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## REPORT OF INDEPENDENT ACCOUNTANTS

We have audited the following financial statements of the Asian Development Bank – Japan Special Fund (JSF):

- |       |   |
|-------|---|
| JSF-1 | Statement of Financial Position, 31 December 1997                                     |
| JSF-2 | Statement of Activities and Changes in Net Assets for the Year Ended 31 December 1997 |
| JSF-3 | Statement of Cash Flows for the Year Ended 31 December 1997                           |
| JSF-4 | Notes to Financial Statements, 31 December 1997                                       |

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 audit. The financial statements of the Asian Development Bank – Japan Special Fund for the year ended 31 December 1996 were audited by other independent accountants whose report dated 19 February 1997 expressed an unqualified opinion on those statements.

We conducted our audit in accordance with generally accepted auditing standards. Those standards 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 audit provides a reasonable basis for our opinion.

In our opinion, the financial statements audited by us present fairly, in all material respects, the financial position of the Asian Development Bank – Japan Special Fund at 31 December 1997 and the results of its activities and changes in net assets and its cash flows for the year in conformity with generally accepted accounting principles.

*Price Waterhouse*  
*(International Firm)*

25 February 1998

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**ASIAN DEVELOPMENT BANK - JAPAN SPECIAL FUND**  
**STATEMENT OF ACTIVITIES AND CHANGES IN NET ASSETS**  
**For the Year Ended 31 December 1997**  
**(With Comparative Amounts for the Year Ended 31 December 1996)**  
Expressed in Thousands of United States Dollars (Note B)

	1997	1996
<b>CHANGES IN UNRESTRICTED NET ASSETS</b>		
CONTRIBUTIONS (Notes B and G)	\$ -	\$ 61,947
REVENUE FROM OTHER SOURCES	209	7
NET ASSETS RELEASED FROM RESTRICTIONS (Notes B and G)	17,138	19,369
Totals	<u>17,347</u>	<u>81,323</u>
<b>EXPENSES</b>		
Services to member countries (Note B)	72,477	76,037
Administrative expenses	1,278	1,253
Provision for losses charged (Notes B and D)	-	1
Totals	<u>73,755</u>	<u>77,291</u>
CONTRIBUTIONS AND REVENUE IN EXCESS OF (LESS THAN) EXPENSES	(56,408)	4,032
EXCHANGE LOSSES (Note B)	(10,137)	(11,694)
DECREASE IN UNRESTRICTED NET ASSETS BEFORE TRANSLATION ADJUSTMENTS	(66,545)	(7,662)
TRANSLATION ADJUSTMENTS (Note B)	(15,787)	(23,398)
DECREASE IN UNRESTRICTED NET ASSETS AFTER TRANSLATION ADJUSTMENTS	<u>(82,332)</u>	<u>(31,060)</u>
<b>CHANGES IN TEMPORARILY RESTRICTED NET ASSETS</b>		
CONTRIBUTIONS (Notes B and G)	-	17,925
<b>REVENUE</b>		
From investments (Notes B and C)		
Interest	\$ 2,534	\$ 2,350
Unrealized investment gains (losses)	(317) 2,217	88 2,438
NET ASSETS RELEASED FROM RESTRICTIONS (Notes B and G)		
Project related	(15,860)	(18,116)
Administrative expenses	(1,278) (17,138)	(1,253) (19,369)
INCREASE (DECREASE) IN TEMPORARILY RESTRICTED NET ASSETS BEFORE TRANSLATION ADJUSTMENTS	(14,921)	994
TRANSLATION ADJUSTMENTS (Note B)	(13,228)	(14,276)
DECREASE IN TEMPORARILY RESTRICTED NET ASSETS AFTER TRANSLATION ADJUSTMENTS	<u>(28,149)</u>	<u>(13,282)</u>
DECREASE IN NET ASSETS	(110,481)	(44,342)
NET ASSETS AT BEGINNING OF THE YEAR	314,902	359,244
<b>NET ASSETS AT END OF THE YEAR</b>	<b>\$204,421</b>	<b>\$314,902</b>

See notes to financial statements (JSF-4).

JSF-1

## ASIAN DEVELOPMENT BANK - JAPAN SPECIAL FUND

## STATEMENT OF FINANCIAL POSITION

31 December 1997

(With Comparative Amounts at 31 December 1996)

Expressed in Thousands of United States Dollars (Note B)

	1997	1996
<b>ASSETS</b>		
DUE FROM BANKS (Note B)	\$ 38,458	\$ 428
INVESTMENTS (Notes A, B and C)		
Government and government-guaranteed obligations	\$ 538	\$ 27,603
Time deposits	<u>268,914</u>	<u>388,543</u>
	269,452	416,146
EQUITY INVESTMENTS (Notes A, B and D), net	373	702
ACCRUED REVENUE	460	916
OTHER ASSETS	3,207	2,429
<b>TOTALS</b>	<b>\$311,950</b>	<b>\$420,621</b>
<b>LIABILITIES AND UNCOMMITTED BALANCES</b>		
PAYABLE TO ORDINARY CAPITAL RESOURCES	\$ 856	\$ 476
ACCOUNTS PAYABLE AND OTHER LIABILITIES	90	106
UNDISBURSED COMMITMENTS (Notes B and E)	106,583	105,137
NET ASSETS (JSF-2), represented by:		
Uncommitted Balances (Note F)		
Unrestricted	\$129,463	\$211,795
Temporarily restricted (Note G)	<u>34,642</u>	<u>61,165</u>
	164,105	272,960
Net Accumulated Investment Income		
Temporarily restricted (Notes A and G)	<u>40,316</u>	<u>41,942</u>
	204,421	314,902
<b>TOTALS</b>	<b>\$311,950</b>	<b>\$420,621</b>

See notes to financial statements (JSF-4).

## ASIAN DEVELOPMENT BANK - JAPAN SPECIAL FUND

## STATEMENT OF CASH FLOWS

For the Year Ended 31 December 1997

(With Comparative Amounts for the Year Ended 31 December 1996)

Expressed in Thousands of United States Dollars (Note B)

	1997	1996
CASH FLOWS FROM OPERATING ACTIVITIES		
Contributions received	\$ -	\$ 79,872
Interest on investments received	3,563	2,502
Interest on bank account	177	-
Services to member countries paid	(72,321)	(65,129)
Administrative expenses paid	(822)	(1,178)
Net Cash Provided by (Used in) Operating Activities	<u>(69,403)</u>	<u>16,067</u>
CASH FLOWS FROM INVESTING ACTIVITIES		
Net cash withdrawn from time deposits	85,544	15,435
Sales of investment securities	79,410	82,144
Maturities of investment securities	17,521	-
Purchases of investment securities	(74,690)	(113,500)
Net Cash Provided by (Used in) Investing Activities	<u>107,785</u>	<u>(15,921)</u>
CASH FLOWS FROM FINANCING ACTIVITIES		
Cash received from (paid to) Ordinary Capital Resources and others - net	(329)	120
Effect of Exchange Rate Changes on Due from Banks	(23)	(18)
Net Increase in Due From Banks	38,030	248
Due from Banks at Beginning of the Year	428	180
Due from Banks at End of the Year	<u>\$ 38,458</u>	<u>\$ 428</u>
RECONCILIATION OF DECREASE IN NET ASSETS TO NET CASH PROVIDED BY (USED IN) OPERATING ACTIVITIES:		
Decrease in net assets (JSF-2)	\$ (110,481)	\$ (44,342)
Adjustments to reconcile decrease in net assets to net cash provided by (used in) operating activities:		
Unrealized investment (gains) losses	317	(88)
Translation adjustments	38,304	37,674
Gain on sale of investments	(411)	-
Provision for losses charged	-	1
Undisbursed commitments	1,446	9,721
Amortisation of discounts/premiums	1,085	907
Other - net	337	12,194
Net Cash Provided by (Used in) Operating Activities	<u>\$ (69,403)</u>	<u>\$ 16,067</u>

See notes to financial statements (JSF-4).

**ASIAN DEVELOPMENT BANK – JAPAN SPECIAL FUND**

**NOTES TO FINANCIAL STATEMENTS**

**31 December 1997**

**(With Comparative Amounts at 31 December 1996)**

**CONTINUED**

**NOTE A – NATURE OF OPERATIONS**

The Japan Special Fund (JSF) was established in March 1988 when Japan and the Bank entered into a financial arrangement whereby Japan agreed to make an initial contribution and the Bank became the administrator. The purpose of JSF is to help developing member countries of the Bank restructure their economies and broaden the scope of opportunities for new investments, thereby assisting the recycling of funds to developing member countries of the Bank. While the JSF resources are used mainly to finance technical assistance (TA) operations, these resources may also be used for equity investment operations in the Bank's developing member countries. Under the agreement between the Bank and the Government of Japan, the Bank may invest the proceeds of JSF pending disbursement. The revenue from such investments, if retained by the Bank, may only be used to pay for direct and identifiable costs incurred in the administration of JSF.

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

*Presentation of the Financial Statements*

The financial statements of the JSF are presented on the basis of unrestricted and temporarily restricted net assets.

JSF reports the contributions of cash and other assets as restricted support if they are received with donor stipulations that limit the use of the donated assets. When the donor restriction expires, that is, when a stipulated time or purpose restriction is accomplished, temporarily restricted net assets are reclassified to unrestricted net assets and reported in the Statement of Activities and Changes in Net Assets as net assets released from restrictions.

*Investments*

All investment securities held by JSF 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 amortised cost is used to approximate fair value for certain short-term investments not traded in the market (time deposits, etc.).

*Contributions*

Contributions by Japan are included in the financial statements from the date indicated by the government of Japan that funds are expected to be made available. Contributions which are restricted by the donor for specific TA projects/programs are classified as temporarily restricted contributions. Those without any stipulation as to specific use are accounted for as unrestricted contributions and reported as such.

*Services to Member Countries*

Services to member countries are recognized in the financial statements of JSF when the TA projects/programs are approved and effective. In general, TA projects/programs become effective when a letter of agreement has been signed by the beneficiary. Upon completion of the TA projects/programs, any undisbursed amounts are written back as a reduction in the services to member countries for the year and the corresponding undisbursed commitments are reduced accordingly.

*Functional Currency and Reporting Currency*

The functional currency of JSF is the Japanese yen while the reporting currency is the United States dollar. 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 year are translated at the applicable exchange rates as of the dates the contributions are received. Rev-

**ASIAN DEVELOPMENT BANK – JAPAN SPECIAL FUND**

**NOTES TO FINANCIAL STATEMENTS**

**31 December 1997**

**(With Comparative Amounts at 31 December 1996)**

Revenue and expense amounts in Japanese yen are translated for each semi-monthly 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. Exchange gains or losses on currency transactions arise on translation differences between the date a project/program is committed and the timing of disbursements. Exchange gains or losses are charged or credited to operations.

*Equity Investments*

Equity investments with readily determinable fair values are reported at fair value. The Bank makes provisions for possible loss of value quarterly based on management's evaluation of potential losses on investments without readily determinable fair values.

*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 and the reported amounts of income 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 JSF considers that its cash and cash equivalents are limited to "DUE FROM BANKS".

**NOTE C – INVESTMENTS**

The currency compositions of the investment portfolio as of 31 December 1997 and 31 December 1996 were as follows:

<u>Currency</u>	<u>1997</u>	<u>1996</u>
Japanese yen	\$151,829,000	\$416,146,000
United States dollar	<u>117,085,000</u>	<u>–</u>
Totals	<u>\$268,914,000</u>	<u>\$416,146,000</u>

As of 31 December 1997, the estimated fair value of the investments was \$269,452,000 (\$416,146,000 – 1996), and was 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 0.68% (0.60% – 1996).

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 – EQUITY INVESTMENTS**

The Bank used JSF resources to make an equity investment in India in 1990 totalling \$373,000 at 31 December 1997 (\$702,000 – 1996). The investment is reported at its estimated fair value and the unrealized loss (gain – 1996) is included in income for the year.

**NOTE E – UNDISBURSED COMMITMENTS**

Undisbursed commitments are denominated in United States dollars and represent effective technical assistance for projects/ programs which have not been disbursed. The fair value of such commitments approximates the amounts outstanding because JSF expects that disbursements will substantially be made for all the projects/programs covered by the commitments.

## CONTINUED

**NOTE F – UNCOMMITTED BALANCES**

Uncommitted balances are composed of amounts which have not been committed by the Bank as at 31 December 1997. These balances include TA projects/programs that had been approved but which had not yet become effective.

As of 31 December 1997 and 31 December 1996 these balances were as follows:

	<u>1997</u>	<u>1996</u>
Uncommitted Balances	\$164,105,000	\$272,960,000
TA projects/programs approved by the Government of Japan and the Bank but not yet effective	(49,243,000)	(25,313,000)
TA projects/programs approved by the Government of Japan and not yet effective	<u>(44,236,000)</u>	<u>(28,915,000)</u>
Uncommitted Balances Available for new Commitments	<u>\$ 70,626,000</u>	<u>\$218,732,000</u>

**NOTE G – CONTRIBUTIONS AND TEMPORARILY RESTRICTED NET ASSETS**

All contributions for the years ended 31 December 1997 and 31 December 1996 were received during the respective years. Some of the contributions received were with the restriction that they were to be utilized for specific TA projects/programs. Such contributions were classified as temporarily restricted support.

Temporarily restricted uncommitted balances are available for the following purposes as of 31 December 1997 and 31 December 1996:

	<u>1997</u>	<u>1996</u>
Environment-related Activities	\$20,113,000	\$37,596,000
Private Sector Promotion	8,760,000	14,963,000
Women in Development	5,586,000	8,367,000
Training/Symposium	<u>183,000</u>	<u>239,000</u>
Totals	<u>\$34,642,000</u>	<u>\$61,165,000</u>

Accumulated investment income net of accumulated administrative expenses has been categorized as temporarily restricted net assets because, under the terms of the agreement between the Bank and the donor, it may only be used for the defrayment of the Fund's administrative expenses.

Accumulated investment income net of accumulated administrative expenses of \$41,942,000 at 31 December 1996 and related accounts in the 1996 statement of activities and changes in net assets have been reclassified from unrestricted to temporarily restricted net assets to conform with the 1997 presentation.

Net assets released from restrictions relate to commitments for services to member countries satisfying the conditions specified by the donor and, in the case of accumulated investment income, to defray the administrative expenses of the Fund.

**NOTE H – 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.

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**ASIAN DEVELOPMENT BANK – JAPAN SPECIAL FUND****NOTES TO FINANCIAL STATEMENTS****31 December 1997****(With Comparative Amounts at 31 December 1996)**

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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.

The Fund's statement of financial position carrying amounts are considered to approximate fair values for all significant financial instruments. See Notes B, C, D and E for discussions with respect to investments, equity investments and undisbursed commitments, respectively.

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