

**FUND FOR LOCAL AUTHORITIES AND
GOVERNMENTS IN BULGARIA – FLAG JSC**

ANNUAL DIRECTORS' REPORT AND
INDIVIDUAL FINANCIAL STATEMENTS
31 December 2016

FUND FOR LOCAL AUTHORITIES AND GOVERNMENTS IN BULGARIA – FLAG JSC

Table of Contents

General information	1
Directors' report.....	2
Individual Statement of Comprehensive Income	19
Individual Statement of Financial Position	20
Individual Statement of Changes in Equity	21
Individual Cash flow statement	22
Notes to the individual Financial Statements	
1. Corporate information.....	23
2.1 Basis of preparation	23
2.2 Summary of significant accounting policies	25
3. Income and expenses	32
4. Income tax	33
5. Cash and cash equivalents	34
6. Receivables and prepayments	34
7. Plant and equipment, software	35
8. Investment in subsidiary	35
9. Loans granted.....	36
10. Loans payable	37
11. Payroll and social securities payables	38
12. Income tax receivable (payable)	38
13. Other liabilities	38
14. Share capital and reserves.....	38
15. Dividend distribution	39
16. Commitments and contingencies	39
17. Related party disclosures	39
18. Financial risk management objectives and policy.....	40
19. Financial instruments	43
20. Events after the reporting period.....	44
Independent Auditor's Report to the sole shareholder of FLAG JSC	

General information

Board of directors:

Dobromir Prodanov Simidchiev - Chairperson
Plamen Todorov Iliev – member
Malina Valentinova Krumova - member
Larisa Manastirli - member
Nadya Yordanova Dankinova – member and Executive director
Maria Blagoeva Lazarova– member
Yulia Petkova Tsolova–Ilieva – member

Registered address

Sofia, 17-19 St. Saint Cyril and Methodius Street

Business address

1 Sixth September Street, Fourth Floor, Sofia

Legal advisor

Law Firm „Lozanova and Groysman”

Servicing banks

Unicredit Bulbank AD
CiBank EAD
DSK Bank EAD

Auditor

Baker Tilly Klitou and Partners OOD
1612 Sofia
104 Akademik Ivan Geshov Blvd, Seventh floor

ANNUAL REPORT

on the principal activities of Fund for Local Authorities and Governments in Bulgaria – FLAG JSC in 2016

This Report has been drawn up in compliance with the requirements laid down in Article 23 of the Regulation laying down the rules for exercising the rights of the government in state-owned commercial undertakings and the Commercial Act.

Mission

Fund for Local Authorities and Governments in Bulgaria – FLAG JSC is created on the basis of Ordinance № 4 of Council of Ministers of Republic of Bulgaria dated 7 March 2007 as an instrument of Government policy for Regional development.

The mission of the Fund is to support the efforts of Bulgarian municipalities, associations of municipalities (including associations of Water suppliers), companies with municipal or mixed state-municipal participation in the process of preparation and successful implementation of projects under the Operational Programmes, Programme for Rural Development, Cross Border Cooperation programmes, Financial mechanism of the EEA, the Norwegian financial mechanism, the Bulgarian-Swiss cooperation programme to reduce economic and social disparities within the enlarged European Union, Fund „Solidarity“ and National Trust Ecofund, which are aimed at modernization and expansion of municipal infrastructure and at creating sustainable and modern communities.

FLAG grants credits to beneficiaries and/or their associates, who prepare or implement projects under the above mentioned programmes or other international programmes after an explicit decision of the Board of directors of the Fund.

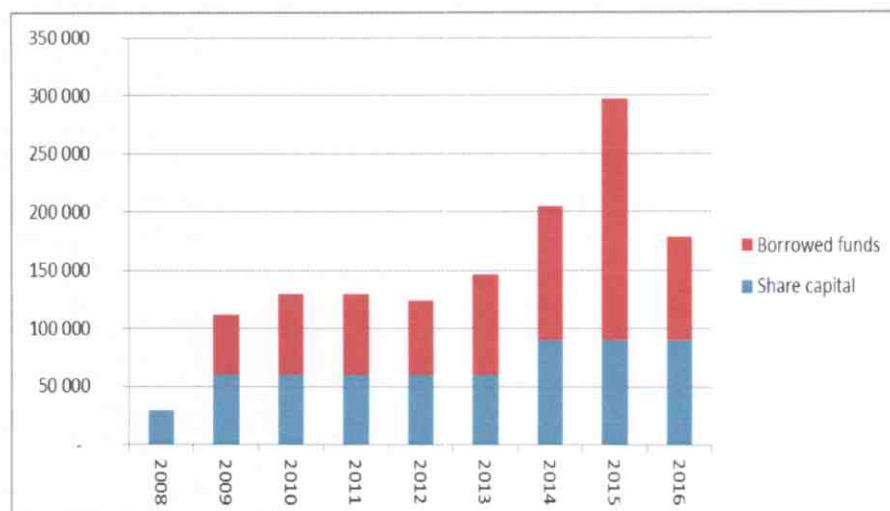
Development of the Fund

1. Working capital and revenues

The table below reflects the changes in the capital of the Fund over the years. As it can be seen, in 2008 the starting share capital of the Company was paid-in and in 2009 began the utilization of funds from the Loan Agreement with the EBRD. The highest amount of working capital was registered in 2015. This is the year in which the portfolio of FLAG reaches the highest values. The reason is the end of the first programming period 2007 - 2013 and the need for all projects to be finalized and settled until 31.12.2016.

Working capital (BGN '000)

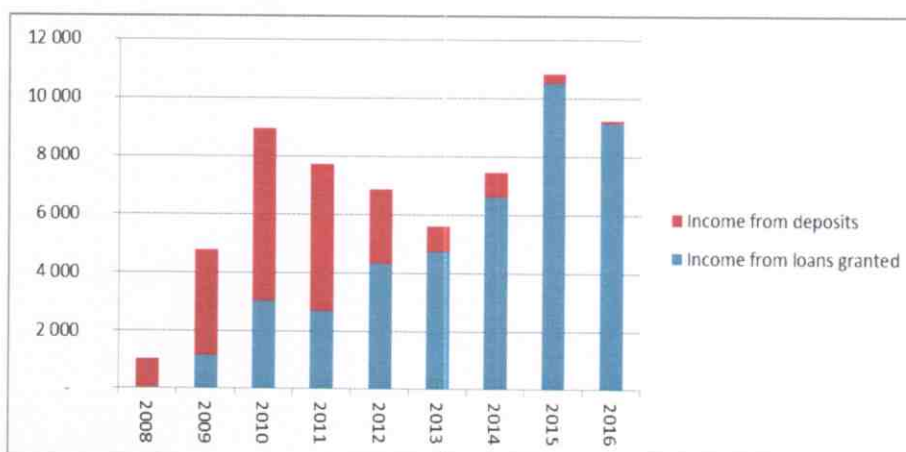
	Share capital	Borrowed funds
2008	30,000	-
2009	60,000	51,574
2010	60,000	69,133
2011	60,000	69,349
2012	60,000	63,675
2013	60,000	86,708
2014	90,000	114,389
2015	90,000	207,057
2016	90,000	88,178



The following table reflects the changes in the revenue structure of the company over the years. It is apparent that in the first years of operation the main part of the revenues of FLAG was from deposits. The reason is on one hand the availability of funds and on the other - the high interest rates on deposits. The gradual change in the market leads to a change in the structure of revenues – increase of the Fund's portfolio, reduction of available funds and respectively reduction of interest income from deposits.

Income from interest (BGN '000)

	Income from loans granted	Income from deposits
2008	-	1,067
2009	1,215	3,570
2010	3,065	5,870
2011	2,708	5,016
2012	4,353	2,511
2013	4,739	881
2014	6,605	858
2015	10,527	306
2016	9,133	92



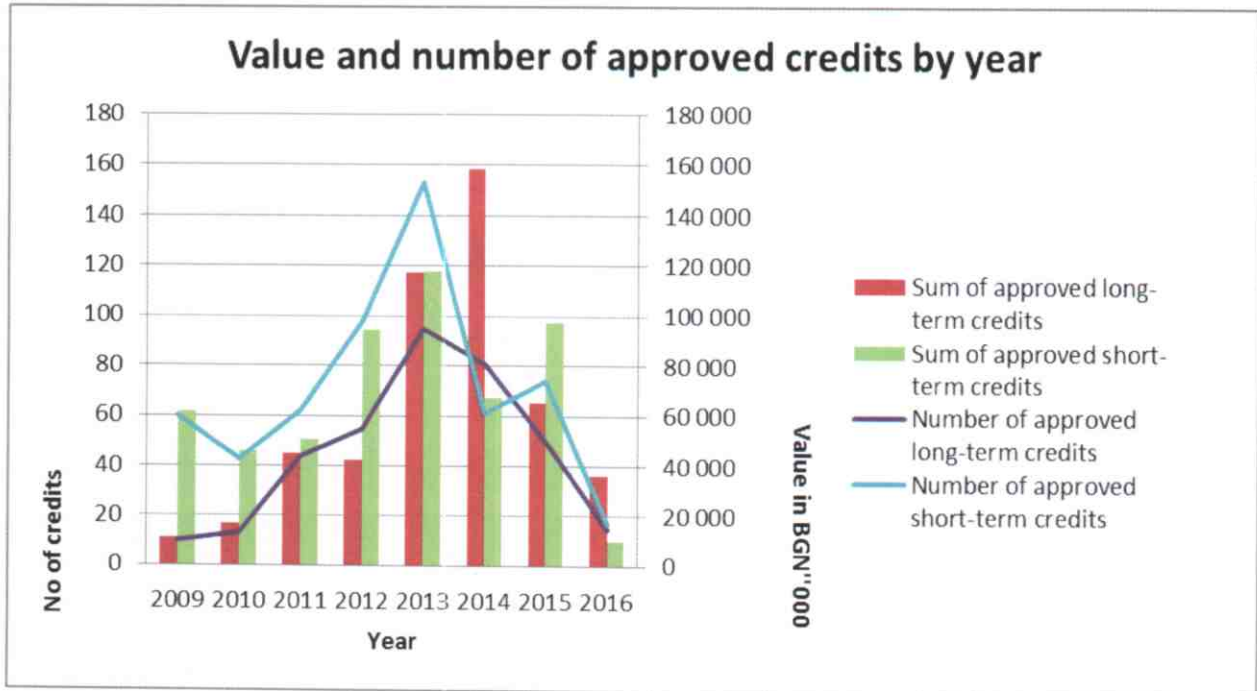
2. Approved credits

The table below shows the development of the activity of FLAG since 2009 when the application for credits started up until the end of 2016. Typical for the company's activity is that it is closely linked to the progress of the Operational programmes – the overall slowdown of activities related to grants led to a peak in the demand for resources in 2014 and 2015 when the projects which were implemented had to be successfully finalized. The reason is that the eligibility of expenditures under the programming period 2007 - 2013 was until the end of 2015.

The total number and amount of approved loans are the highest in 2013. The highest value of approved long-term loans was reached in 2014, with loans actually being utilized in 2015 as well, which is visible from the level of the working capital.

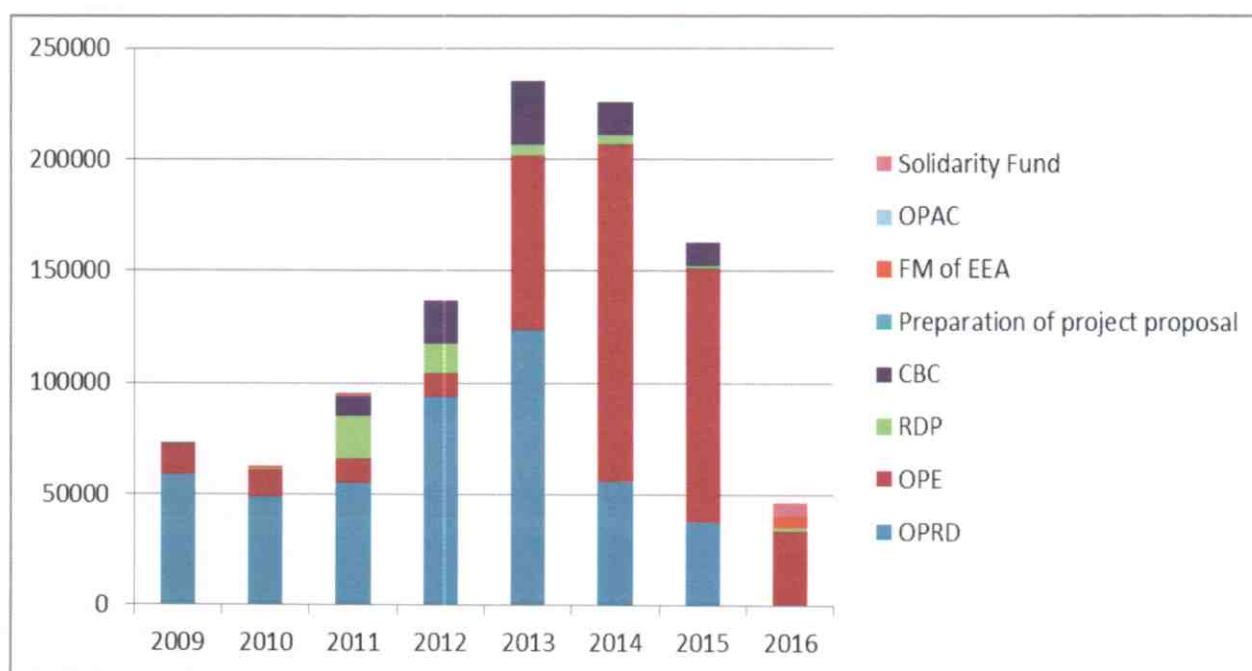
Approved credits – value (BGN '000) and number

Year	Sum of approved long-term credits	Sum of approved short-term credits	Total amount of approved credits	Number of approved long-term credits	Number of approved short-term credits	Total number of credits
2009	11,290	61,486	72,776	10	60	70
2010	17,043	45,742	62,785	13	43	56
2011	44,695	50,748	95,443	44	62	106
2012	42,398	94,162	136,560	55	98	153
2013	117,170	117,886	235,056	95	153	248
2014	158,399	67,158	225,557	81	61	142
2015	65,462	97,653	163,115	50	74	124
2016	36,306	10,318	46,624	15	17	32
Total	492,763	545,153	1,037,916	363	568	931



Approved credits per programmes (BGN `000)

	OPRD	OPE	RDP	CBC	Preparation of project proposal	FM of EEA	OPAC	Solidarity Fund
2009	58,851	13,774	-	-	151	-	-	-
2010	48,881	11,992	425	-	-	1,487	-	-
2011	55,464	10,687	18,720	8,919	272	1,051	330	-
2012	93,781	10,899	12,723	19,157	-	-	-	-
2013	123,455	77,907	5,198	28,496	-	-	-	-
2014	55,795	150,866	4,321	14,575	-	-	-	-
2015	38,107	113,181	1,091	10,736	-	-	-	-
2016	250	33,248	2,095	-	-	4,703	-	6,328
Total	474,584	422,554	44,573	81,883	423	7,241	330	6,328



The structure of approved credits for the period is shown in the table below. It is obvious that at the beginning of the programming period there is not a great demand for loans to finance own participation. This is due to the fact that at the beginning of the programming period the majority of projects with beneficiary municipalities were with 100% grant. Gradually the need for co-financing arose, which the municipalities had undertaken to pay back until the end of the projects. Therefore a growing demand for this type of credits is observed from 2013 onwards.

