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## REPORT OF INDEPENDENT AUDITORS

### Asian Development Bank

In our opinion, the accompanying balance sheet and the related statements of income and expenses, of cash flows, and of changes in capital and reserves present fairly, in all material respects, in terms of United States dollars, the financial position of the Asian Development Bank – Ordinary Capital Resources at 31 December 1998 and 1997, and the results of its operations, its cash flows, and the changes in its capital and reserves for the years then ended, 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 statement presentation. We believe that our audits provide a reasonable basis for the opinion expressed above.

Our audits were conducted for the purpose of forming an opinion on the basic financial statements taken as a whole. The accompanying summary statements of loans and of borrowings as at 31 December 1998 and 1997, and of statement of subscriptions to capital stock and voting power as of 31 December 1998 are presented for purposes of additional analyses and are not required parts of the basic financial statements. Such information has been subjected to the auditing procedures applied in the audits of the basic financial statements and in our opinion, is fairly stated in all material respects in relation to the basic financial statements taken as a whole.

*PricewaterhouseCoopers LLP*

17 February 1999

## ASIAN DEVELOPMENT BANK—ORDINARY CAPITAL RESOURCES

## BALANCE SHEET

31 December 1998 and 1997

Expressed in Thousands of United States Dollars (Note B)

ASSETS				
	1998		1997	
DUE FROM BANKS (Notes B and C)		\$ 62,617		\$ 75,726
INVESTMENTS (Notes B, C, D, and J)				
Government and government-guaranteed obligations	\$ 4,500,649		\$ 2,929,853	
Time deposits	3,446,843		3,815,770	
Other obligations of banks	128,028	8,075,520	295,977	7,041,600
LOANS OUTSTANDING (OCR-5) (Notes A, B, and E)				
Members and guaranteed by members	24,358,635		18,456,407	
Private sector	401,257		382,495	
	24,759,892		18,838,902	
Less—allowance for possible losses	61,507	24,698,385	50,401	18,788,501
EQUITY INVESTMENTS (Notes A, B, and F)	237,008		211,647	
Less—allowance for possible losses	51,115	185,893	37,595	174,052
ACCRUED INCOME				
On investments	107,122		99,522	
On loans	362,474	469,596	244,716	344,238
RECEIVABLE FROM MEMBERS				
Nonnegotiable, noninterest-bearing demand obligations (Notes C and I)	350,289		326,231	
Amounts required to maintain value of currency holdings (Note I)	13,541		3,555	
Subscription installments (Note I)	5,964	369,794	4,550	334,336
OTHER ASSETS				
Receivable from currency swaps (Note H)	6,773,746		5,148,537	
Notional amounts required to maintain value of currency holdings (Note I)	718,693		627,349	
Property, furniture, and equipment (Notes B and G)	160,155		166,910	
Unamortized issuance costs of borrowings	63,815		57,443	
Miscellaneous (Note L)	74,604	7,791,013	61,065	6,061,304
<b>TOTAL</b>		<b>\$41,652,818</b>		<b>\$32,819,757</b>

See notes to financial statements (OCR-8).

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**LIABILITIES, CAPITAL, AND RESERVES**


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	<u>1998</u>		<u>1997</u>
BORROWINGS (OCR-6) (Note H)	\$23,743,713		\$17,494,446
ACCRUED INTEREST ON BORROWINGS	367,540		296,137
ACCOUNTS PAYABLE AND OTHER LIABILITIES			
Payable for currency swaps (Note H)	\$ 7,095,896		\$ 5,327,836
Notional amounts required to maintain value of currency holdings (Note I)	247,931		177,294
Payable to Asian Development Fund	-		721
Advance payments on subscriptions (Note I)	6,496		4,346
Miscellaneous (Note G)	127,995		217,121
Total liabilities	<u>7,478,318</u>		<u>5,727,318</u>
CAPITAL AND RESERVES (OCR-4)			
Capital Stock (OCR-7) (Notes B and I)			
Authorized (SDR34,909,940,000)			
Subscribed			
(SDR34,414,060,000 – 1998, SDR34,397,990,000 – 1997)	48,456,029		46,411,488
Less—"callable" shares subscribed	<u>45,041,908</u>		<u>43,147,207</u>
"Paid-in" shares subscribed	3,414,121		3,264,281
Less—subscription installments not due	<u>244,542</u>		<u>307,105</u>
Subscription installments matured	3,169,579		2,957,176
Less—capital transferred to the Asian Development Fund	67,036		64,237
	<u>3,102,543</u>		<u>2,892,939</u>
Ordinary Reserve (Note J)	6,211,102		5,867,429
Special Reserve (Note J)	181,608		178,969
Surplus (Note J)	276,645		256,645
Net income after allocations and appropriations (OCR-2) (Note J)	464,257		467,458
Accumulated other comprehensive income (OCR-4) (Note J)	<u>(172,908)</u>	10,063,247	<u>(361,584)</u>
<b>TOTAL</b>	<b>\$41,652,818</b>		<b>\$32,819,757</b>

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## ASIAN DEVELOPMENT BANK—ORDINARY CAPITAL RESOURCES

## STATEMENT OF INCOME AND EXPENSES

For the Years Ended 31 December 1998 and 1997

Expressed in Thousands of United States Dollars (Note B)

	<u>1998</u>		<u>1997</u>	
INCOME (Note K)				
From loans (Notes B and E)				
Interest	\$1,392,056		\$1,077,018	
Commitment charge	47,773		48,994	
Other	1,100	\$1,440,929	1,844	\$1,127,856
From investments (Notes B and D)				
Interest	353,592		295,321	
Net gain on sales	29,272	382,864	16,393	311,714
From other sources—net (Notes E and P)		8,747		10,148
TOTAL INCOME		\$1,832,540		\$1,449,718
EXPENSES (Note K)				
Interest and other financial expenses	1,206,478		853,241	
Administrative expenses (Note M)	121,701		95,728	
Provision for possible losses (Notes B, E, and F)	37,465		32,875	
TOTAL EXPENSES		1,365,644		981,844
NET INCOME		466,896		467,874
APPROPRIATION OF GUARANTEE FEES TO SPECIAL RESERVE (Note J)		(2,639)		(416)
<b>NET INCOME AFTER APPROPRIATION TO SPECIAL RESERVE</b>		<b>\$ 464,257</b>		<b>\$ 467,458</b>

See notes to financial statements (OCR-8).

**ASIAN DEVELOPMENT BANK—ORDINARY CAPITAL RESOURCES**  
**STATEMENT OF CASH FLOWS**

**For the Years Ended 31 December 1998 and 1997**

Expressed in Thousands of United States Dollars (Note B)

	<u>1998</u>	<u>1997</u>
<b>CASH FLOWS FROM OPERATING ACTIVITIES</b>		
Interest and other charges on loans received	\$ 1,066,994	\$ 881,577
Interest on investments received	363,414	326,214
Interest and other financial expenses paid	(987,994)	(790,604)
Administrative expenses paid	(121,908)	(87,447)
Other—net	25,905	9,114
Net Cash Provided by Operating Activities	<u>346,411</u>	<u>338,854</u>
<b>CASH FLOWS FROM INVESTING ACTIVITIES</b>		
Net cash withdrawn from (invested in) time deposits and other obligations of banks	525,129	(883,912)
Sales of investment securities	7,799,209	8,535,703
Maturities of investment securities	81,397,038	18,940,430
Purchases of investment securities	(90,727,988)	(28,009,400)
Cash collateral—securities loaned	—	93,018
Principal collected on loans	953,808	1,334,090
Loans disbursed	(5,344,655)	(5,073,249)
Property, furniture, and equipment acquired	(2,263)	(1,715)
Net purchases of equity investments	(63,398)	(10,345)
Net Cash Used in Investing Activities	<u>(5,463,120)</u>	<u>(5,075,380)</u>
<b>CASH FLOWS FROM FINANCING ACTIVITIES</b>		
Net proceeds of new borrowings	12,971,107	5,573,751
Bonds purchased for redemption and borrowings redeemed	(7,897,339)	(840,301)
Matured capital subscriptions collected	29,160	16,188
Issuance expenses paid	(17,019)	(4,727)
Demand obligations of members encashed	28,191	11,300
Net currency swaps	(18,297)	(23,858)
Net Cash Provided by Financing Activities	<u>5,095,803</u>	<u>4,732,353</u>
Effect of Exchange Rate Changes on Due from Banks	<u>7,797</u>	<u>(14,246)</u>
Net Decrease in Due from Banks	(13,109)	(18,419)
Due from Banks at Beginning of Year	<u>75,726</u>	<u>94,145</u>
Due from Banks at End of Year	<u>\$ 62,617</u>	<u>\$ 75,726</u>
<b>RECONCILIATION OF NET INCOME TO NET CASH PROVIDED BY OPERATING ACTIVITIES:</b>		
Net Income (OCR-2)	\$ 466,896	\$ 467,874
Adjustments to reconcile net income to net cash provided by operating activities:		
Change in accrued interest and other expenses	50,841	8,204
Change in accrued income, including interest and commitment charges added to loans	(381,927)	(240,851)
Depreciation and amortization	165,897	55,370
Net gain from sales of investments	(29,272)	(16,394)
Change in accrued/prepaid administrative expenses	(2,833)	19,877
Noncash reimbursement of administrative expenses	—	(27,262)
Provision for possible losses charged	37,465	32,875
Other—net	39,344	39,161
Net Cash Provided by Operating Activities	<u>\$ 346,411</u>	<u>\$ 338,854</u>

1 In addition, time deposits and related interest amounting to \$78,658 were transferred to the Technical Assistance Special Fund (\$230,000 to Asian Development Fund—1997).

2 In addition, nonnegotiable, noninterest-bearing demand promissory notes amounting to \$44,770 (\$29,148 – 1997) were received from members.

See notes to financial statements (OCR-8).

## ASIAN DEVELOPMENT BANK—ORDINARY CAPITAL RESOURCES

## STATEMENT OF CHANGES IN CAPITAL AND RESERVES

For the Years Ended 31 December 1998 and 1997

Expressed in Thousands of United States Dollars (Notes B and I)

	Capital Stock	Ordinary Reserve	Special Reserve	Surplus	Net Income After Allocations and Appropriations	Accumulated Other Comprehensive Income	Total
<b>Balance—</b>							
1 January 1997	\$3,021,721	\$5,522,677	\$178,553	\$230,000	\$571,645	\$ 141,054	\$9,665,650
Comprehensive income for the year 1997 (Note J)					467,458	(502,638)	(35,180)
Appropriation of guarantee fees to Special Reserve			416				416
Change in SDR value of paid-in shares subscribed	(179,528)						(179,528)
Additional paid-in shares subscribed during the year	-						-
Change in subscription installments not due	46,654						46,654
Change in SDR value of capital transferred to Asian Development Fund	4,092						4,092
Allocation of 1996 net income to ordinary reserve (Note J)		315,000			(315,000)		-
Allocation of 1996 net income to surplus (Note J)				256,645	(256,645)		-
Allocation of surplus to Asian Development Fund (Note J)				(230,000)			(230,000)
Credit to ordinary reserve for change in SDR value of capital stock (Note J)		29,752					29,752
<b>Balance—</b>							
31 December 1997 (Forward)	\$2,892,939	\$5,867,429	\$178,969	\$256,645	\$467,458	\$(361,584)	\$9,301,856

## ASIAN DEVELOPMENT BANK—ORDINARY CAPITAL RESOURCES

## SUMMARY STATEMENT OF LOANS

31 December 1998 and 1997

Expressed in Thousands of United States Dollars (Note B)

Borrower/Guarantor	Loans Outstanding <sup>1</sup>	Undisbursed Balance of Effective Loans <sup>2</sup>	Loans Not Yet Effective	Total Loans	Percent of Total Loans
Bangladesh	\$ —	\$ —	\$ 56,700	\$ 56,700	0.15
China, People's Republic of	3,724,115	2,401,048	1,462,000	7,587,163	19.45
Fiji	53,998	40,556	—	94,554	0.24
India	3,651,413	1,263,308	588,000	5,502,721	14.10
Indonesia	5,514,187	4,319,411	—	9,833,598	25.20
Kazakhstan	259,144	95,856	—	355,000	0.91
Korea, Republic of	4,060,643	315,000	—	4,375,643	11.21
Malaysia	505,526	168,087	40,000	713,613	1.83
Myanmar	935	—	—	935	n.a. <sup>3</sup>
Nauru	—	—	5,000	5,000	0.01
Nepal	28,680	17,854	—	46,534	0.12
Pakistan	2,060,883	502,592	—	2,563,475	6.57
Papua New Guinea	139,937	40,059	14,114	194,110	0.50
Philippines	2,682,637	1,462,428	230,462	4,375,527	11.21
Sri Lanka	5,000	—	5,000	10,000	0.03
Thailand	2,061,842	903,011	80,000	3,044,853	7.80
Uzbekistan	1,428	68,572	120,000	190,000	0.49
Viet Nam	—	30,000	—	30,000	0.08
	<u>24,750,368</u>	<u>11,627,782</u>	<u>2,601,276</u>	<u>38,979,426</u>	<u>99.90</u>
Regional	<u>9,524</u>	<u>30,476</u>	<u>—</u>	<u>40,000</u>	<u>0.10</u>
TOTAL – 31 December 1998	<u>24,759,892</u>	<u>11,658,258</u>	<u>2,601,276</u>	<u>39,019,426</u>	<u>100.00</u>
Allowance for possible losses	<u>(61,507)</u>			<u>(61,507)</u>	
<b>NET BALANCE – 31 December 1998</b>	<b><u>\$24,698,385</u></b>	<b><u>\$11,658,258</u></b>	<b><u>\$2,601,276</u></b>	<b><u>\$38,957,919</u></b>	
Made up of loans to:					
Members and guaranteed by members	\$ 24,358,635	\$ 11,531,796	\$ 2,514,576	\$ 38,405,007	
Private sector (net of allowance for possible losses)	<u>339,750</u>	<u>126,462</u>	<u>86,700</u>	<u>552,912</u>	
Net balance – 31 December 1998	<u>\$ 24,698,385</u>	<u>\$ 11,658,258</u>	<u>\$ 2,601,276</u>	<u>\$ 38,957,919</u>	
TOTAL – 31 December 1997	\$ 18,838,902	\$ 13,107,765	\$ 3,324,522	\$ 35,271,189	
Allowance for possible losses	<u>(50,401)</u>			<u>(50,401)</u>	
<b>NET BALANCE – 31 December 1997</b>	<b><u>\$18,788,501</u></b>	<b><u>\$13,107,765</u></b>	<b><u>\$3,324,522</u></b>	<b><u>\$35,220,788</u></b>	
Made up of loans to:					
Members and guaranteed by members	\$ 18,456,407	\$ 13,042,007	\$ 3,197,022	\$ 34,695,436	
Private sector (net of allowance for possible losses)	<u>332,094</u>	<u>65,758</u>	<u>127,500</u>	<u>525,352</u>	
Net Balance – 31 December 1997	<u>\$ 18,788,501</u>	<u>\$ 13,107,765</u>	<u>\$ 3,324,522</u>	<u>\$ 35,220,788</u>	

1 The interest rates charged on loans outstanding range from 5.44297% per annum to 11.00% per annum on loans to governments or with government-guarantee and 6.36031% per annum to 13.73% per annum for loans to the private sector. Amounts outstanding on loans made under the Pool-Based Variable Interest Rate System and market-based variable interest rate loans totalled \$23,339,784 (\$17,238,762 – 1997). The average yield on loans was 6.78% in 1998 (6.89% – 1997).

2 Of the undisbursed balances, the Bank has made irrevocable commitments to disburse various amounts totalling \$499,767 (\$528,143 – 1997).

3 Below 0.01%.

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**MATURITY OF EFFECTIVE LOANS**


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<b>Twelve Months Ending 31 December</b>	<b>Amount</b>	<b>Five Years Ending 31 December</b>	<b>Amount</b>
1999	\$ 1,131,343	2008	12,611,308
2000	1,155,939	2013	9,564,150
2001	1,321,783	2018	5,743,910
2002	1,540,074	2023	1,718,685
2003	1,598,210	2028	32,748
		<b>Total</b>	<b><u>\$36,418,150</u></b>

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**SUMMARY OF CURRENCIES RECEIVABLE ON LOANS OUTSTANDING**


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<b>Currency</b>	<b>1998</b>	<b>1997</b>	<b>Currency</b>	<b>1998</b>	<b>1997</b>
Australian dollar	\$ 220	\$ 305	Netherlands guilder	-	399
Deutsche mark	44,778	56,001	New Zealand dollar	1,233	2,683
Japanese yen	10,173,726	9,202,189	Swiss franc	1,186,268	1,226,729
Malaysian ringgit	41	115	United States dollar	13,353,626	8,350,481
			<b>Total</b>	<b><u>\$24,759,892</u></b>	<b><u>\$18,838,902</u></b>

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## ASIAN DEVELOPMENT BANK—ORDINARY CAPITAL RESOURCES

## SUMMARY STATEMENT OF BORROWINGS

31 December 1998 and 1997

Expressed in Thousands of United States Dollars (Note B)

	B o r r o w i n g s		
	Principal Outstanding <sup>1</sup>		Weighted Average Cost (%)
	1998	1997	1998
<b>Long-Term Borrowing:</b>			
Australian dollar	\$ 614,000	\$ —	5.57
Austrian schilling	85,036	78,904	8.08
Canadian dollar	161,447	174,935	7.88
Deutsche mark	1,019,306	947,651	5.61
Hong Kong dollar	580,832	193,598	8.70
Japanese yen	6,536,291	5,207,340	4.86
Korean won	66,918	56,529	12.33
Netherlands guilder	393,790	381,717	7.13
New Taiwan dollar	297,859	294,136	6.13
Pound sterling	537,495	286,934	8.86
Swiss franc	1,213,773	1,042,928	5.48
United States dollar	10,475,531	5,551,845	6.46
Subtotal	21,982,278	14,216,517	6.03 <sup>2</sup>
<b>Short-Term Borrowing:</b>			
United States dollar	1,797,500	3,325,000	5.21
Principal amount outstanding	23,779,778	17,541,517	5.96
Unamortized discounts and premiums	(36,065)	(47,071)	
<b>TOTAL</b>	<b>\$23,743,713</b>	<b>\$17,494,446</b>	

## MATURITY STRUCTURE OF BORROWINGS OUTSTANDING

Twelve Months Ending 31 December	Amount	Five Years Ending 31 December	Amount
2000	1,056,373	2013	758,510
2001	1,365,988	2018	847,263
2002	3,655,570	2023	43,582
2003	3,972,043	2028	1,460,000
		<b>Total</b>	<b>\$23,779,778</b>

<sup>1</sup> Includes zero coupon borrowings which have been recorded at their discounted values. The aggregate face amounts and discounted values of these borrowings (in United States dollar equivalents) are:

Currency	Aggregate Face Amount		Discounted Value	
	1998	1997	1998	1997
Swiss franc	\$ 353,707	\$336,013	\$147,263	\$132,909
United States dollar	1,254,591	676,063	838,909	319,058

## ASIAN DEVELOPMENT BANK—ORDINARY CAPITAL RESOURCES

## STATEMENT OF SUBSCRIPTIONS TO CAPITAL STOCK AND VOTING POWER

31 December 1998

Expressed in Thousands of United States Dollars (Note B)

MEMBER	SUBSCRIBED CAPITAL					VOTING POWER	
	Number of Shares	Percent of Total	Par Value of Shares			Number of Votes	Percent of Total
			Total	Callable	Paid-in		
REGIONAL							
Afghanistan	1,195	0.035	\$ 16,826	\$ 11,447	\$ 5,379	16,288	0.379
Australia	204,740	5.949	2,882,801	2,680,917	201,883	219,833	5.110
Bangladesh	36,128	1.050	508,693	473,070	35,623	51,221	1.191
Bhutan	220	0.006	3,098	2,774	324	15,313	0.356
Cambodia	1,750	0.051	24,641	20,445	4,196	16,843	0.392
China, People's Rep. of	228,000	6.625	3,210,308	2,985,432	224,876	243,093	5.651
Cook Islands	94	0.003	1,324	1,239	84	15,187	0.353
Fiji	2,406	0.070	33,877	31,498	2,380	17,499	0.407
Hong Kong, China	19,270	0.560	271,327	252,319	19,008	34,363	0.799
India	224,010	6.509	3,154,128	2,933,250	220,878	239,103	5.558
Indonesia	192,700	5.599	2,713,274	2,523,274	190,000	207,793	4.830
Japan	552,210	16.046	7,775,282	7,230,769	544,513	567,303	13.188
Kazakhstan	28,536	0.829	401,795	373,649	28,147	43,629	1.014
Kiribati	142	0.004	1,999	1,859	141	15,235	0.354
Korea, Rep. of	178,246	5.179	2,509,757	2,334,021	175,736	193,339	4.494
Kyrgyz Republic	10,582	0.307	148,998	138,564	10,434	25,675	0.597
Lao PDR	492	0.014	6,928	6,181	746	15,585	0.362
Malaysia	96,350	2.800	1,356,637	1,261,623	95,014	111,443	2.591
Maldives	142	0.004	1,999	1,859	141	15,235	0.354
Marshall Islands	94	0.003	1,324	1,239	84	15,187	0.353
Micronesia, Fed. States of	142	0.004	1,999	1,859	141	15,235	0.354
Mongolia	532	0.015	7,491	6,970	521	15,625	0.363
Myanmar	19,270	0.560	271,327	252,319	19,008	34,363	0.799
Nauru	142	0.004	1,999	1,859	141	15,235	0.354
Nepal	5,202	0.151	73,246	68,106	5,139	20,295	0.472
New Zealand	54,340	1.579	765,124	711,548	53,576	69,433	1.614
Pakistan	77,080	2.240	1,085,310	1,009,304	76,005	92,173	2.143
Papua New Guinea	3,320	0.096	46,747	43,494	3,253	18,413	0.428
Philippines	83,752	2.434	1,179,253	1,096,292	82,961	98,845	2.298
Samoa	116	0.003	1,633	1,464	169	15,209	0.354
Singapore	12,040	0.350	169,527	157,657	11,870	27,133	0.631
Solomon Islands	236	0.007	3,323	3,098	225	15,329	0.356
Sri Lanka	20,520	0.596	288,928	268,694	20,233	35,613	0.828
Taipei, China	38,540	1.120	542,655	504,666	37,989	53,633	1.247
Tajikistan	10,134	0.294	142,690	132,651	10,039	25,227	0.586
Thailand	48,174	1.400	678,304	630,797	47,507	63,267	1.471
Tonga	142	0.004	1,999	1,859	141	15,235	0.354
Tuvalu	50	0.001	704	648	56	15,143	0.352
Uzbekistan	23,834	0.693	335,590	312,090	23,500	38,927	0.905
Vanuatu	236	0.007	3,323	3,098	225	15,329	0.356
Viet Nam	12,076	0.351	170,034	150,532	19,501	27,169	0.632
<b>Total Regional (Forward)</b>	<b>2,187,185</b>	<b>63.555</b>	<b>\$ 30,796,221</b>	<b>\$28,624,433</b>	<b>\$2,171,788</b>	<b>2,805,998</b>	<b>65.230</b>

MEMBER	SUBSCRIBED CAPITAL					VOTING	POWER
	Number of Shares	Percent of Total	Par Value of Shares			Number of Votes	Percent of Total
			Total	Callable	Paid-in		
<b>Total Regional</b> (Forward)	<b>2,187,185</b>	<b>63.555</b>	<b>\$ 30,796,221</b>	<b>\$28,624,433</b>	<b>\$2,171,788</b>	<b>2,805,998</b>	<b>65.230</b>
<b>NONREGIONAL</b>							
Austria	12,040	0.350	169,527	157,657	11,870	27,133	0.631
Belgium	12,040	0.350	169,527	157,657	11,870	27,133	0.631
Canada	185,086	5.378	2,606,066	2,423,572	182,495	200,179	4.653
Denmark	12,040	0.350	169,527	157,657	11,870	27,133	0.631
Finland	12,040	0.350	169,527	157,657	11,870	27,133	0.631
France	82,356	2.393	1,159,597	1,078,382	81,215	97,449	2.265
Germany	153,068	4.448	2,155,243	2,004,303	150,941	168,161	3.909
Italy	55,975	1.627	788,145	727,332	60,813	71,068	1.652
Netherlands	36,294	1.055	511,030	475,252	35,778	51,387	1.195
Norway	12,040	0.350	169,527	157,657	11,870	27,133	0.631
Spain	12,040	0.350	169,527	157,657	11,870	27,133	0.631
Sweden	12,040	0.350	169,527	157,657	11,870	27,133	0.631
Switzerland	20,650	0.600	290,758	270,384	20,374	35,743	0.831
Turkey	12,040	0.350	169,527	157,657	11,870	27,133	0.631
United Kingdom	72,262	2.100	1,017,471	946,224	71,246	87,355	2.031
United States	552,210	16.046	7,775,282	7,230,769	544,513	567,303	13.188
<b>Total Nonregional</b>	<b>1,254,221</b>	<b>36.445</b>	<b>17,659,808</b>	<b>16,417,475</b>	<b>1,242,333</b>	<b>1,495,709</b>	<b>34.770</b>
<b>TOTAL</b>	<b>3,441,406</b>	<b>100.000</b>	<b>\$48,456,029</b>	<b>\$45,041,908</b>	<b>\$3,414,121</b>	<b>4,301,707</b>	<b>100.000</b>

Note: Figures may not add due to rounding.

See notes to financial statements (OCR-8).

## ASIAN DEVELOPMENT BANK—ORDINARY CAPITAL RESOURCES

### NOTES TO FINANCIAL STATEMENTS

31 December 1998 and 1997

#### NOTE A—NATURE OF OPERATIONS AND LIMITATIONS ON LOANS, GUARANTEES, AND EQUITY INVESTMENTS

##### *Nature of Operations*

The Asian Development Bank, a multilateral development finance institution, was established in 1966 with its headquarters in Manila, Philippines. The Bank and its operations are governed by the Agreement Establishing the Asian Development Bank (the Charter). Its principal objective is to help accelerate economic and social development of its developing member countries (DMCs) in the Asian and Pacific region by providing financial and technical assistance (TA) for projects and programs which will contribute to sustainable economic development and social advancement.

Mobilizing financial resources, including cofinancing, is an integral part of the Bank's operational activities. In addition, the Bank, alone or jointly, administers on behalf of donors, including members, their agencies and other development institutions, funds restricted for specific uses which include technical assistance for borrowers as well as for regional programs.

The Bank's ordinary operations comprise loans, equity investments, and guarantees. It finances its ordinary operations through borrowings, paid-in capital, and retained earnings.

##### *Limitations on Loans, Guarantees, and Equity Investments*

Article 12, paragraph 1 of the Charter provides that the total amount outstanding of loans, equity investments, and guarantees made by the Bank shall not exceed the total of the Bank's unimpaired subscribed capital, reserves, and surplus, exclusive of the special reserve. At December 1998 the total of such loans, equity investments, and guarantees aggregated approximately 71.7% (67.9% 1997) of the total subscribed capital, reserves, and surplus as defined.

Article 12, paragraph 3 of the Charter provides that equity investments shall not exceed 10% of the unimpaired actually paid-in capital together with reserves and surplus, exclusive of the special reserve. At 31 December 1998 such equity investments represented approximately 3.7% (4.2% 1997) of the paid-in capital, reserves, and surplus, as defined.

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

##### *Functional Currencies and Reporting Currency*

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

##### *Valuation of Capital Stock*

The authorized capital stock of the Bank is defined in Article 4, paragraph 1 of the Charter "in terms of United States dollars of the weight and fineness in effect on 31 January 1966" (the 1966 dollar) and the value of each share is defined as 10,000 1966 dollars. The capital stock had historically been translated into the current United States dollar (the Bank's unit of account) on the basis of its par value in terms of gold. From 1973 until 31 March 1978, the rate arrived at on this basis was \$1.20635 per 1966 dollar. Since 1 April 1978, at which time the Second Amendment to the Articles of Agreement of the International Monetary Fund (IMF) came into effect, currencies no longer have par values in terms of gold. Pending the Bank's selection of the appropriate successor to the 1966 dollar, the capital stock has been valued for purposes of these financial statements in terms of the Special Drawing Right (SDR) at the value in current United States dollars as computed by the IMF, with each share valued at SDR10,000.

As of 31 December 1998 the value of the SDR in terms of the current United States dollar was \$1.40803 (\$1.34925 –

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1997) giving a value for each share of the Bank's capital equivalent to \$14,080.30 (\$13,492.50 1997). However, the Bank could decide to fix the value of each share at \$12,063.50 based on the 31 March 1978 par value of the United States dollar in terms of gold.

*Translation of Currencies*

Assets and liabilities are translated from their functional currencies to the reporting currency generally at the applicable rates of exchange at the end of a reporting period. Income and expense amounts are translated for each semi-monthly period generally 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. Translation adjustments other than those relating to maintenance of SDR capital values (see *Notes I and J*), are charged or credited to "Accumulated translation adjustments" and reported in "CAPITAL AND RESERVES" as part of "Accumulated other comprehensive income."

*Investments*

All investment securities held by the Bank are considered by Management to be available for sale and are reported at estimated fair value, with unrealized gains and losses excluded from net income and reported in "CAPITAL AND RESERVES" as part of "Accumulated other comprehensive income." 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.). Realized gains and losses are included in income from investments and are measured by the difference between average cost or amortized cost and the net proceeds of sales.

*Loans*

The Bank's loans are made to or guaranteed by members, with the exception of loans to the private sector, and have maturities ranging between 5 and 30 years. The Bank requires its borrowers to absorb exchange risks attributable to

fluctuations in the value of the currencies which it has disbursed. It is the policy of the Bank to place in nonaccrual status loans for which principal, interest, or other charges are overdue by six months. When loans are in nonaccrual status, the related unpaid interest and other charges are reversed and are deducted from loan interest income and other charges, as appropriate. Interest and other charges on nonaccruing loans are included in income only to the extent that payments have actually been received by the Bank. The Bank follows a policy of not taking part in debt rescheduling agreements with respect to public sector loans. In the case of private sector loans, the Bank may agree to debt rescheduling only after alternative courses of action have been exhausted.

The Bank determines that a loan is impaired and therefore subject to provisioning when principal or interest is in arrears for one year for public sector loans made to or guaranteed by a member (unless there is clear and convincing evidence warranting the deferment or acceleration of such provisioning) and six months for private sector loans. If the present value of expected future cash flows discounted at the loan's effective interest rate is less than the carrying value of the loan, a valuation allowance is established with a corresponding charge to provision for possible losses.

The Bank's periodic evaluation of the adequacy of the allowance for possible losses is based on its past loan loss experience, known and inherent risks in existing loans, and adverse situations that may affect a borrower's ability to repay.

*Equity Investments*

Investments in equity securities without readily determinable fair values are reported at cost less an allowance for possible losses. Provisions for possible loss of value are established quarterly based on Management's evaluation of potential losses for such investments. Equity securities with readily determinable fair values are reported at fair value, with unrealized gains and losses excluded from net income

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## ASIAN DEVELOPMENT BANK—ORDINARY CAPITAL RESOURCES

## NOTES TO FINANCIAL STATEMENTS

31 December 1998 and 1997

and reported in “CAPITAL AND RESERVES” as part of “Accumulated other comprehensive income.” The Bank applies the equity method of accounting to one investment where it has the ability to exercise significant influence.

*Property, Furniture, and Equipment*

Property, furniture, and equipment is stated at cost and, except for land, is depreciated over estimated useful lives on a straight-line basis. Maintenance, repairs, and minor betterments are charged to expense.

*Accounting Estimates*

The preparation of the 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 and disclosure of contingent liabilities at the end of the year and the reported amounts of revenues and expenses during the year. The actual results could differ from those estimates.

*Statement of Cash Flows*

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

**NOTE C—RESTRICTIONS ON USE OF  
CURRENCIES AND DEMAND  
OBLIGATIONS OF MEMBERS**

In accordance with Article 24, paragraph 2(i) of the Charter, the use by the Bank or by any recipient from the Bank of certain currencies may be restricted by members to payments for goods or services produced and intended for use in their territories. With respect to the currencies of 37 DMCs for 1998 (36 – 1997), cash in banks (due from banks) and demand obligations totalling \$52,270,000 (\$53,359,000 –1997) and \$221,478,000 (\$213,054,000 – 1997), respectively, may be, but are not currently so restricted.

In accordance with Article 24, paragraphs 2(i) and (ii) of the Charter, two members have restricted the use by the Bank or by any recipient from the Bank of their currencies to payments for goods or services produced in their territories. Cash in banks (due from banks), demand obligations of members, and investments totalling \$22,000 (\$21,000 – 1997), \$2,579,000 (\$1,658,000 +1997) and \$4,460,000 (\$4,296,000 –1997), respectively, have been so restricted.

**NOTE D—INVESTMENTS**

The currency compositions of the investment portfolio as of 31 December 1998 and 1997 expressed in United States dollars were as follows:

Currency	1998	1997
Australian dollar	\$ 342,733,000	\$ 467,843,000
Canadian dollar	429,372,000	575,628,000
Deutsche mark	216,295,000	182,794,000
Italian lira	326,480,000	400,186,000
Japanese yen	1,223,655,000	634,515,000
Pound sterling	281,856,000	284,729,000
Swiss franc	456,100,000	558,629,000
United States dollar	4,162,395,000	3,275,633,000
Other	636,634,000	661,643,000
Total	\$8,075,520,000	\$7,041,600,000

The amortized cost and estimated fair value of the investments by contractual maturity as of 31 December 1998 were as follows:

	Amortized Cost	Estimated Fair Value
Due in one year or less	\$4,860,931,000	\$4,863,104,000
Due after one year through five years	2,662,653,000	2,676,482,000
Due after five years through ten years	531,537,000	535,934,000
Total	\$8,055,121,000	\$8,075,520,000

## CONTINUED

Additional information relating to investments in government and government-guaranteed obligations and other obligations of banks is as follows:

	<u>1998</u>	<u>1997</u>
<b>As of 31 December:</b>		
Amortized cost	\$4,608,278,000	\$3,209,783,000
Estimated fair value	4,628,677,000	3,225,830,000
Gross unrealized gains	25,500,000	19,549,000
Gross unrealized losses	5,101,000	3,502,000
<b>For the years ended 31 December:</b>		
Change in net unrealized gains/losses	4,352,000	(8,152,000)
Proceeds from sales	7,799,209,000	8,535,703,000
Gross realized gains	39,646,000	32,780,000
Gross realized losses	10,374,000	16,387,000

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.

To reduce credit risk, the Bank is restricted by its Investment Authority to invest in (a) securities which are obligations of a limited class of issuers, primarily government or government-guaranteed obligations, multilateral banks and selected commercial banks; and (b) exchange-traded derivatives of such securities. Exposure to interest rate risk may be adjusted within defined bands to reflect changing market circumstances. These adjustments are made through the purchase and sale of both securities and exchange-traded financial futures and options. The use of options has been minimal and there were no outstanding options as of 31 December 1998 (nil – 1997). To increase returns, the Bank may invest in securities denominated in currencies other than the original functional currencies and then enter into covered forward foreign exchange agreements in

order to maintain its original mix of functional currency holdings. Accordingly, the financial futures, options, and covered forwards are held for risk management rather than trading purposes.

**Futures:** Futures are contracts for delayed delivery of securities or money market instruments in which the seller agrees to make delivery at a specified future date of a specified instrument at a specified price or yield. Initial margin requirements are met with cash or securities, and changes in the market prices are settled daily. Changes in the market value of open futures contracts are recognized as gains or losses in the period of the change and included in income from investments. As 31 December 1998 there were no outstanding purchase contracts (\$9,664,000) nor outstanding sales contracts (\$9,477,000) (1997).

**Covered forwards:** Covered forwards are agreements in which cash in one currency is converted into a different currency and simultaneously a forward exchange agreement is executed providing for a future exchange of the two currencies in order to recover the currency converted. The Bank records the covered forward as an investment in the underlying currency. A receivable is created for the forward contract of the originating currency and a payable for the underlying instrument to be converted into the originating currency at maturity. Premiums or discounts are deferred and amortized as income from investments over the life of the underlying instrument. No covered forward agreements were outstanding as 31 December 1998 (nil – 1997).

**Short sales:** Short sales are sales of securities not held in the Bank's portfolio at the time of the sale. The Bank must purchase the security at a later date and bears the risk that the market value of the security will move adversely between the time of the sale and the time the security must be delivered. The payable created upon entering into a short sale is stated at the market value of the security subject to the short sale and gains and losses resulting from changes in market value are included in income from investments in the period of the change. Short sales are used

## ASIAN DEVELOPMENT BANK—ORDINARY CAPITAL RESOURCES

## NOTES TO FINANCIAL STATEMENTS

31 December 1998 and 1997

by the Bank for adjusting the risk exposure of the investment portfolio and for establishing spread positions to enhance income. As at 31 December 1998, there was no open short sale position (nil in 1997).

## NOTE E—LOANS AND GUARANTEES

*Loans*

The carrying amount and estimated fair value of loans outstanding at 31 December 1998 and 1997 were as follows:

	1998	
	Carrying Amount	Estimated Fair Value
Loans to the public sector with interest at variable rates	\$23,053,815,000	\$23,053,815,000
Loans to the public sector with interest at fixed rates	1,304,821,000	1,631,770,000
Loans to the private sector	<u>339,749,000</u>	<u>358,121,000</u>
Total	<u>\$24,698,385,000</u>	<u>\$25,043,706,000</u>

	1997	
	Carrying Amount	Estimated Fair Value
Loans to the public sector with interest at variable rates	\$16,981,610,000	\$16,981,610,000
Loans to the public sector with interest at fixed rates	1,474,797,000	1,829,896,000
Loans to the private sector	<u>332,094,000</u>	<u>343,590,000</u>
Total	<u>\$18,788,501,000</u>	<u>\$19,155,096,000</u>

Prior to 1 July 1986, the lending rate of the Bank was based on a multicurrency fixed lending rate system under which loans carried interest rates fixed at the time of loan approval for the entire life of the loans. Effective 1 July 1986, the Bank adopted a multicurrency pool-based variable lending rate system. In addition, in July 1992, the Bank introduced a pool-based variable United States dollar lending system, and in November 1994, a market-based variable lending system was made available to financial intermediaries in the public sector and to the private sector. For loans to the private sector, approximately 71% (68% in 1997) of the loans were based on a variable interest rate.

Undisbursed loan commitments and an analysis of loans by borrowing member countries as at 31 December 1998 are shown in OCR-5.

*Public Sector Loans*

Loans outstanding to or guaranteed by members with interest rates which vary based on the pool-based variable lending rate system were fair valued using an entry value method. Under this method, fair value was determined based on the terms at which a similar loan would currently be made by the Bank to a similar borrower. For such loans, fair value approximated the carrying amount. For undisbursed balances of effective loans and for loans not yet effective, the contractual amount approximated fair value.

Loans outstanding to or guaranteed by members with fixed interest rates (principally loans made prior to 1 July 1986) were fair valued using a discounted cash flow method. This method takes into account the scheduled cash flows over the average life, by currency, of the loans, and current funding costs for the average life, including a factor for administrative costs.

The estimated fair value of loans to or guaranteed by members was not affected by credit risks based on the Bank's experience with its borrowers.

## CONTINUED

Two public sector loans to Myanmar were in nonaccrual status but were not impaired as of 31 December 1998 (nil – 1997). The principal outstanding and overdue at that date was \$935,000 (nil – 1997). Overdue interest and other charges on these loans totalled \$70,000 (nil – 1997). Loans in nonaccrual status resulted in a reduction of \$68,000 (nil – 1997) in income from public sector loans for the year ended 31 December 1998.

*Private Sector Loans*

Loans outstanding to the private sector were fair valued using a discounted cash flow method. The estimated fair value of these loans was \$358,121,000 (\$343,590,000 – 1997).

Seven private sector loans were in nonaccrual status as of 31 December 1998 (nil – 1997). The principal outstanding at that date was \$51,609,000 (\$41,002,000 1997) of which \$17,752,000 (\$12,062,000 1997) was overdue. Overdue interest and other charges on these loans totalled \$6,665,000 (\$8,376,000 1997). Loans in nonaccrual status resulted in a reduction of \$5,226,000 (\$4,464,000 – 1997) in income from private sector loans for the year ended 31 December 1998.

*Loan Loss Provision*

The Bank has not suffered any losses of principal on loans made to or guaranteed by members. No loan loss provisions have been made against loans outstanding to or guaranteed by members, but loan loss provisions were made against private sector loans during the year (See Note K.)

Information appertaining to loans which are subject to loan loss provisions at 31 December 1998 and 1997 was as follows:

	<u>1998</u>	<u>1997</u>
Loans not subject to loss provisions	\$24,358,635,000	\$18,456,407,000
Loans subject to loss provisions	401,257,000	382,495,000
Total	<u>\$24,759,892,000</u>	<u>\$18,838,902,000</u>
Average amount of loans subject to loss provisions	\$ 381,108,000	\$ 383,388,000
Related interest income recognized on such loans	\$ 28,642,000	\$ 28,126,000
Cash received on related interest income on such loans	\$ 28,413,000	\$ 27,292,000

The changes in the allowance for possible loan losses during 1998 and 1997 were as follows:

	<u>1998</u>	<u>1997</u>
Balance – 1 January	\$ 50,401,000	\$ 38,544,000
Provision during the year	10,981,000	11,857,000
Provision written off	(218,000)	–
Translation adjustments	343,000	–
Balance – 31 December	<u>\$ 61,507,000</u>	<u>\$ 50,401,000</u>

*Loan Guarantees and Cofinancings*

The Bank extends guarantees for the benefit of its members which are not reflected in the financial statements. Such guarantees include partial credit guarantees where only certain principal and/or interest payments are covered. Such guaranteed payments are generally due 10 or more years from the loan inception date. The present value of the contingent future payment obligations of all outstanding guarantees at 31 December 1998 and 1997 is used to calculate the Bank's lending limitation. None of these amounts were subject to call as of that date. The Bank

## ASIAN DEVELOPMENT BANK—ORDINARY CAPITAL RESOURCES

## NOTES TO FINANCIAL STATEMENTS

## 31 December 1998 and 1997

estimates that the fair value of guarantees outstanding at 31 December 1998 approximates their present value. The estimated fair value of loans to or guaranteed by members was not affected by credit risks based on the Bank's experience with its borrowers.

As of 31 December 1998 and 1997, the outstanding amount and present value of the Bank's guarantee obligations covered:

	1998	
	Outstanding Guaranteed Amount	Present Value
Complementary Loans:		
China, People's Rep. of	\$ 28,674,000	\$ 14,857,000
India	65,374,000	30,431,000
Indonesia	24,833,000	12,704,000
Papua New Guinea	3,863,000	3,346,000
Subtotal	122,744,000	61,338,000
Bond Issue:		
Philippines	104,598,000	28,381,000
Term Loans:		
Sri Lanka	115,144,000	56,200,000
Thailand	108,963,000	97,449,000
Subtotal	224,107,000	153,649,000
Total	\$451,449,000	\$243,368,000

	1997	
	Outstanding Guaranteed Amount	Present Value
Complementary Loans:		
China, People's Rep. of	\$ 28,003,000	\$ 13,491,000
India	57,657,000	24,814,000
Indonesia	18,327,000	10,374,000
Papua New Guinea	4,500,000	4,385,000
Subtotal	108,487,000	53,064,000
Bond Issue:		
Philippines	92,250,000	23,176,000
Term Loans:		
Sri Lanka	47,766,000	22,888,000
Thailand	-	-
Subtotal	47,766,000	22,888,000
Total	\$248,503,000	\$ 99,128,000

The terms of the guarantee for Thailand cover the repayment of the principal amount due and outstanding under the Co-Financing Facility Agreement on each repayment date, up to, and including, 1 April 2001 and interest due and outstanding on each interest payment date, up to, and including interest due on or accrued up to 1 April 2001. Under certain circumstances, the guarantee may be extended to cover the principal amount due and outstanding on 1 October 2001 and 1 April 2002 and interest due and outstanding on each interest payment date after 1 April 2001 up to, and including, interest due on or accrued up to 1 April 2002. As of 31 December 1998, the facility has not been fully utilized. Had the facility been fully utilized, the guaranteed amount would have been \$664,214,000 and the present value would have been \$591,997,000. The availability period for drawdowns expired 26 January 1999. No further applications for drawdowns were received by that date.

The Bank functions as lead lender in cofinancing arrangements with other participating financial institutions who also provide funds to the Bank's public and private sector borrowers. In such capacity, the Bank provides loan administration services, which include loan disbursement and loan servicing. The participating financial institutions have no recourse to the Bank for their outstanding loan balances.

Loans administered by the Bank on behalf of participating institutions as of 31 December 1998 and 1997 were as follows:

	1998	
	Amount	No. of Loans
Public Sector Loans	\$ 931,603,000	41
Private Sector Loans	157,634,000	11
Total	\$1,089,237,000	52

CONTINUED

	1997	
	Amount	No. of Loans
Public Sector Loans	\$1,009,291,000	30
Private Sector Loans	88,288,000	15
Total	<u>\$1,097,579,000</u>	<u>45</u>

During the year ended 31 December 1998 a total of \$1,583,000 (\$509,000 1997) was received as compensation for arranging and administering such loans. This amount has been included in "Income from Other Sources."

#### NOTE F—EQUITY INVESTMENTS

The Bank's investments in equity securities issued by private enterprises located in DMCs include a \$10,342,000 (\$36,277,000 1997) investment in the Asian Finance and Investment Corporation Ltd. (AFIC) which is accounted for on the equity method. The holding represents 30.3% of the investee's issued ordinary share capital and net assets. The Bank also holds 100% of AFIC issued convertible noncumulative preference shares in the amount of \$25,000,000 (nil – 1997). In addition, the Bank, together with other financiers, has agreed to provide AFIC a revolving credit facility up to a maximum aggregate principal amount outstanding at any time of \$105,000,000 (nil – 1997). The Bank's obligations amount to \$40,000,000, of which, at 31 December 1998, the outstanding loan is \$9,524,000 (nil – 1997). This amount has been included in "Loans Outstanding" Note E).

Unrealized gains on equity investments reported at market value were \$6,729,000 at 31 December 1998 (\$15,387,000 – 1997) and are reported in "CAPITAL AND RESERVES" as part of "Accumulated other comprehensive income."

Undisbursed equity investment commitments were \$175,429,000 at 31 December 1998 (\$212,594,000 1997).

#### NOTE G—PROPERTY, FURNITURE, AND EQUIPMENT

In 1991, under the terms of an agreement with the Government of the Republic of the Philippines (Government), the Bank returned the former headquarters premises which had been provided by the Government. In accordance with the agreement as supplemented by a memorandum of understanding, the Bank was compensated \$22,657,000 for the return of these premises. The compensation is in lieu of being provided premises under the agreement and accordingly, is deferred and amortized over the estimated life of the new headquarters building as a reduction of occupancy expense. At 31 December 1998 accumulated depreciation for property, furniture, and equipment was \$61,396,000 (\$53,112,000 1997). The amortization for the years ended 31 December 1998 and 1997 amounted to \$566,000 reducing depreciation expense for the new headquarters building from \$4,700,000 (\$4,778,000 1997) to \$4,134,000 (\$4,212,000 1997). At 31 December 1998 the unamortized deferred compensation balance (included in "ACCOUNTS PAYABLE AND OTHER LIABILITIES – Miscellaneous") was \$18,174,000 (\$18,740,000 1997).

#### NOTE H—BORROWINGS AND SWAPS

The Bank uses derivative financial instruments in connection with its borrowing activities to diversify its funding sources across public and private debt markets, currencies and instruments. Currency swaps are used to convert a currency borrowed under advantageous terms into one of the Bank's major operational currencies, taking advantage of the opportunities offered in different financial markets. Such currency swaps enable the Bank to raise operationally needed currencies in a cost-efficient way and to maintain its borrowing presence in the major capital markets. Interest rate swaps are used generally to reduce balance sheet interest rate mismatches arising from lending operations.

The Bank issues structured debt which includes embedded currency and/or interest rate derivatives in order to decrease its cost of borrowing. However, the Bank enters into

## ASIAN DEVELOPMENT BANK—ORDINARY CAPITAL RESOURCES

## NOTES TO FINANCIAL STATEMENTS

31 December 1998 and 1997

simultaneous currency and/or interest rate swaps to fully hedge against the effects of such embedded derivatives.

The Bank has a potential risk of loss if the swap counterparty fails to perform its obligations (see Note O). In order to reduce such credit risk, the Bank only enters into long-term swap transactions with counterparties eligible under the Bank's swap guidelines which includes a requirement that the counterparties have a credit rating of double A or higher. The Bank does not anticipate that any of its counterparties will fail to perform their obligations under such agreements.

**Interest rate swaps:** Under a typical interest rate swap agreement used by the Bank, one party agrees to make periodic payments based on a notional principal amount and an interest rate that is fixed at the outset of the agreement. The counterparty agrees to make floating rate payments based on the same notional principal amount. Amounts receivable or payable under the terms of the swap are accrued over the period to which the payment relates and the related cost or income is included in interest and other financial expenses. The terms of the Bank's interest rate swap agreements specifically match the terms of particular borrowings.

**Currency swaps:** Under a typical currency swap agreement, one party agrees to make periodic payments in one currency while the counterparty agrees to make periodic payments in another currency. The payments may be fixed at the outset of the agreement or vary based on interest rates. A receivable is created for periodic payments to be received, and a payable is created for payments to be made. Swap premiums and discounts are deferred and amortized into interest and other financial expenses over the life of the underlying instruments. The terms of the Bank's currency swap agreements specifically match the terms of particular borrowings.

The fair value of borrowings outstanding is estimated using prevailing market prices where available, or estimated replacement values where market prices are not available.

Outstanding currency and interest rate swap agreements are fair valued at the estimated amount that the Bank would receive or pay to terminate the agreements based upon market quotes from dealers.

As of 31 December 1998 and 1997, the carrying amounts and estimated fair values of borrowings and swaps were as follows:

	1998	
	Carrying Amount	Estimated Fair Value
Balance sheet financial instruments:		
Borrowings	\$23,743,713,000	\$23,009,165,000
Currency swap receivables	6,773,746,000	7,029,990,000
Currency swap payables	7,095,896,000	7,563,385,000
	Notional Amount	Unrealized Gain
Off-balance sheet financial instruments:		
Interest rate swaps	\$ 3,158,490,000	\$ 115,676,000
	1997	
	Carrying Amount	Estimated Fair Value
Balance sheet financial instruments:		
Borrowings	\$17,494,446,000	\$18,532,945,000
Currency swap receivables	5,148,537,000	5,318,477,000
Currency swap payables	5,327,836,000	5,822,528,000
	Notional Amount	Unrealized Gain
Off-balance sheet financial instruments:		
Interest rate swaps	\$ 1,126,408,000	\$ 17,767,000

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**NOTE I—CAPITAL STOCK, CAPITAL TRANSFERRED TO ASIAN DEVELOPMENT FUND, MAINTENANCE OF VALUE OF CURRENCY HOLDINGS, AND MEMBERSHIP**

*Capital Stock*

The authorized capital stock of the Bank as of the end of 1998 and 1997 consists of 3,490,994 shares, of which 3,441,406 shares (3,439,799 – 1997) have been subscribed by members. Of the subscribed shares, 3,198,931 (3,197,866 – 1997) are “callable” and 242,475 (241,933 – 1997) are “paid-in.” The “callable” share capital is subject to call by the Bank only as and when required to meet the Bank’s obligations incurred on borrowings of funds for inclusion in its ordinary capital resources or on guarantees chargeable to such resources. The “paid-in” share capital has been paid or is payable in installments, partly in convertible currencies and partly in the currency of the subscribing member which may be convertible. In accordance with Article 6, paragraph 3 of the Charter, the Bank accepts nonnegotiable, noninterest-bearing demand obligations in satisfaction of the portion payable in the currency of the member, provided such currency is not required by the Bank for the conduct of its operations. The settlement of such amounts is not determinable and, accordingly, it is not practicable to fair value these receivables.

As of 31 December 1998 all matured installments amounting to \$3,169,579,000 (\$2,957,176,000 1997) were received except for \$5,964,000 from five countries (\$4,550,000 – 1997). Installments not due aggregating \$244,542,000 (\$307,105,000 – 1997) are receivable as follows:

**Year ending 31 December:**

1999	\$91,760,000	2001	\$63,633,000
2000	76,212,000	2002	12,937,000

Payments in respect of capital subscription installments in advance of due dates are shown in the balance sheet (under the caption “ACCOUNTS PAYABLE AND OTHER LIABILITIES”) as “Advance payments on subscriptions” pending the determination of the full value of such payments based on the rate of exchange to be used by the Bank as of the date on which such payments are actually due.

*Capital Transferred to Asian Development Fund*

Pursuant to the provisions of Article 19, paragraph 1(i) of the Charter, the Board of Governors has authorized the setting aside of 10% of the unimpaired “paid-in” capital paid by members pursuant to Article 6, paragraph 2(a) of the Charter and of the convertible currency portion paid by members pursuant to Article 6, paragraph 2(b) of the Charter as of 28 April 1973 to be used as a part of the Special Funds of the Bank. The resources so set aside amounting to \$67,036,000 as of 1 December 1998 (\$64,237,000 – 1997) expressed in terms of the SDR on the basis of \$1.40803 (\$1.34925 – 1997) per SDR (\$57,434,000 in terms of \$1.20635 per 1966 dollar *see Note B*), were allocated and transferred to the Asian Development Fund.

*Maintenance of Value of Currency Holdings*

Prior to 1 April 1978, the effective date of the Second Amendment to the IMF Articles, the Bank implemented maintenance of value in respect of holdings of member currencies in terms of 1966 dollars, in accordance with the provisions of Article 25 of the Charter and relevant resolutions of the Board of Directors. The “Amounts required to maintain value of currency holdings” under “RECEIVABLE FROM MEMBERS” represent the aggregate amounts receivable resulting from changes in exchange rates of member currencies from those previously used for the purpose of computing maintenance of value of the Bank’s holdings of certain member currencies. The settlement of such amounts is not determinable and, accordingly, it is not practicable to fair value these receivables.

## ASIAN DEVELOPMENT BANK—ORDINARY CAPITAL RESOURCES

## NOTES TO FINANCIAL STATEMENTS

31 December 1998 and 1997

Since 1 April 1978, inasmuch as the valuation of the Bank's capital stock and the basis of determining possible maintenance of value obligations are still under consideration, notional amounts have been calculated provisionally as receivable from or payable to members in order to maintain the value of currency holdings in terms of the SDR. The timing of any establishment and settlement of such amounts is uncertain and, accordingly, it is not practicable to fair value such receivables and payables. The notional amounts as of 31 December 1998 consisting of receivables of \$718,693,000 (\$627,349,000 1997) and payables of \$247,931,000 (\$177,294,000 1997) consist of (a) the increase of \$423,006,000 (\$307,089,000 1997) in amounts required to maintain the value of currency holdings to the extent of matured and paid capital subscriptions due to the increase in the value of the SDR in relation to the United States dollar during the period from 1 April 1978 to 31 December 1998 and (b) the net decrease of \$47,756,000 (\$142,966,000 1997) in the value of such currency holdings in relation to the United States dollar during the same period.

*Membership*

As of 31 December 1998, the Bank is owned by 57 member countries, 41 countries from the region and 16 countries from outside the region *see* OCR-7). During 1998, the Board of Governors approved the membership applications of Turkmenistan and Tajikistan. As at December 1998 Tajikistan has subscribed to 10,134 shares of the Bank's capital stock and remitted the required paid-in portion of its subscription.

**NOTE J—RESERVES***Ordinary Reserve and Net Income*

Under the provisions of Article 40 of the Charter, the Board of Governors shall determine annually what part of the net income shall be allocated, after making provision for reserves, to surplus and what part, if any, shall be distributed to the members. During 1998, \$367,458,000

(\$315,000,000 1997) of the net income after appropriation of guarantee fees to Special Reserve for the year ended 31 December 1997 was allocated to the Ordinary Reserve, and \$100,000,000 (\$256,645,000 1997) was allocated to Surplus.

The restatement of the capital stock for purposes of these financial statements on the basis of the SDR instead of the 1966 dollar *(see Note B)* resulted in a net charge of \$23,784,000 to the Ordinary Reserve during the year ended 31 December 1998 (credit of \$29,752,000 1997). That charge is the increase in the value of the matured and paid capital subscriptions caused by the change during the year in the value of the SDR in relation to the United States dollar not allocated to members as notional maintenance of value adjustments in accordance with resolutions of the Board of Directors.

*Special Reserve*

The Special Reserve represents commissions on loans and guarantee fees on guarantees set aside pursuant to Article 17 of the Charter. Special Reserve assets consist of term deposits and government and government-guaranteed obligations and are included under the heading "INVESTMENTS." For the year ended 31 December 1998 guarantee fees amounting to \$2,639,000 (\$416,000 1997) were appropriated to Special Reserve. The commission charged on loans was discontinued in 1986.

*Surplus*

During 1998 the Board of Governors allocated \$100,000,000 (\$256,645,000 1997) out of 1997 net income after appropriation of guarantee fees to Special Reserve to Surplus of which \$80,000,000 was subsequently reallocated and transferred to Technical Assistance Special Fund (\$230,000,000 to Asian Development Fund 1997). Surplus represents funds for future use to be determined by the Board of Governors.

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*Comprehensive Income and  
Accumulated Other Comprehensive Income*

In 1998, the Bank adopted Statement of Financial Accounting Standards (SFAS) No. 130 – Reporting Comprehensive Income issued by the Financial Accounting Standards Board. SFAS No. 130 establishes standards for reporting and display of comprehensive income and its components (revenues, expenses, gains, and losses) in a full set of general-purpose financial statements. Comprehensive income has two major components: net income and other comprehensive income. Other comprehensive income include such items as unrealized gains and losses on available-for-sale securities and foreign currency translation adjustments. The 1997 financial statements have been reclassified for comparative purposes.

**NOTE K—INCOME AND EXPENSES**

Total income from loans for the year ended 31 December 1998 was \$1,440,929,000 (\$1,127,856,000 1997). The average yield on the loan portfolio during the year was 6.78% (6.89% 1997).

Total income from investments for the year ended 31 December 1998 was \$382,864,000 (\$311,714,000 – 1997). 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, excluding unrealized gains and losses, was 5.27% (5.24% 1997). If unrealized gains and losses were included, the annualized rate of return would have been 5.32% (5.08% 1997).

Income from other sources includes a share in the net losses of equity investments of \$25,951,000 (\$8,484,000 – 1997) accounted for on the equity method.

Dividends received for the year ended 31 December 1998 amounted to \$18,173,000 (\$5,873,000 1997).

Total interest expense incurred for the year ended 31 December 1998 amounted to \$1,187,630,000 (\$839,363,000 1997).

Other financial expenses consist of amortization of borrowings' issuance costs and other expenses of \$16,039,000 (\$13,544,000 – 1997) and charges of \$2,809,000 (\$334,000 – 1997) representing the difference between reacquisition price and net carrying amount of borrowings extinguished prior to maturity.

Administrative expenses (other than those appertaining directly to ordinary operations and special operations) for the year ended 31 December 1998 were apportioned between Ordinary Capital Resources and the Asian Development Fund according to the number of loans and equity investments approved during the year. Of the total administrative expenses of \$193,176,000 (\$192,180,000 1997), \$71,475,000 (\$96,452,000 1997) was accordingly charged to the Asian Development Fund.

For the year ended 31 December 1998 the provision for possible losses totalled \$37,465,000 (\$10,981,000 for private sector loans and \$26,484,000 for equity investments). For the year ended 31 December 1997 the provision for losses totalled \$32,875,000 (\$11,857,000 for private sector loans and \$21,018,000 for equity investments).

**NOTE L—OTHER ASSETS—MISCELLANEOUS**

Included in miscellaneous assets are amounts receivable from the following related funds as of 31 December 1998 and 1997:

	<u>1998</u>	<u>1997</u>
Asian Development Fund (Note K)	\$12,101,000	\$ –
Technical Assistance Special Fund	65,000	117,000
Japan Special Fund	512,000	856,000
Asian Development Bank Institute Special Fund	<u>78,000</u>	<u>494,000</u>
Total	<u>\$12,756,000</u>	<u>\$1,467,000</u>

## ASIAN DEVELOPMENT BANK—ORDINARY CAPITAL RESOURCES

## NOTES TO FINANCIAL STATEMENTS

31 December 1998 and 1997

NOTE M—STAFF RETIREMENT PLAN AND  
POSTRETIREMENT MEDICAL  
BENEFITS*Staff Retirement Plan*

The Bank has a contributory defined benefit Staff Retirement Plan (the Plan). Every employee, 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 employee has not reached the normal retirement age of 60. The Plan applies also to members of the Board of Directors who elect to join the Plan. 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 accompanying balance sheet. 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 Bank'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*

In 1993, the Bank adopted a cost-sharing plan for retirees medical insurance premiums. Under the plan, the Bank is obligated to pay 80% of the Group Medical Insurance Plan premiums for retirees, including retired members of the Board of Directors, 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 and 1997:

	Pension Benefits	
	1998	1997
Change in benefit obligation:		
Benefit obligation at beginning of year	\$ 439,427,000	\$403,222,000
Service cost	16,813,000	14,704,000
Interest cost	31,853,000	31,237,000
Participants' contributions	19,802,000	13,847,000
Actuarial loss (gain)	20,335,000	(6,362,000)
Benefits paid	(22,723,000)	(17,221,000)
Benefit obligation at end of year	<u>\$ 505,507,000</u>	<u>\$439,427,000</u>
Change in plan assets:		
Fair value of plan assets at beginning of year	\$ 527,904,000	\$487,641,000
Actual return on plan assets	97,866,000	33,160,000
Employer's contribution	11,465,000	10,477,000
Plan participants' contributions	19,802,000	13,847,000
Benefits paid	(22,723,000)	(17,221,000)
Fair value of plan assets at end of year	<u>\$ 634,314,000</u>	<u>\$527,904,000</u>
Funded status	\$ 128,807,000	\$ 88,477,000
Unrecognized actuarial loss	(132,209,000)	(100,124,000)
Unrecognized prior service cost	4,739,000	5,721,000
Unrecognized transition obligation	(5,532,000)	(6,637,000)
Net amount recognized	<u>\$ (4,195,000)</u>	<u>\$ (12,563,000)</u>
Amounts recognized in the balance sheet consist of:		
Accrued benefit cost	\$ (4,195,000)	\$ (12,563,000)
Accrued benefit liability	(218,000)	(127,000)
Net amount recognized	<u>\$ (4,413,000)</u>	<u>\$ (12,690,000)</u>
Weighted-average assumptions as of 31 December		
Discount rate	6.5%	7.0%
Expected return on plan assets	8.0%	8.0%
Rate of compensation increase varies with age and averages	5.5%	6.0%

CONTINUED

	Postretirement Medical Benefits	
	1998	1997
Change in benefit obligation:		
Benefit obligation at beginning of year	\$ 51,476,000	\$ 37,192,000
Service cost	1,714,000	1,354,000
Interest cost	3,696,000	2,865,000
Participants' contributions	-	-
Actuarial loss	1,236,000	10,952,000
Benefits paid	(992,000)	(887,000)
Benefit obligation at end of year	<u>\$ 57,130,000</u>	<u>\$ 51,476,000</u>
Change in plan assets:		
Fair value of plan assets at beginning of year	\$ -	\$ -
Actual return on plan assets	-	-
Employer's contribution	992,000	887,000
Plan participants' contributions	-	-
Benefits paid	(992,000)	(887,000)
Fair value of plan assets at end of year	<u>\$ -</u>	<u>\$ -</u>
Funded status	<u>\$(57,130,000)</u>	<u>\$(51,476,000)</u>
Unrecognized actuarial loss	1,261,000	25,000
Unrecognized prior service cost	-	-
Unrecognized transition obligation	14,933,000	17,342,000
Net amount recognized	<u>\$(40,936,000)</u>	<u>\$(34,109,000)</u>
Amounts recognized in the balance sheet consist of:		
Accrued benefit cost	<u>\$(40,936,000)</u>	<u>\$(34,109,000)</u>
Accrued benefit liability	-	-
Net amount recognized	<u>\$(40,936,000)</u>	<u>\$(34,109,000)</u>
Weighted-average assumptions as of 31 December		
Discount rate	6.5%	7.0%
Expected return on plan assets	N/A	N/A
Rate of compensation increase varies with age and averages	5.5%	6.0%

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.

	Pension Benefits	
	1998	1997
Components of net periodic benefit cost:		
Service cost	\$ 16,813,000	\$ 14,704,000
Interest cost	31,853,000	31,237,000
Expected return on plan assets	(41,824,000)	(36,674,000)
Amortization of prior service cost	982,000	982,000
Amortization of transition obligation	(1,105,000)	(1,105,000)
Recognized actuarial loss	(3,622,000)	(2,154,000)
Net periodic benefit cost	<u>\$ 3,097,000</u>	<u>\$ 6,990,000</u>

	Postretirement Medical Benefits	
	1998	1997
Components of net periodic benefit cost:		
Service cost	\$ 1,714,000	\$ 1,354,000
Interest cost	3,696,000	2,865,000
Expected return on plan assets	-	-
Amortization of prior service cost	-	-
Amortization of transition obligation	2,409,000	2,409,000
Recognized actuarial loss	-	(711,000)
Net periodic benefit cost	<u>\$ 7,819,000</u>	<u>\$ 5,917,000</u>

The projected benefit obligation, accumulated benefit obligation, and fair value of plan assets for the pension plan with accumulated benefit obligations in excess of plan assets were \$487,000,000, \$487,000,000, and \$218,000,000,

## ASIAN DEVELOPMENT BANK—ORDINARY CAPITAL RESOURCES

## NOTES TO FINANCIAL STATEMENTS

31 December 1998 and 1997

respectively as of 31 December 1998 and \$337,000,000, \$337,000,000, and \$127,000,000, respectively, as of 31 December 1997.

A one-percentage-point change in assumed health care 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	1,182,000	(925,000)
Effect on postretirement benefit obligation	10,342,000	(8,302,000)

## NOTE N—FAIR VALUE OF FINANCIAL INSTRUMENTS

The carrying amounts and estimated fair values of the Bank's significant financial instruments as of 31 December 1998 and 1997 are summarized as follows:

**On-balance sheet  
financial instruments:**

## ASSETS:

Due from banks	\$ 62,617,000	\$ 62,617,000
Investments (Note D)	8,075,520,000	8,075,520,000
Loans outstanding (Note E)	24,698,385,000	25,043,706,000
Equity investments	185,893,000	185,893,000
Other assets		
Nonnegotiable, noninterest-bearing demand obligations	350,289,000	350,289,000
Currency swap receivables (Note H)	6,773,746,000	7,029,990,000

## LIABILITIES:

Borrowings (Note H)	23,743,713,000	23,009,165,000
Other liabilities		
Currency swap payables (Note H)	7,095,896,000	7,563,385,000

<u>Notional/Contract Amount</u>	<u>Unrealized Gain (Loss)</u>
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**Off-balance sheet  
financial instruments:**

Investments (Note D)		
Futures – Purchase	\$ –	\$ –
– Sell	–	–
Borrowings (Note H)		
Interest rate swaps	3,158,490,000	115,676,000
Guarantees (Note E)	451,449,000	–

## CONTINUED

	1997	
	Carrying Amount	Estimated Fair Value
<b>On-balance sheet financial instruments:</b>		
ASSETS:		
Due from banks	\$ 75,726,000	\$ 75,726,000
Investments (Note D)	7,041,600,000	7,041,600,000
Loans outstanding (Note E)	18,788,501,000	19,155,096,000
Equity investments	174,052,000	174,052,000
Other assets		
Nonnegotiable, noninterest-bearing demand obligations	326,231,000	326,231,000
Currency swap receivables (Note H)	5,148,537,000	5,318,477,000
LIABILITIES:		
Borrowings (Note H)	17,494,446,000	18,532,945,000
Other liabilities		
Currency swap payables (Note H)	5,327,836,000	5,822,528,000
	Notional/Contract Amount	Unrealized Gain (Loss)
<b>Off-balance sheet financial instruments :</b>		
Investments (Note D)		
Futures – Purchase	\$ 9,664,000	\$ –
– Sell	9,477,000	–
Borrowings (Note H)		
Interest rate swaps	1,126,408,000	17,767,000
Guarantees (Note E)	248,503,000	–

Additional fair value information, including methods used to estimate certain values, is included in the notes referenced in the above table.

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.

If available, quoted market values are used to determine fair values. Financial instruments for which market quotations are not readily available are valued using methodologies and assumptions which necessarily require the use of subjective judgments. Accordingly, the actual value at which such financial instruments could be exchanged in a current transaction or whether they are actually exchangeable is not determinable.

**NOTE O—OFF-BALANCE SHEET CREDIT RISK**

The Bank is a party to off-balance sheet financial instruments. These financial instruments involve elements of credit risk in excess of amounts reflected on the balance sheet. Credit risk represents the maximum potential accounting loss due to possible nonperformance by obligors and counterparties under the terms of the contract.

	1998	1997
<b>Credit risk at 31 December:</b>		
Currency swaps (Note H)	\$156,657,000	\$72,257,000
Interest rate swaps (Note H)	117,823,000	34,445,000
Guarantees (Note E)	243,368,000	99,128,000

**NOTE P—SPECIAL AND TRUST FUNDS**

The Bank's operations include special operations, which are financed from special funds resources, consisting of the Asian Development Fund, the Technical Assistance Special Fund, Japan Special Fund, and the Asian Development Bank Institute Special Fund.

ASIAN DEVELOPMENT BANK—ORDINARY CAPITAL RESOURCES

NOTES TO FINANCIAL STATEMENTS

31 December 1998 and 1997

In addition, the Bank, alone or jointly with donors, administers on behalf of the donors, including members of the Bank, their agencies and other development institutions, projects/programs supplementing the Bank's operations. Such projects/programs are funded with external funds administered by the Bank and with external funds not under the Bank's administration. The funds are restricted for specific uses including technical assistance to borrowers and technical assistance for regional programs. The responsibilities of the Bank under these arrangements range from project processing to project implementation including the facilitation of procurement of goods and services.

Special funds and funds administered by the Bank on behalf of the donors are not included in the assets of Ordinary Capital Resources. The breakdown of the total of such funds together with the funds of the special operations as of 31 December 1998 and 1997 was as follows:

	1998	
	Total Net Assets	No. of Funds
Special Funds		
Asian Development Fund	\$20,535,398,000	1
Technical Assistance Special Fund	97,187,000	1
Japan Special Fund	183,170,000	1
Asian Development Bank Institute Special Fund	17,998,000	1
Subtotal	<u>20,833,753,000</u>	<u>4</u>
Trust Funds		
Funds administered by the Bank	48,585,000	21
Funds not administered by the Bank	17,322,000	1
Subtotal	<u>65,907,000</u>	<u>22</u>
Total	<u>\$20,899,660,000</u>	<u>26</u>

	1997	
	Total Net Assets	No. of Funds
Special Funds		
Asian Development Fund	\$18,219,229,000	1
Technical Assistance Special Fund	53,968,000	1
Japan Special Fund	204,421,000	1
Asian Development Bank Institute Special Fund	8,890,000	1
Subtotal	<u>18,486,508,000</u>	<u>4</u>
Trust Funds		
Funds administered by the Bank	51,733,000	19
Funds not administered by the Bank	19,670,000	1
Subtotal	<u>71,403,000</u>	<u>20</u>
Total	<u>\$18,557,911,000</u>	<u>24</u>

During the year ended 31 December 1998 a total of \$992,000 (\$735,000 – 1997) was received as compensation for administering projects/programs under Trust Funds. The amount has been included in "Income from Other Sources."