EAST AFRICAN DEVELOPMENT BANK

ANNUAL REPORT 2018

Your partner in development

ANNUAL REPORT 2018

CORPORATE PROFILE OF EADB

REGISTERED OFFICE AND PRINCIPAL PLACE OF BUSINESS

Uganda (Headquarters)

Plot 4 Nile Avenue
EADB Building
P. O. Box 7128
Kampala, Uganda

Kenya

Country office,
Kenya
7th Floor, The Oval
Office, Ring Road,
Parklands Westland
P.O. Box 47685,
Nairobi

Rwanda

Ground Floor,
Glory House Kacyiru
P.O. Box 6225,
Kigali Rwanda

Tanzania

349 Lugalo/ Urambo
Street Upanga
P.O. Box 9401
Dar es Salaam,
Tanzania

BANKERS

Uganda (Headquarters)
Standard Chartered –London
Standard Chartered – New York
Standard Chartered - Frankfurt
Citibank – London
Citibank – New York
Kenya
Standard Chartered
Rwanda
Bank of Kigali
Tanzania
Standard Chartered

AUDITOR

PricewaterhouseCoopers
Certified Public Accountants,
10th Floor Communications House,
1 Colville Street,
P.O. Box 882
Kampala, Uganda

ESTABLISHMENT

The East African Development Bank (EADB) was established in 1967

SHAREHOLDING

The shareholders of the EADB are Kenya, Uganda, Tanzania and Rwanda. Other shareholders include the African Development Bank (AfDB), the Netherlands Development Finance Company (FMO), German Investment and Development Company (DEG), SBIC-Africa Holdings, Commercial Bank of Africa, Nairobi, Nordea Bank of Sweden, Standard Chartered Bank, London, Barclays Bank Plc., London and Consortium of former Yugoslav Institutions.

MISSION

To promote sustainable socio-economic development in East Africa by providing development finance, support and advisory services.

VISION

To be the partner of choice in promoting sustainable socio-economic development.

OUR CORE VALUES

- Service
- Integrity
- Leadership
- Innovation
- Team Work

FOCUS AREAS 2016-2020

- Food Security
- Infrastructure
- Skills Development
- Climate Change
- Regional Integration

CONTENTS

LIST OF FIGURES

LIST OF TABLES

ABBREVIATIONS AND ACRONYMS

ADF	African Development Fund
AfDB	African Development Bank
ALCO	Assets and Liabilities Committee
BADEA	Arab Bank for Economic Development in Africa
BIF	Burundian Franc
CDM	Clean Development Mechanism
DEG	German Investment and Development Company
EA	East Africa
EACDF	East African Community Development Fund
EU	European Union
EUR	Euro
FDI	Foreign Direct Investment
FMO	The Netherlands Development Finance Company
GDP	Gross Domestic Product
IAS	International Accounting Standards
IASB	International Accounting Standards Board
IFC	International Finance Corporation
IFRIC	International Financial Reporting Interpretations Committee
IFRS	International Financial Reporting System
IRENA	International Renewable Energy Agency
IUCEA	Inter-University Council for East Africa
KES	Kenyan Shilling
KfW	Kreditanstalt für Wiederaufbau
ODA	Overseas Development Assistance
OPEC	Organization of the Petroleum Exporting Countries
PWC	PricewaterhouseCoopers
RCC	Regional Collaboration Centre (UNFCCC)
RWF	Rwandan Franc
SBIC-Africa	Standard Bank Investment Corporation -Africa
SIDA	Swedish International Development Cooperation
SMEs	Small and Medium Enterprises
TZS	Tanzanian Shilling
UNFCCC	United Nations Framework Convention on Climate Change
UGX	Ugandan Shilling
USA	United States of America
USD	United States Dollar
VAT	Value Added Tax
WEO	World Economic Outlook

LETTER OF TRANSMITTAL

The Honourable Minister for Finance, Planning and Economic Development

The Republic of Uganda

The Cabinet Secretary, the National Treasury

The Republic of Kenya

The Honourable Minister for Finance and Planning

The United Republic of Tanzania

The Honourable Minister for Finance and Economic Planning

The Republic of Rwanda

In accordance with Articles 26 and 35 of the Charter for the East African Development Bank (the "Bank"), the Board of Directors herewith submits to the Honourable Members of the Governing Council and to the Members of the Bank, the Annual Report of the Bank for the period 1st January to 31st December 2018.

This Report describes the activities of the Bank during the year and shows the Bank's financial position as at 31st December 2018. The Report also presents a summary of the economic performance of the Member States of the EADB.

Honourable Members of the Governing Council, please accept the assurances of my highest consideration and esteem.

Mr. Keith Muhakanizi

CHAIRPERSON

BOARD OF DIRECTORS

GOVERNING COUNCIL

Hon. Matia Kasaija

(Chairperson)

Minister for Finance, Planning and Economic Development, Republic of Uganda

Hon. Dr. Philip Mpango

Minister for Finance and Planning, United Republic of Tanzania

Hon. (Amb.) Ukur Yatani

Cabinet Secretary, National Treasury, Republic of Kenya

Dr. Uzziel Ndagijimana

Minister for Finance and Economic Planning, Republic of Rwanda

BOARD OF DIRECTORS

Keith Muhakanizi

Permanent Secretary, Secretary to the Treasury, Ministry of Finance, Planning and Economic Development, Republic of Uganda - **Chairperson**

Dr. Julius Monzi Muia

Principal Secretary, the National Treasury, Republic of Kenya - **Member**

James Doto

Permanent Secretary, Pay Master General, Ministry of Finance and Planning, United Republic of Tanzania - **Member**

Caleb Rwamuganza

Permanent Secretary, Secretary to the Treasury, Ministry of Finance and Economic Planning, Republic of Rwanda - **Member**

Francis N. Karuiru

Private sector representative, Republic of Kenya - **Member**

Khadija I. Simba

Private sector representative, United Republic of Tanzania - **Member**

BOARD OF DIRECTORS

Dr. Mukhtar Abdu Sarkinbai

African Development Bank Representative -
Member

Mbundu Faustin

Private sector representative, Republic of Rwanda -
Member

James Tumusiime

Private sector representative, Republic of Uganda -
Member

Vivienne Yeda

Director General

STATEMENT BY THE CHAIRPERSON OF THE BOARD OF DIRECTORS

On behalf of the Board of Directors, I am delighted to present the Bank's Annual Report and financial statements for the year ended 31 December 2018.

EADB continued to perform well in 2018, posting a net profit of USD 6.5 million. We were ranked the second Best Performing DFI by the Association of African Development Finance Institutions (AADFI) and rated Investment Grade Baa3 with a stable outlook by Moody's Investors Service.

During the year, EADB has continued to attract funding from development partners and formally launched a new USD 6 million facility supported by KfW to finance projects that promote biodiversity conservation in Uganda.

EADB is continuing to implement its 2016-2020 Strategic Plan and is committed to its key focus sectors: food security, climate change, regional integration, skills development and infrastructure. Our commitment to the focus areas is evidenced by two large agricultural programmes that support smallholder farmers in Kenya and Uganda, our commitment to carbon neutrality, the scaling up of our corporate social investment programmes in the education and health sectors and a number of large regional infrastructure projects .

$ 6.5 million

Net profit in 2018

On behalf of the Board of Directors, I wish to recognize the contributions made by all stakeholders towards the Bank's successful performance. We appreciate our clients, shareholders, development partners and funders for the continued support. I also wish to appreciate my fellow Directors for their leadership of the Bank. I also wish to take this opportunity to congratulate the Management and Staff of the Bank for yet another year of good performance.

Mr. Keith Muhakanizi
Chairperson, Board of Directors

STATEMENT BY THE DIRECTOR GENERAL

EADB FINANCED
1,855 SMEs

Creating
15,841
permanent
and temporary jobs

TRAINED
448 Doctors
in oncology and neurology
since 2016

CELEBRATED
50 Years

$ 6.5 million
Net Profit

In 2018, EADB is proud to have increased its development contribution to its Member States. Whilst we have continued to support corporates, we have particularly increased our support to the small and medium enterprises (SMEs) sector, which is a new operational area for the Bank, and which is considerably underfinanced.

EADB has three (3) successful programmes that offer affordable financing to SMEs in an attempt to boost local value chains and improve the socio-economic wellbeing of communities. In Uganda, the Bank has financed 1,855 SMEs, which are estimated to have contributed to the creation or sustenance of 15,841 permanent and temporary jobs, of which over a third are female jobs. Whilst more needs to be done to promote gender equality, our intervention to promote female-orientated access to finance has contributed towards female job creation in a very male dominated environment.

Our Medical Training and Fellowship Programme has trained 448 doctors across East Africa in the fields of oncology and neurology since 2016. Consequently, we are likely to exceed our target of training 600 doctors by 2020. We supported a record intake under our STEM Scholarship of eight (8) scholars in the 2018 intake and continue to support the returning scholars to implement beneficial initiatives in the education sector, such as training in interactive teaching methods for other teachers and local communities.

We have also strengthened our pledge to support mitigation and adaptation measures against climate change throughout the region. We host the UNFCCC's Regional Collaboration Centre for Eastern and Southern Africa and collaborate with them to support Clean Development Mechanism (CDM) projects in our Member States, including cook stove projects in Kenya and Rwanda, a wind power project in Kenya and a hydropower plant in Uganda. In 2018, EADB is proud to have committed to carbon neutrality, and will strive to reduce our carbon emissions and offset the remaining emissions through purchasing carbon emission reductions from projects in the region.

We concluded the year celebrating our 50 years of operation, posting a very healthy profit of USD 6.5 million and hosting a strategic workshop to develop a strategy to support the next generation in 2068. We look forward to continuing to serve the region to deliver our goals for the next generation.

Vivienne Yeda,
Director General

ECONOMIC REVIEW

1.1 RECENT PERFORMANCE

1.1.1 ECONOMIC GROWTH

Global Macroeconomic and Financial Environment

Global growth slowed in 2018, from 3.8% in 2017 to 3.6% in 2018, driven by slowing growth in advanced economies. The risks to global growth emanate from a lesser global output gap and the removal of expansionary monetary policies.

<<< Global growth slowed in 2018

2017
3.8%

3.6%
2018

China, the world's second-biggest economy grew by 6.6% in 2018, representing roughly a third of the total global expansion. China's growth is now forecast to remain stronger than initially anticipated, but will slow down gradually over the forecast period, partly on account of US tariffs imposed on approximately USD 200 billion worth of Chinese exports.

Progress in per capita income growth will be uneven across emerging market and developing economies, and generally insufficient to tackle extreme poverty in Sub-Saharan Africa. The outlook is subject to significant risks, including the possibility of disorderly financial market movements, escalating trade protectionism, heightened policy uncertainty, and rising geopolitical tensions.

Table 1: Real economic activity

	Outturns		Projections	
	2017	2018	2019	2020
World Output	3.8	3.6	3.3	3.6
Advanced Economies	2.4	2.2	1.8	1.7
Emerging Market and Developing Economies	4.8	4.5	4.4	4.8
Middle East, North Africa, Afghanistan, and Pakistan	2.2	1.8	1.5	3.2
Sub-Saharan Africa	2.9	3.0	3.5	3.7
East African Community	2.9	4.4	6.1	5.5
Burundi	0.0	0.1	0.4	0.5
Kenya	4.9	6.0	5.8	5.9
Rwanda	6.2	8.6	7.8	8.1
South Sudan	-5.5	-1.2	8.8	5.2
Tanzania	7.1	7.0	7.3	7.0
Uganda	5.0	6.2	6.3	6.2

Source: IMF World Economic Outlook, April 2019 and the Ministry of Finance and Planning Tanzania

Economic Growth in Advanced Economies

According to the IMF World Economic Update, April 2019, real economic activity in advanced economies declined from 2.4% in 2017 to 2.2% in 2018, and is expected to decline further to 1.8% in 2019 and 1.7% in 2020. US trade policy is expected to adversely affect US growth looking forward, whilst elsewhere narrowing output gaps and tightening monetary policies are expected to reduce growth back to its potential.

>>> Emerging economies grew faster in 2018

2020
4.8%

4.5%
2018

4.4%
2019

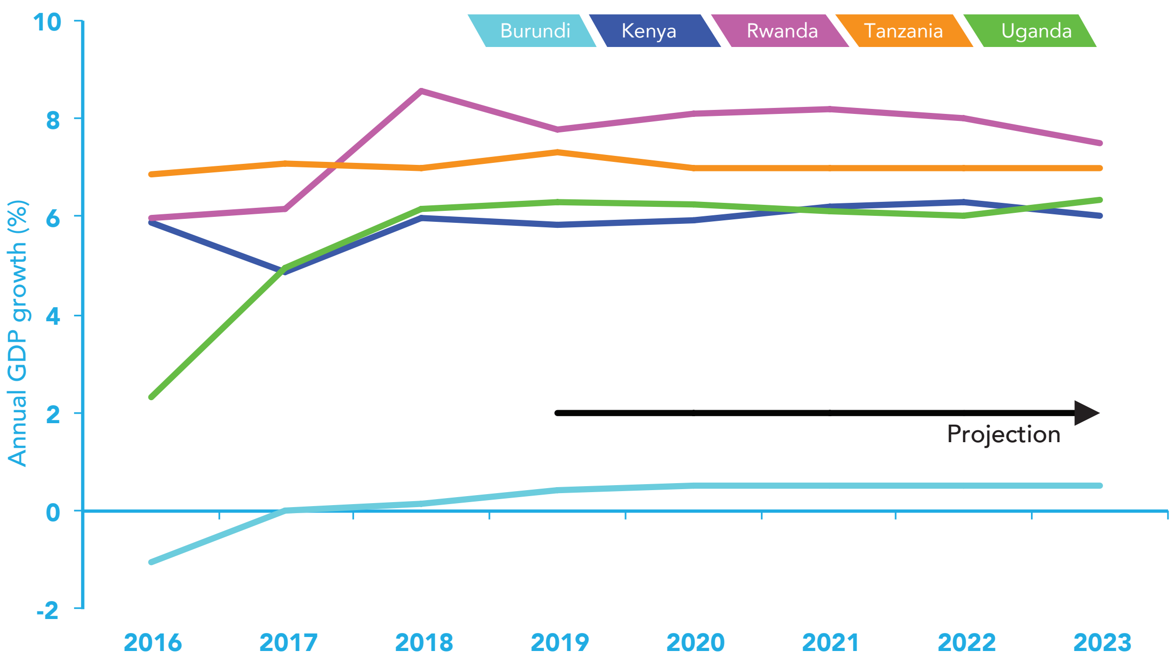
Economic Growth in Developing Economies

Emerging economies grew faster than the rest of the world in 2018, expanding by 4.5%, and are expected to continue to do so over the medium-term: by 4.4% in 2019 and 4.8% in 2020. Energy exporters have a more positive outlook under slightly higher global oil prices, but geopolitical tensions will constrain potential growth in other countries. As aforementioned, China will continue to perform well, but will be held back by US trade restraints.

Economic Growth in East Africa

Average economic growth in East Africa (excluding Burundi and South Sudan) improved from 5.8% in 2017 to 6.9% in 2018, which was reflected across all East African countries.

Figure 1: Economic growth in EAC



Source: IMF World Economic Outlook, April 2019 and the Ministry of Finance and Planning Tanzania

+0.1%

Burundi:

The Burundi economy grew by 0.1% in 2018, which marks the first year of positive growth since 2015. The economy levelled out in 2017 and began to grow in 2018, but growth was driven more as a result of its low base than from improved economic fundamentals.

+1.1%

Kenya:

Economic growth expanded from 4.9% in 2017 to 6.0% in 2018, driven largely by the services sector and also due to political calmness following the 2017 elections. Consumer demand was affected in the second half of 2018 by tax rises in the 2018/19 budget.

+2.4%

Rwanda:

Rwanda fared well in 2017, due to the rapidly growing construction sector, and continued to grow in 2018, driven again by the construction and services sectors. Rwandan GDP growth increased from 6.2% in 2017 to 8.6% in 2018. In particular, government infrastructure investments have maintained buoyant economic growth and are likely to continue to do so over the medium-term as the government implements Vision 2020.

-1.2%
from -5.5%

South Sudan:

The economy of South Sudan was boosted by a slight improvement in global oil prices and better climatic conditions (although harvests are disrupted by conflict), causing the extent of the depression to lessen in 2018. GDP growth has improved from minus 5.5% in 2017 to minus 1.2% in 2018.

-0.1%

Tanzania:

The National Bureau of Statistics rebased Tanzania's national accounts in 2018, which caused a 4% increase in the size of the economy. Economic growth fell slightly to 7.0% in 2018, from 7.1% in 2017, yet this still depicts strong economic growth.

+1.2%

Uganda:

Uganda's economy has continued to recover from the severe drought experienced in 2016, which caused GDP growth to fall to 2.3%. In 2018, the economy grew by 6.2% (from 5.0% in 2017), driven by the services sector. Industrial growth was supported by robust construction activity and on-going public infrastructure projects as well as an expansion in mining (particularly gold production at the African Gold Refinery in central Uganda). Meanwhile, services expansion was spurred by on-going investment and upgrades in the information and communications technology (ICT) sector. Financial services also emerged as a driver of services growth, with the subsector benefitting from increased credit activity in a relatively low interest-rate environment.

1.1.2 PRICES AND MONETARY POLICY

INFLATION

Burundi	2017 **16.6%** to **12.7%** 2018 ▼
Kenya	Reached **8%** ▲ **4.7%** 2018 ▼
Rwanda	2017 **4.9%** to **1.4%** 2018 ▼
South Sudan	**104%** ▲ 2nd highest to Venezuela in the world
Tanzania	2017 **5.3%** to **3.5%** 2018 ▼
Uganda	**2.6%** ▼ Average

Burundi:

Inflation picked up in 2017 as a foreign exchange shortage hit Burundi, causing the exchange rate to depreciate and ultimately affecting inflation. Inflation fell slightly in 2018, from 16.6% in 2017 to 12.7%, yet remained elevated as the above fundamentals persisted.

Kenya:

In 2017, inflation reached 8% and exceeded the Central Bank of Kenya's inflation target of 5% +/- 2.5%. However, inflation has fallen back within the CBK's target range in 2018 to 4.7%.

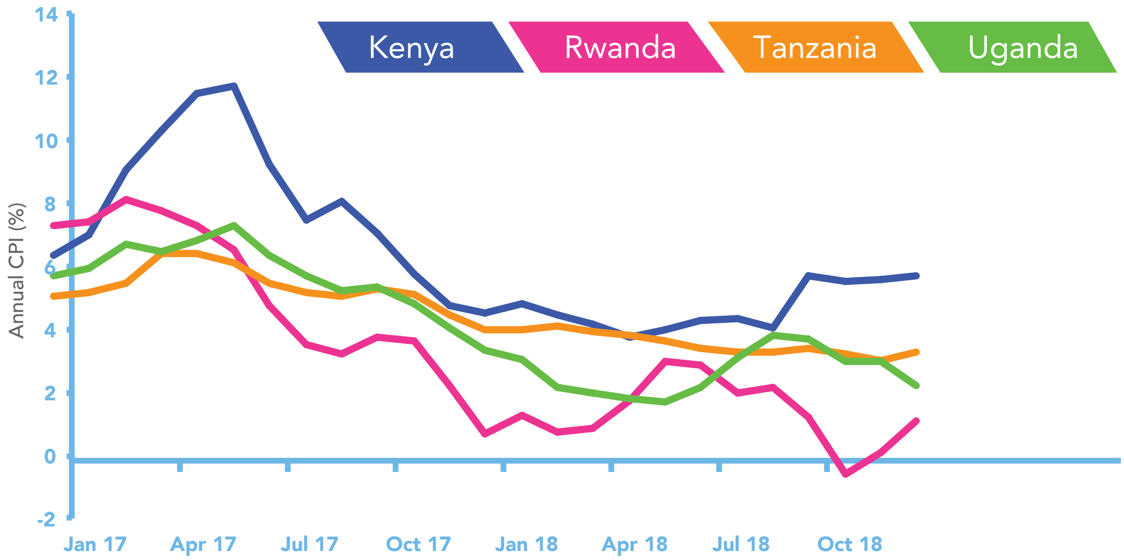
Rwanda:

Inflation fell dramatically below the National Bank of Rwanda's 5% policy target in 2018, driven by improved harvests (in turn driven by better weather conditions) and a more stable exchange rate. Rwandan inflation fell from 4.9% in 2017 to 1.4% in 2018.

South Sudan:

Inflation peaked in South Sudan at 836% in October 2016 and has fallen since, yet remained elevated throughout 2017 and 2018. In 2018, South Sudan's inflation was the second highest in the world (to Venezuela) at 104%, driven by the on-going conflict and the rapid depreciation of the South Sudanese Pound.

Figure 2: Annual headline inflation in EAC



Source: National Central Banks and Statistics Bureaus

Tanzania:

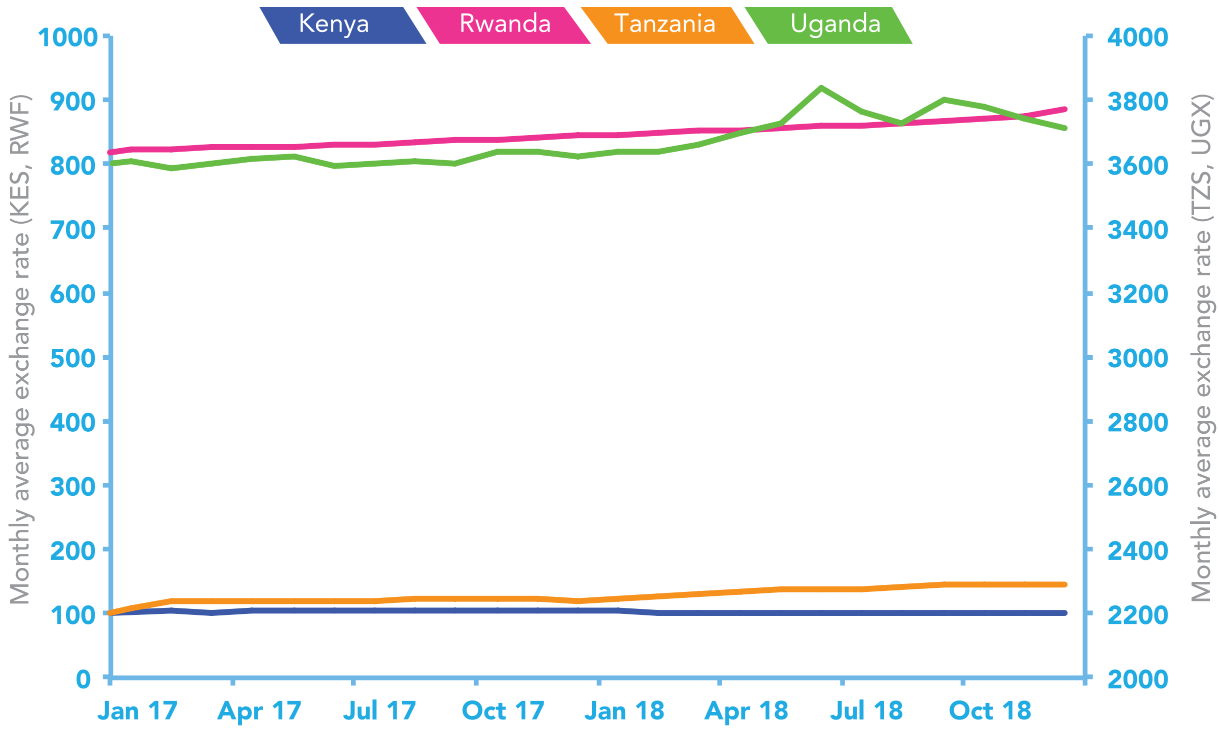
Inflation fell from 5.3% in 2017 to 3.5% in 2018 as food prices remained low and global oil prices fell. Inflation fell steadily throughout 2018, from 4.0% in January to 3.3% in December, driven by falling oil prices that the Energy and Water Utilities Regulatory Authority (EWURA) passed on to consumers.

Uganda:

Inflation fell significantly below the Bank of Uganda's 5% inflation target in 2018, to average 2.6%, compared to 5.7% in 2017. As with the rest of the region, subdued price pressures were driven by low food and fuel prices. The Bank of Uganda increased the Central Bank Rate in October 2018 in response to anticipated inflationary pressures in 2019.

Exchange Rates

Figure 3: Monthly average exchange rates



Source: National Central Banks and Statistics Bureaus

Burundi:

The Burundian Franc depreciated by 3.1% in 2018 to an average of BIF/USD 1783 over the year. The relative exchange rate stability is mainly due to an improved economic environment and Government controls on foreign currency.

Kenya:

The Kenyan Shilling appreciated by 2.0% in 2018, reversing its 1.9% depreciation in 2017. The Kenyan Shilling frequently demonstrates more stability than other East African currencies; in 2018, slowing expectations of the expected monetary contraction by the US Federal Reserve supported the appreciation.

Rwanda:

The Rwandan Franc depreciated by 3.6% in 2018, less than the 5.6% in 2017, also supported by US monetary policy and a Government focus to reduce the current account deficit.

Tanzania:

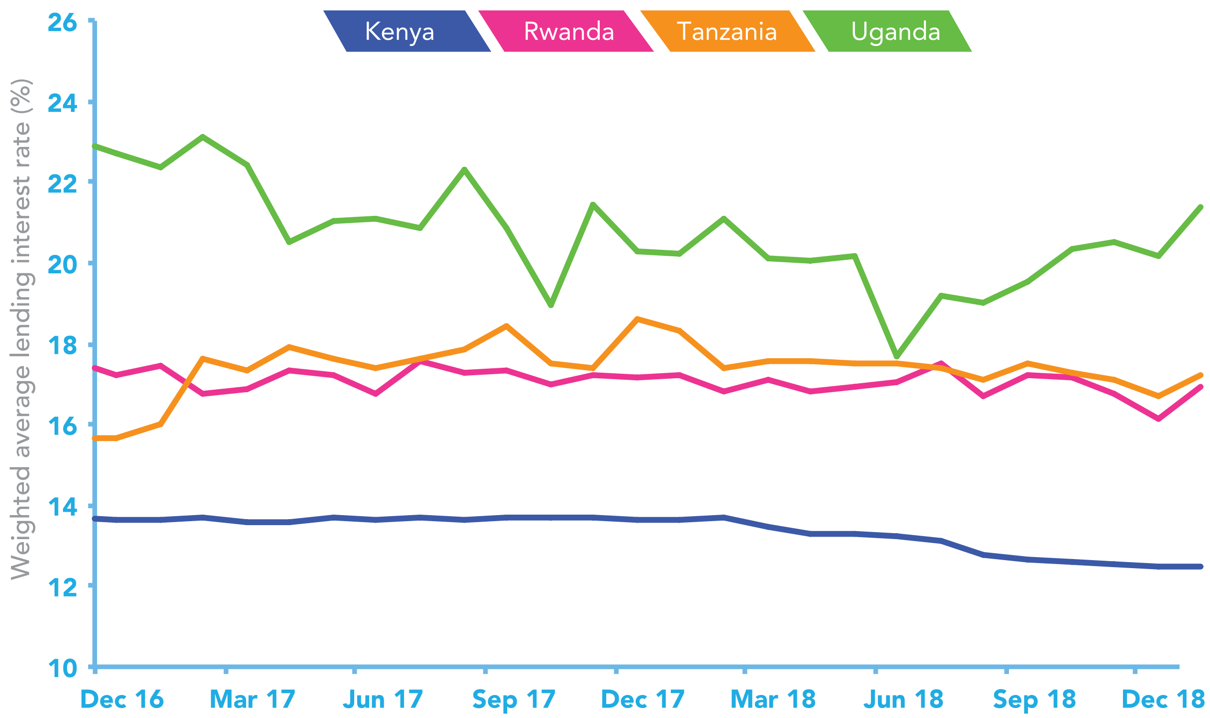
The Tanzanian Shilling's pace of depreciation also slowed in 2018, to 1.6% from 2.4% in 2017, despite a fall in exports over the year. The Central Bank's closure of many foreign exchange bureaus appears to have increased confidence in financial sector stability, which will also benefit the exchange rate.

Uganda:

Although the Ugandan Shilling demonstrated more volatility than its peers, it depreciated at a slower pace in 2018 with the rest of the region. The Ugandan Shilling depreciated by 3.2% in 2018, compared to 5.6% in 2017, supported by growing exports and stronger consumer demand.

Interest Rates

Figure 4: Weighted average commercial bank lending interest rates



Source: National Central Banks

Kenya:

Commercial banks weighted average lending rates fell steadily throughout 2018, from 13.7% in January 2018 to 12.6% by December 2018 (to average 13.1% in 2018, compared to 13.7% in 2017), driven by the enforced interest rate cap, which caps lending rates at 4 percentage points above the Central Bank Rate. The cap also slowed growth in financial services throughout 2018, although bank performance did show signs of improvement over the year in terms of falling NPLs and some recovery in private sector credit growth.

Rwanda:

Commercial banks weighted average lending rates were largely stable in Rwanda, falling slightly from 17.2% in 2017 to 17.0% in 2018. The National Bank of Rwanda has also announced a significant growth in new authorised loans over 2018, supported by the growing economy and falling NPLs.

Tanzania:

Weighted average lending rates have largely remained stable in 2018 compared to 2017, falling from 17.6% in 2017 to 17.4% in 2018. However over the course of 2018 they have fallen steadily from 18.3% in January 2018 to 16.7% in December 2018, which has also supported private sector credit growth.

Uganda:

Weighted average lending rates fell from 21.3% in 2017 to 19.8% in 2018, supported by accommodative monetary policy. Overall, the financial sector emerged as a key driver of economic growth in 2018, benefitting from increased credit activity under the relatively low interest rate environment and rising profitability.

BOX 1: FOOD SECURITY

1

East Africa's population is estimated at around **160million** People growing at an average of **2.5%** p.a

2

The majority of the people in East Africa are still largely dependent on rain-fed agriculture and subsistence farming.

3

EADB contributes to East Africa's quest for food security by supporting programmes and practices that enhance agricultural productivity...

EADB gave **Ushs 20b** through Centenary Rural Development Bank

Centenary Rural Development Bank distributed **1,562 Loans** to agricultural SMEs

the Loan is estimated to create over **3,536** permanent Jobs | over **6,061** Temporary Jobs

will benefit over **59,853 SMEs** working along the agricultural value chain

The population of East Africa is estimated at around 160 million and is estimated to be growing at an average of 2.5% per annum. This relatively high growth rate coupled with increasing urbanisation is straining the available resources for productive agriculture and, in particular, resources to meet the aggregate food requirements at the household level.

Households need to be enabled to acquire enough food either through production, exchange or transfer in order to meet the nutritional needs on a consistent basis. Addressing issues of crop failure, seasonality of production and nutritional insufficiency is therefore as important as value addition to agricultural output in view of diminishing fertility of soils.

The relationship between agricultural productivity, hunger, poverty and sustainable development has long been established. The majority of the people in East Africa are still largely dependent on rain-fed agriculture and subsistence farming. Malnutrition and food insufficiency are known to be higher in this kind of populations.

EADB contributes to East Africa's quest for food security by supporting programmes and practices that enhance agricultural productivity, conserve soil fertility, reduce post-harvest losses, improve nutritional values and ensure market access for both primary and secondary agricultural products. The Agri-Finance Enhancement Programme offers lines of credit to commercial banks to on-lend at favourable conditions to SMEs operating throughout the agricultural value chain.

By the close of 2018, EADB had given UGX 20 billion to Centenary Rural Development Bank, which had been redistributed in 1,562 loans to agricultural SMEs across the value chain, including production, marketing, animal breeding and more. EADB estimates that the loan to Centenary Rural Development Bank will create over 3,536 permanent jobs, over 6,061 temporary jobs, over 2,610 female jobs and will benefit over 59,852 SMEs working along the agricultural value chain.

Francis Kateiguta's dairy farm, Kabale

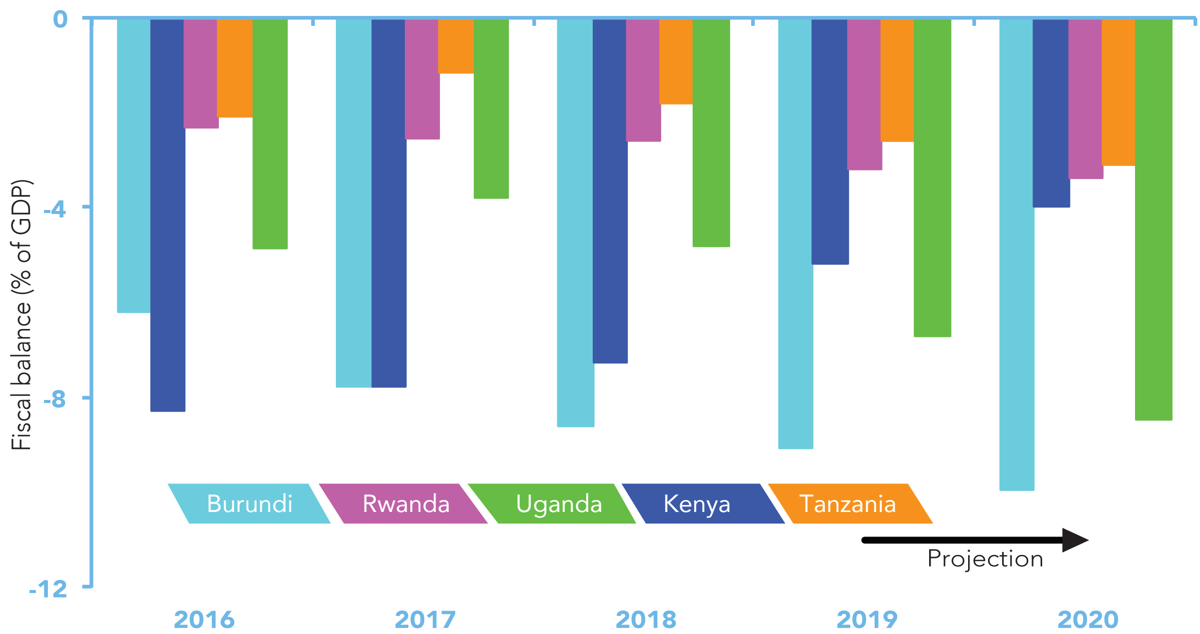
James Byambwenu's banana plantation, Ntungamo

1.1.3 FISCAL SUSTAINABILITY

All East African Countries have a persistent fiscal deficits, which continued in 2018 (with the exception of South Sudan, whose fiscal balance is more volatile). While Kenya reported a narrowing fiscal deficit in 2018, all other East African countries experienced widening fiscal deficits.

Figure 5 displays the fiscal deficit of each East African economy from 2016 and provides projections to 2020.

Figure 5: Fiscal balance (% of GDP)



Source: IMF World Economic Update, April 2019

Burundi:

Burundi's fiscal balance fell further to demonstrate the largest deficit in East Africa in 2018 at minus 8.6%. The effect of donor aid withdrawals and a weak economy continued to adversely affect government revenue, which shows little sign of recovering over the medium-term.

Kenya:

The current fiscal deficit poses a large risk for Kenya, and consequently the government targets to reduce the deficit to 3% of GDP. Indeed, by reducing both recurring expenditures and targeting higher revenue collections, the Kenya government reduced the fiscal deficit from 7.8% of GDP in 2017 to 7.3% of GDP in 2018, and is expected to reduce it further over the medium-term.

Rwanda:

Rwanda's fiscal deficit remained low in 2018, and positively is concentrated on investment expenditure rather than a public service wage bill. Rwanda's fiscal deficit widened slightly in 2018, from minus 2.5% in 2017 to minus 2.6%. The Rwanda Revenue Authority widened its tax base to increase revenue collections, but, although disciplined, expenditure increased marginally.

South Sudan:

South Sudan's fiscal balance has improved in 2017 and 2018, to 3.9% and minus 1.0% respectively, compared to its sizeable deterioration in 2015 and 2016. A reduction in central bank reserves to finance government expenditure and an inability to borrow from international sources, combined with an inflow of donor support, drove the mostly positive fiscal balance. Nonetheless, the fiscal deficit is expected to return over the medium-term.

Tanzania:

Tanzania demonstrated the most healthy fiscal deficit in East Africa in 2018, supported by government efforts to contain recurrent expenditure, reduce tax evasion and improve revenue administration. Tanzania's fiscal balance fell slightly in 2018, from minus 1.2% in 2017, to minus 1.8%. However, the fiscal deficit remains low and the marginal fall in the fiscal balance has been driven by public infrastructure investments, which should boost economic growth over the medium-term.

Uganda:

Uganda's fiscal balance fell from minus 3.8% in 2017 to minus 4.8% in 2018 as the government invested heavily in infrastructure projects. The Uganda Revenue Authority has attempted to increase tax collection and widen the tax base, yet Ugandan tax to GDP remains amongst the lowest in East Africa. The fiscal deficit has been primarily funded by domestic debt, which remains sustainable over the medium-term.

1.1.4 EXTERNAL SECTOR AND TRADE IN EAST AFRICA

The whole of East Africa remained in a current account deficit in 2018, largely driven by sizeable trade deficits and reduced aid inflows. The current account deficit only improved in Kenya, whilst in the remainder of East Africa, current account deficits deteriorated in 2018.

Figure 6 displays the current account deficit of each East African economy from 2016 and provides projections to 2020.

Burundi:

In 2017, Burundi's current account deficit overtook that of Rwanda's to become the largest (as a proportion of GDP) in East Africa, a trend that continued into 2018. Burundi's current account balance decreased from minus 12.3% in 2017 to minus 13.4% in 2018, exacerbated by the suspension of aid from many donors and falling prices for tea and coffee, which constitute a significant amount of Burundi's export basket.

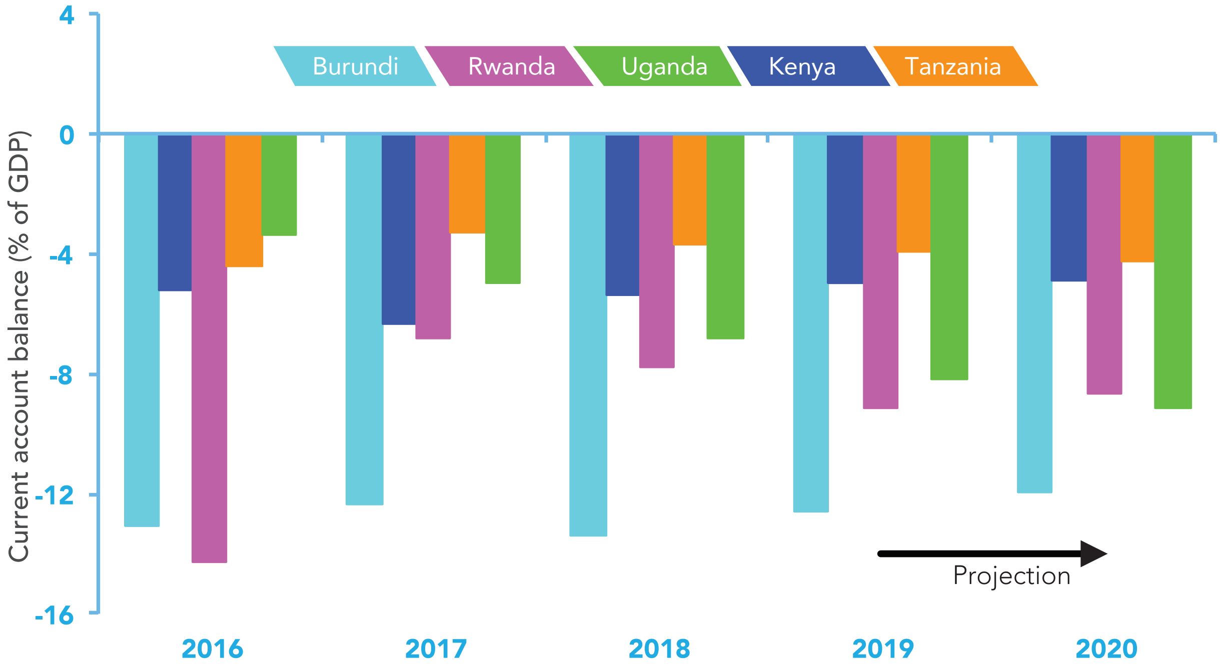
Kenya:

Kenya's current account deficit increased in 2017 due to increased food imports, caused by drought, and increased oil prices. However in 2018, the return to normal weather conditions reduced food imports and increased agricultural (food and horticulture) exports. In addition, lesser imports for large public sector investments, such as the standard gauge railway, reduced the import bill and benefited the current account deficit. Consequently, Kenya's current account balance improved from minus 6.3% in 2017 to minus 5.4% in 2018.

Uganda:

As throughout much of East Africa, Uganda experienced an improvement in agricultural exports in 2018 following the drought that affected the agricultural sector in 2016 and 2017, but the government ramped up its public sector infrastructure investments in anticipation of oil production in 2020, which increased the current account deficit. Consequently, Uganda's current account balance worsened in 2018, from minus 5.0% of GDP in 2017 to minus 6.8% of GDP in 2018.

Figure 6: Current account balance (% of GDP)



Source: IMF World Economic Update, April 2019

Rwanda:

Following a sharp improvement in the current account balance in 2017, Rwanda's current account balance deteriorated in 2018, yet remains healthier than in the years prior to 2017. Rwanda has made concerted efforts to diversify its export base and to reduce imports through the 'Made in Rwanda' import substitution campaign, which should better protect Rwanda's current account balance against external price shocks looking forward. However, a combination of falling tea and coffee prices (Rwanda's main exports) and rising oil prices (a significant import) contributed to a deterioration in the current account balance in 2018, from minus 6.8% in 2017 to minus 7.8% in 2018.

South Sudan:

South Sudan's current account balance is a little more volatile than its neighbours. The current account balance was (just) positive in 2016, yet turned negative in 2017 and 2018 as oil production crashed, causing a current account deficit of 6.6% in 2017 and 12.5% of GDP in 2018. A lack of government revenue has prevented a wider current account deficit through stemming imports.

Tanzania:

Despite rising exports in 2018, Tanzania's imports grew by a faster rate to cause the current account balance to fall slightly from minus 3.3% of GDP in 2017 to minus 3.7% of GDP in 2018. Agricultural exports increased under better climatic conditions, whilst gold production and exports also grew, although a ban on mineral concentrates constrained some export growth. However, imports grew by a much larger degree to support sizeable public sector infrastructure investments. Nonetheless, Tanzania had the smallest current account deficit in East Africa in 2018.

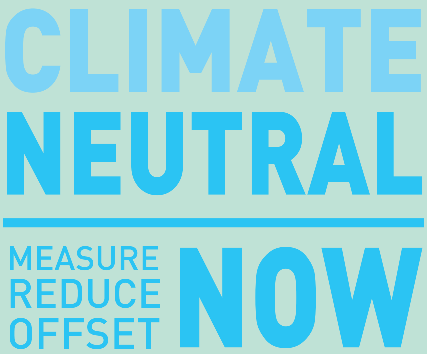
Box 2: Climate change

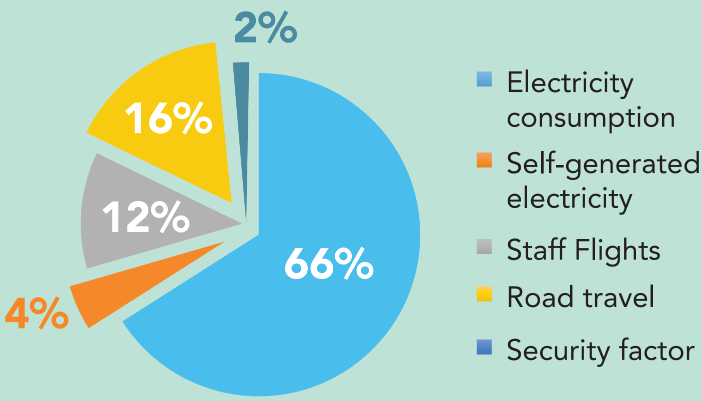
Climate change is now recognised as one of the biggest challenges to socio-economic development. The attendant changes in weather patterns and unpredictable floods and droughts pose a challenge to planning for the Member States of the Bank. Indeed, all East African countries are dependent on climate-sensitive economic sectors, such as agriculture, for output and income generation. Further, due to their low level of development, they are less resilient to negative effects of climate change.

Therefore, it is important that all development actors within the East African region promote a drive to a low carbon economy or green growth through promotion of actions for adaptation and/ or mitigation of climate change. This will require promotion of climate friendly products, markets, technologies, investments, and consumption behaviour.

In 2018, EADB committed to carbon neutrality: to achieve zero net carbon emissions.
The Bank will achieve this through a two-pronged approach. Firstly, the Bank has identified that 66% of EADB's carbon emissions originate from electricity consumption, and therefore it will investigate ways to reduce our electricity consumption or switch to renewable energy in 2019.

EADB's carbon emissions





Secondly, all of the Bank's remaining carbon emissions will be offset by purchasing UN certified Carbon Emission Reductions (CERs). The Bank has tried to invest in projects from all of our Member States, where available, and plan to buy CERs from the Kenya Cook Stove Project, the DelAgua Health "Tubeho Neza" Programme in Rwanda and Bujagali Hydropower Project in Uganda.

The Kenya Cook Stove Project provides fuel-efficient cook stoves to families throughout Kenya. These new brick stoves replace the inefficient "three stone fires" and are provided to the communities free of charge. The stoves halve the wood fuel use and on average prevents three tonnes of CO2 from being emitted each year. This carbon saving is further boosted by the reduction of local deforestation, due to the reduced demand for firewood.

The DelAgua Health "Tubeho Neza" Programme in Rwanda was initiated in 2012 by DelAgua Health, a social enterprise, and the Rwanda Ministry of Health (MOH). The programme intends to distribute 600,000 water filters and 600,000 cook stoves to the poorest 25% of families in Rwanda. Preliminary results suggest that after 2 years, Phase 1 of the programme achieved 46% reduction in diarrhoea in children under 5, 73% reduction in household air pollution for families cooking outdoors and 27.7% reduction in cook stove emission exposure among children.

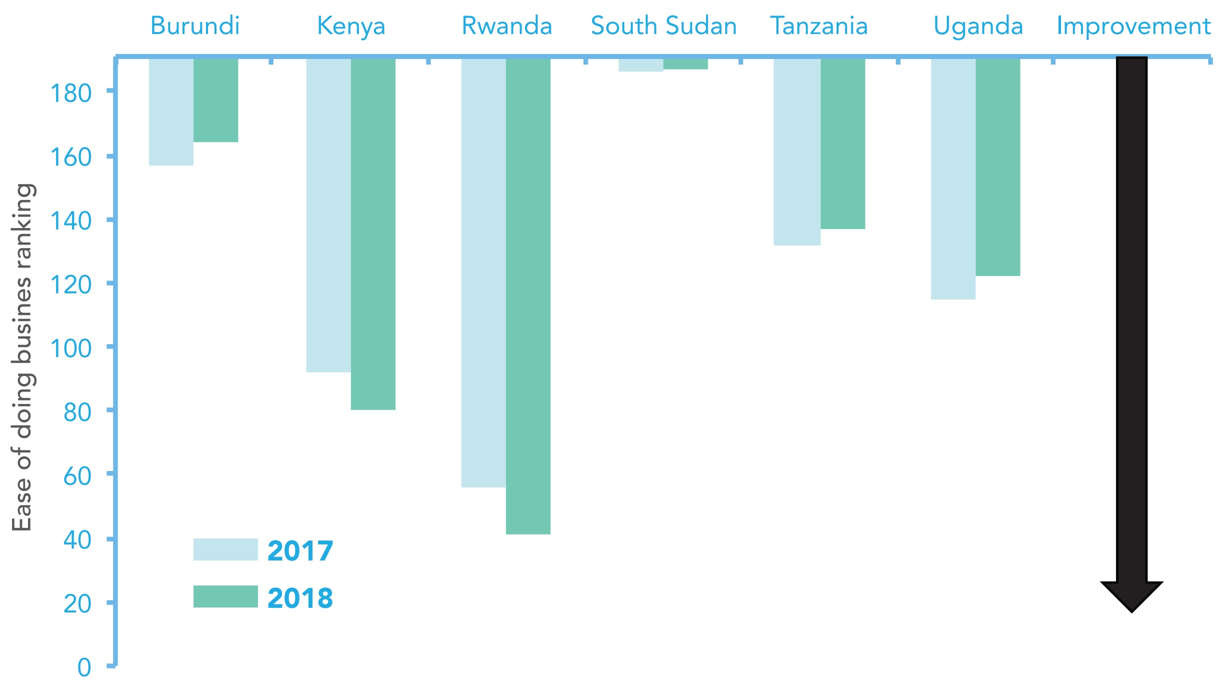
The Bujagali Hydropower Project is a hydropower facility on the Victoria Nile in the Republic of Uganda. The Project consists of five 51 MW turbines (255 MW in total), which supply ±1,300 GWh per year to the local electricity grid. Upon commissioning in 2012, the Project doubled the installed power capacity in Uganda, addressing the long-term need for economical, large-scale, power generation in a country that has one of the lowest electrification rates in Africa.

1.1.5 BUSINESS ENVIRONMENT

The World Bank's 2018 Ease of Doing Business Report appears to show a polarising business environment in East Africa. Whilst Kenya and Rwanda are constantly implementing business friendly reforms to make their economies more attractive for private sector investment, instability in Burundi and South Sudan are making their economies less attractive options for many foreign investors.

Figure 7 demonstrates the World Bank's ease of doing business ranking for each East African economy in 2017 and 2018. The countries are ranked out of 190 global economies, with 1 being the most business friendly and 190 the least business friendly.

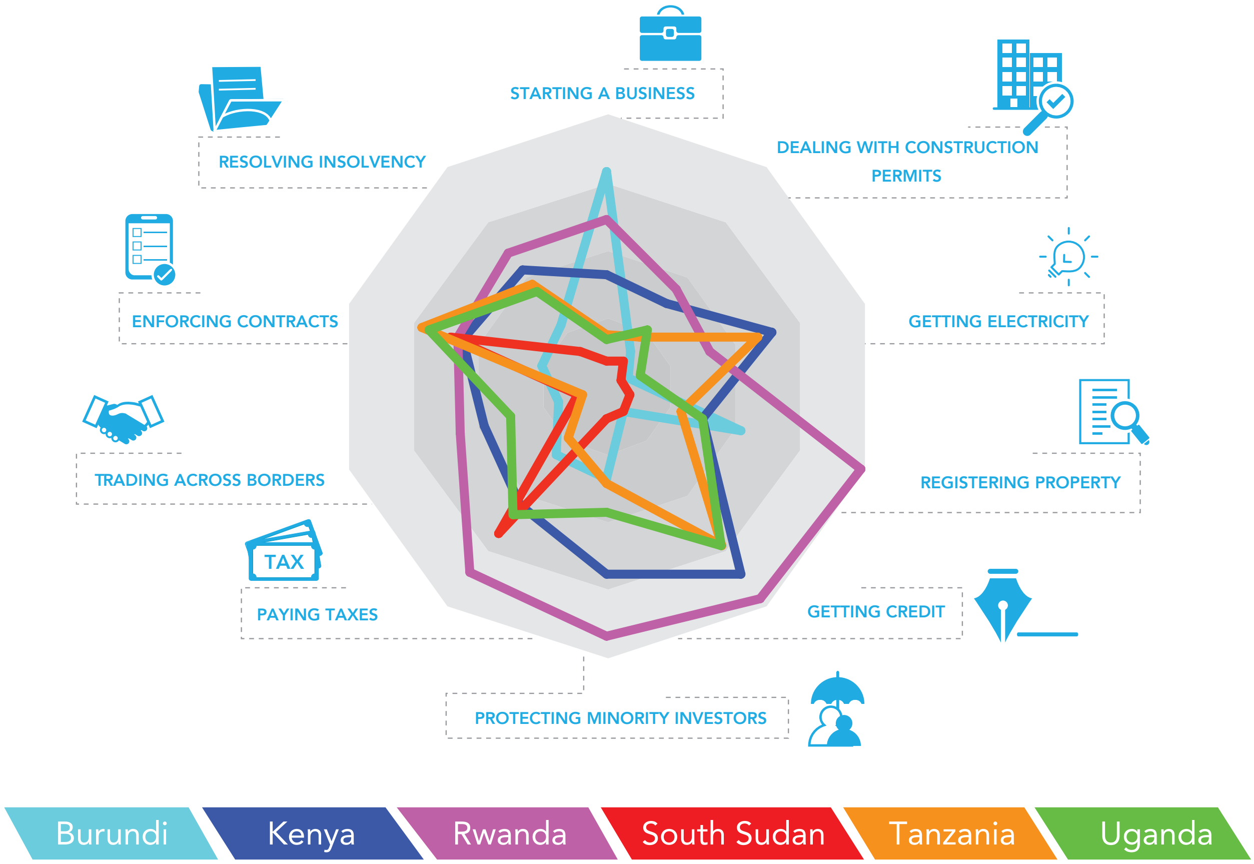
Figure 7: Overall Ease of Doing Business Rankings



Source: WB Ease of Doing Business 2018 report

Figure 8 provides more detail into the World Bank's ease of doing business ranking, by providing a ranking for 10 different topics: starting a business, dealing with construction permits, getting electricity, registering property, getting credit, protecting minority investors, paying taxes, trading across borders, enforcing contracts and resolving insolvency. The outer perimeter represents the friendliest business environment for each category and the nucleus the least friendly business environment.

Figure 8: Ease of Doing Business Breakdown



Source: WB Ease of Doing Business 2018 report

Burundi:

Burundi's ease of doing business ranking contracted by 7 places in 2018, from 157 in 2017 to 164 in 2018. The ease of registering a business in Burundi ranked highly at 42 (out of 190 countries) in 2018, despite a negative business reform for the topic.

Kenya:

Kenya's ease of doing business ranking continued to improve in 2018, as in 2017, supported by 6 business reforms in staring a business, dealing with construction permits, getting electricity, getting credit, paying taxes and trading across borders. In 2018, Kenya's overall ease of doing business rank increased by 12 positions from 92 in 2017 to 80. Getting credit scored particularly well at 29.

Rwanda:

Rwanda has also made continuous improvements in their ease of doing business, and maintains its position as the most business friendly economy in East Africa. In 2018, Rwanda improved its overall ease of doing business ranking by 15 positions, from 56 in 2017 to 41 in 2018, supported by 5 business reforms in: dealing with construction permits, registering property, protecting minority investors, paying taxes and enforcing contracts. Rwanda ranked extremely highly in registering property and getting credit, at 2nd and 6th respectively from 190 countries.

South Sudan:

South Sudan's ease of doing business ranking declined by one position in 2018 to 187 (out of 190 countries), not helped by an unfriendly business reform in the process of starting a business. South Sudan fared relatively well for paying taxes.

Table 2: Business Reforms Undertaken

Country	Positive (✓) or negative (✗) reform	Topic	Details of reform
Burundi	✗	Starting a business	Burundi made starting a business more expensive by increasing the cost of registering a business.
Kenya	✓	Starting a business	Kenya made starting a business easier by merging procedures required to start-up and formally operate a business.
Kenya	✓	Dealing with construction permits	Kenya made dealing with construction permits less expensive by eliminating fees for clearances from the National Environment Management Authority (NEMA) and the National Construction Authority.
Kenya	✓	Getting electricity	Kenya improved the reliability of electricity by investing in its distribution lines and transformers and by setting up a specialized squad to restore power when outages occur.
Kenya	✓	Getting credit	Kenya improved access to credit information by starting to distribute data from two utility companies.
Kenya	✓	Paying taxes	Kenya made paying taxes easier by implementing an online platform, iTax, for filing and paying corporate income tax and the standards levy.
Kenya	✓	Trading across Borders	Kenya reduced the time for import documentary compliance by utilizing its single window system, which allows for electronic submission of customs entries.
Rwanda	✓	Dealing with construction permits	Rwanda increased quality control during construction by introducing risk-based inspections.
Rwanda	✓	Registering property	Rwanda made registering property easier by implementing online services to facilitate the registration of property transfers.
Rwanda	✓	Protecting minority investors	Rwanda strengthened minority investor protections by making it easier to sue directors, clarifying ownership and control structures and requiring greater corporate transparency.
Rwanda	✓	Paying taxes	Rwanda made paying taxes easier by establishing an online system for filing and paying taxes.
Rwanda	✓	Enforcing contracts	Rwanda made enforcing contracts easier by making judgements rendered at all levels in commercial cases available to the general public through publication on the judiciary's website.
South Sudan	✗	Starting a business	South Sudan made starting a business more expensive by increasing business registration fees.
Tanzania	✓	Dealing with construction permits	Tanzania made dealing with construction permits easier by implementing a one-stop shop and streamlining the building permit process.
Tanzania	✗	Registering property	Tanzania made registering property more expensive by increasing the land and property registration fee.
Uganda	✓	Trading across Borders	Uganda reduced the time for export documentary compliance and border compliance by allowing for electronic document submission and processing of certicates of origin and by further developing the Malaba One-Stop Border Post.

Source: WB Ease of Doing Business 2018 report

Tanzania:

Tanzania's ease of doing business ranking contracted by 5 places in 2018, from 132 in 2017 to 137 in 2018. Tanzania implemented a positive business reform in dealing with construction permits and ranked particularly well in getting credit and enforcing contracts at 55 and 58 respectively.

Uganda:

Uganda's ease of doing business also deteriorated in 2018, from 115 in 2017 to 122 in 2018, despite a positive business reform in trading across borders. Like Tanzania, Uganda ranked particularly well in getting credit, at joint 55 out of 190 countries.

1.2 ECONOMIC PROSPECTS

Burundi:

There is a possibility that Burundi's domestic instability will continue into the 2020 elections. Consequently, the Burundian economy is likely to stabilise at near zero growth over the medium-term, only supported by a small recovery in the agriculture and mining sectors.

Kenya:

Public sector infrastructure investments will continue to benefit the Kenyan economy, which will continue to grow over the medium-term.

Rwanda:

An increase in public infrastructure investment ahead of Rwanda's Vision 2020 should increase economic growth over the medium-term. Further, successful implementation of the aforementioned infrastructure investments should boost Rwanda's economic growth potential over the long-term. Improvements in both the current and fiscal accounts, helped by higher mineral prices and fiscal discipline, should also stabilise the exchange rate and inflation over the medium-term.

South Sudan:

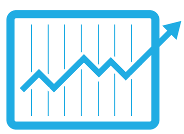
With little near-term prospect of domestic stability, it is unlikely that the economy will leave its depression over the medium-term. Continued government expenditure on security, financed through Central Bank monetisation, will drain the economy of resources, whilst the majority of the population are in need of humanitarian support.

Tanzania:

Economic growth is expected to remain buoyant, encroaching upon 7% over the medium term, supported by the expanding services sector and public sector infrastructure investments. Lesser reliance on public sector investments and greater private sector investment would further increase Tanzania's potential output.

Uganda:

Economic growth is expected to continue to recover over the medium term under sizeable public sector infrastructure investments. However, the aforementioned public sector infrastructure investments are likely to increase imports and domestic debt and thus worsen the current account and fiscal balances. The persistent current account deficit also poses an exchange rate risk over the medium term.



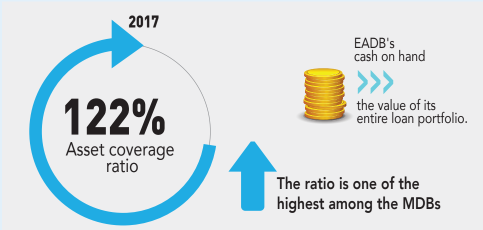
2 OVERVIEW OF THE YEAR'S ACTIVITIES

2.1 INTERNATIONAL CREDIT RATING

In July 2018, Moody's Investors Service maintained EADB's long-term issuer rating at Baa3 with a stable outlook. The rating is based on some of the following factors:

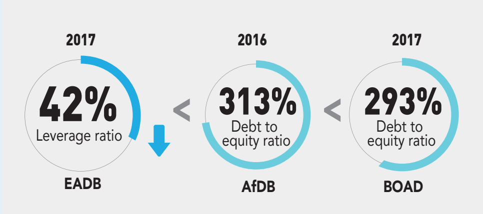
Capital remains strong:

The bank's asset coverage ratio (usable equity/ (gross loans plus equity plus expected loss on liquid assets)), at 122% in 2017, remained very high. The ratio is one of the highest among the MDBs and signals the bank's usable equity is larger than its gross portfolio. In other words, EADB's cash on hand is greater than the value of its entire loan portfolio.



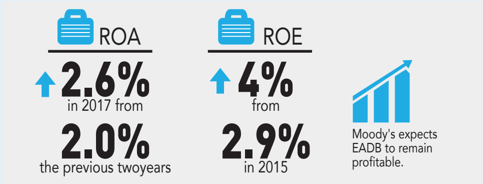
Leverage remains highly favourable:

EADB's leverage ratio (debt as a percentage of usable equity) remains very low. It was 42% in 2017, which is low both in absolute terms and compared with its rated MDB peers. In comparison, AfDB's debt to equity ratio stood at 313% in 2016, while that of the West African Development Bank (BOAD, Baa1 stable) was 293% in 2017.



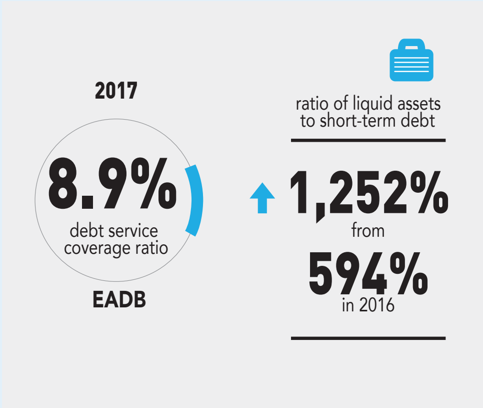
EADB remains profitable:

In 2017, EADB's return on average assets (ROA) increased to 2.6% in 2017 from 2.0% in the previous two years, while its return on average equity (ROE) rose to 4% from 2.9% in 2015. Moody's expects EADB to remain profitable, supported by the expansion in its investment activities.



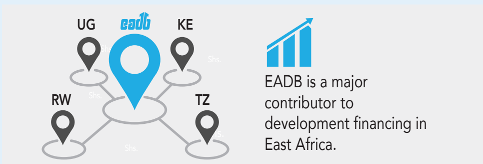
EADB has strong liquidity,

reinforced by low levels of borrowing relative to liquid assets, moderate funding costs and a relatively long-dated debt maturity structure. Its debt service coverage ratio (short-term debt plus currently maturing long-term debt (ST + CMLTD) to discounted liquid assets) is one of the strongest among the MDBs. The ratio was 8.9% in 2017. As the maturity of most additional borrowing was medium term and long term, the bank's ratio of liquid assets to short-term debt has also improved in recent years. In 2017, the ratio rose significantly to the exceptionally strong level of 1,252% from 594% in 2016.



EADB is a major contributor to development financing in East Africa:

It enjoys a high level of commitment from its Member States, which view it as an important vehicle for delivering key development objectives across the East Africa region.



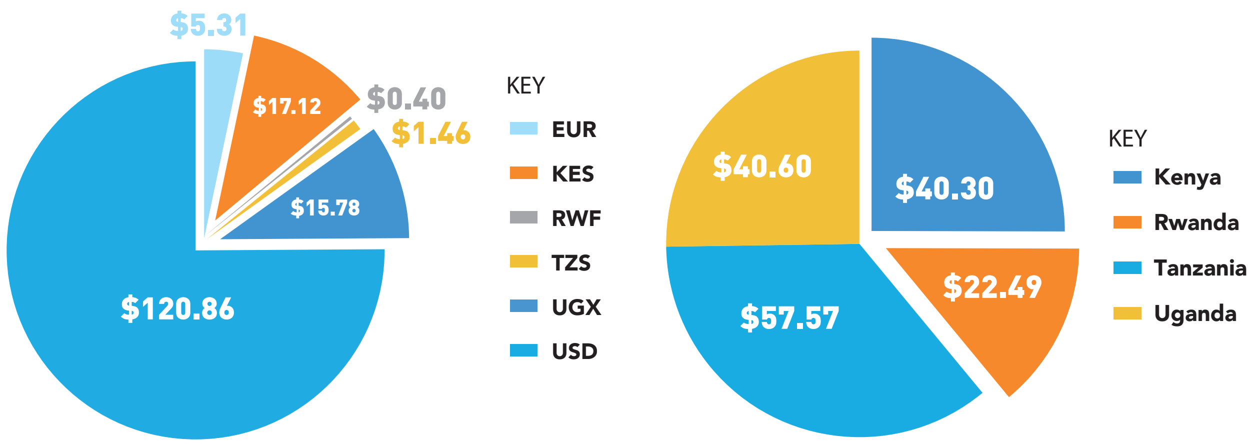
In summary, Moody's report states that, the bank's credit strengths include strong liquidity and capital buffers that are among the strongest of the multilateral development banks.

2.2 LENDING OPERATIONS

2.2.1 PORTFOLIO STATUS

The gross portfolio as at 31 December 2018 was USD 160.9 million.

Figure 9: Portfolio by currency and country



Source: EADB

The United States Dollar remained the dominant currency in the Bank's portfolio, with projects funded in dollars amounting to USD 121.0 million, or 75% of the gross portfolio.

Tanzania had the largest national portfolio, amounting to USD 57.6 million, or 36% of the total portfolio. Uganda had the second largest national portfolio, worth USD 40.6 million (25%), followed by Kenya with USD 40.3 million (25%) and Rwanda with USD 22.5 million (14%).

United States Dollar remained the dominant currency with **75%** **Gross portfolio**

As at 31st December 2018, the top three sectors with the highest exposures were Financial Intermediaries, Real Estate and Electricity, Gas, Oil and Water. The portfolio was dominated by Financial Institutions: Development Financial Institutions had an exposure of USD 37.7 million (23%) and Commercial Banks had an exposure of USD 26.5 million (16%). This was followed by Real Estate, which had an exposure of USD 38.9 million (24%) and Electricity, Gas, and Oil & Water, which had an exposure of USD 19.5 million (12%).

Portfolio Quality

GROSS PORTFOLIO
as at 31st December 2018
USD 160.9 million
(↓19%)

GROSS PORTFOLIO
as at 31st December 2017
USD 198.2 million

GROSS PORTFOLIO
as at 31st December 2016
USD 190.1 million

The gross portfolio (loans and equity investments) as at 31st December 2018 was USD 160.9 million, compared to USD 198.2 million as at December 2017 and USD 190.1 million as at 31st December 2016, reflecting an annual decline of 19%. The number of projects decreased to 64 as at 31st December 2018 from 70 as at 31st December 2017.

Long-term loans remained the leading product at the Bank, accounting for 93% of the total portfolio and a gross exposure of USD 149.5 million.

The Bank's total provisions as at 31st December 2018 was USD 3.2 million, compared to USD 7.7 million at the end of December 2017. This decrease in provisioning and impairment is due to write-offs following the new accounting standards (IFRS 9), which changed the risk classification and provisioning of projects from the old 'incurred loss' model to 'expected loss' model.

The Bank's balance sheet also reflects a net portfolio size (loans and equity investments) of USD 157.7 million as at end December 2018, compared to USD 190.5 million as per the end of December 2017.

Environmental and Social Analysis

EADB recognizes that sustainable development depends upon a positive interaction between economic and social development on the one hand and environmental protection on the other. The Bank contributes to sustainable development through financing activities and therefore acknowledges that identifying and managing environmental risks should be part of the normal process of risk assessment and management.

As at 31st December 2018, the Bank had eight (8) projects categorized as Class 1. These are projects with significant adverse environmental and social (E&S) impact, but which had sufficient mitigation measures in place to manage the E&S impact. These measures are part of the conditions subsequent to disbursement and are monitored by the Bank as part of its supervision activities. The bulk of the Bank's projects and exposures were projects classified as Class 2, which are projects with potentially limited adverse E&S impacts that are few, site specific, and for which mitigation measures are readily available. The rest of the projects were classified under Class 4 and these are projects whose impact is as a result of the Bank's on lending to other financial institutions.

Eight (8)
Class 1 Projects

2.3 KEY ACTIVITIES OF THE BANK

Country Office Kenya

Country office Kenya activities and operations in 2018 were geared towards promoting the Bank's current key focus areas of food security and skills development.

On the food security front, Country office Kenya continued to market the Agricultural Financing Kenya programme. Two new partner financial institutions entered the programme in 2018: Kenya Women Microfinance Bank and Sidian Bank.

On the skills development, the Country office, Kenya has entered into an agreement with Sunshine Education Services Ltd, one of the leading private secondary schools in Nairobi, to finance the expansion of school infrastructure to increase enrolment. Further, under the Country office, Kenya, the two Jumuia Hospitals (with a combined inpatient capacity of 205 beds) and Strathmore Law School (which can accommodate 600 students) projects were completed in 2018.

Figure 10: Strathmore Law School

Country Office Rwanda

In 2018, EADB continued to support the extension and modernization of Green Hills Schools in Nyarutarama, Gasabo District in City of Kigali. The school provides employment to 312 workers, of which 161 are male and 151 are female, and education to hundreds of students.

Figure 11: Green Hills Academy

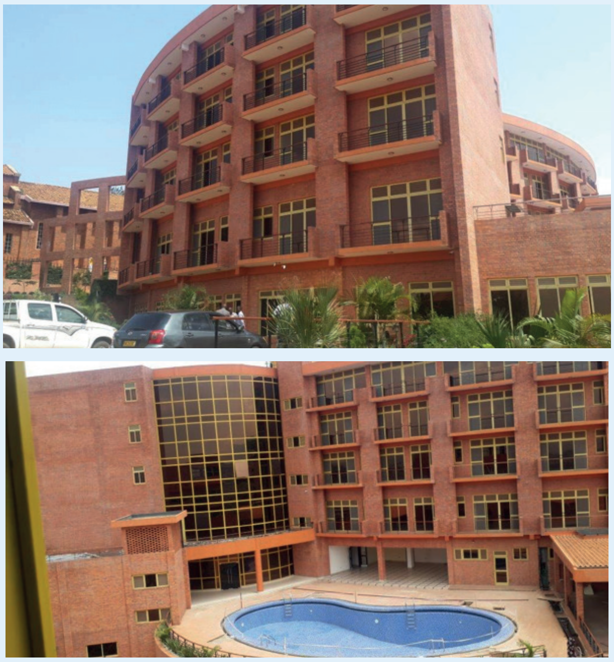
In addition, EADB had four lines of credit running with the Development Bank of Rwanda (BRD) in 2018, worth USD 5, USD 5, USD 10 and USD 15 million for BRD to on-lend to projects in Rwanda. The sub-projects financed are in the agriculture, education, hospitality, manufacturing and real estate sectors. Trust Industry and Sainte Famille Hotel are examples of two projects financed under the EADB-BRD lines of credit.

TRUST Industries is a company dealing in personal hygiene products. It currently has four plants: a bar soap plant, a paper mill plant, a detergents plant and a tissues conversion plant. TRUST Industries employs 303 people, of which 180 are male and 123 are female.

Figure 12: Trust Industry

The Sainte Famille Hotel is a 3-star hotel in Kigali City. The hotel has 56 rooms, a bar, rooftop restaurant, swimming pool, conference hall, shops and office facilities. At present, the Sainte Famille Hotel has created 5 permanent and over 1,000 temporary jobs; however upon its opening in July 2019, it is expected to create over 50 permanent jobs and to contribute towards Rwanda's development of the tourism and business conference sector.

Figure 13: Sainte Famille Hotel



Country Office Tanzania

In 2018, the Country Office, Tanzania hosted a high-level training seminar for senior lawyers from across the region.

The training, held between 06th August and 10th October 2018, was designed to build the capacity of public sector lawyers involved in negotiating transactions and drafting agreements for the extractive industries.

This was the sixth activity in a series of workshops that brought together participants from Kenya, Uganda, Rwanda and Tanzania with facilitators from international law firm DLA Piper.

The objective of the trainings is to assist East African public sector lawyers and judges, in the wake of resource discoveries, to correctly structure transactions and related policies to ensure the region and its citizens benefit from the exploitation of extractive resources.

Figure 14: Training on Extractive Industries for Public Sector Lawyers, Tanzania

Country Office Uganda

In 2018, Country Office Uganda successfully hosted the EADB 50th Year Anniversary celebrations that demonstrated the Bank's role in banking, investment and social responsibility within the East Africa Region. The event attracted participants from partners and stakeholders around the world. The event, through the Generation 2068 conference, provided a platform for ideas and recommendations critical to EADB's next strategic plan (2021-2025) and a 50-year vision for sustainable development, integration and cooperation in East Africa.

Country Office Uganda also launched the EADB Biodiversity Investment Fund (BIF), a fund created through a partnership between EADB, KFW and the Government of Uganda to provide financing to biodiversity-friendly investments. The fund targets seven specific sectors namely; tourism, forestry, organic agriculture, fisheries and aquaculture, wildlife-based enterprises and renewable energy. The financing is targeted to businesses that can achieve measurable impacts under each of the following pillars:

- Green Production and Services
- Inclusive Business
- Conservation and Habitat Restoration.

Country Office Uganda had the pleasure of welcoming two new members to the team over 2018: Mr. Francis Ogwang, the incoming Country Manager Uganda, and Mr. Heri Kalungwana, a Senior Investment Officer. The two have joined at a time when the Country Office is in the process of implementing the Bank's medium-term plans of expanding business opportunities to support Uganda's economic growth.

Environmental and Social Department

EADB employed an Environmental and Social Management Expert in August 2018.

During his time at the Bank, the expert has worked on the bank's Environmental and Social Policy, Climate Change Policy, and Gender Policy and Action Plan, and is currently supporting the development of an Occupation Health, Safety and Environment Policy.

The ESM expert has provided training to EADB staff in Kenya, Rwanda and Tanzania and has prepared a training session for the staff based at EADB headquarters in Uganda. He has also trained staff at Centenary Bank in environmental and social management, as part of the Agrifinance Enhancement Programme.

Finally, the expert has also interacted in the peer review of potential projects, including the lines of credit for Centenary Bank (RFEP), FINCA (AEP), Opportunity Bank (AEP) and Equity Bank (AEP).

Finance Department

2018 was a very busy year for the Finance Department, mainly due to a number of new standards that became effective, notably the famous IFRS 9 Financial instruments, which, among other things, focuses upon loan classification and forward looking impairment. In addition to IFRS 9, IFRS 15, which focuses upon revenue from contracts with customers, also became effective. Preparations were also made for IFRS 16, which focuses upon leasing standard, which will become effective from 1st January 2019.

The department was therefore heavily involved in ensuring that the adoption of new standards was smooth and did not slow down the normal activities or delay Bank's reports. A number of training sessions were conducted, especially for IFRS 9, to ensure that all Bank staff grasped the new standard and its implications, both in business and reporting.

It gives us great pleasure to report that the adoption of the new standards happened smoothly, and the Bank's 2018 financial statements are fully compliant to the international financial reporting standard.

In addition to the new standards, the department continued to professionally discharge other duties including loan disbursements, loans billing, treasury back office operations, suppliers' payments, budgeting and financial reporting. All these responsibilities and others, not mentioned, were judiciously discharged and as at the end of the year there were no outstanding issues that could impact the Bank.

The department maintained an effective internal control and as a result there were no incidents reported during the year. The Finance Policy was reviewed to incorporate requirements of the new standards as well as new developments in finance and risk management.

During the year the department also championed a review of the level of implementation of the strategic plan after two years of implementation; the results will be used in the preparation of the new strategic plan and targets.

For 2019, the department will review the implementation of the new standards and make necessary improvements where needed. The department will also champion implementation of the new leasing standard (IFRS 16), which is effective from 1st January 2019.

The department will collaborate with the Information and Communication Technology (ICT) Department and others to improve the Bank's core banking system as well as financial reporting system to take advantage of technological changes and modern practices.

Human Resources Department

In 2018, as the Bank celebrated its 50th anniversary, the Human Resources (HR) department continued to provide strategic direction and advice related to bank-wide human resource management. This included talent acquisition, human capital development, performance management and delivery of quality HR welfare services.

The Bank hired a Head of Operations and a Head of Finance, who both brought on-board a breadth of knowledge and experience in their respective fields, spanning over 20 years each. It is anticipated that these leaders will inspire efficient delivery of service and in turn improve the productivity of other employees. In addition to this, the Bank also recruited a Country Manager and Senior Investment Officer for Country Office Uganda, a Senior Investment Officer for Country Office Rwanda and a Senior HR Officer. Further to this, the Bank retained the services of an Environment and Social Management expert, through partnership with IPC.

The capacity building initiatives included trainings in Financial Modelling, Rural Financial Enhancement, Anti Money Laundering and Terrorism Financing and Environment and Social Management, among others.

The department's focus for 2019 is continuous improvement of the performance management system and capacity enhancement.

Internal Audit Department

During 2018, the Internal Audit Department was streamlined to comply with standards in other international development institutions.

Monitoring and Evaluation Department

The monitoring and evaluation department carried out a regular supervision mission of the Rural Finance Enhancement Programme and the Agrifinance Enhancement Programme in February and August 2018. The Rural Finance Enhancement Programme and Agrifinance Enhancement Programme are two interventions to develop SMEs in the rural and agricultural sectors across Uganda. Given the size of SMEs supported under the programme, EADB acts through offering lines of credit to partner financial institutions to on-lend to the specified recipient. In 2018, EADB had five partner financial institutions under the programmes, although one partner financial institution exited the programme due to their non-compliance. A sample of projects was chosen covering different sectors across Central, Eastern and

South-Western Uganda.

Most sub-projects were largely deemed to be compliant with the programmes and provided developmental additionality.

In the February supervision mission to Central and Eastern Uganda, Ngemeraku Investments Limited and Quality Supermarkets provided significant employment creation and boosted the competitiveness of domestic industries. Joshua Gandigude demonstrated a substantial impact to local communities in developing local supply chains to construct property in Iganga, as did Godfrey Ssengendo who provides transport for refugees in Northern Uganda.

In the August supervision mission to Central and South-Western Uganda, Kiddawalime Bakery Limited in Mbarara demonstrated an enormous contribution to the local community by employing over 200 people, including over 70 women, as did Mukasa Tenywa Godfrey, who's leisure and education centre employs over 100 people in the local community and provides geography and swimming lessons for thousands of students. Phenehas Barigye's petrol station in Mbarara also demonstrated a substantial socio-economic impact, both from job creation and in developing market infrastructure.

Both programmes demonstrated a substantial socio-economic impact. Our calculations below demonstrate the impact of these programmes on communities in Uganda by the end of 2018.

Figure 15: Socio-economic Impact of the AEP and RFEP

	Social impact of the AEP	Social impact of the RFEP
Portfolio size (UGX millions)	76,951	30,963
Number of sub-loans	1522	114
Permanent jobs created	3995	3948
Temporary jobs created	6849	1049
Female jobs created	2949	2053
Access to electricity	95 communities	5 communities
Access to improved drinking water		9 communities
Access to transport and communications infrastructure	95 communities	9 communities
Students education contributed towards		17007
Industries supported through the value chain	68200	431
SMEs supported through the value chain	67629	377

Portfolio Department

By the end of 2018, the Bank's portfolio stood at USD 160.9 million, and was spread across various sectors including: education and health, agriculture and fisheries, housing, energy, agro, marine and food processing, aviation and financial intermediation, amongst others.

At the beginning of 2018, a number of long-term clients successfully exited the Bank's portfolio after completing development enhancing projects. S&L Holdings, Aponye, Ghomme Health and Educational Services and the Bank of Kigali all exited the portfolio at the beginning of the year.

Additional lines of credit were also issued to existing clients in 2018 to expand their projects. Kayonza Tea Growers, Nkumba University and DFCU Limited all increased their borrowing from EADB in 2018.

Whilst a number of new clients also joined the Bank's portfolio in 2018, including Viva Academy and Sunshine Educational.

The Bank continued to expand its banking partnerships by providing lines of credit to new partners such as Sidian Bank and Mercantile Credit Bank Limited under the KfW Rural Financial Enhancement Programme and Agricultural Enhancement Programme, which seek to improve access to medium- and long-term sustainable agricultural financial services for the SME sector.

Treasury Department

During 2018, the Bank continued to implement its treasury activities in accordance with the provisions of Treasury Policies and Procedures under the supervision of the Assets and Liabilities Committee (ALCO).

The main treasury operations conducted included; investments, resource mobilization and the hedging of currency risk exposures arising from its financing operations. Treasury investments were held in time deposits with banks in the region and outside the region. At the end of 2018, EADB held treasury investments worth USD 165.5 million in various currencies.

During 2018, the Bank drew on lines of credit from existing partners, and signed a new USD 15 million line of credit with the Arab Bank for Economic Development Bank in Africa (BADEA) to finance exports from Arab countries to the East African Region.

2.4 CORPORATE SOCIAL RESPONSIBILITY ACTIVITIES

Medical Training and Fellowship Programme (METAF)

The Medical Training and Fellowship Programme is a four-year project (2017-20) that aims to increase the early detection, research and treatment of cancer and neurological diseases in East Africa, especially in communities and areas where access to qualified professionals remains a challenge. Funded by EADB, the METAF programme is delivered by the British Council in partnership with the Royal Council of Physicians (RCP), which acts as the technical partner.

The programme was developed in response to the growing burden of non-communicable diseases, especially cancer and neurological disorders in EADB Member States (Kenya, Rwanda, Tanzania and Uganda). Premised on British Council's expertise in managing training programmes and the RCP's expertise in improving medical care across the globe, the programme is a high impact sustainable training model employing a twin approach of short-term clinical trainings within East Africa and long-term fellowships tenable in the United Kingdom.

The scholarship was officially launched in 2017 and trained 85 doctors in neurology and 175 doctors in oncology throughout the year.

An additional 244 doctors were trained in 2018. Extra trainings were held in Rwanda, to make up for delayed trainings in 2017, and in Kenya, to make up for trainings that were postponed due to the doctor's strike in early 2017. In total, 5 trainings were held in Kenya, two in neurology and three in oncology) that reached a total of 121 doctors; 2 trainings were held in Rwanda (both in neurology) that reached a total of 29 doctors; 3 trainings were held in Tanzania (one in neurology and two in oncology) that reached a total of 63 doctors; and two trainings were held in Uganda (both in oncology) that reached a total of 31 doctors.

Science, Technology and Engineering University Scholarship (STEM) Scholarship

The Science, Technology, Engineering and Math's (STEM) University Scholarship Programme offers multiple fast-track 12-month scholarships to experienced teachers and lecturers who have a Bachelor's degree in the STEM subjects. Successful scholars are offered the opportunity to pursue a graduate degree in the same fields at Rutgers University, New Jersey, USA.

EADB sponsors the programme and offers: full tuition, room, board and living expenses for the students, plus annual health insurance and a round-trip ticket to the US at the start of their programme and back to their home country in East Africa at the end of the programme. The programme partners with the Africa-America Institute, who in turn implement the programme on behalf of EADB and provide the students with information about internships at American and local companies working in Africa.

In August 2017, EADB and AAI sent four scholars to Rutgers University, who all graduated in August 2018. Ms. Miriam Kabagorobya, from Uganda, was the first lady to be admitted to Rutgers under the scholarship. She undertook a Master's degree in Science Education and in July 2018 was offered the opportunity to study for a PhD with Syracuse University. Mr. Dennis Akuom, from Kenya, also undertook a Master's Degree in Science Education, while Mr. Barnabas Mafula and Mr. Chris Mbae Njagi, both from Kenya, pursued Master's degrees in Cell and Developmental Biology. Finally, Mr. Edward Mureka, from Kenya, undertook a Master's degree in Material Science and Engineering (MSE).

In August 2018, EADB doubled the STEM scholarship and awarded eight scholars the opportunity to study for a master's degree at Rutgers University. In 2018, EADB was delighted to sponsor two female scholars and our first Rwandan and Tanzanian students. Purity Kendi Muthitu and Ruth Mathenge, both from Kenya, were admitted to study Maths Education and Physics Education respectively. Fabien Habimana, from Rwanda, and Mathias Halinga, from Tanzania, were both awarded the opportunity to study Industrial System Engineering. Usufu Nyakoojo, from Uganda, was admitted to study Maths Education, whilst Nixon Odari, Moffat Ongeri and Brian Odiwor, all from Kenya, were awarded the opportunity to study Maths Education, Physics Education and Science Education respectively.

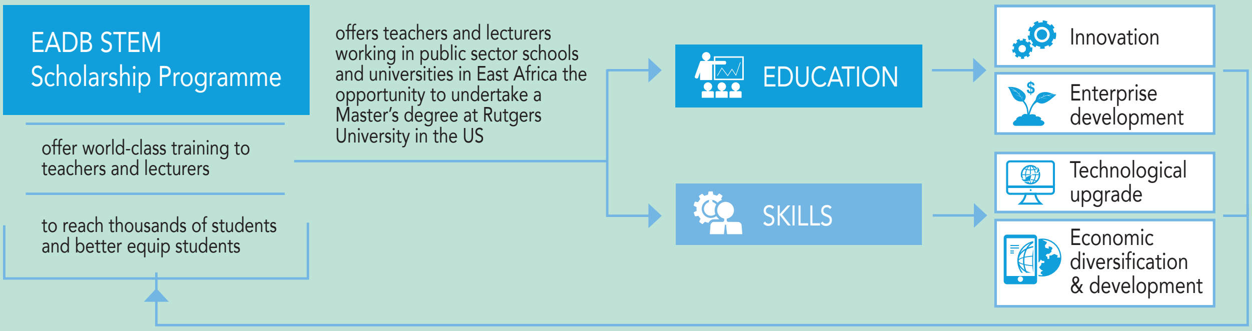
Building Capacity for Lawyers in Extractive Industry

EADB continues its partnership with DLA Piper, a global law firm, towards strengthening capacity related to extractive industry contract negotiations in East Africa. This partnership takes the form of co-hosting regional training seminars aptly themed Extractive Industries Training - the product of the partnership between EADB and DLA Piper, a global law firm. These high-level symposiums have been designed to endow and sharpen the skills of the public sector lawyers involved in structuring, negotiating transactions and drafting agreements for and on behalf of governments in extractive sectors and other large scale projects.

Up to the end of 2017, five workshops had been conducted. The first was held in Rwanda in March 2015, followed by successive workshops in Uganda in June 2015, Tanzania in September 2015, Kenya in August 2016 and Rwanda in August 2017.

In 2018, a sixth workshop was held in Dar es Salaam, Tanzania, that trained 41 public sector lawyers and academics from across the region in International Business Negotiation.

Box 3: Skills development



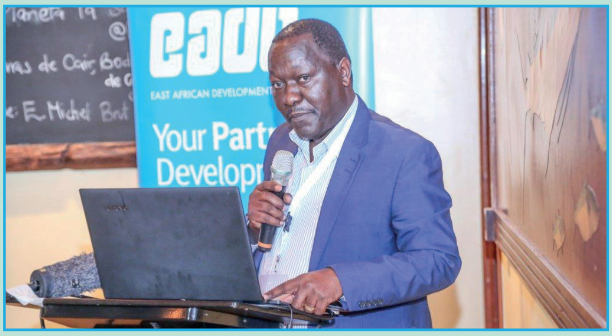
Lack of or inadequate education and training deny people opportunities for self-advancement by limiting their access to gainful employment or keeping them in low-productivity and low paying jobs. Ultimately this excludes such persons from making a meaningful contribution to economic growth. Good quality education and training have thus been recognised as important ways of breaking the "cycle of poverty".

Acquisition of education and skills can lead to innovation, enterprise development, technological upgrade and transfer and increased investments and ultimately economic diversification and development.

The EADB STEM Scholarship Programme offers teachers and lecturers working in public sector schools and universities in East Africa the opportunity to undertake a Master's degree at Rutgers University in the US in the STEM fields (Science, Technology, Engineering and Mathematics).

EADB recognises the mismatch between student's learning outcomes and the needs of the labour market, particularly in the STEM fields (where Sub-Saharan Africa has fewer graduates than any other region). By offering world-class training to teachers and lecturers in the STEM fields, we hope to reach thousands of students and better equip students for the demands of the labour market upon graduation. It is our intention that this will reduce youth unemployment and increase levels of research and development in East Africa, thereby driving technological innovation and long-term socio-economic growth.

In 2018, EADB congratulated its largest cohort onto the STEM scholarship: Mr. Fabien Habimana (Rwanda, Industrial Systems and Engineering), Mr. Mathias Halinga (Tanzania, Industrial Systems and Engineering), Ms. Purity Kendi (Kenya, Maths Education), Ms. Ruth Mathenge (Kenya, Physics Education), Mr. Usufu Nyakoojo (Uganda, Maths Education), Mr. Nixon Odari (Kenya, Maths Education), Mr. Patrick Odhiambo (Kenya, Physics Education) and Mr. Brian Odiwuor (Kenya, Maths Education).



EADB Board Member, Mr. Francis Karuiru at the STEM send-off in Nairobi

EADB Scholar Mr. Usufu Nyakoojo at the STEM send-off in Nairobi

2.5 RISK MANAGEMENT

The Bank is exposed to a number of risks potentially impacting its business, financial condition, results of operations and cash flows. As a DFI organization, certain elements of risk are inherent in its transactions and operations and are present in the business decisions made. The Bank, therefore, encounters risk as part of the normal course of its business and designs risk management processes to help manage these risks. The Bank's success is dependent on its ability to identify, understand and manage the risks presented by its business activities so that it can appropriately balance its mandate and profitability.

Risk Management Framework

The Bank operates through departments and business units. Risk and Capital are managed via a framework of principles, organizational structures and measurement and monitoring processes that are closely aligned with the activities of the departments and business units:

- Core risk management responsibilities are embedded in the Board and delegated to Management and Bank committees responsible for execution and oversight. The Board regularly monitors the risk and capital profile of the Bank. Systems, processes and policies are critical components of EADB risk management capability.
- The Bank operates a three-line of defence risk management model whereby front office functions, risk management oversight and audit are played by functions independent of one another.
- Systems, processes and policies are critical components of our risk management capability.
- Monitoring, stress-testing tools are in place for key capital and liquidity thresholds and metrics.

The Bank designs risk management processes to help manage risks

Risk Related to EADB's Business

These risks include, but are not limited to, credit risk, market risk, liquidity risk, operational risk, technology (cyber security) risk, legal risk and reputational risk. The Bank also focuses on identifying environmental and social risk and assessing possible impact on greening and inclusive business. However, there may be additional risks that are not presently material or known.

One of the main types of risks inherent in EADB's business is credit risk. An important feature of the Bank's credit risk management system is to employ an internal credit risk control system through which it identifies, measures, monitors and mitigates existing and emerging credit risk of customers. As this process involves detailed analyses of the customer or credit risk, taking into account both quantitative and qualitative factors, it is subject to human error. In exercising their judgment, EADB's project analysts may not always be able to assign an accurate credit rating to a customer or credit risk, which may result in our exposure to higher credit risks than indicated by its risk rating system. However, the Bank has undertaken certain actions to enhance its credit policies and guidelines to address potential risks associated with particular sectors, industries or types of customers.

The Bank's financial and accounting estimates and risk management framework relies on analytical forecasting and models. The processes used to estimate inherent loan losses and to measure the fair value, as well as the processes used to estimate the effects of changing interest rates and other market measures on the Bank's financial condition and results of operations, depends upon the use of analytical and forecasting models. Some tools for managing risk are based upon the use of observed historical market behaviour. The Bank relies on quantitative models to measure risks and to estimate certain financial values. These models are used in determining the pricing, grading loans, measuring interest rate and assessing capital adequacy.

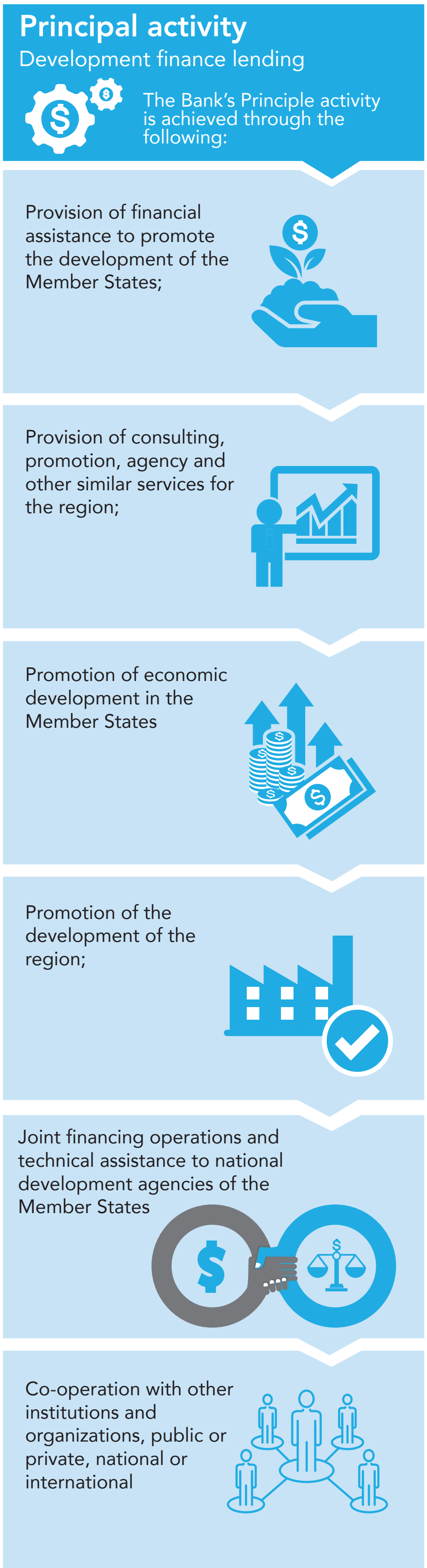
More recently, the Bank embarked on enhancing its Enterprise Risk Management Framework by developing different policies and guidelines, models and metrics for measuring market risk (VaR model), Risk Control Self-Assessment (RCSA), Key Risk Indicators (KRI), etc. Year 2018 was the implementation-testing period and great achievements have been made in minimizing and reducing aforementioned risks.

credit risk is the main type of risks inherent in EADB's business

3
DIRECTORS' REPORT AND FINANCIAL STATEMENTS

For the year ended 31 December 2018

DIRECTORS' REPORT



1. Introduction

The directors submit their report together with the audited financial statements for the year ended 31 December 2018, which disclose the state of affairs of East African Development Bank ("EADB" or "the Bank").

2. Incorporation

The Bank was created under the Treaty for the East African Co-operation of 1967, which was subsequently amended and re-enacted as the Treaty and Charter of the East African Development Bank in 1980.

3. Mission and Vision

The Bank's Vision is to be a partner of choice in promoting sustainable social-economic development.

The Bank's Mission is to promote sustainable social economic development in East Africa by providing development finance, advisory and support services.

4. Principal activity

The principal activity of the Bank is development finance lending under the Bank's Charter. The Bank's Principle activity is achieved through following:

(a) Provision of financial assistance to promote the development of the Member States;

(b) Provision of consulting, promotion, agency and other similar services for the region;

(c) Promotion of economic development in the Member States, in such fields as industry, tourism, agriculture, telecommunications and other fields of development;

(d) Promotion of the development of the region;

(e) Joint financing operations and technical assistance to national development agencies of the Member States and use of such agencies as channels for financing specific projects;

(f) Co-operation with other institutions and organizations, public or private, national or international, which are interested in the development of the Member States;

DIRECTORS' REPORT (continued)

5. Business Objectives and Strategies

The main objective of the Bank is to bring economic development in Member States through different interventions mainly medium and long term lending.

The Bank's strategy is anchored on member states' national development strategies as well as the East African Community. Currently the Bank is operating under its 2016-2020 strategy which, among other things, focuses on five key areas in the region namely:

- food security covering agriculture, agribusiness and forestation;
- social development covering education, health and housing;
- infrastructure development covering energy, water, transport, manufacturing and ICT;
- regional integration covering trade and cross border projects; and
- Climate Change covering environmental protection, biodiversity and green investments.

The Board gets progress reports of the strategy implementation on quarterly basis as well as an annual review when approving the annual budget and plans.

6. Governance

Governance plays a key role in the management of the affairs of the Bank and in the overall execution of its mandate. The Bank has various structures and measures in place to promote and safeguard good governance.

The key elements of the governance structure comprise: the Governing council which is the supreme organ of the Bank; the Board of Directors which reports to the Governing Council, and the advisory panel to the Board.

a) Governing Council

The Governing Council is comprised of Ministers responsible for Finance in Member States and meets regularly to receive and consider reports from the Board of Directors. Governing Council Members who served during the year end to the date of this report were:

	Name	Details
1	Hon. Dr. Philip Mpango - Member	Minister for Finance and Planning, United Republic of Tanzania
2	Mr. Henry K. Rotich – Member (Up to 24 July 2019)	Cabinet Secretary, The National Treasury, Republic of Kenya

DIRECTORS' REPORT (continued)

6. Governance

b) Governing Council

	Name	Details
3	Hon. Amb. Claver Gatete – Member (Up to April 2018)	Minister for Finance and Economic Planning, Republic of Rwanda
4	Dr. Uzziel Ndagijimana - Member (From April 2018)	Minister for Finance and Economic Planning, Republic of Rwanda
5	Hon. Matia Kasaija - Member	Minister for Finance, Planning and Economic Development, Republic of Uganda
6	Hon. Amb. Ukur Yatani – Member (from 25 July 2019)	Cabinet Secretary, The National Treasury, Republic of Kenya

During the year, the Governing Council held one meeting to deliberate on the Bank's financial performance and other issues from the Board of Directors.

c) Board of Directors and sub-committees

The Board of Directors is vested with all powers in the Bank and meets at least on quarterly basis to receive and consider reports from Management. The Board of Directors is comprised of Permanent Secretaries of the Ministries responsible for Finance in Member States as well as private sector representatives from Member States. Non-Sovereign shareholders (class B shareholders) are represented by the African Development Bank.

The Board has two committees namely the Board Human Resources Committee which is responsible for all staffing issues in the Bank and the Board Audit Committee which is responsible for all internal control issues. The Audit committee currently is also responsible for Bank's risk management.

The Board of Directors met three times during the year to deliberate on various issues including the Bank's financial performance and approval of projects.

The Board Human Resources committee and the Audit Committee met twice during the year and deliberated on various staffing issues, Internal Audit reports and Risk management reports respectively.

DIRECTORS' REPORT (continued)

6. Governance (continued)

b) Board of Directors and sub-committees (continued)

The Board members who served during the year end to the date of this report were:

	Name	Details
1	Dr Kamau Thugge – Chairman (Up to 24 July 2019)	Principal Secretary, the National Treasury, Republic of Kenya
2	Mr Keith Muhakanizi - Member	Permanent Secretary and Secretary to the Treasury, Ministry of Finance, Planning and Economic Development, Republic of Uganda
3	Mr Caleb Rwamuganza - Member	Permanent Secretary, Secretary to the Treasury, Ministry of Finance and Economic Planning, Republic of Rwanda
4	Mr James Doto - Member	Permanent Secretary, Ministry of Finance and Planning, United Republic of Tanzania
5	Dr Julius Muia – from 25 July 2019	Principal Secretary, the National Treasury, Republic of Kenya
6	Mr Francis N. Karuiru - Member	Private Sector Representative, Republic of Kenya
7	Mrs Khadija I. Simba - Member	Private Sector Representative, United Republic of Tanzania
8	Mr Mbundu Faustin - Member	Private Sector Representative, Republic of Rwanda
9	Mr. James Tumusiime - Member	Private Sector Representative, Republic of Uganda
10	Mr Trevor De Kock – Member (Up to September 2018)	African Development Bank – Class B shareholders Representative
11	Dr. Abdu Mukhtar – Member (from September 2018)	African Development Bank - Class B shareholders Representative
12	Ms Vivienne Yeda - Member	Director General, East African Development Bank

c) Advisory Panel

The Advisory panel is comprised of eminent personalities with extensive experience in international and development financing and they advise the Bank on best practises and effective strategies to pursue. The current members of the Advisory panel are:

Members of the Advisory Panel

	Name	Details
1	Mr Mahesh K. Kotecha	Former Managing Director Capital Markets Assurance Corporation, New York and Capital Markets Assurance Corporation, Asia and former Managing Director of Mbia Insurance Corporation
2	Mr Toyoo Gyohten	President, Institute for International Monetary Affairs, Japan and Senior Adviser, Bank of Tokyo, Mitsubishi Limited
3	Mr Lars Ekengren	Former Deputy Director General, SIDA
4	Mr Jannik Lindbaek	Former Executive Vice president and CEO of the International Finance Corporation (IFC)

7. Capital and Shareholding

The Bank's Authorised Share capital is USD 2,160,000,000 comprised of 160,000 shares with a par value of USD 13,500 each. The authorized shares are classified into Class A shares (144,000) which are available for subscription to only member states and in equal proportion and Class B (16,000) which are available for subscription to members other than member states.

The paid up share capital amounted to USD 189,823,500 comprised of 12,280 Class A shares valued at USD 165,780,000 and 1,781 class B shares valued at USD 24,043,500.
The shareholders at the end of year were as follows:

Bank's Shareholders

Name	2018 and 2017		
	Shares	Value	%
Class A		**USD'000**	
Government of Kenya	3,800	51,300	27.03%
Government of the United Republic of Tanzania	3,343	45,130	23.77%
Government of Uganda	3,800	51,300	27.03%
Government of Rwanda	1,337	18,050	9.51%
Total Class A	**12,280**	**165,780**	**87.33%**
Class B			
African Development Bank	1,240	16,740	8.82%
FMO – Netherlands	375	5,062	2.67%
DEG – Germany	100	1,350	0.71%
Yugoslavia Consortium	28	378	0.20%
SBIC - Africa Holdings	24	324	0.17%
Commercial Bank of Africa	5	68	0.04%
Nordea Bank Sweden	5	68	0.04%
Standard Chartered Bank	2	27	0.01%
Barclays Bank Plc., London	2	27	0.01%
Total Class B	**1,781**	**24,044**	**12.67%**
Total Class A & B	**14,061**	**189,824**	**100%**

DIRECTORS' REPORT (continued)

8. Financial Performance

The Bank remained strong during the year and the credit rating agencies (the Moodys and Global Credit Rating) confirmed the Bank's investment grade rating with stable outlook.

The Moodys rating report released in July 2018 re-affirmed the Bank's Baa3 rating with stable outlook sighting, among other things, '*the Bank's strong capital and liquidity balanced against the low average credit quality of its shareholders and concentration risk of its loan portfolio*'.

On the other hand the Global Credit Rating report released in November 2018 also re-affirmed the Bank's BB+ rating with stable outlook sighting, among other things, '*a strong financial profile balancing a concentrated funding structure with a very strong liquidity position, very strong capital and leverage, and a moderate risk position*'.

More importantly, the Bank continued to register solid performance with yet another year with profitable results despite a slight fall in profitability and total assets due to the operating environment which limited the growth of its lending program.

The financial results of the Bank are summarised below and are contained in full on pages 20-95*.

Performance highlights

Performance Measure	2018 USD'000	2017 USD'000	Change USD'000	% Change
Net operating income	15,377	18,023	(2,646)	(15%)
Operating expenses	8,871	7,495	(1,061)	14%
Profit before income tax	**6,506**	**10,213**	**(3,707)**	**(36%)**
Total assets	366,832	390,411	(23,579)	(6%)
Net loans	156,444	190,025	(33,581)	(18 %)
Equity	256,153	261,360	(5,207)	(2 %)
Return on Assets	1.77%	2.62%	(0.84%)	(32 %)
Return on Equity	2.54%	3.91%	(1.37 %)	(35 %)

** This corresponds to pages 65-141 in this Annual Report.*

DIRECTORS' REPORT (continued)

9. Cash flow and Liquidity Management

The Bank places significant importance on liquidity management and the detailed liquidity risk management report is contained on note 35 (c).

There was net cash inflow during the year as a result of positive generation from operating activities as well as investing activities the sum of which surpassed cash outflow in financing activities. Cash generation from operations amounted to USD 27.30 million compared to USD 2.07 million in 2017 mainly due to higher collection from loans and lower new disbursements.

Cash flow from investing activities amounted to USD 6.00 million compared to USD 3.37 million as a result of maturing placements with commercial Banks.

On the other hand, there was a net cash outflow of USD 18.18 million on financing activities compared to USD 15.34 million in 2017 as a result of higher repayments from previous borrowings.

During the year the Bank maintained adequate liquidity and the actual liquidity ratio at the end of 2018 was 4.00 times compared to 3.14 in 2017 and both are above the target ratio of 1.33 times.

10. Market overview

During the year the Bank's operating environment was characterised by slow growth of credit as well as high non-performing loans. This was more evident in Kenya and Tanzania. This forced the Bank to adopt a prudent approach and made very few new disbursements out of the approved facilities which, as a result of continued collections from the existing loan portfolio led to net decline in the loan portfolio.

According to the International Monetary Fund (IMF)'s world economic update for July 2019, the global economic growth is estimated at 3.6% which is lower than 3.8% recorded in 2017. The same report forecasts 2019 growth to slow down further to 3.2% sighting escalation in trade tension, uncertainties around Brexit and China slowdown.

The IMF's economic outlook for sub-Saharan Africa estimates the economy to have grown at 3.1% in 2018 but expects the growth to improve to 3.4% in 2019.

On the other hand the African Development Bank (AfDB)'s African Economic Outlook for 2019 estimates growth in African economies in 2018 at 3.5%, about the same level in 2017 and project it to grow at 4% in 2019.

The report estimate East Africa GDP growth at 5.7% and consider it to be the highest growing region in the continent. The report projects growth in East Africa to improve to 5.9% in 2019.

DIRECTORS' REPORT (continued)

10. Market overview (continued)

Overall conclusion is that there is positive trend in the region indicating recovery from slow down and growth of credit both of which are important elements for the Bank's successful operations.

11. Future Plans

The Bank's core strategy remains the promotion of the social economic growth in member states. The positive economic indicators in the member states provide a conducive environment for growth.

It can be noted that all member states have ambitious plans in infrastructure development as well as industrialization agenda and the Bank views these as growth opportunities in its loan portfolio. Intervention in promotion of small and medium enterprises and in the offering of social services, notably education, health and housing will feature prominently in the Bank's agenda.

The Bank will continue to mobilize appropriately priced credit facilities in order to fund the growth of operations in the member states, building on the good progress registered so far.

In order to maintain its investment grade rating the Bank will continue to improve its risk management strategies to ensure that the pursuit of growth does not in any way compromise its good risk management record.

The Bank will continue to engage key stakeholders with a view to build effective and efficient alliances to facilitate growth of its projects in the region.

12. Risk and Risk Management

The Bank has robust risk management program documented in its Enterprise-wide risk management policy.

The Bank adopts three pillars risk management philosophy where business units act as first line of defence with risk champions in each risk taking department taking leading roles. Risk and Compliance function act as the second line of defence and co-ordinate organization-wide risk management with periodic risk management reports to the Board. Audit function independently assess effectiveness of the Bank's risk management and recommend improvements. Detailed risk management activities are contained on Note 35.

DIRECTORS' REPORT (continued)

13. Solvency

The Board of Directors confirm that the financial statements have been prepared based on the International Financial Reporting Standards and that they have been prepared on going concern basis. The Board is confident that the Bank has all necessary resources to continue operating on this basis for a foreseeable future.

14. Resources

The Bank is endowed with immense resources enabling it to operate efficiently and they are expected to continue being available to support the operations.

The resources which the Bank prides in include its motivated and highly skilled human capital. This is the bedrock of the Bank's performance and more efforts will be deployed to ensure that staff are well equipped to continue delivering on the Bank's mandate.

In addition, the Bank has a modern technology operating platform which facilitates operations across the region. The Bank will continue to improve and enhance its technology platform while at the same time making sure that required risk management safeguards are implemented to avoid disruptions.

The Bank also takes pride in its very committed shareholders who, in addition to provision of the capital, stand ready to provide even more resources through their callable capital commitments which at the end of the 2018 stood at USD 842,899,500. Efforts will continue to be made to ensure that delivery is made to their expectations at all times.

15. Employee Welfare

Employees are the most important resource of the Bank and therefore deliberate efforts are made to maintain harmonious relationship in order to improve performance.

The Bank ensures that employees are well remunerated based on their actual performance and results achieved. The Bank operates a defined contribution retirement benefit scheme to which employees contribute 10% of their basic salary and the Bank contributes 10%, 12.5% or 15% of the employee's basic salary depending on the length of service. The scheme is independently managed by a professional fund manager who provides periodic reports to a committee nominated by staff.

The Bank also makes contribution to the statutory pension schemes for the employees.

The Bank provides medical insurance cover for employees, their spouses and up to four qualifying dependants through a reputable medical insurance provider. Continuous monitoring on the services offered by the insurance cover is undertaken to guarantee quality service is provided to staff.

DIRECTORS' REPORT (continued)

15. Employee Welfare (continued)

The Bank also provide continuous training to staff in various, need driven areas, to ensure that their performance is improved. The Bank will continue to innovate and improve staff welfare.

The Bank is an equal employer and staff are offered equal opportunities based on their merits and not based on gender, disability or any similar attributes.

16. Related Party Transactions

The Bank's related party transactions are concluded at arm's length basis. Details of related party transactions at the end of the year are shown on Note 39.

17. Social and Environmental controls

The Bank is an ardent advocate of sustainable development and ensures that all its projects do not negatively affect the people aimed to benefit or their environment.

The Bank's Environmental and Social policy provides guidance on day to day operations to ensure that safeguards are provided in all financed projects. Periodic reports are provided as part of monitoring process to assess the potential social or environmental impact.

The Bank does not finance projects with potential impact to environment before environmental impact assessment report approved by competent authorities in member states is submitted showing their support for the project.

18. Stakeholders

Cordial relationship was maintained with all key stakeholders including shareholders, fund providers, customers, employees, service providers and the public at large. The Bank values contribution and support of all its stakeholders and implement strategies to assess the stakeholders expectations and how they will be met. The Bank will continue to actively engage with its stakeholders with the view to improve the value creation process.

19. Dividends

The Directors do not recommend the payment of dividends for the year (2017: Nil). This is in line with shareholders' strategy to build up the capital of the Bank.

DIRECTORS' REPORT (continued)

20. Events after reporting date

There are no any events after the reporting period that warrant reporting.

21. Auditor

The current Bank's external auditor, PricewaterhouseCoopers Certified Public Accountants, has indicated willingness to continue in office. Appointment of the auditor for the year ending 31 December 2019 will be done by the Governing council in accordance with article 2 (d) of the charter.

By order of the Board

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Chairman – Board of Directors	**Director**
30-12-19	30/12/2019
------------------------------	------------------------------
Date	**Date**

STATEMENT OF DIRECTORS' RESPONSIBILITIES

The Charter requires the Directors to prepare financial statements for each financial year which give a true and fair view of the financial position of the Bank at the end of the financial year and its financial performance for the year then ended. The Directors are responsible for ensuring that the Bank keeps proper accounting records that are sufficient to show and explain the transactions of the Bank; disclose with reasonable accuracy at any time the financial position of the Bank; and that enables them to prepare financial statements of the Bank that comply with prescribed financial reporting standards and the requirements of the Charter. They are also responsible for safeguarding the assets of the Bank and for taking reasonable steps for the prevention and detection of fraud and other irregularities.

The Directors accept responsibility for the preparation and presentation of these financial statements in accordance with International Financial Reporting Standards and in the manner required by the Charter. They also accept responsibility for:

(i) Designing, implementing and maintaining internal control as they determine necessary to enable the preparation of financial statements that are free from material misstatements, whether due to fraud or error;

(ii) Selecting suitable accounting policies and then apply them consistently; and

(iii) Making judgements and accounting estimates that are reasonable in the circumstances.

In preparing the financial statements, the Directors have assessed the Banks's ability to continue as a going concern and disclosed, as applicable, matters relating to the use of going concern basis of preparation of the financial statements. Nothing has come to the attention of the Directors to indicate that the Bank will not remain a going concern for at least the next twelve months from the date of this statement.

The Directors acknowledge that the independent audit of the financial statements does not relieve them of their responsibility.

Approval of the financial statements

The financial statements were approved by the Board of Directors on 5th August 2019 and the Governing Council on 20th December 2019 and were signed on their behalf by:

Chairman – Board of Directors : ______________________

Director General : ______________________

pwc

REPORT OF THE INDEPENDENT AUDITOR TO THE MEMBERS OF EAST AFRICAN DEVELOPMENT BANK

REPORT ON THE AUDIT OF THE FINANCIAL STATEMENTS

Our opinion

In our opinion, the financial statements give a true and fair view of the state of the financial affairs of East African Development Bank ("the Bank") as at 31 December 2018, and of its profit and its cash flows for the year then ended in accordance with International Financial Reporting Standards.

What we have audited

The financial statements of East African Development Bank set out on pages 20 to 95* comprise:

- the statement of financial position as at 31 December 2018;
- the statement of comprehensive income for the year then ended;
- the statement of changes in equity for the year then ended;
- the statement of cash flows for the year then ended; and
- notes to the financial statements, which include a summary of significant accounting policies.

Basis for opinion

We conducted our audit in accordance with International Standards on Auditing ("ISAs"). Our responsibilities under those standards are further described in the Auditor's responsibilities for the audit of the financial statements section of our report.

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

Independence

We are independent of the Bank in accordance with the International Ethics Standards Board for Accountants' Code of Ethics for Professional Accountants ("the IESBA Code"). We have fulfilled our other ethical responsibilities in accordance with the IESBA Code.

** This corresponds to pages 65-141 in this Annual Report.*

pwc

REPORT OF THE INDEPENDENT AUDITOR TO THE MEMBERS OF EAST AFRICAN DEVELOPMENT BANK (continued)

REPORT ON THE AUDIT OF THE FINANCIAL STATEMENTS (CONTINUED)

Key audit matter

A key audit matter is one that, in our professional judgment, was of most significance in our audit of the financial statements of the current period. This matter was addressed in the context of our audit of the Bank's financial statements as a whole, and in forming our opinion thereon, and we do not provide a separate opinion on this matter.

Key audit matter	How our audit addressed the key audit matter
Impairment of loans and advances to customers	**Our audit procedures are summarised as follows:**
The Bank made provisions for expected credit losses on loans and advances of USO 3 million at 31 December 2018 (1 January 2018: USO 19 million) and a first-time adoption adjustment to retained earnings of USO 12 million as at 1 January 2018. In arriving at the expected credit loss as at 1 January 2018, The Directors have taken into account substantial negative developments on certain key borrowers resulting in significant additional provisions as of that date. We refer you to Note 16 of the financial statements for further information. The Directors exercised significant judgment in estimating expected credit losses over the remaining lifetime of loans and advances whose credit risk increased significantly since origination and loans in default; and, for the next 12 months for all other loans and advances.	We evaluated the appropriateness of the methodology applied by management in the estimation of expected credit losses for consistency with IFRS 9; We tested , on a sample basis , the reasonableness of PDs used by management and the accuracy of the underlying historical data applied by management in deriving PDs; We tested, on a sample basis the reasonableness of EAD for both on and off-balance sheet items; We tested, on a sample basis, the reasonableness of the present values of expected future cash flows of loans and advances used by management in the estimation of LGD;

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REPORT OF THE INDEPENDENT AUDITOR TO THE MEMBERS OF EAST AFRICAN DEVELOPMENT BANK (continued)

REPORT ON THE AUDIT OF THE FINANCIAL STATEMENTS (CONTINUED)

Key audit matter (continued)

Key audit matter	How our audit addressed the key audit matter
Impairment of loans and advances to customers	**Our audit procedures are summarised as follows:**
Specifically , significant judgement has been exercised in: • defining both default and significant increase in credit risk, based on quantitative and qualitative factors; and • estimating probabilities of default ("PD"), loss given default ("LGD") and exposure at default ("EAD") over the relevant period being either 12 months or remaining lifetime of the relevant loans and advances.	We recomputed , on a sample basis, expected credit losses for loans and advances and assessed the overall reasonableness of provisions for loans and advances made by management as at 1 January and 31 December 2018, also focused on the following : • The appropriateness of the methodology used to estimate the components of expected credit losses , being PD, LGD and EAD for consistency with I FRS 9; • the relevance and application of historical and forward-looking data used to estimate probabilities of default; • the reasonableness of the timing and amount of the present value of expected future cash flows on loans and advances , which is the key driver for LGD; and • the estimates made by management in deriving EAD for on and off We assessed the reasonableness of additional provisions made as at 1 January 2018 on first time adoption of IFRS 9 for compliance with the standard with specific reference to forward looking information incorporated into ECL calculations by management in respect of major developments on certain key borrowers.

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REPORT OF THE INDEPENDENT AUDITOR TO THE MEMBERS OF EAST AFRICAN DEVELOPMENT BANK (continued)

REPORT ON THE AUDIT OF THE FINANCIAL STATEMENTS (CONTINUED)

Other information

The Directors are responsible for the other information. The other information comprises the information included in the annual report but does not include the financial statements and our auditor's report thereon.

Our opinion on the financial statements does not cover the other information and we do not express any form of assurance conclusion thereon. In connection with our audit of the financial statements, our responsibility is to read the other information identified above and, in doing so, consider whether the other information is materially inconsistent with the financial statements or our knowledge obtained in the audit, or otherwise appears to be materially misstated.

If, based on the work we have performed, we conclude that there is a material misstatement of this other information, we are required to report that fact. We have nothing to report in this regard.

Responsibilities of the Directors for the financial statements

The Directors are responsible for the preparation of financial statements that give a true and fair view in accordance with International Financial Reporting Standards and in the manner required by the Treaty and Charter of the East African Development Bank ("the Bank's Charter"), and for such internal control as the Directors determine is necessary to enable the preparation of financial statements that are free from material misstatement, whether due to fraud or error.

In preparing the financial statements, the Directors are responsible for assessing the ability of the Bank to continue as a going concern, disclosing, as applicable, matters related to going concern and using the going concern basis of accounting unless the Directors either intend to liquidate the Bank or to cease operations, or have no realistic alternative but to do so.

The Directors are responsible for overseeing the financial reporting process.

Auditor's responsibilities for the audit of the financial statements

Our objectives are to obtain reasonable assurance about whether the financial statements as a whole are free from material misstatement, whether due to fraud or error, and to issue an auditor's report that includes our opinion.

REPORT OF THE INDEPENDENT AUDITOR TO THE MEMBERS OF EAST AFRICAN DEVELOPMENT BANK (continued)

REPORT ON THE AUDIT OF THE FINANCIAL STATEMENTS (CONTINUED)

Auditor's responsibilities for the audit of the financial statements (Continued)

Reasonable assurance is a high level of assurance, but is not a guarantee that an audit conducted in accordance with ISAs will always detect a material misstatement when it exists.

Misstatements can arise from fraud or error and are considered material if, individually or in the aggregate, they could reasonably be expected to influence the economic decisions of users taken on the basis of these financial statements.

As part of an audit in accordance with ISAs, we exercise professional judgement and maintain professional scepticism throughout the audit. We also:

- Identify and assess the risks of material misstatement of the financial statements, whether due to fraud or error, design and perform audit procedures responsive to those risks, and obtain audit evidence that is sufficient and appropriate to provide a basis for our opinion. The risk of not detecting a material misstatement resulting from fraud is higher than for one resulting from error, as fraud may involve collusion, forgery, intentional omissions, misrepresentations, or the override of internal control.

- Obtain an understanding of internal control relevant to the audit in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the internal control.

- Evaluate the appropriateness of accounting policies used and the reasonableness of accounting estimates and related disclosures made by the Directors.

- Conclude on the appropriateness of the Directors' use of the going concern basis of accounting and, based on the audit evidence obtained, whether a material uncertainty exists related to events or conditions that may cast significant doubt on the ability to continue as a going concern. If we conclude that a material uncertainty exists, we are required to draw attention in our auditor's report to the related disclosures in the financial statements or, if such disclosures are inadequate, to modify our opinion. Our conclusions are based on the audit evidence obtained up to the date of our auditor's report. However, future events or conditions may cause the Bank to cease to continue as a going concern.

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REPORT OF THE INDEPENDENT AUDITOR TO THE MEMBERS OF EAST AFRICAN DEVELOPMENT BANK (continued)

REPORT ON THE AUDIT OF THE FINANCIAL STATEMENTS (CONTINUED)

Auditor's responsibilities for the audit of the financial statements (Continued)

- Evaluate the overall presentation, structure and content of the financial statements, including the disclosures, and whether the financial statements represent the underlying transactions and events in a manner that achieves fair presentation.

We communicate with the Directors regarding, among other matters, the planned scope and timing of the audit and significant audit findings, including any significant deficiencies in internal control that we identify during our audit.

From the matters communicated with the Directors, we determine those matters that were of most significance in the audit of the financial statements of the current period and are therefore the key audit matters. We describe these matters in our auditor's report unless law or regulation precludes public disclosure about the matter or when, in extremely rare circumstances, we determine that a matter should not be communicated in our report because the adverse consequences of doing so would reasonably be expected to outweigh the public interest benefits of such communication.

The engagement partner on the audit resulting in this independent auditor's report is CPA Uthman Mayanja – P0181.

PricewaterhouseCoopers

Certified Public Accountants
Kampala
10 January 2020

CPA Uthman Mayanja

Statement of Comprehensive Income

	Notes	2018 USD'000	2017 USD'000
Interest income	3	**21,537**	24,831
Interest expense	4	**(6,370**	(8,555)
Net interest income		**15,167**	16,276
Fee and commission income	5	**424**	581
Other operating income	6	**2,967**	3,884
Other gains/(losses)	7	**(111**	(12)
Net fair value gain on investment property	20	**(261**	4
Net operating income		**18,186**	20,733
Credit impairment losses	16(a)	**(2,809**	(2,711)
Operating income after impairment charges		**15,377**	18,022
Employee benefits expense	8	**(3,690**	(3,591)
Depreciation and amortization	10	**(775**	(770)
Other operating expenses	9	**(4,406**	(3,448)
Profit before income tax	10	**6,506**	10,213
Income tax expense	11	**-**	-
Profit for the year		**6,506**	10,213
Other Comprehensive income		-	-
Total comprehensive income		**6,506**	10,213
Earnings per share – basic and diluted (Expressed in USD per share)	12	**463**	726

Statement of financial position

	Notes	2018 USD'000	2017 USD'000
Assets			
Cash at Bank	13	**10,867**	14,006
Placements with commercial banks	14	**165,519**	151,974
Investment securities held to maturity	15	**-**	70
Loans and lease receivables	16	**156,444**	190,025
Equity investments	18	**1,273**	436
Other assets	19	**565**	775
Property and equipment	21	**13,111**	13,767
Investment property	20	**18,873**	19,134
Intangible assets	22	**180**	224
Total assets		**366,832**	390,411
Liabilities			
Other liabilities	23	**6,719**	5,790
Borrowings	24	**91,458**	109,518
Special funds	25	**3,990**	3,990
Grants	26	**1,033**	2,274
Capital fund	28	**7,479**	7,479
Total liabilities		**110,679**	129,051
Capital and reserves			
Share capital	27	**189,824**	189,824
Share premium	27	**3,874**	3,874
Funds waiting allotment	29	**83**	83
Special reserve	30	**12,507**	12,443
Fair value reserve	31	**525**	455
Revaluation reserves	33	**7,901**	7,939
Retained earnings		**41,439**	46,742
Total shareholders' equity		**256,153**	261,360
Total shareholders' equity and liabilities		**366,832**	390,411

The financial statements set out on pages 20 to 95* were approved by the Board of Directors on 5th August 2019 and the Governing Council on 20th December 2019 and were signed on their behalf by:

Chairman – Board of Directors: ____________ **Director General:** ____________

** This corresponds to pages 65-141 in this Annual Report.*

Statement of Changes in Equity

Year ended 31 December 2017	Notes	Share capital USD '000	Share pre-mium USD '000	Special reserves USD '000	Funds awaiting allotment USD '000	Fair value reserve USD '000	Retained earnings USD '000	Revaluation reserve USD '000	Total equity USD '000
At start of year		**189,824**	**3,874**	**12,358**	**103**	**505**	**36,523**	**7,980**	**251,167**
Comprehensive income									
Profit for the year		-	-	-	-	-	10,213	**-**	**10,213**
Other comprehensive income		-	-	-	-	-	-	-	**-**
Total comprehensive income		-	-	-	-	-	10,213	-	**10,213**
Transactions with owners									
Transfer to special reserve	30	-	-	85	-	-	(85)	-	**-**
Reclassification to special funds/capital and grants	29	-	-	-	(20)	-	-	-	**(20)**
Revaluation reserve	33	-	-	-	-	-	41	(41)	**-**
Transfer to fair value reserve	31	-	-	-	-	(50)	50	-	-
At end of year		**189,824**	**3,874**	**12,443**	**83**	**455**	**46,742**	**7,939**	**261,360**
Year ended 31 December 2018									
At start of year as previously stated		189,824	3,874	12,443	83	455	46,742	7,939	261,360
Changes on initial application of IFRS 9	16a	-	-	-	-	-	(11,713)	-	(11,713)
									-
At start of year as restated		189,824	3,874	12,443	83	455	35,029	7,939	249,647
Comprehensive income									
Profit for the year		-	-	-	-	-	6,506	**-**	**6,506**
Other comprehensive income		-	-	-	-	-	-	**-**	**-**
Total comprehensive income		**-**	**-**	**-**	**-**	**-**	**6,506**	**-**	**6,506**

Statement of Changes in Equity (continued)

	Notes	Share capital	Share premium	Special reserves	Funds awaiting allotment	Fair value reserve	Retained earnings	Revaluation reserve	Total equity
		USD '000	**USD '000**	**USD '000**	**USD '000**	**USD '000**	**USD '000**	**USD '000**	**USD '000**
Transactions with owners									
Transfer to special reserve	30	-	-	64		-	(64)		
Transfer from the revaluation reserve	33	-	-	-	-	-	38	(38)	
Transfer to fair value reserve	31	-	-	-	-	70	(70)	-	
At end of year		**189,824**	**3,874**	**12,507**	**83**	**525**	**41,439**	**7,901**	**256,153**

Statement of cash flows

Statement of cash flows	Note	2018 USD'000	2017 USD'000
Cash flows from operating activities			
Interest receipts		**18,781**	20,095
Interest payments	24	**(5,710)**	(7,584)
Net fee and commission receipts		**446**	256
Other income received		**664**	632
Payments to employees and suppliers		**(7,387)**	(6,989)
Cash outflows from operating activities		**6,794**	6,410
Net change in loans and advances		**20,056**	(5,848)
Net other receipts from customers		**986**	2,456
Settlement of other liabilities		**(538)**	(951)
Net cash generated from operating activities		**27,298**	2,067
Investing activities			
Purchase of property and equipment	20 & 21	**(46)**	(90)
Purchase of computer software	22	**(29)**	(72)
Placements with commercial Banks		**6,079**	3,534
Net cash used in investing activities		**6,004**	3,372
Financing activities			
Settlement of medium and long term borrowings		**(19,922)**	(30,580)
Proceeds from borrowings	24	**1,744**	15,237
Net cash generated from financing activities		**(18,178)**	(15,343)
Net increase in cash and cash equivalents		**15,124**	(9,904
Cash and cash equivalent at the start of the year		**159,326**	169,357
Foreign exchange losses		**(281)**	(127)
At end of year	**32**	**174,169**	159,326

NOTES

1. Reporting entity

East African Development Bank (the "Bank") is a regional Bank established under the Bank's Charter of 1980 with its current membership comprising the four East African Countries of Uganda, Kenya, Tanzania and Rwanda with its head office in Kampala, Uganda. The Bank is primarily involved in development finance lending and the provision of related services as stipulated under its Charter.

The Bank's principal office address is:
Plot 4 Nile Avenue
EADB Building
P. O. Box 7128
Kampala, Uganda

For purposes of the Bank's Charter, the profit and loss statement is represented by the statement of comprehensive income and the balance sheet by the statement of financial position in these financial statements.

2. Principal accounting policies

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

A) Basis of preparation

The Bank's financial statements have been prepared in accordance with International Financial Reporting Standards ("IFRS"). Additional information required by the Charter is included where appropriate. The financial statements have been prepared under the historical cost convention, except where otherwise stated in these accounting policies. The financial statements have been presented in United States dollars rounded off to the nearest thousand (USD '000).

The preparation of financial statements in conformity with IFRS requires the use of certain critical accounting estimates. It also requires the Directors to exercise judgement in the process of applying the Bank's accounting policies. Changes in assumptions may have a significant impact on the financial statements in the period the assumptions are changed. The areas involving a higher degree of judgement or complexity, or areas where assumptions and estimates are significant to the financial statements are disclosed in Note 34.

NOTES (Continued)

2. Principal accounting policies (continued)

B) Changes in accounting policy and disclosures

(I) New and amended standards adopted by the Bank

(i) IFRS 9: Financial Instruments

The Bank has adopted IFRS 9 as issued by the IASB in July 2014 with a date of transition of 1 January 2018, which resulted in changes in accounting policies and adjustments to the amounts previously recognized in the financial statements.

The Bank did not early adopt any of IFRS 9 in previous periods. As permitted by the transitional provisions of IFRS 9, the Bank elected not to restate comparative figures.
Any adjustments to the carrying amounts of the financial assets at the date of transition were recognised in opening retained earnings of the current period. Further details on the transition adjustment are described in more detail under Note 2 (i(b)).

Consequently, for notes disclosures, the consequential amendments to IFRS 7 disclosures have also only been applied to the current period. The adoption of IFRS 9 has resulted in changes in our accounting policies for recognition, classification and measurement of financial assets and financial liabilities and impairment of financial assets. IFRS 9 also significantly amends other standards dealing with financial instruments such as IFRS 7 'Financial Instruments: Disclosures'.

Set out below are disclosures relating to the impact of the adoption of IFRS 9 on the Bank. Further details of the specific IFRS 9 accounting policies applied in the current period (as well as the previous IAS 39 accounting policies applied in the comparative period) are described in more detail under (j) financial assets and liabilities.

(a) Classification and measurement of financial instruments

The measurement category and the carrying amount of financial assets and liabilities in accordance with IAS 39 and IFRS 9 at 1 January 2018 are compared as follows:

Financial assets	Measurement category under IAS 39	Carrying amount	IFRS 9 Measurement category	Carrying amount
		USD'000		USD'000
Cash at Bank	Amortized cost	14,006	Amortized cost	14,006
Placements with commercial Banks	Amortized cost	151,974	Amortized cost	151,974
Loans and lease receivables	Amortized cost	190,025	Amortized cost	178,312
Investment securities held to maturity	Amortized cost (Held to Maturity)	70	Amortized cost	70
Equity investments	Fair Value through Profit or Loss (Designated)	436	FVPL (Designated)	2,036
		356,511		**346,398**

NOTES (Continued)

2. Principal accounting policies (continued)

B) Changes in accounting policy and disclosures (continued)

(I) New and amended standards adopted by the Bank (continued)

(i) IFRS 9: Financial Instruments (Continued)

(b) Reconciliation of statement of financial position balances from IAS 39 to IFRS 9

The Bank performed a detailed analysis of its business models for managing financial assets and analysis of their cash flow characteristics. The following table reconciles the carrying amounts of financial assets and liabilities, from their previous measurement category in accordance with IAS 39 to their new measurement categories upon transition to IFRS 9 on 1 January 2018:

Financial assets	IAS 39 carrying amount at 31 December 2017	Changes in classification	IFRS 9 impairment change	IFRS 9 Carrying amount at 1 January 2018
	USD'000	USD'000	USD'000	USD'000
Cash at Bank	14,006	-	-	14,006
Placements with commercial Banks	151,974	-	-	151,974
Loans and lease receivables	190,025	-	(11,713)	178,312
Investment securities held to maturity	70	-	-	70
Equity investments	436	-	-	436
	356,511	**-**	**(11,713)**	**344,798**
Financial Liabilities				
Other Liabilities	5,790	-	-	5,790
Borrowings	109,518	-	-	109,518
	115,308	**-**	**-**	**115,308**

There have been no changes in the classification measurement basis and carrying amounts of the Banks holdings of, borrowings and other liabilities.

The table below explains the changes in the loss allowance on loans and advances to customers at amortised cost between 31 December 2017 and 1 January 2018.

	At 31 December 2017	Additional IFRS 9 Impairment allowance	At 1 January 2018
	USD'000	USD'000	USD'000
Loans and lease receivable	**7,718**	**11,713**	**19,431**

NOTES (Continued)

2. Principal accounting policies (continued)

(ii) IFRS 15

This standard replaces IAS 11: Construction Contracts, IAS 18: Revenue, IFRIC 13: Customer Loyalty Programs, IFRIC 15: Agreements for the Construction of Real Estate, IFRIC 18: Transfer of Assets from Customers and SIC-31: Revenue – Barter Transactions Involving Advertising Services.

The standard contains a single model that applies to contracts with customers and two approaches to recognising revenue: at a point in time or over time. The standard specifies how and when the Bank will recognise revenue as well as requiring such entities to provide users of financial statements with more informative, relevant disclosures.

There was no material impact of application of IFRS 15 and no adjustment to retained earnings was required.

(II) New and amended standards yet to be adopted by the Bank

(a)	IFRS 16 Leases	-	Effective date 1st January 2019
(b)	IFRS 17 Insurance Contracts	-	Effective date 1st January 2021
(c)	IFRIC 23 – Uncertainty over tax	-	Effective date 1st January 2019

IFRS 16, Leases

IFRS 16 was published in January 2016 and becomes effective on 1st January 2019. It replaces the previous leases Standard, IAS 17 Leases, and related Interpretations. The Standard sets out the principles for the recognition, measurement, presentation and disclosure of leases for both parties to a contract, i.e. the customer ('lessee') and the supplier ('lessor') and it removes the current distinction between operating and financing leases and requires recognition of an asset (the right to use the leased item) and a financial liability to pay rentals for virtually all lease contracts with an exemption for short-term and low-value leases.

The Bank is still assessing the impact of the standard and adoption will be made in the financial statements starting 1st January 2019.

NOTES (Continued)

2. Principal accounting policies (continued)

B) Changes in accounting policies and disclosures (continued)

IFRIC 23 – Uncertainty over tax

The International Accounting Standard Board (IASB) issued IFRIC Interpretation 23 – Uncertainty over Income Tax treatment on 7 June 2017 which clarifies application of recognition and measurement requirements in IAS 12 Income Taxes when there is uncertainty over income tax treatments and is effective for annual periods beginning 1st January 2019.

The adoption of the Interpretation is not expected to impact the Bank's financial statements as it only clarifies existing guidance.

IFRS 17 Insurance Contracts

IFRS 17 replaces IFRS 4 and is effective for annual periods beginning January 2021. It provides a comprehensive guidance for insurance contracts including recognition, measurement, presentation and disclosure.

The standard applies to all types of insurance contracts (i.e. life, non-life, direct insurance and re-insurance), as well as to certain guarantees and financial instruments with discretionary participation features.

C) Functional and presentation currency

Items included in the Bank's financial statements are measured using the currency of the primary economic environment in which the Bank operates ('the functional currency'). These financial statements are presented in United States Dollars (USD), which is the Bank's functional currency. Except as indicated, the financial information has been rounded off to the nearest thousand.

Assets and liabilities expressed in various currencies are translated into US Dollars at rates of exchange ruling at the statement of financial position date. Transactions during the year are converted at exchange rates ruling at the transaction date. The resulting differences from the conversion and translation of all transactions and balances are dealt with in the statement of comprehensive income in the period in which they arise.

D) Segment reporting

Operating segments are reported in a manner consistent with the internal reporting provided to the chief operating decision-maker (CODM). The CODM, which is responsible for allocating resources and assessing performance of the operating segments, has been identified as the Bank's board of Directors.

NOTES (Continued)

2. Principal accounting policies (continued)

E) Revenue recognition

(i) *Interest income and expense*

Interest income and expense for all interest-bearing financial instruments are recognised within 'interest income' or 'interest expense' respectively in the statement of comprehensive income using the effective interest method.

The effective interest method is a method of calculating the amortised cost of a financial asset or a financial liability 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 payments or receipts through the expected life of the financial instrument or, when appropriate, a shorter period to the net carrying amount of the financial asset or financial liability.

When calculating the effective interest rate, the Bank estimates cash flows considering all contractual terms of the financial instrument (for example, prepayment options) but does not consider future credit losses. The calculation includes all fees and points paid or received between parties to the contract that are an integral part of the effective interest rate, transaction costs and all other premiums or discounts.

Transaction costs are incremental costs that are directly attributable to the acquisition, issue or disposal of a financial asset or liability.

Once a financial asset or a group of similar financial assets has been written down as a result of an impairment loss, interest income is recognised using the rate of interest used to discount the future cash flows for the purpose of measuring the impairment loss.

Interest income and expense presented in the statement of comprehensive income includes interest on financial assets and liabilities at amortised cost on an effective interest rate basis.

(ii) Fees and commission income

Fees and commission income that are integral to the effective interest rate on a financial asset or liability are included in the measurement of effective interest rate.

Other fees and commission income including account servicing fees are recognized as the contractual service is performed per requirement of IRFS 15.

(iii) *Dividend income*

Dividend income is recognised when the right to receive dividends is established.

NOTES (Continued)

2. Principal accounting policies (continued)

F) Property, plant and equipment

Property, plant and equipment are stated at cost or valuation less accumulated depreciation and impairment losses. Cost includes expenditures that are directly attributable to the acquisition of the asset. The cost of self-constructed assets includes the cost of materials and direct labour, any other costs directly attributable to bringing the asset to a working condition for its intended use, and the costs of dismantling and removing the items and restoring the site on which they are located. Purchased software that is integral to the functionality of the related equipment is capitalised as part of that equipment.

Freehold land and buildings are measured at fair value less accumulated depreciation on buildings and impairment losses recognised at the date of revaluation. Valuations are performed with sufficient frequency to ensure that the fair value of a revalued asset does not differ materially from its carrying amount.

Revaluation surplus

In accordance with IAS 16, the nature of revaluation surplus results from valuation of assets with significant changes in fair value. The fair value of land and buildings is usually determined from market-based evidence by appraisal that is done by professionally qualified valuers after every three years.

Changes in fair value are recognized in other comprehensive income and accumulated in equity under revaluation surplus.

A revaluation surplus is recorded in other comprehensive income and credited to the asset revaluation reserve in equity. However, to the extent that it reverses a revaluation deficit of the same asset previously recognised in profit or loss, the increase is recognised in profit and loss. A revaluation deficit is recognised in profit or loss, except to the extent that it offsets an existing surplus on the same asset recognised in the asset revaluation reserve.

An annual transfer from the asset revaluation reserve to retained earnings is made for the difference between depreciation based on the revalued carrying amount of the asset and depreciation based on the asset's original cost.

Additionally, accumulated depreciation as at the revaluation date is eliminated against the gross carrying amount of the asset and the net amount is restated to the revalued amount of the asset. Upon disposal, any revaluation reserve relating to the particular asset being sold is transferred to retained earnings.

Management and Directors review the residual value and useful life of an asset at the year end and any change considered to be appropriate in accounting estimate is recorded through the statement of comprehensive income.

NOTES (Continued)

2. Principal accounting policies (continued)

F) Property, plant and equipment (continued)

Depreciation is calculated to write off the cost of the property and equipment on a straight-line basis over the expected useful lives of the assets concerned. The rates for depreciation used are as follows:

Buildings	5.0%
Motor vehicles	25.0%
Office equipment	10.0% - 25.0%
Furniture	12.5%

Gains and losses on disposal of property and equipment are determined by reference to their carrying amount and are taken into account in determining the result for the year

G) Intangible assets

Computer software costs which are clearly identifiable and controlled by the Bank and have probable benefits exceeding the costs beyond one year are recognised as an intangible asset. Intangible assets are stated at cost net of accumulated amortization and impairment losses.

Subsequent expenditure on software is capitalized only when it increases the future economic benefits embodied in specific assets to which it relates. All other expenditure is expensed as incurred.

Amortization is recognized in statement of comprehensive income on a straight line basis over an estimated useful life of software from the date that it is available for users. The estimated useful life of the software is four years.

H) Leases

a) Bank is the lessee

(i) Operating leases

Leases in which a significant portion of the risks and rewards of ownership are retained by another party, the lessor, are classified as operating leases. Payments, including pre-payments, made under operating leases (net of any incentives received from the lessor) are charged to profit or loss on a straight-line basis over the period of the lease. The total payments made under operating leases are charged to 'other operating expenses' on a straight-line basis over the period of the lease. When an operating lease is terminated before the lease period has expired, any payment required to be made to the lessor by way of penalty is recognised as an expense in the period in which termination takes place.

NOTES (Continued)

2. Principal accounting policies (continued)

H) Leases

• Bank is the lessee (continued)

This treatment will change once the Bank adopt IFRS 16 in 2019 which, among other things, require booking of right of use asset.

(ii) Finance leases

Leases of assets where the Bank has substantially taken all the risks and rewards of ownership are classified as finance leases. Finance leases are capitalised at the lease's commencement, at the lower of the fair value of the leased property and the present value of the minimum lease payments. Each lease payment is allocated between the liability and finance charges so as to achieve a constant rate on the finance balance outstanding. The corresponding rental obligations, net of finance charges, are included in deposits from Banks or deposits from customers depending on the counter party. The interest element of the finance cost is charged to profit or loss over the lease period so as to produce a constant periodic rate of interest on the remaining balance of the liability for each period.

• Bank is the lessor

When assets are held subject to a finance lease, the present value of the lease payments is recognised as a receivable. The difference between the gross receivable and the present value of the receivable is recognised as unearned finance income. Lease income is recognised over the term of the lease using the net investment method (before tax), which reflects a constant periodic rate of return. The leases entered into by the Bank are primarily finance leases.

I) Capital work-in-progress

Assets in the course of construction (capital work-in-progress) are not depreciated. Upon completion of the project the accumulated cost is transferred to an appropriate asset category where it is depreciated according to the policy.

J) Financial assets and liabilities

Measurement methods

Amortized cost and effective interest rate

The amortised cost is the amount at which the financial asset or financial liability is measured at initial recognition minus the principal repayments, plus or minus the cumulative amortisation using the effective interest method of any difference between that initial amount and the maturity amount and, for financial assets, adjusted for any loss allowance.

NOTES (Continued)

2. Principal accounting policies (continued)

J) Financial assets and liabilities (continued)

Measurement methods (continued)

The effective interest rate is the rate that exactly discounts estimated future cash payments or receipts through the expected life of the financial asset or financial liability to the gross carrying amount of a financial asset (i.e. its amortised cost before any impairment allowance) or to the amortised cost of a financial liability. The calculation does not consider expected credit losses and includes transaction costs, premiums or discounts and fees and points paid or received that are integral to the effective interest rate, such as origination fees.

Financial assets and financial liabilities are recognized when the entity becomes a party to the contractual provisions of the instrument. At initial recognition, the Bank measures a financial asset or financial liability at its fair value plus or minus, in the case of a financial asset or financial liability not at fair value through profit or loss, transaction costs that are incremental and directly attributable to the acquisition or issue of the financial asset or financial liability, such as fees and commissions.

Transaction costs of financial assets and financial liabilities carried at fair value through profit or loss are expensed in profit or loss. Immediately after initial recognition, an expected credit loss allowance (ECL) is recognized for financial assets measured at amortized cost and investments in debt instruments measured at FVOCI, which results in an accounting loss being recognized in profit or loss when an asset is newly originated.

When the fair value of financial assets and liabilities differs from the transaction price on initial recognition, the Bank recognises the difference as follows:

- When the fair value is evidenced by a quoted price in an active market for an identical asset or liability (i.e. a Level 1 input) or based on a valuation technique that uses only data from observable markets, the difference is recognised as a gain or loss.

- In all other cases, the difference is deferred and the timing of recognition of deferred day one profit or loss is determined individually. It is either amortised over the life of the instrument, deferred until the instrument's fair value can be determined using market observable inputs, or realised through settlement.

NOTES (Continued)

2. Principal accounting policies (continued)

J) Financial assets and liabilities (continued)

(a) Financial Assets

(i) Classification and subsequent measurement

From 1 January 2018, the Bank has applied IFRS 9 and classifies its financial assets in the following measurement categories:

- Fair value through profit or loss (FVPL);
- Fair value through other comprehensive income (FVOCI); or
- Amortized cost.

The classification requirements for debt and equity instruments are described below:

Debt instruments

Debt instruments are those instruments that meet the definition of a financial liability from the issuer's perspective, such as loans, government and corporate bonds and trade receivables purchased from clients in factoring arrangements without recourse.

Classification and subsequent measurement of debt instruments depend on:

(i) The Bank's business model for managing the asset; and
(ii) The cash flow characteristics of the asset.

Based on these factors, the Bank classifies its debt instruments into one of the following three measurement categories:

- Amortized cost: Assets that are held for collection of contractual cash flows where those cash flows represent solely payments of principal and interest ('SPPI'), and that are not designated at FVPL, are measured at amortized cost. The carrying amount of these assets is adjusted by any expected credit loss allowance recognized. Interest income from these financial assets is included in 'Interest and similar income' using the effective interest rate method.

- Fair value through other comprehensive income (FVOCI): Financial assets that are held for collection of contractual cash flows and for selling the assets, where the assets' cash flows represent solely payments of principal and interest, and that are not designated at FVPL, are measured at fair value through other comprehensive income (FVOCI). Movements in the carrying amount are taken through OCI, except for the recognition of impairment gains or losses, interest revenue and foreign exchange gains and losses on the instrument's amortized cost which are recognized in profit or loss. When the financial asset is derecognized, the cumulative gain or loss previously recognized in OCI is reclassified from equity to profit or loss and recognized in 'Net Investment income'. Interest income from these financial assets is included in 'Interest income' using the effective interest rate method.

NOTES (Continued)

2. Principal accounting policies (continued)

J) Financial assets and liabilities (continued)

- Fair value through profit or loss: Assets that do not meet the criteria for amortized cost or FVOCI are measured at fair value through profit or loss. A gain or loss on a debt investment that is subsequently measured at fair value through profit or loss and is not part of a hedging relationship is recognized in profit or loss and presented in the profit or loss statement within 'Net trading income' in the period in which it arises, unless it arises from debt instruments that were designated at fair value or which are not held for trading, in which case they are presented separately in 'Net investment income'. Interest income from these financial assets is included in 'Interest income' using the effective interest rate method.

Business model: the business model reflects how the Bank manages the assets in order to generate cash flows. That is, whether the Bank's objective is solely to collect the contractual cash flows from the assets or is to collect both the contractual cash flows and cash flows arising from the sale of assets. If neither of these is applicable (e.g. financial assets are held for trading purposes), then the financial assets are classified as part of 'other' business model and measured at FVPL.

Factors considered by the Bank in determining the business model for a group of assets include past experience on how the cash flows for these assets were collected, how the asset's performance is evaluated and reported to key management personnel, how risks are assessed and managed and how managers are compensated.

An example is the liquidity portfolio of assets, which is held by the Bank as part of liquidity management and is generally classified within the hold to collect and sell business model.

Securities held for trading are held principally for the purpose of selling in the near term or are part of a portfolio of financial instruments that are managed together and for which there is evidence of a recent actual pattern of short-term profit-taking. These securities are classified in the 'other' business model and measured at FVPL.

SPPI: Where the business model is to hold assets to collect contractual cash flows or to collect contractual cash flows and sell, the Bank assesses whether the financial instruments' cash flows represent solely payments of principal and interest (the 'SPPI test'). In making this assessment, the Bank considers whether the contractual cash flows are consistent with a basic lending arrangement i.e. interest includes only consideration for the time value of money, credit risk, other basic lending risks and a profit margin that is consistent with a basic lending arrangement. Where the contractual terms introduce exposure to risk or volatility that are inconsistent with a basic lending arrangement, the related financial asset is classified and measured at fair value through profit or loss.

NOTES (Continued)

2. Principal accounting policies (continued)

J) Financial assets and liabilities (continued)

Financial assets with embedded derivatives are considered in their entirety when determining whether their cash flows are solely payment of principal and interest.

The Bank reclassifies debt investments when and only when its business model for managing those assets changes. The reclassification takes place from the start of the first reporting period following the change. Such changes are expected to be very infrequent and none occurred during the period.

Equity instruments

Equity instruments are instruments that meet the definition of equity from the issuer's perspective; that is, instruments that do not contain a contractual obligation to pay and that evidence a residual interest in the issuer's net assets. Examples of equity instruments include basic ordinary shares.

The Bank subsequently measures all equity investments at fair value through profit or loss, except where the Bank management has elected, at initial recognition, to irrevocably designate an equity investment at fair value through other comprehensive income. The Bank policy is to designate equity investments as FVOCI when those investments are held for purposes other than to generate investment returns. When this election is used, fair value gains and losses are recognised in OCI and are not subsequently reclassified to profit or loss, including on disposal. Impairment losses (and reversal of impairment losses) are not reported separately from other changes in fair value.

Dividends, when representing a return on such investments, continue to be recognised in profit or loss as other income when the Bank's right to receive payments is established. Gains and losses on equity investments at FVPL are included in the Net trading income line in the statement of profit or loss.

(ii) Impairment

The Bank assesses on a forward-looking basis the expected credit losses associated with its debt instrument assets carried at amortised cost and FVOCI and with the exposure arising from loan commitments and financial guarantee contracts.

The Bank recognises a loss allowance for such losses at each reporting date. The measurement of ECL reflects:

- An unbiased and probability-weighted amount that is determined by evaluating a range of possible outcomes;
- The time value of money; and

NOTES (Continued)

2. Principal accounting policies (continued)

J) Financial assets and liabilities (continued)

***(ii) Impairment** (continued)*

- Reasonable and supportable information that is available without undue cost or effort at the reporting date about past events, current conditions and forecasts of future economic conditions.

Previous accounting policy for impairment

At each statement of financial position date the Bank assesses whether there is objective evidence that financial assets not carried at fair value through profit or loss are impaired. Financial assets are impaired when objective evidence demonstrates that a loss event has occurred after the initial recognition of the asset, and that the loss event has an impact on the future cash flows on the asset that can be estimated reliably.

The Bank considers evidence of impairment at both a specific asset and collective level. All individually significant financial assets are assessed for specific impairment. All significant assets found not to be specifically impaired are then collectively assessed for any impairment that has been incurred but not yet identified. Assets that are not individually significant are then collectively assessed for impairment by grouping together financial assets (carried at amortised cost) with similar risk characteristics.

In assessing collective impairment, the Bank determines a loss ratio using historical financial information. Loss ratio is determined as total impairment as a fraction of total loans and lease receivables. This loss ratio maybe adjusted depending on management's judgement of the current economic and credit conditions. The loss ratio is then applied to those loans and lease receivables that have not been assessed for specific impairment.

Impairment losses on assets carried at amortised cost are measured as the difference between the carrying amount of the financial assets and the present value of estimated future cash flows discounted at the assets' original effective interest rate. Losses are recognised in the statement of comprehensive income and reflected in an allowance account against loans and advances. Interest on the impaired asset continues to be recognised through the unwinding of the discount.

When a subsequent event causes the amount of impairment loss to decrease, the impairment loss is reversed through the statement of comprehensive income.

Loans and advances are shown at gross amount adjusted for any provision for impairment losses. A provision for loan impairment is established if there is objective evidence that the Bank will not be able to collect all amounts due according to the original contract terms of the loans. The amount of the provision is the difference between the carrying amount and the estimated recoverable amount. When a loan is deemed uncollectible, it is written off against the related provision for impairment. Subsequent recoveries are credited to the provision for loan losses in the statement of comprehensive income.

NOTES (Continued)

2. Principal accounting policies (continued)

J) Financial assets and liabilities (continued)

(iii) Modification of loans

As a long term lender, it is not unusual for the Bank to renegotiate or otherwise modify the contractual cash flows of loans to customers. When this happens, the Bank assesses whether or not the new terms are substantially different to the original terms. The Bank does this by considering, among others, the following factors:

- If the borrower is in financial difficulty, whether the modification merely reduces the contractual cash flows to amounts the borrower is expected to be able to pay.
- Whether any substantial new terms are introduced, such as a profit share/ equity-based return that substantially affects the risk profile of the loan.
- Significant extension of the loan term when the borrower is not in financial difficulty.
- Significant change in the interest rate.
- Change in the currency the loan is denominated in.
- Insertion of collateral, other security or credit enhancements that significantly affect the credit risk associated with the loan.

If the terms are substantially different, the Bank derecognises the original financial asset and recognizes a 'new' asset at fair value and recalculates a new effective interest rate for the asset. The date of renegotiation is consequently considered to be the date of initial recognition for impairment calculation purposes, including for the purpose of determining whether a significant increase in credit risk has occurred. However, the Bank also assesses whether the new financial asset recognised is deemed to be credit-impaired at initial recognition, especially in circumstances where the renegotiation was driven by the debtor being unable to make the originally agreed payments. Differences in the carrying amount are also recognised in profit or loss as a gain or loss on derecognition.

If the terms are not substantially different, the renegotiation or modification does not result in derecognition, and the Bank recalculates the gross carrying amount based on the revised cash flows of the financial asset and recognises a modification gain or loss in profit or loss.

NOTES (Continued)

2. Principal accounting policies (continued)

J) Financial assets and liabilities (continued)

(iv) Derecognition other than modification

Financial assets, or a portion thereof, are de-recognised when the contractual rights to receive the cash flows from the assets have expired, or when the Bank assesses that the possibility for such cash flow is remote especially when a loan remain in non-performing category for long period without being turned around successfully.

In most cases the Bank continues to follow up for repayments and when cash flows can be ascertained with reasonable degree of certainty then recognition of the expected cash flow is included in the financial statements. In other cases recognition is made when actual collection happens.

(b) Financial liabilities

(i) Classification and subsequent measurement

In both the current and prior period, financial liabilities are classified as subsequently measured at amortised cost, except loan commitments.

(ii) Derecognition

Financial liabilities are derecognised when they are extinguished (i.e. when the obligation specified in the contract is discharged, cancelled or expires).

The exchange between the Bank and its original lenders of debt instruments with substantially different terms, as well as substantial modifications of the terms of existing financial liabilities, are accounted for as an extinguishment of the original financial liability and the recognition of a new financial liability. The terms are substantially different if the discounted present value of the cash flows under the new terms, including any fees paid net of any fees received and discounted using the original effective interest rate, is at least 10% different from the discounted present value of the remaining cash flows of the original financial liability. In addition, other qualitative factors, such as the currency that the instrument is denominated in, changes in the type of interest rate, new conversion features attached to the instrument and change in covenants are also taken into consideration. If an exchange of debt instruments or modification of terms is accounted for as an extinguishment, any costs or fees incurred are recognised as part of the gain or loss on the extinguishment. If the exchange or modification is not accounted for as an extinguishment, any costs or fees incurred adjust the carrying amount of the liability and are amortised over the remaining term of the modified liability.

NOTES (Continued)

2. Principal accounting policies (continued)

J) Financial assets and liabilities (continued)

(K) Derivative instruments

The Bank uses derivative instruments in its portfolios for asset/liability management, and risk management. These instruments are mainly cross-currency swaps and interest rate swaps. The derivatives are used to manage exposure to currency risk which arises when the Bank issues loans in the local currencies of member states out of predominantly USD denominated borrowings. The interest component of the derivatives is reported as part of interest income and expense.

The Bank classifies all derivatives as held-for-trading and these are measured at fair value, with all changes in fair value recognised in the statement of comprehensive income.

Derivatives embedded in other financial instruments or other non-financial host contracts are treated as separate derivatives when their risks and characteristics are not closely related to those of the host contract and the host contract is not carried at fair value with unrealised gains or losses reported in profit or loss. Where material, such derivatives are separated from the host contract and measured at fair value with unrealised gains and losses reported in the statement of comprehensive income.

L) Impairment of non-financial assets

The carrying amounts of the Bank's assets are reviewed at each statement of financial position date to determine whether there is any indication of impairment. If such a condition exists, the assets' recoverable amount is estimated and an impairment loss recognised in the statement of comprehensive income whenever the carrying amount of an asset exceeds the recoverable amount.

M) Fiduciary assets

Assets held in a fiduciary capacity are not treated as assets of the Bank in the statement of financial position.

N) Offsetting

Financial assets and liabilities are only offset and the net amount reported in the statement of financial position where there is a legally enforceable right to set off the recognised amounts and the Bank intends to either settle on a net basis, or realize the asset and settle the liability simultaneously.

Income and expenses are presented on a net basis when permitted by the accounting standard or for gains and losses arising from a group of similar transactions.

During the year there was no offsetting transaction (2017: Nil).

NOTES (Continued)

2. Principal accounting policies (continued)

O) Provisions

A provision is recognised if, as a result of a past event, the Bank has a present legal or constructive obligation that can be estimated reliably, and it is probable that an outflow of economic benefits will be required to settle the obligation. Provisions are determined by discounting the expected future cash flows at a pre-tax rate that reflects current market assessments of the time value of money and, where appropriate, the risks specific to the liability.

Where the Bank expects a provision to be reimbursed, for example under an insurance contract, the reimbursement is recognised as a separate asset but only when the reimbursement is virtually certain.

P) Employees benefits

i) Retirement obligations

The Bank operates a defined contribution retirement benefit scheme to which employees contribute 10% of their basic salary and the Bank contributes 10%, 12.5% or 15% of the employees' basic salary depending on his/her length of service. The Bank complies with member states regulations with respect to social security contributions where applicable.

A defined contribution plan is a pension plan under which the Bank pays fixed contributions into a separate entity. The Bank has no legal or constructive obligations to pay further contributions if the fund does not hold sufficient assets to pay all employees the benefits relating to employee service in the current and prior periods.

A defined benefit plan is a pension plan that is not a defined contribution plan. Typically defined benefit plans define an amount of pension benefit that an employee will receive on retirement, usually dependent on one or more factors, such as age, years of service and compensation.

The Bank's contributions to the scheme are charged to the statement of comprehensive income in the year in which they are made. Costs relating to early retirement are charged to the statement of comprehensive income in the year in which they are incurred.

ii) Service gratuity

The Director General is entitled to contract gratuity equivalent to 20% of the annual gross salary. Gratuity is accounted for on an accruals basis. An accrual for the amount payable is made each year and is charged to the statement of comprehensive income.

NOTES (Continued)

2. Principal accounting policies (continued)

P) Employees benefits (continued)

iii) Other entitlements

The estimated monetary liability for employees' accrued annual leave entitlement at the reporting date is recognised as an expense accrual.

Q) Investment properties

Properties held for long-term rental yields that are not occupied by the Bank is classified as investment properties.

Certain properties of the Bank consist of a portion that is held for rental and a portion used for administrative purposes or occupied by Bank staff. In respect to such properties, portions that are held for rental yields or capital appreciation and can be leased or sold separately have been accounted for as investment property.

The properties held purely for rental yields have been classified under investment property. When the use of property changes from owner occupied to investment property, the property is re-measured at fair value and reclassified as investment property. Any gain arising on revaluation is recognized through other comprehensive income. Any loss arising on revaluation is recognized through the surplus or deficit.

R) Grants

Grants are recognised at their fair value where there is reasonable assurance that the grant will be received and all attaching conditions will be complied with.

When the grant relates to an expense item, (revenue grant) it is recognised as income over periods necessary to match the grant on a systematic basis to the costs that it is intended to compensate. Where the grant relates to an asset, (capital grant) it is recognised in the statement of comprehensive income on a systematic basis over the expected useful life of the relevant asset.

S) Cash and cash equivalents

For the purposes of the statement of cash flows, cash and cash equivalents comprise of cash with Banks held as demand and time deposits with original maturities of less than 90 days.

NOTES (Continued)

2. Principal accounting policies (continued)

T) Contingent liabilities – Financial guarantees and loan commitments

Letters of credit acceptances and guarantees are accounted for as Off Balance Sheet items and described as contingent liabilities.

Financial guarantee contracts require issuer to make pre-agreed payments to reimburse the holder for loss incurred because a specified debtor fails to make payments when due in accordance with the terms of a debt instrument. Such financial guarantees are given to Banks, financial institutions and others on behalf of customers to secure loans, overdrafts and other Banking facilities.

Financial guarantees are initially measured at fair value and subsequently measured at the higher of:

- The amount of loss allowance; and
- The premium received on initial recognitions less income less income recognized in accordance with the principles of IFRS 15.

Loan commitments provided by the Bank are measured as the amount of the loss allowance assuming the customer draws on the loan. However, the drawdown from the loans commitments is subject to fulfilments of conditions agreed in the loan contract and therefore the provision takes into account such conditions.

U) Taxation

In accordance with Article 49 of the Bank's Charter, the Bank, its property, other assets, income and its operations and transactions are exempt from all taxation and custom duties within member countries.

V) Dividends

Dividends on ordinary shares are charged to equity in the period in which they are declared. Proposed dividends are shown as a separate component of equity until declared.

W) Comparatives

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

NOTES (Continued)

		Notes	2018 USD '000	2017 USD '000
3	**Interest income**			
	Interest income on loans to projects		**15,884**	17,243
	Interest income on lease receivables		**27**	51
	Interest income on investment security held to maturity		**3**	21
	Interest income on deposits with other Banks		**5,623**	7,516
			21,537	24,831
4	**Interest expense**			
	Interest on medium and long term borrowings		**5,227**	5,798
	Interest on lines of credit		**1,143**	2,757
			6,370	8,555
5	**Fee and commission income-Net**			
	Gross fees and commission income			
	Appraisal fees		**64**	85
	Other fees and commission income		**494**	464
	Commitment fees		**23**	113
			581	662
	Gross fees and commission expense			
	Commission charges		**(62)**	(24)
	Commitment fees		**(54)**	(57)
	Other fees and commission expense		**(41)**	-
			(157)	(81)
	Net fee and commission income		**424**	581
6	**Other Operating Income**			
	Rent income		**673**	630
	Dividend income		**40**	123
	Recovery of previously written off loans		**987**	2,456
	Grant income		**1,241**	418
	Other income on asset leasing		**7**	19
	Write (off)/back of other liabilities		**19**	238
			2,967	3,884

NOTES (Continued)

		Notes	2018 USD '000	2017 USD '000
7	**Other gains/(losses)**			
	Net foreign exchange gain/(losses)		**(155**	38
	Net fair value gains/(losses) on equity investments at fair value	18	**44**	(50)
			(111	(12)
8	**Employee benefits expense**			
	Salaries and wages		**2,556**	2,561
	Pension and gratuity (Note 36)		**349**	360
	Other staff costs		**785**	670
			3,690	3,591
9	**Other operating expenses**			
	Rental expense		**114**	109
	Staff duty travel		**127**	143
	Directors expenses		**96**	139
	Insurance		**243**	262
	Advertising and publicity		**383**	144
	Legal fees		**501**	346
	Repairs and maintenance		**114**	138
	Computer software expenses		**178**	177
	Other IT related expenses		**1**	3
	Internal audit costs		**75**	91
	Statutory Audit fees		**57**	47
	Consultancy fees		**159**	445
	Project insurance		**405**	315
	Subscription to professional bodies		**2**	32
	Scholarships (Note 26)		**1,121**	336
	Other administrative expenses		**830**	721
			4,406	3,448
10	**Profit before income taxes**			
	Profit before income tax is stated after charging the following:			
	Directors emoluments:			
	- Fees and allowances		**37**	55
	- Other expenses		**58**	84
	Depreciation (note 21)		**702**	713
	amortization of intangible assets (note 22)		**73**	57
	Impairment of loans and advances		**2,809**	2,711
	Employee benefits expense (Note 8)		**3,690**	3,591
	Auditors remuneration		**57**	47

NOTES (Continued)

11 Taxation

In accordance with Article 49 of the Bank's Charter, the Bank, its property, other assets, income and its operations and transactions are exempt from all taxation and custom duties within member countries.

12 Earnings per share – basic and diluted

Basic earnings per share is calculated by dividing the net profit for the year attributable to ordinary shareholders by the weighted average number of ordinary shares outstanding during the year.

Diluted earnings per share is calculated by adjusting the weighted average number of ordinary shares for the number of shares not yet issued but for which payments have been received by the Bank.

	2018 USD '000	2017 USD '000
Net profit attributable to ordinary shareholders	**6,506**	10,213
Weighted average number of ordinary shares in issue and paid up during the year (Note 27)	**14,061**	14,061
Basic earnings per share	**463**	726
Earnings per share – basic and diluted		
Dilutive number of ordinary shares	**6**	6
Total issued and dilutive shares	**14,067**	14,067
Diluted earnings per share	**463**	726

Dilutive shares represent the number of shares generated from the balance of funds awaiting allotment (Note 29).

	2018 USD '000	2017 USD '000
13 Cash at Bank		
Cash at Bank	**10,867**	14,006

NOTES (Continued)

14	Placements with commercial Banks	2018	2017
		USD '000	USD '000
	Placements with Banks in member states	**130,406**	131,947
	Placements with overseas Banks	**35,113**	20,027
		165,519	151,974
	The above amount is analyzed as follows:		
	Amounts due within 3 months of date of acquisition	**163,302**	146,677
	Amounts due after 3 months of date of acquisition	**2,217**	5,297
		165,519	151,974

The weighted average effective interest rate on deposits due from Banks was 3.76 % (2017: 4.68%).

		2018	2017
		USD '000	USD '000
15	Equity investments at fair value		
	UGX corporate bond – Housing Finance Bank Uganda Limited	-	70

The interest rate for the bond, which was denominated in Uganda Shillings, was fixed at 13.5% per annum, it matured in 2018.

16	Loans and lease receivables	2018	2017
		USD'000	USD'000
	Loans and advances (net)	**156,206**	189,616
	Finance lease receivables (net)	**238**	409
		156,444	190,025
	Loans to projects	**159,438**	197,328
	Finance lease receivables	**238**	415
	Gross loans	**159,676**	197,743
	Impairment losses on loans and advances (Note 16a)	**(3,232**	(7,718
	Net carrying amounts	**156,444**	190,025

NOTES (Continued)

16 Loans and lease receivables

Included within loans to projects is financing amounting to Nil (2017: USD 1.60 million) extended to projects in exchange for shares in the borrower companies acquired at terms under which the shares are redeemable by the borrower company at the higher of valuation of the shares or the amount invested plus a guaranteed minimum annual rate of return. The portion of USD 1.60 Million was transferred to equity investments valued at fair value (Note 18). The Directors have assessed the fair value of the embedded equity derivative within these instruments and concluded that it is not material and as such it has not been accounted for in these financial statements.

(a) Loan impairment charges

Year ended 31 December 2018

Loans and receivables	USD'000
Opening loss allowance as at 1 January 2018 (Calculated under IFRS 9)	**19,431**
Less Impairment on written off projects	(19,012)
Increase in allowance recognized in profit/loss for the year	2,813
Closing loss allowance as at 31 December 2018	**3,232**

Year ended 31 December 2017	Allowance for identified impairment	Allowance for unidentified impairment	Total
	USD'000	USD'000	USD'000
At start of year	2,407	2,601	5,008
Increase in impairment allowances	2,998	228	3,226
Reversal of impairment	(385)	(130)	(515)
Loan impairment charge for the year	2,613	98	2,711
Amounts written off during the year	(1)	-	(1)
At end of year	**5,019**	**2,699**	**7,718**

NOTES (Continued)

17 Segment information

Management has determined the operating segments based on information reviewed by the board of Directors for the purpose of allocating resources and assessing performance.

The board of Directors considers the business from both a geographic and product perspective. Geographically, the board considers the performance in Kenya, Uganda, Tanzania and Rwanda.

The reportable operating segments derive their revenue primarily from lending to foster development through various products such as project loans, leases and equity.

The board assesses the performance of the operating segments based on a measure of gross loans and advances to customers, portfolio quality, approvals, disbursements and profit. The measure also excludes the effects of unrealised gains/ losses on financial instruments. Interest expenditure is not allocated to segments, as this type of activity is part of managing the cash position of the Bank by treasury.

The segment information provided to the board of Directors for the reportable segments for the year ended 31 December 2018 and 2017 respectively is as follows:

Loan exposure by country

Year ended 31 December 2018				
Loan exposure by country				
Country	**Gross Balances**	**%**	**Net Balances**	**%**
	USD'000		**USD'000**	
Uganda	40,597	25%	40,236	26%
Kenya	39,789	25%	37,364	24%
Tanzania	56,803	36%	56,390	36%
Rwanda	22,487	14%	22,454	14%
Total Region	**159,676**	100%	**156,444**	100%
Exposure by product				
Product				**%**
Long term loans	144,502	90%	142,022	91%
Medium term loans	8,745	5%	8,099	5%
Short term loans	6,191	4%	6,090	4%
Loans sub-total	**159,438**	100%	**156,211**	**100%**
Asset Lease	238	0%	233	0%
Total All Products	**159,676**	**100%**	**156,444**	**100%**

NOTES (Continued)

17 Segment information (continued)

Year ended 31 December 2017

Loan exposure by country				
Country				
Uganda	49,047	25%	47,937	25%
Kenya	54,763	28%	49,731	26%
Tanzania	63,595	32%	62,473	33%
Rwanda	30,338	15%	29,884	16%
Total Region	**197,743**	100%	**190,025**	100%

Exposure by product				
Product	**Gross Balances**	**%**	**Net Balances**	**%**
	USD'000		**USD'000**	
Long term loans	181,317	92%	174,181	92%
Medium term loans	5,276	3%	5,197	3%
Short term loans	9,098	4%	8,637	4%
Loans sub-total	**195,691**	**99%**	**188,015**	**99%**
Equity	1,601	1%	1,601	1%
Asset Lease	451	0%	409	0%
Total All Products	**197,743**	**100%**	**190,025**	**100%**

Year ended 31 December 2018

Total portfolio quality				
Category	**Gross port folio**	**%**	**Net Portfolio**	**%**
Performing Portfolio	**USD'000**		**USD'000**	
Normal (Stage 1 & 2)	145,176	91%	143,927	92%
	145,176	**91%**	**143,927**	**92%**
Non-Performing Portfolio				
Stage 3	14,500	9%	12,517	8%
	14,500	**9%**	**12,517**	**8%**
Total	**159,676**	**100%**	**156,444**	**100%**

NOTES (Continued)

17 Segment information (continued)

Year ended 31 December 2017

Total portfolio quality				
Category	**Gross portfolio**	**%**	**Net Portfolio**	**%**
Performing Portfolio	**USD'000**		**USD'000**	
Normal	150,200	76%	147,891	78%
Watch	29,497	15%	29,054	15%
	179,697	**91%**	**176,945**	**93%**
Non-Performing Portfolio				
Substandard	1,862	1%	1,706	1%
Doubtful	1,419	1%	957	1%
Loss	14,765	7%	10,417	5%
	18,046	**9%**	**13,080**	**7%**
	197,743	**100%**	**190,025**	**100%**

Approvals and disbursements				
	Approvals		**Disbursements**	
	Actual 2018	**Actual 2017**	**Actual 2018**	**Actual 2017**
	USD'000	**USD'000**	**USD'000**	**USD'000**
By country				
Uganda	17,562	12,670	4,521	5,780
Kenya	8,742	9,370	3,897	2,503
Tanzania	-	-	-	21,575
Rwanda	-	-	-	5,000
	26,304	**22,040**	**8,418**	**34,858**
By product				
Loans	**26,304**	**22,040**	**8,418**	**34,858**

The table below shows the distribution of loans and receivables by sector

Distribution of loans and receivables by sector	2018	2017
Agriculture and Fisheries	**1%**	2%
Agro, Marine and Food Processing	**7%**	7%
Construction Companies, Building Materials & Real estate	**26%**	23%
Financial Institutions	**39%**	35%
Education, Health and other Community Services	**8%**	7%
Electricity	**12%**	13%
Hotels, Tourism, Leisure and Entertainment	**7%**	13%
	100%	**100%**

NOTES (Continued)

17 Segment information (continued)

Segment statement of comprehensive income for year ended December 2018

	Uganda	Kenya	Tanzania	Rwanda	Head Office	Total
	USD'000	USD'000	USD'000	USD'000	USD'000	USD'000
Interest income	3,993	4,929	5,102	2,065	5,448	21,537
Interest expense	(1,475)	(1,354)	(503)	(36)	(3,002)	(6,370)
Net interest income	**2,518**	**3,575**	**4,599**	**2,029**	**2,446**	**15,167**
Fee and commission income	157	156	156	113	(156	426
Other operating income	245	782	-	-	1,939	2,966
Other gains /(losses)	(362)	287	(49)	(13)	25	(112)
Net fair value gain/(loss) investment property	-	-	-	-	(261)	(261)
Total operating income	**2,558**	**4,800**	**4,706**	**2,129**	**3,993**	**18,186**
Reduction in provision for impairment of loans and lease receivables	(405)	(2,485)	46	35	-	(2,809)
Operating income after impairment charges	**2,153**	**2,315**	**4,752**	**2,164**	**3,993**	**15,377**
Employee benefits expense	(859)	(968)	(696)	(281)	(886)	(3,690)
Depreciation and amortization	-	(14)	(20)	(10)	(731)	(775)
Other operating expenses	(884)	(884)	(884)	(442)	(1,312)	(4,406)
Profit before income tax	**410**	**449**	**3,152**	**1,431**	**1,064**	**6,506**
Income tax expense	-	-	-	-	-	-
Profit for the year	**410**	**449**	**3,152**	**1,431**	**1,064**	**6,506**
Total comprehensive income	**410**	**449**	**3,152**	**1,431**	**1,064**	**6,506**

NOTES (Continued)

17 Segment information (continued)

Segment statement of comprehensive income for year ended December 2017						
	Uganda	**Kenya**	**Tanzania**	**Rwanda**	**Head Office**	**Total**
	USD'000	**USD'000**	**USD'000**	**USD'000**	**USD'000**	**USD'000**
Interest income	4,887	5,690	4,301	2,417	7,536	24,831
Interest expense	(1,684)	(1,960)	(1,482)	(833)	(2,596)	(8,555)
Net interest income	**3,203**	**3,730**	**2,819**	**1,584**	**4,940**	**16,276**
Fee and commission income	111	164	194	150	(37	582
Other operating income	292	15	2,293	-	1,284	3,884
Other gains and losses	(53)	573	(66)	(16)	(450)	(12)
Net fair value gain/(loss) investment property	-	-	129	-	(125	4
Total operating income	**3,553**	**4,482**	**5,369**	**1,718**	**5,612**	**20,734**
Reduction in provision for impairment of loans and lease receivables	-	(1,094)	-	-	(1,617)	(2,711)
Operating income after impairment charges	**3,553**	**3,388**	**5,369**	**1,718**	**3,995**	**18,023**
Employee benefits expense	(231)	(295)	(230)	(41)	(2,793)	(3,591)
Depreciation and amortization	-	(5)	(20)	(20)	(726)	(770)
Other operating expenses	(690)	(690)	(690)	(689)	(690)	(3,449)
Profit before income tax	**2,632**	**2,398**	**4,429**	**968**	**(214)**	**10,213**
Income tax expense	-	-	-	-	-	-
Profit for the year	**2,632**	**2,398**	**4,429**	**968**	**(214)**	**10,213**
Total comprehensive income	**2,632**	**2,398**	**4,429**	**968**	**(214)**	**10,213**

NOTES (Continued)

17 Segment information (continued)

Segment statement of financial position for year ended December 2018						
	Uganda	Kenya	Tanzania	Rwanda	Head office	Total
Assets	**USD'000**	**USD'000**	**USD'000**	**USD'000**	**USD'000**	**USD'000**
Cash at Bank	4,572	3,292	2,014	83	906	10,867
Placements with commercial Banks	-	-	-	-	165,519	165,519
Loans and lease receivables	41,167	48,397	46,715	20,165	-	156,444
Equity investments	-	508	765	-	-	1,273
Other assets	165	81	71	19	229	565
Investment properties	-	-	4,205	-	14,668	18,873
Property and equipment	11,361	839	910	1	-	13,111
Intangible assets	-	-	-	-	180	180
Total assets	**57,265**	**53,117**	**54,680**	**20,268**	**181,502**	**366,832**
Liabilities	-	-	-	-	-	
Other liabilities	-	4,974	-	-	1,745	6,719
Borrowings	18,112	20,540	10,000	435	42,371	91,458
Special funds	-	-	-	-	3,990	3,990
Grants	-	-	150	-	883	1,033
Capital fund	-	-	-	-	7,479	7,479
Total liabilities	**18,112**	**25,514**	**10,150**	**435**	**56,468**	**110,679**
Capital and reserves						
Share capital	21,123	24,556	34,091	5,740	104,314	189,824
Share premium	-	-	-	3,874		3,874
Funds waiting allotment	-	-	-	-	83	83
Special reserve	-	-	-	-	12,507	12,507
Fair value reserve	-	-	-	-	525	525
Revaluation reserves	-	-	-	-	7,901	7,901
Retained earnings	14,621	15,330	9,644	7,069	(5,225	41,439
Total shareholders' equity	**35,744**	**39,886**	**43,735**	**16,683**	**120,105**	**256,153**
Total shareholders' equity and liabilities	**53,856**	**65,400**	**53,885**	**17,118**	**176,573**	**366,832**

NOTES (Continued)

17 Segment information (continued)

Segment statement of financial position for year ended December 2017						
	Uganda	Kenya	Tanzania	Rwanda	Head office	Total
Assets	USD'000	USD'000	USD'000	USD'000	USD'000	USD'000
Cash at Bank	4,175	6,416	114	188	3,113	14,006
Deposits due from commercial Banks	-	-	-	-	151,974	151,974
Investment securities held to maturity	-	-	-	-	70	70
Loans and lease receivables	48,962	52,937	63,741	30,339	(5,953)	190,025
Equity investments	-	110	326	-	-	436
Other assets	133	45	54	16	527	775
Investment properties	14,840	-	4,294	-	-	19,134
Property and equipment	11,503	1,053	1,211	-	-	13,767
Intangible assets	-	-	-	-	224	224
Total assets	**79,613**	**60,561**	**69,740**	**30,543**	**149,955**	**390,411**
Liabilities						
Other liabilities	4,603	-	-	-	1,187	5,790
Borrowings	15,679	16,952	20,412	9,715	46,760	109,518
Special funds	-	-	-	-	3,990	3,990
Grants	-	-	-	-	2,274	2,274
Capital fund	-	-	-	-	7,479	7,479
Total liabilities	**20,282**	**16,952**	**20,412**	**9,715**	**61,690**	**129,051**
Capital and reserves						
Share capital	21,123	24,556	34,091	5,740	104,314	189,824
Share premium	-	-	-	3,874	-	3,874
Funds waiting allotment	-	-	-	-	83	83
Special reserve	-	-	-	-	12,443	12,443
Fair value reserve	-	-	-	-	455	455
Retained earnings	-	-	-	-	46,750	46,750
Revaluation reserves	-	-	-	-	7,931	7,931
Total shareholders' equity	**21,123**	**24,556**	**34,091**	**9,614**	**171,976**	**261,360**
Total shareholders' equity and liabilities	**41,405**	**41,508**	**54,503**	**19,329**	**233,666**	**390,411**

NOTES (Continued)

18 • Equity investments at fair value

The Bank has advanced financing in the form of equity in exceptional cases where the project is assessed to have a significant impact on the community and its development but where the equity participation is necessary for improving the capital structure of the company or where the sponsors are unable to raise additional equity to enable the borrower operate on a commercially sound footing. Usually these are companies, which have substantial development impact but whose cash flows cannot support continuous repayments for long term loans. These investments are reported at their fair values in accordance with the Bank's accounting policies.

	2018 USD '000	2017 USD '000
Equity investments		
At start of year	**436**	487
Additions (Reclassified from loans)	**1,591**	-
	2,027	487
Less:		
Investments that matured during the year	**(798)**	-
Fair value gain/(loss)	**44**	(51
At end of year	**1,273**	436

19 Other assets

Prepayments	**73**	95
VAT Receivable	**336**	250
Fees and commission Receivable	**34**	136
Tenants receivable	**94**	95
Other receivables	**28**	199
	565	775

20 Investment property valuation

At start of year	**19,134**	19,069
Additions	**-**	61
Net fair value gain/(losses)	**(261)**	4
At end of the year	**18,873**	19,134

NOTES (Continued)

20 Investment property valuation (continued)

An independent valuation of the Bank's land and buildings was performed by professional valuers Knight Frank Limited and Africa Property Limited to determine the fair value of the land and buildings as at 31 December 2018 based on estimated open market values.

Properties that are held by the Bank for generation of rental income have been classified under investment property as per Note 21. Land and buildings occupied by the Bank for administrative use is classified under property, plant and equipment (Note 21).

The table below shows revenue, costs and capital commitments related to investment property:

	2018	2017
	USD '000	USD '000
Rental income from investment property	**628**	582
Direct operating expenses: Rented properties	**57**	54
Direct operating expenses: Unrented properties	**2**	1
Approved capital commitment	**305**	267

NOTES (Continued)

21 Property, plant & equipment (continued)

	Land and buildings	Capital work in progress	Office equip-ment	Motor Vehicle	Furniture & fittings	Total
	USD 000'	USD 000'	USD 000'	USD 000'	USD 000'	USD 000'
At 1 January 2017						
Cost or valuation	13,840	347	1,819	686	795	17,487
Accumulated depreciation	(963)	-	(917)	(676)	(476)	(3,032)
Net book amount	12,877	347	902	10	319	14,455
Year ended 31 December 2017						
Opening net book amount	12,877	347	902	10	319	14,455
Additions		30				30
Transfers from WIP	93	(110)	19	-	-	2
Disposals						
Cost	-	-	(7)			(7)
Depreciation charge	(475)	-	(157)	(9)	(72)	(713)
Closing net book amount	12,495	267	757	1	247	13,767
At 31 December 2017						
Cost or valuation	13,933	267	1,831	686	795	17,512
Accumulated depreciation	(1,438)	-	(1,074)	(685)	(548)	(3,745)
Net book amount	12,495	267	757	1	247	13,767

NOTES (Continued)

21 Property, plant & equipment (continued)

	Land and buildings	Capital work in progress	Office equipment	Motor Vehicle	Furniture & fittings	Total
	USD 000'	USD 000'	USD 000'	USD 000'	USD 000'	USD 000'
Year ended 31 December 2018						
Opening net book amount	12,495	267	757	1	247	13,767
Revaluation surplus						
Additions		46				46
Transfers from WIP		(8	4	-	4	-
Depreciation charge	(476)	-	(155)	-	(71)	(702)
Closing net book amount	12,019	305	606	1	180	13,111
Year ended 31 December 2018						
Cost or valuation	13,933	305	1,835	686	799	17,558
Accumulated depreciation	(1,914)	-	(1,229)	(685)	(619)	(4,447)
Net book amount	**12,019**	**305**	**606**	**1**	**180**	**13,111**

The revaluation model under IAS 16 – Property, plant and equipment has been applied to land and buildings under own-use (this includes residential properties rented out to staff). An independent valuation was performed by a professional valuer (Knight Frank Limited) to determine the fair value of land and buildings as at 31 December 2014.

If land and buildings were stated on the historical cost basis, the amounts would be as follows:

	2018	2017
	USD'000	USD'000
Cost	**8,759**	8,759
Accumulated depreciation	**(4,649)**	(4,211
Net book amount	**4,110**	4,548

NOTES (Continued)

22 Intangible assets

Cost		
At start of year	**1,934**	1,653
Additions during the year	**29**	281
	1,963	1,934
Amortization		
At start of year	**(1,710)**	(1,653)
Amortization charge for the year	**(73)**	(57)
	(1,783)	(1,710)
At end of year	**180**	224

23 Other liabilities

Deposits on leased assets	**122**	122
Advances from customers	**34**	34
Rent received in advance	**48**	43
Administrative accruals	**633**	196
Deferred Income	**238**	209
Prepaid rental income	**74**	122
KFW line of credit	**4,974**	4,603
FAPA-AfDB grant funds	**-**	52
Other creditors	**596**	409
	6,719	5,790

The KFW line of credit relates to an agricultural financing programme under the German Financial Cooperation in Kenya and Uganda meant for on-lending to selected Partnering Financial Institutions (PFIs) in local currency both medium and long term facilities. The beneficiaries of the above funds are Kenya Women Finance Trust, Sidian Bank and Finca Uganda.

NOTES (Continued)

24 Borrowings

	2018	2017
	USD'000	USD'000
Lines of credit with multi-lateral development Banks	**81,632**	98,352
Lines of credit with other Financial Institutions	**9,826**	11,166
	91,458	109,518
Maturity analysis of borrowings		
Amounts payable within one year	**-**	13,262
Amounts payable after one year but within five years	**39,631**	30,556
Amounts payable after five years	**51,827**	65,700
	91,458	109,518

24 Borrowings movement analysis

	2018	2017
	USD'000	USD'000
Opening balance	**109,518**	123,681
Additional borrowing	**1,744**	15,237
Interest incurred during the year	**6,370**	8,555
Principle payments within the year	**(19,922)**	(30,580)
Interest payments within the year	**(5,710)**	(7,584)
Revaluation gain/ (loss)	**(542)**	209
Net Balance	**91,458**	109,518

NOTES (Continued)

24 Borrowings (continued)

Lender	Tenor	Rate type	Interest rate %	Currency	2018	2017
					USD'000	USD'000
Nordic Development fund	30	Fixed	0.75	EUR	**4,997**	5,552
European Investment Bank	7	Fixed	9.16	KES	**2,697**	3,422
Republic of Uganda-KFW	9	Fixed	6	UGX	**5,328**	5,453
Republic of Uganda-KFW	9	Fixed	6	UGX	**1,520**	1,556
European Investment Bank	6	Fixed	9.30	UGX	**743**	1,014
European Investment Bank	7	Fixed	9.41	KES	**1,314**	1,621
European Investment Bank	7	Fixed	9.38	KES	**1,168**	1,441
European Investment Bank	5	Fixed	8.56	UGX	**-**	1,764
European Investment Bank	7	Fixed	10.25	TZS	**-**	4,773
European Investment Bank	7	Fixed	8.26	RWF	**426**	569
Republic of Uganda-KFW	9	Fixed	6	UGX	**1,506**	1,541
European Investment Bank	7	Fixed	9.84	KES	**2,005**	2,418
Republic of Uganda-KFW	9	Fixed	6	UGX	**4,946**	5,062
African Development Bank	14	Variable	2.56	USD	**-**	2,074
European Investment Bank	7	Variable	4.78	USD	**1,121**	1,569
Opec Fund for International Development	7	Variable	5.59	USD	**8,182**	10,909
European Investment Bank	7	Variable	4.75	USD	**1,591**	2,227
African Development Bank	10	Variable	5.98	USD	**26,250**	30,000
Arab Bank for Economic Development	9	Variable	6.53	USD	**11,997**	11,997
KFW-agricultural financing Kenya	15	Fixed	5	KES	**1,164**	-
KFW-agricultural financing Kenya	15	Fixed	5	KES	**569**	-
Commercial Bank of Africa	2	Fixed	10.5	KES	**9,823**	9,695
dfcu Bank limited	3	Variable	8.97	UGX	**-**	1,379
					87,347	106,036
Accrued interest payable					**4,111**	3,482
					91,458	109,518

NOTES (Continued)

24 Borrowings (continued)

The KFW lines of credit include the Rural Finance Enhancement Programme and Agri Finance Enhancement Programme for on-lending to selected Partnering Financial Institutions (PFIs) in local currency. EADB has a contractual obligation to repay principal and accumulated interest in Uganda shillings to Ministry of Finance, Planning & Economic Development (the recipient) on maturity.

The weighted average effective interest rate on borrowings was 6.45% (2017: 7.11%). The Bank has not given any security for the borrowings and has not defaulted on any of them. More information regarding the currency, maturity and contractual repricing rates for the Bank's borrowings are shown in Note 35.

25 Special funds (Norwegian /EADB fund)

	2018	2017
	USD '000	USD '000
At start and end of year	**3,990**	3,990

Norwegian/ EADB fund

This fund was created out of a 1986/7 grant of NOK 30 million by the Norwegian Government to the Government of Uganda towards rehabilitation of Ugandan industries. Under the grant agreement, the Bank was allowed to use a portion of interest paid on the loans to cover administrative expenses. Any balance of interest on loans and other interest earned on funds made available under the agreement was to accrue to a special fund to be managed by the Bank.

The special fund was to be used for certain expenditure including; a) payments to consultants and experts, b) strengthening the Bank's administrative capacity, c) technical assistance, d) loans on concessionary terms, e) or any other purpose agreed by the government of Norway and the Bank. The agreement is silent on the use of capital repayments. Consultations are underway with the Norwegian Government to determine the utilisation/ disposition of the remaining balance.

26 Grants

	2018	2017
	USD '000	USD '000
At start of year	**2,274**	2,483
Additions	**-**	209
Grant utilization	**(1,241)**	(418)
	1,033	2,274

NOTES (Continued)

26 Grants (continued)

The table below shows the counter parties from whom the grants were obtained.

SIDA / EADB fund for technical assistance	**-**	910
SWISS/ EADB fund for technical assistance	**774**	1,053
Housing Finance feasibility study grant	**150**	150
AfDB credit knowledge management system grant	**109**	161
	1,033	2,274

The SIDA/EADB fund

The SIDA/ EADB fund for technical assistance was established following a grant from the Government of Sweden through SIDA. The funds were meant for EADB's institutional support and capacity building.

During the year ended 31 December 2018, the Bank utilised part of the grant amounting to USD 910,000 (2017: USD 418,100) on regional capacity building by training selected East African lawyers through the extractive industries seminars, medical training and teacher graduate scholarships.

Medical Training and Fellowship (METAF) Program

The East African Development Bank (EADB) Medical Training and Fellowship (METAF) program is a four-year program (2017-2020) that aims to increase the early detection, research and treatment of cancer and neurological disorders in East Africa, especially in communities and areas where access to qualified professionals remains a challenge. The program is delivered by the British Council as the Program Manager in partnership with the Royal College of Physicians (RCP) as the technical partner.

The programme was developed in response to the growing burden of non-communicable diseases, especially cancer and neurological disorders in member states of the EADB – Kenya, Tanzania, Rwanda and Uganda. Premised on British Council's expertise in managing training programmes and the RCP's expertise in improving medical care across the globe, the programme is a high impact sustainable training model employing a twin approach of short-term clinical trainings within East Africa and long-term fellowships tenable in the United Kingdom (UK).

NOTES (Continued)

26 Grants (continued)

EADB Math, Science, Technology and Engineering University Scholarship Program (STEM)

The EADB Math, Science, Technology and Engineering University Scholarship Program was launched in partnership with The Africa-America Institute. The multiple fast track, 12-month scholarships are available to experienced teachers and lecturers with bachelor's degrees in mathematics, science, technology and engineering with an interest in pursuing a graduate degree in those fields in the United States at Rutgers University.

The STEM scholarship aims to maximize the impact of EADB's investment into the higher education sector by granting scholarships to accomplished lecturers who have agreed to return to their East African universities and continue teaching after they have received their graduate degree at Rutgers University. The fully-funded EADB graduate level scholarships provide full tuition, room and living expenses within a stipulated budget. Masters degrees include, Math Education, Science Education, Cell and development biology, Chemical and Biochemical Engineering, Industrial and Systems Engineering and Materials Science and Engineering.

SWISS/ EADB fund

The SWISS fund for technical assistance was established following a grant from the Swiss Government. The funds were to be utilised for EADB's institution building support, staff training, corporate strategy and restructuring study. The Bank began utilising this grant for capacity building through offering scholarships. During the year ended 31 December 2018, the Bank utilised part of the grant amounting to USD 331,000 (2017: Nil)

Housing Finance Feasibility study grant

The grant represents funds received from the Government of Tanzania to fund the housing finance feasibility study.

AfDB (Credit knowledge management system grant)

This relates to the capital grant received from African Development Bank for the purchase of customised web based credit knowledge management software amounting to USD 209,000. Grant income is recognised in the statement of comprehensive income on a straight line basis over the life of the expected useful life of the software which management has estimated as four years.

NOTES (Continued)

27 Share capital

	Paid up share capital	Callable share capital	Total	Paid up share capital	Callable share capital	Total
	Number	Number	Number	USD'000	USD'000	USD'000
Authorised share capital						
Class A	24,000	120,000	144,000	324,000	1,620,000	1,944,000
Class B	16,000	1,037	17,037	216,000	14,000	230,000
	40,000	121,037	161,037	540,000	1,634,000	2,174,000
Issued share capital						
Class A						
At 1 January 2017, 31 December 2017 and 2018	12,280	61,400	73,680	165,780	828,901	994,681
Class B						
At 1 January 2017, 31 December 2017 and 2018	1,781	1,037	2,818	24,044	14,000	38,044

Paid in capital

	Class A	Class B	Total	Class A	Class B	Total
	Number	Number	Number	USD'000	USD'000	USD'000
At 1 January 2017, 31 December 2017 and 2018	**12,280**	**1,781**	**14,061**	**165,780**	**24,044**	**189,824**

NOTES (Continued)

27 Share capital (continued)

Shareholders	Number of shares as at 31 December 2018	Number of shares as at 31 December 2017	Amount as at 31 December 2017 and 2018	Share-holding
			USD'000	%
Class A				
Government of Kenya	3,800	3,800	51,300	27.03%
Government of Tanzania	3,343	3,343	45,130	23.77%
Government of Uganda	3,800	3,800	51,300	27.03%
Government of Rwanda	1,337	1,337	18,050	9.51%
Total Class A	**12,280**	**12,280**	**165,780**	**87.33%**
Class B				
African Development Bank	1,240	1,240	16,740	8.82%
FMO – Netherlands	375	375	5,062	2.67%
DEG – Germany	100	100	1,350	0.71%
Yugoslavia Consortium	28	28	378	0.20%
SBIC - Africa Holdings	24	24	324	0.17%
Commercial Bank of Africa	5	5	68	0.04%
Nordea Bank Sweden	5	5	68	0.04%
Standard Chartered Bank	2	2	27	0.01%
Barclays Bank Plc., London	2	2	27	0.01%
Total Class B	**1,781**	**1,781**	**24,044**	**12.67%**
Total Class A & B	**14,061**	**14,061**	**189,824**	**100%**

Authorised share capital

In 2015 the authorized capital stock was increased from USD 1,080,000,000 to USD 2,160,000,000 consisting of 80,000 additional shares being 100% increase in capital stock of the Bank with a par value of USD 13,500 each. This was to enable admission of new members into the Bank. In addition, a resolution was passed in 2013 approving African Development Bank (AfDB), a class B shareholder, to subscribe for a further 740 class B paid up shares and 1,037 class B callable shares at USD 13,500 each.

Class A

The authorised number of Class A ordinary shares is 144,000, (2017: 144,000) at a par value of USD 13,500 each. Class A ordinary shares are available for subscription to only member states and in equal proportion.

NOTES (Continued)

27 Share capital (continued)

Class B

The authorised number of Class B ordinary shares is 16,000, (2017: 16,000) at a par value of USD 13,500 each. Class B ordinary shares are available for subscription to members other than member states. All issued Class B shares are fully paid up.

Share premium

Share premium arose on the shares issued to the Republic of Rwanda on admission at a value of USD 17,913 per share. The total number of shares issued and paid for by the Republic of Rwanda on the admission program is 878 (2017: 878). Share premium therefore amounts to USD 4,413 per share which is equivalent to USD 3.9 million (2017: USD 3.9 million).

Callable capital

The capital stock of paid-in and callable Class A shares shall be available for subscription by member states in such proportion that, for every six shares subscribed, one share shall be fully paid-in with the remaining being callable. The Bank's Charter provides that the Bank may make calls on its callable share capital in the event that it is unable to repay borrowings and any other eligible payments due out of pre-existing resources.

In March 2012, the Bank's Charter was amended to allow class B shareholders to subscribe to callable capital of the Bank. In 2013, the Governing Council passed a special waiver on article 4(2) b of the Bank's Charter that sets out that for every four shares subscribed every one share is fully paid in. Following the waiver, 1,037 class B callable shares were allotted to African Development Bank.

Dividends

Payment of dividends is made to subscribers of Class B shareholders in proportion to the number of shares held by such members. Dividends to Class A shares holders are paid in proportion to the number of shares paid in by each member but only after Class B dividend is paid.

28	Capital fund	2018	2017
		USD '000	USD '000
	At start and end of year	**7,479**	7,479

NOTES (Continued)

28 Capital fund (continued)

This represents the balance of funds received from the Norwegian Government, in 1982 and 1987 for the Norwegian/ EADB fund on a grant basis. In 2012, the Bank initiated the process of obtaining approval from the donors to close the fund and transfer the outstanding balance to the Bank's capital to be allotted amongst member states. During 2013, the Bank received a response from the donor requesting that the capitalisation of the fund be put on hold until the Norwegian Government completes its consultations.

29 Funds awaiting allotment

	2018	2017
	USD'000	USD '000
At start of year	**83**	103
Amounts reclassified (to)/from grants, special funds and capital fund	**-**	(20)
At end of year	**83**	83

30 Special reserve

At start of year	**12,443**	12,358
Transfer of commission and guarantee fees from Statement of Comprehensive Income	**64**	85
At end of year	**12,507**	12,443

The transfer to the special reserve is made in accordance with Article 17 of the Bank's Charter, the reserve being credited with commissions earned. The special reserve is non distributable and serves the purpose of enabling the Bank meet its liabilities on borrowings or guarantees chargeable.

NOTES (Continued)

31 Fair value reserve

The fair value reserve includes the cumulative net change in the fair value of derivative financial instruments and equity investments measured at fair value through the profit and loss account. The reserve represents an appropriation of unrealised fair value differences which are shown separately from retained earnings until realised. The movement in fair value reserve is shown below:

Fair value reserve	2018 USD '000	2017 USD '000
At start of year	**455**	505
Transfer from retained earnings	**70**	(50)
At end of year		
	525	455

32 Cash and cash equivalents

For the purposes of the statement of cash flows, cash and cash equivalents comprise the following:

	2018 USD '000	2017 USD '000
Cash and Bank balances (Note 13)	**10,867**	14,006
Balances due from Banks originally maturing less than 3 months	**163,302**	145,320
	174,169	159,326

33 Revaluation reserve

The revaluation surplus arose from the revaluation of land and buildings as at 31 December 2014 and is non distributable.

	2018 USD '000	2017 USD '000
At start of year	**7,939**	7,980
Transfer of excess depreciation to retained earnings	**(38)**	(41)
At end of year	**7,901**	7,939

NOTES (Continued)

34 Use of estimates and judgments

The Bank makes estimates and assumptions that affect the reported amounts of assets and liabilities within the next financial year. Estimates and judgments are continually evaluated and are based on historical experience and other factors, including expectations of future events that are believed to be reasonable under the circumstances.

Thus note provides an overview of the areas that involve a higher degree of judgement and major sources of estimation uncertainty that have a significant risk of resulting in a material adjustment within the next financial year

Measurement of expected credit loss allowance

The measurement of the expected credit loss allowance for financial assets measured at amortized cost and FVOCI is an area that requires the use of complex models and significant assumptions about the future economic conditions and credit behaviour of the customers which are used to derive the inputs of expected credit loss (ECL), namely probability of default, exposure at default (ED) and loss given default (LGD).

34 Use of estimates and judgments

A number of judgements and assumptions are required in applying the accounting requirements for measuring ECL such as:

- Determining criteria for significant increase in credit risk (SICR);
- Choosing appropriate models and assumptions for measuring the ECL;

Establishing groups of similar financial assets for the purpose of measuring ECL.

Determining fair values

The determination of fair value for financial assets and liabilities for which there is no observable market price requires the use of valuation techniques. For financial instruments that trade infrequently and have little price transparency, fair value is less objective, and requires varying degrees of judgment depending on liquidity, concentration, uncertainty of market factors, pricing assumptions and other risks affecting the specific instrument.

NOTES (Continued)

35 Financial risk management

(a) Introduction and overview

The Bank has exposure to the following risks from its use of financial instruments:

- Credit risk;
- Liquidity risk; and
- Market risk

This note presents information about the Bank's exposure to each of the above risks, the Bank's objectives, policies and processes for measuring and managing risk and the Bank's management of capital.

Risk management framework

The Bank's board of Directors has overall responsibility for the establishment and oversight of the Bank's risk management framework. The Asset and Liability Committee (ALCO), Project Committee and the Risk Management Unit are responsible for developing and monitoring the risk management policies in their specified areas. The Board Audit Committee reports regularly to the Board of Directors on their activities while the board of Directors reports to the Governing council.

35 Financial risk management

(a) Introduction and overview

The Bank's risk management policies are established to identify and analyse the risks faced by the Bank, to set appropriate risk limits and controls, and to monitor risks and adherence to limits. Risk management policies and systems are reviewed regularly to reflect changes in market conditions, products and services offered. The Bank through its procedures aims to develop a disciplined and constructive control environment in which all employees understand their roles and obligations.

The Bank's Audit and Governance Committee is responsible for monitoring compliance with the Bank's risk management policies and procedures, and for reviewing the adequacy of the risk management framework in relation to the risks faced by the Bank. The Audit Committee is assisted in these functions by Internal Audit. Internal Audit undertakes both regular and adhoc reviews of risk management controls and procedures, the results of which are reported to the Audit Committee.

NOTES (Continued)

35 Financial risk management (continued)

(b) Credit risk

Credit risk is the risk of financial loss to the Bank if a customer or counterparty to a financial instrument fails to meet its contractual obligations, and arises principally from the Bank's loans and advances to customers, other Banks and investment securities. For risk management reporting purposes, the Bank considers all elements of credit risk exposure such as individual obligator default risk and sector risk.

In the normal course of its business, the Bank incurs credit risk from counterparties, loans and advances to customers. The credit risk exposure is, however, managed through constant monitoring of the status of financial institutions where deposits are maintained. As a policy, the Bank places its deposits with strong local Banks and internationally rated financial institutions. Credit risk is also minimized by the Bank's policy of diversification.

The Ban has investment policies and guidelines for the type of financial products and services and to restrict exposure to individual projects and industries.

Management of credit risk

The risk management committee is responsible for oversight of the Bank's credit risk, including, formulating credit policies, covering collateral requirements and credit assessments, risk grading and reporting.

Documentary, legal procedures and compliance with regulatory and statutory requirements undertaken in consultation with the Bank's legal Department, establishing the authorization structure for the approval and renewal of credit facilities with concurrence of the board of Directors, reviewing and assessing credit risk. The Bank assesses all credit exposures, prior to facilities being committed to customers. Renewals and reviews of facilities are subject to the same review process, limiting concentrations of exposure to counterparties, products and industries (for loans and advances). New loan project requests are subject to Bank's risk grading in order to ensure that only viable projects are taken into the books.

The Bank also has a Portfolio team which is responsible for monitoring the credit quality of loans and ensuring appropriate corrective action is taken. The credit administration also provides advice, guidance and specialist skills to Operations Department to promote best practice in the management of credit risk. The Portfolio team prepares regular reports for Management and the Board's consideration on the performance of the loan portfolio.

NOTES (Continued)

35 Financial risk management (continued)

(b) Credit risk (continued)

The Operations Department is required to implement the Bank's credit policies and procedures, and ensure that credit approval authorities are observed. The Operations Department is responsible for the quality and performance of its credit portfolio and for monitoring and controlling all credit risks in its portfolio, including those subject to Board approval. The Regular audits of the Operations Department and the Bank's credit processes are undertaken by Internal Audit.

Loans and advances (incl. loan commitments and guarantees)

The estimation of credit exposure for risk management purposes is complex and requires the use of models, as the exposure varies with changes in market conditions, expected cash flows and the passage of time. The assessment of credit risk of a portfolio of assets entails further estimations as to the likelihood of defaults occurring, of the associated loss ratios and of default correlations between counterparties. The Bank measures credit risk using Probability of Default (PD), Exposure at Default (EAD) and Loss Given Default (LGD). This is similar to the approach used for the purposes of measuring Expected Credit Loss.

Credit risk grading

The Bank uses internal credit risk grading that reflect its assessment of the probability of default of individual counterparties. The Bank use internal rating models tailored to the various categories of counterparty. Borrower and loan specific information collected at the time of application (such as sector and business risk, management/Directors quality, financial resources, and level of collateral is fed into this rating model. This is supplemented with external data such as credit bureau scoring information on individual borrowers.

NOTES (Continued)

35 Financial risk management (continued)

(b) Credit risk (continued)

Expected credit loss measurement

FRS 9 outlines a 'three-stage' model for impairment based on changes in credit quality since initial recognition as summarised below:

- A financial instrument that is not credit-impaired on initial recognition is classified in 'Stage 1' and has its credit risk continuously monitored by the Bank.
- If a significant increase in credit risk ('SICR') since initial recognition is identified, the financial instrument is moved to 'Stage 2' but is not yet deemed to be credit-impaired.
- If the financial instrument is credit-impaired, the financial instrument is then moved to 'Stage 3'.
- Financial instruments in Stage 1 have their ECL measured at an amount equal to the portion of lifetime expected credit losses that result from default events possible within the next 12 months. Instruments in Stages 2 or 3 have their ECL measured based on expected credit losses on a lifetime basis
- A pervasive concept in measuring ECL in accordance with IFRS 9 is that it should consider forward looking information.
- Purchased or originated credit-impaired financial assets are those financial assets that are credit impaired on initial recognition. Their ECL is always measured on a lifetime basis (Stage 3).

Change in credit quality since initial recognition

The following diagram summarises the impairment requirements under IFRS 9 (other than purchased or originated credit-impaired financial assets)

Change in credit quality since initial recognition

Recognition of expected credit losses

12 Months Expected Credit Losses	Lifetime Expected Credit Losses	Lifetime Expected Credit Losses
Stage 1	**Stage 2**	**Stage 3**
*Performing initial recognition**	*Underperforming Assets with significant increase in credit risk since initial recognition**	*Non-performing Credit impaired assets*

**Except for purchased or originated credit impaired assets*

NOTES (Continued)

35 Financial risk management (continued)

(b) Credit risk (continued)

The 3 stages are as detailed below:

Stage 1: includes financial instruments that have not experienced a significant increase in credit risk since initial recognition or that have low credit risk at the reporting date. For these assets, 12-month expected credit losses ('ECL') are recognised. 12-month ECL are the expected credit losses that result from default events that are possible within 12 months after the reporting date.

Stage 2: includes financial instruments that have had a significant increase in credit risk since initial recognition (unless they have low credit risk at the reporting date) but that do not have objective evidence of impairment. For these assets, lifetime ECL are recognised. Lifetime ECL are the expected credit losses that result from all possible default events over the expected life of the financial instrument.

Stage 3: includes financial assets that have objective evidence of impairment at the reporting date. For these assets, lifetime ECL are recognised and interest revenue is calculated on the net carrying amount (that is, net of credit allowance).

The Bank has considered the following in determining the staging of facilities:

1. Qualitative factors

    - The client's risk rating

2. Quantitative factors

    - The facilities arrears status
    - Number of restructures, if any
    - Reasons for restructure
    - Change in client rating over the past 12 months

3. The indicators of Significant Increase in Credit Risk (SICR) are:

    - Is the facility more than 30 days past due
    - Has it been restructured due to cash flow difficulties
    - Has there been an increase in rating of the facility

NOTES (Continued)

35 Financial risk management (continued)

(b) Credit risk (continued)

Significant increase in credit risk (SICR)

Measuring ECL – Explanation of inputs, assumptions and estimation techniques

The Expected Credit Loss (ECL) is measured on either a 12-month (12M) or Lifetime basis depending on whether a significant increase in credit risk has occurred since initial recognition or whether an asset is considered to be credit-impaired. Expected credit losses are the discounted product of the Probability of Default (PD), Exposure at Default (EAD), and Loss Given Default (LGD), defined as follows:

- The PD represents the likelihood of a borrower defaulting on its financial obligation (as per "Definition of default and credit-impaired" above), either over the next 12 months (12M PD), or over the remaining lifetime (Lifetime PD) of the obligation.

- EAD is based on the amounts the Bank expects to be owed at the time of default, over the next 12 months (12M EAD) or over the remaining lifetime (Lifetime EAD). For example, for a revolving commitment, the Bank includes the current drawn balance plus any further amount that is expected to be drawn up to the current contractual limit by the time of default, should it occur.

- Loss Given Default (LGD) represents the Bank's expectation of the extent of loss on a defaulted exposure. LGD varies by type of counterparty, type and seniority of claim and availability of collateral or other credit support. LGD is expressed as a percentage loss per unit of exposure at the time of default (EAD). LGD is calculated on a 12-month or lifetime basis, where 12-month LGD is the percentage of loss expected to be made if the default occurs in the next 12 months and Lifetime LGD is the percentage of loss expected to be made if the default occurs over the remaining expected lifetime of the loan.

The ECL is determined by projecting the PD, LGD and EAD for each future month and for each individual exposure or collective segment. These three components are multiplied together and adjusted for the likelihood of survival (i.e. the exposure has not prepaid or defaulted in an earlier month). This effectively calculates an ECL for each future month, which is then discounted back to the reporting date and summed. The discount rate used in the ECL calculation is the original effective interest rate or an approximation thereof.

NOTES (Continued)

35 Financial risk management (continued)

(b) Credit risk (continued)

Measuring ECL – Explanation of inputs, assumptions and estimation techniques(continued)

The Lifetime PD is developed by applying a maturity profile to the current 12M PD. The maturity profile looks at how defaults develop on a portfolio from the point of initial recognition throughout the lifetime of the loans. The maturity profile is based on historical observed data and is assumed to be the same across all assets within a portfolio and credit grade band. This is supported by historical analysis.

The 12-month and lifetime EADs are determined based on the expected payment profile, which varies by product type

Forward-looking information incorporated in the ECL models

To incorporate forward looking information into the ECL calculations, macroeconomic overlays were applied to the probability of default. Overlays were estimated and applied for three different scenarios, base case scenario, downside scenario and optimistic scenario.

These macroeconomic overlays and the probability of each economic scenario occurring were set using management judgement.

The main factors considered while assessing the possible impact of the economic scenario are:

- expected trend of the gross domestic product (GDP),
- expected trend of the consumer price index and
- growth of credit to private sector

Analysis is then made to determine how such changes are likely going to affect the probabilities of default as well as loss given default. Determination of such impact is made after consideration of input given by consultants including actuaries.
The table below shows the weightings for each scenario as applied by the bank

Macro-economic scenarios			
	Base case	Downside	Optimistic
Probability	80%	10%	10%
PD overlay	0	0.1	(0.05)

NOTES (Continued)

35 Financial risk management (continued)

(b) Credit risk (continued)

Maximum exposure to credit risk — Financial instruments subject to impairment

The following tables contain analyses of the credit risk exposure of financial instruments for which an ECL allowance is recognised. The gross carrying amount of financial assets below also represents the Bank's maximum exposure to credit risk on these assets

Loans and lease receivables

At 31 December 2018	Kenya	Uganda	Tanzania	Rwanda	Total
	USD'000	USD'000	USD'000	USD'000	USD'000
Stage 1	27,849	37,321	37,529	22,487	125,186
Stage 2	-	716	19,274	-	19,990
Stage 3	11,940	2,560	-	-	14,500
Carrying amount	**39,789**	40,597	56,803	22,487	159,676
At 1 January 2018					
Stage 1	28,263	44,451	40,873	30,339	143,926
Stage 2	-	-	20,467	-	20,467
Stage 3	26,106	3,762	1,862	-	31,730
Carrying amount	**54,369**	48,213	63,202	30,339	196,123

Maximum exposure to credit risk — Financial instruments not subject to impairment

The Company assessed its other financial assets for impairment as shown in Note 2 (a) and found them not to be impaired. In arriving at the conclusion the Bank assessed, among others, the credit standing of the counterparties and probability of default of its placements and bank balances.

NOTES (Continued)

The table below shows the other financial assets not subject to impairment

	2018	2017
	USD'000	USD'000
Cash at Bank	**10,867**	14,006
Placements with commercial Banks	**165,519**	151,974
Investment securities held to maturity	**-**	70
	176,386	166,050

35 Financial risk management (continued)

(b) Credit risk (continued)

Loss allowance (continued)

The loss allowance recognised in the period is impacted by a variety of factors, as described below:

- Transfers between Stage 1 and Stages 2 or 3 due to financial instruments experiencing significant increases (or decreases) of credit risk or becoming credit-impaired in the period, and the consequent "step up" (or "step down") between 12-month and Lifetime ECL;
- Additional allowances for new financial instruments recognised during the period, as well as releases for financial instruments de-recognised in the period;
- Impact on the measurement of ECL due to changes in PDs, EADs and LGDs in the period, arising from regular refreshing of inputs to models; Impacts on the measurement of ECL due to changes made to models and assumptions;
- Discount unwind within ECL due to the passage of time, as ECL is measured on a present value basis;
- Foreign exchange retranslations for assets denominated in foreign currencies and other movements; and
- Financial assets derecognised during the period and write-offs of allowances related to assets that were written off during the period.

NOTES (Continued)

35 Financial risk management (continued)

(b) Credit risk Measurement (continued)

Loss allowance (continued)

The following tables explain the changes in the loss allowance between the beginning and the end of the annual period due to these factors:

Year ended 31 December 2018	Stage 1	Stage 2	Stage 3		
	12-Month ECL	Lifetime ECL	Lifetime ECL	Others	Total
	USD'000	USD'000	USD'000	USD'000	USD'000
Loans and receivables					
Gross carrying amount as at 1 January 2018	**143,944**	**20,467**	**31,730**	**-**	**196,141**
Transfers					-
Transfer from Stage 1 to Stage 2	811	(811)	-	-	-
Financial assets derecognised during the period other than write offs	(38,029)	(2,773)	(981)	-	(41,783)
					-
New financial assets originated	8,418	-	-	-	8,418
Changes in interest accruals	11,571	1,578	2,763	-	15,912
Write offs	-	-	(19,012)	-	(19,012)
Gross carrying amount as at 31 December 2018	**126,715**	**18,461**	**14,500**	**-**	**159,676**
Expected Credit Loss					
As at 1 January 2018	1,435	228	17,768	-	**19,431**
Increase/(Decrease) in impairment	(410)	(4)	3,223	4	**2,813**
Write offs	-	-	(19,012)	-	**(19,012)**
As at 31 December 2018	**1,025**	**224**	**1,979**	**4**	**3,232**
Net carrying amount as at 31 December 2018	**125,690**	**18,237**	**12,521**	**(4)**	**156,444**

NOTES (Continued)

35 Financial risk management (continued)

(b) Credit risk Measurement (continued)

Credit risk as presented under IAS 39

	loans and advances to projects	Other loans and advances
Year ended 31 December 2017		
	USD '000	**USD '000**
Individually assessed		
Gross amount	**18,046**	-
Allowance for impairment	**(2,481)**	-
Carrying amount	**15,565**	**-**
Collectively assessed:		
Gross amount	**177,368**	1,601
Allowance for impairment	**(2,908)**	-
Carrying amount	**174,460**	**1,601**
Total carrying amount	**190,025**	**1,601**
Past due but not impaired:		
Watch (31 to 90 days)	**29,497**	-
Substandard (91 to 180) days	**-**	-
Doubtful (181 to 360) days	**-**	-
Neither past due nor impaired:		
Normal	**147,871**	1,601
Allowance for impairment – collectively assessed	**(2,908)**	**-**
Total carrying amount	**174,460**	**1,601**

Impaired loans and advances
Impaired loans and advances are those for which the Bank determines that it is probable that it will be unable to collect all principal and interest due according to the contractual terms of the loan agreement(s). These loans are internally classified as substandard, doubtful or loss accounts.

NOTES (Continued)

35 Financial risk management (continued)

(b) Credit risk Measurement (continued)

Credit risk as presented under IAS 39 (continued)

Past due but not impaired loans and advances

Loans where contractual interest or principal payments are past due but the Bank believes that impairment is not appropriate on the basis of the level of security/ collateral available and/or the stage of collection of amounts owed to the Bank. These loans are internally classified as watch, when the account is 31 to 90 days in arrears, substandard if the account is between 91 and 180 days in arrears, doubtful for loans between 181 and 360 days in arrears and loss for loans over 361 days in arrears.

Loans with renegotiated terms

Loans with renegotiated terms are loans that have been restructured due to deterioration in the borrower's financial position and where the Bank has made concessions that it would not otherwise consider. Once the loan is restructured, it remains in this category for monitoring purposes independent of satisfactory performance after restructuring, for at least two scheduled payments as a way of demonstrating positive performance.

Allowances for impairment

The Bank establishes an allowance for impairment losses that represents its estimate of incurred losses in its loan portfolio taking into account prudential guidelines of International Financial Reporting Standards (IFRS). The main components of this allowance are a specific loss component that relates to individually significant exposures and a collective loan loss allowance established for groups of homogeneous assets in respect of losses that have been incurred on a collective basis.

Write off policy

Financial assets are written off when there is no reasonable expectation of recovery, such as a debtor failing to engage in a repayment plan with the Bank. Where loans or receivables have been written off, the Bank continues to engage in enforcement activity to attempt to recover the receivable due. Where recoveries are made, these are recognised in profit or loss.

NOTES (Continued)

35 Financial risk management (continued)

(b) Credit risk Measurement (continued)

Collateral and other credit enhancements

The Bank holds collateral against loans and advances to customers in the form of legal mortgages, sovereign guarantees, insurance guarantees and floating charge over assets. Estimates of fair value are based on the value of the collateral assessed at the time of borrowing.

An estimate of fair value of collateral and other security enhancements held against financial assets is shown below:

	Gross exposure	Impairment allowance	Carrying amount	Fair value of collateral held
Loans and lease receivables	31,730	(17,768)	13,962	51,228
Loans and lease receivables	14,500	(1,979)	12,521	23,506

Credit exposures relating to off-statement of financial position	2018	2017
	USD '000	USD '000
Loan commitments	**6,207**	1,902

Settlement risk

The Bank's activities may give rise to risk at the time of settlement of transactions and trades. Settlement risk is the risk of loss due to the failure of the counterparty to honour its obligations to deliver cash, securities or other assets as contractually agreed. Settlement limits form part of the credit approval/limit monitoring process described earlier.

(c) Liquidity risk

Liquidity risk is the risk that the Bank will encounter difficulty in meeting obligations on its financial liabilities. It includes both the risk of being unable to fund assets at appropriate maturities and rates and the risk of being unable to liquidate an asset at a reasonable price and in an appropriate time frame.

NOTES (Continued)

35 Financial risk management (continued)

(c) Liquidity risk (liquidity risk continued)

The Bank has access to a diverse funding base. Funds are raised mainly from borrowings and share capital. This enhances funding flexibility, limits dependence on one source of funds and generally lowers the cost of funds. The Bank strives to maintain a balance between continuity of funding and flexibility through the use of liabilities with a range of maturities. The Bank continually assesses liquidity risk by identifying and monitoring changes in funding required in meeting business goals and targets set in terms of the overall Bank strategy. In addition, the Bank has an Asset and Liability Committee that meet on a regular basis to monitor liquidity risk, review and approve liquidity policies and procedures.

The Bank maintains a minimum of 1.33 times coverage of designated liabilities for the next twelve months in liquid assets as per the liquidity policy. Designated liabilities consist of liabilities and budgeted commitments that are due in twelve months.

The liquidity policy ratio as at the end of the year is as follows:

	2018 USD '000	2017 USD '000
Cash and cash equivalents	**174,169**	159,326
Less		
	(18,720)	(13,280)
Designated liabilities	**(51,359)**	(61,355)
Cash and cash equivalents as per liquidity policy	**104,090**	84,691
Liquidity ratio	**4.00**	3.14
Budgeted designated liabilities		
Repayment of term loans	**21,602**	24,758
Interest on borrowings	**4,819**	5,341
Acquisition of fixed assets	**2,132**	4,396
Staff and administration expenses	**9,966**	11,521
	38,519	46,016

Cash and cash equivalents as per liquidity policy is arrived at after deducting loan disbursement commitments of USD 18.72 million (2017: USD 13.28 million).

The liquidity policy of the Bank defines cash and cash equivalents as its operational and strategic liquidity pool which comprises cash and placements with commercial banks with original maturity periods not exceeding 3 months.

The Bank registered a liquidity ratio of 4.0 (2017: 3.14) which exceeds the minimum liquidity ratio as per the policy of 1.33.

NOTES (Continued)

35 Financial risk management (continued)

(c) Liquidity risk (continued)

The table below analyses assets and liabilities into relevant maturity groupings based on the remaining period at 31 December 2018 to the contractual maturity date.

	Matured	< 6 Months	> 6 Months < 1 Year	> 1 Year < 3 Years	>3 Years < 5 Years	>5 Years < 7 Years	> 7 Years	Total
	USD '000	USD '000	USD '000	USD '000	USD '000	USD '000	USD '000	USD '000
Assets								
Cash at Bank	10,867	-	-	-	-	-	-	10,867
Placements	-	165,774	495	-	-	-	-	166,269
Loans and lease receivables	648	24,259	28,573	74,963	47,865	11,682	4,147	192,137
Equity Investments	-	-	-	1,273	-	-	-	1,273
Other assets receivable	567	-	-	-	-	-	-	567
Total assets	**12,082**	**190,033**	**29,068**	**76,236**	**47,865**	**11,682**	**4,147**	**371,113**
Liabilities								
Other accounts payable	6,719	-	-	-	-	-	-	6,719
Medium and long term loans	-	8,125	18,296	28,045	27,238	12,668	14,128	108,500
Total liabilities	**6,719**	**8,125**	**18,296**	**28,045**	**27,238**	**12,668**	**14,128**	**115,219**
Net liquidity gap -31 Dec 2018	**5,363**	**181,908**	**10,772**	**48,191**	**20,627**	**(986**	**(9,981**	**255,894**
Cumulative gap - 31 Dec 2018	**5,363**	**187,271**	**198,043**	**246,234**	**266,861**	**265,875**	**255,894**	
Net liquidity gap -31 Dec 2017	**9,954**	**168,818**	**10,141**	**58,301**	**36,926**	**894**	**(11,662**	**273,372**
Cumulative gap -31 Dec 2017	**9,954**	**178,772**	**188,913**	**247,214**	**284,140**	**285,034**	**273,372**	

NOTES (Continued)

35 Financial risk management (continued)

(c) Liquidity risk (continued)

Off balance sheet items

The Bank's off balance sheet items comprise of loans commitments, letters of credit and capital commitments. The dates of the contractual amounts of the Bank's off-balance sheet financial instruments that it commits to extend credit to customers, letters of credit and capital commitments are summarised in the table below.

	< 6 Months	> 6 Months < 1 Year	> 1 Year < 3 Years	> 3 Years < 5 Years	> 5 Years 7 Years	> 7 Years	Total
	USD '000	USD '000	USD '000	USD '000	USD '000	USD'000	USD '000
Loan commitments	3,365	2,716	-	126	-	-	6,207
Capital commitments	-	305	-	-	-	-	305
Total	**3,365**	**3,021**	**-**	**126**	**-**	**-**	**6,512**

(d) Interest rate risk

In broad terms the interest rate risk is the sensitivity of the Bank's financial performance to changes in the interest rates. The Bank's operations are subject to the risk of interest rate fluctuations to the extent that interest earning assets and interest bearing liabilities mature or reprice at different times or in differing amounts. Risk management activities are aimed at optimizing net interest income, given market interest rates levels consistent with the Bank's business strategies. In order to minimize interest risk, the Bank has a policy where the approved lending commitments are matched to specific lines of credit or source of funds, including adopting the funding interest rate characteristics (fixed or variable) to its on lending activities.

As at 31 December 2018, if interest rates on interest bearing assets and liabilities had been higher/ lower by 200 bps, with all other variables held constant, the impact on comprehensive income would be USD 2.5 million (2017: 2.4 million), which is 0.98 percent of the total shareholders' equity. This is shown in the table below.

	2018	2017
	(USD'000)	(USD'000)
Total Assets repricing within 6 months	300,454	335,687
Total liabilities repricing within 6 months	50,089	92,423
Interest gap	250,366	243,264
Impact of interest rise by 200 bps	2,504	2,433
Impact on total shareholders' equity	0.98%	0.93%

NOTES (Continued)

35 Financial risk management (continued)

(d) Interest rate risk (continued)

The table below summarizes the exposure to interest rate risks. Included in the table are the Bank's assets and liabilities at carrying amounts, categorized by the earlier of contractual re-pricing or maturity dates. The Bank does not bear an interest rate risk on off balance sheet items.

	Up to 1 Month	1 to 3 Months	3 to 6 Months	6 to 12 Months	1 to 5 Years	Over 5 Years	Non-interest bearing	Total
	USD '000	USD '000	USD '000	USD '000	USD '000	USD '000	USD '000	USD '000
Assets								
Cash and Bank balances	-	-	-	-	-	-	10,867	10,867
Placements	45,252	118,050	1,722	495	-	-	-	165,519
Loans and advances	4,679	125,303	5,448	5,212	12,994	6,040	-	159,676
Equity investments	-	-	-	-	-	-	1,273	1,273
Other assets receivable	-	-	-	-	-	-	567	567
Total assets	**49,931**	**243,353**	**7,170**	**5,707**	**12,994**	**6,040**	**12,707**	**337,902**
Liabilities								
Other accounts payable	-	-	-	-	-	-	6,718	6,718
Medium and long term loans	-	37,962	12,127	-	28,586	12,758	25	91,458
Total liabilities	**-**	**37,962**	**12,127**	**-**	**28,586**	**12,758**	**6,743**	**98,176**
Interest sensitivity gap at 12/31/2018	**49,931**	**205,391**	**(4,957)**	**5,707**	**(15,592)**	**(6,718)**	**5,964**	**239,726**
Cumulative gap at 31 Dec 2018	**49,931**	**255,322**	**250,365**	**256,072**	**240,480**	**233,762**	**239,726**	
Interest sensitivity gap at 12/31/2017	**71,981**	**177,844**	**(6,560)**	**7,203**	**575**	**(13,612**	**12,372**	**249,801**
Cumulative gap at 12/31/2017	**71,981**	**249,825**	**243,264**	**250,467**	**251,042**	**237,430**	**249,801**	

NOTES (Continued)

35 Financial risk management (continued)

(e) Currency risk

The Bank does not actively engage in dealing and trading operations in currencies and so the Bank's exposure to currency risk mainly involves the risk of foreign exchange losses or gains arising on the retranslation of monetary assets, liabilities and off balance sheet items denominated in foreign currency. To minimize currency risk in a multi-currency environment, the Bank matches it's funding in one currency with assets in the same currency.

ASSETS (Figures in USD)	UGX '000	KES '000	TZS '000	RWF '000	EUR '000	GBP '000	SEK '000	Total
Cash and Bank balances	2,427	599	2,011	80	5,001	16	2	10,136
Placements with Banks	1,464	6,981	119	-	-	-	-	8,564
Loans and advances at amortized costs	15,719	15,088	691	404	5,302	-	-	37,204
Equity investments - Available for sale	-	134	764	-	-	-	-	899
Other assets receivable	-	7	-	-	-	-	-	7
TOTAL ASSETS	**19,610**	**22,809**	**3,585**	**484**	**10,303**	**16**	**2**	**56,810**
LIABILITIES (Figures in USD)								
Other accounts payable	100	11	15	-	4,974	-	-	5,100
Medium and long term borrowings	16,978	18,929	-	435	5,002	-	-	41,344
TOTAL LIABILITIES	**17,078**	**18,940**	**15**	**435**	**9,976**	**-**	**-**	**46,444**
Net Currency position current month	**2,532**	**3,869**	**3,570**	**49**	**327**	**16**	**2**	**10,366**
Net Currency position Dec 2017	**2,720**	**4,438**	**1,957**	**28**	**1,143**	**22**	**2**	**10,311**

NOTES (Continued)

35 Financial risk management (continued)

(e) Currency risk (continued)

Sensitivity analysis

The 10% movement of USD against other currencies at 31 December 2018 would have increased or decreased comprehensive income by USD 0.94 million (2017: USD 0.94 million). This is assuming that all other variables, in particular interest rates remain constant.

	2018 (USD'000	2017 (USD'000)
FX denominated assets	**58,779**	64,862
FX denominated liabilities	**46,604**	54,551
Net open position	**12,175**	10,311
Impact of a 10% movement in exchange rate	**1,107**	937

(f) Fair value of financial assets and liabilities

The carrying amount of financial assets and liabilities approximate to their fair value.

(g) Fair value of financial instruments

IFRS 7 specifies a hierarchy of valuation techniques based on whether the inputs to those valuation techniques are observable or unobservable. Observable inputs reflect market data obtained from independent sources; unobservable inputs reflect the Bank's market assumptions. These two types of inputs have created the following fair value hierarchy:

- Level 1 – Fair value is determined using unadjusted quoted prices in an active market for identical assets and liabilities. Types of financial assets include: actively traded government and other agency securities, listed derivative instruments and listed equities. Types of financial liabilities include listed derivative instruments.

- Level 2 – Fair value is determined using valuation models with direct or indirect market observable inputs. Types of financial assets include: corporate and other government bonds and loans, and over-the-counter (OTC) derivatives. Types of financial liabilities include over-the-counter (OTC) derivatives.

- Level 3 – Fair value is determined using Valuation models using significant non-market observable inputs. Types of financial assets include: highly structured OTC derivatives with unobservable parameters and corporate bonds in illiquid markets. Types of financial liabilities include highly structured OTC derivatives with unobservable parameters.

NOTES (Continued)

35 Financial risk management (continued)

(g) Fair value of financial instruments (continued)

This hierarchy requires the use of observable market data when available. The Bank considers relevant and observable market prices in its valuations where possible. Refer to note 21 for disclosures of the land and buildings that are measured at fair value.

	Level 3	Total
	USD '000	USD '000
31 December 2018		
Financial assets at fair value through profit or loss		
Equity investments at fair value	**1,273**	1,273
31 December 2017		
Financial assets at fair value through profit or loss		
Equity investments at fair value	**436**	436

Reconciliation of level 3 items

	2018	2017
	USD '000	USD '000
Equity investments		
At start of year	**436**	487
Additions (Reclassified from loans)	**1,591**	-
Investments exited (Reclassified to loans)	**(798)**	-
Fair value gain/ (loss)	**44**	(51)
At end of year	**1,273**	436

The movement in fair value of equity investments has been analysed in Note 18.

The following table analyses the non-financial assets carried at fair value, by valuation method. The different levels have been defined as follows:

- Quoted prices (unadjusted) in active markets for identical assets or liabilities (Level 1).

NOTES (Continued)

35 Financial risk management (continued)

(g) Fair value of financial instruments (continued)

- nputs for the year ended 31 December 2018 other than quoted prices included within level 1 that are observable for the asset or liability, either directly (that is, as prices) or indirectly (that is, derived from prices) (Level 2).

- Inputs for the asset or liability that are not based on observable market data (that is, unobservable inputs) (Level 3).

(h) Capital management

The Bank's objectives when managing capital, which is a broader concept that the 'equity' on the face of the statement of financial position, are:

- To comply with the capital requirements set under the Bank's Charter
- To safeguard the Bank's ability to continue as a going concern so that it can continue to provide returns for shareholders and benefits for other stakeholders; and
- To maintain a strong capital base to support the development of its business.

The Bank's capital requirements are strictly observed under Article 11 of the Bank's Charter which requires that the Bank's outstanding loans, equity investments and guarantees do not at any one time exceed three times the Bank's unimpaired subscribed capital plus reserves and surplus relating to its ordinary capital resources but excluding the special reserve. The Bank was well within this limit as of 31 December 2018. The ratio is computed as a ratio of loans, equities and lease receivables divided by shareholders equity less special reserves.

	2018 USD '000	2017 USD '000
Gross loans and lease receivables	**159,676**	197,743
Shareholders' equity	**256,153**	261,360
Special reserve	**(12,507)**	(12,443)
	403,322	446,660
Ratio	**0.66**	0.79

The Bank's capital adequacy ratio (Capital/Risk weighted assets) at 31 December 2018 was 67% (2017: 67%)

NOTES (Continued)

36 Employee retirement benefit plans and gratuity

	Note	2018 USD '000	2017 USD '000
Contribution to the retirement benefit plan	(i)	**272**	284
Contribution to the statutory pension scheme (NSSF)	(ii)	**5**	4
Gratuity	(iii)	**72**	72
		349	360

The Bank operates a defined contribution retirement benefit scheme to which employees contribute 10% of their basic salary and the Bank contributes 10%, 12.5% or 15% of the employees' basic salary depending on his/her length of service. A Board of Trustees manages the scheme, the scheme administrator is Alexander Forbes, custodian Standard Chartered Bank Uganda and Fund manager Sanlam Investments ltd.

(i) The Bank also makes contributions to a statutory pension scheme, the National Social Security Fund for its casual staff. The contributions and obligations under the scheme are limited to specific contributions legislated from time to time and the Bank's contribution is currently 10% of the employees' gross salary and Kenya Shillings 200 for Kenyan employees resident in Kenya.

(ii) Gratuity is paid to the Director General at 20% of annual gross salary at the end of each year.

Other staff benefits

The Bank ensures proper welfare of its staff by providing welfare schemes such as car loan purchase scheme, educational assistance, housing and medical schemes. The Bank also pays for professional membership and subscription fees for staff that belong to professional bodies. In addition, employees are eligible for loans subject to prevailing policies and the Bank operates a medical insurance scheme for all its employees. Costs associated with proving these benefits are expensed as and when incurred and reported under employee benefits expense (Note 8).

37	Capital commitments	2018	2017
		USD '000	USD '000
	Authorized and contracted for	**305**	347

NOTES (Continued)

38 Off balance sheet items and contingencies

The Bank conducts business involving guarantees, performance bonds and indemnities. The following are the commitments and contingencies outstanding as at year-end.

	Note	2018 USD '000	2017 USD '000
Un-disbursed commitments		**6,207**	1,902

Nature of contingent liabilities

a) Commitments to lend are agreements to lend to a customer in future subject to certain conditions. Such commitments are normally made for a fixed period.

The Bank is a litigant in several cases which arise from normal day to day Banking activities. The Directors believe the Bank has strong grounds for success and are confident that they should get rulings in their favor in matters before court. In cases where the Bank may not be successful, Directors and management are confident that such cases would not significantly impact the Bank's operations either individually or in aggregate.

Management has also carried out an assessment of all the cases outstanding as at 31 December 2018 and did not find any that warranted a provision. This position is supported by independent professional legal advice.

39 Related party transactions

The Bank is owned by four East African Community member states of Kenya, Tanzania, Uganda and Rwanda who collectively own 87% of the total number of shares, which is 100% of the ordinary class A shares. The remaining 13% is widely held by class B shareholders.

A number of Banking transactions are entered into with related parties in the normal course of business. These include loans, deposits with Banks, borrowings and capital contributions by the member states. The volumes of related-party transactions and outstanding balances at year-end, for the year are as follows:

NOTES (Continued)

39 Related party transactions (continued)

	2018 USD '000	2017 USD '000
Loans and advances to Directors		
- Eddron Communications Limited	**-**	220
- Green Hills Academy Ltd	**405**	532
- Loan to government of United Republic of Tanzania	**4,646**	6,485
Deposits held with Banks that are shareholders of the Bank and related entities:		
- Commercial Bank of Africa ltd	**35,024**	35,033
- Standard Chartered Bank PLC	**35,113**	20,027
- Interest income earned on all of the above	**2,612**	2,094
Borrowings payable by the Bank to shareholders		
- African Development Bank	**26,917**	32,722
- Commercial Bank of Africa ltd	**9,826**	9,770
Interest expense on borrowings as paid to shareholders	**2,618**	4,099

As at 31 December 2018, full provision and write off of USD 0.243 million was made (2017 USD 0.09 million) for impairment against the loan to Eddron Communications Limited. No provision has been made for any other loans to related parties. Loans to employees are given at concessionary rates.

Key management compensation	2018 USD '000	2017 USD '000
Salaries and other employee benefits	**379**	376
Other short-term employee benefits - Gratuity	**72**	72
	451	448
Directors' remuneration		
- Fees and allowances	**37**	55
- Salaries and other short-term employee benefits (included within key management compensation above)	**451**	448
- Other expenses	**60**	84
	548	587

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