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## REPORT OF INDEPENDENT AUDITORS

Asian Development Bank

In our opinion, the accompanying statement of financial position and the related statements of activities and changes in net assets, and of cash flows present fairly, in all material respects, in terms of United States dollars, the financial position of the Asian Development Bank – Asian Development Bank Institute Special Fund at 31 December 1998 and 1997, and the results of its activities and changes in net assets and its cash flows for the year ended 31 December 1998 and the period 24 March to 31 December 1997, in conformity with generally accepted accounting principles. These financial statements are the responsibility of the Bank's management; our responsibility is to express an opinion on these financial statements based on our audits. We conducted our audits of these statements in accordance with generally accepted auditing standards which require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statements presentation. We believe that our audits provide a reasonable basis for the opinion expressed above.

*PricewaterhouseCoopers LLP*

17 February 1999

**ASIAN DEVELOPMENT BANK—ASIAN DEVELOPMENT BANK INSTITUTE SPECIAL FUND**  
**STATEMENT OF FINANCIAL POSITION**

**31 December 1998 and 1997**

Expressed in Thousands of United States Dollars (Note B)

	<b>1998</b>	<b>1997</b>
<b>ASSETS</b>		
DUE FROM BANKS (Note B)	\$ 714	\$ 276
INVESTMENTS (Notes B, C, and D)		
Time deposits	12,233	3,575
PROPERTY, FURNITURE, AND EQUIPMENT (Note B)	\$4,722	\$4,225
Less—allowance for depreciation	<u>1,146</u>	<u>303</u>
OTHER ASSETS	1,946	1,643
<b>TOTAL</b>	<b>\$18,469</b>	<b>\$9,416</b>
<b>LIABILITIES AND UNCOMMITTED BALANCES</b>		
ACCOUNTS PAYABLE TO ORDINARY CAPITAL RESOURCES	\$ 78	\$ 494
ACCOUNTS PAYABLE AND OTHER LIABILITIES	393	32
UNCOMMITTED BALANCES (ADBISF-2)	17,998	8,890
<b>TOTAL</b>	<b>\$18,469</b>	<b>\$9,416</b>

See notes to financial statements (ADBISF-4).

**ASIAN DEVELOPMENT BANK—ASIAN DEVELOPMENT BANK INSTITUTE SPECIAL FUND  
STATEMENT OF ACTIVITIES AND CHANGES IN NET ASSETS**

**For the Year Ended 31 December 1998 and the Period 24 March to 31 December 1997**

Expressed in Thousands of United States Dollars (Note B)

	<u>1998</u>	<u>1997</u>
<b>CHANGES IN UNRESTRICTED NET ASSETS</b>		
CONTRIBUTIONS (Note B)	\$16,254	\$ 11,828
REVENUE		
Income from investments (Notes B and C)	<u>57</u>	<u>28</u>
Total	16,311	11,856
EXPENSES	<u>8,745</u>	<u>2,788</u>
CONTRIBUTIONS AND REVENUE IN EXCESS OF EXPENSES	7,566	9,068
EXCHANGE LOSSES	(37)	—
TRANSLATION ADJUSTMENTS (Note B)	<u>1,579</u>	<u>(178)</u>
INCREASE IN UNRESTRICTED ASSETS AFTER TRANSLATION ADJUSTMENTS	9,108	8,890
NET ASSETS AT BEGINNING OF YEAR	8,890	—
<b>NET ASSETS AT END OF YEAR</b>	<b>\$17,998</b>	<b>\$ 8,890</b>

See notes to financial statements (ADBISF-4).

**ASIAN DEVELOPMENT BANK—ASIAN DEVELOPMENT BANK INSTITUTE SPECIAL FUND**  
**STATEMENT OF CASH FLOWS**

**For the Year Ended 31 December 1998 and the Period 24 March to 31 December 1997**

Expressed in Thousands of United States Dollars (Note B)

	<b>1998</b>	<b>1997</b>
<b>CASH FLOWS FROM OPERATING ACTIVITIES</b>		
Contributions received	\$ 16,254	\$ 11,828
Interest on investments received	52	26
Administrative expenses paid	<u>(8,241)</u>	<u>(4,119)</u>
Net Cash Provided by Operating Activities	<u>8,065</u>	<u>7,735</u>
<b>CASH FLOWS FROM INVESTING ACTIVITIES</b>		
Net cash invested in time deposits	(6,115)	(3,343)
Sales of investment securities	28,753	14,185
Purchases of investment securities	(29,821)	(14,345)
Furniture and equipment acquired	<u>(47)</u>	<u>(4,225)</u>
Net Cash Used in Investing Activities	<u>(7,230)</u>	<u>(7,728)</u>
Effect of Exchange Rate Changes on Due from Banks	<u>(397)</u>	<u>269</u>
Net Increase in Due from Banks	438	276
Due from Banks at Beginning of Year	<u>276</u>	<u>—</u>
Due from Banks at End of Year	<u>\$ 714</u>	<u>\$ 276</u>
<b>RECONCILIATION OF INCREASE IN NET ASSETS TO NET CASH PROVIDED BY OPERATING ACTIVITIES:</b>		
Increase in net assets (ADBISF-2)	\$ 9,108	\$ 8,890
Adjustments to reconcile increase in net assets to net cash provided by operating activities:		
Translation adjustments	(1,579)	178
Amortization of discounts/premiums	(4)	(2)
Depreciation	719	303
Other—net	<u>(179)</u>	<u>(1,634)</u>
Net Cash Provided by Operating Activities	<u>\$ 8,065</u>	<u>\$ 7,735</u>

See notes to financial statements (ADBISF-4).

ASIAN DEVELOPMENT BANK—ASIAN DEVELOPMENT BANK INSTITUTE SPECIAL FUND  
NOTES TO FINANCIAL STATEMENTS

31 December 1998 and 1997

CONTINUED

**NOTE A—NATURE OF OPERATIONS**

In 1996, the Bank approved the establishment of the Asian Development Bank Institute (the Institute) in Tokyo, Japan as a subsidiary body of the Bank. The Institute's operations commenced upon the receipt of the first fund from the Government of Japan on 24 March 1997, and it was inaugurated on 10 December 1997. The Institute maintains its own financial accounts and is financed by a Special Fund. The Institute's funds consist of voluntary contributions, donations, and grants from members, nongovernment organizations, and foundations. The objectives of the Institute, as defined under its Statute, are the identification of effective development strategies and the improvement of capacity for sound development management in developing member countries.

**NOTE B—SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES**

*Presentation of the Financial Statements*

The financial statements of the Institute are presented on the basis of those for not-for-profit organizations.

The Institute reports the contributions of cash and other assets as unrestricted support as these are contributed by donors without conditions other than for the purposes of pursuing the objectives of the Institute.

*Investments*

All investment securities held by the Institute are reported at estimated fair value, with realized and unrealized gains and losses included in revenue. Estimated fair value generally represents market value. Cost or amortized cost is used to approximate fair value for certain short-term investments not traded in the market (time deposits, etc.).

*Property, Furniture, and Equipment*

Property, furniture, and equipment is stated at cost and is depreciated over their estimated useful lives using the straight-line method.

*Contributions*

Contributions from donors are included in the financial statements from the date indicated by the donors that funds are expected to be made available.

*Functional Currency and Reporting Currency*

The currencies of contributing members are functional currencies. The reporting currency is the United States dollar and the financial statements are expressed in thousands of current United States dollars.

*Translation of Currencies*

Assets, liabilities, and uncommitted balances are translated from the functional currency to the reporting currency at the applicable rates of exchange at the end of a reporting period. Contributions included in the financial statements during the period are translated at the applicable exchange rates as of the respective dates of commitment. Revenue and expense amounts in currency other than the United States dollar are translated for each semimonthly period at the applicable rates of exchange at the beginning of each period; such practice approximates the application of average rates in effect during the period.

*Accounting Estimates*

The preparation of financial statements in conformity with generally accepted accounting principles requires Management to make estimates and assumptions that affect the reported amounts of assets and liabilities as at the end of the year (24 March – 31 December 1997) and the reported amounts of income and expenses during the year (24 March – 31 December 1997). The actual results could differ from those estimates.

ASIAN DEVELOPMENT BANK—ASIAN DEVELOPMENT BANK INSTITUTE SPECIAL FUND

NOTES TO FINANCIAL STATEMENTS

31 December 1998 and 1997

*Statement of Cash Flows*

For the purposes of the statement of cash flows, the Institute considers that its cash and cash equivalents are limited to "DUE FROM BANKS."

**NOTE C—INVESTMENTS**

The investment portfolio was composed wholly of investments denominated in Japanese yen. As of 31 December 1998 and 1997, the estimated fair value of the investments approximates the amortized cost. All such investments are due in one year or less.

The annualized rate of return on the average investments held during the year, based on the portfolio held at the beginning and end of each month was 0.48% (0.53% – annualized rate of return for the period ended 31 December 1997).

Investments are governed by the Investment Authority approved by the Board of Directors. The main investment management objective is to maintain security and liquidity. Subject to these parameters, the Bank seeks the highest possible return on its investments.

**NOTE D—FAIR VALUE OF FINANCIAL INSTRUMENTS**

Fair value of a financial instrument is defined as the amount at which the instrument could be exchanged in a current transaction between willing parties, other than in a forced or liquidation sale.

The fair value of financial instruments that are short-term approximates their carrying amounts.

The Institute's statement of financial position carrying amounts are considered to approximate fair values for all significant financial instruments.

**NOTE E—STAFF RETIREMENT PLAN AND POSTRETIREMENT MEDICAL BENEFITS**

*Staff Retirement Plan*

The Institute participates in the contributory defined benefit Staff Retirement Plan (the Plan) of the Bank. Every member of the professional staff, as defined under the Plan, shall, as a condition of service, become a participant from the first day of service, provided that at such a date, the staff has not reached the normal retirement age of 60. Retirement benefits are based on length of service and highest average remuneration during two years of eligible service. The Plan assets are segregated and are not included in the statement of financial position. The costs of administering the Plan are absorbed by the Bank, except for fees paid to the investment managers and related charges, including custodian fees, which are borne by the Plan.

Participants are required to contribute 9 1/3% of their remuneration to the Plan and may also make voluntary contributions. The Institute's contribution is determined at a rate sufficient to cover that part of the costs of the Plan not covered by the participants' contributions.

*Postretirement Medical Benefits Plan*

The Institute participates in the cost-sharing plan of the Bank for retirees medical insurance premiums of ADB. Under the plan, the Institute is obligated to pay 80% of the Group Medical Insurance Plan premiums for retirees and their eligible dependents who elected to participate. The cost-sharing plan is currently unfunded.

Generally accepted accounting principles require an actuarially determined assessment of the periodic cost of postretirement medical benefits.

The following table sets forth the pension and postretirement benefits at 31 December 1998:

	<u>Pension Benefits</u>	<u>Post- retirement Medical Benefits</u>
Change in benefit obligation:		
Benefit obligation at beginning of year	\$ —	\$ —
Service cost	193,000	103,000
Interest cost	17,000	7,000
Participants' contributions	<u>54,000</u>	<u>—</u>
Benefit obligation at end of year	<u>\$ 264,000</u>	<u>\$ 110,000</u>
Change in plan assets:		
Fair value of plan assets at beginning of year	\$ —	\$ —
Employer's contribution	86,000	—
Plan participants' contributions	<u>54,000</u>	<u>—</u>
Fair value of plan assets at end of year	<u>\$ 140,000</u>	<u>\$ —</u>
Funded status	\$(124,000)	\$(110,000)
Unrecognized actuarial loss, prior service cost, and transition obligation	<u>—</u>	<u>—</u>
Net amount recognized	<u>\$ (124,000)</u>	<u>\$ (110,000)</u>
Amounts recognized in the statement of financial position consists of:		
Prepaid benefit cost	\$(124,000)	\$(110,000)
Accrued benefit liability	<u>80,000</u>	<u>—</u>
Net amount recognized	<u>\$ (44,000)</u>	<u>\$ (110,000)</u>
Weighted-average assumptions as of 31 December		
Discount rate	6.5%	6.5%
Expected return on plan assets	8.0%	N/A
Rate of compensation increase varies with age and averages	5.5%	5.5%

For measurement purposes, an 11.5% annual rate of increase in the per capita cost of covered health care benefits was assumed for the valuation as at 31 December 1998. The rate was assumed to decrease gradually to 3.5% for 2009 and remain at that level thereafter.

	<u>Pension Benefits</u>	<u>Postretirement Medical Benefits</u>
Components of net periodic benefit cost:		
Service cost	\$193,000	\$103,000
Interest cost	<u>17,000</u>	<u>7,000</u>
Net periodic benefit cost	<u>\$210,000</u>	<u>\$110,000</u>

Assumed health care cost trend rates have a significant effect on the amounts reported for the health care plan. A one-percentage-point change in assumed health care cost trend rates would have the following effects:

	<u>1-Percentage- Point Increase</u>	<u>1-Percentage- Point Decrease</u>
Effect on total service and interest cost components	22,000	(18,000)
Effect on postretirement benefit obligation	22,000	(18,000)