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European Investment Fund Annual Report 2005

Member of the EIB Group

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Innovative finance to finance innovation

EIF highlights at 31 December 2005

2005 activities	EUR m
Venture capital / private equity commitments	24 funds for 468
Venture capital / private equity disbursements	318
Guarantee commitments	35 operations for 1 685

Total outstandings	12 515
Venture capital / private equity commitments	220 funds for 3 208
Guarantee commitments	165 operations for 9 307

2005 key financial data	
Subscribed capital	2 000
Own funds	601
Treasury and debt securities	551
Net income for the year	42.9
Return on equity	7.4%
Dividends declared	17.1

Shareholders	
European Investment Bank	61.9%
European Union via the European Commission	30.0%
23 financial institutions	8.1%

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Products and policies

European Investment Fund (EIF) is the EU financial institution within EIB Group specialising in small- and medium-sized enterprises (SMEs). It operates in close partnership with the European Commission and a wide range of financial institutions.

EIF's activity is centred upon two main areas: it acts as a fund-of-funds in the venture capital and private equity markets, and offers SME credit guarantees and securitisations. EIF also provides financial engineering services.

EIF always works through funds, banks or guarantee institutions, and uses own resources as well as funds mandated by its shareholders or by third parties.

Venture capital/private equity

EIF's venture capital instruments consist of equity investments in venture capital funds that support SMEs, particularly those that are early-stage and technology-oriented.

As a fund-of-funds specialist geared towards investing in new funds, EIF does not make direct investments in SMEs. By taking minority positions and encouraging commitments from a wide range of investors, notably the private sector, EIF plays a valuable role.

Portfolio guarantees and securitisation

EIF guarantees consist of two main products: credit enhancement, or guarantees for securitised SME loan and lease portfolios, and credit insurance, guarantees and counter-guarantees for portfolios of SME loans or leases. A special case for which EIF uses credit insurance is the SME Guarantee Facility, part of the European Commission's Multiannual Programme for Enterprise and Entrepreneurship (MAP) mandate managed by EIF.

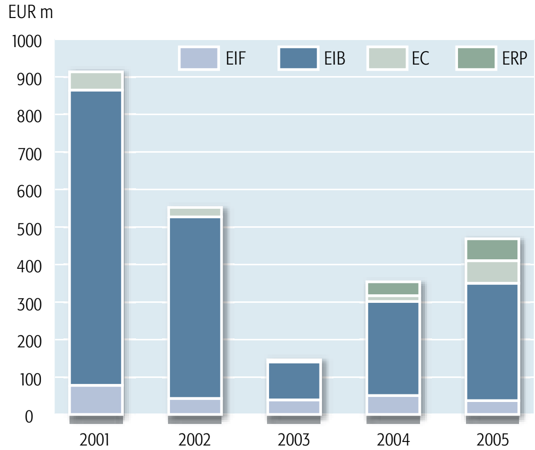
Guarantees for micro-finance, a unique window under the MAP Loan Facility, have also become a particularly important activity in several EU countries.

Within the EIB Group, EIF's activities are particularly relevant to three of EIB's five strategic priorities, endorsed by EIB's Board of Governors in June 2005: "Innovation 2010 Initiative" (i2i), SMEs, and Cohesion and regional policy.

In line with this strategic orientation, through the leverage effect of its venture capital and guarantee instruments, EIF is able to contribute to the development of an innovative and knowledge-based European economy by supporting growth and employment in SMEs, in particular in the EU Member States and in the Acceding and Candidate countries.

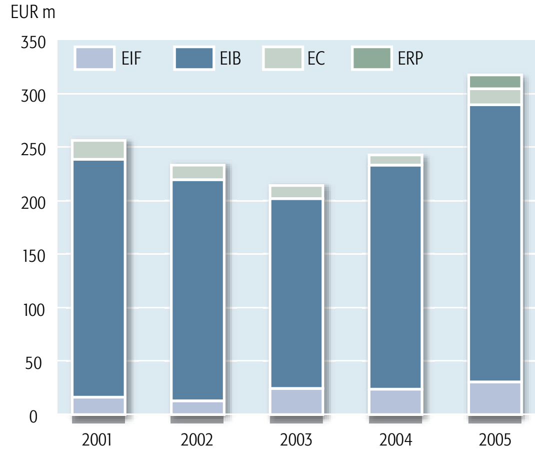
Overview of performance and results

VC commitments



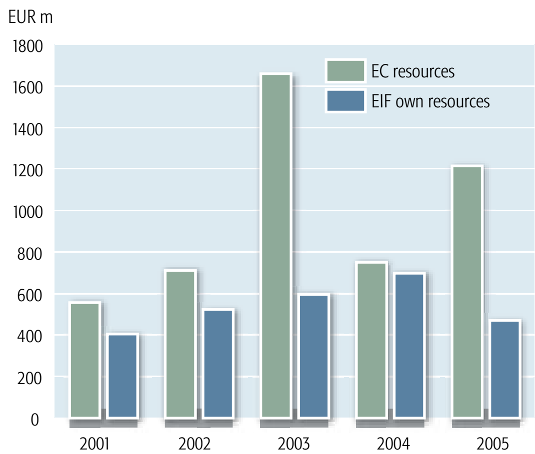
	2001	2002	2003	2004	2005
	912.2	**550.9**	**145.4**	**353.7**	**467.7**
	77.1	43.5	38.0	49.7	36.3
	786.2	482.9	101.7	251.7	312.6
	48.9	24.6	5.7	14.8	61.3
	-	-	-	37.5	57.5

VC disbursements



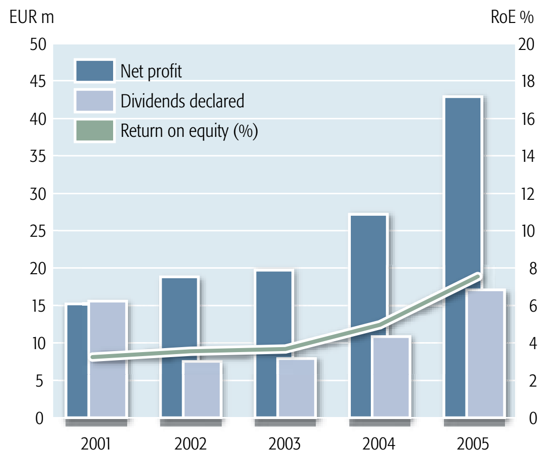
	2001	2002	2003	2004	2005
	256.3	**233.0**	**214.3**	**242.3**	**317.7**
	16.1	13.2	24.7	23.7	30.3
	222.6	206.2	177.3	209.1	259.4
	17.7	13.5	12.3	9.5	14.5
	-	-	-	-	13.5

Guarantee commitments



	2001	2002	2003	2004	2005
	554.9	711.9	1657.3	749.7	1213.3
	403.2	523.7	594.1	697.1	472.1

Profit for the financial year



	2001	2002	2003	2004	2005
	15.2*	18.8	19.7	27.2	42.9
	15.6	7.5	7.9	10.9	17.1**
	3.2	3.5	3.6	4.9	7.4

* Net profit excluding EUR 60.5m of exceptional income in 2001, which resulted from the transfer of the Trans-European Networks activity to EIB, as part of the EIF Reform.

** Subject to final approval by AGM.

Foreword by the Chairman of the Board

As the only European Community institution with a specialised focus on SME financing, EIF has an essential role to play in pursuing core EU objectives such as innovation, research and development, entrepreneurship, growth, and job creation.

Within the Community policies, the Lisbon Strategy for European competitiveness remains a key motor of EIF's activities. The European Research Area objectives, which revolve around maximising Europe's considerable research potential in science and technology and encouraging greater private investment in R&D, are also of increasing importance.

Furthermore, as underlined in the European Council Summit conclusions in March 2005, EIF has been encouraged to diversify its activities, notably towards flexible funding solutions in favour of innovative SMEs, particularly in technology activities.

As part of EIB Group, EIF is a significant contributor to three of the European Investment Bank's five strategic priorities: "Innovation 2010 Initiative", SMEs, and Cohesion and regional policy. As such, the Fund is a pillar of the newly-adopted Group strategy, approved by EIB's Board of Governors in June 2005, which implies better operational coordination and an increasing number of joint operations, as already initiated through joint securitisation deals in 2005. By developing such instruments, both institutions are in a better position to increase the value added of their operations for clients and also to better address financing requirements of SMEs.

In pursuing all these objectives, EIF is also working towards contributing to successful EU enlargement. JEREMIE, the currently proposed EIB Group - European Commission initiative, will aim to encourage access to various forms of finance for SMEs in regional development areas.

Philippe Maystadt

The scale and scope of EIF's investments are considerable. However EIF's influence is reflected not only in the number of operations which are signed, but also in the Fund's stable presence on the venture capital and SME guarantee markets and its reach in terms of encouraging best practice standards.

A parallel objective to which the Fund is bound by its statutes is to generate an appropriate return on its resources and, in terms of financial results, 2005 was a successful year, greatly surpassing forecast figures.

EIF continues to enjoy strong overall shareholder support and, after a slight change in the shareholding structure in 2005, looks forward to welcoming new shareholders in 2006.

Finally, I would like to express my particular thanks to Giovanni Ravasio for his valuable contribution to the Fund's activities and progress during his mandate as Chairman of the Board of Directors from early 2002 until September 2005. Throughout his term of office, he oversaw important developments in the Fund as it diversified its instruments and scope and entered into its eleventh year of activities.

Introduction by the Chief Executive

2005 was another fruitful year for EIF in terms of both operational activity and the institution's growth and ability to respond to new opportunities.

In 2005, EIF continued to broaden its venture capital investment activities beyond seed and start-up, adding more mid- and later-stage funds to its spectrum. Similarly, a rebalancing of the guarantees portfolio was implemented, notably towards participating to a larger extent in mid- and lower-rated tranches. The venture capital portfolio still concentrates on technology (principally information and communications technologies) and life sciences, representing just over half of the portfolio.

In 2005, EIF's new commitments totalled over EUR 2,000m in 24 venture funds and 35 guarantees funded by EIF's own resources as well as by resources under mandate. EIF continued to implement the European Commission's Multiannual Programme for Enterprise and Entrepreneurship 2001-2006 (MAP) for both early stage venture capital and SME guarantees, following a one-year extension of the original programme and an additional budgetary allocation for 2006, approved by the European Parliament and Council.

Overall, 2005 was an exciting year of new developments. In a groundbreaking operation in Europe, EIF structured and co-arranged the securitisation of loans to micro-finance institutions in a transaction involving a number of countries, including in the Balkans region. The JEREMIE (Joint European Resources for Micro to Medium Enterprises) initiative was set in motion late 2005 by the European Commission's DG Regional Policy and by EIF to enhance SME access to finance in the EU regions. Furthermore, a new high-tech fund-of-funds was launched early 2006 with the Spanish 'Centre for the Development

Francis Carpenter

of Industrial Technology' and other private and public sector investors. Looking forward, in addition to the Brussels office, EIF intends to extend its presence with staff in several external offices.

Other achievements in 2005 included EIF's AAA/Aaa/AAA ratings being once again reconfirmed by the rating agencies Standard & Poor's, Moody's and Fitch, the establishment of EIF's Compliance Function, as well as important progress towards meeting IFRS accounting requirements, to be completed in 2006.

As far as financial performance is concerned, 2005 showed a significant improvement on the previous year, with an audited net profit of EUR 42.9m, compared to EUR 27.2m in 2004 (EUR 19.7m in 2003), and a return on equity of 7.44%.

These very satisfying results were possible thanks to the ongoing commitment and considerable energy which EIF staff dedicated to meeting objectives and to maintaining the Fund's strong reputation in the venture capital and guarantees markets.

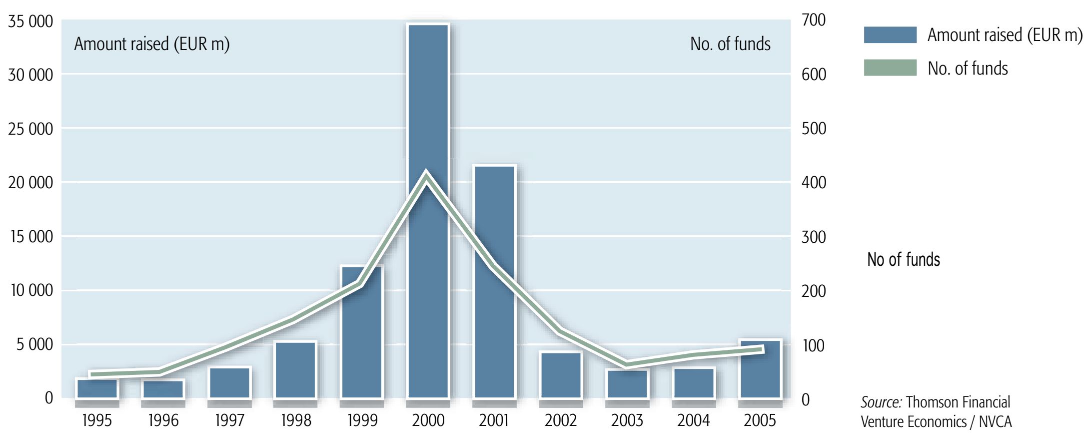
Venture capital and private equity

The European market environment

Over the past decade, the venture capital industry has gone from a peak of exuberance and rapid fundraising to a period of gloom after the bursting of the so-called "internet bubble" in 2000, followed by better returns in 2005. There are few serious investors in European venture capital, and fundraising still remains extremely patchy with many European venture capital funds at a difficult crossroads.

Overall venture capital investing into European companies in 2005 slowed compared to 2004, although total funds raised reached the highest amount in three years. Sofinnova Capital 5 was one of the largest funds that closed in 2005 (excluding buy-outs), a fund in which EIF invested EUR 27m. In terms of stage focus, there was a significant increase in later-stage investments, with levels being at their highest since 2002. In contrast, the decrease in seed and first round investments continued. As concerns sector focus, investments were increasingly diversified; the IT industry recorded the most significant overall decline[1].

The chart below indicates the overall evolution in European fund raising levels over the last decade[2]. 2006 is foreseen to be a decisive year for the venture capital industry.



Source: Thomson Financial Venture Economics / NVCA

EVCA job creation study

As illustrated in a recent Research Paper published by EVCA[3], private equity and venture capital play "a vital role in the conservation and creation of employment at a European level." Indeed, across the Member States, venture-backed companies showed an average annual growth rate in employment of 30.5% between the surveyed years of 1997 and 2004, some forty times the rate in EU 25 between 2000 and 2004 (0.7%). Furthermore, it was small companies (defined as less than 20 people) and biotech, health care & medical devices, and ICT companies which showed the strongest growth rates.

The research also revealed the importance of research and development in venture-backed companies where, on average, roughly one third of employees worked in that area and expenditure reached an average 45% of the sampled companies' budgets.

To meet the EU's employment target of 70% by the year 2010, according to the European Commission, an annual employment growth rate of 1.5% is required. As the study concludes, "the private equity and venture capital sector is well poised to contribute to this endeavour." In this context, EIF's commitment has had a considerable impact on the creation of jobs in Europe.

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1 Ernst & Young / Dow Jones VentureOne.
2 Thomson Venture Economics. Data at 13/03/06.
3 "Employment Contribution of Private Equity and Venture Capital in Europe", EVCA, November 2005.

Investments in 2005

EIF venture capital commitments in 2005 totalled EUR 468m in 24 funds, of which EUR 368m were signed (21 funds).

EIF used its own resources, as well as resources managed under mandates from its two main shareholders: the Risk Capital Mandate (RCM) from the European Investment Bank, and the Multiannual Programme for Enterprise and Entrepreneurship (MAP) from the European Commission. An important third mandate, from a non-shareholder, is the ERP-EIF Dachfonds, which EIF manages on behalf of the German Federal Ministry of Economics and Technology (BMWi) and the European Recovery Programme (ERP) and which exceeded its expectations in 2005 with EUR 115m committed in four funds.

EIF was closely associated with one of the 2005 success stories being an investor in Skype (voice over internet) through its investment in the first fund managed by Mangrove Capital Partners: New Tech Venture Capital fund. EIF supported Mangrove from inception, having identified this potentially successful first-time fund management team in the technology segment and having invested Community resources under the ETF Start-up facility (part of MAP) in 2000, which yielded a substantial return.

EIF equity investments signed and committed in 2005

All figures in EUR m (historical exchange rate)

Fund	Geographic focus	Resources	Commitments	Signatures
Adara Ventures SICAR	Spain	EC	10.0	10.0
Amadeus III	United Kingdom	RCM/EIF	29.3	29.3
ARGUS Capital Partners II	Central and Eastern Europe	RCM/EIF	30.0	30.0
Astorg III	France	RCM/EIF	30.0	30.0
Baytech II	Germany & Multi-country	ERP/RCM	25.0	25.0
BV 4	France	RCM/EIF	25.0	25.0
Crescent Capital II	United Kingdom	EC	8.8	8.8
Eqvitec Technology Mezzanine Fund II	Finland	RCM/EIF	12.0	12.0
FFT 3 - Fonds de Fonds Technologique	France	RCM	50.0	50.0
GED Iberian South FCR	Spain	ETF2 (EIB)	7.5	
Ibersuizas Capital Fund II	Spain	RCM/EIF	40.0	
INCOM III KG	Multi-country	ERP/RCM/EIF	30.0	
Life Sciences Partners III B.V.	Multi-country	RCM	17.0	17.0
Middle Market Fund III*	France	RCM/EIF		3.9*
New Tech Venture Capital Fund II	Multi-country	EC	15.0	7.6
NGN BioMed Opportunity I	Germany & Multi-country	ERP/RCM/EIF	30.0	30.0
Nordic Biotech Venture Fund II KS	Denmark	RCM/EIF	10.4	10.4
Perfectis II	France	RCM/EIF	12.0	12.0
Pond III	Multi-country	RCM/EIF	16.2	16.2
Pontis Venture Partners I Beteiligungs-Invest AG	Austria	EC	4.5	4.5
Prime Technology Ventures II N.V.*	Multi-country	RCM/EIF		1.1*
Sofinnova Capital 5	Multi-country	RCM/EIF	27.0	27.0
Talde Capital II, F.C.R.	Spain	EC	8.0	8.0
Wellington Partners III Life Science Fund L.P.	Germany & Multi-country	ERP/EC	30.0	
Wellington Partners III Technology Fund L.P.*	Germany & Multi-country	ERP/RCM/EIF		10.0*
Grand Total			**467.7**	**367.8**

* Follow-on EIF investment after additional closing of fund.

Total portfolio

EIF's total venture capital portfolio amounted to EUR 3.2bn in commitments at end 2005 across 220 funds; the resulting leverage effect, i.e. funding raised by other investors, was the mobilisation of some EUR 15bn.

Compared to the European average, EIF remains particularly active in the early stage sector with over 40% of its portfolio in seed and start-up funds. EIF's presence is important, especially in times of market difficulties, to attract private sector European investors to this segment. Nevertheless, the portfolio's focus has been steadily broadened to include mid- and later-stage funds, partly to help support existing funds in the portfolio to provide follow-on investments to maturing investee companies.

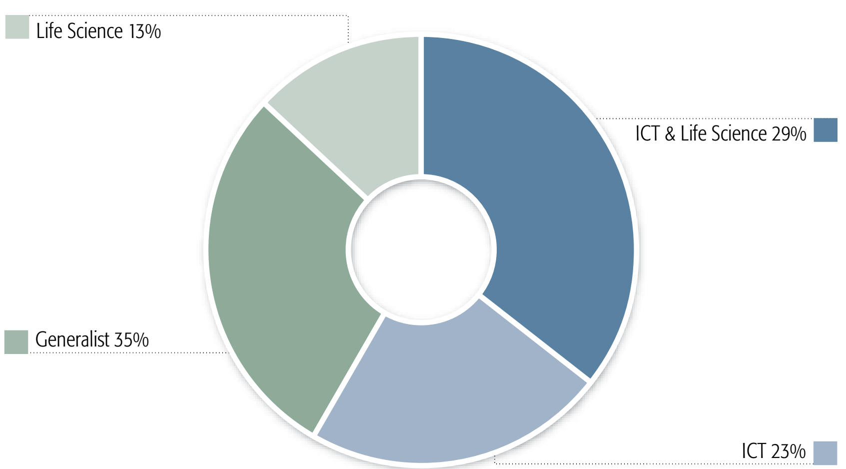
In terms of sector breakdown, the focus remains on early-stage technology, primarily information and communications technologies and life sciences, as shown in the following graphic.

EIF strives for a balanced geographic spread. Roughly one quarter of the portfolio is invested in multi-country funds, partly because smaller countries or those with a less developed VC market may be unable to support country-dedicated funds. Such funds have the added value of helping to harmonise the EU venture capital market and are typically found in Central and Eastern Europe.

EIF's core objectives remain the support of SME finance for innovation, R&D, entrepreneurship, growth, and job creation within the Lisbon Objectives to transform the EU into the "most competitive and dynamic knowledge-based economy in the world". The European Council Spring 2005 Summit conclusions highlighted EIF's role, encouraging it to extend its activity towards flexible funding for the financing of innovative SMEs through individual investor (business angel) and technology transfer networks.

The scale and scope of EIF's investments as well as its expertise, catalytic role and influence in developing best practice and corporate governance have established EIF as a leading institution on the European VC market. EIF's key role has been confirmed by the deployment of new joint investment facilities with public partners and the continuation of mandate management on behalf of its major shareholders.

EIF total equity investments: sector breakdown (at 31/12/05)



EIB Risk Capital Mandate

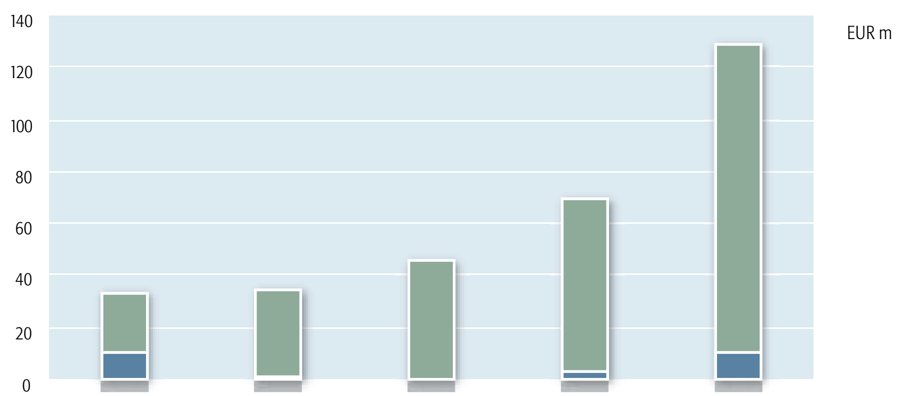
EIF has been operating the Risk Capital Mandate (RCM) on behalf of the European Investment Bank since the year 2000. The mandate's objective is to support technology and industrial innovation throughout early stage, expansion and development capital, with a particular focus on innovative high-tech firms, and hence to contribute to a balanced development of markets across European regions.

The bulk of EIF's venture capital investments (over 80%) are carried out using the EUR 2bn available under this mandate. With the current 200% gearing, the RCM investment potential reaches a theoretical EUR 4bn alongside which EIF co-invests using its own resources.

At 31/12/05, amounts signed using EIB resources reached almost EUR 2.6bn. In terms of geographic focus, multi-country operations make up some 28% of the EIB portfolio, followed by operations in France and the United Kingdom, and then Italy, Germany and Spain.

In 2005, capital repayments for the RCM portfolio totalled EUR 118.5m and dividends received EUR 10.3m. Since the portfolio's inception and at 31/12/05, EIB has received EUR 320m in capital repayments and EUR 33m in dividends. The evolution of these payments over recent years is illustrated in the following graph. Various elements from cash flow and the profit and loss account are taken into consideration to give a view of the portfolio's turnaround.

The decline in values of venture capital markets over the past years has obviously influenced the performance of the RCM portfolio. The timing of investments is also significant since a large number of investments took place after mid-2000 making it a relatively young portfolio in which VC funds have not yet matured.



	2001	2002	2003	2004	2005	
	10.3	1.4	0.5	3.0	10.3	Dividends received
	22.7	33.1	45.1	66.6	118.5	Capital repayments

Banexi Ventures Partners' BV4 fund

Promoting technology venture capital and excellence

Snapshot

The investment in the Banexi Ventures Partners' (BVP) latest initiative, BV 4, perfectly illustrates EIF's strategy, which includes a continuing early-stage focus, an area from which many traditional investors have retreated and hence where there remains a strong need for EIF, as a permanent long-term partner, and a high technology focus (life sciences, information and communications technologies, semiconductors, materials).

Managed by a leading European VC house with a brand name backed by a long-term investment track record, the new fund is dedicated to investments in IT, electronics, semiconductors and optics and, to a lesser extent, life sciences.

EIF added value

Important role in fundraising:

- EIF has backed BVP since the latter's first institutional fund in 1998. As an investor in all predecessor funds, EIF's renewed and increased support sent a strong positive signal to the market and to the other potential investors.
- Thanks to its close relationship with BVP, EIF has been associated with and contributed to the team's preparatory work for the new fund.
- EIF's early commitment helped BVP to start fundraising with a substantial initial mass, creating a positive momentum by reinforcing investor confidence and raising project visibility among the investment community.

Direct contribution to the Lisbon strategy for European competitiveness:

- Benefits EU technology transfer and development;
- Stimulates economic growth and qualified job creation driven by innovation;
- Underlines EIF's leadership role in the VC fund-of-funds market.

Profile

France is recognised by the industry as having been one of the leading European markets for venture capital activity in 2005. BVP's experienced team enjoys a strong reputation thanks to both the range and quality of its track record, having invested over EUR 250m in more than 230 companies since 1983, including some high profile exits.

Against this favourable backdrop, EIF's interest in BVP also derived from BVP's strong deal flow in IT, semiconductors and life sciences and its team's relationship networks. BVP contributes to the realisation of viable projects from the seed and early stage to the development and mature stages.

Businesses benefiting from this funding:

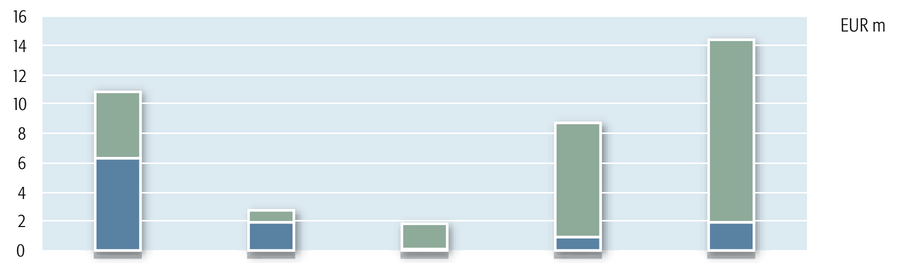
- IT investments include Kelkoo, which created the first pan-European online shopping guide, ranked third in Europe behind Amazon and Ebay in terms of audience. It was successfully sold to Yahoo! in 2004 and the exit was awarded Venture Capital Deal of the Year at the European Private Equity Awards.
- Inventel is a leader in telecoms access devices and wireless technologies and is an important partner of telecom operators in Europe. The company has a strong focus on R&D, engineering and design services. Its expertise in wireless voice and data communications (WiFi, Bluetooth) has gained the company a solid customer base and a reputation for innovation, high quality and reliability. The company was successfully sold to Thomson in 2005.

The BV 4 VC fund managed by BVP will directly benefit the European Union in terms of technology transfer, European technology promotion, economic growth and the creation of qualified jobs, in line with the objectives of the Lisbon and Stockholm Summits and the Innovation 2010 Initiative.

Own resources

EIF invests its own resources alongside EIB resources (Risk Capital Mandate) and the ERP-EIF Dachfonds. Using EIB Group resources, EIF aims to invest in independent management teams that provide risk capital particularly to early stage SMEs and those companies, which are developing or using advanced technologies in industry or services.

In 2005, EIF invested EUR 31.3m of own resources. At 31/12/05, cumulative amounts signed using own resources reached almost EUR 270m. Capital repayments totalled EUR 12.5m and dividends received totalled EUR 1.9m. Since the portfolio's inception and at 31/12/05, the portfolio has received almost EUR 46m in capital repayments and almost EUR 15m in dividends. The evolution of these payments over recent years is illustrated in the following graph. Various elements from cash flow and the profit and loss account are taken into consideration to give a view of the portfolio's turnaround.



	2001	2002	2003	2004	2005	
	6.3	1.9	0.1	0.9	1.9	Dividends received
	4.5	0.8	1.7	7.8	12.5	Capital repayments

European Commission mandate

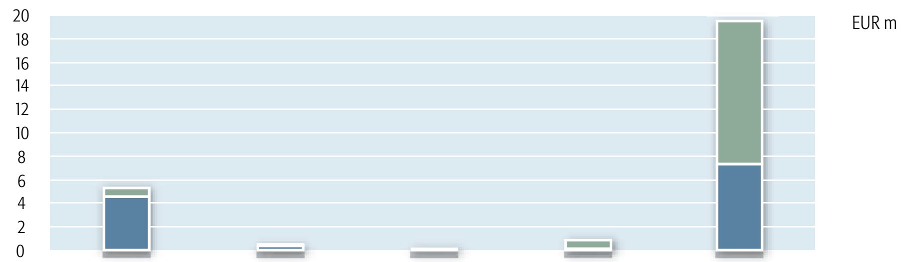
Under the European Commission's Multiannual Programme for Enterprise and Entrepreneurship (MAP), EIF manages the ETF Start-up facility and the Seed Capital Action venture capital schemes. Initially covering 2001-2005, the European Parliament, on a proposal from the ITRE (Industry, Research and Energy) Committee, and the European Council approved a one-year extension to the programme, with an accompanying budgetary increase until end 2006.

These programmes target seed or early stage funds, a stage where private sector co-investors continue to be scarce, to finance the development of innovation and research as well as incubators operating as funds. Seed Capital Action is a grant scheme that supports the recruitment of additional investment managers in seed capital funds.

In 2005, signatures in the ETF Start-up portfolio totalled EUR 39m, bringing the cumulative portfolio to EUR 178m signatures in 27 funds at 31/12/05. Capital repayments totalled EUR 12.1m and dividends received totalled EUR 7.3m. Various elements from cash flow and the profit and loss account are taken into consideration to give a view of the portfolio's turnaround.

In 2005, the portfolio benefited from one of Europe's success stories through its investment in Skype (voice over internet), resulting from its EUR 10m investment made in June 2000 in Mangrove Capital Partner's debut fund: New Tech Venture Capital (NTVC).

Also in 2005, EIF invested in NTVC II, a fund noteworthy in part for the role played by the Luxembourg Société Nationale de Crédit et d'Investissement (SNCI) - EIF co-operation agreement, where EIF assisted SNCI in its due diligence work. This investment is one of the few funds with a multi-country focus under the ETF Start-up facility.



	2001	2002	2003	2004	2005	
	4.5	0.4	-	0.1	7.3	Dividends received
	0.8	0.1	0.2	0.8	12.1	Capital repayments

ERP-EIF Dachfonds

Officially launched in 2004, the ERP-EIF Dachfonds is a fund-of-funds with a total size of EUR 500m investing in venture capital funds focusing mainly on Germany-based high-tech early stage companies. EIF manages the facility on behalf of the German Federal Ministry of Economics and Technology (BMWi) and the European Recovery Programme (ERP), from which EUR 250m were committed, matched by an EIF co-investment.

Despite a generally difficult climate for German VC funds focussing on early stage high-tech investments, the ERP-EIF Dachfonds exceeded its expectations in 2005, committing, alongside other EIF resources, EUR 115m in four funds. At 31/12/05, the ERP-EIF Dachfonds has committed an overall EUR 190m in six funds, which in turn helped to raise another EUR 554m from private investors, highlighting the programme's leveraging effect on the market.

2005 highlights include the signature of NGN BioMed Opportunity I fund, which focuses on a special niche of life science companies that are in an advanced clinical phase of development and close to market entry, the Wellington Partners Life Science Fund L.P., which focuses on early stage life science companies, as well as a EUR 30m commitment in INCOM III - Technofonds GmbH & Co KG, a very well networked fund in northern Germany where venture capital or other support for early and development stage companies is rather scarce.

NEOTEC

This new type of fund-of-funds mandate was launched in 2005 with the Centre for the Development of Industrial Technology (CDTI: Centro para el Desarrollo Tecnológico Industrial), a public business entity of the Spanish Ministry of Industry, Tourism and Commerce.

EIF's investment will represent around 25% of the fund's final target size of some EUR 200m. First closing was in February 2006 at EUR 175m. The programme is intended to bring together Spanish public and corporate and banking private sector investors for investments in Spanish SMEs fostering innovation and research and development.

Building on similar initiatives in other Member States, notably in France and the United Kingdom, the CDTI-EIF partnership will leverage EIF resources to ensure a coordinated approach between EIF, national public bodies and the private sector. Furthermore, it will give Spanish public and private investors access to EIF's know-how in fund-of-funds management.

Nordic Biotech

Asset assembling strategies to mitigate early-stage life sciences investment risks

Snapshot

EIF's expertise and breadth of portfolio enables it to specifically target niche strategies in European venture funding, as demonstrated by its investment in Nordic Biotech. Nordic Biotech is a special situation investor in life science companies aiming at assembling late-stage assets in newly-established firms to achieve critical mass in their market position.

EIF rationale for investing

- Unique business models in venture capital in Europe, with an imaginative investment strategy;
- Attractive risk return profile;
- Catalytic effect in the fundraising process, by supporting investor confidence and raising project visibility in the investment community at crucial first closing stage.

Profile

Nordic Biotech's business model is a promising niche strategy with an interesting return potential based on its team's specific skill set and credentials coupled with low competition in their target sector.

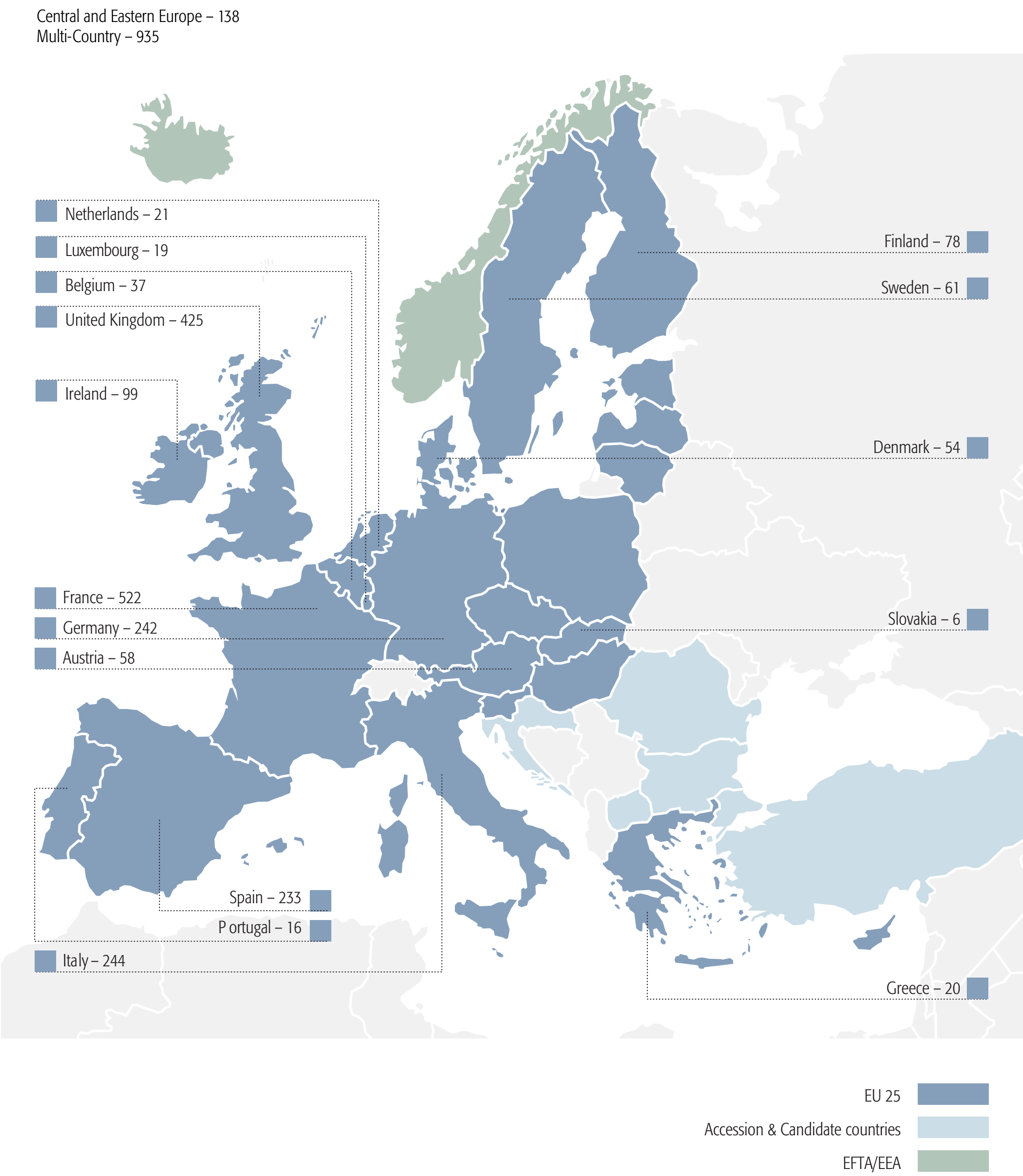
What differentiates Nordic Biotech from other venture capital firms is its willingness to look at companies that are still at a completely embryonic stage – maybe not even a company, but just a patent.

The new fund, with a focus on biotechnology, will support young companies involved in the most advanced fields of science and technologies, in the areas of pharmaceutical/biotech drug discovery and development. Cooperating closely with well-known academics and business leaders primarily in the Nordic region, the fund capitalises on significant European scientific know-how.

The investment strategy, which brings late stage assets into seed companies, mitigates the most significant risks associated with early stage investments in life sciences, such as time-to-market of products and high failure rate on early stage biotech developments.

EIF equity investments total portfolio: EUR 3,208m in commitments at 31 December 2005

All figures in EUR m (historical exchange rate)



Guarantees and securitisation

EU SME lending environment

Over the last few years, banks have increasingly anticipated the new regulatory capital regime under Basel II, also with respect to SME lending. Aggregate loan exposures of up to EUR 1m generally benefit from more favourable capital requirements for retail exposure, while banks tend to direct their lending activity to the internally better-rated companies, particularly for higher loan amounts. Arguably, this may lead to reduced access to credit for less well-rated SMEs, when at the same time, overall SME lending volumes may rise.

An emerging trend is for banks and other specialised funds to provide mezzanine finance to SMEs and mid-caps. SMEs are notoriously short of equity capital, which restricts their borrowing and growth potential. Senior lenders can consider mezzanine loans similar to equity as they are subordinated to the senior facility.

Since 1998, SME securitisation has played an increasingly important role in banks' portfolio management. In 2005, total European SME securitisations nearly tripled to EUR 33.9bn. SME securitisations now represent an important segment of the European securitisation market, which amounted to some EUR 315bn in 2005, a 28% year-on-year increase. SME securitisations have been structured by originators from a number of European countries, including Austria, France, Germany, Italy, the Netherlands, Portugal, Spain, Switzerland, and the United Kingdom. The well-established SME securitisation programmes such as the FTPYME programme in Spain and KfW's Promise platform in Germany accounted for a large portion of the total issuance in this sector. The bigger volume of SME securitisations combined with the good performance of SME transactions result in greater liquidity and lower spread levels, which have a positive knock-on effect on SME lending in general.

SME securitisation volumes are expected to continue to grow in the foreseeable future as securitisation increasingly forms an integral part of the business model of financial institutions. Accordingly, the rationale for securitisation is expected to shift further from pure capital relief motivation towards funding and overall balance sheet management considerations.

Commitments in 2005

EIF's guarantee operations draw on own funds as well as funds provided by the European Commission under the guarantee window of the current EU programme, Multiannual Programme for Enterprise and Entrepreneurship (MAP), and initially under the Growth and Employment Initiative 1998-2000.

Overall, EIF guarantees issued in 2005 totalled EUR 1.7bn. EIF's own resource activity consisted of credit enhancement operations totalling EUR 457m and one credit insurance deal for EUR 15m. Some EUR 1.2bn were signed for 25 operations under MAP.

Particularly noteworthy in 2005, EIF structured and co-arranged the securitisation of loans to micro-finance institutions, the first such deal ever seen in Europe. This milestone transaction (known as 'Microfinance Loan Obligations 2005-1') involved several countries in south-eastern Europe.

A reorientation of EIB Group's strategy at the beginning of 2005 led to a strengthened co-operation between EIF and EIB and resulted in two joint securitisation operations being signed during the year: Douro SME Series 1, a Portuguese SME securitisation transaction originated by Banco BPI (Banco Português do Investimento) with PME Investimentos providing a guarantee on a more subordinated tranche and where EIF was advisor and guarantor alongside EIB and KfW as investors, and Geldilux TS 2005 (Germany), where EIF acted as credit enhancer of part of two mezzanine tranches, again alongside EIB and KfW as investors.

Also as a result of the shift in business model, EIF entered into more mezzanine tranche operations in the course of the year, whilst continuing to strive for a balanced overall portfolio approach and ensuring that these operations contribute to fair risk return coverage.

EIF guarantee commitments in 2005

All figures in EUR m

Product	Contract name	Country	Signatures
Credit enhancement	Bancaja 4 FTYPME	Spain	9.0
	Douro SME Series 1	Portugal	26.4
	FTYPME Pastor 3	Spain	43.7
	GATE SME CLO 2005-1	Multi-country	5.0
	Geldilux TS 2005	Germany	16.5
	Gracechurch Corporate Loans 2005-1	United Kingdom	56.0
	Mars 2005	Belgium	183.8
	Microfinance Loan Obligations 2005-1	South-eastern Europe	6.3
	SKGF	Sweden	15.0
	Wincap SME CDO	Multi-country	110.4
		Subtotal	**472.1**
MAP	ALMI	Sweden	52.2
	Association pour le droit à l'initiative économique	France	5.9
	Ati-Alleanza di Garanzia	Italy	140.0
	Ati Artigiancredit Piemonte-Emilia Romagna-Lombardia	Italy	150.0
	Ati Sistema Garanzia Umbria-Marche	Italy	72.5
	Ati-Garanzia Diretta	Italy	31.0
	Austria Wirtschaftsservice GmbH	Austria	2.5
	Bank BPH S.A.	Poland	50.0
	BBMKB	Netherlands	150.0
	BRD - Groupe Société Générale	Romania	20.0
	Bürges	Austria	7.5
	Bürges	Austria	48.0
	Central-European International Bank Ltd.	Hungary	5.0
	CERSA	Spain	174.8
	Ceskomoravska Zarucni a Rozvojova Banka	Czech Republic	15.9
	Credit and Export Guarantee Fund Kredex	Estonia	4.9
	Cultura Sparebank	Norway	0.9
	Deutsche Ausgleichsbank	Germany	66.0
	Fonds de Participation	Belgium	22.5
	Fonds de Participation	Belgium	0.0*
	Hipoteku Banka	Latvia	0.0*
	HVB Bank Hungary Rt.	Hungary	15.0
	Investiciju Ir Verslo Garantijos UAB	Lithuania	0.0*
	Mediocredito Centrale	Italy	70.0
	Polfund Fundusz Poreczen Kredytowych S.A.	Poland	1.3*
	Raiffeisen Bank	Romania	0.0*
	Slovene Enterprise Fund	Slovenia	0.0*
	SOCAMA	France	55.5
	SOFARIS	France	31.9
	SOFARIS	France	0.0*
	Tatra Banka A.S.	Slovakia	20.0
	TEMPME S.A.	Greece	0.0*
	The Danish Investment Fund	Denmark	0.0*
		Subtotal	**1 213.3**
		Grand Total	**1 685.4**

* Commitments extended in 2005 without changes to signed or committed amounts.

Total portfolio

EIF's total guarantee portfolio amounted to EUR 9.3bn at end 2005, through 165 transactions.

Across its guarantee product lines, EIF acts as a unique market player, due to status as a AAA/Aaa/AAA rated European institution that operates on a risk/return related basis. EIF's particular added value is the overall leverage effect brought about by its participation in SME guarantee transactions.

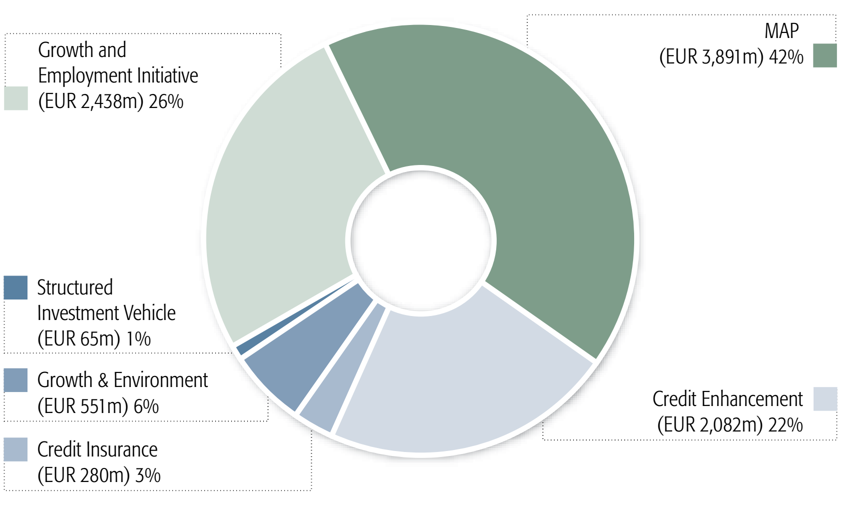
EIF's activity in the field of credit enhancement is strong, with total guarantee commitments amounting to EUR 2,082m at 31/12/05. EIF is a key participant in the established European SME securitisation sector and now looks towards emerging securitisation markets for new business opportunities.

EIF has also performed very well under the European Commission's SME Guarantee Facility, with the total portfolio amounting to EUR 3,891m at 31/12/05.

EIF has continued to increase its already good geographical coverage. EIF has operations in almost all of the eligible countries, which span EU Member States, the Acceding and Accession States and Norway, Iceland and Liechtenstein. Negotiations are underway with financial intermediaries in those eligible countries where operations have yet to be concluded. In 2005, EIF's activity extended to a new type of securitisation operation that involved local micro-finance institutions, with a similar transaction envisaged in 2006 in further Eastern European countries.

The European Commission's extension of the MAP mandate in 2006 and the planned successor programme in 2007 confirm the effective role played by EIF in supporting SMEs, contributing to economic growth and development in Europe.

EIF guarantee operations: product breakdown
EUR 9,307m in commitments (at 31/12/05)



EIF added value in SME loan securitisation

Through its loan securitisation activity, EIF facilitates the transfer of SME credit risk from banks and leasing companies to the capital markets by guaranteeing certain tranches of credit risk, which creates capital relief and increased lending capacity to SMEs. Credit enhancement brings particular benefit to small- and medium-sized banks, which are the most important funding source for SMEs as EIF's participation enables them to assume the higher credit risk associated with SME lending.

Loan securitisation involves the packaging of loans or leases and may be structured as either "true sale" securitisation, whereby securities are sold to investors backed by the cash flows arising from the underlying loans or, instead, "synthetic" transactions, which transfer loan portfolios' credit risk to the capital markets, while the originating bank retains ownership of the assets. EIF fully or partially underwrites illiquid and riskier tranches. EIF's expertise also results in cost-efficient deal structuring.

2005 was another strong year for the European SME securitisation industry and the market is buoyant and expanding. EIF is a principal player in this market, underpinned by its AAA/Aaa/AAA credit rating by all three rating agencies, its Multilateral Development Bank status and zero weighting under the New Basel Capital Accord, as well as several years of experience in the field. EIF was instrumental in launching nine of the twenty or so transactions in 2005 in the specialised SME securitisation segment.

In 2005, EIF's new priority was to be involved as guarantor or risk protection seller in the new EU Member States and to cover new geographical areas. Furthermore, EIF widened its scope in terms of eligible risk to be underwritten by allowing some new operations to be rated at least B1, down from Ba2.

EIF developed a more active and in-depth role in the transactions closed in 2005, participating in the structuring and closing of Douro 2005-1, a Portuguese SME securitisation transaction, which demonstrated the complementarity between EIF, national guarantee schemes and investors.

EIF participated as risk protection seller in a successful true sale German transaction, Geldilux, brought to the market by HVB and backed by SME financing in Germany, with EIB and KfW as investors. EIF also provided guarantees on synthetic and true sale transactions backed by SME financing in the United Kingdom (Gracechurch Corporate Loans 2005-1) and Spain (FTPYME Pastor 3 and FTPYME Bancaja 4). In Belgium, EIF acted as sole underwriter for all the mezzanine tranches in a privately-placed synthetic securitisation.

EIF launched an innovative milestone transaction, financing commercially-priced funding to micro-finance institutions in south-eastern Europe. EIF structured and co-arranged the securitisation of loans to such micro-finance institutions and acted as guarantor and placement agent. It is estimated that the deal will result in the direct financing of at least 20,000 new micro-loans.

At 31/12/05, EIF had a credit enhancement portfolio totalling EUR 2,082m supporting securitisations in an aggregate amount of EUR 51,400m backed by loans to some 270,000 SMEs. Access to finance is one of the major business constraints for SMEs and this continued dynamic development in SME loan securitisation significantly enhances access to debt finance by increasing the lending capacity of banks.

Microfinance Loan Obligations 2005-1

Bridging a gap in commercial lending: micro-finance securitisation

Snapshot

For the first time in Europe, EIF has structured and co-arranged a securitisation of loans to micro-finance institutions (MFIs). It is estimated that this transaction will result in the direct financing of some 20,000 new micro-loans. Micro-loan beneficiaries are typically excluded from traditional commercial lending.

This very significant transaction involves several countries, including Romania, Bulgaria and a number of neighbouring countries in the Balkans region. Through this asset-backed funding deal, MFIs will secure long-term funding to support continued growth in their micro-lending activity. Despite the small size of the micro-loans (a few thousand euros on average), there is high potential in terms of business productivity gains and job creation.

EIF added value

- Active role of EIF as deal facilitator (on a remunerated basis) by acting as co-structurer and co-arranger.
- Geographical diversification through a multi-jurisdictional transaction.
- High additionality by providing credit enhancement to an unrated senior tranche.

Profile

Micro-lending has been clearly identified as one of the key political objectives in the EU and beyond (2005 was the United Nation's "International Year of Microcredit"). EIF has built on its experience under the MAP Micro Loan window and leveraged its expertise in structuring transactions.

For the first closing, EIF and Symbiotics S.A. (a professional services company offering innovative investment intermediation services to micro-finance investors and fund managers) have sourced assets in emerging markets in Albania, Montenegro, Romania and Russia. Further closings are scheduled for April and October 2006, which would bring total notes issuance up to approximately EUR 30m and would include assets in Bulgaria, the Former Yugoslav Republic of Macedonia and Serbia. All underlying assets are senior unsecured term loans to MFIs.

By supporting the targeted MFIs through an innovative capital market transaction, EIF ensures that a large number of micro-entrepreneurs receive new micro-loan financing over the next 4-5 years. Although individual micro-loans are small (EUR 3,000 on average), one should not underestimate the very high potential in terms of business productivity gains and job creation.

The transaction also brings diversification to the funding sources of MFIs, which historically have relied to a large extent on donor funding and subsidised funding lines from development banks (e.g. KfW).

Without EIF's involvement in structuring the transaction and as a guarantor, it would have been impossible – at least for the time being – to launch such an innovative, complex structure that brings together several MFIs in the Balkans region and provides financing for micro-finance entrepreneurs through the capital markets.

European Commission mandate

Under mandate from the European Commission, EIF manages the SME Guarantee Facility, which comprises part of the Multiannual Programme for Enterprise and Entrepreneurship (MAP). Within this facility, EIF works to meet European Union policy objectives to support SMEs by providing enhanced access to finance. Thirty-one countries are eligible under MAP, namely, EU 25, Bulgaria, Iceland, Liechtenstein, Norway, Romania and Turkey.

This mandate is a very successful mechanism for assisting SMEs due to the high leverage effect brought about by EIF's involvement, wherein each EUR 1 in budget allocation results in EUR 72 of investment for SMEs, an excellent example of budget optimisation. In view of the programme's effectiveness, the budget period was extended by one year, i.e. until the end of 2006.

Under the SME Guarantee Facility, EIF provides guarantees and counter-guarantees (re-insurance) to financial intermediaries for their portfolios of SME debt finance. EIF typically covers 50% of the credit risk of the individual loans or leases in the dedicated portfolio. EIF's obligation to pay its share of losses under a specific portfolio is capped at a pre-set amount.

At 31/12/05, EIF had entered into 45 agreements in 27 countries, for a total guarantee commitment of EUR 6,328m and the estimated underlying loan volume supported by these intermediaries under MAP and the predecessor mandate programme was EUR 18,328m to more than 260,000 businesses. In 2005, EIF signed 25 guarantee operations, including extensions, amounting to EUR 1.2bn.

The SME Guarantee Facility contains four product windows, namely, the Loan Guarantee, the Micro-credit Guarantee, the Equity Guarantee and the ICT Loan Guarantee.

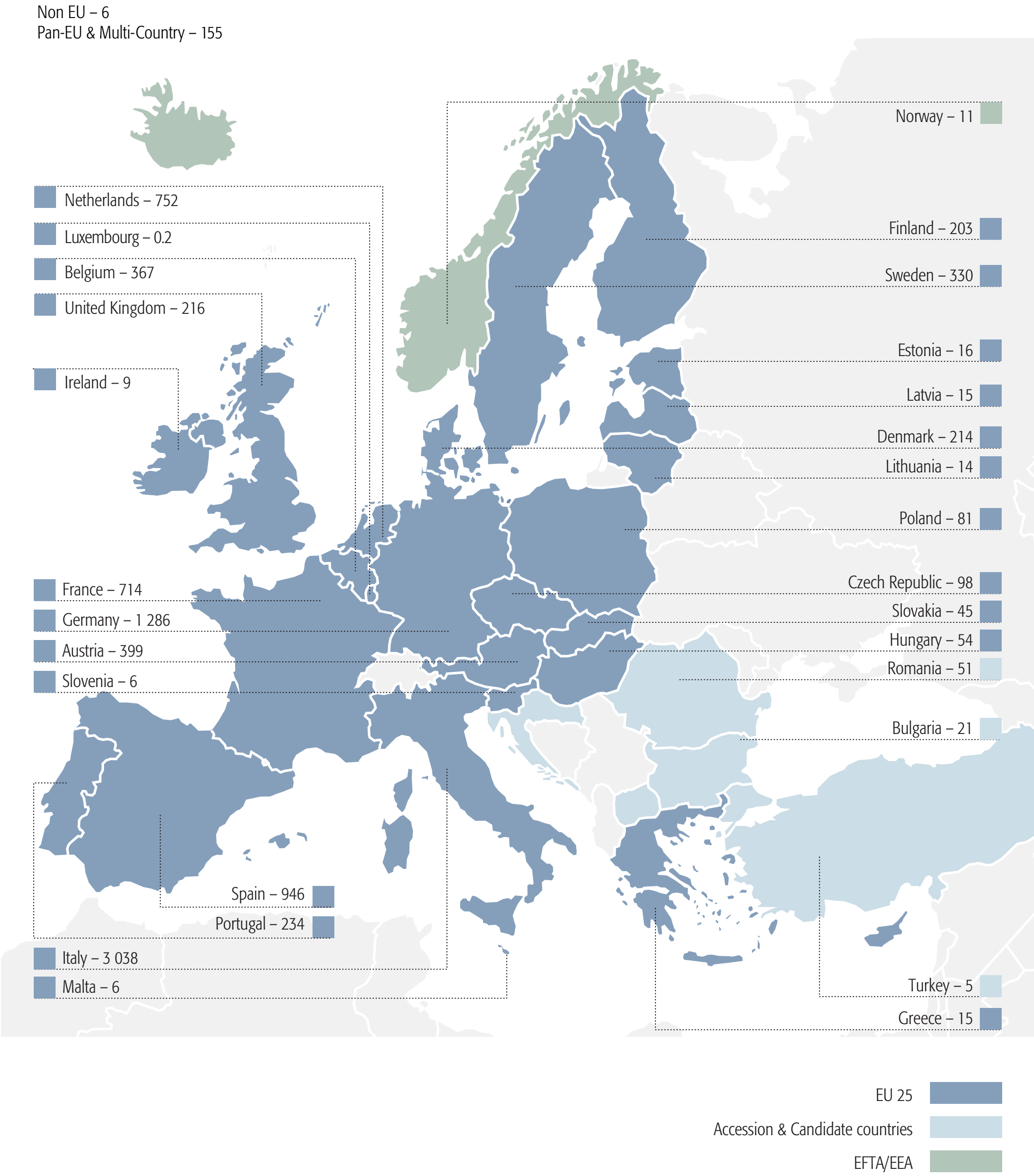
The Loan Guarantee window has the strongest utilisation. EIF has signed 36 operations with financial institutions and banks from the public and private sectors. The geographical coverage is particularly good, including most of the new Member States plus Bulgaria, Romania and Turkey. The underlying loan volume supported with the Loan Guarantee window was estimated at EUR 9,572m at 31/12/05.

Under the Micro-credit Guarantee, EIF's financial intermediaries may issue micro-loans to businesses that do not employ more than ten employees. EIF's micro-finance guarantees total EUR 193m, which is a considerable amount given that the average micro-loan is just under EUR 10,000. Over 20,000 very small businesses are supported under the Micro-credit Guarantee window. Through its activity, EIF played a key role in the United Nation's "International Year of Microcredit" in 2005.

The objective of the Equity Guarantee is to support own funds investments in small- and medium-sized companies with growth potential. The underlying equity investments reached EUR 203m at 31/12/05.

EIF guarantee commitments total portfolio: EUR 9,307m in commitments at 31 December 2005

All figures in EUR m



New business

Competitiveness and Innovation Framework Programme

The financial instruments of the Competitiveness and Innovation Framework Programme (CIP), the MAP successor, will enter into force on 1 January 2007 and will cover the period 2007-2013 for a budgetary amount of EUR 1bn.

CIP has been designed as a more ambitious programme compared to its MAP predecessor. It covers a larger geographical area and extends the range of instruments to include new market segments and products.

The CIP programme is one of the EU's core SME and innovation policy instruments. CIP's overall objectives are to generate economic growth and create more jobs, as well as to boost productivity, competitiveness and innovation capacity in the EU.

Of the three specific programmes under CIP, it is financial instruments of the Entrepreneurship and Innovation programme which will involve EIF. The windows proposed within this programme are:

- High Growth Innovative Companies Scheme for both early and expansion stage venture capital funds as well as co-investments in side-funds with business angels;
- SME Guarantee Facility (SME loan guarantees, microcredit guarantees, and equity and mezzanine guarantees), and an SME loan securitisation risk-sharing scheme;
- Capacity Building Scheme (Seed Capital Action and partnership with international finance institutions).

It is anticipated that the CIP windows to be operated by EIF will have a similarly high leverage effect as in MAP, optimising use of European Union funds to support SMEs' access to finance.

EIF will promote its business activities under CIP primarily through a new website, created and managed by EIF and financed by the European Commission, set up with the exclusive aim of providing SME-focussed information about the specific situation in each country where the CIP windows operate. EIF's "Access to Finance" website project began in September 2005, and the aim is to pilot the website in 2006, ready to be fully operational when CIP comes into force.

Discussions are currently underway to open CIP to technology transfer activities. In March 2005, the European Council urged EIF "to diversify its activities, in particular towards the financing of innovative SMEs through individual-investor (business-angel) and technology-transfer networks", an action which "should be supported by the new Community competitiveness and innovation programme".

The European Parliament committee also called in May 2005 for adequate funding for the support of innovative SMEs and initiatives aimed at helping the commercialisation of research and the transfer of technology, notably through EIF.

Preparatory Action

In 2005, EIF and EIB co-signed an agreement with the European Commission as part of the Commission's Preparatory Action "Support for SMEs in the New Financial Environment".

EIF is managing EIB Group's EUR 2m contribution, destined to fund Technical Assistance to credit institutions, which qualify for either an EIB global loan or an EIF guarantee.

The Preparatory Action's general objective is to improve the capacity of local, regional or cooperative financial institutions or banks to extend loans to SMEs, particularly micro-loans, in the ten new EU Member States whilst, in parallel, also developing the credit institutions' in-house administrative, assessment and monitoring abilities.

This contributes to one of EIF's main objectives of spreading best market practices in its business fields and addressing existing knowledge gaps across Europe.

JEREMIE

The Joint European Resources for Micro to Medium Enterprises initiative, known as JEREMIE, was launched in October 2005 as a key co-operation between the European Commission and EIB Group. JEREMIE is an important component of EIB Group's strategic orientation that includes cohesion, innovation and SMEs as Group priority objectives.

JEREMIE aims to optimise the European Union's cohesion policy instruments for SME finance in the European regions and reflects the emphasis placed by EU policies on market-based instruments, such as those operated by EIF under the MAP mandate.

The initiative will enable Member States and Acceding States (Bulgaria and Romania) to enhance European Regional Development Fund (ERDF) funding devoted to SMEs by transforming grants, which would otherwise be used as one-off allocations, into financial products that support SMEs' access to finance. The total ERDF allocation exceeds EUR 300bn for the period 2007-2013.

The programming phase (2006-2007) will be co-funded by the Directorate-General for Regional Policy and EIF's own resources. EIF will assess the gaps between supply and demand for SME access to finance in the ERDF-eligible regions and will propose action plans in the SME sector. EIF's evaluations will assist Member States and the European Commission to define operational programmes during the structural funds programming phase in 2006.

During the implementation phase (2007-2015) Member States and/or regions will have the option to open JEREMIE national and/or regional accounts using ERDF funds. EIB loans will complement the funding provided to these accounts through JEREMIE.

Member States and regions will select fundholders to provide financial products using ERDF funds for schemes at regional level, which accommodate local conditions. On the basis of EIF's evaluations, products will include venture capital, equity and guarantees, specifically engineered to support new and expanding micro-, small- and medium-sized enterprises.

JEREMIE will support non-grant instruments such as secured debt financing for subordinate debt, convertible instruments, mezzanine debt and risk capital such as seed and venture capital. Guarantee and mutual guarantee mechanisms will be used to facilitate SMEs' access to micro-credit. JEREMIE also foresees selected use of grants to build and maintain infrastructures that facilitate access to finance, for example, technology transfer offices, incubators, "business angels" networks and investment readiness programmes. Technical assistance will also be provided.

The initiative aims at leveraging ERDF funding with EIB Group and other international or national finance institution resources. It is too early to estimate the total ERDF budget that will be dedicated by Member States to JEREMIE – the success of this breakthrough initiative will depend on determining factors including the immediate availability of ERDF funding at programme level, the current project-by-project approach for the expertise provided by EIF and fundholders, and funding provided in the long term, by 2015.

EIF has established a JEREMIE implementation team to carry out evaluations to assist Member States, regions and the European Commission to define operational programmes during the structural funds programming phase. EIF's aim is to take an active role as a fundholder during the implementation phase from 2007, drawing on its expertise to promote SME finance on behalf of Member States and regions through a range of financial products, co-operating with national banks and multilateral development banks.

Technical assistance

In the course of 2005, Advisory Services concentrated on two main assignments, one for the Flemish Ministry of Economy, Enterprise, Science, Innovation and Foreign Trade, and one for the Centre for the Development of Industrial Technology (CDTI) in Spain, proposing innovative financial engineering and more specific expertise in the field of venture capital. Towards the end of the year, regional advisory moved within the JEREMIE initiative. Indeed, the development of Advisory Services since 2003 played a crucial role in the European Commission considering EIF as a central point of JEREMIE.

Cooperation with Flanders

In September 2005, the Flemish Government and EIF signed two agreements: a general cooperation agreement and a technical assistance contract.

The cooperation agreement aims to develop long-term cooperation between EIB Group and the Flemish Region, through exchanges of information, workshops, staff visits and personnel secondments.

The technical assistance contract is carried out on behalf of the Flemish Ministry of Economy, Enterprise, Science, Innovation and Foreign Trade. It involves assisting the Flemish Region in both evaluating and implementing programmes, which provide financial support to start-ups and SMEs and hence play a crucial role in the further development and prosperity of the Flemish economy.

The cooperation includes the ARKimedes programme, which is a fund investing funds raised in the broad public into new venture capital funds; the Vlaams Innovatiefonds (VINNOF), which is a seed fund specifically targeting very early stage technology ventures, and intended to leverage other sources of funding such as the Instituut voor Wetenschap en Technologie; the "waarborgregeling" system, a system of SME loan guarantees; and the "Non-Recurring Cost" fund (NRC), which will provide loans for the financing of long-term development projects.

CDTI

Throughout 2005, EIF worked with the Centro para el Desarrollo Tecnológico Industrial (CDTI), the Centre for the Development of Industrial Technology of the Spanish Ministry of Industry, Tourism and Commerce, carrying out a feasibility study for both a venture capital fund-of-funds targeting investments in Spanish SMEs fostering innovation and research and development, and a management company.

CDTI's mission is to support and promote innovation and technology development in Spain. Within this context the aim was to develop the Spanish government's own strategy in support of technology venture capital in cooperation with the private sector.

The assignment facilitated the transfer of good practice and EIF expertise, notably in the area of fund-of-funds management and was particularly successful, culminating in the launch of the CDTI fund-of-funds, as described in the venture capital section.

Technology Transfer

The Technology Transfer Accelerator project (TTA), carried out for and financed by Directorate-General Research (DG RTD) of the European Commission, sought to assess the feasibility of a new type of investment vehicle focusing on the financing gap between research and early stage investment. In September 2005, EIF's final report was published including the following key observations.

Firstly, existing European research and technology transfer structures suffer from a major lack of critical mass. European public research organisations remain largely fragmented.

Secondly, venture capital is largely absent from the seed phase notably because the amounts involved are often too small compared to the fund size and due to the high potential risk and the intense level of effort required for an investment. Furthermore, venture capitalists may have difficulties appraising opportunities largely based on technology, with limited information on business prospects and no track record, and they will often prefer to delay investment until a spin-off is sufficiently advanced.

Thirdly, a number of research commercialisation projects do not lend themselves to existing standard financing tools and techniques.

Fourthly, it is clear that the commercialisation of European research is lagging, since Europe does not enjoy advantages such as those seen, for example, in the United States, including the significantly larger R&D budgets; a large, homogeneous market; aggressive technology transfer organisations; the presence of numerous world-leading corporations, and a more developed and innovative seed and early stage venture capital scene.

EIF is in discussions with several potential market participants in order to set up a new financial vehicle, which would address unmet needs in technology transfer and the commercialisation of intellectual property (IP) by managing the IP from several research institutions/universities in order to have critical mass and leverage the experience. The vehicle would be responsible for marketing the licensing to industry partners and the creation of spin-off companies, as well as seeking both funding and coaching from investors in such a structure.

In parallel, to capitalise on the results of the TTA study, EIF is participating in two consortia: AFIBIO (Access to finance in the biotechnology sector), focusing on biotechnology and ACHIEVE, focusing on information and communication technology, both selected by DG RTD for Sixth Framework Programme funding.

AFIBIO's overall objective is to analyse the biotechnology and healthcare sectors' needs in terms of funding and R&D commercialisation. One of the aims is to develop an efficient network of key actors, and develop tools and guidance material for both entrepreneurs and investors. Goals also include the identification of sources of finance along the development chain, notably to improve support at the pre-seed and early development stages, and the elaboration of a rating system for seed/early stage investors whereby entrepreneurs rate their experience with various sources of finance for the benefit of other entrepreneurs.

ACHIEVE's main objective is to test the implementation of an entrepreneurship coaching scheme for innovative companies, which would take a project through conception, development, marketing and financing. The goal would be to thus increase the number of entrepreneurs successfully developing their innovations and bridge the gap between start-ups and early stage ventures and venture capitalists and other investors. Actions include the development of business building tools as well as the provision of individual support (e.g. mentoring) and small team coaching. ACHIEVE aims to build a network of incubators and an associated accreditation system to benchmark incubators and candidate enterprises. It will also organise the International Venture Capital Summit to bring together entrepreneurs and investors.

Cooperation with shareholders

EIF welcomes opportunities for business cooperation with its shareholders, from the financial institutions to the European Commission and the European Investment Bank. Within the EIB Group policy for increased cooperation and joint operations, a framework has been put in place for further operational synergies to reinforce access to SME financing. This involves products such as securitisation, and guarantees or counter-guarantees combined with EIB credit lines (global loans), as well as venture capital activities.

Ongoing mandates and potential new facilities with the European Commission attest to this successful collaboration, notably under the extended MAP and EIF's major role under the successor programme, CIP.

The JEREMIE and Preparatory Action initiatives also reflect the strengths of the institutions joining forces, together with EIB.

EIF has considerably developed its VC, securitisation and MAP guarantee activities with the financial shareholders and examples of joint collaboration are numerous, including with Kreditanstalt für Wiederaufbau, Bank Austria, Barclays and Banco Português do Investimento (securitisation); Raiffeisen Zentralbank Österreich AG (guarantees and securitisation, notably in the new Member States); Banca Intesa subsidiaries (securitisation and MAP); Caisse des dépôts et consignations and Sanpaolo IMI (venture capital); Encouragement Bank and Hungarian Development Bank Ltd. (MAP guarantee).

Staff contributions

Training

In 2005, EIF's Risk Management and Monitoring (RMM), with the support of the Fund's Investments and Legal services, developed a "Limited Partner Course" to contribute to inter-institutional training schemes. This course was designed in close collaboration with the European Commission's Directorate-General for Economic and Financial Affairs (DG ECFIN) and a first session was given to participants from DG ECFIN and DG ENTR (Directorate-General for Enterprise and Industry).

The course is largely based on the book "Beyond the J Curve" co-written by two RMM colleagues, Dr. Thomas Meyer and Pierre-Yves Mathonet. It combines theoretical and practical sessions in the form of case studies and covers a broad spectrum of subjects, ranging from the private equity environment, to the investment process, to design tools and to management tools.

Discussions are underway to present the course to a wider audience of private equity professional associations, and hence contribute to sharing and developing knowledge in the market.

Staff participated in numerous ongoing technical subjects and senior staff in management development programmes.

Publications

- *Liquiditätsmanagement in Private Equity und Venture Capital Dachfonds – Herausforderungen und Lösungsansätze.* Dr. T. Meyer & Dr. M.-J. Gschrei (& Associates). RWB Schriftenreihe Private Equity. Vol. 2. Munich (2005).
- *Exposed to the J-Curve.* U. Grabenwarter & Dr. T. Weidig (QuantExperts). Euromoney plc. January 2005.
- *Beyond the J Curve – Managing a Portfolio of Venture Capital and Private Equity Funds.* Dr. T. Meyer & P.-Y. Mathonet. John Wiley & Sons (2005).
- *Renditefaktor Kassenhaltung.* Dr. T. Meyer & Dr. M.-J. Gschrei. Venture Capital Magazine 06/2005.
- *The Case for Venture Capital.* Dr. T. Meyer & P.-Y. Mathonet. Alternative Fund Investment, September 2005.
- *Handbuch der regionalen Wirtschaftsförderung, Vol. 1.* Dr. H. Krämer-Eis & F. Riedl. Köln, July 1998. Vol. 1., B V, pp. 1-28, Köln, Nov. 2005. Eberstein, H.H. / Karl, H. (eds.).
- *An often misunderstood industry.* Dr. T. Meyer. Alternative Fund Investment, November 2005.

Further information and links on the above publications are available on **www.eif.org**

Risk Management and Monitoring

Overview

EIF aligns its risk management systems to changing economic conditions and evolving regulatory standards and therefore adapts them on an ongoing basis as best market practices develop. Credit, market and operational systems are in place to control and report on the main risks inherent to EIF's operations.

Risk Management and Monitoring (RMM) independently reports directly to the Chief Executive. This segregation of duties and the "four-eyes" principle ensure an unbiased review of EIF's business activities. Furthermore, within the EIB Group context, RMM operates in close contact with the European Investment Bank's Risk Management Directorate.

RMM encompasses four teams: a Risk Management team and an Administration and Monitoring team each for venture capital and for portfolio guarantees activities.

The basis for an effective risk management process is the identification and analysis of existing and potential risks inherent in any product. Hence RMM covers EIF's venture capital and guarantee activities, monitors risk regularly on individual transactions as well as on a portfolio level, and assesses new and old transactions.

For this purpose, RMM:

- reviews the risk management methodologies, processes, and instruments in use in EIF's Investments department;
- issues independent opinions on all transaction proposals;
- independently reviews internal ratings (portfolio guarantees) and grades (venture capital) assigned by Investments; and
- checks limits.

An overall portfolio view is compiled at regular intervals and is incorporated in the Asset Liability Management Framework which is being further improved. RMM is also responsible for the execution of on-site monitoring visits with regard to guarantee activities under the European Commission's mandates. Furthermore, over the last two years, RMM has been working on addressing Basel II implications for EIF's guarantee activities.

Risk assessment: venture capital

Over the last couple of years, EIF staff has developed an innovative toolset for its venture capital business in order to design, manage and monitor portfolios tailored to the dynamics of this market. An integrated IT system provides firm control over the operational risks and serves as a central reference point for front- and back-office staff.

Interaction between front office and risk management notably includes flash-reports to highlight "hot spots" in the portfolio and a grading-based methodology to determine the monitoring coverage and intensity as well as the range for the expected performance.

EIF portfolio management systems are not mechanical exercises, but rely on experienced staff, who conduct on-site visits, and check and question financial reporting.

Risk assessment/rating: portfolio guarantees

In accordance with EIF's Credit Risk Policy Guidelines, Guarantees and Securitisation, within the Investments department, assigns an internal rating to each new own risk guarantee transaction. The rating is based on a model, which summarises the transaction's credit quality, mapped to the rating agencies' models.

There are three key dimensions that EIF considers when entering into a new guarantee transaction: credit quality, Weighted Average Life, and minimum incremental return.

Capital allocation, provisioning and pricing are functions of the expected and unexpected loss, i.e. they vary according to the assigned rating. The individual internal rating is assigned upon closing and is revised quarterly for each transaction. Furthermore, the principle of "monitoring by exception" is applied. If there is an event which could cause an upgrade or a downgrade of a transaction, it triggers an analysis.

In the course of the independent opinion process for a potential new guarantee transaction, and in line with the Model Review Procedure, RMM conducts a Model Review for each new rating as well as sample checks of updated ratings. The purpose of the Model Review is to reduce the model risk, establishing guidelines for the use of all quantitative tools models for valuation and risk assessment within EIF. It defines, inter alia, that each basic model has to be independently reviewed within EIF and that assumptions made to adjust basic models for individual transactions have to be documented and reviewed by RMM.

The guarantee transactions are monitored regularly through:

- an ongoing risk review of each existing guarantee operation;
- checking for compliance with contractual obligations by the relevant counterparty (e.g. timely reporting, compliance with eligibility criteria, verification of financial covenants, timely payment of fee due, etc.);
- assessing the expected evolution of each guarantee operation in terms of its performance compared to ex-ante estimates set prior to signature;
- assessing whether the level of capital allocation and general provisions made for each operation are adequate and proposing, if deemed necessary, specific provisions for individual loss items;
- establishing and maintaining the Watch List (for transactions rated below Ba2) in accordance with the internal guidelines.

Furthermore, on the basis of the deal-specific analysis above, RMM carries out an analysis of the Guarantee Portfolio as a whole.

Basel II

Basel II has implications for EIF's guarantees business as it is expected to result, on the one hand, in a moderate reduction of regulatory capital for loans to smaller SMEs (retail segment) and, on the other hand, in an increase for mid-sized SMEs. In view of the BIS II capital charges on securitisation exposures, the use of SME securitisation is likely to expand under the Basel II rules. As most of the economic capital is in fact attributable to mezzanine tranches, the success in identifying investors for these tranches determines the continued growth of this asset class in Europe. EIF is expected to play an important role as catalyst for other investors. Indeed, EIF considers that a number of SME securitisations would not have been closed in 2005 without EIF's participation.

Over the last two years, EIF has been progressively working towards addressing the quantification of risks under the New Basel Accord. EIF's Grading-based Economic Model gives a forecast for the portfolio lifetime investment return. In other words, it projects the range of likely outcomes for the portfolio on maturity and eliminates temporary "J-curve" effects. The return measure used is the pooled Internal Rate of Return, taking into account the timing and amount of the cash flows generated from venture capital investments using EIF own resources. This approach allows a number of "at risk" measures to be calculated for EIF's venture capital portfolio.

EIF services have been closely cooperating with EIB on various issues including consolidation of risk exposures at Group level. Contacts have been established with the Luxembourg financial supervisory authority (CSSF – Commission de Surveillance du Secteur Financier) in order to verify the Group's risk methodologies and systems in the run-up to the Basel II implementation. One of the requirements of Basel II is that all activities within a group be consolidated for risk and capital measurement purposes and, in particular, that EIB and EIF services cooperate in the areas of operational risk, venture capital and Asset-Backed Securitisation/ guarantee operations. EIF will implement, with the support of EIB Risk Management (RM) and in agreement with the CSSF, an Operational Risk framework in line with the one already in place at EIB.

In close cooperation and regular consultation with EIB RM, it has been agreed that EIF will take the lead role in preparing and presenting two common methodologies to the CSSF. Firstly, given that EIF has the European VC fund expertise within EIB Group, it will prepare capital adequacy measurement for Group activities in this field. Secondly, as EIF has already been following a risk-based internal rating and capital allocation approach for its securitisation and guarantee operations, EIF's Guarantees and Securitisation will prepare a common methodology for EIB Group ABS/guarantee activities.

Provisioning

The tables below illustrate the annual amounts set aside for the venture capital portfolio value adjustment using EVCA II compliant valuation methodology and SME guarantees provisioning (to cover the expected loss). Value adjustments include management fees paid to fund managers, but principally provisions for lower net asset values of the funds. Up until 31/12/05, value adjustments did not include unrealised capital gains, which at 31/12/05 and since the portfolios' inceptions, totalled EUR 64.1m for the RCM (EUR 29.4m at 31/12/04); EUR 9.8m for own resources (EUR 7.0m at 31/12/04); and EUR 19.6m for the European Commission (EUR 2.9m at 31/12/04).

Venture capital: value adjustments/write-backs

	2001	2002	2003	2004	2005
EIF VC portfolio	-2.9	-11.3	-10.9	-5.4	0.3
EIB VC portfolio	-31.0	-150.7	-114.1	-78.7	-25.8
EC VC portfolio	-4.5	-7.3	-12.4	-10.0	8.2

SME Guarantees: provisioning

	2001	2002	2003	2004	2005
Provisions relating to guarantees	-19.7	-3.6	-3.7	-4.3	-3.7

Figures for 2001 include provisions related to the TENs Guarantees Portfolio subsequently transferred to EIB.
From 2002 onwards, the provisioning policy was amended.

Risk assessment of treasury management

EIF treasury investments, at end 2005, totalled EUR 551m and consisted of short-term and long-term treasury with the objective of maintaining an adequate level of liquidity. For accounting purposes, treasury is divided into an investment portfolio mainly composed of high quality bonds held to maturity, an available-for-sale portfolio comprising floating rate notes and an operational portfolio including term deposits up to three months. In addition, an overdraft facility has been formalised, allowing an access to EUR 50m within three business days.

Credit risk policy for treasury transactions is monitored through the attribution of credit limits to the counterparties for short-term and long-term transactions. Weighted exposure for each counterparty must not exceed the authorised limit.

EIF's own resources treasury management is outsourced to EIB. The table below illustrates the size and credit quality of EIF's various treasury portfolios at 31/12/05.

Nominal exposure (EUR m)

	Short Term External Rating	Long Term External Rating				
Portfolio/Rating	A-1+ / P-1	<A or NR	A	AA	Aaa	**Total**
Operational Portfolio	61.0	-	-	-	-	**61.0**
AFS Portfolio	-	-	-	-	48.4	**48.4**
Investment Portfolio	-	-	52.8	115.7	248.5	**417.0**
Total nominal treasury funds	**61.0**	**-**	**52.8**	**115.7**	**296.9**	**526.3**

IFRS

EIF's work to produce figures consistent with International Financial Reporting Standards (IFRS) has been a critical project throughout 2005.

EIF began its project to implement IFRS in 2004 and by 2005 followed IFRS rules for EIB Group reporting consolidation and in relation to the fiduciary mandates managed by EIF on behalf of the European Commission. EIF will publish IFRS stand-alone financial statements for the year ended 31/12/06.

The primary challenge has been to address the fair value principle for EIF's specific business lines, notably because of the fund-of-funds nature of venture capital operations. Standard IAS 39 was identified as having a major impact on EIF's business, as this standard requires "fair value" accounting for non-quoted equity, as well as for treasury portfolio valuation and potentially for the portfolio guarantees. However, other IFRS standards also have implications for EIF including IAS 37, 18 and 4 for guarantee operations and IAS 19 for the pension scheme.

EIF's services mobilised external support in response to the IFRS exercise and activity was intense throughout the year. Experience of IFRS in the venture capital industry is still limited and a standardised methodology for valuations has yet to be determined. EIF, however, has developed an enhanced Net Asset Value approach for its venture capital mandates, which is compatible with audit requirements and has been endorsed by EIF's external auditors.

In the course of 2006, further IFRS procedures will be defined, notably the disclosures in the notes to the accounts and the valuation of the portfolio guarantee, for which industry norms were only finalised in summer 2005.

Audit and controls

EIF's principal audit and control mechanisms include both internal and external auditors working under the supervision of the Audit Board, which maintains the independence and integrity of the audit function. EIF's internal and external auditors liase with the internal and external auditors of EIB, and those of the European Commission, with regard to the fiduciary mandates.

EIF is also audited by the European Court of Auditors for programmes mandated to EIF by the European Commission. In relation to the Commission's shareholder participation in EIF, the Court of Auditors operates within a specific tripartite agreement that permits audit of the participation's value.

The audit methodology used at EIF is the External Control Framework mechanism that covers all key business processes. EIF equally operates a comprehensive Internal Control Framework with its Internal Auditor. Furthermore, an independent evaluation on the effectiveness of EIF's venture capital investments on the development of this market in Europe is being carried out.

In 2005, EIF's Rules of Procedure were modified to enhance the Audit Board's role, notably in terms of producing an annual activity report, which is published in full on EIF's website, and in meeting the Board of Directors on an annual basis. A Code of Conduct, which defines the rules and principles which apply to all the Audit Board's members, was approved in June 2005 and is equally to be found on EIF's website. Finally, in 2005, the Audit Board conducted a review of its role and methods of operating, resulting in an Audit Board Charter, approved in 2006, and the drafting of a procedures manual.

Compliance

The EIF Compliance function was established in early 2005 with the remit to identify, assess, advise on, monitor and report on compliance risk. The structure and tasks of EIF Compliance have been established on the basis of the 2005 recommendations of the Basel Committee on Banking Supervision. It operates with full independence from EIF management, other EIF services or EIF stakeholders.

The core competences of EIF Compliance relate to protection against reputational risk, advice and control in relation to governance issues and safeguarding against money laundering and insider dealing. In addition, EIF Compliance advises on corporate responsibility and business ethics, and reviews all investment proposals. The competences of EIF Compliance and its integration in the internal procedures are laid down in the EIF Compliance Procedure and the EIF Compliance Charter. The EIF Compliance Charter is published on EIF's website.

EIF Compliance reports directly to the Secretary of the Fund and, in specific cases, addresses the Board of Directors. It cooperates with the EIB Group Chief Compliance Officer on Group-related polices and issues. As EIF is a Community body, EIF Compliance also works with the European Commission to identify, assess and monitor compliance with the Community policies that are relevant to EIF's business. EIF Compliance works with industry bodies for best business practice.

EIF Compliance has issued statements on Governance and Corporate Social Responsibility and opinions on areas relating to governance, operational guidelines and individual operations. A report on compliance is presented annually to the Board of Directors. EIF Compliance is a strong new element of the EIF governance structure that will be further developed in 2006.

Results for the financial year

Independent Auditor's Report

To the Audit Board
of the EUROPEAN INVESTMENT FUND
43, avenue J. F. Kennedy
L-2968 Luxembourg

Following our appointment by the Audit Board, we have audited the accompanying annual accounts of the EUROPEAN INVESTMENT FUND for the year ended December 31, 2005. These annual accounts are the responsibility of the Board of Directors. Our responsibility is to express an opinion on these annual accounts based on our audit.

We conducted our audit in accordance with International Standards on Auditing. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the annual accounts are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the annual accounts. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall annual accounts presentation. We believe that our audit provides a reasonable basis for our opinion.

In our opinion, the attached annual accounts give, in accordance with the general principles of the Council Directives of the European Union on the annual accounts and consolidated accounts of banks and other financial institutions, a true and fair view of the financial position of the EUROPEAN INVESTMENT FUND as of December 31, 2005 and of the results of its operations and its cash flows for the year then ended.

PricewaterhouseCoopers S.à r.l.
Réviseur d'Entreprises
Represented by

Luxembourg, 24 February 2006

Pierre Krier

Statement by the Audit Board

The Audit Board, set up pursuant to article 22 of the Statutes of the European Investment Fund (EIF),

- having designated PricewaterhouseCoopers s.à.r.l. Réviseur d'Entreprises as external auditor of the EIF,
- acting in accordance with the customary standards of the audit profession,
- having studied the financial statements […] and such documents which it deemed necessary to examine in the discharge of its duties,
- having examined and discussed the report dated 24 February 2006 drawn up by PricewaterhouseCoopers s.à.r.l. Réviseur d'Entreprises,
- noting that this report gives an unqualified opinion on the financial statements of EIF for the financial period ending 31 December 2005

considering Articles 17, 18 and 19 of the Rules of Procedure,

hereby confirms

- that the operations of the Funds have been carried out in compliance with the formalities and procedures laid down in the Statutes, the Rules of Procedure and the guidelines and directives […] adopted by the Board of Directors;
- that the annual accounts, comprising the balance sheet, […] profit and loss account, cash flow statement and notes to the accounts of the European Investment Fund give a true and fair view of the financial position of the Fund in respect of its assets and liabilities, and of the results of its operations for the financial year under review.

Luxembourg, 24 February 2006

THE AUDIT BOARD

Sylvain Simonetti   Hannu Lipponen   Raimundo Poveda Anadón

Balance sheet at 31 December 2005

EUR

ASSETS	Notes	2005	2004
Cash at bank and in hand	3.1		
Current accounts		24 662 133	34 850 979
Term deposits		48 500 000	51 500 000
		73 162 133	**86 350 979**
Debt securities and other fixed-income securities	3.2, 3.4	477 804 919	458 819 917
Shares and other variable income securities	3.3, 3.4	89 766 315	70 355 318
Intangible fixed assets	3.4	1 217 367	1 393 078
Tangible and other fixed assets	3.4	4 520 456	4 575 816
Other assets	3.5	10 374 032	8 696 382
Prepayments and accrued income	3.6	18 070 406	14 749 526
TOTAL ASSETS		**674 915 628**	**644 941 016**

OFF-BALANCE SHEET ITEMS			
Guarantees issued	5.1		
On drawn		2 955 820 269	2 912 062 998
On undrawn		101 250 177	131 039 293
		3 057 070 446	**3 043 102 291**
Commitments	5.3	103 027 172	104 212 743
Assets held for third parties	5.4	330 445 113	250 617 974
Fiduciary operations	5.5	8 802 309 137	7 474 830 878
	5.6	**12 292 851 868**	**10 872 763 886**

LIABILITIES			
Creditors	4.1	1 274 379	5 023 188
Accruals and deferred income	4.2	15 011 299	15 845 846
Provisions for liabilities and charges			
Provisions relating to guarantees	4.3	29 953 934	30 656 978
Provisions relating to pensions and similar obligations	4.4	6 551 001	4 644 296
Other provisions		3 557 349	2 183 906
		40 062 284	**37 485 180**
Capital	4.5		
Subscribed		2 000 000 000	2 000 000 000
Uncalled		-1 600 000 000	-1 600 000 000
		400 000 000	**400 000 000**
Share premium account		12 770 142	12 770 142
Statutory reserve	4.6	67 755 278	62 314 590
Profit brought forward	4.6	95 181 382	84 298 631
Profit for the financial year	4.6	42 860 864	27 203 439
TOTAL LIABILITIES		**674 915 628**	**644 941 016**

The accompanying notes form an integral part of these annual accounts.

Profit and loss account for the year ended 31 December 2005

EUR

	Notes	2005	2004
Net interest and similar income	6.1	22 597 900	22 256 429
Income from securities			
Income from investments in venture capital funds		1 893 192	890 120
Commission income	6.2	35 507 169	28 565 954
Net profit / (loss) on financial operations	6.3	1 553 038	-691 592
Other operating income	6.5	2 165 391	27 319
General administrative expenses:			
Staff costs:			
– wages and salaries	6.4	-10 533 004	-8 578 721
– social security costs of which: EUR 755 622 relates to pension contributions (2004: EUR 647 533)		-1 232 734	-1 008 265
		-11 765 738	**-9 586 986**
Other administrative expenses		-4 758 224	-3 975 887
		-16 523 962	**-13 562 873**
Value adjustments in respect of tangible and intangible fixed assets		-937 025	-600 295
Value adjustment in respect of shares and other variable income securities	3.3	269 899	-5 392 432
Provisions for commitments	4.3	-3 664 738	-4 289 191
Profit for the financial year		**42 860 864**	**27 203 439**

The accompanying notes form an integral part of these annual accounts.

Cash flow statement for the year ended 31 December 2005

EUR

	2005	2004
Cash flows from operating activities		
Profit for the financial year	*42 860 864*	*27 203 439*
Value adjustments in respect of tangible & intangible fixed assets	937 025	600 295
Value adjustments in respect of shares & other variable income securities	(1 585 162)	5 482 482
Net increase / (decrease) in provisions for commitments	(703 043)	3 202 385
Net increase / (decrease) in provisions relating to pensions & similar obligations	460 000	150 000
Profit on operating activities	*41 969 684*	*36 638 601*
Decreases / (increases) in other assets	(1 677 650)	(5 320 371)
Decreases / (increases) in prepayments & accrued income	(3 320 880)	413 787
Increases / (decreases) in creditors & other provisions	(2 375 367)	3 472 450
Increases / (decreases) in accruals & deferred income	(834 547)	(160 892)
Increases / (decreases) in contributions relating to pension & similar obligations	1 446 705	1 792 174
Net cash from operating activities	**35 207 945**	**36 835 749**
Cash flows from investing activities		
Decreases / (increases) in tangible & intangible fixed assets	(705 953)	(861 128)
Net decreases / (increases) in shares & other variable income securities	(17 825 836)	(15 967 787)
Net decreases / (increases) in debt securities & other fixed income securities	(18 985 002)	20 114 913
Net cash from investing activities	**(37 516 791)**	**3 285 998**
Cash flows from financing activities		
Dividends paid	(10 880 000)	(7 894 000)
Net cash from financing activities	**(10 880 000)**	**(7 894 000)**
Summary statement of cash flows		
Cash at bank and in hand at the beginning of the financial year	86 350 979	54 123 231
Net cash from:		
Operating activities	35 207 945	36 835 750
Investing activities	(37 516 791)	3 285 998
Financing activities	(10 880 000)	(7 894 000)
Cash at bank & in hand at the end of the financial year	**73 162 133**	**86 350 979**

The accompanying notes form an integral part of these annual accounts.

Notes to the annual accounts

1. General

The EUROPEAN INVESTMENT FUND (hereafter the "Fund") was incorporated on June 14, 1994 as an international financial institution.

The primary task of the Fund, while providing adequate return on equity, is to contribute to the pursuit of European Community objectives through

the provision of guarantees; the acquisition, holding, managing and disposal of equity participations; the administration of special resources entrusted by third parties, and related activities.

The Fund operates as a partnership the members of which are the European Investment Bank (hereafter the "EIB"), the European Union, represented by the Commission of the European Communities (the "Commission"), and a group of financial institutions of Member States of the European Union and of one acceding state. The members of the Fund shall be liable for the obligations of the Fund only up to the amount of their share of the capital subscribed and not paid in.

The financial year of the Fund runs from January 1 to December 31 each year.

As detailed in note 4.5, the EIB has a majority shareholding in the Fund. Consequently the Fund is included in the consolidated accounts of the EIB Group. The consolidated accounts may be obtained from the registered office of the EIB at 100, boulevard Konrad Adenauer, L-2950 Luxembourg.

2. Accounting policies and presentation of annual accounts

2.1 Presentation of annual accounts

The Fund's annual accounts are based on the general principles of the Council Directive of the European Communities 86/635/EEC of December 8, 1986 as amended by the Council Directive 2001/65/EC of September 27, 2001 relating to the annual accounts and consolidated accounts of banks and other financial institutions.

These annual accounts have been prepared in accordance with the historical cost convention, using the accounting policies set out below.

2.2 Valuation of foreign currency balances and transactions

The share capital of the Fund is expressed in euro ("EUR") and the accounting records are maintained in that currency. Non-monetary items, which include "Intangible fixed assets" and "Tangible and other fixed assets" denominated in a foreign currency are reported using the exchange rate at the date of the transaction (historical cost).

Monetary items, which include all other assets, liabilities, and off-balance sheet items expressed in a currency other than EUR are reported using the closing foreign exchange rate ruling on the date of the closure of the annual accounts, as issued by the European Central Bank.
Income and charges in foreign currencies are translated into EUR at the exchange rate ruling on the date of the transaction.

Other exchange differences arising from the translation of monetary items are recognised in the profit and loss account in the period in which they arise.

2.3 Debt securities and other fixed-income securities

Debt securities and other fixed-income securities are categorised and valued as follows:

- floating rate notes with maturities exceeding one year and fixed rate notes other than commercial paper are included in the "Investment Portfolio" and are valued at the lower of cost or market value and respectively at amortised cost.
- floating rate notes and commercial paper with maturities of less than one year are included in the "Short-term Portfolio" and are shown at nominal value.

Premiums paid over the maturity value, and discounts received in comparison to the maturity value of securities, are taken to the profit and loss account in equal instalments over the remaining period to maturity. The net cumulative amortisation of premiums and discounts from the date of acquisition is included in "Accruals and deferred income" or "Prepayment and accrued income" in the balance sheet.

2.4 Investments in venture capital funds

Investments in venture capital funds are included in "Shares and other variable income securities". They are acquired for the longer term in the normal course of the Fund's activities and are shown in the balance sheet at their original purchase cost.

Based on the reports received from fund managers up to the balance sheet date, the investments in venture capital are valued on a line-by-line basis at the lower of cost or attributable net asset value ("NAV"), thus excluding any attributable unrealised gain that may be prevailing in this portfolio.

The attributable net asset value is determined through applying either the Fund's percentage ownership in the underlying vehicle to the net asset value reflected in the most recent report or, to the extent available, the precise share value at the date of such report, submitted by the respective fund manager.

For the final valuation, the attributable net asset value is adjusted for the events having occurred between the available NAV date and the balance sheet date to the extent that it is considered to be material.

Investments in venture capital funds in existence for less than two years at balance sheet date are valued based on the same principles. Unrealised losses due only to administrative expenses of these recently created funds will however be ignored.

2.5 Intangible and tangible fixed assets

Intangible fixed assets include the development costs of software that are capitalised under specific conditions such as identifiable expenses or existence of a future benefit for the Fund.

Intangible and tangible fixed assets are valued at purchase price, including the expenses incidental thereto, reduced by accumulated value adjustments calculated to write off the value of such assets on a straight line basis over their expected useful life as follows:

	Useful life
Intangible fixed assets:	
Software	2 to 5 years
Internally developed software	3 years
Tangible fixed assets:	
Buildings	30 years
Fixtures and fittings	3 to 10 years
Office equipments	3 to 5 years
Computer equipments and vehicles	3 years

2.6 Provisions relating to guarantees

Provisions relating to guarantees have been calculated in line with the methodology set out in the Fund's Credit Risk Policy Guidelines approved by the Board of Directors on December 4, 2001, as amended by the Board of Directors on May 4, 2004.

It results, as far as general provision is concerned, in a valuation of the provisioning requirements based on credit ratings, done transaction-by-transaction.

On a prospective basis, for the operations signed since January 1, 2002 the provisioning requirements are built up during the two thirds of the weighted average life of the guarantees in order to better conform with fair value accounting principles. The provisioning requirements remain booked in full for the guarantee operations signed until December 31, 2001. In addition, where it has been felt appropriate, a specific provision has been built up.

2.7 Provisions relating to pensions and similar obligations

The main pension plan of the European Investment Fund is a contributory defined benefit pension scheme, which covers all employees. It has entered into force in March 2003, replacing a defined contribution pension scheme. All contributions of the Fund and its members of staff are transferred to the EIB for management and are invested by the EIB, in accordance with the rules and principles applied by the EIB for its own pension scheme. The amount transferred to the EIB for management is included under the heading "Other assets". The annual contributions are set aside and accumulated as a specific provision on the liabilities side of the Fund's balance sheet, together with annual interest.

Commitments for retirement benefits are to be valued on a periodic basis using the "projected unit credit method" to ensure that the provision recorded in the accounts is fairly stated.

2.8 Guarantees issued

The amount disclosed in respect of issued guarantees represents the total commitment which refers to both the drawn and un-drawn principal amounts of the underlying loans and, if relevant, to the present value of the flow of future interest payments covered by the guarantees.

2.9 Net interest and similar income

Interest and similar income are recognised on a time proportion basis. The gross amount of interest and similar income received is reduced by premiums on fixed-income securities amortised during the financial year, and interest and similar expenses paid.

2.10 Commission income

Up-front commissions received for arranging and granting guarantees are recognised when a binding obligation has been entered into.

Guarantee commissions received are recognised on a time proportion basis over the life of the guarantee.

3. Detailed disclosures relating to asset headings

3.1 Cash at bank and in hand

The remaining life of cash at bank and in hand is as follows:

	2005 EUR	2004 EUR
Repayable on demand	24 662 133	34 850 979
Up to three months	48 500 000	51 500 000
	73 162 133	**86 350 979**

3.2 Debt securities and other fixed-income securities

Debt securities and other fixed-income securities are analysed as follows:

	2005 EUR	2004 EUR
Short-term Portfolio	12 500 000	40 001 500
Investment Portfolio	465 304 919	418 818 417
	477 804 919	**458 819 917**

Debt securities and other fixed-income securities held by the Fund are all listed on a recognised market.

Debt securities and other fixed-income securities with a remaining duration to maturity of less than one year amount to EUR 60 877 625.

The market value of the debt securities and other fixed-income securities amounts to EUR 493 219 583 (2004: EUR 477 680 034).

The Fund participates as lender in a Securities Lending and Borrowing Programme with three counterparties, resulting in an increased security lending balance and revenue in the last two months of the year. The market value of securities lent at year-end amounts to EUR 39 466 869 (2004: EUR 58 220).

3.3 Shares and other variable income securities

Shares and other variable income securities include investments in venture capital funds and are analysed as follows:

	2005 EUR	2004 EUR
Net disbursed amount at cost	120 644 615	102 818 779
Value adjustment	(30 310 466)	(30 580 365)
Unrealised loss on foreign currencies	(567 834)	(1 883 096)
	89 766 315	**70 355 318**

Investments in venture capital funds represent equity investments and related financing structures.

The unrealised gains on these investments, which are not recorded in the accounts, in accordance with the valuation method described in note 2.4, amount to EUR 9 763 782 (2004: EUR 7 047 415).

The unrealised foreign exchange loss arising from the revaluation of venture capital funds at year-end closing rates amounts to EUR 567 834 (2004: unrealised loss of EUR 1 883 096). In accordance with the Fund's provisioning policy this amount is included in the exchange loss of the year.

3.4 Movements in fixed assets (expressed in EUR)

HEADINGS	Purchase Price at the beginning of the year	Additions	Disposals	Purchase Price at the end of the year	Cumulative value adjustments at the end of the year	Carrying amount at the end of the year
Debt securities and other fixed income securities (investment portfolio)	418 818 417	99 160 855	(52 672 853)	465 306 419	(1 500)	465 304 919
Shares & other variable income securities	102 818 779	30 287 442	(12 461 605)	120 644 616	(30 878 301)	89 766 315
Intangible fixed assets	1 990 313	414 973	0	2 405 286	(1 187 919)	1 217 367
Tangible and other fixed assets of which:	6 595 995	290 981	0	6 886 976	(2 366 520)	4 520 456
a) Land & Buildings	5 161 380	0	0	5 161 380	(1 331 733)	3 829 647
b) Fixtures & fittings	357 470	0	0	357 470	(215 081)	142 389
c) Office equipment	685 798	82 719	0	768 517	(440 124)	328 393
d) Computer equipment	298 510	208 262	0	506 772	(295 509)	211 263
e) Vehicles	84 073	0	0	84 073	(84 073)	0
f) Other fixed assets	8 764	0	0	8 764	0	8 764
Total	**530 223 504**	**130 154 251**	**(65 134 458)**	**595 243 297**	**(34 434 240)**	**560 809 057**

3.5 Other assets

Following the introduction of a defined benefit pension scheme in 2003 (see note 2.7), "Other assets" include the assets of the pension scheme transferred to the EIB for management and investment on behalf of the Fund. The movements for the year are as follows:

	2005 EUR	2004 EUR
Pension contributions	3 415 959	2 401 923
Net pension fund rights purchased/sold	1 138 402	1 080 403
Pension risk fund	1 310 000	850 000
Optional Supplementary Pension Scheme	307 315	249 514
Interests earned on Pension funds	673 270	326 276
Accounts receivable relating to pensions managed by the EIB	**6 844 946**	**4 908 116**
Other debtors	3 529 086	3 788 266
	10 374 032	**8 696 382**

The 2004 figures detailing the breakdown of Accounts receivable relating to pensions have been reviewed and re-stated to ensure on-going comparability. The total figure of EUR 4 908 116 is unaffected. See also note 4.4.

3.6 Prepayments and accrued income

Prepayments and accrued income are analysed as follows:

	2005 EUR	2004 EUR
Prepayment	16 500	0
Interest receivable on debt securities	11 093 763	10 423 692
Interest receivable on term deposits	59 648	53 920
Accrued commission on guarantees & management fees	6 900 495	4 271 914
	18 070 406	**14 749 526**

4. Detailed disclosures relating to liability headings

4.1 Creditors

Creditors are analysed as follows:

	2005 EUR	2004 EUR
Trade creditors and other payables	926 868	3 410 119
Optional Supplementary Pension Scheme	341 511	259 070
Current account with EIB	6 000	1 353 999
	1 274 379	**5 023 188**

4.2 Accruals and deferred income

Accruals and deferred income are analysed as follows:

	2005 EUR	2004 EUR
Deferred income on issued guarantees	8 303 325	11 851 932
Premium amortised on "Investment portfolio"	6 692 088	3 993 914
Deferred income on commercial paper	15 886	0
	15 011 299	**15 845 846**

As mentioned in the note 2.3, the discounts and premiums are netted. Discounts amount to EUR 2 459 869 (2004: EUR 3 352 891) and premiums amount to EUR 9 151 957 (2004: EUR 7 346 805). The total amount of discounts and premiums to be accrued on the remaining life of these securities respectively amounted to EUR 2 355 451 (2004: 2 730 027) and EUR 8 064 901(2004: EUR 6 116 848).

4.3 Provisions for commitments

The movements relating to provisions in respect of contingent losses that may arise from the guarantee portfolio are set out below:

	2005 EUR	2004 EUR
Balance at the beginning of the financial year	30 656 978	27 454 593
Transfer relating to SME guarantees	3 664 738	4 289 191
Utilisation of the provision	(1 951 332)	(1 086 806)
Correction from prior years	(2 416 450)	0
Balance at the end of the financial year	**29 953 934**	**30 656 978**

The balance of EUR 29 953 935 (2004: EUR 30 656 978) solely pertains to the Fund's own risk SME guarantee portfolio. For corrections from prior years, see also notes 6.2 and 6.5.

4.4 Provisions relating to pensions and similar obligations

Commitments in respect of retirement benefits as at December 31, 2005 have been valued in January 2006 by an independent actuary using the projected unit credit method. The calculations are based on the following main assumptions:

- A discount rate of 4.31% for determining the actuarial present value of benefits accrued;
- A retirement age of 62;
- Probable resignation of 3% up to age 55;
- Use of Swiss BVG 2000 actuarial tables.

The commitment as evaluated in the independent actuary report dated February 7, 2006 amounts at EUR 5 869 000. As of December 2005, the Fund has allocated EUR 6 551 001 to the provisions relating to pensions to ensure full coverage of the commitments.

The movements in the "provisions relating to pensions and similar obligations" are as follows:

	2005 EUR	2004 EUR
Provision at December 31, 2004	4 644 296	2 702 122
Contributions during the year	1 906 705	1 942 174
Provision at December 31, 2005	**6 551 001**	**4 644 296**

The Board of Directors in its meeting of December 3, 2002 approved the principle of the creation of a defined benefit pension fund replacing the previous defined contribution pension scheme. Following the advice of an independent actuary a risk fund with an initial amount of EUR 550 000 was set up.

Following the allocation of EUR 460 000 for 2005 (2004: EUR 150 000), this fund now amounts to EUR 1 310 000. Also refer to notes 2.7 and 3.5. This amount is recorded in the profit and loss account under "Other administrative expenses".

The above figures do not include the liability towards members of staff in respect of the Optional Supplementary Pension Scheme (a contributory defined benefit pension scheme). The corresponding amount of EUR 341 511 (2004: EUR 259 070) is included under "Creditors".

4.5 Capital

The authorised capital amount to EUR 2 billion, divided into 2 000 shares with a nominal value of EUR 1 000 000 each. The subscribed share capital of EUR 2 000 000 000 representing 2 000 shares is called for an amount of EUR 400 000 000 representing 20% of the subscribed share capital.The subscribed share capital is detailed as follows:

	2005 EUR	2004 EUR
Subscribed and paid in (20%)	400 000 000	400 000 000
Subscribed but not yet called (80%)	1 600 000 000	1 600 000 000
Balance at the end of the year	**2 000 000 000**	**2 000 000 000**

The capital is subscribed as follows :

	2005 Number of shares	2004 Number of shares
European Investment Bank	1 238	1 183
European Commission	600	600
Financial Institutions	162	217
	2 000	**2 000**

4.6 Statutory reserve and profit brought forward

Under the terms of Article 27 of its Statutes, the Fund is required to appropriate to a statutory reserve at least 20% of its annual net profit until the aggregate reserve amounts to 10% of subscribed capital. Such reserve is not available for distribution.

A minimum amount of EUR 8 572 173 is required to be appropriated in 2006 with respect to the financial year ended December 31, 2005. Movements in reserves and profit brought forward are detailed as follows (in EUR):

	Statutory reserve	Profit brought forward	Profit for the financial year
Balance at the beginning of the financial year	62 314 590	84 298 631	27 203 439
Dividend paid			(10 880 000)
Other allocation of last financial year profit	5 440 688	10 882 751	(16 323 439)
Profit for the financial year			42 860 864
Balance at the end of the financial year	**67 755 278**	**95 181 382**	**42 860 864**

The General Meeting of Shareholders of April 12, 2005 approved the distribution of a dividend amounting to EUR 10 880 000 relating to the year 2004 (2003: EUR 7 894 000), corresponding to EUR 5 440 per share.

5. Disclosures relating to off-balance sheet items

5.1 Guarantees

5.1.1 SME Guarantees

Guarantees issued are analysed with reference to their maturity as follows:

	Drawn EUR	Undrawn EUR	Total 2005 EUR	Total 2004 EUR
Up to five years	177 058 656	286 529	177 345 185	498 592 428
From five to ten years	503 154 461	59 645 668	562 800 129	367 663 408
From ten to fifteen years	936 703 022	9 567 980	946 271 002	948 226 129
Over fifteen years	636 465 654	15 000 000	651 465 654	269 697 049
	2 253 381 793	**84 500 177**	**2 337 881 970**	**2 084 179 014**

Of the above total amount, EUR 10 582 915 (2004: EUR 18 741 651) has been issued in favour of the EIB.

The drawn down portion of the guarantees issued includes an amount of EUR 1 286 849 representing the present value of future interest for guarantees contracts in default (2004: EUR 1 182 775).

5.1.2 TEN Guarantees

TEN infrastructure guarantee operations, complementary to EIB's activities, have been transferred to the latter. The relevant contract was signed with the EIB on December 7, 2000. The EIB assumes the advantages of the transferred portfolio, but also bears the ultimate risk of the transactions, the Fund remaining merely a guarantor of record.

	Drawn EUR	Undrawn EUR	Total 2005 EUR	Total 2004 EUR
Up to five years	169 390 462	0	169 390 462	386 999 004
From five to ten years	254 695 063	0	254 695 063	301 573 045
From ten to fifteen years	202 082 218	16 750 000	218 832 218	188 255 965
Over fifteen years	76 270 733	0	76 270 733	82 095 263
	702 438 476	**16 750 000**	**719 188 476**	**958 923 277**

The drawn down portion of the guarantees issued includes an amount of EUR 18 599 037 (2004: EUR 25 306 165) representing the present value of future interest covered by guarantees.

5.2 Statutory ceiling on the overall commitments for operations

As regards guarantee operations, under the terms of Article 26 of the Fund's Statutes, the overall commitment of the Fund, excluding commitments made by the Fund on behalf of third parties, may not exceed three times the amount of its subscribed capital for guarantee operations.

The present level of subscribed capital establishes a ceiling of EUR 6 000 000 000 in relation to total guarantees outstanding committed by the Fund currently totalling EUR 2 337 881 970 (2004: EUR 2 084 179 014).

The TEN guarantee operations managed by the Fund on behalf of EIB are not included in the above amount of guarantees outstanding in view of the risk thereon having been taken over by the EIB EUR 719 188 476 (2004: EUR 958 923 277).

The ceiling decided by the General meeting pursuant to Article 12 and Article 26 of the Statutes and presently applied in respect of the Fund's own venture capital operations is 50% of own funds. Taking into account the 2005 results, the ceiling stands at EUR 300 711 514 (reduced by the proposed 2005 dividend payment) whilst the commitments in respect of the venture capital operations at current rate amount to EUR 267 765 296 (2004: EUR 236 935 960).

5.3 Commitments

Commitments represent investments in venture capital funds committed and not yet disbursed amounting to EUR 103 027 172 at current rate (2004: EUR 104 212 743).

5.4 Assets held for third parties

Assets held for third parties, as set out below, represent trust accounts opened and maintained in the name of the Fund but for the benefit of the Commission, the EIB and the German Federal Ministry of Economics and Technology (Bundesministerium für Wirtschaft und Technologie "BMWi"). Sums held in these accounts remain the property of the Commission, the EIB and the BMWi so long as they are not disbursed for the purposes set out in relation to each programme.

Under the SME Guarantee Facility (SMEG 1998 and SMEG 2001 also called Multi-Annual Programme for enterprises (MAP)), the Fund is empowered to issue guarantees in its own name but on behalf and at the risk of the Commission.

Under the ETF Start-Up Facility (ESU 1998 and ESU 2001 also called Multi-Annual Programme for enterprises (MAP)), the Fund is empowered to acquire, manage and dispose of ETF start-up investments, in its own name but on behalf and at the risk of the Commission.

The support provided by the Seed Capital Action is aimed at the long-term recruitment of additional investment managers by the venture capital funds to increase the number of qualified personnel and to reinforce the capacity of the venture capital and incubator industries to cater for investments in seed capital.

Within the context of its venture capital activity, the Fund manages on behalf, and at the risk of the EIB the European Technology Facilities (ETF) 1 and 2, which have been implemented by the Fund since 1998.

Within the framework of the Risk Capital Mandate signed with the EIB in 2000, the EIF took over the EIB's existing venture capital portfolio, with further investments being funded as part of the "Innovation 2000 Initiative" of the EIB.

Under the ERP-EIF Dachfond agreement, initiated in 2004, the Fund manages venture capital activity on behalf, and at the risk of the BWMi.

The Fund is managing a European Commission facility, the Preparatory Action Facility, on behalf of the EIB Group. The facility is particularly targeting micro lending and will be used for grants to finance technical assistance to SMEs, which must be coupled with an EIF guarantee or an EIB global loan.

	2005 EUR	2004 EUR
Preparatory Action Facility	1 984 100	0
SMEG 1998 (SME Guarantee 1998)	84 900 592	101 577 956
ESU 1998 (ETF Start-up 1998) (1)	46 989 476	35 646 572
Seed Capital Action	233 967	174 840
SMEG 2001 (MAP Guarantee)	98 052 846	58 715 357
ESU 2001 (MAP Equity) (1)	62 886 585	37 146 969
Trust accounts with the Commission (2)	295 047 566	233 261 694
Trust accounts with the EIB	35 281 010	17 356 280
Trust account with the BWMi	116 537	0
	330 445 113	**250 617 974**

5.5 Fiduciary operations

Pursuant to Article 28 of its Statutes, the Fund may accept the tasks of administering special resources entrusted to it by third parties. In execution of this article, the Fund manages and disposes of investments in venture capital funds, in its own name but on behalf and at the risk of

- the EIB, in accordance with European Technology Facility, European Technology Facility 2 and Transfer, Implementation and Management of Risk Capital Investments (Risk Capital Mandate) agreements,
- the Commission, in accordance with ETF Start-Up Facility and Seed Capital Action agreements, and
- the German Ministry of Economics and Technology (Bundesministerium für Wirtschaft und Technologie "BMWi"), in accordance with ERP-EIF Dachfond agreement.

The Fund is also empowered to issue guarantees in its own name but on behalf and at the risk of the Commission according to the Fiduciary and Management Agreement concluded with the Commission (SME Guarantee Facility). However, the EC programmes are only liable for a contracted percentage of the full signature amounts shown below, up to the limit of the agreed budgetary allocation.

(1) The figures above do not include the net cash flow in venture capital, of EUR 64 106 432 for ESU 1998 (2004: EUR 69 406 321) and EUR 11 529 611 for ESU 2001 (2004: EUR 3 830 680) made on behalf of the Commission that are included in 5.5.

(2) The trust accounts with the Commission include cash at bank, money market balances, investments in securities at nominal value and the relevant security accruals. They do not represent a final valuation of the relevant programmes.

Fiduciary operations concluded pursuant to the Fiduciary and Management Agreements are analysed as follows:

	2005 EUR	2004 EUR
Guarantees committed on behalf of the Commission		
Under the SMEG 1998([1])		
Drawn	2 408 056 772	2 408 651 512
Undrawn	29 657 161	34 288 284
Under the SMEG 2001([1])		
Drawn	2 260 559 212	1 096 629 303
Undrawn	1 630 616 168	1 610 565 154
Investments made on behalf of the Commission ([2])		
Under ESU 1998		
Drawn	62 561 332	67 832 005
Undrawn	22 542 188	29 692 967
Under ESU 2001		
Drawn	11 547 921	3 830 680
Undrawn	56 095 200	24 555 979
Under Seed Capital Action		
Drawn	100 000	0
Undrawn	200 000	300 000
Investments made on behalf of the EIB ([2])		
Under EIB Risk Capital Mandate		
Drawn	1 134 366 738	993 048 981
Undrawn	940 387 112	968 483 117
Under European Technology Facility		
Drawn	117 131 315	114 038 105
Undrawn	61 977 464	85 414 791
Investments made on behalf of the External mandators ([2])		
Under ERP-EIF Dachfond		
Drawn	13 579 987	0
Undrawn	52 930 567	37 500 000
	8 802 309 137	**7 474 830 878**

5.6 European Investment Fund commitments included in the off-balance sheet items

From the total off-balance sheet of EUR 12 292 851 868 (2004: EUR 10 872 763 886) the Fund bears the final risk for the following operations:

	2005 EUR	2004 EUR
Guarantees issued		
Drawn	2 253 381 793	1 977 371 682
Undrawn	84 500 177	106 807 332
	2 337 881 970	2 084 179 014
Commitments in venture capital operations	103 027 172	104 212 743
	2 440 909 142	**2 188 391 757**

([1]) Those amounts are valued based on the valuation method described in note 2.8.

([2]) Those amounts are valued at current rate. The drawn amounts correspond to the net disbursed. The value adjustment calculation is performed based on the valuation method described in note 2.4.

- a value adjustment has been estimated at EUR 369 294 981 (2004: EUR 343 503 900) leading to a net adjusted value of EUR 882 203 072 (2004: EUR 763 583 186), on the investments managed on behalf of the EIB. Unrealised gains on these investments, which have not been included in the value adjustment consistent with the methodology described in note 2.4 amounts to EUR 64 075 671 (2004: EUR 29 378 549).
- a value adjustment has been estimated at EUR 26 001 446 (2004: EUR 34 180 406 estimated amount) leading to a net adjusted value of EUR 48 107 807 (2004: EUR 37 482 279 estimated amount), on the investments made on behalf of the Commission. Unrealised gains on these investments, which have not been included in the value adjustment consistent with the methodology described in note 2.4 amounts to EUR 19 575 199 (2004: EUR 2 943 701).

6. Detailed information on the profit and loss account

6.1 Net interest and similar income

Net interest and similar income comprises:

	2005 EUR	2004 EUR
Interest on debt securities	21 319 995	20 571 066
Interest on term deposits	945 793	1 115 721
Interest on bank current accounts	1 006 056	649 679
Net premiums amortised on “Investment portfolio”	(1 333 726)	(824 138)
Interests on pensions	346 994	252 068
Interest & similar charges	312 788	492 033
	22 597 900	**22 256 429**

As mentioned in the note 2.3, the discounts and premiums of the debt securities are netted. The discounts amount to EUR 631 145 (2004: EUR 863 060) and the premiums amount to EUR 1 964 871 (2004: EUR 1 687 198).

6.2 Commission income

Commission income is detailed as follows:

	2005 EUR	2004 EUR
Commissions on own Portfolio Guarantees	16 217 332	14 561 339
Commissions on mandates relating to venture capital operations	11 879 431	9 546 507
Commissions on mandates relating to guarantees	5 612 594	3 999 681
Income from Advisory activity	336 423	448 427
Other commissions	10 000	10 000
Correction from prior years	1 451 389	0
	35 507 169	**28 565 954**

The above amount of “Correction from prior years” corresponds to previous years income adjustments on EIF own guarantee portfolio. This adjustment is related to a guarantee program for which commission income and recoveries received were recorded net of guarantee calls paid. Based on information received in 2005, prior year adjustments have been made to state commission income, and guarantee calls with recoveries separately (see notes 4.3 and 6.5).

6.3 Net profit on financial operations

Net profit on financial operations amounting to EUR 1 553 038 (2004: loss EUR 691 592) mainly corresponds to gains arising from transactions or cash positions in foreign currencies for an amount of EUR 1 554 538 (2004: loss EUR 698 384), of which EUR 1 315 262 is an unrealised gain on foreign exchange revaluation of the venture capital portfolio (2004: loss EUR 90 050).

6.4 Wages and salaries

Wages and salaries include expenses of EUR 2 457 900 (2004: EUR 2 701 121) incurred in relation to staff seconded from the EIB.

6.5 Other operating income

Other operating income is made up of the following:

	2005 EUR	2004 EUR
Recoveries from Guarantees 2005	879 755	0
Recoveries from Guarantees from prior years	1 260 307	0
Other	25 329	27 319
	2 165 391	**27 319**

These recoveries are related to a guarantee program for which commission income and recoveries received were recorded net of guarantee calls paid. Based on information received in 2005, prior year adjustments have been made to state commission income, and guarantee calls with recoveries separately (see notes 4.3 and 6.2).

7. Personnel

The number of persons, including 14 EIB secondees (2004: 12 EIB secondees), employed at the year-end was as follows:

	2005	2004
Chief Executive	1	1
Employees	95	78
Total	**96**	**79**
Average of the year	**89**	**72**

8. Related parties transactions

8.1 European Investment Bank

The amounts included in the financial statements and relating to the European Investment Bank are disclosed as follows:

	2005 EUR	2004 EUR
ASSETS		
Prepayments and accrued income	1 563 582	1 420 710
Other assets	6 844 946	4 908 115
LIABILITIES		
Creditors	227 939	1 925 557
Other provisions	1 861 730	999 327
Accruals & deferred income	200 000	210 000
Capital paid in	247 600 000	236 600 000
OFF BALANCE SHEET		
Guarantees Drawn	609 872 484	754 428 318
Guarantees undrawn	16 250 000	16 250 000
Assets held for third parties	35 281 010	17 356 280
Investments drawn in venture capital	1 251 498 053	1 107 087 086
Investments undrawn in venture capital	1 002 364 576	1 053 897 909
INCOME		
Net interest and similar income	346 994	252 068
Management fees	8 103 283	7 357 381
EXPENSES		
Wages & Salaries	2 457 900	2 701 121
IT expenses	812 342	798 644
Services	234 637	200 866

8.2 Commission of the European Communities

The amounts included in the financial statements and relating to the Commission of the European Communities are disclosed as follows:

	2005 EUR	2004 EUR
ASSETS		
Accounts Receivable	3 228 845	1 374 808
LIABILITIES		
Accounts Payable	466 106	1 340 033
Deferred fees	3 620 837	5 957 467
Capital paid in	120 000 000	120 000 000
OFF BALANCE SHEET		
Guarantees Drawn	4 668 615 985	3 505 280 815
Guarantees undrawn	1 660 273 329	1 644 853 438
Assets held for third parties	295 047 566	233 261 694
Investments drawn in venture capital	74 209 253	71 662 685
Investments undrawn in venture capital	78 828 508	54 548 946
INCOME		
Management fees	7 950 238	5 246 537
Commissions received	2 336 630	2 865 892
EXPENSES		
Treasury management fees	58 608	46 331

8.3 Other related parties

The venture capital fund investments held by the Fund are not to be considered as related parties, as the aim is not to exercise control over the financial and operating policies of the fund's management.

9. Taxation

The Protocol on the Privileges and Immunities of the European Communities, appended to the Treaty of 8 April 1965 establishing a Single Council and a Single Commission of the European Communities, applies to the Fund, which means that the assets, revenues and other property of the Fund are exempt from all direct taxes.

Governing bodies and management

Board of Directors (at 1 April 2006)

Chairman

Philippe MAYSTADT
President, European Investment Bank, Luxembourg

Chairman until 19/09/05: ***Giovanni RAVASIO***

Members

Detlef LEINBERGER
Mitglied des Vorstandes, KfW Bankengruppe, Frankfurt/Main

David McGLUE
Director, Directorate for Financial Operations, Programme Management and Liaison with the EIB Group, Directorate-General for Economic and Financial Affairs, European Commission, Luxembourg

Ralph MÜLLER
Ministerialrat, Leiter des Referates Haushalt und Finanzen der EU und der EIB Gruppe, Bundesministerium der Finanzen, Berlin

María PÉREZ RIBES
Subdirectora General de Instituciones Financieras Europeas, Dirección General de Financiación Internacional, Ministerio de Economia y Hacienda, Madrid

Peter SEDGWICK
Vice-President, European Investment Bank, Luxembourg

Heinz ZOUREK
Director General, Directorate-General for Enterprise and Industry, European Commission, Brussels

Member until 19/09/05: ***Sauli NIINISTÖ,*** *Vice-President, European Investment Bank, Luxembourg*

Alternates

Jean-Pierre ARNOLDI
Administrateur général de la Trésorerie, Ministère des Finances, Brussels

Mauro CICCHINÈ
President, DEXIA CREDIOP, Rome

Thomas HACKETT
Director General, Directorate for Lending Operations - Europe, European Investment Bank, Luxembourg

Rémy JACOB
Deputy Secretary General, European Investment Bank, Luxembourg

Jean-Marie MAGNETTE
Head of Unit, Liaison with EIB Group and New Financial Instruments, Directorate-General for Economic and Financial Affairs, European Commission, Luxembourg

Graham MEADOWS
Director General, Directorate-General for Regional Policy, European Commission, Brussels

Jacek TOMOROWICZ
Director, Foreign Policy Department, Ministry of Finance, Warsaw

Alternate until 19/09/05: ***Terence BROWN,*** *Director General, Directorate for Lending Operations - Europe, European Investment Bank, Luxembourg*

EIF management

Christa Karis, Alessandro Tappi, Jean-Philippe Burcklen, Francis Carpenter,
Marc Schublin, Frédérique Schepens, Jobst Neuss, Jacques Lilli Darcy, Thomas Meyer

People at EIF

Chief Executive	Secretary General	Director, Investments
Francis Carpenter	**Robert Wagener**	**John A. Holloway**
Risk Management and Monitoring	*Corporate Affairs*	*Venture Capital*
JEREMIE		*Guarantees and Securitisation*

Matthias Ummenhofer, Maria Leander, Robert Wagener, Ulrich Grabenwarter, Hubert Cottogni, Alexander Ando, Jouni Hakala, Eva Goulas, John A. Holloway

Risk Management and Monitoring

Thomas Meyer

Helmut Kraemer-Eis

Pierre-Yves Mathonet

JEREMIE

Marc Schublin

Hubert Cottogni

Alexander Andò

Graham Cope

Corporate Affairs

Maria Leander
Legal

Frédérique Schepens
Corporate Affairs and Finance

Jobst Neuss
Compliance

Eva Goulas
Human Resources

Venture Capital

Jean-Philippe Burcklen

David Walker

Christine Panier

Ulrich Grabenwarter

Jouni Hakala

Matthias Ummenhofer

Paul Van Houtte

Jacques Lilli Darcy

Laurent Braun

Guarantees and Securitisation

Alessandro Tappi

Christa Karis

Per-Erik Eriksson

Gunnar Mai

Audit Board (at 1 April 2006)

Chairman

Sylvain SIMONETTI
Head of Unit, Internal Audit, Directorate-General for Economic and Financial Affairs,
European Commission, Luxembourg

Members

Hannu LIPPONEN
Senior Vice President, Finance, Finnvera plc, Kuopio

Raimundo POVEDA ANADÓN
Former Director General, Banking Policy Directorate, Bank of Spain,
Madrid (retired in 2000)

The Audit Board prepares an Activity Report to the General Shareholders Annual Meeting for the preceding financial year. The report essentially reviews both internal and external audit work of the year, as well as co-operation with the European Court of Auditors, and it assesses the Fund's actions in response to the last Audit Board's recommendations. The full Activity Report is available via EIF's website: **www.eif.org.**

Capital and Shareholders (at 1 April 2006)

EIF has an authorised capital of EUR 2,000m divided into 2,000 shares of EUR 1m each.

As a result of 11 financial institutions having exercised the Share Purchase Undertaking (PUT) on their respective shareholding in 2005, EIB acquired a total of 55 EIF shares. According to the terms of sale and acquisition of these shares, the 11 financial institutions remained entitled to dividends until and including 30/06/05.

EIF's capital was entirely subscribed on 31/12/05 by EIB (61.9%), the European Community represented by the European Commission (30%), and a number of European banks and financial institutions (8.1%).

Discussions underway with new shareholders are expected to be completed during 2006.

Institution		Number of shares
European Investment Bank		1 238
European Community represented by the European Commission		600
23 financial institutions (breakdown below)		162
Total		**2 000**
Austria	Bank Austria Creditanstalt AG	3
	Erste Bank des Oesterreichischen Sparkassen AG	3
	Raiffeisen Zentralbank Österreich AG	3
Bulgaria	Encouragement Bank A.D.	3
Denmark	The Danish Investment Fund	3
Finland	Finnvera plc	6
France	Caisse des dépôts et consignations (CDC)*	15
	Dexia Crédit Local	10
Germany	Kreditanstalt für Wiederaufbau	45
	Landeskreditbank Baden-Württemberg Förderbank	5
	LfA Förderbank Bayern	5
Hungary	Hungarian Development Bank Ltd.	5
Italy	Banca Intesa S.p.A.	5
	Dexia Crediop S.p.A.	10
	Sanpaolo IMI Private Equity S.p.A.	10
Luxembourg	Banque et Caisse d'Epargne de l'Etat	3
	BIP Investment Partners S.A.	3
Malta	Bank of Valletta plc	5
Netherlands	NIBC	3
Portugal	Banco BPI S.A.	6
Spain	Instituto de Crédito Oficial (ICO)	5
Sweden	Stiftelsen Industrifonden	3
United Kingdom	Barclays Bank plc	3

* CDC bought five shares from Dexia Crédit Local.

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Please note that all documentation on EIF (Statutes, Rules of Procedures, Annual Reports, etc.) is available through the website.

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