



COMMISSION OF THE EUROPEAN COMMUNITIES

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**ANNUAL STATUS REPORT FROM THE COMMISSION ON THE GUARANTEE  
ITS MANAGEMENT IN 1997**

CONTENTS

1.	LEGAL BASES.....	3
2.	POSITION OF THE FUND AT 31 DECEMBER 1997.....	3
3.	PAYMENTS INTO THE FUND.....	4
3.1	PAYMENTS FROM THE GENERAL BUDGET IN THE COURSE OF THE FINANCIAL YEAR.....	4
3.2	INTEREST FROM FINANCIAL INVESTMENT OF THE FUND'S LIQUID ASSETS .....	5
3.3	RECOVERY FROM DEFAULTING DEBTORS.....	6
4.	THE FUND'S LIABILITIES.....	6
4.1	DEFAULT PAYMENTS .....	6
4.2	EIB REMUNERATION .....	6

ANNEXES

ANNEX I:	LEGAL BASES FOR PAYMENTS FROM THE GENERAL BUDGET.....	8
1.	DECISIONS COVERED BY TRANSFER 9/97.....	8
2.	DECISIONS COVERED BY TRANSFER 58/97.....	9
ANNEX II:	EIB STATUS REPORT ON THE FUND AND ITS MANAGEMENT - REVENUE AND EXPENDITURE ACCOUNT AND BALANCE SHEET AT 31 DECEMBER 1997.....	10
1.	DEVELOPMENT OF THE FUND IN 1997.....	10
2.	THE FUND'S RESOURCES .....	10
2.1	THE FUND'S ACCOUNT.....	10
2.1.1	<i>Payments made by the Fund from 1 January to 31 December 1997.....</i>	<i>10</i>
2.1.2	<i>Amounts recovered from defaulting debtors from 1 January to 31 December 1997.....</i>	<i>11</i>
2.2	THE FUND'S ASSETS .....	11
2.3	LIQUIDITY RISK.....	12
3.	INVESTMENTS MADE DURING 1997 .....	13
3.1	TREASURY OPERATIONS .....	13
3.2	INVESTMENT PORTFOLIO .....	15
ANNEX III:	CONSOLIDATED BALANCE SHEET AT 31 DECEMBER 1997.....	19

**ANNUAL STATUS REPORT BY THE COMMISSION ON THE GUARANTEE FUND AND ITS  
MANAGEMENT IN 1997**

**1. LEGAL BASES**

Council Regulation (EC, Euratom) No 2728/94 of 31 October 1994 set up a Guarantee Fund for external actions to repay the Community's creditors in the event of default by beneficiaries of loans granted or guaranteed by the Community.

In accordance with Article 6 of the Regulation the Commission entrusted financial management of the Fund to the European Investment Bank (EIB) under an agreement signed between the Community and the EIB on 23 November 1994 in Brussels and on 25 November 1994 in Luxembourg.

Under Article 8.2 of the agreement, by 1 March each year the Bank must send the Commission a status report on the Fund and its management, the revenue and expenditure account and the financial statement for the Fund for the preceding year. An extract from the report covering 1997 is in Annex II.

In addition, Article 7 of the Regulation establishing the Fund requires the Commission to send the European Parliament, the Council and the Court of Auditors a report on the situation of the Fund and its management for each financial year by 31 March of the following year.

**2. POSITION OF THE FUND AT 31 DECEMBER 1997**

At the close of the 1997 financial year, the Fund totalled ECU 862 112 532.84 (Annex II). This is the sum, since the Fund was established, of all

- budget payments (ECU 1 065 955 000),
- incremental yearly net results (ECU 69 356 934.57),
- late payments from non-member countries (ECU 136 379 054.93),
- debts corresponding to the payments not made to the Bank (ECU 325 474.94)
- minus calls on the Fund's resources (ECU 409 903 931.60).

The total amount of the consolidated balance sheet (Annex III) is ECU 1 177 873 839.58, which breaks down into ECU 315 000 000 in deposits, ECU 10 929 584.43 on current account, ECU 519 335 151.46 in the securities portfolio, ECU 16 847 796.95 in interest accrued and not paid at 31 December 1997 (ECU 1 641 880.52 in interest accrued and not yet due on fixed-term deposits,

ECU 15 168 388.90 in coupons accrued and not yet due and ECU 37 527.53 accrued interest on sight-deposits to be paid) and ECU 315 761 306.74 in receivables from the recipients of loans granted or guaranteed by the Community, including ECU 291 337 822.02 in principal, interest due and default interest covered by guarantee payments under the Fund and ECU 24 423 484.72 in default interest incurred but not received at 31 December 1997.

Article 3 of the Regulation establishing the Fund requires that the amount of the Fund has to reach an appropriate level (target amount) set at 10% of the total outstanding capital liabilities arising from each operation, plus unpaid interest due.

Outstanding lending and loan guarantee operations for non-member countries plus unpaid interest due totalled ECU 7 961 million at 31 December 1997, of which ECU 287 million was accounted for by unpaid interest.

The ratio between the Fund's resources and outstanding capital liabilities within the meaning of the Regulation was 10.83%. Since this is higher than the target amount of 10%, there had to be a repayment from the Fund to the general budget of the Communities, as provided for in the third paragraph of Article 3 of the Regulation. The amount to be repaid to the budget comes to ECU 66 million.

The following sections describe developments affecting the Fund's resources and liabilities in 1997.

### **3. PAYMENTS INTO THE FUND**

#### **3.1 Payments from the general budget in the course of the financial year**

Articles 2 and 4 of the Regulation establishing the Fund stipulate that it is to be endowed by payments from the general budget equivalent to 14% of the capital value of loan and loan guarantee operations until the target amount is reached. Under Article 5 the provisioning rate rises to 15% for new operations if the Fund's resources fall below 75% of the target amount as a result of guarantees being activated to cover any default.

The legal bases for the provisioning arrangements are described in Annex I.

The Council Decision of 31 October 1994 concerning budgetary discipline authorised the entry in the general budget of a reserve for loan and loan guarantee operations. This item, which was allocated provisional appropriations of ECU 329 million in 1997, is intended to endow the Fund by transferring amounts into the budget item for payments into the Fund.

On these legal bases, two transfers totalling ECU 286 095 000 were adopted by the budgetary authority in 1997 to endow the Guarantee Fund.

- Transfer 9/97: ECU 217 095 000

This first transfer at the beginning of the year was for payments into the Fund under the Council Decisions of 15 February 1993, 24 January 1994, 1 June 1995, 10 April 1995, 30 October 1995, 25 July 1996 and 14 April 1997, in accordance with the arrangements set out in the Annex to the Regulation establishing the Fund (see Annex I).

- Transfer 58/97: ECU 69 000 000

This second transfer was for payments into the Fund in respect of loan operations adopted by the Council on 22 July 1997 and 17 November 1997. The decisions covered by this transfer are given in Annex I.

The two transfers to the Fund were made in July and December 1997.

### **3.2 Interest from financial investment of the Fund's liquid assets**

The Fund's liquid assets are invested in accordance with the management principles laid down in the Annex to the Community/EIB Agreement.

These principles state that during the Fund's first years of operation it will be treated as a money-market investment fund dealing solely in short-term instruments up to one year, as long as the total amount invested does not exceed ECU 300 million. As the amount of the Fund exceeded this ECU 300 million threshold in 1995, the Commission agreed with the EIB to amend the investment principles early in 1996.

The list of banks authorised to receive deposits is agreed by the Commission and the EIB. The original list has been revised several times in the light of the latest changes in bank ratings. Most of the banks are members of the ecu clearing system. They all have a Moody's rating of at least A1 for long-term investments and P1 for short-term ones and investments made with them are governed by rules to ensure a good spread and avoid risk exposure.

In 1997 interest on deposits, the Guarantee Fund current account and securities, totalled ECU 34 496 982.56, broken down as follows:

- deposits: ECU 10 604 863.19. This represents the situation at 31 December including interest received on bank deposits (ECU 10 246 603.49) and interest incurred (ECU 358 259.70) in 1997. The interest incurred corresponds to interest which has not been received by the Fund at the end of the year but will be paid at the dates fixed for maturity of the investments. The interest accrued in 1996 but received in 1997 (ECU 1 283 620.82) is deducted from the accrued interest entered in the accounts during 1997 (ECU 1 641 880.52).
- current account: ECU 454 374.60, comprising interest recorded on the current account.

- securities portfolio: ECU 23 437 744.77. The interest on securities is generated by investments placed in the form of securities in accordance with the principles of investment laid down in the Agreement giving the EIB the task of managing the Fund's liquid assets. From this figure must, however, be subtracted the ECU 6 592 658.64 charged in the course of the year as the difference between the entry price and the redemption value divided pro rata temporis over the remaining life of the securities held (corresponding to the spread of the premium or discount entered in the profit and losses account).

The interest received is entered in the results for the financial year.

### **3.3 Recovery from defaulting debtors**

Any late repayments by defaulting countries on operations where the Fund has honoured the guarantee are paid into the Fund. The running total now comes to ECU 136 379 054.93 (see point 2.1.2 of Annex II) of which ECU 45 033 282.25 was recovered in 1997.

## **4. THE FUND'S LIABILITIES**

### **4.1 Default payments**

The Fund's guarantee was called in on four occasions in 1997, involving a total of ECU 54 290 853.91 (see point 2.1.1 of Annex II).

### **4.2 EIB remuneration**

Article 6 of the management agreement between the Commission and the EIB sets an annual commission of 0.125% calculated on the Fund's average monthly balances. The figure is to be reviewed at the end of any year in which the Fund's liquid assets reach ECU 300 million and no later than three years following the date of the first payment into the Fund, taking into account such things as the growth of the Fund's activities.

As the Fund had reached ECU 300 million at the end of 1995, the EIB's remuneration was reviewed. Taking into account the Bank's experience of the workload involved in its management, a supplementary agreement dated 17 September and 23 September 1996 to the Agreement on the financial management of the Fund took the annual payment to 0.05% of the Fund's assets; this rate was applied retrospectively on 31 December 1994.

For 1997 the Bank's remuneration was fixed at ECU 325 474.94 and entered in the profit and loss account as accruals (liabilities) on the balance sheet. This payment was made to the EIB at the beginning of January 1998.

ANNEXES

<b>ANNEX I : LEGAL BASES FOR PAYMENTS FROM THE GENERAL BUDGET.....</b>	<b>8</b>
<b>1. DECISIONS COVERED BY TRANSFER 9/97.....</b>	<b>8</b>
<b>2. DECISIONS COVERED BY TRANSFER 58/97.....</b>	<b>9</b>
<b>ANNEX II : EIB STATUS REPORT ON THE FUND AND ITS MANAGEMENT - REVENUE AND EXPENDITURE ACCOUNT AND BALANCE SHEET AT 31 DECEMBER 1997.....</b>	<b>11</b>
<b>1. DEVELOPMENT OF THE FUND IN 1997.....</b>	<b>10</b>
<b>2. THE FUND'S RESOURCES.....</b>	<b>10</b>
2.1 THE FUND'S ACCOUNT.....	10
2.1.1 <i>Payments made by the Fund from 1 January to 31 December 1997.....</i>	<i>10</i>
2.1.2 <i>Amounts recovered from defaulting debtors from 1 January to 31 December 1997.....</i>	<i>11</i>
2.2 THE FUND'S ASSETS.....	11
2.3 LIQUIDITY RISK.....	12
<b>3. INVESTMENTS MADE DURING 1997.....</b>	<b>13</b>
3.1 TREASURY OPERATIONS.....	13
3.2 INVESTMENT PORTFOLIO.....	15
<b>ANNEX III : CONSOLIDATED BALANCE SHEET AT 31 DECEMBER 1997.....</b>	<b>19</b>

## LEGAL BASES FOR PAYMENTS TO THE GUARANTEE FUND FROM THE GENERAL BUDGET

The Annex to the Regulation concerning arrangements for payments under the Guarantee Fund stipulates that for borrowing/lending operations or guarantees to financial bodies under a framework facility spread over several years and with a micro-economic and structural purpose, payments will be made in annual tranches calculated on the basis of the annual amounts indicated in the financial statement attached to the Commission proposal, adapted, where appropriate, in the light of the Council decision.

In the case of other borrowing/lending operations such as balance of payments loans to non-member countries, irrespective of whether they are made in one or more than one tranche, the amount to be paid into the Fund will be calculated on the basis of the total amount for the operation decided on by the Council.

Two transfers were made under this procedure in 1997.

### 1. DECISIONS COVERED BY TRANSFER 9/97

- Council Decision of 15 February 1993 calling on the EIB to grant loans for projects of mutual interest in certain non-member countries with which the Community has cooperation agreements, within a fixed ceiling of ECU 250 million a year for a period of three years.
- As part of the financial cooperation with the Mediterranean countries:
  - Council Decision of 24 January 1994 for a three-year loan of ECU 115 million for Syria.
  - Council Decisions of 30 October 1995 for three-year loans of ECU 30 million for Malta and ECU 50 million for Cyprus.
- Council Decision of 10 April 1995 concerning the granting of macro-financial aid of ECU 55 million to Belarus.
- Council Decision of 1 June 1995 granting a Community guarantee to the EIB against losses under loans for projects in South Africa, with an overall loans ceiling of ECU 300 million over two years.
- Council Decision of 25 July 1996 repealing Decision 94/939/EC of 22 December 1994 providing further macro-financial assistance of ECU 130 million for the Slovak Republic.



- Council Decision of 14 April 1997 granting a Community guarantee to the European Investment Bank against losses under loans for projects outside the Community (central and eastern European countries, Mediterranean countries, Latin American and Asian countries and South Africa).

**2. DECISIONS COVERED BY TRANSFER 58/97**

- Council Decision of 22 July 1997 concerning the grant of macrofinancial aid to the Former Yugoslav Republic of Macedonia.
- Council Decision of 22 July 1997 concerning the grant of macrofinancial aid to Bulgaria.
- Council Decision of 17 November 1997 granting exceptional financial aid to Armenia and Georgia.

**EIB STATUS REPORT ON THE FUND AND ITS MANAGEMENT  
REVENUE AND EXPENDITURE ACCOUNT AND BALANCE SHEET  
AT 31 DECEMBER 1997**

**1. DEVELOPMENT OF THE FUND IN 1997**

As stated in point 2.3, the total holdings of the Fund stood at ECU 845.3 million at 31 December 1997 as compared with ECU 548.8 million in 1996. The operating result came to ECU 27.5 million as against ECU 18.0 million at 31 December 1996. Portfolio income reached ECU 16.8 million, representing more than 61% of the revenue recorded at 31 December 1997 as against 22% in 1996.

The Fund's resources were increased substantially by ECU 217 095 000 on 15 July 1997 and by ECU 69 million on 29 December 1997.

**2. THE FUND'S RESOURCES**

**2.1 The Fund's account**

Resources		at 31/12/96	in 1997	TOTALS
- Provisions	+	779 860 000.00	286 095 000.00	1 065 955 000.00
- Activation of guarantee	-	355 613 077.69	54 290 853.91	409 903 931.60
- Late recovery	+	91 345 772.68	45 033 282.25	136 379 054.93
Account balance		515 592 694.99	276 837 428.34	792 430 123.33

The activations of the guarantee remained fairly low in 1997.

*2.1.1 Payments made by the Fund from 1 January to 31 December 1997*

VALUE DATE	AMOUNT
28/01/97	5 688 651.22
15/04/97	35 341 529.43
23/05/97	7 125 866.41
16/10/97	6 134 806.85
<b>TOTAL</b>	<b>54 290 853.91</b>

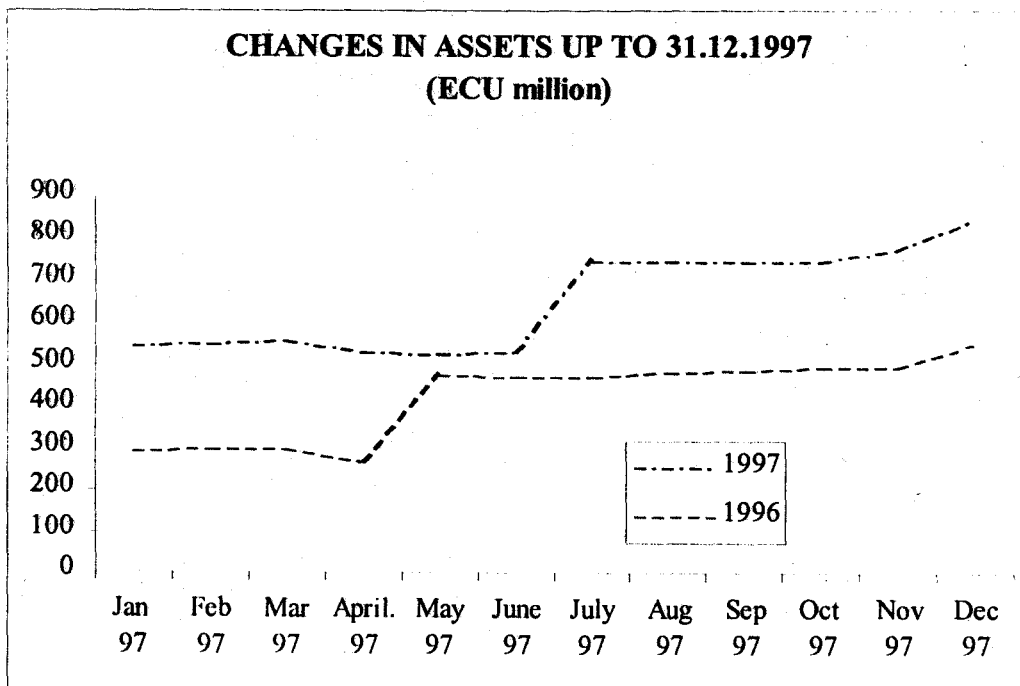
2.1.2 Amounts recovered from defaulting debtors from 1 January to 31 December 1997

VALUE DATE	AMOUNT
09/01/97	3 999 642.94
13/02/97	4 000 000.00
10/04/97	31 378.11
18/04/97	7 000 000.00
30/05/97	833 379.60
02/06/97	1 446 515.51
03/11/97	461.02
03/11/97	17 267.42
03/11/97	16 509 236.82
28/11/97	8 000 000.00
23/12/97	3 195 400.83
<b>TOTAL</b>	<b>45 033 282.25</b>

2.2 The Fund's assets

The Fund operates in one currency only - the ecu - and consists of the following:

- ECU 315 million invested in short-term monetary deposits;
- ECU 10.9 million on current account;
- ECU 519.3 million in the investment portfolio (see table in 2.3).



### 2.3 Liquidity risk

In accordance with the strategy agreed with the Commission for the management of Guarantee Fund assets, the funds available are distributed as follows;

- (i) When Fund assets do not exceed ECU 300 million, short-term investment only.
- (ii) From ECU 300 million:
  - a minimum of one third for short-term investment;
  - a maximum of two thirds for long-term investment with maturity not exceeding ten years;
  - the average term for all investments must not exceed five years.

At all events, the short-term investment must never be lower than ECU 150 million.

	Fixed-rate investments			Variable-rate securities	TOTALS
	less than 3 months	3 months to 1 year	1 to 5 years		
Current accounts	10 929 584.43				10 929 584.43
Fixed-term deposits	270 000 000.00	45 000 000.00			315 000 000.00
Securities portfolio	71 945 578.48	28 161 470.60	222 439 807.14	196 788 295.24	519 335 151.46
TOTALS	352 875 162.91	73 161 470.60	222 439 807.14	196 788 295.24	845 264 735.89
in percentages	41.76	8.66	26.32	23.26	100.00

Cover of more than ECU 352.8 million at less than three months is maintained to correspond to the time by which the Commission must call on the Fund in the event of defaults on loan repayments.

The remaining assets have been scheduled so that there is a regular flow of revenue and sufficient liquidity.

At 31 December 1997 the term of long-term fixed-rate investment came to 2.1 years compared with the maximum 2.5 years authorised; the term for variable-rate securities was two months, exactly the same as the average term provided for in the strategy for the management of Fund assets.

**3. INVESTMENTS MADE DURING 1997**

**3.1 Treasury operations**

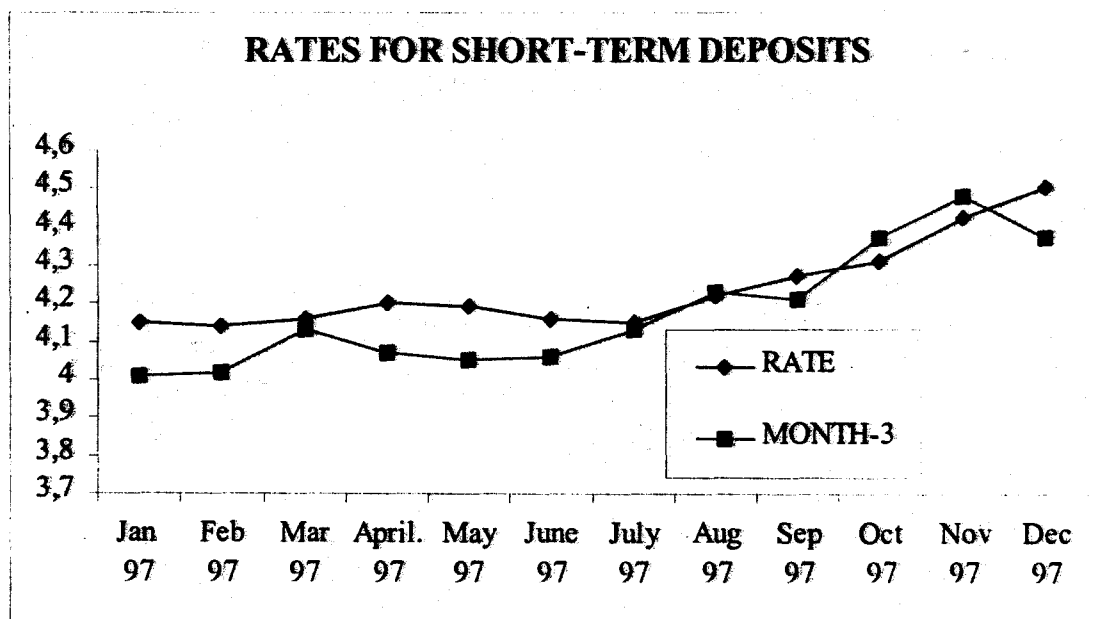
The yield on investments in 1997 averaged 4.24% as against 4.50% in 1996.

The yield obtained is 0.06 basis points above the three-month LIBID rate which was the reference for 1996 and 1997.

MONTH	YIELD	LIBID three months	MARGIN
January - December	4.24%	4.18%	0.06%

Movements in rates over 1997

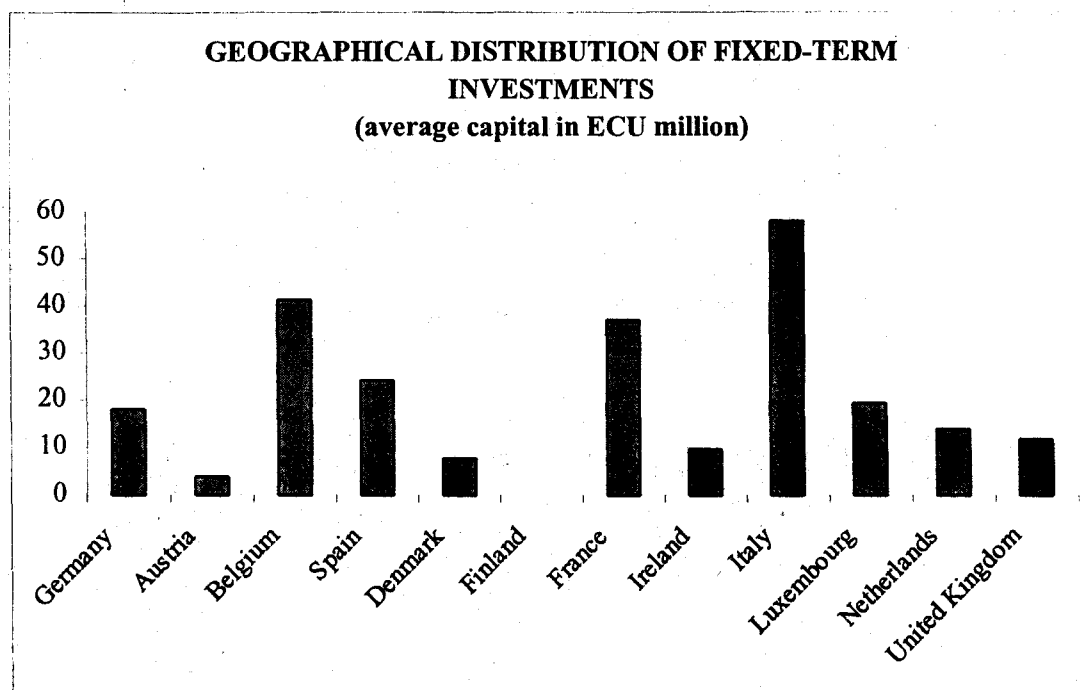
The table below shows the rates obtained for interbank money-market investments as compared with the three-month LIBID reference rate.



Geographical breakdown of the countries with which the Fund made fixed-term deposits with indication of the average capital (ECU million).

	Average capital in 1997 (million)	Average capital in 1996 (million)
- Germany	18.2	47.7
- Austria	3.9	5
- Belgium	41.4	42.5
- Spain	24.2	8.5
- Denmark	7.7	22.4
- Finland	-	0.9
- France	37.1	69.2
- Ireland	9.7	13
- Italy	58.1	17.3
- Luxembourg	19.4	15.4
- Netherlands	13.9	31.8
- United Kingdom	11.8	28.7
- TOTALS	245.4	302.4

The EIB is pursuing its objective of better geographical distribution while at the same time maintaining the competitiveness of the yield obtained.



### 3.2 Investment portfolio

The securities portfolio, seen as an investment portfolio, is made up of securities in ecus acquired with the intention of keeping them until maturity: the fixed-interest securities whose residual period to maturity is less than 3 months total ECU 71 945 478.48, the other fixed-interest securities with a term of less than five years total ECU 250 601 277.60 and the variable-rate securities total ECU 196 788 295.24.

The starting value of the securities in this portfolio is the cost of acquisition. The difference between the entry price and the redemption value is divided pro rata temporis over the remaining life of each of the securities.

At 31 December 1997 the nominal value of the investment portfolio was ECU 506.2 million against a book value of 519.3 million (including the premium to be written off).

The portfolio gave a result of 16.8 million at 31 December 1997. This result breaks down as follows:

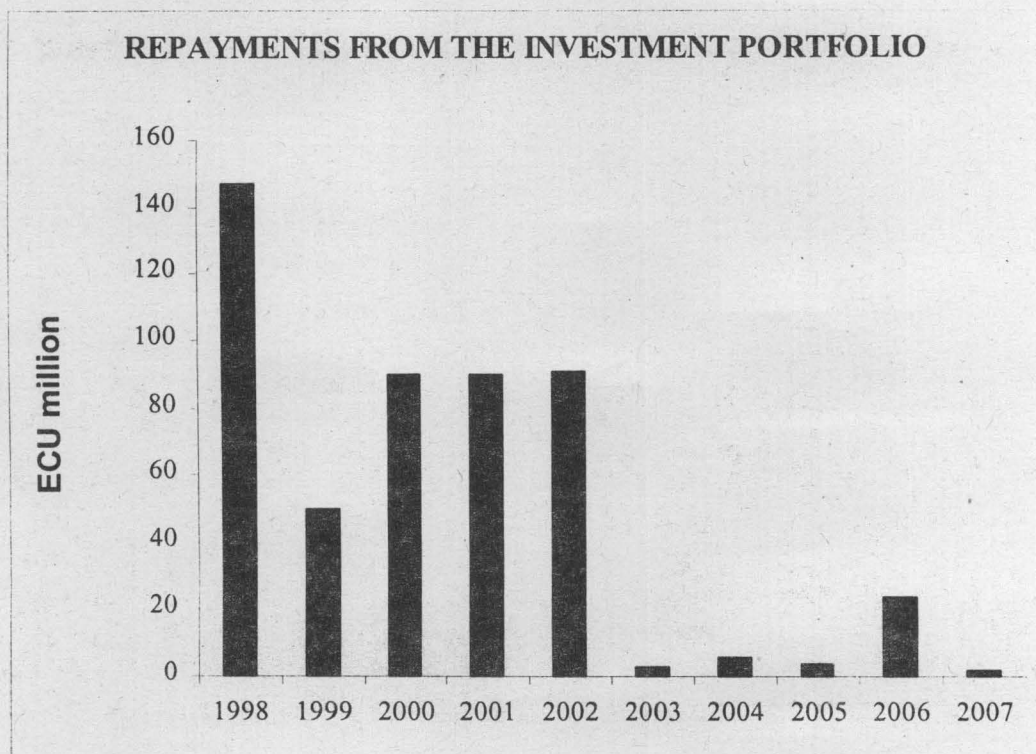
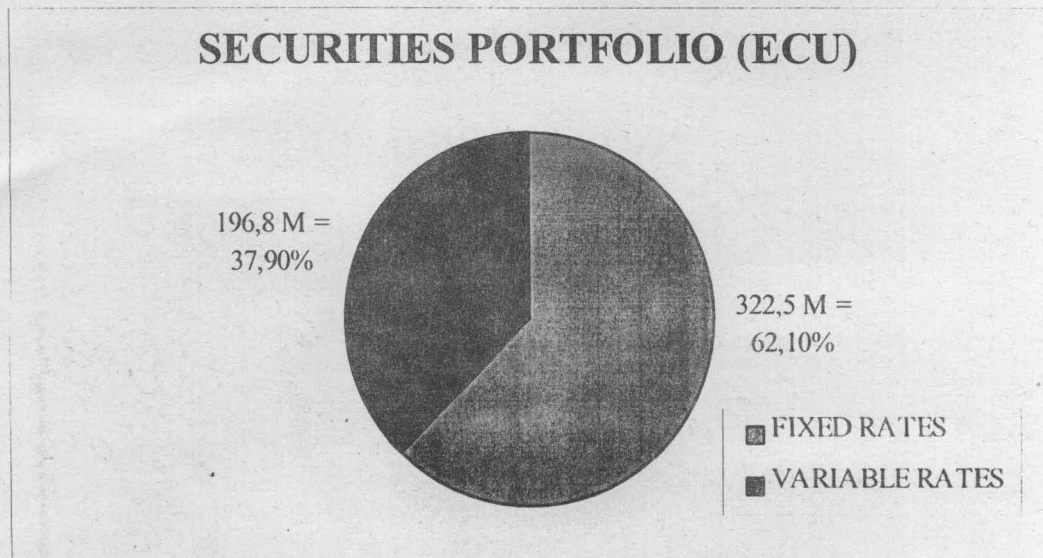
Interest received	23 437 744.77
Appreciation	9 583.63
Spread of the premium	<u>-6 592 658.64</u>
	16 854 669.76

The book profit of the investment portfolio came to 4.44%.

#### Performance indicators

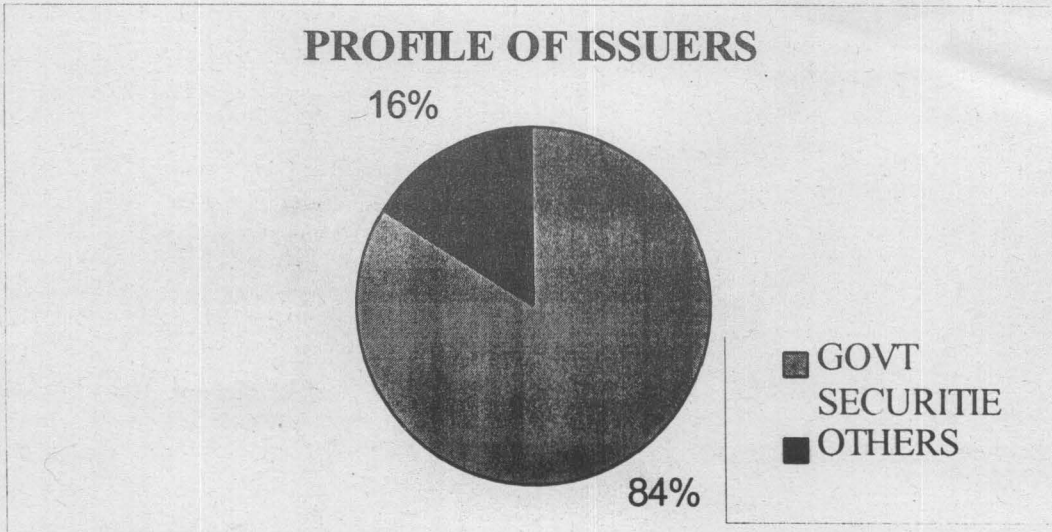
1. Variable-rate: 4.18%, the same as the Libid 3 month reference.
2. Fixed-rate: by way of indication, the guidelines mention that the Salomon Brothers ECU bond index for a six-month period is 3.53%. The yield on the Guarantee Fund portfolio calculated in the same way comes to 4.04%.

Breakdown of the portfolio between fixed-rate and variable-rate securities:





**Profile of issuers:** in accordance with the agreement between the Community and the Bank on the management of the Guarantee Fund, all the securities held have a minimum credit rating of A1.



POSITION OF THE GUARANTEE FUND AT 31 DECEMBER 1997

<b>ASSETS</b>	<b>31 December 1997</b>
<u>Receivables with credit institutions</u>	
CURRENT ACCOUNT	10 929 584.43
FIXED-TERM DEPOSITS	315 000 000.00
	<u>325 929 584.43</u>
<u>Investment portfolio</u>	
SECURITIES PORTFOLIO	519 335 151.46
	<u>519 335 151.46</u>
<u>Other receivables</u>	
ACCRUALS	16 847 796.95
	<u>16 847 796.95</u>
<b>TOTAL</b>	<u><b>862 112 532.84</b></u>
<b>LIABILITIES</b>	<b>31/12/1997</b>
<u>Guarantee Fund</u>	
GUARANTEE FUND	792 430 123.33
	<u>792 430 123.33</u>
<u>Other liabilities</u>	
ACCRUALS	325 474.94
	<u>325 474.94</u>
<u>Result</u>	
Result carried over	41 813 114.11
Result for 1997	27 543 820.46
	<u>69 356 934.57</u>
<b>TOTAL</b>	<u><b>862 112 532.84</b></u>
<b>PROFIT AND LOSS AT 31 December 1997</b>	
<b>1. INCOME</b>	
Interest and similar income	23 437 744.77
Appreciation on transfer of investment securities	9 583.63
Interest on investments	10 604 863.19
Interest on current account	454 374.60
<b>SUB-TOTAL</b>	<u>34 506 566.19</u>
<b>2. COSTS</b>	
Spread of premium or discount	- 6 592 658.64
Commissions	- 325 474.94
Financial charges	- 44 612.15
<b>SUB-TOTAL</b>	<u>- 6 962 745.73</u>
<b>NET RESULT</b>	<u><b>27 543 820.46</b></u>

**ANNEX III**

**CONSOLIDATED FINANCIAL BALANCE SHEET OF THE GUARANTEE FUND AT  
31 DECEMBER 1997**

The consolidated financial balance sheet at 31 December 1997 is provided to supplement the position of the Guarantee Fund as set out in Annex II. The consolidated balance sheet also includes an additional ECU 315 761 306.74 which breaks down as follows:

- on the assets side, receivables with recipients of loans granted or guaranteed by the Commission totalling ECU 291 337 822.02 for third countries' arrears on the payment of principal, interest due and default interest covered by the Guarantee Fund and ECU 24 423 484.72 for default interest incurred but not received at 31 December 1997. This default interest has been calculated in line with the penalty rates laid down in the loan contracts.
  
- on the liabilities side, the Fund's resources which still have to be replenished (ECU 273 524 876.67), default interest incurred but not received (ECU 24 423 484.72), interest received on late recoveries (ECU 17 812 945.35) entered in the profit and loss account.

CONSOLIDATED FINANCIAL BALANCE SHEET OF THE GUARANTEE FUND AT 31 DECEMBER 1997

	ECU
<b>ASSETS</b>	
Current account	10 929 584.43
Fixed-term deposits	315 000 000.00
Portfolio	
Investment portfolio	519 335 151.46
Receivables with recipients of loans granted or guaranteed by the Community	
Arrears covered by the fund (1)	291 337 822.02
Default interest incurred but not received	24 423 484.72
Other receivables	
Accruals	16 847 796.95
<b>TOTAL ASSETS</b>	<b><u>1 177 873 839.58</u></b>
<b>LIABILITIES</b>	
Guarantee Fund	
Payments from the budget	1 065 955 000.00
Default interest incurred but not received	24 423 484.72
	<b><u>1 090 378 484.72</u></b>
Other liabilities	
Accruals	325 474.94
Result	
Result carried over	41 813 114.11
Result for 1997	45 356 765.81
	<b><u>87 169 879.92</u></b>
<b>TOTAL LIABILITIES</b>	<b><u>1 177 873 839.58</u></b>

PROFIT AND LOSS AT 31/12/97

<b>1. INCOME</b>	
Interest on investment securities	23 437 744.77
Appreciation on transfer of investment securities	9583.63
Interest on investments	10 604 863.19
Interest on current account	454 374.60
Default interest received on late recoveries	17 812 945.35
<b>TOTAL INCOME</b>	<b><u>52 319 511.34</u></b>
<b>2. COSTS</b>	
Spread of premium or discount	6 592 658.64
Commissions	325 474.94
Financial charges	44 612.15
<b>TOTAL COSTS</b>	<b><u>6 962 745.73</u></b>
<b>NET RESULT</b>	<b>45 356 765.81</b>

(1) Capital, interest, default interest covered by payments from the Fund

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