 December 2006	(451)	(71)	522	-

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Notes to the financial statements (continued)

12 Net currency position (continued)

	Euro	United States dollars	Other currencies	Total
	€000	€000	€000	€000
Net currency position at 31 December 2005				
Assets				
Placements with credit institutions	12,597	6,815	-	19,412
Other assets	129	21	-	150
Loans	4,510	-	-	4,510
Provisions for impairment of loan investments	(1,372)	-	-	(1,372)
Share investments at fair value through profit or loss	-	-	733	733
Total assets	15,864	6,836	733	23,433
Liabilities and contributor's resources				
Other liabilities	(7)	-	-	(7)
Provisions for impairment of guaranteed parallel investments	(1,060)	(734)	-	(1,794)
Total contributor's resources	(15,300)	(6,332)	-	(21,632)
Total liabilities and contributor's resources	(16,367)	(7,066)	-	(23,433)
Net currency position at 31 December 2005	(503)	(230)	733	-

The Fund uses the euro as the unit of measurement for the presentation of its financial statements but the activities and resources of the AREF are denominated in United States dollars. The exchange rate used for the conversion of assets and liabilities denominated in United States dollars into euro at 31 December 2006, where appropriate, was 1.3168 (2005: 1.1830).

13 Liquidity position

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

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

The Italian Investment Special Fund

Notes to the financial statements (continued)

13 Liquidity position (continued)

	Up to and including 1 month	Over 1 month and up to and including 3 months	Over 3 months and up to and including 1 year	Over 1 year and up to and including 5 years	Maturity undefined	Total
	€000	€000	€000	€000	€000	€000
Liquidity position at 31 December 2006						
Assets						
Placements with credit institutions	22,414	-	-	-	-	22,414
Other assets	168	2	9	-	-	179
Loans	-	85	-	450	1,570	2,105
Provisions for impairment of loan investments	-	(4)	-	(130)	(435)	(569)
Share investments at fair value through profit or loss	-	-	-	-	522	522
Total assets	22,582	83	9	320	1,657	24,651
Liabilities and contributor's resources						
Other liabilities	-	(7)	-	-	-	(7)
Provisions for impairment of guaranteed parallel investments	-	-	-	-	(2,306)	(2,306)
Total contributor's resources	-	-	-	-	(22,338)	(22,338)
Total liabilities and contributor's resources	-	(7)	-	-	(24,644)	(24,651)
Net liquidity position at 31 December 2006	22,582	76	9	320	(22,987)	-
Cumulative net liquidity position at 31 December 2006	22,582	22,658	22,667	22,987	-	-

	Up to and including 1 month	Over 1 month and up to and including 3 months	Over 3 months and up to and including 1 year	Over 1 year and up to and including 5 years	Maturity undefined	Total
	€000	€000	€000	€000	€000	€000
Liquidity position at 31 December 2005						
Assets						
Placements with credit institutions	19,412	-	-	-	-	19,412
Other assets	93	54	3	-	-	150
Loans	-	-	1,467	2,655	388	4,510
Provisions for impairment of loan investments	-	-	(376)	(860)	(136)	(1,372)
Share investments at fair value through profit or loss	-	-	-	-	733	733
Total assets	19,505	54	1,094	1,795	985	23,433
Liabilities and contributor's resources						
Other liabilities	-	(7)	-	-	-	(7)
Provisions for impairment of guaranteed parallel investments	-	-	-	-	(1,794)	(1,794)
Total contributor's resources	-	-	-	-	(21,632)	(21,632)
Total liabilities and contributor's resources	-	(7)	-	-	(23,426)	(23,433)
Net liquidity position at 31 December 2005	19,505	47	1,094	1,795	(22,441)	-
Cumulative net liquidity position at 31 December 2005	19,505	19,552	20,646	22,441	-	-

14 Interest rate risk

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

The Italian Investment Special Fund

Notes to the financial statements (continued)

14 Interest rate risk (continued)

	Up to and including 1 month €000	Over 1 month and up to and including 3 month €000	Over 3 months and up to and including 1 year €000	Non-interest- bearing funds €000	Total €000
Interest rate risk at 31 December 2006					
Assets					
Placements with credit institutions	22,414	-	-	-	22,414
Other assets	-	-	-	179	179
Loans	450	85	1,570	-	2,105
Provisions for impairment of loan investments	-	-	-	(569)	(569)
Share investments at fair value through profit or loss	-	-	-	522	522
Total assets	22,864	85	1,570	132	24,651
Liabilities and contributor's resources					
Other liabilities	-	-	-	(7)	(7)
Provisions for impairment of guaranteed parallel investments	-	-	-	(2,306)	(2,306)
Total contributor's resources	-	-	-	(22,338)	(22,338)
Total liabilities and contributor's resources	-	-	-	(24,651)	(24,651)
Interest sensitivity gap at 31 December 2006	22,864	85	1,570	(24,519)	-

	Up to and including 1 month €000	Over 1 month and up to and including 3 month €000	Over 3 months and up to and including 1 year €000	Non-interest- bearing funds €000	Total €000
Interest rate risk at 31 December 2005					
Assets					
Placements with credit institutions	19,412	-	-	-	19,412
Other assets	-	-	-	150	150
Loans	1,000	2,995	515	-	4,510
Provisions for impairment of loan investments	-	-	-	(1,372)	(1,372)
Share investments at fair value through profit or loss	-	-	-	733	733
Total assets	20,412	2,995	515	(489)	23,433
Liabilities and contributor's resources					
Other liabilities	-	-	-	(7)	(7)
Provisions for impairment of guaranteed parallel investments	-	-	-	(1,794)	(1,794)
Total contributor's resources	-	-	-	(21,632)	(21,632)
Total liabilities and contributor's resources	-	-	-	(23,433)	(23,433)
Interest sensitivity gap at 31 December 2005	20,412	2,995	515	(23,922)	-

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

	United		United	
	Euro 2006 %	States dollars 2006 %	Euro 2005 %	States dollars 2005 %
Assets				
Placements with credit institutions	2.76	4.30	1.99	2.78
Loans	6.83	-	5.67	-

The Italian Investment Special Fund

Notes to the financial statements (continued)

15 Fair value of financial assets and liabilities

The carrying amounts of financial assets and liabilities presented on the balance sheet approximate to their fair value.

16 Segment information

In accordance with IAS 14, the primary segment of the Fund is Sub-Account and the secondary segment is business operation.

At 31 December 2006, the activities of the Fund comprised five Sub-Accounts and a single secondary segment (Banking operations).

The results for the year and the assets and liabilities of the five Sub-Accounts are as follows:

Income statement	AREF	BiH SME	KREF	S&M RSF	WB LEF	Combined Fund
For the year ended 31 December 2006	€000	€000	€000	€000	€000	€000
Interest and similar income	139	194	43	307	170	853
Net gains from share investments at fair value through profit or loss	(64)	-	35	-	-	(29)
Foreign exchange	6	-	-	-	(334)	(328)
Other operating expenses	(1)	(2)	(2)	(1)	(1)	(7)
Operating profit before provisions	80	192	76	306	(165)	489
Provisions for impairment of loan investments and guarantees	(167)	32	(420)	902	(130)	217
Net (loss)/profit for the year	(87)	224	(344)	1,208	(295)	706

Balance sheet	AREF	BiH SME	KREF	S&M RSF	WB LEF	Combined Fund
At 31 December 2006	€000	€000	€000	€000	€000	€000
Assets						
Placements with credit institutions	1,659	6,683	1,609	3,820	8,643	22,414
Other assets	7	57	13	25	77	179
Loans	-	85	-	1,570	450	2,105
Provisions for impairment	-	(4)	-	(435)	(130)	(569)
Share investments at fair value through profit or loss	72	-	450	-	-	522
Total assets	1,738	6,821	2,072	4,980	9,040	24,651
Liabilities and contributor's resources						
Other liabilities	(1)	(2)	(2)	(1)	(1)	(7)
Provisions for impairment of guaranteed parallel investments	(826)	-	(1,480)	-	-	(2,306)
Total contributor's resources	(911)	(6,819)	(590)	(4,979)	(9,039)	(22,338)
Total liabilities and contributor's resources	(1,738)	(6,821)	(2,072)	(4,980)	(9,040)	(24,651)

Income statement	AREF	BiH SME	KREF	S&M RSF	WB LEF	Combined Fund
For the year ended 31 December 2005	€000	€000	€000	€000	€000	€000
Interest and similar income	172	159	29	356	-	716
Net gains from share investments at fair value through profit or loss	167	-	547	-	-	714
Foreign exchange	834	-	-	-	-	834
Other operating expenses	(2)	(1)	(2)	(2)	-	(7)
Operating profit before provisions	1,171	158	574	354	-	2,257
Provisions for impairment of loan investments and guarantees	580	153	24	(599)	-	158
Net profit/(loss) for the year	1,751	311	598	(245)	-	2,415

The Italian Investment Special Fund

Notes to the financial statements (continued)

16 Segment information (continued)

Balance sheet	AREF	BiH SME	KREF	S&M RSF	WB LEF	Combined Fund
At 31 December 2005	€000	€000	€000	€000	€000	€000
Assets						
Placements with credit institutions	6,815	5,870	1,486	5,241	-	19,412
Other assets	21	40	8	81	-	150
Loans	-	722	-	3,788	-	4,510
Provisions for impairment	-	(35)	-	(1,337)	-	(1,372)
Share investments at fair value through profit or loss	231	-	502	-	-	733
Total assets	7,067	6,597	1,996	7,773	-	23,433
Liabilities and contributor's resources						
Other liabilities	(1)	(2)	(2)	(2)	-	(7)
Provisions for impairment of guaranteed parallel investments	(734)	-	(1,060)	-	-	(1,794)
Total contributor's resources	(6,332)	(6,595)	(934)	(7,771)	-	(21,632)
Total liabilities and contributor's resources	(7,067)	(6,597)	(1,996)	(7,773)	-	(23,433)

17 Guarantees

At 31 December 2006, the Bank had outstanding loans amounting to €0.2 million (2005: €1.4 million) under BiH SME, for which, in the event of a future default, losses incurred by the Bank may be refunded in part from the resources of the BiH SME sub-account of the Fund. At 31 December 2006, the Fund's maximum exposure under such guarantees was €0.2 million (2005: €1.4 million).

At 31 December 2006, the Bank had outstanding loans amounting to €1.0 million (2005: €17.8 million) under S&M RSF, for which, in the event of a future default, losses incurred by the Bank may be refunded in part from the resources of the S&M RSF sub-account of the Fund. At 31 December 2006, the Fund's maximum exposure under such guarantees was €1.6 million (2005: €3.8 million).

At 31 December 2006, the Bank had outstanding loans amounting to €1.0 million (2005: nil) under WB LEF, for which, in the event of a future default, losses incurred by the Bank may be refunded in part from the resources of the WB LEF sub-account of the Fund. At 31 December 2006, the Fund's maximum exposure under such guarantees was €0.5 million (2005: nil).

18 Post balance sheet events

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

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

Report on the Financial Statements

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

President's responsibility for the financial statements

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

Auditor's responsibility

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

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

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

Opinion

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

Other matters

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

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

A handwritten signature in black ink that reads "PricewaterhouseCoopers LLP". The signature is written in a cursive, flowing style.

PricewaterhouseCoopers LLP
Chartered Accountants and Registered Auditors
London

6 March 2007

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