
THE BLACK SEA PROPERTY FUND LIMITED

Annual Report and Financial
Statements

For the year ended 31 December 2007

THE BLACK SEA PROPERTY FUND LIMITED

Annual report and financial statements for the year ended 31 December 2007

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THE BLACK SEA PROPERTY FUND LIMITED

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Chairman's statement

Dear Shareholders:

This is my first opportunity to update you since the changes to Black Sea's board of directors this past October. So what I would like to do is to introduce your new board, explain what we have been doing since we took office, give you an overview of our assets, and touch on some other matters.

I know that in the past Black Sea's annual and semi-annual reports have been glossy productions replete with colour photographs, architects' renderings and the like. By contrast, this year's report is a photocopied production containing only dry words and even drier numbers. But given the decline in our share price, we have tried to cut back in a number of areas, and this is one. We all know that the last six months have been trying for equity investors the world over and especially for investors in property related investments. Major financial institutions in the UK and the US have collapsed. Many international financial institutions have had major asset write downs of their property investments. And residential real estate prices throughout the developed world have fallen sharply. This is not to excuse the fact that the quoted price for our shares has fallen by about fifty percent since last October. We are not at all happy about this, especially since one of our board members is a very substantial shareholder. But it is also important to keep in mind that as Benjamin Graham said, "in the short run the market is a voting machine but in the long run it is a weighing machine".

We have no great insight into the voting aspect of the market, but as for the weighing aspect, you should place into the balance all of the facts set forth in this report. Some facts that seem especially crucial are that we carry about £15 million of cash on our balance sheet with no debt, and in an inflationary time our investments are valued at historical cost. As at 31 December we had an NAV per share of 17.6p and Colliers, which does a third party valuation each year, has valued our property investments higher than last year. We have started a new development in Sofia that looks promising and our participation in Obzor looks as if it will pay off as well. But against this information you need to balance that we are involved in litigation in Bulgaria over two of our assets, that the units in our Nikea Park development are not selling, that three of our assets remain undeveloped land (producing no cash return today and none for the foreseeable future), that one of our assets is in a very early development stage, and that we face complex regulatory challenges, explained in more detail below.

But it is for you as shareholders to weight the value of your shares and decide how to proceed. The previous board had authorised a return of capital in the amount of 1p per share, but we think that a better use of shareholder funds would be a buyback – so those shareholders who wish to stay can stay and those shareholders who wish to exit can exit. So we have decided to spend up to £5 million of our capital to facilitate a buyback in accordance with AIM rules. The buyback will be handled by our listing broker, or "NOMAD," Numis Securities. A formal announcement in accordance with AIM rules containing terms and conditions of the buyback will be made presently.

* * * *

Changes to Corporate Governance

With that said let me put some meat on the bones by giving you some background on the changes that occurred last autumn. As many of you know, our largest shareholder is QVT LP, a large London-based investment fund that was an early investor in Black Sea. Over time, QVT became dissatisfied with Black Sea's board composition, some of Black Sea's investments, and the management compensation structure. About a year ago QVT began negotiations with the former board to force changes in Black Sea's management and to obtain board representation. In September the former board served a "protective termination notice" on the manager giving notice that pursuant to the management contract the manager would be terminated twelve months hence. At about the same time, QVT requisitioned an extraordinary general meeting of shareholders to replace two sitting directors with several new ones. When the smoke cleared, the board comprised two former directors and five new ones. At the EGM on 29 October 2007 about 86% of those shares voting voted in favour of the new directors.

The new directors are Angelo Moskov, Andrey Kruglykhin, Antony Gardner-Hillman, me – and Andrew Wignall, who was invited to join the Board in March 2008. Angelo is a partner with QVT specializing in emerging Europe, a dual Bulgarian-UK national with experience at several leading western investment banks and extensive business experience in Bulgaria. Andrey is a Russian national, resident in the UK and a consultant to QVT. Andrey is a fluent Bulgarian speaker, who has lived in Bulgaria for a number of years and has run a major Bulgarian company. Tony is an Oxford trained solicitor, who has practiced law in Jersey for many years and was one of the founders of a leading Jersey trust and administration company. Andrew is a UK qualified chartered accountant, who practiced accountancy in Jersey for many years before moving into the funds' management and administration business. I am a US qualified lawyer with about fourteen years' experience in emerging markets and have spent the better part of this decade managing offshore emerging market funds. Our two holdover directors are Irena Komitova and Bogdan Stanchev, both Bulgarian nationals. Irena and Bogdan are both entrepreneurs with good contacts in Bulgaria and experience in many different businesses.

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Chairman's statement (continued)

So to sum up, we now have a seven person board. All are fluent English speakers and four of the seven are fluent Bulgarian speakers as well. The majority of the board have extensive business experience and contacts in Bulgaria. We have experience in law, accountancy, emerging market investments, real estate, fund management and perhaps most importantly, in Bulgaria.

On the ground in Sofia is a substantial team that takes care of the day to day business of Black Sea, Development Capital Management Bulgaria EAD ("DCMB"). George Sidjimkov heads the team. George is a Bulgarian national with a UK university degree, a business degree from a leading US business school, and experience as an investment banker with a major international bank in London. George heads up a team of ten young professionals based in downtown Sofia. That team includes several lawyers, marketing people, a project manager, and an architect. All are native Bulgarian speakers and fluent English speakers as well. Having worked closely with them for half a year, I can say that I believe that the Sofia team is up to the task of bringing our existing projects to fruition and finding those new opportunities that will produce future profits.

Regulatory Matters

We had our first board meeting in Sofia in November and agreed that our initial objectives were to rationalise Black Sea's management structure and to get a handle on our assets and what had happened previously. As you know, investment funds are established by promoters who make their money through a management contract that typically provides for a fixed management fee as a percentage of assets under management and a performance fee based on results. This in essence reflects the arrangements made with Black Sea's manager, Development Capital Management (Jersey) Limited ("DCMJ"), when Black Sea was established. Since neither the individual board members nor QVT are promoters seeking to derive fees from the management of Black Sea's assets, we decided to focus on the management structure and examine whether it benefited our shareholders. Given the board's expertise and background, we came to the conclusion that Black Sea could be structured more efficiently by internalizing its management so that DCMB reported directly to the board of directors, rather than to DCMJ.

We thus entered into negotiations with DCMJ for a reduction in their annual management fees, a revision of their legal responsibilities, and for the acquisition of DCMB. Under these arrangements, DCMJ would agree to undertake a monitoring and oversight role to ensure that the Fund complied with the investment restrictions set out in the prospectus. Black Sea's board believed that this deal would be of substantial and direct benefit to shareholders. The consent of the Jersey regulator (the Jersey Financial Services Commission) is required to effect these kinds of proposals and if such consent is given shareholder approval would then be required. Unfortunately, we have not yet obtained the regulator's approval for these proposals.

It does not, however, appear to make any sense to allow the current arrangement to continue – the board does not believe it is of benefit to shareholders to pay substantially higher fees rather than lower fees, to have an unwieldy governance structure, and to force the retention of a manager – when the board believes that this arrangement is not in the best interests of shareholders. So we will continue to negotiate with the regulator or, as an alternative, consider whether to migrate Black Sea to another jurisdiction that will permit the structure that we think appropriate. Either way we will require shareholder and regulatory approval so we should be returning to you with more details presently.

Overview of the Bulgarian Economy and Real Estate Market

During 2007, Bulgaria's economy continued to grow at a favourable pace. GDP increased by 6.2% year-over-year as compared with 6.3% the previous year. Unemployment continued its downward trend and at the end of the year totalled 6.9% of the total labour force as compared with 9.1% the previous year. The average monthly wage increased by 19.7% during 2007, reaching €220 per month by the end of the year, as compared with €184 at the end of the previous year. The Government has attempted to stimulate business and investment by lowering the corporate tax rate to 10% and the personal tax rate to a flat 10% of income beginning in January of this year. On the other hand, inflation reached 12.5% year-over-year as of December 2007 as compared with 6.5% the previous year. And the current account deficit stood at 21.5% of GDP as of the end of 2007 as compared with 17.8% the prior year.

Although there is a lot of news about the decline in price in residential real estate in many western countries, we have not seen any hard evidence of a similar decline in Bulgaria. We have heard reports of credit tightening in Bulgaria, but again have seen no hard evidence that a greater wariness on the part of lenders has yet to affect the Bulgarian residential real estate market. To the contrary, one could argue that if anything there is too much money in Bulgaria chasing too few deals.

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Chairman's statement (continued)

Prices for attractive residential property in Bulgaria's major cities, Sofia and Varna, have increased rapidly and now average around €1,100 per square metre. Sofia in particular continues to have obvious unmet demand and there seem to be opportunities in second tier cities that have not yet participated in growth in Sofia, Varna, the Black Sea coast and Bansko. Colliers informs us that the holiday homes inventory increased by 67% over the last year with a cumulative total of 79,000 units in inventory. Nonetheless, prices are still low by world standards – the marketing people tell us that the Black Sea coast today is where the Costa del Sol was thirty years ago. Bulgaria is a small country. The Bulgarian Black Sea coast is relatively compact. Prime coastal locations are in limited supply. And as the region in general and Bulgaria in particular increases in affluence demand should increase as well.

Much of the development to date has been in "holiday villages" along the Black Sea coast and at the Bansko ski resort. Even a casual visitor to the Black Sea coast has to be struck by massive building of obviously low quality developments and wonder who will take up the supply of these commodity-type, undifferentiated assets. Towns that barely existed a few years ago are now home to these tightly-clustered "holiday villages" that lack much in the way of charm or amenities. Much of this supply was targeted toward UK speculators, who intended to buy "off plan" with borrowed money and then unload the investment prior to completion, or who intended to use their apartment for a couple of weeks a year and then rent it out, often with the developer "guaranteeing" some sort of moderately attractive initial yield. According to what we read and hear, the UK off-plan and buy-to-let markets are at best somnolent so the latest marketing concept is to capitalise on historical and cultural ties by offering these units to the newly affluent Russians. We have seen this strategy to be successful at a high quality development like Obzor, but just how enthusiastic the Russians will be over more undifferentiated assets remains unclear.

Overview of Our Portfolio

Over the last financial year, we have made two new investments in undeveloped land, one in Sofia and the other in the Borovetz ski resort, just outside of Sofia. Luckily virtually none of our assets are commodity assets and we have nothing in the Bansko area. So we currently have six investments including three investments on the Black Sea, an investment in Pamporovo, a mountain region in the south of Bulgaria, and two investments in or near Sofia. It is important to note that each of the investments is structured differently so we have different rights as to each. In some investments we are more of a lender with the right to repayment and an equity kicker. In other assets, our investment is pure equity with all of the risks and possible rewards.

Along the Black Sea we have three investments: an investment in a holiday village under development in Obzor, an investment in undeveloped land in Byala, and an investment in a completed resort outside of Varna. We also have a possible opportunity, an option, essentially a put option on the part of the developer, to participate in a development in Kavarna. Let me give you the details as to each.

YOOBulgaria Obzor

Obzor is a town located approximately mid-way between Varna to the north and Bourgas to the south along the Black Sea coast. "YOO" is a brand representing upscale residential developments in various locations throughout the world. The YOOBulgaria Obzor project comprises 257 designer apartments with most fronting directly on the Black Sea. The idea at the outset was to market units in the UK and elsewhere in western Europe "off-plan" but that market has largely been supplanted by affluent Russian buyers. Our participation is as a mezzanine lender with a local bank as the primary lender. The project has a total financing commitment of €17.0 million and we have committed €5.3 million of that amount. This works out to a commitment of €650 per square metre. The project is well along and as of the end of April 197 units or 77% of the available stock have been sold or reserved. The marketing is done by third parties and the money received is escrowed with the primary lender. We expect that the development should be completed by the third quarter of this year.

The structure of this investment is that once the project is completed the primary lender will be repaid. Black Sea will then receive the return of its investment plus a guaranteed profit of €162.50 per square metre sold. The difference between the sale price and Black Sea's initial investment plus guaranteed profit will then be split 70/30 with the larger share going to the developer. The returns payable to Black Sea are subject to an IRR cap of 90% so any profit in excess of this IRR will accrue to the developer. Once the project is completed, Black Sea has the obligation (or right, depending on how you want to look at it) to purchase any unsold units at €650 per square metre (which is about the cost of construction) minus what has already been disbursed. Units are currently going for an average of about €1400 per square metre. So we are optimistic that this project will work out well for Black Sea and that cash will start coming in sometime over the next few months.

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Chairman's statement (continued)

Byala

Byala is a town a little to the north of Obzor. Our investment is in 161,820 square metres of undeveloped land in a pristine location directly on the Black Sea. There is no infrastructure in place such as road, water, electric or sewage. The structure of the transaction was that Black Sea advanced €9.7 million in the form of an interest free loan to the same developer who is developing Obzor and in return had the right to participate in the planned development. That developer was required to meet a number of conditions precedent by March of 2008 or transfer the land to Black Sea. The developer failed to meet the conditions precedent by the required date so we have demanded that he transfer the land to us, and he has agreed to do so. There are certain Bulgarian regulatory and tax issues that must be complied with, but we expect that the transaction will be completed no later than the end of the second quarter of this year. At that point we will have to decide whether to develop the land ourselves or sell it to a third party.

Kavarna

Kavarna is a town north of Varna on the Black Sea. The same developer who developed Obzor owns seaside land on a high cliff overlooking the Black Sea. The developer essentially has a put option that requires us to finance this development upon his meeting certain conditions precedent and we have a call option to participate in the future development if the developer decides to develop the land. The conditions precedent have not yet been met and we have therefore not advanced any financing. The contractual structure is similar to that of Obzor – we are mezzanine lenders with an upside that partially has the character of equity and partially has the character of debt. Our participation is attractive so long as the development is well designed, constructed, and marketed and the market for higher end holiday property on the Black Sea remains firm. At this time it is still unclear whether the developer will be able to meet the conditions precedent, so we do not know whether this is something in which we will participate.

Nikea Park

Nikea Park is a completed development located in the Golden Sands resort area 18 km from Varna. Black Sea backed a local Bulgarian developer by financing 119 of the 154 apartment units in a nine story apartment building about 500 metres off the beach. Besides studio, one and two bedroom apartments, Nikea Park comprises a swimming pool, bar, restaurant, kiosk, and spa. Black Sea's investment was €4 million. The original idea was to market those units "off plan" and to appeal to the buy-to-let market in the UK. Given the subsequent developments in the UK residential market, this marketing concept did not prove overly successful and it is now thought that the most promising market is the newly affluent Russians.

This investment has had several issues. There have been problems with the construction as well as with the pricing and marketing of units. Under the contract, Black Sea seems to have limited rights regarding the pricing and marketing of units, which are handled by the developer. The developer seems to have little incentive to price units realistically or to move our units because only when the developer receives payment from the sale or reservation of one of Black Sea's units is he required to pay us. Upon sale, our overall return was agreed to be the return of our initial investment, €100 per square metre as guaranteed profit, and then the difference between €600 and the achieved sales price being split 30/70 with 30% going to Black Sea and 70% going to the developer. But since the developer is not required to pay us anything till he receives payment and the interest rate is lower than the rate of inflation, the developer has little incentive to sell our units today rather than tomorrow. In addition, the developer owns units apart from Black Sea – note that we only financed 119 of the 154 units – and has given those units priority in marketing. The developer currently offers unsold units for short term rentals and Black Sea's rights are limited under the contract to share in the rental income.

So far, eight of Black Sea's 119 apartments have been sold at an average selling price of €1,070 per square metre, and three have been reserved. The developer however has failed to pay us in accordance with the contract and Black Sea has commenced legal proceedings in Bulgaria. Nikea Park is obviously an unsatisfactory asset, and we are exploring various options to rescue our investment.

Magnolia Holidays, Pamporovo

Magnolia Holidays in the Pamporovo ski resort, in the Rodopa Mountains is another problematic investment. The idea behind this development was that Black Sea would finance the construction of a ski resort development in Pamporovo in southern Bulgaria. The resort development was expected to comprise 420 luxury apartments, commercial shops and so on. Black Sea was a mezzanine lender with a regional bank as the primary lender. The structure of the deal was that Black Sea agreed to lend a local developer €13.7 million (equivalent to €577 per square metre) to finance 348 units and we advanced €5.5 million or €230.8 per square metre. When a unit is sold, Black Sea is entitled to repayment of the financing amount and a guaranteed profit equal to that same amount. In addition, Black Sea is entitled to the difference between the achieved

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Chairman's statement (continued)

sales price per square metre (net of VAT and agent's commission) and €807.8 per square metre split 70/30 with 30% going to us.

We have encountered difficulties with this investment. The construction originally scheduled for completion in January 2008 has failed to proceed on schedule and what has been constructed is a half finished shell of an apartment complex. The developer has run out of money and we have refused to provide further financing, in part because some of the money we have disbursed has not been fully accounted for. This past December we commenced a legal action in a Bulgarian court alleging that the developer had failed to pay interest due under the loan. Subsequently we commenced a legal action to seize the collateral securing our loan – essentially all of the assets of the development company, which owns the land and what has been constructed on it. After a questionable adverse decision by a lower court, we have appealed to the Plovdiv District Court and expect a decision presently.

Borovetz

Borovetz is a ski area less than an hour from downtown Sofia and 12 kilometres outside the town of Samokov. Borovetz is the oldest Bulgarian ski resort and is undergoing massive development in connection with the "Super Borovetz" project. Super Borovetz, which is being promoted by the Government and financed by substantial international investors, is intended to modernize and greatly increase the ski resort's capacity. In 2007, Black Sea acquired over 124,000 square metres of land at Borovetz at €85 per square metre¹. The land is in close proximity to the lift station currently being constructed as part of Super Borovetz.

The idea is to build a resort that includes a branded hotel and individual apartments. We have hired a well known international architectural firm, which has completed a rendering of a future resort. We have approached a number of international hotel chains to serve as the anchor tenant and have had some interest. We are working on obtaining zoning of the land and are hopeful that this will be accomplished later this year. But it is still early in the process; there is no construction underway and none anticipated for the foreseeable future.

Borovetz is a large and complex situation. The attractions are obvious: a future modern ski resort outside the nation's capital and largest city, not far from the Sofia airport, and close enough to the city centre that commuters could live in Borovetz and work in Sofia. But there are also serious challenges. The success of our development is contingent on the completion of Super Borovetz and that development is massive, highly challenging, and behind schedule. Currently Super Borovetz is a large open construction site that under the best of circumstances will not be completed for several years. International hotel operators are not fully comfortable with Bulgaria yet, much less with the uncertainty of a project on the scale of Borovetz. So how Borovetz will play out for Black Sea is still uncertain and we have not yet decided whether our optimal strategy is to complete the development or at some point to sell the property to a third party.

Evergreen

In early 2007, DCMB spotted an opportunity in the Malinova Dolina, Vitosha district in Sofia: a 24,600 square metre land plot zoned for residential development in the shadow of snow capped Mt. Vitosha. But first some background. Sofia, like many cities in the developing world, has insufficient infrastructure to handle its ever growing population of people and automobiles. The existing housing stock, roads and highways were created for a very different world. The housing stock in downtown Sofia is in need of rejuvenation, but there are structural problems that have prevented this from progressing as quickly as one would hope. So the solution has been for the city to expand southward towards Mt. Vitosha. Malinova Dolina, a district that was once considered out in the middle of nowhere and undesirable, has now become highly sought after following the construction of a large office park in the area and the Government's plans to extend the subway system to this end of the city.

Following the acquisition of the land for €4 million, DCMB hired a noted young local architect to provide the design. What he came up with is a plan that includes twenty-seven detached homes and seventy-two apartments in six buildings. The intended market is affluent Bulgarians looking for an alternative to living and working in the city centre as well as expats and domestic and foreign investors. The market has responded very favourably and as of the end of April we have sixteen reservations that if completed will have a total value of €5.4 million. We have managed to push through several price increases and feel that the demand continues to be strong.

¹ There is a slight complication here in that Black Sea reserved a second, much smaller, parcel of land, which we have decided not to develop but, rather, to return to the seller in return for our deposit, which is about €360,000.

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Chairman's statement (continued)

All of our zoning and permits are in place and the issues involving infrastructure seem manageable. We expect to commence construction around the third quarter of this year and hope to complete this project before the end of next year. We are in talks with local banks for financing, which is estimated at about €9 million. Shareholders who want to get a better idea of what Evergreen offers should go to www.evergreen.bg.

* * * *

I look forward to communicating further after we have completed our results for the first half of 2008. We are aware that news has been sparse, in part because of certain regulatory constraints, but we intend to have a road show in London before the end of the second quarter to meet with our shareholders and answer any questions that our shareholders may have. Shareholders who wish to participate should get in touch with our NOMAD, Numis Securities, which will be managing the process.

Respectfully yours,

John D. Chapman
Chairman

8 May 2008

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Directors' Report

For the year ended 31 December 2007

The Directors submit their Report and Financial Statements for the year ended 31 December 2007

The Company was incorporated on 27 January 2005, in Jersey and was launched as an unclassified Fund on 14th March 2005 within the provisions of the Collective Investment Funds (Jersey) Law 1988.

Listing

The Fund is listed on AIM.

Investment Strategy and Principal Activity

The Black Sea Property Fund seeks to generate substantial capital gains through the financing and sale of residential property in Bulgaria, including the prime areas of Bulgaria's Black Sea coast and the ski resorts. The Fund, which raised £50 million on launch, offers investors the opportunity to gain exposure to early stage residential property, in a growing economy.

Results and Dividends

It is not intended in normal circumstances that the Fund will pay dividends on the shares,

The proceeds realised from the Property Portfolio will be available for reinvestment into further investment property (net of any performance fee due). The Board will, however, consider the distribution of capital profits on the Property Shares after the first 3 periods of the Fund's life and at any time if the Property Investment Adviser does not believe there to be further attractive investment opportunities. Following the end of the fifth period of the Fund's life, the proceeds of sale of the Property Portfolio will be returned to Shareholders as determined by the Board.

The income statement is set out on page 12 of this Annual Report and Financial Statements. The Directors do not recommend the payment of a dividend.

Life of the Company

The Company will have a life of 5 years plus up to 2 further years for the planned realisation of the Property Portfolio. The life may be extended by special resolution of Shareholders (requiring a two-thirds majority of those voting).

Board of Directors

The Directors of the Company are :

Executive: John Chapman (Chairman)

Non-executive:

Antony Gardner-Hillman
Irena Komitova
Andrey Kruglykhin
Angelo Moskov
Bogdan Stanchev
Andrew Wignall

Changes in Directors

Mr John Chapman, Mr Angelo Moskov, Mr Andrey Kruglykhin and Mr Antony Gardner-Hillman were appointed Directors on 19 October 2007.

The following Directors resigned on the dates noted: Mr Melville Trimble (19 October 2007), Mr Roger Maddock (19 October 2007), and Mr William Drysdale (08 November 2007).

On 10 March 2008 Mr Andrew Wignall was appointed and Mr W. Roger King resigned as a Director of the Company.

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Directors' Report (continued)

Custodian - Fixed Income Portfolio

BNP Paribas (Jersey branch) provides custody services in relation to the Fund.

Shareholder's Interests

<i>Extent of Holdings</i>	<i>No. of shareholders</i>
1-9,999	66
10,000-99,999	68
100,000 - ,499,999	32
500,000+	38
	<u>204</u>

At 14 March 2008 the Company was aware of the following interests of 3% or more in the Ordinary share capital of the Company:

	<i>Number</i>	<i>% held</i>
Nutraco Nominees Limited	39,352,650	15.70%
Vidacos Nominees Limited	37,046,110	14.78%
Deutsche Bank Aktiengesellschaft	27,125,000	10.82%
Euroclear Nominees Limited	21,640,008	8.63%
BNY (OCS) Nominees Limited	21,640,008	8.63%
Morstan Nominees Limited	16,921,675	6.75%
HSBC Global Custody Nominee (UK) Limited	9,187,500	3.66%

The Company has received notification of the following beneficial ownerships:

<i>Beneficial shareholder</i>	<i>Percentage interest</i>
Black Rock Investment Management	18.00%
QVT Fund LP	10.37%
SVM Asset Management	8.03%
New Star Asset Management	7.49%

The Directors are not otherwise aware of interests of 3% or more in the Company's issued share capital.

Directors' Interests

The maximum amount of remuneration payable to the Directors permitted under the Articles is £100,000 per annum, plus reasonable expenses. The Directors received in aggregate £101,525 for the year ended 31 December 2007.

At 31 December 2007 Mr W. Roger King held an interest in 50,000 shares (2006 50,000)

Mr Chapman and Mr Kruglykhin are consultants to, and Mr. Moskov is a partner with, QVT Financial LLP, which is a substantial shareholder of the Fund

By Order Of The Board
BNP Paribas Fund Services Jersey Limited
Secretary

8 May 2008

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Statement of Directors' Responsibilities

The Directors are responsible for preparing the financial statements in accordance with applicable law and International Financial Reporting Standards.

Company law requires the Directors to prepare financial statements for each financial year which give a true and fair view of the state of affairs of the Company and of the profit and loss of the Company for that year.

In preparing those financial statements the Directors are required to:

- select suitable accounting policies and then apply them consistently;
- make judgements and estimates that are reasonable and prudent;
- prepare the financial statements on a going concern basis unless it is inappropriate to presume that the Fund will continue in business; and
- state whether applicable accounting standards have been followed, subject to any material departures disclosed and explained in the financial statements.

The Directors are responsible for keeping accounting records that disclose with reasonable accuracy, at any time, the financial position of the Company and enable them to ensure that the financial statements comply with the Companies (Jersey) Law 1991, as amended. They are also responsible for safeguarding the assets of the Company and hence for taking reasonable steps for the prevention and detection of fraud, and other irregularities.

Independent auditors' report to the members of The Black Sea Property Fund Limited

We have audited the financial statements of The Black Sea Property Fund Limited for the year ended 31 December 2007 which comprise the Consolidated Income Statement, the Consolidated and Company Balance Sheets, the Consolidated Statement of Changes in Equity, the Consolidated Statement of Cash Flows and the related notes. These financial statements have been prepared under the accounting policies set out therein.

This report is made solely to the company's members, as a body, in accordance with Article 110 of the Companies (Jersey) Law 1991. Our audit work has been undertaken so that we might state to the company's members those matters we are required to state to them in an auditor's report and for no other purpose. To the fullest extent permitted by law, we do not accept or assume responsibility to anyone other than the company and the company's members as a body, for our audit work, for this report, or for the opinions we have formed.

Respective responsibilities of directors and auditors

As described in the Statement of Directors' Responsibilities on page 10, the company's directors are responsible for preparation of the financial statements in accordance with applicable law and International Financial Reporting Standards.

Our responsibility is to audit the financial statements in accordance with the relevant legal and regulatory requirements and International Standards on Auditing (UK and Ireland).

We report to you our opinion as to whether the financial statements give a true and fair view and are properly prepared in accordance with the Companies (Jersey) Law 1991. We also report to you if, in our opinion, the company has not kept proper accounting records or if we have not received all the information and explanations we require for our audit.

We read the Chairman's Statement, the Manager's Report and the Directors' Report accompanying the financial statements and consider the implications for our report if we become aware of any apparent misstatements within it.

Basis of audit opinion

We conducted our audit in accordance with International Standards on Auditing (UK and Ireland) issued by the Auditing Practices Board. An audit includes examination, on a test basis, of evidence relevant to the amounts and disclosures in the financial statements. It also includes an assessment of the significant estimates and judgements made by the directors in the preparation of the financial statements, and of whether the accounting policies are appropriate to the company's circumstances, consistently applied and adequately disclosed.

We planned our audit so as to obtain all the information and explanations which we considered necessary in order to provide us with sufficient evidence to give reasonable assurance that the financial statements are free from material misstatement, whether caused by fraud or other irregularity or error.

The Group has made loans to a third party developer, Magnolia Holidays EAD, as described in Note 6 to the Financial Statements. No interest or capital payments have been received from Magnolia Holidays EAD and the Group is undertaking legal action in an attempt to recover these funds through exercising its charge on the collateral, being the share capital of Magnolia Holidays EAD. The outcome of the legal action is uncertain and there are no satisfactory audit procedures that we could perform to obtain reasonable assurance that the net assets of Magnolia Holidays EAD are sufficient collateral for the outstanding amount. The Group's loan receivable balance shows £4,538,494 in respect of the receivable amounts from Magnolia Holidays EAD.

In forming our opinion we also evaluated the overall adequacy of the presentation of information in the financial statements.

Qualified opinion arising from limitation in audit scope

Except for the financial effects of such adjustments, if any, as might have been determined to be necessary had we been able to satisfy ourselves as to the loan receivable balance described above, in our opinion the financial statements:

- give a true and fair view, in accordance with International Financial Reporting Standards, of the state of the company's affairs as at 31 December 2007 and of its profit for the year then ended; and
- have been properly prepared in accordance with the Companies (Jersey) Law 1991.

KPMG Channel Islands Limited

Chartered Accountants

8 May 2008

THE BLACK SEA PROPERTY FUND LIMITED

Annual report and financial statements for the year ended 31 December 2007

Consolidated Income Statement

For the Year Ended 31 December 2007

	Notes	Year ended 31 Dec 2007 £	Year ended 31 Dec 2006 £
Revenue		20,276	-
Gross Profit		20,276	-
Bank interest		65,156	173,143
Loan Interest		1,170,938	579,017
Total revenue		1,256,370	752,160
Gain on investments	8	4,220,954	90,016
Currency gains / (losses)		67,413	(23,540)
Total income		5,544,737	818,636
Operating expenses			
Management fee	2	(1,000,000)	(1,000,000)
Other operating expenses	3	(1,658,254)	(2,222,441)
Total operating expenses		(2,658,254)	(3,222,441)
Profit before tax		2,886,483	(2,403,805)
Tax	5	(118,547)	(35,057)
Profit / (loss) for the year		2,767,936	(2,438,862)
Basic earnings per share (pence)	4	1.1	(1.0)
Diluted earnings per share (pence)	4	1.1	(1.0)

All income is attributable to the equity holders of The Black Sea Property Fund Limited. There are no minority interests.

The notes on pages 16 to 29 are an integral part of these financial statements.

Annual report and financial statements for the year ended 31 December 2007

Consolidated Balance Sheet
As at 31 December 2007

	Notes	Group 2007 £	Company 2007 £	Group 2006 £	Company 2006 £
Non-current assets					
Investments in subsidiaries	9	-	56,406	-	17,199
Plant and Equipment	6	123,165	-	-	-
Investment Property	6	10,680,846	-	247,238	-
Exercised Options over property	6	150,799	150,799	150,799	150,799
Interest in property	6	96,941	-	518,561	-
Loans and receivables	6	17,785,638	32,000,569	14,446,857	15,396,339
		<u>28,837,389</u>	<u>32,207,774</u>	15,363,455	15,564,337
Current assets					
Other receivables	10	376,870	8,354	10,019	9,820
Investments at fair value through profit or loss	7	13,200,466	13,200,466	23,424,780	23,424,780
Cash and cash equivalents		1,877,181	262,395	3,213,477	3,009,810
		<u>15,454,517</u>	<u>13,471,215</u>	26,648,276	26,444,410
Total assets		<u>44,291,906</u>	<u>45,678,989</u>	42,011,731	42,008,747
Current liabilities					
Other payables	11	(283,145)	(174,846)	(216,503)	(176,040)
Net assets		<u>44,008,761</u>	<u>45,504,143</u>	41,795,228	41,832,707
Equity					
Share capital	12	50,138,313	50,138,313	50,138,313	50,138,313
Retained earnings		(6,129,552)	(4,634,170)	(8,343,085)	(8,305,606)
Total equity		<u>44,008,761</u>	<u>45,504,143</u>	41,795,228	41,832,707
Net asset value per Ordinary share (pence)	13	<u>17.6</u>	<u>18.2</u>	16.7	16.7

These financial statements were approved by the Board of Directors on 8 May 2008

John D. Chapman
Director

Andrew Wignall
Director

The notes on pages 16 to 29 are an integral part of these financial statements.

THE BLACK SEA PROPERTY FUND LIMITED

Annual report and financial statements for the year ended 31 December 2007

Consolidated Statement of Changes in Equity For the Year Ended 31 December 2007

Group

For the year ended 31 December 2006

	Share capital £	Retained earnings £	Total £
As at 1 January 2006	50,138,313	(5,910,129)	44,228,184
Net operating loss for the year	-	(2,438,862)	(2,438,862)
Foreign exchange on subsidiary translation	-	5,906	5,906
	-----	-----	-----
At 31 December 2006	50,138,313	(8,343,085)	41,795,228
	=====	=====	=====

For the year ended 31 December 2007

	Share capital £	Retained earnings £	Total £
As at 1 January 2007	50,138,313	(8,343,085)	41,795,228
Net operating profit for the year	-	2,767,936	2,767,936
Foreign exchange on subsidiary translation	-	(554,403)	(554,403)
	-----	-----	-----
At 31 December 2007	50,138,313	(6,129,552)	44,008,761
	=====	=====	=====

The notes on pages 16 to 29 are an integral part of these financial statements.

THE BLACK SEA PROPERTY FUND LIMITED

Annual report and financial statements for the year ended 31 December 2007

Consolidated Statement of Cash Flows

For the Year Ended 31 December 2007

	Group 2007 £	Company 2007 £	Group 2006 £	Company 2006 £
Operating activities				
Gain/(loss) before tax for the year	2,886,483	3,789,848	(2,403,805)	(2,366,521)
Gain on investments held at fair value through profit or loss	(4,220,954)	(4,220,954)	(90,016)	(90,016)
Currency (gains)/ losses	(67,413)	(67,413)	23,540	23,540
Increase in loan interest receivable	(550,339)	(1,550,717)	(287,511)	(306,230)
(Increase)/decrease in other receivables	(366,851)	1,466	281	480
Increase/(decrease) in other payables	66,642	(1,194)	(93,613)	(98,334)
Net cash outflow from operating activities after interest and before taxation	(2,252,432)	(2,048,964)	(2,851,124)	(2,837,081)
Tax paid	(64,329)	-	-	-
Net cash outflow from operating activities	(2,316,761)	(2,048,964)	(2,851,124)	(2,837,081)
Investing activities				
Loans to developers	(1,723,684)	-	(14,166,652)	-
Loans repaid	751,031	751,031	-	-
Loan interest repaid	-	-	-	-
Loans to subsidiaries	-	(13,478,113)	-	(14,592,343)
Options over property payment	-	-	(12,486)	(12,486)
Purchase of land and property	(10,558,526)	-	(247,238)	-
Purchase of property subsidiary	-	(34,805)	-	(12,896)
Purchase of accumulation money market funds	(9,561,721)	(9,561,721)	(2,385,090)	(2,385,090)
Sales of accumulation money market funds	21,557,924	21,557,924	18,385,014	18,385,014
Net cash inflow/(outflow) from investing activities	465,024	(765,684)	1,573,548	1,382,199
Financing activities				
Sales commission and formation costs paid	-	-	25,000	25,000
Net cash inflow from financing activities	-	-	25,000	25,000
Net decrease in cash and cash equivalents	(1,851,737)	(2,814,648)	(1,252,576)	(1,429,882)
Cash and cash equivalents at 31 December 2006	3,213,477	3,009,810	4,467,734	4,431,318
Effect of foreign exchange rates	515,441	67,233	(1,681)	8,374
Cash and cash equivalents at 31 December 2007	1,877,181	262,395	3,213,477	3,009,810

The notes on pages 16 to 29 are an integral part of these financial statements.

THE BLACK SEA PROPERTY FUND LIMITED

Annual report and financial statements for the year ended 31 December 2007

Notes to the financial statements

1 Accounting Policies

The consolidated financial statements of the Company for the year ended 31 December 2007 comprise the Company and its subsidiaries (together, the 'Group') and have been prepared in accordance with International Financial Reporting Standards ("IFRS") issued by the International Accounting Standards Board (IASB) and interpretations issued by the International Financial Reporting Committee of the IASB (IFRIC).

IFRS Applied

The following IFRS standards have been applied in the current financial year: IFRS 7 "Financial Instruments: Disclosures" and the amendment to IAS 1 "Presentation of Financial Statements"

There is no material financial impact arising from the application of these standards and interpretations. The financial statements have been updated to include new disclosures arising from these standards where appropriate.

(a) Basis of measurement

The consolidated financial statements have been prepared on the historical cost basis except for the following:

- financial instruments at fair value through profit and loss are measured at fair value.
- investment property is measured at fair value.

(b) Use of estimates and judgements

The preparation of financial statements requires management to make judgements, estimates and assumptions that affect the application of accounting policies and the reporting amounts of assets, liabilities, income and expenses. Actual results may differ from these estimates.

Estimates and underlying assumptions are reviewed on an ongoing basis. Revisions to accounting estimates are recognised in the period in which the estimate is revised and in any future periods affected.

(c) Revenue recognition

Interest receivable on fixed interest securities is recognised in 'Interest income' using the effective interest method. The effective interest method is a way of calculating the amortised cost of a financial asset or a financial liability (or groups of financial assets or financial liabilities) and of allocating the interest income or interest expense over the relevant period.

The effective interest rate is the rate that exactly discounts estimated future cash receipts or payments through the expected life of the financial instrument or, where appropriate, a shorter period, to the net carrying amount of the financial asset or financial liability. When calculating the effective interest rate, the Company estimates cash flows considering all contractual terms of the financial instrument but not future credit losses. The calculation includes all amounts paid or received by the Company that are an integral part of the effective interest rate, including transaction costs and all other premiums or discounts.

Interest on impaired financial assets is calculated by applying the original effective interest rate of the financial asset to the carrying amount as reduced by any allowance for impairment.

(d) Basis of consolidation

The consolidated financial statements incorporate the financial statements of the Company and entities controlled by the Company (its subsidiaries) made up to 31 December each year. Control exists when the Company has the power, directly or indirectly, to govern the financial and operating policies of an entity so as to obtain benefits from activities. The financial statements of subsidiaries are included in the consolidated financial statements from the date that control commences up to the date that control ceases.

(e) Expenses

Expenses are charged through the income statement, except for expenses which are attributable to the disposal of an investment, which are deducted from the disposal proceeds of the investment. In addition, certain expenses associated with the acquisition of an investment have been capitalised.

THE BLACK SEA PROPERTY FUND LIMITED

Annual report and financial statements for the year ended 31 December 2007

Notes to the financial statements (continued)

(f) Investments

General

Assets are recognised at the trade date of acquisition and are recognised initially at fair value plus any directly attributable transaction costs.

Plant and equipment is stated at cost less accumulated depreciation and any recognised impairment loss. Depreciation is charged so as to write off the cost of assets, other than land or properties under construction, over their estimated useful lives, using straight line method at 4%, on the following bases:

Equipment - 25 years

The gain or loss on the disposal or retirement of an asset is determined as the difference between the sales proceeds and the carrying amount of the asset and is recognised in the income statement.

Investments at fair value through profit or loss

An instrument is classified as at fair value through profit or loss if it is held for trading or is designated as such upon initial recognition. Financial instruments are designated at fair value through profit or loss if the Company manages such investments and makes purchase and sale decisions based on their fair value. Fair value is the amount at which an investment could be exchanged between knowledgeable willing parties in an arms length transaction.

Purchases of investments are recognised on the trade date, being the date that amounts are due for payment. Investments are derecognised when the rights to receive cash flows from the investments have expired or the Company has transferred substantially all risks and rewards of ownership.

Investments are initially recognised at fair value being the transaction price. Transaction costs for all financial assets carried at fair value through profit or loss are expensed as incurred.

Subsequent to initial recognition, all financial assets at fair value through the profit or loss are measured at fair value. Gains and losses arising from changes in fair value are presented in the income statement in the year in which they arise. On disposal, realised gains and losses are also recognised in the income statement.

Fair values of financial instruments traded in active markets are based on quoted market prices at the balance sheet date. The quoted market price used for financial assets held by the Company is the current bid price.

Loans and receivables

Loans and receivables include loans and advances originated by the Company that are not intended to be sold in the short term and are recognised on an amortised cost basis. Loans and receivables are recognised when cash is advanced to borrowers and are derecognised when the borrowers repay their obligations, the loans are sold or written off or substantially all the risks and rewards of ownership are transferred. They are initially recorded at fair value plus any directly attributable transaction costs and are subsequently measured at amortised cost using the effective interest method, less impairment losses. A provision for impairment is established when there is objective evidence that the Company will not be able to collect all amounts due from the relevant borrower. Where they are denominated in a foreign currency they are translated at the prevailing balance sheet exchange rate.

Where the interest rate associated with such loans and receivables is below market, an adjustment is made to reflect the fair value accordingly.

Investment property

Property that is held for capital appreciation, and that is not occupied by the companies in the Group, is classified as investment property.

Investment property comprises freehold land and freehold buildings. Land held for capital appreciation or for development as an investment property is immediately classified as investment property.

Investment property is measured initially at its cost, including related transaction costs. After initial recognition, investment property is carried at fair value, although the property may not be revalued in the year of acquisition. Changes in fair values are recorded in the income statement.

THE BLACK SEA PROPERTY FUND LIMITED

Annual report and financial statements for the year ended 31 December 2007

Notes to the financial statements (continued)

Fair value is based on active market prices, adjusted if necessary for any difference in the nature, location or condition of the specific asset. If this information is not available, the Group uses alternative valuation methods. The valuations are prepared annually by Colliers International.

Interest in Property

Interest in property represents amounts capitalised in relation to non-derivative options to acquire property at future dates. Amounts capitalised are amortised over the period of the corresponding options.

(g) Movements in fair value

Changes in the fair value of all held-at-fair-value assets are taken to the income statement. On disposal, realised gains and losses are also recognised in the income statement.

(h) Cash and cash equivalents

Cash and cash equivalents comprise current deposits with banks.

(i) Taxation

The Company is an Exempt Company for Jersey taxation purposes. The Company pays an exempt company fee, for each company within the Group, which is currently £600 per company per annum.

The subsidiary companies, BSPF Magnolia EAD, BSPF Project 1 EAD, BSPF Project 4 EAD, BSPF Super Borovetz EAD, and BSPF Tchernomore EAD will be liable for Bulgarian corporation tax at a rate of 10%. The subsidiary companies are not liable for any further local taxes; however withholding tax may be liable on repatriation of assets and income to the Company, as currently there is no double taxation treaty between Jersey and Bulgaria.

Deferred tax is recognised in respect of all temporary differences that have originated but not reversed at the balance sheet date, where transactions or events that result in an obligation to pay more tax in the future or right to pay less tax in the future have occurred at the balance sheet date. This is subject to deferred tax assets only being recognised if it is considered more likely than not that there will be suitable profits from which the future reversal of the temporary differences can be deducted.

(j) Foreign currency

The results and financial position of the Company are expressed in pounds sterling, which is the Company's functional currency.

Transactions in currencies other than sterling are recorded at the rates of exchange prevailing on the dates of the transactions. At each balance sheet date, monetary items and non-monetary assets and liabilities that are fair valued and that are denominated in foreign currencies are retranslated at the rates prevailing on the balance sheet date. Gains and losses arising on retranslation are included in net profit or loss for the period where investments are classified as at fair value through profit or loss. Exchange differences on translation of the Company's net investment in foreign operations are recognised directly in equity.

(k) Share Capital

Ordinary share capital

Ordinary shares are classified as equity. External costs directly attributable to the issue of new shares are shown as a deduction to reserves.

Founder shares

Founder shares are classified as equity.

(l) Segmental Analysis

A business segment is a group of assets and operations engaged in providing products or services that are subject to risks and returns that are different from those of other business segments. A geographical segment is engaged in providing products or services within a particular economic environment that are subject to risks and returns that are different from those of segments operating in other economic environments.

THE BLACK SEA PROPERTY FUND LIMITED

Annual report and financial statements for the year ended 31 December 2007

Notes to the financial statements (continued)

Other than the investment in money market funds in the UK, the Group is organised into one main geographical and business segment focusing on the Bulgarian property market. No additional disclosure is included in relation to segmental reporting as the Group's activities are limited to one main business segment and one main geographical segment.

(m) New standards and interpretations not applied

At the date of authorisation of these financial statements, the following standards and interpretations were in issue but not yet effective:

- IFRS 8 - Operating Segments (effective for annual periods beginning on or after 1 January 2009)
- Amendment to IAS 1 – Presentation of Financial Statements: A Revised Presentation (effective for annual periods beginning on or after 1 January 2009).
- Amendments to IAS 23 – Borrowing Costs (effective for annual periods beginning on or after 1 January 2009)
- Amendments to IAS 27 – Consolidated and Separate Financial Statements (effective for annual periods beginning on or after 1 July 2009)
- Amendments to IAS 32 and IAS 1 – Puttable Financial Instruments and Obligations arising on Liquidation (effective for annual periods beginning on or after 1 January 2009)
- Revised IFRS 3 – Business Combinations (effective for annual periods beginning on or after 1 July 2009)

The Directors anticipate that the adoption of these standards and interpretations in future periods will have no material impact on the financial statements for the Company.

2 Management fee

	Group 2007 £	Group 2006 £
Management fee	1,000,000	1,000,000
	-----	-----

The management fee paid to Development Capital Management (Jersey) Limited is 2% per annum of the amount subscribed plus any gains retained by the Company for reinvestment.

The management agreement between the Company and the Manager is terminable by either party on twelve month's notice, subject to an initial term of 36 months from admission. On 6 September 2007, the Company notified the Manager that the management agreement would be terminated 12 months hence.

The Manager is entitled to receive a performance fee of 20% of any cash returns from the sale of a property investment above a hurdle rate of 10% compound per annum up to 100% and 30% of any returns in excess of this. As at 31 December 2007 there is no contingent performance fee. Twenty percent of the performance fee is subject to a claw back retention against the future performance of the Company.

3 Other operating expenses

	Group 2007 £	Group 2006 £
Marketing and public relations	426,399	827,230
Amortisation charge	423,257	291,506
Legal and professional fees	279,967	167,102
Advisory and consultancy fees	177,850	610,043
Directors' remuneration	101,525	70,120
Administration fees	58,193	55,933
Travel and subsistence	51,414	47,163
Auditors remuneration for:		
Audit services	46,484	45,500
Non-audit services	-	27,687
Custodian fees and bank charges	34,379	19,490
Other	58,786	60,667
	-----	-----
	1,658,254	2,222,441
	-----	-----

The Company has no employees. All operational activities are carried out by the Manager on behalf of the Company.

THE BLACK SEA PROPERTY FUND LIMITED

Annual report and financial statements for the year ended 31 December 2007

Notes to the financial statements (continued)

4 Earnings per share

The earnings per ordinary share is based on the net profit for the year of £2,767,936 (2006: loss of £2,438,862) and on 250,691,563 (2006: 250,691,563) ordinary shares.

The diluted return per ordinary share is based on the net profit for the year and 251,728,907 (2006: 251,728,907) ordinary shares, which reflects the potential dilution as discussed in note 12.

5 Tax

	Group 2007 £	Group 2006 £
Irrecoverable overseas tax	118,547	35,057
	-----	-----

This tax represents irrecoverable withholding tax on the interest on loans to subsidiaries.

6 Investing activities

(a) Investment property and plant and equipment

	Investment Property £	Plant and equipment £	Total £
At 1 January 2007			
Cost	247,238	-	247,238
Accumulated depreciation	-	-	-
	-----	-----	-----
Net book amount	247,238	-	247,238
	-----	-----	-----
Year ended 31 December 2007			
Opening net book amount	247,238	-	247,238
Additions	10,433,608	124,918	10,558,526
Depreciation charge	-	(1,753)	(1,753)
	-----	-----	-----
	10,680,846	123,165	10,804,011
	-----	-----	-----
At 31 December 2007			
Cost	10,680,846	124,918	10,805,764
Accumulated depreciation	-	(1,753)	(1,753)
	-----	-----	-----
Net book amount	10,680,846	123,165	10,804,011
	-----	-----	-----

(b) Exercised options over property

	Group & company 2007 Unlisted £	Group & company 2006 Unlisted £
Opening book cost	150,799	138,313
Purchases at cost	-	-
Expenses capitalised	-	12,486
	-----	-----
Closing book cost	150,799	150,799
	-----	-----

The consideration for the options of £138,313 was in the form of shares in the Company.

THE BLACK SEA PROPERTY FUND LIMITED

Annual report and financial statements for the year ended 31 December 2007

Notes to the financial statements (continued)

(c) Interest in property

	Group 2007	Company 2007	Group 2006	Company 2006
	£	£	£	£
Interest in property	96,941	-	518,561	-

An interest free loan was made to a third party in order to secure an option to acquire land at Byala at a future date under certain conditions. This interest free loan is accounted for at amortised cost using the effective interest rate method. As the loan bears interest at a rate below a market rate, a discount has been separately capitalised as "interest in property" in recognition of the asset that the option represents, and is being amortised over its useful economic life. Following the end of this financial year, the Company demanded that this third party transfer the Byala land to the Company in satisfaction of the contract. As of 30 April, 2008, this transfer has not yet been completed.

(d) Loans

	Group 2007	Company 2007	Group 2006	Company 2006
	£	£	£	£
Loans and interest	17,553,875	31,768,806	14,215,094	15,164,575
Expenses capitalised	231,763	231,763	231,763	231,764
	17,785,638	32,000,569	14,446,857	15,396,339

Details of loans and the corresponding developments in existence at the year end are given below:

Magnolia, Pamporovo

The Company has made loans totalling EUR 5,596,096 to its subsidiary BSPF Magnolia EAD on 14 November 2005, 23rd May 2006, 18th November 2006 and 2nd April 2007. The interest rate is a multiple of 1.25 times the aggregate of 5% and the six month Euribor rate. The loans and interest are payable on demand.

BSPF Magnolia EAD has subsequently made loans totalling EUR 5,488,938 to a developer, Magnolia Holidays EAD with the same interest rate. Interest from Magnolia Holidays EAD is payable on demand. The repayment date of the loan is the earlier of when all units have been sold or 9 January 2009. The loan to Magnolia Holidays EAD has been secured by a share pledge over that company's entire share capital of 50,000 registered shares as well as security interests in other assets.

Byala

The Company has made two loans of EUR 9,709,200 to its subsidiary BSPF (Property) Limited, which has then lent these funds to the Bulgarian Property Investment Trust AD. No interest is accruing on these loans and they are repayable on property completion. The loan to the Bulgarian Property Investment Trust AD is secured by a first ranking mortgage over 161,820 square metres of land in Byala.

Sofia

The Company has made a loan of EUR 4,453,638 to its subsidiary BSPF (Property) Limited, which has then lent these funds to its subsidiary, BSPF Tchernomore EAD. The interest rate is a multiple of 1.25 times the aggregate of 5% and the six month Euribor rate. The loans and interest are payable on demand. These funds have been utilised by BSPF Tchernomore EAD to acquire 24,600 square metres of development land in the Malinova district of Sofia and for the design and development process.

Borovetz

The Company has made loans totalling EUR 453,744 to its subsidiary BSPF (Property 2) Limited, which has then lent these funds to its subsidiary BSPF Super Borovetz EAD. The first tranche of EUR 360,720 was lent 26 January 2006 at 5% per annum. The second tranche of EUR 93,024 was lent on 4 May 2007. The interest per annum is a multiple of 1.25 times the aggregate of 5% and the six month Euribor rate. The loans and interest are payable on demand. This loan is unsecured.

These funds have been utilized to pay a deposit for the acquisition of up to 40,000 square metres of development land in the Borovetz ski resort.

THE BLACK SEA PROPERTY FUND LIMITED

Annual report and financial statements for the year ended 31 December 2007

Notes to the financial statements (continued)

Nikea Park

The Company has made loans totalling EUR 4,006,605 to its subsidiary BSPF (Property 4) Limited, which has then lent on the funds to Bulmix 97 Group OOD. Interest is accruing at 7% per annum on these loans and they are repayable on the sale of the individual units at Nikea Park. The loan to Bulmix 97 Group OOD is secured by a second ranking mortgage over the land and first ranking mortgage over the units as well as the construction rights for these units.

Obzor

The Company has made loans totalling EUR 5,274,750 to its subsidiary BSPF (Property 5) Limited, which has then lent on EUR 3,663,000 of the funds to the Black Sea Investment Trust AD. Interest is accruing at 7% per annum on these loans. The loan to the Black Sea Investment Trust AD has been secured by a third ranking mortgage (after two mortgages in favour of the financing bank). The loan is repayable upon completion of the property for all sold units. BSPF (Property 5) Limited will acquire ownership of the unsold units at a cost of EUR 650 per square metre less the disbursed amount of EUR 195 per square metre.

Borovetz II

The Company has made loans totalling EUR 11,398,819 to BSPF Project 4 EAD. The interest rate is a multiple of 1.25 times the aggregate of 5% and the six month Euribor rate. The loan is repayable on demand and is unsecured.

These funds have been utilized by BSPF Project 4 EAD to acquire 123,961 square metres of development land in the Borovetz ski resort.

7 Investments held at fair value through profit or loss

	Group & Company 2007 Unlisted £	Group & Company 2006 Unlisted £
Accumulation Money Market Funds		
Opening book cost	23,045,435	38,903,523
Movements in year:		
Purchases at cost	9,561,721	2,385,090
Sales – proceeds	(21,557,924)	(18,385,014)
- realised gain on sales	1,117,155	485,798
- realised exchange losses on sales	(343,469)	(343,962)
Closing book cost	11,822,918	23,045,435
Closing unrealised appreciation on Money Market Funds	596,939	974,152
Closing unrealised exchange gain/(loss)	780,609	(594,807)
Closing fair value	13,200,466	23,424,780

8 Gains on investments

	2007 £	2006 £
Foreign exchange gain/(loss) on loans	2,449,065	(202,488)
Movement in unrealised appreciation	998,203	150,668
Gain on disposal of Money Market Funds	773,686	141,836
Net gain on investments	4,220,954	90,016

THE BLACK SEA PROPERTY FUND LIMITED

Annual report and financial statements for the year ended 31 December 2007

Notes to the financial statements (continued)

9 Investment in subsidiary undertakings

	Company 2007		Company 2006	
	Euro	£	Euro	£
Direct subsidiaries:				
BSPF (Property) Limited	1	1	1	1
BSPF (Property 2) Limited	1	1	1	1
BSPF (Property 3) Limited	1	1	1	1
BSPF (Property 4) Limited	1	1	1	1
BSPF (Property 5) Limited	1	1	1	1
BSPF (Property 6) Limited	1	1	-	-
BSPF Project 1 EAD	25,565	17,252	-	-
BSPF Project 4 EAD	25,565	17,552	-	-
BSPF Magnolia EAD	25,562	17,194	25,562	17,194
	<u>76,698</u>	<u>52,004</u>	<u>25,567</u>	<u>17,199</u>
Indirect subsidiaries:				
BSPF Tchernov More EAD	6,391	4,402	-	-
BSPF Super Borovetz EAD	-	-	-	-
	<u>83,089</u>	<u>56,406</u>	<u>25,567</u>	<u>17,199</u>

The Euro amounts have been translated at the respective rate prevailing at the date of acquisition.

The Company holds 50,000 Ordinary shares of Bulgarian Lev 1 in BSPF Magnolia EAD, BSPF Project 1 EAD, and BSPF Project 4 EAD which are incorporated in Bulgaria. These shares are fully paid and represent the entire issued share capital of each entity.

The Company also holds 1 Ordinary share of EUR 1 in each of the remaining subsidiaries which are incorporated in Jersey. This represents the entire issued share capital of these companies. The authorised share capital of each is EUR10,000.

10 Other receivables

	Group 2007	Company 2007	Group 2006	Company 2006
	£	£	£	£
Bank and deposit interest receivable	4,117	4,117	-	-
Inventories	79,705	-	-	-
Prepayments	103,021	4,237	10,019	9,820
Other debtors	190,027	-	-	-
	<u>376,870</u>	<u>8,354</u>	<u>10,019</u>	<u>9,820</u>

11 Other payables

	Group 2007	Company 2007	Group 2006	Company 2006
	£	£	£	£
Amounts due to subsidiaries	-	(3)	-	(3)
Tax liability	(89,275)	-	(35,057)	-
Trade creditors	(844)	-	-	-
Accruals	(174,867)	(174,843)	(181,446)	(176,037)
Advances from customers	(16,438)	-	-	-
Other creditors	(1,721)	-	-	-
	<u>(283,145)</u>	<u>(174,846)</u>	<u>(216,503)</u>	<u>(176,040)</u>

None of the amounts are passed due or impaired.

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Notes to the financial statements (continued)

12 Called up share capital

	Company 2007	Company 2006
Founder shares of no par value	10	10
Ordinary shares of no par value	Unlimited	Unlimited
	£	£
Issued and fully paid:		
2 Founder shares of no par value	-	-
250,691,563 Ordinary shares of no par value	50,138,313	50,138,313
	<u>-----</u>	<u>-----</u>

Founder shares are not eligible for participation in Company investments and carry no voting rights at general meetings of the Company.

A further 1,037,344 ordinary shares will be issued contingent upon final construction permits being granted for the options over the sites at Shabla and Kavarna.

13 Net asset value per share

The net asset value per ordinary share is based on the net assets attributable to equity shareholders of £44,008,761 (2006: £41,795,228) and on 250,691,563 (2006: 250,691,563) ordinary shares, being the number of ordinary shares in issue at the period end.

14 Financial instruments

The Company's financial instruments comprise money market funds, cash balances and debtors and creditors that arise directly from its operations, for example, in respect of sales and purchases awaiting settlement and debtors for accrued income.

The main risks the Company faces from its financial instruments are (i) market price risk, (comprising currency risk, interest rate risk and other price risk), (ii) liquidity risk, and (iii) credit risk.

The Board regularly reviews and agrees on policies for managing each of these risks. The Manager's policies for managing these risks are summarised below and have been applied throughout the period. The numerical disclosures exclude short-term debtors and creditors.

(i) Market price risk

Market price risk arises mainly from uncertainty about future prices of financial instruments used in the Company's operations. It represents the potential loss the Company might suffer through holding market positions as a consequence of price movements and movements in exchange rates.

It is the Board's policy to hold a broad spread of fixed interest investments using collective schemes in order to reduce risk arising from factors specific to a particular country or sector. The Manager monitors the prices of the money market funds throughout the year and reports to the Board, which meets regularly in order to review investment strategy.

(ii) Currency risk

The functional currency and presentational currency of the Company is sterling. Options over property, loans and other investments are denominated in Euros and the Company is therefore exposed to movements in the exchange rate between the Euro and sterling. The company does not hedge this risk.

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Notes to the financial statements (continued)

Currency rate exposure

An analysis of the Group's currency exposure is detailed below:

	2007		2006	
	Financial investments £	Net monetary assets £	Financial investments £	Net monetary assets £
Sterling	-	11,198,245	-	2,516,844
Euro	30,986,104	1,752,046	37,871,637	1,401,425
Bulgarian Lev	-	72,366	-	5,322
	<u>30,986,104</u>	<u>13,022,657</u>	<u>37,871,637</u>	<u>3,923,591</u>

Foreign currency sensitivity

The table below details the Group's sensitivity to a 5% increase in the value of sterling against the relevant currency. With all other variables held constant, net assets attributable to shareholders and the change in net assets attributable to shareholders per the consolidated income statement would have decreased by the amounts shown below. The analysis is performed on the same basis for 2006.

	2007		2006	
	Profit and loss £	Equity £	Profit and loss £	Equity £
Euro	1,554,152	87,602	1,893,582	70,071
Bulgarian Lev	-	3,618	-	266
	<u>1,554,152</u>	<u>91,220</u>	<u>1,893,582</u>	<u>70,337</u>

A 5% weakening of sterling against the relevant currency would have resulted in an equal and opposite effect on the above financial statement amounts to the amounts shown above, on the basis that all other variables remain constant.

(iii) Interest rate risk

Interest rate movements may affect: (i) the fair value of the investments in fixed interest rate securities, (ii) the level of income receivable on cash deposits, and (iii) interest payable on the company's variable rate borrowings.

The interest rate profile of the Company excluding short term debtors and creditors, as at 31 December 2007 was as follows:

	Weighted average period for which rate is fixed Years	Weighted average interest rate* %	2007	2007	2007
			Fixed rate £	Floating rate £	Non-interest bearing £
Assets					
Euro loans to third parties	2	7.00	6,085,624	4,640,795	7,156,160
Equities	-	-	-	-	13,200,466
Euro cash deposit	-	-	-	1,752,046	-
Bulgarian Lev cash deposit	-	-	-	72,367	-
Sterling cash deposit	-	-	-	52,769	-
			<u>6,085,624</u>	<u>6,517,977</u>	<u>20,356,626</u>

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Notes to the financial statements (continued)

	Weighted average period for which rate is fixed Years	Weighted average interest rate* %	2006 Fixed rate £	2006 Floating rate £	2006 Non-interest bearing £
Assets					
Euro loans to third parties	3	7.00	3,788,377	3,859,396	7,317,645
Equities	-	-	-	-	23,424,780
Euro cash deposit	-	-	-	1,401,425	-
Bulgarian Lev cash deposit	-	-	-	5,322	-
Sterling cash deposit	-	-	-	1,806,730	-
			<u>3,788,377</u>	<u>7,072,873</u>	<u>30,742,425</u>

*The weighted average interest rate is based on the current yield of each asset, weighted by its market value. The weighted average interest rate on bank loans is based on the interest rate payable, weighted by the total value of the loans. This excludes the loan to third parties for the Nikea Park development as the loan is repayable dependant on sales and development.

The floating rate assets consist of cash deposits on call, earning interest at prevailing market rates.

The non-interest bearing assets represent the equity element of the portfolio.

Maturity profile

The following table sets out the carrying amount, by maturity, of the Company's financial instruments that are exposed to interest rate risk:

	Within 1 year £	Within 2 – 3 years £	2007 Within 4 – 5 years £	More than 5 years £	Total £
Fixed rate					
Loans to third parties	-	2,822,768	-	-	2,822,768
	<u>-</u>	<u>2,822,768</u>	<u>-</u>	<u>-</u>	<u>2,822,768</u>
Floating rate					
Loans to third parties	4,640,795	-	-	-	4,640,795
Cash	1,877,182	-	-	-	1,877,182
	<u>6,517,977</u>	<u>-</u>	<u>-</u>	<u>-</u>	<u>6,517,977</u>
Non-interest bearing					
Loans to third parties	7,156,160	-	-	-	7,156,160
Other payables	(283,145)	-	-	-	(283,145)
	<u>6,873,015</u>	<u>-</u>	<u>-</u>	<u>-</u>	<u>6,873,015</u>

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Notes to the financial statements (continued)

	Within 1 year	Within 2 – 3 years	2006 Within 4 – 5 years	More than 5 years	Total
	£	£	£	£	£
Fixed rate					
Loans to third parties	-	912,587	-	-	912,587
	-	912,587	-	-	912,587
Floating rate					
Loans to third parties	-	3,859,396	-	-	3,859,396
Cash	3,213,477	-	-	-	3,213,477
	3,213,477	3,859,396	-	-	7,072,873
Non-interest bearing					
Loans to third parties	-	7,317,645	-	-	7,317,645
Other payables	-	-	-	-	-
	-	7,317,645	-	-	7,317,645

The loan of EUR 3,919,530 to third parties for the Nikea Park development has been excluded from the maturity profile as the loan is repayable dependant on sales and development.

Interest rate sensitivity

An increase of 100 basis points in interest rates during the period would have increased the net assets attributable to shareholders and changes in net assets attributable to shareholders by £37,667 (2006 £35,361). A decrease of 100 basis points would have had an equal but opposite effect.

(iv) Liquidity risk

A significant portion of the Company's assets comprise cash balances and readily realisable securities, which can be sold to meet funding commitments if necessary. As at 31 December 2007 the Company does not have any significant liabilities due.

(v) Credit risk

The Company places funds with third parties and is therefore potentially at risk from the failure of any such third party of which it is a creditor. The Company expects to place any such funds on a short-term basis only and spread these over a number of different providers.

Management has a credit policy in place and the exposure to credit risk is monitored on an ongoing basis.

The Company's principal financial assets are loans and receivables, other receivables, investments and cash and cash equivalents. The maximum exposure of the Group to the credit risk is the carrying amount of each class of financial assets.

Loans and receivables are represented by loans to and receivables from third parties.

Other receivables are represented mainly by prepayments and other debtors where no significant credit risk is recognised.

Investments are represented by holdings in money market funds which are rated AAA and use risk spreading to minimise exposure to any one counterparty.

The Company's credit risk is primarily attributable to loans to and receivables from third parties. Management monitors each loan according to the individual characteristics of each project, including regular contact with developers, site visits and regular reporting by an outsourced real estate consultant to evaluate whether there is any impairment.

With the exception of the loan to Magnolia Holidays EAD, all financial assets of the Company are neither past due nor impaired.

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Notes to the financial statements (continued)

(vi) Credit risk exposure

In summary, compared to the amounts in the Consolidated Balance Sheet, the maximum exposure to credit risk at 31 December 2007 was as follows:

	2007		2006	
	Balance sheet	Maximum exposure	Balance sheet	Maximum exposure
	£	£	£	£
Non-current assets				
Loans and receivables	17,688,697	17,688,697	13,928,296	13,928,296

Magnolia Holidays EAD has defaulted on their loan repayment to the wholly owned subsidiary of the Company, BSPF Magnolia EAD in the amount of EUR 5,488,938 and the interest thereon of EUR 636,050. On 17th January 2008, the lender commenced a court action to force repayment of the defaulted amount in the Plovdiv District Court. That court ruled against the lender, which then appealed to the Plovdiv Regional Court, and the Company currently awaits a decision.

Fair value of financial assets and liabilities

The book value of the cash at bank and loans to third parties included in these financial statements are approximate to their fair value.

Investments held for trading are valued at their fair value, which has been determined with reference to quoted market prices.

15 Post balance sheet events

On 17 of January 2008 BSPF Magnolia EAD, a wholly owned subsidiary of the company, declared the loan provided to Magnolia Holidays EAD in the sum of EUR 5,488,938 and the interest of EUR 636,050 as due and payable.

Magnolia Holidays EAD did not pay any of the amounts claimed by BSPF Magnolia EAD. As a result, on 29 January 2008, BSPF Magnolia EAD registered the enforcement of a share pledge, which is security under the Loan and Guarantee Agreement. The pledge is for 50,000 shares, which is the entire registered share capital of Magnolia Holidays EAD.

On 6 February 2008, Magnolia Holidays EAD filed an application with the Plovdiv Regional Court to suspend the enforcement of the share pledge on the grounds that the claimed amount had not yet become due and payable. The Court granted the application with a ruling on 11 February 2008.

On 20 February 2008 BSPF Magnolia EAD appealed the ruling of the Plovdiv Regional Court. The case has been forwarded to the Plovdiv District Court and awaits decision.

Bulgarian counsel is of the opinion that under the relevant law the appeal is meritorious, but the ultimate outcome of the appeal cannot be assured.

On 10 March 2008 the board of directors decided not to proceed with the completion of Borovetz III. Under the preliminary contract signed with the vendors in May 2007 BSPF Super Borovetz EAD had paid a deposit of EUR 360,720 plus VAT. This amount will be returned to the Company plus a contribution to the costs incurred by the Company.

16 Commitments

The Company has an agreement to advance EUR 5,274,750 to the developer of the site at Obzor. At the period end EUR 3,663,223 of this loan has been advanced.

The Company has also signed an agreement to advance up to EUR 4,678,500 for the development of the site at Kavarna upon the fulfilment of required contractual conditions. No advances have yet been made on this loan.

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Notes to the financial statements (continued)

17 Related party transactions

The Company purchased three options at launch from the Manager. The option over the Obzor development was purchased from the Manager in exchange for 691,563 ordinary shares in the Company. The two remaining options over the sites at Kavarna and Shabla have been assigned to the Company.

Consideration of 1,037,344 ordinary shares in the Company will be issued to the Manager contingent upon final construction permits being granted in respect of the sites at Kavarna and Shabla. At the year end, final construction permits had not been issued on either site and therefore no value has been ascribed to the options..

Information regarding subsidiaries and subsidiary loans can be found in notes 6(e) and 9.

The management fees incurred for the year are disclosed in note 2. As at 31 December 2007 there were no unpaid amounts.

18 Directors interests

Total compensation to the Directors over the period was £101,525.

Mr. W. Roger King holds 50,000 Ordinary shares in the Company.

Mr Angelo Moskov is a partner of QVT Managed Funds, which control or have a beneficial interest in 75,091,775 ordinary shares in the Company.

19 Fund domicile

The Black Sea Property Fund Limited is a company domiciled in Jersey, Channel Islands.

THE BLACK SEA PROPERTY FUND LIMITED

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Corporate information

Registered office	Manager and promoter	Strategic Adviser
BNP House Anley Street St Helier Jersey CI JE2 3QE	Development Capital Management (Jersey) Limited BNP House Anley Street St Helier Jersey CI JE2 3QE	Colliers International Business Park Sofia Mladost 4 Build 13B 1715 Sofia Bulgaria
Property Investment Adviser	Nominated Advisor and Broker	Auditors to the Company
Development Capital Management (Bulgaria) EAD 14 Tzar Osvoboditel Boulevard Sofia 1000 Bulgaria	Numis Securities Limited The London Stock Exchange Building 10 Paternoster Square London EC4M 7LT	KPMG Channel Islands Limited PO Box 453 5 St Andrew's Place St Helier Jersey CI JE4 8WQ
Custodian	Administrator and Secretary	Registrar
BNP Paribas (Jersey Branch) BNP House Anley Street St Helier Jersey CI JE2 3QE	BNP Paribas Fund Services Jersey Limited BNP House Anley Street St Helier Jersey CI JE2 3QE	Capita IRG (Offshore) Limited 12 Castle Street St Helier Jersey CI JE2 3RT
Legal Adviser (Jersey)	Legal Adviser (United Kingdom)	
Ozannes Advocates PO Box 733 29 Esplanade St Helier Jersey CI JE4 0ZS	Stephenson Harwood One, St Paul's Churchyard London EC4M 8SH United Kingdom	