


MANAGEMENT'S DISCUSSION AND ANALYSIS

FINANCIAL STATEMENTS





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MANAGEMENT'S DISCUSSION AND ANALYSIS

The Management's Discussion and Analysis contains forward-looking statements that may be identified by such terms as "believes," "expects," "intends," or words of similar meaning. Such statements involve several assumptions and estimates based on current expectations, which are subject to risks and uncertainties beyond ADB's control. Consequently, actual future results could differ materially from those currently anticipated.

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The term "country," as used in the context of ADB, refers to a member of ADB and does not imply any view on the part of ADB as to the member's sovereignty or independent status.

Overview

The Asian Development Bank (ADB) is an international development finance institution whose vision is to make the Asian and Pacific region free of poverty. ADB was established in 1966 through the "Agreement Establishing the Asian Development Bank" (the Charter), ratified by 31 countries to promote the social and economic development of the region. ADB has 61 members (as of 31 December 2002), of which 44 are in the region. ADB is rated triple-A by Moody's and Standard & Poors.

In pursuing its objectives, ADB provides different forms of financial assistance to its developing member countries (DMCs). The main instruments are loans, technical assistance, grants, guarantees, and equity investments, which are met through various funding resources. Such funding resources are ADB's ordinary capital resources (OCR) and Special Funds resources to fund operations solely under ADB's administration; and trust funds, which are externally funded and administered by ADB on behalf of donors. The Charter requires that each funding resource be kept separate from the other.

Ordinary capital resources

The OCR come from three distinct sources: private placements and capital markets in the form of borrowings; paid-in capital provided by shareholders; and accumulated retained income (reserves), which provide a buffer for risk arising from operations (see <http://www.adb.org/about/fnncemgt.asp>).

Financial policies

ADB adheres to prudent and conservative financial policies. The most important financial risk facing ADB as a multilateral development bank (MDB) is country credit risk. ADB's income and reserves policy, and its liquidity policy, serve as the operational framework for addressing such country credit risk.

The review of the income and reserves policy, undertaken by the Board of Directors in 1997, identified ADB's decisive income indicators—the interest coverage ratio (ICR) and the reserve to loan ratio (RLR). The ICR is the ratio of net income to financial expenses plus a factor of one. It measures the extent to which net income can fall without jeopardizing ADB's ability to service its financial expenses from current income. The review concluded that the minimum level for the ICR should be 1.31. The RLR is the ratio of total reserves to the sum of outstanding loans, equity investments, and guarantees. The RLR measures the adequacy of ADB's earning base relative to its loan assets. The policy maintains an RLR of 25%. At the end of 2002, ADB's ICR was 1.65 and the RLR was 30.83.

Due to the need to increase ADB's risk-bearing capacity resulting from the 1997 Asian financial crisis, ADB reviewed its OCR loan charges in 1999. A change in the structure of these charges was recommended and approved by the Board of Directors, and became effective on 1 January 2000. ADB's lending spread for pool-based loans

was raised from 40 to 60 basis points. A front-end fee of 1% was introduced for new loans, and a commitment fee of 0.75% was adopted for new program loans.

In 2002, the Board of Directors approved a new liquidity policy, which is aimed at maintaining investor confidence by ensuring that ADB has the capacity to meet its cash requirements in the event of a major disruption in its cash flows. The old policy maintained a prudential minimum level of liquid assets at no less than 40% of year-end undisbursed loan balance. The new policy has more dynamic cash flow-driven liquidity requirements:

- the prudential minimum level of liquidity to be held at all times during a calendar year is 40% of the next 3 years' proxy net cash requirements, which is the sum of net disbursement and debt redemption;
- the discretionary liquidity will have a ceiling of 50% of the size of prudential minimum liquidity and will be funded by debt without prior authorization of the Board of Directors; and
- the core liquidity portfolio, which will be broadly equivalent to the prudential minimum liquidity, can be funded by equity capital and debt.

The three major elements that determine the effectiveness and efficiency of ADB's financial inter-mediation consist of its stand-alone financial strength, appropriateness of its financial loan products, and the strength of shareholder support.

The annual review of ADB's income outlook and allocation of the previous year's net income provides the instrument for reviewing ADB's medium-term prospects and the adequacy of its equity capital, net income, and reserves. These are measures of ADB's risk-bearing capacity, which play an important role in ensuring ADB's financial soundness. Based on the annual review, the Board of Directors makes a recommendation to the Board of Governors on the amount of ADB's OCR net income that should be allocated to the ordinary reserve and how much to surplus.

In May 2000, ADB's Board of Governors adopted Resolution No. 270, requesting that the Board of Directors study ADB's future resource requirements to finance its ordinary operations, and to report its findings and recommendations to the Board of Governors. However, ADB's financial framework had to be reviewed before the Board of Directors could assess the implications of the OCR lending operations projected in the 3-year rolling work program on its resource requirements over the medium term. Thus, there was a need to address issues related to the statutory controls and policies related to lending and borrowing limitations.

The Board of Directors considered in October 2002¹ a working paper reviewing ADB's lending and borrowing limitations in light of different interpretations taken by other MDBs on lending limitations, and in response to questions of interpretation raised by several ADB Directors about ADB's lending and borrowing limitation policies, as provided for by ADB's Charter. The review concluded that

¹ This set of policies was adopted by the Board in February 2003.

Selected Financial Data

(as of 31 December, amounts in \$ million)

	Statutory Reported Basis ^a				
	2002	2001	2000	1999	1998
Income and Expenses					
From Loans	1,710.0	1,813.7	1,861.3	1,674.6	1,440.9
From Investments	330.4	403.4	399.9	344.0	382.9
From Other Sources	19.7	21.6	39.7	9.2	8.7
Total Income	2,060.1	2,238.7	2,300.9	2,027.8	1,832.5
Interest and Other Financial Expenses	1,155.1	1,434.1	1,576.7	1,447.2	1,206.5
Administrative Expenses ^b	90.6	59.0	92.6	105.9	121.7
Technical Assistance to Members	56.0	20.0	–	–	–
Provision for Losses	4.5	9.8	5.9	24.8	37.4
Total Expenses	1,306.2	1,522.9	1,675.2	1,577.9	1,365.6
Operating Income Before FAS 133	753.9	715.8	625.7	449.9	466.9
FAS 133 Adjustments	224.8	147.5	–	–	–
Net Income	978.7	863.3	625.7	449.9	466.9
Average Earning Assets	38,244	36,272	36,693	34,788	28,558
Annual Return on Average Earning Assets	2.56%	2.28%	1.71%	1.29%	1.63%
Return on Loans	5.93%	6.42%	6.59%	6.41%	6.78%
Return on Investments	4.26%	5.91%	5.09%	3.96%	5.27%
Cost of Borrowings	4.10%	5.54%	5.90%	5.66%	5.70%
Reserve-to-Loan Ratio	32.04%	28.47%	27.26%	25.97%	27.70%
Interest Coverage Ratio	1.85	1.58 ^c	1.40	1.31	1.39
		Pre-FAS 133 Basis		Current Value Basis	
		2002	2001	2002^d	2001^d
Net Income		754	716	1,183	473
Average Earning Assets		38,244	36,271	40,680	38,431
Annual Return on Average Earning Assets		1.97%	1.97%	2.91%	1.23%
Return on Loans		5.93%	6.42%	10.53%	3.11%
Return on Investments		4.26%	5.91%	9.80%	2.66%
Cost of Borrowings		4.32%	5.63%	9.85%	3.02%
Reserve-to-Loan Ratio		30.83%	28.09%	28.99%	26.66%
Interest Coverage Ratio		1.65	1.50	2.02	1.33

– Nil.

^a Financial Accounting Standards (FAS) 133 was implemented in 2001. Accordingly, statutory reported basis is the same as pre-FAS 133 basis prior to 2001.

^b Net of administration charge allocated to the Asian Development Fund.

^c Excludes the one-time cumulative effect of recording the adoption of FAS 133 on 1 January 2001.

^d Excludes the cumulative effect of the adoption of current value basis accounting.

the financial framework ADB would adopt in assessing its future resource requirements would include

- a policy limiting ADB's outstanding commitments, i.e., the sum of outstanding disbursed loan and undisbursed loan balance, equity investments, and guarantees² to no more than the sum of the total callable capital, paid-in capital, and reserves (including surplus but excluding special reserve); and
- a policy limiting ADB's gross outstanding borrowings to no more than the sum of callable capital of nonborrowing members, paid-in capital, and reserves (including surplus and special reserves), subject to the Charter limit of 100% of callable capital.

² ADB's financial policies require that the political risk guarantees be charged against ADB's lending limitation at the nominal value of the guaranteed obligations and at the present value of partial credit guarantees.

Basis of financial reporting

Statutory reporting: ADB prepares its financial statements in accordance with generally accepted accounting principles applied in the United States (US). Effective 1 January 2001, ADB adopted the Financial Accounting Standards (FAS) 133, "Accounting for Derivative Instruments and Hedging Activities," along with its related amendments under FAS 138. These two standards are collectively termed "FAS 133."

As defined and required by FAS 133, ADB has marked all derivative instruments to fair value and reported in the balance sheet with changes in the fair value recognized in current net income.

Under FAS 133, two options exist in accounting for derivative instruments: hedge or non-hedge accounting. In hedge accounting, changes in the fair value of certain hedge

instruments have to be reflected in current income, while others have to be reflected in other comprehensive income as an adjustment to the carrying value of the hedge item. In non-hedge accounting, all changes in the fair value of hedge instruments need to be recognized as current income. A preliminary assessment using the FAS 133 hedge accounting criteria indicates that most of ADB's derivative transactions are highly effective in hedging underlying transactions and are appropriate for its operations in achieving lower funding costs. At the same time, however, ADB has also found that applying the FAS 133 hedge criteria does not entirely reflect ADB's risk management strategies. Compliance with the hedge criteria would impose undue constraints on ADB's future borrowing, loan, and hedge programs, and likely detract from its focus of minimizing the cost of borrowings. Therefore, ADB believes it is more important to continue pursuing the objective of minimizing the cost of borrowings rather than follow the accounting definition of a qualifying hedge. The application of the FAS 133 qualifying hedge criteria would not make the economic risks inherent in ADB's financial assets and liabilities fully evident. Accordingly, ADB chooses to adopt non-hedge accounting and recognizes changes in fair value of derivative instruments in the period as part of the net income.

Supplemental reporting: ADB manages its balance sheet by selectively using derivatives to minimize the interest rate and currency risks associated with its financial assets and liabilities. It uses derivative instruments to enhance asset/liability management of individual positions and portfolios, and to reduce borrowing costs. As certain financial instruments (including all derivatives and certain investments) are recognized at their fair value, while others are still at cost (loans and borrowings), FAS 133 does not fully reflect the overall economic value of ADB's financial instruments.

ADB also prepares two supplemental financial statements in this *Management's Discussion and Analysis*: current value basis and pre-FAS 133 basis. ADB believes that the financial statements under current value basis present the economic value of all its financial instruments. On the other hand, the pre-FAS 133 basis presents the financial information that is comparable to that in prior years for management information and decision making.

Discussion and analysis of current value

The Condensed Current Value Balance Sheets (*see page 130*) present ADB's estimates of the economic value of its financial assets and liabilities, taking into consideration changes in interest rates, exchange rates, and credit risks. Current value reflects the exit price for financial instruments with liquid markets and accordingly is similar in most respects to fair value. For financial instruments with no market, current value reflects the expected cash flow streams discounted with the appropriate interest and exchange rates. The reversal of the FAS 133 effects removes the impact related to the adoption of FAS 133, as these effects are already accounted for in the current value adjustment. *For details, see the Condensed Current Value Income Statement and a summary of the effects on net income of the current value adjustments in the balance sheet on page 131.*

Current value balance sheets

Loan portfolio: The majority of ADB's loans are made to or guaranteed by ADB members. ADB does not sell its loans, believing that there is no comparable market for them. The current value of loans incorporates Management's best estimate of the probable expected cash flows, including interest, to ADB. Estimated cash flows from principal repayments, interest, and other loan charges are discounted by the applicable market yield curves for ADB's funding cost, plus ADB's lending spread.

The current value also includes ADB's appropriate credit risk assessment. To recognize the risk inherent in these and other potential overdue payments, ADB has adjusted the value of the loans through its loan loss provisioning for private sector operations. For public sector loans, ADB has never suffered a loss, except opportunity losses resulting from the difference between the present value of expected payments for interest and charges, according to the loan's contractual terms, and actual timing of cash flows. Accordingly, no loan loss provision is provided against public sector loans.

The positive adjustment of \$2.4 billion, equivalent to 8.3% of ADB's loan balance—from the FAS 133 reported basis of \$29.5 billion to the current value basis of \$31.9 billion—indicates that the loans in the portfolio, on average, carry a higher interest rate than ADB would be able to originate such loans at current rates.

Investments and related swaps: Under both the reported and current value basis, the investments held by ADB are carried and reported at fair values. Fair value is based on market quotations. In the case of instruments for which market quotations are not readily available, the current value is calculated using market-based valuation models. During 2002, ADB entered into two asset swap transactions as a result of the new liquidity policy.

Equity investments: Equity investments with readily determinable fair values (i.e., market value) are reported at fair value. Unlisted equity investments without market value are reported at cost less allowance for losses, which represent a fair approximation of the current value.

Receivables from members: Receivables from members consist of unrestricted and may be restricted promissory notes. The current value of receivables from members is based on the cash flow of the projected encashment of the promissory notes, discounted using appropriate interest and exchange rates.

Borrowings after swaps: The current value of these liabilities includes the value of the debt securities and the financial derivative instruments associated with the borrowings portfolio. The current value of these liabilities is calculated using market-based valuation models.

The increase in the valuation of these liabilities of \$2.4 billion—equivalent to 9.3% in the value of the borrowings portfolio after swaps, from the FAS 133 reported basis of \$26.0 billion to the current value basis of \$28.4 billion—represents the difference between the average cost of ADB's borrowing portfolio and its current value based on relevant market yield curves.

Current value income statements

The total current value adjustment of \$429.0 million for the year ended 31 December 2002 (unfavorable adjustment of \$243.2 million in 2001) represents the change in the current value of all ADB's financial instruments during the year. The current value adjustment reflects changes in both interest rates and currency exchange rates. For 2001, the current value adjustment included a transition loss of \$81.7 million, which was the cumulative effect of the adoption of the current value basis of accounting on 1 January 2001.

For the year 2002, current value net income was \$1.2 billion, compared with the pre-FAS 133 net income of \$753.9 million and the statutory reported net income of \$978.7 million (see table on page 131). The \$429 million increase from the pre-FAS 133 basis to current value basis (i.e., current value adjustment) comprises net effect of \$130.9 million from the valuation of all outstanding financial instruments; \$89.7 million of unrealized investment holding gains; and \$208.4 million of accumulated translation adjustments for the year ended 31 December 2002 (see table on page 131).

Condensed Current Value Balance Sheets at 31 December 2002 and 2001

(\$ thousand)

	31 December 2002					31 December 2001
	FAS 133 Reported Basis	Reversal of FAS 133 Effects ^a	Pre-FAS 133 Basis	Current Value Adjustments	Current Value Basis	Current Value Basis
Due from Banks	473,360	-	473,360	-	473,360	68,823
Investments and Accrued Income ^b	9,102,853	-	9,102,853	-	9,102,853	8,330,341
Loans Outstanding and Accrued Interest	29,485,151	(1,098)	29,484,053	2,438,050	31,922,103	30,697,150
Equity Investment	211,267	-	211,267	-	211,267	208,018
Receivable from Members	316,547	-	316,547	(135,055)	181,492	200,543
Receivable from Swaps						
Investments	511,937	(8,005)	503,932	8,005	511,937	-
Borrowings	9,231,868	(641,150)	8,590,718	641,150	9,231,868	6,379,403
Other Assets	504,209	-	504,209	-	504,209	478,096
TOTAL	49,837,192	(650,253)	49,186,939	2,952,150	52,139,089	46,362,374
Borrowings and Accrued Interest	26,236,013	(9,221)	26,226,792	2,418,385	28,645,177	26,734,750
Payable for Swaps						
Investments	548,218	(17,167)	531,051	17,167	548,218	-
Borrowings	9,027,166	(261,793)	8,765,373	261,793	9,027,166	6,784,076
Accounts Payable and Other Liabilities	1,673,632	-	1,673,632	-	1,673,632	1,955,836
Total Liabilities	37,485,029	(288,181)	37,196,848	2,697,345	39,894,193	35,474,662
Paid-In Capital	3,246,837	-	3,246,837	-	3,246,837	2,989,775
Net Notional Maintenance of Value Receivable/Payable	(488,456)	-	(488,456)	-	(488,456)	(462,456)
Ordinary Reserve	8,470,092	-	8,470,092	(466,055)	8,004,037	7,589,531
Special Reserve	183,764	-	183,764	-	183,764	182,903
Surplus	116,645	-	116,645	-	116,645	116,645
Cumulative Revaluation Adjustments Account	147,501	(147,501)	-	-	-	-
Net Income after Appropriation	977,815	(224,756)	753,059	429,010	1,182,069	471,314
Accumulated Other Comprehensive Income	(302,035)	10,185	(291,850)	291,850	-	-
Total Equity	12,352,163	(362,072)	11,990,091	254,805	12,244,896	10,887,712
TOTAL	49,837,192	(650,253)	49,186,939	2,952,150	52,139,089	46,362,374

- Nil.

() Negative.

^a Translated using exchange rates at transaction date.

^b Including securities transferred under securities lending arrangement of \$1,129,208 in 2002 and \$1,489,870 in 2001.

Condensed Current Value Income Statements for the Years Ended 31 December 2002 and 2001
(\$ thousand)

	31 December 2002			31 December 2001
	Year-to-Date Reported Basis	Adjustments to Current Value	Year-to-Date Current Value Basis	Year-to-Date Current Value Basis
Income				
From Loans	1,709,943	–	1,709,943	1,813,640
From Investments	330,448	–	330,448	403,436
From Other Sources Net	19,723	–	19,723	21,634
Total Income	2,060,114	–	2,060,114	2,238,710
Expenses				
Interest and Other Financial Expenses	1,155,167	–	1,155,167	1,434,112
Administrative Expenses	90,553	–	90,553	59,039
Technical Assistance to Member Countries	55,998	–	55,998	19,962
Provision for Losses	4,476	(4,476)	–	–
Total Expenses	1,306,194	(4,476)	1,301,718	1,513,113
Operating Income				
Before FAS 133 Adjustment	753,920	4,476	758,396	725,597
FAS 133 Adjustment	224,756	(224,756)	–	–
Current Value Adjustments	–	429,010	429,010	(243,150)
Provision for Losses	–	(4,476)	(4,476)	(9,838)
Net Income	978,676	204,254	1,182,930	472,609
Appropriation of Guarantee Fees to Special Reserve	(861)	–	(861)	(1,295)
Net Income After Appropriation	977,815	204,254	1,182,069	471,314

Summary of Current Value Adjustments
(\$ thousand)

	Balance Sheet Effects (as of 31 December 2002)				Less Prior Year Effects	Income Statement Effects (Year to Date)	
	Loans	Investments	Borrowings after Swaps	Other Assets		31 December 2002	31 December 2001
Total Current Value Adjustments on Balance Sheet	2,438,050	(9,162)	(2,039,028)	(135,055)	(123,930)	130,875	40,189
Unrealized Gains on Investments						89,702	23,969
Accumulated Translation Adjustments						208,433	(307,308)
Total Current Value Adjustments						429,010	(243,150)

The net increase of \$130.9 million in the current value adjustments on the balance sheet during 2002 was a result of an increase in the mark-to-current value on loans of \$792.8 million and on receivable from members of \$12.9 million, offset by an increase in the mark-to-current value on borrowings of \$665.7 million and an investment swap payable of \$9.1 million.

Unrealized investment holding gains, reflected as part of "Accumulated Other Comprehensive Income" under the reported basis, are presented as current value adjustments for current value reporting. For 2002, the change in the mark-to-market unrealized investment holding gains amounted to \$89.7 million.

The increase in the current value adjustment from 2001 to 2002, considering the \$81.7 million loss in

transition adjustment, was due primarily to changes in exchange rates. Translation adjustments, reflected as part of "Accumulated Other Comprehensive Income" under the reported basis, are presented as current value adjustments. Specifically, a significant portion of ADB's loans, investments, and borrowings was denominated in Japanese yen. While the Japanese yen depreciated sharply in 2001 and appreciated sharply in 2002 against the US dollar, this exchange rate volatility resulted in a significant positive change of translation adjustments of \$208.4 million.

Operating activities

In pursuing its objectives, ADB provides financial assistance through loans, technical assistance, guarantees, and

equity investments to its DMCs to help them meet their development needs.

Loans: Until 30 June 2001, ADB's three lending windows for loans from OCR were the pool-based multicurrency loan (PMCL) window, pool-based single-currency loan (PSCL) window in US dollars, and market-based loan (MBL) window. With the introduction of the London interbank offered rate (LIBOR)-based loan (LBL) products on 1 July 2001, the PMCL and MBL were no longer offered; on 1 July 2002, the PSCL in US dollars was retired. For ADB to evolve into a full-fledged LIBOR-based lender, the Board of Directors also approved the retirement of all existing loan products, and the program of offering borrowers the option to transform the undisbursed balances of their PSCLs in US dollars and MBLs into LBLs provided that the undisbursed PSCL balance was not less than 40% of the loan amount as of 30 June 2001. By 15 December 2002, total undisbursed balances of \$6.7 billion under 97 PSCLs to 11 borrowing countries were transformed to LBL terms as scheduled. *For details, see the table below and <http://www.adb.org/finance/>.* As of 31 December 2002, the transformation program had been completed. The LBL is a timely response to borrower demand for new ADB financial loan products that suit project needs and external debt risk management strategies. The LBL products give borrowers a high degree of flexibility in managing interest rate and exchange rate risks and at the same time provide low intermediation risk to ADB.

OCR loan approvals, disbursements, repayments, and prepayments: In 2002, 36 OCR loans totaling \$4.0 billion were approved, compared with 30 OCR loans totaling \$4.0 billion approved in 2001. Of the total OCR 2002 amount, 87.9% of the loans went to India, People's Republic of China, Pakistan, and Indonesia (in order of magnitude). Disbursements in 2002 totaled \$3.1 billion, an increase of 7.6% from \$2.8 billion in 2001. Principal repayments for the year were \$3.3 billion, of which

\$2.0 billion represented prepayments on loans. In 2002, 18 loans were fully prepaid and 1 loan was partially prepaid. On 31 December 2002, cumulative loans outstanding after allowance for losses amounted to \$29.1 billion.

Status of loans: Three public sector OCR loans (two to Myanmar and one to Nauru), and 13 private sector loans were in nonaccrual status at the end of 2002. The total outstanding balances of these public and private sector loans were \$3.2 million (\$3.1 million in 2001) and \$83.9 million (\$75.4 million in 2001), respectively. The increase in private sector loans in nonaccrual status was mainly due to defaulted loans. One loan came out of nonaccrual status during 2002. The combined total of \$87.1 million represented 0.3% of the total OCR loans outstanding.

Lending rates: The lending rates for the PMCL and PSCL US dollar loan windows are based on the previous semester's average cost of borrowings. The interest from the MBL window is on either fixed or floating rate terms. The lending rates for MBLs are determined on the basis of the 6-month LIBOR with reset dates of either 15 March and 15 September or 15 June and 15 December. *ADB's pool-based variable lending rates for multicurrency loans and for US dollar loans are shown on page 133.* For the second half of 2002, the lending rate for multicurrency loans decreased to 3.91% per annum, and the rate for US dollar loans decreased to 6.34% per annum.

In addition to lending rates, lending spread is charged to all borrowers. As of 1 January 2000, this was between 40 and 60 basis points. For private enterprises, the lending spread is determined on a case-by-case basis to cover ADB's risk exposure to particular borrowers and projects.

Twenty-seven LBLs became effective in 2002, of which 23 are in US dollars and 4 in Japanese yen. In addition, undisbursed balances of \$6.7 billion under 97 PSCL US dollar loans were transformed to LBL terms. The lending rates are based on the 6-month LIBOR by reference to each loan service payment date, plus a lending spread.

LIBOR^a-Based Loan Transformation

	1 st Batch		2 nd Batch		3 rd Batch		Total	
	(31 July 2002)		(31 October 2002)		(15 December 2002)		Transformation	
	No. of Loans	\$ Million	No. of Loans	\$ Million	No. of Loans	\$ Million	No. of Loans	\$ Million
Bangladesh	-	-	-	-	2	97	2	97
China, People's Republic of	13	1,316	-	-	1	92	14	1,408
Fiji Islands	-	-	-	-	1	26	1	26
India	11	1,989	-	-	-	-	11	1,989
Indonesia	-	-	-	-	30	1,658	30	1,658
Malaysia	-	-	-	-	2	48	2	48
Papua New Guinea	-	-	-	-	5	102	5	102
Philippines	-	-	-	-	22	1,084	22	1,084
Thailand	-	-	-	-	3	51	3	51
Uzbekistan	-	-	-	-	6	236	6	236
Viet Nam	-	-	-	-	1	20	1	20
TOTAL	24	3,305	-	-	73	3,414	97	6,719

- Nil.

^a London interbank offered rate.

Lending Rates^a (% per annum)

	2002	2001	
1 January	5.08	5.50	Multicurrency
	6.69	6.70	US Dollar
1 July	3.91	5.21	Multicurrency
	6.34	6.70	US Dollar

^a Lending rates are set on 1 January and 1 July every year and are valid for 6-month periods.

For public sector LBLs, rebates and surcharges are standard features, which can have two components: adjustment of ADB's basic lending spread; and adjustment of the cost base. To maintain the principle of cost pass-through pricing, ADB returns the actual sub-LIBOR funding cost margin to its LBL public sector borrowers through rebates. A surcharge could arise if ADB's funding cost is above 6-month LIBOR, which is remote unless ADB experiences serious credit deterioration. Rebate/surcharge rates are set on 1 January and 1 July every year and are based on the actual average funding cost margin for the preceding 6-month period. In 2002, ADB returned the actual sub-LIBOR funding cost margin of \$2.4 million to its LBL public sector borrowers based on the rebate rates.

Technical assistance: ADB considers technical assistance (see <http://www.adb.org/TA/>) programs as an important part of ADB's overall operations in helping DMCs meet their development objectives. From 1967 to 1991, technical assistance expenses were charged to the OCR and to other technical assistance funding resources—Technical Assistance Special Fund, Japan Special Fund, and trust/grant funds. From 1992 to 2000, no technical assistance expenses were charged to the OCR. In 2001, the Board of Directors approved the financing of high-priority technical assistance programs out of OCR current income within a rolling 4-year financing framework. The amount of financing required varies between years and is subject to the approval of the Board of Directors.

Guarantees: ADB provides guarantees as credit enhancements for eligible projects to cover risks that the private sector cannot easily absorb or manage on its own. Reducing these risks can make a significant difference in mobilizing debt funding for projects. ADB has used its guarantee instruments successfully for infrastructure projects, financial institutions, capital markets, and trade finance. The guarantee instruments are recognized as off-balance sheet financial instruments in ADB's annual financial statements. *ADB's total exposure toward signed and effective loan guarantees is disclosed in Note E of the OCR Financial Statements.*

ADB offers two guarantee products—political risk guarantees (PRG) and partial credit guarantees (PCG)—both designed to mitigate risk exposure of commercial lenders and capital market investors. These guarantees are not issued on a stand-alone basis but are provided for projects in which ADB has direct participation. ADB can cooperate with other multilateral, official, and private sector lenders and insurers in providing its guarantee products.

Rebate Rates (% per annum)

	US Dollar	Japanese Yen
1 January 2002	0.41	0.17
1 July 2002	0.36	0.16

Political risk guarantees: ADB's PRG program is designed to facilitate cofinancing by providing lenders/capital market investors of an ADB-assisted project with cover against specifically defined political risks. Coverage is available against any combination of the risks of expropriation, currency inconvertibility or nontransferability, political violence, and breach of contract, and is available for loans and other forms of debt instruments. Equity instruments are ineligible for PRG coverage. Tenors are based on the merits of the underlying project. All or part of the outstanding debt service obligations to a lender may be covered. The cover may be for principal and/or interest payment obligations. For private sector projects, ADB can issue a PRG without a counterparty guarantee from the host government. However, PRG exposure to a private sector project without a counterparty guarantee from the host government is subject to a maximum of \$150 million or 50% of the project cost, whichever is lower. Fees are market-based and comprise guarantee fees, front-end fees, and standby fees. ADB's PRG is callable when a guaranteed event has occurred and such an event has resulted in debt service default to the guaranteed lender.

In 2002, ADB approved four PRG transactions: One supporting a \$25 million commercial loan to develop a power project in Viet Nam has become effective. This PRG was provided under ADB's Co-Guarantee Program whereby ADB acted as the guarantor-of-record, and laid off all risks associated with the PRG to a private sector political risk insurer. The three remaining approved PRGs, with total support of \$235 million, were not effective as of 31 December 2002.

Partial credit guarantees: The PCG provides comprehensive cover (of both commercial and political risks) for a specific portion of the debt service profile provided by cofinanciers. PCG cover is particularly useful for projects in DMCs with restricted access to financial markets, but which ADB considers creditworthy and financially sound. Since the 1997 Asian financial crisis, borrowers, project sponsors, cofinanciers, and host governments have aimed to hedge currency mismatch risks by using the revenue currency as the borrowing currency. ADB's PCGs can cover local currency debt, including domestic bond issues or long-term loans from local financial institutions. For private sector transactions not supported by a counterparty guarantee from the host government, the exposure limit stands at \$75 million or 25% of the project cost, whichever is less. Guarantee fees for private sector transactions are market-based. Fees for transactions backed by the host government guarantee

comprise a standard guarantee fee of 40 basis points (0.4%) per annum on the present value of the outstanding guarantee obligation plus a front-end fee to cover ADB's processing costs. Fees can be charged either to the borrower or the lender. One PCG project (\$500 million equivalent in Japanese yen) in the public sector was approved and effective in 2002 to support the Power Sector Restructuring Project in the Philippines.

ADB is committed to further develop the capital markets in the region by using its guarantee products and complementary financing scheme (CFS). ADB's guarantee instruments and CFS are reliable instruments in catalyzing capital flows to its DMCs by providing necessary credit enhancements.

Private sector equity investments and loans: ADB's Charter allows ADB to use the OCR to make total equity investments in private enterprises up to 10% of its unimpaired paid-in capital, together with reserves and surplus, exclusive of special reserve. As of 31 December 2002, there were 57 companies in which ADB held equity only, 24 for loans only, and 17 companies in which it provided both equity and loans. The total equity portfolio for the OCR for both outstanding and undisbursed approved facilities net of allowance for probable losses amounted to \$409.2 million at 31 December 2002. This represented about 33% of the ceiling defined by the Charter.

As of 31 December 2002, the overall private sector portfolio (equity investments and loans) was about \$1.2 billion, which was within the operational limit of \$1.5 billion set by the Board of Directors. As an interim arrangement, pending the implementation of a more objective capital allocation methodology, approvals of private sector operations in excess of \$1.5 billion are allowed, beginning September 2001. It is also ADB's policy to limit a single project exposure (aggregate equity investment and loan) to the lesser of \$75 million or 25% of total project cost. In 2002, ADB approved equity investments amounting to \$35.5 million in four projects.

Equity

Total shareholders' equity on reported basis grew from \$10.9 billion as of 31 December 2001 to \$12.4 billion as of 31 December 2002. This was primarily due to the 2002 net income of \$978.7 million, favorable translation adjustments of \$200.7 million, net effect of change in special drawing rights (SDR) value on capital and reserves of \$189.7 million, unrealized investment holding gains of \$89.7 million, and capital subscriptions received of \$10.5 million.

In addition to subscribed and paid-in capital, capital backing in the form of callable capital can be called only if required to meet ADB's obligations incurred on borrowings or guarantees under the OCR. As of 31 December 2002, the callable capital subscribed amounted to \$43.9 billion.

Borrowings

In 2002, ADB completed 80 borrowing transactions in US dollars, Australian dollars, Japanese yen, euro, and Hong Kong dollars, raising \$5.9 billion in long-term funds (see table on page 135). The average maturity of such long-term

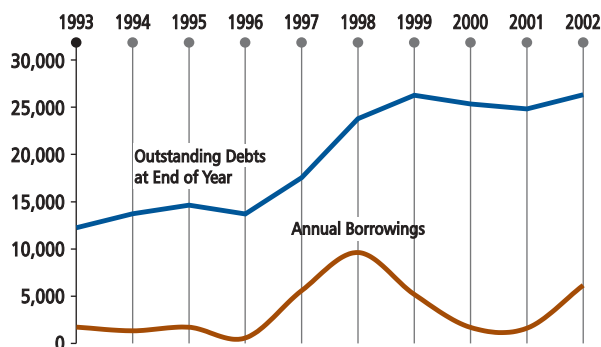
borrowings was 7.2 years, compared with 6.2 years in 2001. After swaps, \$3.3 billion or 57% of 2002 borrowings was in US dollars and the remaining \$2.6 billion in Japanese yen. ADB's swap guidelines require that the swap counterparties have a credit rating of double A or higher. ADB does not anticipate that any of its counterparties will fail to perform their obligations under such agreements.

ADB's overriding borrowing objective has always been to ensure that funds are available to meet its net cash requirements at the lowest possible cost. Subject to this objective, ADB seeks to diversify its funding sources across markets, instruments, and maturities. One of ADB's core funding strategies is to maintain a strong presence in key currency bond markets through regular issuance of benchmark global bonds. Consequently, ADB continues to enhance the execution of its global bond issues, focusing on offering investors fairly priced bonds through a price discovery process, achieving a broad-based distribution both geographically as well as by investor type, and ensuring secondary market liquidity. Importantly, ADB also issues bonds on an opportunistic basis to generate funds at the lowest cost possible. In this regard, ADB can execute opportunistic and private placement transactions on short notice and in the size, structure, and maturity that meet investors' requirements. As part of its development mandate, ADB continues to contribute to the development of the regional bond markets through local currency bond issuance. Finally, ADB makes use of the euro-commercial paper (ECP) program to bridge-finance cash flow deficiencies when market conditions are not favorable for issuing long-term debt.

Of the total 2002 borrowings, \$3 billion was raised through three public offerings. In January 2002, ADB launched a 5-year \$2.0 billion benchmark global bond issue, marking its return to the global US dollar market for the first time since May 2000. In addition, ADB launched in August and October 2002 two opportunistic US dollar bond issues in the principal amount of \$500 million each and with maturities of 10 and 7 years, respectively.

To minimize costs, ADB further enhanced its private placement funding strategy in 2002. As a result, private placement borrowing volume increased significantly in 2002, providing ADB with \$2.9 billion or almost 50% of the year's total borrowing. Of the total 2002 private placement

Borrowings, 1993–2002
(\$ million)



Borrowings

(amounts in \$ million)

	2002	2001	2000	1999
Long Term				
Total Principal Amount	5,944.9	1,207.1	1,692.6	4,815.9
Average Maturity to First Call (years)	7.2	6.2	5.6	4.5
Average Final Maturity (years)	9.9	8.7	7.3	6.2
Number of Transactions				
Public Offerings	3	2	3	7
Private Placements	77	15	1	3
Number of Currencies (before swaps)				
Public Offerings	1	2	1	4
Private Placements	5	3	1	1
Short Term^a				
Total Principal Amount ^b	2,830.0	1,249.7	250.0	1,885.0
Number of Transactions	36	9	2	50
Number of Currencies	2	2	1	1

^a All euro-commercial paper.

^b At year-end, the outstanding principal amount was \$200 million in 2002, \$400 million in 2001, nil in 2000, and \$370 million in 1999.

borrowing, \$0.6 billion was raised through 50 callable foreign exchange-linked notes targeted at institutional investors in Japan. These notes typically have principal amounts in Japanese yen and coupon rates linked to exchange rates between two currencies, such as the Japanese yen and the US dollar. Aside from the issuance of these structured notes, ADB also raised \$1.7 billion through eight bond issues placed with the Japanese retail market. With issue size ranging from \$40 million to \$800 million, such issues allow ADB to raise cost-efficient funds in volume. Most of these borrowings have longer maturities, which are attractive for smoothening ADB's redemption profile. Finally, ADB executed 19 transactions totaling \$0.6 billion in the form of foreign exchange- and interest rate-linked notes targeted at large institutional investors in Asia. All private placement borrowings were swapped on a fully hedged basis into "plain vanilla" floating liabilities in Japanese yen and US dollars.

In addition to these long-term borrowings, ADB executed a total of 36 ECP transactions in 2002, raising \$2.8 billion in short-term funds. All ECPs in 2002 were issued in US dollars and subsequently swapped into Japanese yen. As of 31 December 2002, only \$200 million ECPs were outstanding.

Liquidity portfolio management

The liquidity portfolio helps ensure the uninterrupted availability of funds to meet loan disbursements, debt servicing, and other cash requirements. It also contributes to ADB's earning base.

The Investment Authority, which is approved by the Board of Directors, governs liquid asset investments. Its primary objective is to ensure the security and liquidity of funds invested. To meet this objective, ADB seeks to maximize returns on its liquidity portfolio investments.

ADB's investments are made in the same currencies as received. In compliance with its Charter, ADB does not

convert currencies for investment. At present, liquid investments are held in 18 currencies.

ADB's liquid assets are held in obligations of governments and other official entities, time deposits, and other unconditional obligations of banks and financial institutions, and, to a limited extent, in corporate bonds, mortgage-backed securities, and asset-backed securities of high credit quality.

The liquid assets are held in three subportfolios—core portfolio, operational cash portfolio, and cash cushion portfolio—all of which have different risk profiles and performance benchmarks. *The year-end balance of the liquidity portfolios in 2002 and 2001, excluding securities transferred*

under securities lending arrangement and pending sales and purchases, is presented below.

The core portfolio is invested to ensure that the primary objective of a liquidity buffer is met. Cash inflows and outflows are minimized to achieve the core portfolio's objective of maximizing the total return relative to a defined risk tolerance level. The core portfolio is funded largely by equity. For this part, the performance is measured against external benchmarks with an average duration of about 2 years. The remaining part of the core portfolio is funded by debt and is invested to maximize the spread earned by ADB between borrowing cost and investment income.

The operational cash portfolio is designed to meet net cash requirements over a 1-month period. It is funded by

Year-End Balance of Liquidity Portfolio

(\$ million)

	2002	2001
Core Portfolio	6,546.0	5,202.0
Operational Cash Portfolio	144.0	381.0
Cash Cushion Portfolio	1,081.0	1,101.0
TOTAL	7,771.0	6,684.0

Return on Liquidity Portfolio

	Annualized Financial Return (%)	
	2002	2001
Core Portfolio	6.89	7.25
Operational Cash Portfolio	1.72	3.59
Cash Cushion Portfolio	1.04	2.29
RETURN ON TOTAL PORTFOLIO	5.36	6.11

equity and invested in short-term, highly liquid money market instruments. The portfolio performance is measured against short-term external benchmarks.

The cash cushion portfolio holds the proceeds of ADB's borrowing transactions pending disbursements. The portfolio is invested in short-term instruments; performance is measured against short-term external benchmarks.

Risk management

ADB seeks to ensure that appropriate and robust tools for risk management of treasury operations are in place. In 2002, ADB substantially completed the installation of an advanced treasury risk management system. Prior to "live" operation in 2003, the system will be tested and undergo a period of parallel operation with other systems.

The treasury risk management system will link the front, middle, and back office treasury functions into a seamless, "straight-through-processing" environment. This will enable more accurate, effective, and efficient risk management of treasury operations. In addition, it will permit the introduction of new tools for measuring and monitoring market and credit risks, such as various value-at-risk measures, and facilitate stress-testing and risk-adjusted performance and attribution analysis.

In 2002, significant progress was also made in strengthening other aspects of the risk management infrastructure. Risk guidelines and procedures were consolidated and updated. New methodologies for valuing highly structured transactions were adopted. Investment benchmarks were reviewed; and further improvements, designed to increase operational efficiencies, were introduced. In addition, risk-adjusted performance measurement was strengthened, particularly in connection with the operation of the externally managed OCR investment portfolio.

In country credit risk management, an internal quantitative credit risk model was completed in October 2002. The model is intended to be the basis for ADB to integrate a systematic approach to credit risk management by having estimates of expected and unexpected loss linked to the equity capital adequacy, loan loss allowance, minimum net income requirement, and pricing of OCR loans. The outputs given by the credit risk model will be used as inputs for determining ADB's minimum net income requirements.

In ADB's private sector operations, the Risk Management Unit has two main functions: special assets management to give special attention to the more vulnerable private sector projects; and credit review to evaluate and give an independent credit assessment, separate from the operating division's judgment on each project.

Summary of financial performance and allocation of net income

Income and expenses: Gross income decreased by 8.0% from \$2.2 billion in 2001 to \$2.1 billion in 2002 because of a decrease in loan, investment, and other income. Of the total gross income, \$1.7 billion was generated by the loan portfolio, \$330.4 million by the investment portfolio, and \$19.7 million from other sources.

Total operating expenses were \$1.3 billion in 2002, down by \$216.8 million, or 14.2% from the previous year of \$1.5 billion. The reduction in expenses was because of a \$278.9 million decrease in interest and other financial expenses and a \$5.4 million decrease in provision, offset by a \$31.5 million increase in administrative expenses, and increase in technical assistance financing of \$36.0 million for 2002. The decrease in interest and other financial expenses was mainly due to lower interest rates for variable rate borrowings. The increase in administrative expenses resulted primarily from the deferral of direct loan origination expenses of \$34.8 million in 2001, compared with \$19.4 million in 2002 and increases in severance pay and postretirement benefits that are accounted for based on projected benefits. Total operating expenses accounted for 63.4% of the gross income, compared with 68.0% in 2001.

For the year ended 31 December 2002, reported net income was \$978.7 million, compared with \$863.3 million of 2001. The increase of \$115.4 million (representing a 13.4% increase) in net income is predominantly attributable to the following.

- Increase in income of \$77.3 million reflected the year-to-date change in fair value of ADB's derivative instruments, net of amortization of transition adjustment due to FAS 133. The FAS 133 adjustment is limited to the change in value of derivative instruments as opposed to all financial instruments.

- The remaining increase in income of \$38.1 million was primarily due to the reduction in interest and other financial expenses outweighing the increase in administrative expenses and technical assistance financing and the decrease in loan and investment income for the year.

FAS 133 adjustments: The \$224.8 million FAS 133 adjustment for the year ended 31 December 2002 represented a rise of \$242.1 million in the values of the derivatives net of the \$17.3 million amortization of the FAS 133 transition adjustments during the year. The \$242.1 million gain on derivatives arose predominantly because ADB has several US dollar interest rate swaps with fixed interest receivable and floating interest payable. The net decrease in US dollar interest rates in 2002 meant that these derivatives gained in value.

Allocation of net income: In accordance with the income and reserves policy approved in 1997, ADB reviewed in 2002 its income outlook and allocation of 2001 net income. Based on the review, the Board of Governors approved that, of the 2001 net income after appropriation to special reserve of \$862.0 million, \$714.5 million be allocated to ordinary reserve and \$147.5 million to a separate category of reserves, "Cumulative Revaluation Adjustments Account." This represents cumulative FAS 133 adjustments. For 2002, the Board of Directors approved that there should be no change in OCR loan charges.

Staff retirement plan and postretirement medical benefits: Retirement benefits are provided through a contributory defined benefit plan (Pension Plan) where staff employed by ADB are expected to contribute 9 1/3% of their salary and are allowed to make additional voluntary

contributions. The Pension Plan is administered by ADB as a separate fund, which is required to be kept separate from ADB's resources.

In addition, the postretirement medical benefits plan is provided to retirees who have elected to enroll in the Postretirement Plan. ADB covers 75% of the medical insurance premium.

For the two benefit plans, the recognition of ADB's obligations is based on the projected benefits obligation, net of the fair value of the projected plans assets under certain actuarial assumptions. As of 31 December 2002, the Pension Plan and the Postretirement Plan showed an unfunded status of \$185.5 million and \$124.0 million, respectively. To the extent allowed, certain costs, gains/losses, and obligations are deferred and recognized in relevant accounting periods as permitted by the accounting standards. Consequently, the unfunded amounts are not recognized as liabilities but the periodic retirement pension and postretirement costs based on actuarial valuation have been recognized in the OCR accounts. Recognition of future costs will depend on the outcome of future events. In that respect, the fund status and the periodic costs are reviewed annually with the assistance of actuaries. Such a review may lead to a revision in the funding rate to the Pension Plan and Postretirement Plan.

Special Funds

ADB is authorized by its Charter to establish and administer Special Funds. Special Funds being administered as of 31 December 2002 were the Asian Development Fund (ADF); the Technical Assistance Special Fund (TASF); the Japan Special Fund (JSF), including the Asian Currency Crisis Support Facility (ACCSF); and the ADB Institute Special Fund. Financial statements for each fund are prepared in accordance with generally accepted accounting principles, except for the ADF, which are special purpose financial statements prepared in accordance with ADF regulations (see <http://www.adb.org/finance/ADF/>).

Asian Development Fund

The ADF is ADB's concessional lending window from which loans are provided to DMCs with low per capita gross national product and limited debt repayment capacity. The governments of 28 donor members (regional and nonregional) have contributed to the totality of the ADF, which is the only multilateral source of concessional assistance dedicated exclusively to the needs of Asia and the Pacific. The ADF supports activities that promote poverty reduction and improve the quality of life of ADB's poorer DMCs (see <http://www.adb.org/finance/ADF/>).

ADF VIII: The current ADF replenishment (known as ADF VIII), authorized in December 2000 by Resolution No. 276 of the Board of Governors, is intended to finance ADB's concessional lending operations for 2001–2004. The total replenishment was \$2.79 billion based on the exchange rates specified in the Resolution. By the end of 2002, 23 donors had submitted their Instruments of Contribution to ADF VIII for a total of \$2.27 billion. Twenty-one donors deposited unqualified Instruments of

Contribution. Canada and Taipei, China deposited Instruments of Contribution containing a qualification, as permitted by the Resolution, that all installment payments except the first were subject to budgetary appropriations. Two donors—Italy and the United States—had not submitted their Instruments of Contribution by year-end.

By the end of the year, all donors that had submitted their Instruments of Contribution had paid both their first and second installments. *For details of amounts released for operational commitment in 2002, see the column labeled "Addition" in Table 31 in the Statistical Annex.*

Shortly after it became a member of ADB in April 2002, Portugal deposited Instruments of Contribution to both ADF VII and ADF VIII for €34.2 million and €16.9 million, respectively. The contribution to the ADF VII formed part of the ADF resources that funded loan approvals in 2002.

In addition, Spain indicated that it would make an additional contribution of \$100 million (€113.4 million equivalent) to the ADF VIII, emphasizing the humanitarian obligation for all donors to respond to the needs of Afghanistan and its neighboring countries. In August 2002, the Board of Directors approved the acceptance of this contribution subject to the terms and conditions set forth in the Resolution. Spain provided its first installment in cash.

Of the 25 donors to the ADF VIII, 17 opted to follow the accelerated encashment schedule specified in the Resolution, which has an encashment profile of 7 years. Six other donors—Austria, France, Germany, Switzerland, Thailand, and United Kingdom—applied the regular encashment profile, which extends over 10 years. Belgium applied the International Development Association 12 5-year encashment profile, while Australia modified the standard profile to accommodate its budgetary requirements, but its notes will be encashed within 7 years.

Asian Development Fund Commitment Authority (\$ million, at year-end)

	2002	2001
ADF VIII Contributions	1,072.9	417.3
ADF VII Contributions	310.0	120.6
ADF VI Contributions	0.0	-
Expanded Advance Commitment Authority	1,600.0	800.0
Total ADF Resources ^a	2,983.0	1,337.9
Less:		
Loans Committed	2,229.5 ^b	712.9 ^c
Carryover of Conditional Loans Committed ^d	630.9	584.8
Provision for Disbursement Risk	89.9	35.0
TOTAL^e	32.7	5.3

0.0 Less than 0.1 million.

- Nil.

^a Excludes pre-ADF VIII amounts for determining the ADF commitment authority under the new financial planning framework for managing ADF resources, as approved by the Board of Directors on 15 April 1997.

^b Excludes loans that were conditionally approved in October–December 2002.

^c Excludes loans that were conditionally approved in November–December 2001.

^d Loans that were conditionally approved in 2000 and were funded in January 2001.

^e Total may not add due to rounding.

ADF VII: In May 2002, the US deposited promissory notes for a further \$98.0 million of its ADF VII contribution, consisting of \$28.2 million for the balance of its third installment, and \$69.8 million as partial payment (69.8%) of its fourth installment. Accordingly, four donors—Austria, France, Germany, and Malaysia—which had previously exercised their pro rata rights and not made their fourth installments available for operational commitment, released 69.8% of such installments. The total amount released was \$48.4 million. These resources became part of the ADF VIII commitment authority in 2002. As of 31 December 2002, the US' arrears under ADF VII were \$30.2 million and the amount withheld by other donors totaled \$20.9 million.

ADF VI: The US cleared its ADF VI arrears by depositing a promissory note in the amount of \$17,050 in May 2002.

ADF loan approvals, disbursements, and repayments: In 2002, 53 ADF loans totaling \$1.6 billion were approved, compared with 46 ADF loans totaling \$1.4 billion approved in 2001. Of the 2002 amount, about 47.7% went to Pakistan, Bangladesh, and Viet Nam (in order of magnitude). Disbursements during 2002 totaled \$1,135.5 million, an increase of 10.9% from \$1,024.3 million in 2001. At the end of the year, cumulative disbursements from ADF resources were \$18.7 billion. Loan repayments during the year amounted to \$262.3 million, and cumulative repayments were \$1.9 billion. As of 31 December 2002, ADF loans outstanding amounted to \$17.2 billion.

Status of loans: At the end of 2002, 28 public sector loans to Myanmar, and 14 public sector loans to Solomon Islands were in nonaccrual status. Total outstanding ADF loans to Myanmar amounted to \$452.1 million, and to Solomon Islands \$46.0 million, together comprising about 2.9% of the total ADF loans outstanding.

Investment portfolio position: The ADF investment portfolio amounted to \$3.3 billion at 31 December 2002, compared with \$2.6 billion at 31 December 2001. About 22% of the portfolio was invested in bank deposits, and 78% in floating and fixed income securities. The financial rate of return on ADF investments in 2002 was 4.7%, compared with 5.4% in 2001.

The portfolio was denominated in 10 currencies. Euro, pound sterling, Australian dollars, and Canadian dollars accounted for 78% of the portfolio.

Technical Assistance Special Fund

Review of activities: During 2002, People's Republic of China (its 2nd), Pakistan (its 25th), and India (its 18th) made direct voluntary contributions to the TASF, amounting to \$1,000,000, \$70,000, and \$46,545, respectively. These were made on a wholly untied basis.

At the end of 2002, total TASF resources amounted to \$919.6 million. Of this, \$851.3 million had been committed, leaving an uncommitted balance of \$68.3 million. For details, see Table 32 in the Statistical Annex.

Operations and resource position: Technical assistance committed (approved and effective) decreased from \$34.7 million in 2001 to \$27.9 million in 2002 with

Technical Assistance Special Fund Cumulative Resources (\$ million)

	2002	2001
Regularized Replenishment Contributions	238.0	238.0
Allocations from OCR Net Income	501.0	501.0
Direct Voluntary Contributions	88.5	87.4
Income from Investment and Other Sources	95.6	88.1
Transfers from the TASF to the ADF	(3.5)	(3.5)
TOTAL	919.6	911.0

() Negative.

58 technical assistance projects made effective during the year. In 2002, \$3.9 million (\$5.5 million in 2001), representing completed and canceled technical assistance projects, was written back as a reduction in technical assistance for the year and the corresponding undisbursed commitment was eliminated. Revenue from investments dropped from \$10.9 million in 2001 to \$4.8 million in 2002, because of a decrease in the size of the investment portfolio and general lower yield prevailing globally. As a result, the uncommitted balance available for future commitments decreased from \$81.3 million in 2001 to \$68.3 million in 2002. The TASF contributed 26% of funding for total technical assistance approved in 2002.

At the end of the year, TASF investments stood at \$155 million, down 16% from 2001. Other assets—comprising due from banks, advances to consultants, and others—totaled \$10.1 million. Accounts payable to the OCR and others amounted to \$130,000.

Japan Special Fund

Review of activities: The technical assistance grants funded by the Japan Special Fund (JSF) continued to support ADB operations aimed at reducing poverty. In March 2002, Japan contributed 2.9 billion yen (\$22.5 million equivalent) as a regular contribution to the JSF. As of 31 December 2002, Japan's cumulative contribution to the JSF, since its inception in 1988, amounted to 97.3 billion yen (about \$836.0 million equivalent), comprising regular contributions of 79.2 billion yen and supplementary contributions of 18.1 billion yen. In 2002, ADB approved 65 technical assistance grants for the JSF totaling \$36.4 million inclusive of those that were approved but not yet effective (see table on page 139). The uncommitted balance after taking into account approved technical assistance grants not yet effective as of 31 December 2002 was \$135.4 million. For details, see tables 33 and 34 in the Statistical Annex.

Sectoral activities: In 2002, the JSF financed 20% of the total amount of technical assistance approved by ADB, including 54% of the total amount of project preparatory technical assistance approved during the year. The breakdown of JSF approvals by sector is shown in the table on page 139.

Japan Special Fund Technical Assistance^a by Sector, 2002

	\$ Million	%
Agriculture and Natural Resources	8.3	22.8
Social Infrastructure	7.6	20.9
Transport and Communications	6.9	19.0
Others ^b	4.6	12.6
Energy	4.5	12.4
Multisector	2.1	5.8
Finance	1.8	4.9
Industry and Nonfuel Minerals	0.6	1.6
TOTAL	36.4	100.0

^a Includes regional technical assistance.

^b Includes projects outside ADB's economic sector classification system; these projects pertain to, among others, central government administration, operation and regulation, customs operations, public sector reform programs, judicial and legislative operations, public finance management, fiscal reforms, environment projects, gender, governance, and tourism.

Asian Currency Crisis Support Facility

Review of activities: The Asian Currency Crisis Support Facility (ACCSF) was established in March 1999 for a 3-year period as an independent component of the JSF. The ACCSF was terminated on 23 March 2002. Pending the completion of related administrative matters, the remaining funds will be retained in the ACCSF.

At the end of 2002, Japan's cumulative contributions for interest payment assistance (IPA) and technical assistance components of the ACCSF amounted to 27.5 billion yen (\$241.0 million equivalent). In 2002,

Asian Currency Crisis Support Facility Technical Assistance by Country, 2002

	\$ Million	%
Indonesia	7.3	76.0
Philippines	2.3	24.0
TOTAL	9.6	100.0

Asian Currency Crisis Support Facility Technical Assistance by Sector, 2002

	\$ Million	%
Finance	4.0	41.7
Others ^a	1.9	19.8
Industry and Nonfuel Minerals	1.5	15.6
Social Infrastructure	1.3	13.5
Agriculture and Natural Resources	0.9	9.4
TOTAL	9.6	100.0

^a Includes projects outside ADB's economic sector classification system; these projects pertain to, among others, central government administration, operation and regulation, customs operations, public sector reform programs, judicial and legislative operations, public finance management, fiscal reforms, environment projects, gender, governance, and tourism.

\$90 million was transferred from the ACCSF to the Japan Fund for Poverty Reduction (JFPR). ADB approved 10 technical assistance grants for ACCSF funding amounting to \$9.6 million inclusive of those that were approved but not yet effective (*see tables above*). The uncommitted balance of ACCSF funds for the IPA and technical assistance after taking into account approved technical

The Japan Special Fund (JSF) is assisting ADB's developing member countries in their fight against poverty, and is helping ADB address its poverty reduction objective.

With poverty continuing to be the major obstacle to Bangladesh's economic growth, the need to provide facilities and services for the poor remains significant. A JSF technical assistance grant of \$500,000 is addressing this need by helping rural women in Bangladesh increase their household incomes through livestock production, including improving breed and animal health, research, livestock and poultry husbandry, fodder development, livestock processing, and environmental management. The agreement was signed in September 2002 (*see http://www.adb.org/Documents/TARs/BAN/R162_01.pdf*).

Also in September, ADB signed an agreement with the Government of Nepal to provide a \$450,000 technical assistance grant aimed at assessing the needs of poor rural women and developing a feasible and comprehensive package of interventions to improve their socioeconomic status (*see <http://www.adb.org/Documents/Speeches/2002/ms2002084.asp>*). The technical assistance reaffirms ADB's mission to reduce poverty, and supports the Government of Nepal's efforts to advance gender equality and empower poor Nepalese women.

Technical assistance projects were also provided through the Asian Currency Crisis Support Facility (ACCSF), which had been established in 1999 as an independent component of the JSF.

Although the ACCSF has ended, the impact of the projects funded under this facility will be long lasting.

The \$1.5 million technical assistance from ACCSF to Indonesia for developing an anti-money laundering regime is aimed at increasing the soundness of Indonesia's financial system, boosting economic development, and promoting good governance (*see <http://www.adb.org/Documents/ADBBO/AOTA/35498012.ASP>*). In the Philippines, the \$1 million technical assistance from ACCSF will draft a time-bound plan for implementing an effective anti-money laundering regime; and provide support for facilitating execution of that plan (*see http://www.adb.org/Documents/TARs/PHI/tar_phi36003.pdf*).

assistance grants not yet effective was \$23.7 million as of 31 December 2002. For details, see Table 34 in the *Statistical Annex*.

ACCSF financing was targeted at activities that supported policy dialogue, human resource development, institutional strengthening, and other relevant efforts focusing on bank and corporate debt restructuring; created or developed sound financial monitoring, supervision, and regulation; enhanced public sector and corporate governance; developed social safety nets; and protected the environment.

Sectoral activities: In 2002, the ACCSF financed 5% of the total amount of technical assistance approved by ADB (see http://www.adb.org/Documents/Reports/Japan_Special_Fund/2001/jsf_accsf.pdf).

ADB Institute Special Fund

The costs for operating the ADB Institute are met from the ADB Institute Special Fund, which is administered by ADB in accordance with the Statute of ADB Institute. Japan made its seventh contribution in the amount of 1.3 billion yen (equivalent to \$9.8 million) in May 2002.

As of 31 December 2002, cumulative commitments amounted to 8.7 billion yen (equivalent to about \$71.3 million), excluding translation adjustments. Of the total contributions received, \$62.0 million had been used as of 31 December 2002, mainly for research and capacity-building activities, including organizing symposiums, forums, and training; preparing research reports, publications, and web sites; and associated administrative expenses.

As of 31 December 2002, the balance of net current assets excluding property, furniture, and equipment available for future projects and programs of ADB Institute was about \$9.3 million. For more on the ADB Institute, see <http://www.adbi.org/>.

Trust funds managed by ADB

In addition to the OCR and Special Funds resources, ADB also manages and administers the Japan Scholarship Program (JSP), Japan Fund for Poverty Reduction (JFPR), Japan Fund for Information and Communication Technology (JFICT), and channel financing of grants provided by bilateral donors to support technical assistance and soft components of loans. These funds do not form part of ADB's own resources.

Japan Scholarship Program

The JSP was established in 1988 to provide an opportunity for qualified citizens of DMCs to undertake postgraduate studies in economics, management, science and technology, and other development-related fields at selected educational institutions in Asia and the Pacific. The JSP is funded by Japan and administered by ADB. Currently, 18 institutions in 10 countries participate in the JSP.

Between 1988 and 2002, Japan contributed about \$53 million to the JSP. A total of 1,479 scholarships have been awarded to recipients from 34 members. Of the total, 1,142 have already completed their courses. Women have received 426 scholarships. The number of new scholarships

They share a vision of an Asia and Pacific region without poverty. They share the belief that individuals can make a difference. They have something else in common as well. The Regional Program Officer of Habitat for Humanity International (East/Southeast Asia Region) and the National Project Coordinator, Technical Education and Skills Development Authority (TESDA), Philippines, were both recipients of the ADB-Japan Scholarship Program (JSP).

During a 2002 gathering of scholars from the Philippine-based Asian Institute of Management (AIM) and the International Rice Research Institute, the two alumni of AIM's Masters in Development Management Program attributed their personal growth to education, and thanked the ADB-JSP for making that education possible.

Both have applied their educations to working in fields where they can help others experience the real possibility of change. Habitat for Humanity International—a nonstock, nonprofit organization dedicated to eliminating poverty housing and homelessness—helps people build homes. Based on the premise that housing sets the stage for making development possible, the program helps home partners believe in themselves again. The TESDA-United Nations Development Programme Project empowers women by facilitating their access to entrepreneurial support services. Providing economic opportunities that help women improve their incomes is critical for poverty reduction.

awarded annually has grown from 49 in 1988 to 143 in 2002 (see http://www.adb.org/Documents/Brochures/Scholarship_Program/).

Channel financing arrangements

Official grant cofinancing plays a vital role in ADB operations, particularly in view of the continuing constraints on TASF and ADF resources. These grant funds support ADB's technical assistance program and finance mostly soft components of its loan projects.

A majority of such grants are provided by bilateral donors under channel financing arrangements (CFAs). ADB acts as administrator of the funds and applies its own guidelines and procedures in consultant recruitment, procurement, disbursement, and project supervision.

Under a CFA, the donor enters into a comprehensive agreement with ADB whereby the donor provides an untied grant fund to be administered by ADB (but the fund does not become part of ADB's own resources); the donor indicates its preferred sectors and recipient countries in the use of the fund; ADB regularly provides the donor with a list and description of proposed technical assistance projects that satisfy the donor's preferences; and the donor and ADB agree on the specific activities to be financed under the fund. Funds provided under a CFA are transferred to an interest-bearing account and may also be

Immediate humanitarian and reconstruction assistance is needed in Afghanistan. Roads, shelter, and employment for the refugees and displaced persons, and support to all regions of the country are needed, as is a smooth transition from humanitarian to recovery and reconstruction assistance.

In 2002, ADB approved three grant projects financed by the Japan Fund for Poverty Reduction (JFPR) as part of the assistance pledged by the Japanese Government in January 2002 at the International Conference on Reconstruction Assistance to Afghanistan. *For more on Afghanistan, see the Special Theme chapter.*

Road project: In addition to helping meet the immediate need of rehabilitating a busy transport route, the \$15 million grant will provide jobs for 10,000 returning refugees

and internally displaced persons. Over 200,000 refugees have returned to Afghanistan from the southern route. They need jobs. And, to avoid further overcrowding of Kabul, the refugees need to be temporarily sheltered in the areas north and west of Kandahar. The road project will provide training in road construction, income-generating activities, microcredit services, and nutrition and childcare support. Basic health education and services and medicines will be provided by 400 community health workers.

Education project: The education project will address Afghanistan's nonformal education needs—to provide literacy and vocational skills to street children, former child combatants, and ex-soldiers. It will stress community-based, gender-sensitive education. About 37,000 pupils will benefit

from the project, including over 7,000 girls who will receive education stipends.

Health project: On 23 December 2002, ADB also approved JFPR assistance for \$3 million to improve the health and nutrition sector, including the reproductive health of the rural poor in Afghanistan. The project will explore ways for the Ministry of Health to contract nongovernment organizations to help develop community-based primary health care and thereby reduce rural poverty. The project aims to cut child mortality rates by 30% over 3 years and reduce common infectious diseases, child malnutrition, and maternal mortality rates. The project will also generate jobs in the construction and community health subsectors.

invested by ADB pending disbursement. Donors are provided with regular financial statements and progress reports on the use of the funds. ADB is responsible for project preparation, processing, and administration. CFAs may be replenished with additional funds at the donor's discretion.

The primary advantage of CFAs is that funding for several individual technical assistance projects may be provided under a single agreement. Accordingly, they minimize the need for detailed negotiations on a case-by-case basis and foster administrative efficiency. The first CFA was negotiated in 1980. Since then, ADB has entered into CFAs with several bilateral donors: Australia, Belgium, Canada, Denmark, Finland, France, Italy, the Netherlands, New Zealand, Norway, Spain, Sweden, Switzerland, and United Kingdom.

In addition to the traditional type of CFA (which may be used for several sectors), the processing of thematic CFAs with bilateral agencies has risen sharply in the last couple of years in such areas as renewable energy, climate change, poverty reduction, governance, and water. Several thematic CFAs are now being packaged as umbrella facilities to allow more than one donor to contribute.

In 2002, a new thematic poverty-focused multidonor CFA was established with the first contribution made by the United Kingdom for an amount equivalent to \$60 million. Norway made a contribution to the Governance Cooperation Fund for \$2 million; and Switzerland replenished its contribution to its CFA with ADB for an

additional \$600,000; and the Netherlands made an additional contribution of \$4 million to its existing Cooperation Fund for the Water Sector.

Japan Fund for Poverty Reduction

The Japan Fund for Poverty Reduction (JFPR) was established in May 2000. The JFPR is a trust fund to support poverty reduction and social development activities that can add substantive value to ADB-financed projects (see Box above). Since 2000, Japan has contributed \$244 million in total and \$81 million for 29 projects have been approved for implementation (see <http://www.adb.org/JFPR/> and Table 35 in the Statistical Annex).

Japan Fund for Information and Communication Technology

The Japan Fund for Information and Communication Technology (JFICT) was established in July 2001. The JFICT is a trust fund to assist DMCs in bridging the digital divide to help reduce poverty. The JFICT had an initial contribution of 1.3 billion yen (approximately \$10.7 million) for a 3-year period.

In 2002, two projects were approved: E-Health Membership Insurance Cards in Viet Nam for \$0.5 million, and the Development of a Business Plan for a Center for Learning, Information, Communication, and Knowledge for Asia and the Pacific (CLICK) for \$0.2 million (see http://www.adb.org/Documents/others/CLICK/R21_03.pdf and Table 36 in the Statistical Annex).

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REPORT OF INDEPENDENT AUDITORS

Asian Development Bank

In our opinion, the accompanying balance sheets and the related statements of income and expenses, cash flows, and 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 2002 and 2001, and the results of its operations and its cash flows for the years then ended, in conformity with accounting principles generally accepted in the United States of America. These financial statements are the responsibility of the management of the Asian Development Bank; 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 auditing standards generally accepted in the United States of America 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, 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 our opinion.

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 2002 and 2001, and of statement of subscriptions to capital stock and voting power as at 31 December 2002 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.

Price Waterhouse Coopers LLP

Detroit, Michigan
10 March 2003

ASIAN DEVELOPMENT BANK—ORDINARY CAPITAL RESOURCES

BALANCE SHEET

31 December 2002 and 2001

Expressed in Thousands of United States Dollars (Note B)

A S S E T S				
	2002		2001	
DUE FROM BANKS (Notes B and C)		\$ 473,360		\$ 68,823
INVESTMENTS (Notes B, C, D, and J)				
Government and government-guaranteed obligations	\$ 2,997,595		\$ 2,037,916	
Time deposits	1,930,562		2,673,253	
Other securities	2,971,376		2,063,876	
Securities transferred under securities lending arrangement	<u>1,129,208</u>	9,028,741	<u>1,489,870</u>	8,264,915
LOANS OUTSTANDING (OCR-5) (Notes A, B, and E) (Including FAS 133 adjustment of \$1,098 – 2002 and \$1,212 – 2001)				
Members and guaranteed by members	28,817,999		28,334,516	
Private sector	<u>399,714</u>		<u>404,458</u>	
	29,217,713		28,738,974	
Less—allowance for loan losses	<u>72,477</u>	29,145,236	<u>80,128</u>	28,658,846
EQUITY INVESTMENTS (Notes A, B, and F)		211,267		208,018
ACCRUED INCOME				
On investments	74,112		65,426	
On loans	<u>339,915</u>	414,027	<u>394,297</u>	459,723
RECEIVABLE FROM MEMBERS (Note I)				
Nonnegotiable, noninterest-bearing demand obligations (Note C)	313,416		333,047	
Amounts required to maintain value of currency holdings	316		11,100	
Subscription installments	<u>2,815</u>	316,547	<u>4,353</u>	348,500
RECEIVABLE FROM SWAPS (Notes B, D and H)				
Investments (Including FAS 133 adjustment of \$8,005 – 2002)	511,937		-	
Borrowings (Including FAS 133 adjustment of \$641,150 – 2002 and \$330,164 – 2001)	<u>9,231,868</u>	9,743,805	<u>6,379,403</u>	6,379,403
OTHER ASSETS				
Property, furniture, and equipment (Notes B and G)	164,956		155,262	
Investment related receivables	160,003		159,500	
Unamortized issuance costs of borrowings	58,979		52,343	
Miscellaneous (Note L)	<u>120,271</u>	504,209	<u>110,991</u>	478,096
TOTAL		\$49,837,192		\$44,866,324

The accompanying notes are an integral part of these financial statements (OCR-8).

LIABILITIES, CAPITAL, AND RESERVES				
	2002		2001	
BORROWINGS (OCR-6) (Notes B and H) (Including FAS 133 adjustment of \$9,221 – 2002 and \$26,261 – 2001)		\$ 25,905,301		\$ 24,880,784
ACCRUED INTEREST ON BORROWINGS		330,712		371,405
PAYABLE FOR SWAPS (Notes B, D and H) Investments (including FAS 133 adjustment of \$17,167 – 2002)	\$ 548,218		\$ -	
Borrowings (Including FAS 133 adjustment of \$261,793 – 2002 and \$194,674 – 2001)	9,027,166	9,575,384	6,784,076	6,784,076
ACCOUNTS PAYABLE AND OTHER LIABILITIES				
Investment related payables	1,418,797		1,778,553	
Undisbursed technical assistance commitments (Note K)	64,845		19,753	
Advance payments on subscriptions (Note I)	33		4	
Miscellaneous (Notes G and L)	189,957	1,673,632	157,526	1,955,836
CAPITAL AND RESERVES (OCR-4)				
Capital stock (OCR-7) (Notes B and I)				
Authorized (SDR34,909,940,000)				
Subscribed (SDR34,870,170,000 – 2002 and SDR34,746,270,000 – 2001)	47,234,435		43,628,112	
Less—"callable" shares subscribed	43,912,259		40,559,590	
"Paid-in" shares subscribed	3,322,176		3,068,522	
Less—subscription installments not due	10,848		18,967	
Subscription installments matured	3,311,328		3,049,555	
Less—capital transferred to the Asian Development Fund	64,491		59,780	
	3,246,837		2,989,775	
Net notional amounts required to maintain value of currency holdings (Notes B and I)	(488,456)		(462,456)	
Ordinary reserve (Note J)	8,470,092		7,812,436	
Special reserve (Note J)	183,764		182,903	
Surplus (Note J)	116,645		116,645	
Cumulative Revaluation Adjustments Account (Note J)	147,501		-	
Net income after appropriation (OCR-2) (Note J)	977,815		861,965	
Accumulated other comprehensive income (OCR-4) (Note J)	(302,035)	12,352,163	(627,045)	10,874,223
TOTAL		\$49,837,192		\$44,866,324

ASIAN DEVELOPMENT BANK—ORDINARY CAPITAL RESOURCES

STATEMENT OF INCOME AND EXPENSES

For the Years Ended 31 December 2002 and 2001

Expressed in Thousands of United States Dollars (Note B)

	2002		2001	
INCOME (Note K)				
From loans (Notes B and E)				
Interest	\$1,595,479		\$1,765,025	
Commitment charge	50,297		47,050	
Other	64,167	\$1,709,943	1,565	\$1,813,640
From investments (Notes B and D)				
Interest	256,641		322,586	
Net gain on sales	74,221		81,032	
Net loss from futures	(414)	330,448	(182)	403,436
From other sources—net (Notes E and P)		19,723		21,634
TOTAL INCOME		\$2,060,114		\$2,238,710
EXPENSES (Note K)				
Interest and other financial expenses (Note H)	1,155,167		1,434,112	
Administrative expenses (Note M)	90,553		59,039	
Technical assistance to member countries	55,998		19,962	
Provision for losses (Notes B and E)	4,476		9,838	
TOTAL EXPENSES		1,306,194		1,522,951
OPERATING INCOME BEFORE FAS 133 ADJUSTMENT		753,920		715,759
FAS 133 ADJUSTMENT (Notes B and K)		224,756		112,845
INCOME BEFORE CUMULATIVE EFFECT OF CHANGE IN ACCOUNTING PRINCIPLE		978,676		828,604
CUMULATIVE EFFECT OF CHANGE IN ACCOUNTING PRINCIPLE (Note B)		-		34,656
NET INCOME		978,676		863,260
APPROPRIATION OF GUARANTEE FEES TO SPECIAL RESERVE (Note J)		861		1,295
NET INCOME AFTER APPROPRIATION TO SPECIAL RESERVE		\$ 977,815		\$ 861,965

The accompanying notes are an integral part of these financial statements (OCR-8).

ASIAN DEVELOPMENT BANK—ORDINARY CAPITAL RESOURCES

STATEMENT OF CASH FLOWS

For the Years Ended 31 December 2002 and 2001

Expressed in Thousands of United States Dollars (Note B)

	2002	2001
CASH FLOWS FROM OPERATING ACTIVITIES		
Interest and other charges on loans received	\$ 1,531,725	\$ 1,559,651
Interest on investments received	283,375	366,408
Interest and other financial expenses paid	(1,141,698)	(1,367,316)
Administrative expenses paid	(58,110)	(77,599)
Technical assistance disbursed	(12,694)	(337)
Others—net	30,116	19,550
Net Cash Provided by Operating Activities	<u>632,714</u>	<u>500,357</u>
CASH FLOWS FROM INVESTING ACTIVITIES		
Sales of investment	6,279,108	6,627,494
Maturities of investment	170,407,495	199,790,074
Purchases of investment	(177,340,600)	(205,830,483)
Principal collected on loans	3,333,905	1,195,800
Loans disbursed	(2,812,703)	(2,555,876)
Property, furniture, and equipment acquired	(18,724)	(6,825)
Net sales (purchases) of equity investments	6,551	(8,934)
Net Cash Used in Investing Activities	<u>(144,968)</u>	<u>(788,750)</u>
CASH FLOWS FROM FINANCING ACTIVITIES		
Net proceeds of new borrowings	8,225,115	2,458,205
Bonds purchased for redemption and borrowings redeemed	(8,211,815)	(2,164,031)
Matured capital subscriptions collected ¹	3,898	15,740
Borrowing issuance expenses paid	(19,168)	(21,319)
Demand obligations of members encashed	50,607	53,492
Net currency swaps	(171,778)	(33,913)
Net Cash (Used in) Provided by Financing Activities	<u>(123,141)</u>	<u>308,174</u>
Effect of Exchange Rate Changes on Due from Banks	<u>39,932</u>	<u>(13,504)</u>
Net Increase in Due from Banks	404,537	6,277
Due from Banks at Beginning of Year	<u>68,823</u>	<u>62,546</u>
Due from Banks at End of Year	<u>\$ 473,360</u>	<u>\$ 68,823</u>
RECONCILIATION OF NET INCOME TO NET CASH PROVIDED BY OPERATING ACTIVITIES:		
Net Income (OCR-2)	\$ 978,676	\$ 863,260
Adjustments to reconcile net income to net cash provided by operating activities:		
FAS 133 Adjustment	(224,756)	(112,845)
Change in accrued income, including interest and commitment charges added to loans	(186,904)	(266,895)
Depreciation and amortization	151,997	138,548
Change in accrued interest and other expenses	(88,105)	(23,173)
Net gain from sales of investments	(73,807)	(80,850)
Undisbursed technical assistance commitments	45,092	19,753
Change in administration charge receivable	33,238	1,771
Provision for losses charged	4,476	9,838
Cumulative effect of change in accounting principle	—	(34,656)
Others—net	(7,193)	(14,394)
Net Cash Provided by Operating Activities	<u>\$ 632,714</u>	<u>\$ 500,357</u>

¹ In addition, nonnegotiable, noninterest-bearing demand promissory notes amounting to \$17,022 (\$29,952 – 2001) were received from members. The accompanying notes are an integral part of these financial statements (OCR-8).

ASIAN DEVELOPMENT BANK-ORDINARY CAPITAL RESOURCES

STATEMENT OF CHANGES IN CAPITAL AND RESERVES

For the Years Ended 31 December 2002 and 2001

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

	Capital Stock	Net Notional Maintenance of Value	Ordinary Reserve	Special Reserve	Surplus	Cumulative Revaluation Adjustments Account	Net Income After Appropriations	Accumulated Other Comprehensive Income	Total
Balance— 1 January 2001	\$3,049,828	\$ -	\$7,166,484	\$181,608	\$116,645	\$ -	\$ 625,716	\$(306,646)	\$10,833,635
Comprehensive income for the year 2001 (Note J)				1,295			861,965	(320,399)	542,861
Change in SDR value of paid-in shares subscribed	(110,960)								(110,960)
Change in subscription installments not due	48,656								48,656
Change in SDR value of capital transferred to Asian Development Fund	2,251								2,251
Reclassification of notional maintenance of value		(462,456)							(462,456)
Allocation of 2000 net income to ordinary reserve (Note J)			625,716				(625,716)		-
Credit to ordinary reserve for change in SDR value of capital stock (Note J)			20,236						20,236
Balance— 31 December 2001 (Forward)	\$2,989,775	\$(462,456)	\$7,812,436	\$182,903	\$116,645	\$ -	\$ 861,965	\$(627,045)	\$10,874,223

	Capital Stock	Net Notional Maintenance of Value	Ordinary Reserve	Special Reserve	Surplus	Cumulative Revaluation Adjustments Account	Net Income After Appropriations	Accumulated Other Comprehensive Income	Total
Balance—									
31 December 2001 (Forward)	\$2,989,775	\$(462,456)	\$7,812,436	\$182,903	\$116,645	\$ -	\$861,965	\$(627,045)	\$10,874,223
Comprehensive income for the year 2002 (Note J)				861			977,815	325,010	1,303,686
Change in SDR value of paid-in shares subscribed	242,691								242,691
Change in subscription installments not due	8,563								8,563
Additional paid-in shares subscribed during the year	10,519								10,519
Change in SDR value of capital transferred to Asian Development Fund	(4,711)								(4,711)
Change in notional maintenance of value		(26,000)							(26,000)
Allocation of 2001 net income to ordinary reserve (Note J)			714,464				(714,464)		-
Allocation of 2001 net income to cumulative revaluation adjustment account (Note J)						147,501	(147,501)		-
Charge to ordinary reserve for change in SDR value of capital stock (Note J)			(56,808)						(56,808)
Balance—									
31 December 2002	\$3,246,837	\$(488,456)	\$8,470,092	\$183,764	\$116,645	\$147,501	\$977,815	\$(302,035)	\$12,352,163

Accumulated Other Comprehensive Income (Note J) For the Years Ended 31 December 2002 and 2001

Expressed in Thousands of United States Dollar (Note B)

	FAS 133 Adjustment and Amortization		Accumulated Translation Adjustments		Unrealized Investment Holding Gains		Accumulated Other Comprehensive Income	
	2002	2001	2002	2001	2002	2001	2002	2001
Balance, 1 January	\$ (54,898)	\$ -	\$ (665,472)	\$ (376,002)	\$ 93,325	\$ 69,356	\$ (627,045)	\$ (306,646)
Transition adjustment	-	(116,313)	-	-	-	-	-	(116,313)
Amortization	34,567	61,415	-	-	-	-	34,567	61,415
Other comprehensive income for the year	-	-	200,741	(289,470)	89,702	23,969	290,443	(265,501)
Balance, 31 December	\$(20,331)	\$(54,898)	\$(464,731)	\$(665,472)	\$183,027	\$93,325	\$(302,035)	\$(627,045)

The accompanying notes are an integral part of these financial statements (OCR-8).

ASIAN DEVELOPMENT BANK—ORDINARY CAPITAL RESOURCES

SUMMARY STATEMENT OF LOANS

31 December 2002 and 2001

Expressed in Thousands of United States Dollars (Note B)

Borrower/Guarantor	Loans Outstanding ¹	Undisbursed Balances of Effective Loans ²	Loans Not Yet Effective	Total Loans	Percent of Total Loans
Bangladesh	\$ 62,002	\$ 282,365	\$ 30,200	\$ 374,567	0.87
China, People's Rep. of	6,152,455	2,234,928	1,176,460	9,563,843	22.26
Fiji Islands	50,747	42,158	–	92,905	0.22
India	4,326,459	2,645,623	1,013,600	7,985,682	18.58
Indonesia	7,799,928	2,037,063	386,000	10,222,991	23.79
Kazakhstan	277,492	79,831	–	357,323	0.83
Korea, Rep. of	3,921,433	–	–	3,921,433	9.13
Malaysia	438,450	61,678	–	500,128	1.16
Marshall Islands	3,540	460	–	4,000	0.01
Myanmar	899	–	–	899	n.a. ³
Nauru	2,300	–	–	2,300	0.01
Nepal	39,867	–	–	39,867	0.09
Pakistan	2,352,958	876,306	622,738	3,852,002	8.96
Papua New Guinea	173,590	137,479	–	311,069	0.72
Philippines	2,551,482	1,125,399	85,000	3,761,881	8.75
Sri Lanka	86,881	119,291	16,026	222,198	0.52
Thailand	798,322	137,043	–	935,365	2.18
Uzbekistan	126,395	251,193	236,500 ⁴	614,088	1.43
Viet Nam	64,759	89,046	40,000	193,805	0.45
	<u>29,229,959</u>	<u>10,119,863</u>	<u>3,606,524</u>	<u>42,956,346</u>	<u>99.96</u>
Regional	<u>4,444</u>	<u>11,556</u>	<u>–</u>	<u>16,000</u>	<u>0.04</u>
TOTAL - 31 December 2002	<u>29,234,403</u>	<u>10,131,419</u>	<u>3,606,524</u>	<u>42,972,346</u>	<u>100.00</u>
Allowance for loan losses	(72,477)			(72,477)	
Unamortized front-end fee	(16,690)			(16,690)	
NET BALANCE - 31 December 2002	<u>\$ 29,145,236</u>	<u>\$ 10,131,419</u>	<u>\$ 3,606,524</u>	<u>\$ 42,883,179</u>	
Made up of loans to:					
Members and guaranteed by members	\$ 28,817,999	\$ 9,916,449	\$ 3,466,524	\$ 42,200,972	
Private sector (net of allowance for loan losses)	<u>327,237</u>	<u>214,970</u>	<u>140,000</u>	<u>682,207</u>	
Net balance - 31 December 2002	<u>\$ 29,145,236</u>	<u>\$ 10,131,419</u>	<u>\$ 3,606,524</u>	<u>\$ 42,883,179</u>	
TOTAL - 31 December 2001	\$ 28,738,974	\$ 10,514,720	\$ 3,281,315	\$ 42,535,009	
Allowance for loan losses	(80,128)			(80,128)	
NET BALANCE - 31 December 2001	<u>\$ 28,658,846</u>	<u>\$ 10,514,720</u>	<u>\$ 3,281,315</u>	<u>\$ 42,454,881</u>	
Made up of loans to:					
Members and guaranteed by members	\$ 28,334,516	\$ 10,268,101	\$ 3,221,315	\$ 41,823,932	
Private sector (net of allowance for loan losses)	<u>324,330</u>	<u>246,619</u>	<u>60,000</u>	<u>630,949</u>	
Net balance - 31 December 2001	<u>\$ 28,658,846</u>	<u>\$ 10,514,720</u>	<u>\$ 3,281,315</u>	<u>\$ 42,454,881</u>	

¹ Amounts outstanding on loans made under the pool-based variable interest rate systems and market-based variable/floating interest rate loans totaled \$28,586,399 (\$28,007,486 - 2001). The average yield on loans was 5.93% (6.42% - 2001).

² Of the undisbursed balances, ADB has made irrevocable commitments to disburse various amounts totaling \$85,311 (\$97,520 - 2001).

³ Below 0.01%.

⁴ Includes approval of \$70 million categorized under Regional.

The accompanying notes are an integral part of these financial statements (OCR-8).

MATURITY OF EFFECTIVE LOANS

Twelve Months Ending 31 December	Amount	Five Years Ending 31 December	Amount
2003	\$ 1,527,981	2012	11,140,302
2004	3,506,713	2017	9,479,663
2005	3,316,284	2022	4,985,665
2006	1,844,570	2027	1,415,787
2007	2,016,410	2030	<u>132,447</u>
		Total	<u>\$39,365,822</u>

SUMMARY OF CURRENCIES RECEIVABLE ON LOANS OUTSTANDING

Currency	2002	2001	Currency	2002	2001
Australian dollar	\$ 31	\$ 71	New Zealand dollar	184	370
Euro	10,401	11,024	Swiss franc	75,031	77,262
Japanese yen	7,608,832	7,401,173	United States dollar	<u>21,539,924</u>	<u>21,249,074</u>
			Total	<u>\$ 29,234,403</u>	<u>\$ 28,738,974</u>

ASIAN DEVELOPMENT BANK—ORDINARY CAPITAL RESOURCES

SUMMARY STATEMENT OF BORROWINGS

31 December 2002 and 2001

Expressed in Thousands of United States Dollars (Note B)

	Borrowings		Swap Arrangements ²	
	Principal Outstanding ¹		Payable (Receivable) ³	
	2002	2001	2002	2001
Long-Term Borrowing:				
Australian dollar	\$ 2,624,569	\$ 1,265,406	\$(2,413,935)	\$(1,290,423)
Canadian dollar	158,670	157,104	(170,238)	(176,767)
Deutsche mark	—	—	—	(731,048)
Euro	1,150,843	677,970	(1,279,491)	—
Hong Kong dollar	76,933	—	(79,615)	—
Japanese yen	4,171,908	4,663,401	3,222,992	1,656,207
			(1,006,720)	(393,505)
Korean won	—	60,929	—	(66,207)
Netherlands guilder	—	280,799	—	(307,358)
New Taiwan dollar	431,779	560,320	(464,610)	(600,565)
Pound sterling	157,974	360,350	—	(221,421)
Swiss franc	900,686	738,282	(456,328)	(356,923)
United States dollar	16,450,968	15,648,410	5,597,078	4,751,057
			(3,159,995)	(1,834,626)
Subtotal	<u>26,124,330</u>	<u>24,412,971</u>		
Short-Term Borrowing:				
Japanese yen	—	—	207,096	376,812
United States dollar	200,000	400,000	(200,936)	(400,560)
Subtotal	<u>200,000</u>	<u>400,000</u>		
Principal amount outstanding	26,324,330	24,812,971		
Unamortized discounts/premiums and transition adjustments	(419,029)	67,813		
FAS 133 Adjustment to financial expenses				
Total	<u>\$25,905,301</u>	<u>\$24,880,784</u>		

MATURITY STRUCTURE OF BORROWINGS OUTSTANDING⁵

Twelve Months Ending 31 December		Amount	Five Years Ending 31 December		Amount
2003	\$4,910,041	2012	5,734,753		
2004	4,983,862	2017	857,017		
2005	3,519,175	2022	84,437		
2006	1,164,305	2027	160,439		
2007	4,876,529	2032	33,772		
		Total	<u>\$26,324,330</u>		

¹ 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	
	2002	2001	2002	2001
Swiss franc	\$352,559	\$ 291,905	\$180,174	\$ 141,726
United States dollar	753,063	1,254,591	580,968	1,058,410

² Include currency and interest rate swaps. At 31 December 2002, the remaining duration of swap agreements ranged from less than one year to 30 years. Approximately 25.39% of the swap receivables and 23.89% of the payables are due from 31 December 2007 through 03 December 2032.

³ Adjusted by the cumulative effect of the adoption of FAS 133 effective 1 January 2001.

	Net Currency Obligation ³		Weighted Average Cost (%) After Swaps ⁴		
	2002	2001	2002		
	\$ 210,634	\$ (25,017)	(10.13)		
	(11,568)	(19,663)	0.32		
	-	(731,048)			
	(128,648)	677,970	(1.38)		
	(2,682)	-	(6.03)		
	6,388,180	5,926,103	3.03		
	-	(5,278)	1.68		
	-	(26,559)			
	(32,831)	(40,245)	(0.95)		
	157,974	138,929	11.57		
	444,358	381,359	6.05		
	18,888,051	18,564,841	4.84		
			<u>4.50</u>		
	207,096	376,812	(0.03)		
	(936)	(560)	<u>0.41</u>		
			(0.03)		
			4.36		
			<u>(0.27)</u>		
			<u>4.10</u>		
INTEREST RATE SWAP ARRANGEMENTS⁶					
		Average Rate (%)			
		Receive	Pay		
	Notional Amount		Fixed	Floating	Maturing Through ⁷
Receive Fixed Swaps:					
Australian dollar ⁸	\$ 151,982	3.75	3.59	(0.32)	2005–2032
Euro ⁹	84,435	4.40	3.62		2010
Japanese yen	84,434	5.50		(0.28)	2004
United States dollar	5,215,471	5.11		1.48	2003–2017
United States dollar ¹⁰	42,217	2.14		(0.31)	2016–2027
Receive Floating Swaps:					
Japanese yen	430,616	2.23	4.13	(0.34)	2003–2032
United States dollar	80,917	2.01	6.60	1.17	2003–2014
Total	\$ 6,090,072				

⁴ In calculating cost of borrowings, the cumulative effect of the adoption of FAS 133 is excluded. Also, calculation is based on borrowings, net of swap exposure. Thus the weighted average cost may be negative if related swaps payable exposure is included in other currency calculation.

⁵ Bonds with put and call options were considered maturing on the first put or call date.

⁶ The interest rate swap information is based on interest rates at 31 December 2002. To the extent that interest rates change, variable interest rate information will change.

⁷ Swaps with early termination date were considered maturing on the first termination date.

⁸ Consists of a currency coupon swap with interest receivable in Australian dollar and interest payable in Japanese yen.

⁹ Consists of a currency coupon swap with interest receivable in Euro and interest payable in Japanese yen.

¹⁰ Consists of a currency coupon swap with interest receivable in United States dollar and interest payable in Japanese yen.

The accompanying notes are an integral part of these financial statements (OCR-8).

ASIAN DEVELOPMENT BANK—ORDINARY CAPITAL RESOURCES

STATEMENT OF SUBSCRIPTIONS TO CAPITAL STOCK AND VOTING POWER

31 December 2002

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	0.034	\$ 16,187	\$ 11,013	\$ 5,174	15,486	0.355
Australia	204,740	5.871	2,773,367	2,579,147	194,220	219,031	5.025
Azerbaijan	15,736	0.451	213,157	198,162	14,995	30,027	0.689
Bangladesh	36,128	1.036	489,383	455,112	34,271	50,419	1.157
Bhutan	220	0.006	2,980	2,669	312	14,511	0.333
Cambodia	1,750	0.050	23,705	19,669	4,037	16,041	0.368
China, People's Rep. of	228,000	6.539	3,088,442	2,872,102	216,340	242,291	5.559
Cook Islands	94	0.003	1,273	1,192	81	14,385	0.330
Fiji Islands	2,406	0.069	32,591	30,302	2,289	16,697	0.383
Hong Kong, China	19,270	0.553	261,028	242,741	18,287	33,561	0.770
India	224,010	6.424	3,034,395	2,821,902	212,493	238,301	5.467
Indonesia	192,700	5.526	2,610,276	2,427,489	182,787	206,991	4.749
Japan	552,210	15.836	7,480,126	6,956,283	523,843	566,501	12.997
Kazakhstan	28,536	0.818	386,543	359,465	27,078	42,827	0.983
Kiribati	142	0.004	1,924	1,788	135	14,433	0.331
Korea, Rep. of	178,246	5.112	2,414,485	2,245,420	169,065	192,537	4.417
Kyrgyz Republic	10,582	0.303	143,342	133,304	10,037	24,873	0.571
Lao PDR	492	0.014	6,665	5,947	718	14,783	0.339
Malaysia	96,350	2.763	1,305,138	1,213,731	91,407	110,641	2.538
Maldives	142	0.004	1,924	1,788	135	14,433	0.331
Marshall Islands	94	0.003	1,273	1,192	81	14,385	0.330
Micronesia, Fed. States of	142	0.004	1,924	1,788	135	14,433	0.331
Mongolia	532	0.015	7,206	6,705	501	14,823	0.340
Myanmar	19,270	0.553	261,028	242,741	18,287	33,561	0.770
Nauru	142	0.004	1,924	1,788	135	14,433	0.331
Nepal	5,202	0.149	70,465	65,521	4,944	19,493	0.447
New Zealand	54,340	1.558	736,079	684,537	51,542	68,631	1.575
Pakistan	77,080	2.210	1,044,110	970,990	73,120	91,371	2.096
Papua New Guinea	3,320	0.095	44,972	41,843	3,129	17,611	0.404
Philippines	84,304	2.418	1,141,965	1,062,004	79,961	98,595	2.262
Samoa	116	0.003	1,571	1,409	163	14,407	0.331
Singapore	12,040	0.345	163,091	151,672	11,419	26,331	0.604
Solomon Islands	236	0.007	3,197	2,980	217	14,527	0.333
Sri Lanka	20,520	0.588	277,960	258,495	19,465	34,811	0.799
Taipei, China	38,540	1.105	522,055	485,509	36,547	52,831	1.212
Tajikistan	10,134	0.291	137,273	127,615	9,658	24,425	0.560
Thailand	48,174	1.382	652,555	606,852	45,704	62,465	1.433
Timor-Leste	350	0.010	4,741	4,402	339	14,641	0.336
Tonga	142	0.004	1,924	1,788	135	14,433	0.331
Turkmenistan	8,958	0.257	121,343	112,809	8,534	23,249	0.533
Tuvalu	50	0.001	677	623	54	14,341	0.329
Uzbekistan	23,834	0.684	322,851	300,243	22,608	38,125	0.875
Vanuatu	236	0.007	3,197	2,980	217	14,527	0.333
Viet Nam	12,076	0.346	163,579	144,818	18,761	26,367	0.605
Total Regional (Forward)	2,212,781	63.458	\$29,973,889	\$27,860,527	\$2,113,362	2,841,585	65.192

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		
Total Regional (Forward)	2,212,781	63.458	\$29,973,889	\$27,860,527	\$2,113,362	2,841,585	65.192
NONREGIONAL							
Austria	12,040	0.345	163,091	151,672	11,419	26,331	0.604
Belgium	12,040	0.345	163,091	151,672	11,419	26,331	0.604
Canada	185,086	5.308	2,507,138	2,331,571	175,567	199,377	4.574
Denmark	12,040	0.345	163,091	151,672	11,419	26,331	0.604
Finland	12,040	0.345	163,091	151,672	11,419	26,331	0.604
France	82,356	2.362	1,115,578	1,037,446	78,132	96,647	2.217
Germany	153,068	4.390	2,073,429	1,928,218	145,211	167,359	3.840
Italy	63,950	1.834	866,254	805,582	60,672	78,241	1.795
The Netherlands	36,294	1.041	491,631	457,211	34,420	50,585	1.161
Norway	12,040	0.345	163,091	151,672	11,419	26,331	0.604
Portugal	12,040	0.345	163,091	151,618	11,473	26,331	0.604
Spain	12,040	0.345	163,091	151,672	11,419	26,331	0.604
Sweden	12,040	0.345	163,091	151,672	11,419	26,331	0.604
Switzerland	20,650	0.592	279,721	260,120	19,601	34,941	0.802
Turkey	12,040	0.345	163,091	151,672	11,419	26,331	0.604
United Kingdom	72,262	2.072	978,847	910,305	68,542	86,553	1.986
United States	552,210	15.836	7,480,126	6,956,283	523,843	566,501	12.997
Total Nonregional	1,274,236	36.542	17,260,546	16,051,732	1,208,814	1,517,183	34.808
TOTAL	3,487,017	100.000	\$47,234,435	\$43,912,259	\$3,322,176	4,358,768	100.000

Note: Figures may not add due to rounding.

The accompanying notes are an integral part of these financial statements (OCR-8).

NOTES TO FINANCIAL STATEMENTS

31 December 2002 and 2001

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

Nature of Operations

The Asian Development Bank (ADB), a multilateral development finance institution, was established in 1966 with its headquarters in Manila, Philippines. ADB and its operations are governed by the Agreement Establishing the Asian Development Bank (the Charter). Its purpose is to foster economic development and co-operation in the Asian and Pacific region and to contribute to the acceleration of the process of economic development of the developing member countries (DMCs) in the region, collectively and individually. With the adoption of its poverty reduction strategy at the end of 1999, ADB made reducing poverty in the region its main goal. ADB provides financial and technical assistance (TA) for projects and programs which will contribute to achieving this purpose.

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

ADB's ordinary operations comprise loans, equity investments, and guarantees. Commencing 2001, limited technical assistance to member countries to support high priority TA programs is included. ADB 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 ADB shall not exceed the total of ADB's unimpaired subscribed capital, reserves, and surplus, exclusive of the special reserve. At 31 December 2002, the total of such loans, equity investments, and guarantees aggregated approximately 78.4% (83.9% – 2001) 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 paid-in capital together with reserves and surplus, exclusive of the special reserve. At 31 December 2002, such equity investments represented approximately 3.3% (3.5% – 2001) 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 ADB 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 (ADB'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 ADB'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 2002, the value of the SDR in terms of the current United States dollar was \$1.35458 (\$1.25562 – 2001) giving a value for each share of ADB's capital equivalent to \$13,545.80 (\$12,556.20 – 2001). However, ADB 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."

CONTINUED

Derivative Financial Instruments

In June 1998, the Financial Accounting Standards Board (FASB) issued Statement of Financial Accounting Standards (SFAS) No. 133, "Accounting for Derivative Instruments and Hedging Activities." SFAS No. 133 was further amended by SFAS No. 137, "Accounting for Derivative Instruments and Hedging Activities – Deferral of the Effective Date of FASB Statement No. 133" and SFAS No. 138, "Accounting for Certain Derivative Instruments and Certain Hedging Activities, an amendment of Statement 133." The standards are herein collectively referred to as FAS 133. FAS 133, is effective for ADB on 1 January 2001. This statement establishes accounting and reporting standards requiring that every derivative instrument be recorded in the Balance Sheet as either an asset or liability measured at its fair value. Changes in the fair value of derivatives are recorded in net income or other comprehensive income, depending on whether a derivative is designated as part of a hedge transaction and, if it is, the type of hedge transaction.

ADB uses derivative instruments for asset/liability management of individual positions and portfolios, as well as for the reduction of transaction costs. In applying FAS 133 for purposes of financial statement reporting, ADB has elected not to define any qualifying hedging relationships. Rather, all derivative instruments, as defined by FAS 133, have been marked to fair value and all changes in the fair value have been recognized in net income. ADB has elected not to define any qualifying hedging relationships, not because economic hedges do not exist, but rather because the application of FAS 133 hedging criteria does not make evident the impact of economic risks inherent in ADB's financial assets and liabilities.

The cumulative effect of a change in accounting principle includes the difference between the carrying value and the fair value of the derivative instruments in the borrowings portfolio on 31 December 2000 as well as loans that met hedge criteria, offset by any gains or losses on those borrowings and loans for which a fair value exposure was being hedged. The net effect gave rise to a transition loss of \$81,657,000 in 2001, out of which, a loss of \$116,313,000 is reported in other comprehensive income and a gain of \$34,656,000 is reported in net income. The allocation between net income and other comprehensive income was based upon the hedging relationships that existed before the initial application of this statement.

Since ADB has not defined any qualifying hedging relationships under this standard, the amount recorded in other comprehensive income as part of the transition is being reclassified into earnings in the same period or periods in which the hedged forecasted transaction affects earnings.

Investments

All investment securities and negotiable certificate of deposits held by ADB other than derivative instruments 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." All derivative instruments are marked to market. Estimated fair value generally represents market value. Time deposits are classified as "Held-to-Maturity" and are reported at cost. Realized gains and losses are included in income from investments and are measured by the difference between amortized cost and the net proceeds of sales. With respect to futures, realized gain or loss is reported based on daily settlement of the net cash margin.

Securities Transferred Under Securities Lending Arrangement

ADB accounts for transfers of financial assets in accordance with FAS 140, "Accounting for Transfers and Servicing of Financial Assets and Extinguishments of Liabilities—a replacement of FAS 125." In general, transfers are accounted for as sales under FAS 140 when ADB has relinquished control over the transferred assets. Transfers that are not accounted for as sales are accounted for as repurchase agreements and collateralized financing arrangements.

Loans

ADB's loans are made to or guaranteed by members, with the exception of loans to the private sector, and have maturities ranging between 3 and 30 years. ADB requires its borrowers to absorb exchange risks attributable to fluctuations in the value of the currencies which it has disbursed. Loan interest income and loan commitment fees are recognized on accrual basis. With the introduction of Libor-based loans in 2001, in line with ADB's principle of cost pass through pricing, any variation in the actual cost of borrowings is passed to Libor-based borrowers as surcharge or rebate.

It is the policy of ADB to place loans in nonaccrual status for which principal, interest, or other charges are overdue by six months. Interest and other charges on nonaccruing loans are included in income only to the extent that payments have been received by ADB. ADB follows a policy of not taking part in debt rescheduling agreements with respect to public sector loans. In the case of private sector loans, ADB may agree to debt rescheduling only after alternative courses of action have been exhausted.

NOTES TO FINANCIAL STATEMENTS

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ADB 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 (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 loan losses.

ADB's periodic evaluation of the adequacy of the allowance for loan 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.

ADB levies front-end fees on all new loans. These fees are deferred and amortized over the life of the loans after offsetting deferred direct loan origination costs.

Equity Investments

Investments in equity securities without readily determinable fair values are reported at cost less probable losses inherent in the portfolio but not specifically identifiable.

The reserve against losses for equity investments is established quarterly based on Management's evaluation of potential losses for such investments. Equity investments with readily determinable fair values are reported at fair value, with unrealized gains and losses excluded from net income and reported in "CAPITAL AND RESERVES" as part of "Accumulated other comprehensive income." ADB 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 are stated at cost and, except for land, 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.

Accounting and Reporting Developments

In November 2002, FASB issued FASB interpretation (FIN) No. 45, "Guarantor's Accounting and Disclosure Requirements for Guarantees, Including Indirect Guarantees of Indebtedness of Others" - an interpretation of FASB Statements No. 5, 57, and 107 and rescission of FASB Interpretation No. 34. This interpretation requires a guarantor to recognize, at the inception of a guarantee, a liability for the fair value of all of the obligations it has undertaken in issuing a guarantee, including its ongoing obligation to stand ready to perform over the term of the guarantee in the event that the specified triggering events or conditions occur. This provision applies to guarantees issued or modified after 31 December 2002. FIN No. 45 also clarifies requirements about disclosures on guarantees. Full disclosures on all outstanding financial guarantees have been made in Notes E and N to the financial statements.

In January 2003, FASB issued FIN No. 46, "Consolidation of Variable Interest Entities - an Interpretation of Accounting Research Bulletin No. 51, Consolidated Financial Statements." FIN No. 46 requires a variable interest entity be consolidated and disclosed in the notes to the financial statements if ADB is subject to a majority of the risk of loss from the variable interest entity's activities or entitled to receive a majority of the entity's residual returns or both. Variable interest entity in ADB relates to an equity investment that is presently accounted for under the equity method. This interpretation is effective 31 January 2003 for entities created after that date or in the first fiscal year beginning after 15 June 2003 for the existing entities. Adoption of this standard will not have a significant impact on ADB's financial statements.

Statement of Cash Flows

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

Reclassification

Certain reclassifications of prior year's information have been made to conform to the current year's presentation.

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 ADB or by any recipient from ADB of certain

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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 40 DMCs for 2002 (39 – 2001), cash in banks (due from banks) and demand obligations totaling \$51,660,000 (\$51,919,000 – 2001) and \$229,518,000 (\$217,926,000 – 2001), respectively, may be, but are not currently so restricted.

In accordance with Article 24, paragraphs 2(i) and (ii) of the Charter, one member (two – 2001) has restricted the use by ADB or by any recipient from ADB of its currency to payments for goods or services produced in its territory. As such, cash in banks (due from banks) and investments totaling \$86,000 (\$36,000 – 2001) and \$2,662,000 (\$4,783,000 – 2001), respectively, have been restricted. None of the demand obligations held by ADB in 2002 was restricted (\$2,778,000 – 2001).

NOTE D—INVESTMENTS AND SWAP TRANSACTIONS

The main investment management objective is to maintain security and liquidity. Subject to these parameters, ADB seeks the highest possible return on its investments. Investments are governed by the Investment Authority approved by the Board of Directors in 1999. ADB is restricted by its Investment Authority to invest in investment instruments which are obligations of a limited class of issuers, primarily government or government-guaranteed obligations and corporate obligations.

ADB entered into two asset swap transactions as a new investment vehicle with total notional amount of \$40,053,000.

Included in other securities as of 31 December 2002 were corporate bonds and other obligations of banks amounting to \$2,309,323,000 (\$1,529,545,000 – 2001) and asset/mortgage-backed securities of \$662,054,000 (\$534,331,000 – 2001).

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 securities, financial futures and options. To increase returns, ADB may invest in securities denominated in currencies other than the originating 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 for trading purposes.

The currency compositions of the investment portfolio as of 31 December 2002 and 2001 expressed in United States dollars are as follows:

Currency	2002	2001
Australian dollar	\$ 371,126,000	\$ 245,470,000
Canadian dollar	147,575,000	136,680,000
Euro	305,862,000	278,641,000
Japanese yen	1,563,582,000	1,078,786,000
Pound sterling	198,868,000	183,040,000
Swiss franc	400,449,000	321,441,000
United States dollar	5,758,717,000	5,785,007,000
Others	282,562,000	235,850,000
Total	\$9,028,741,000	\$8,264,915,000

The estimated fair value and amortized cost of the investments by contractual maturity at 31 December 2002 are as follows:

	Estimated Fair Value	Amortized Cost
Due in one year or less	\$2,772,725,000	\$2,770,965,000
Due after one year through five years	4,772,139,000	4,637,959,000
Due after five years through ten years	1,483,877,000	1,441,126,000
Total	\$9,028,741,000	\$8,850,050,000

Time deposit at cost approximates its fair value. Additional information relating to investments in government and government-guaranteed obligations and other securities is as follows:

	2002	2001
As of 31 December		
Amortized cost	\$6,919,488,000	\$5,500,606,000
Estimated fair value	7,098,180,000	5,591,662,000
Gross unrealized gains	178,697,000	91,430,000
Gross unrealized losses	5,000	374,000
For the years ended 31 December		
Change in net unrealized gains	87,636,000	24,703,000
Proceeds from sales	6,279,108,000	6,627,494,000
Gross realized gains	81,017,000	86,397,000
Gross realized losses	6,796,000	5,547,000

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Asset/Mortgage-backed Securities: Asset/Mortgage-backed securities are instruments whose cash flow is based on the cash flows of a pool of underlying assets or mortgage loans managed by a trust.

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. ADB generally closes out open positions prior to maturity. Therefore, cash receipts or payments are limited to the change in market value of the futures. At 31 December 2002, the nominal amount of outstanding purchase and sales contracts were \$161,700,000 and \$121,100,000, respectively (\$294,500,000 and \$187,300,000 – 2001).

NOTE E—LOANS AND GUARANTEES

Loans

ADB does not currently sell its loans, nor does it believe there is a comparable market for its loans. The estimated fair value of all loans is based on the estimated cash flows from principal repayments, interest and other charges discounted at the applicable market yield curves for ADB's borrowing cost plus lending spread. The estimated fair value of public sector loans is not affected by credit risks based on ADB's experience with its borrowers. Allowance for loan losses is made against private sector loans.

The carrying amount and estimated fair value of loans outstanding at 31 December 2002 and 2001 are as follows:

	2002		2001	
	Carrying Value	Estimated Fair Value	Carrying Value	Estimated Fair Value
Fixed rate multicurrency loans	\$ 495,503,000	\$ 635,883,000	\$ 559,641,000	\$ 708,134,000
Pool-based multicurrency loans	7,090,757,000	7,847,113,000	7,006,085,000	7,902,889,000
Pool-based single currency (US\$) loans	15,081,772,000	16,917,561,000	16,158,226,000	17,108,946,000
LIBOR-based single currency loans	6,428,575,000	6,459,242,000	4,873,607,000	4,906,480,000
Fixed rate single currency loans	48,629,000	62,304,000	61,287,000	70,701,000
Total	\$29,145,236,000	\$31,922,103,000	\$28,658,846,000	\$30,697,150,000

Prior to 1 July 1986, the lending rate of ADB 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, ADB adopted a multicurrency pool-based variable lending rate system. In addition, in July 1992, ADB introduced a United States dollar pool-based variable lending rate system, and in November 1994, a market-based variable lending rate system was made available to financial intermediaries in the public sector and to the private sector borrowers. For loans to the private sector borrowers, approximately 72% (69% – 2001) of the loans were based on variable lending rates.

Since 1988, ADB has charged front-end fees for private sector loans. Effective 1 January 2000, ADB levies front-end fee of 1% for public sector loans for which the loan negotiations are completed after that date. In addition, the lending spread applied to all outstanding pool-based OCR public sector loans and new public sector market-based loans has been increased from 0.4% to 0.6%. Also effective the same date, a flat commitment fee of 0.75% is charged for new program loans,

while the progressive commitment fee of 0.75% is maintained for project loans.

The front-end fees earned for the year ended 31 December 2002 were \$37,057,000 (\$34,793,000 – 2001) for loans and \$6,092,000 (nil – 2001) for guarantees. Administrative expenses relating to direct loan origination of \$19,440,000 for the year ended 31 December 2002 (\$34,793,000 – 2001) were deferred and offset against front-end fees earned.

Commencing 1 July 2001, ADB offered LIBOR-based loans (LBLs) in any of the following currencies—Euro, Japanese yen, or United States dollar. The new LBL lending facility offers borrowers the flexibility of (i) choice of currency and interest rate basis; (ii) options to link repayment schedules to actual disbursements for financial intermediary borrowers; (iii) change the original loan terms (currency and interest rate basis) at any time during the life of the loan; and (iv) options to cap or collar the floating lending rate at any time during the life of the loan. LBL terms are available for all new loans for which the invitation to negotiate is issued on or after 1 July 2001.

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When ADB introduced the LBL, it also offered its borrowers the option to transform undisbursed balances of their eligible pool-based single currency loans in United States dollar to LBL terms. Ninety seven of such loans with a total undisbursed balance of \$6.8 billion were transformed to LBL terms as of 31 December 2002. ADB's loan product available to borrowers is only LBL starting 1 July 2002.

In 2002, ADB received 19 full and partial prepayments amounting to \$1,977,139,000 (\$52,497,000 – 2001) from four borrowers and collected premiums of \$62,521,000 (\$2,841,000 – 2001) on the prepayments which have been included in "Other income from loans."

Undisbursed loan commitments and an analysis of loans by borrowing member countries as of 31 December 2002 are shown in OCR-5. The carrying amounts of loan outstanding by loan products at 31 December 2002 and 2001 are as follows:

	<u>2002</u>	<u>2001</u>
Public Sector		
Fixed rate		
multicurrency loans	\$ 495,503,000	\$ 559,641,000
Pool-based		
multicurrency loans	7,082,638,000	6,995,932,000
Pool-based single		
currency (US\$) loans	15,083,794,000	16,158,226,000
Market-based loans –		
floating rate	4,330,709,000	4,298,838,000
Market-based loans –		
fixed rate	2,317,000	1,095,000
LIBOR-based loans	1,839,462,000	320,784,000
	<u>28,834,423,000</u>	<u>28,334,516,000</u>
Less: Unamortized		
front-end fee	(16,424,000)	–
	<u>28,817,999,000</u>	<u>28,334,516,000</u>
Private Sector		
Pool-based		
multicurrency loans	10,442,000	12,497,000
Currency specific loans	154,942,000	190,094,000
Private sector		
facility loans	7,333,000	7,340,000
Market-based loans –		
floating rate	178,982,000	152,747,000
Market-based loans –		
fixed rate	37,131,000	37,336,000
Libor-based loans	6,706,000	–
Revolving facility –		
AFIC	4,444,000	4,444,000
	<u>399,980,000</u>	<u>404,458,000</u>
Less: Allowance for		
loan loss	(72,477,000)	(80,128,000)
Unamortized		
front-end fee	(266,000)	–
	<u>(72,743,000)</u>	<u>(80,128,000)</u>
	<u>327,237,000</u>	<u>324,330,000</u>
Total	<u>\$29,145,236,000</u>	<u>\$28,658,846,000</u>

Loans in Nonaccrual Status

Two public sector loans to Myanmar and one public sector loan to Nauru were in nonaccrual status as of 31 December 2002 (two to Myanmar and one to Nauru – 2001). The principal outstanding for these three loans as of 31 December 2002 was \$3,199,000 (\$3,095,000 – 2001) of which \$1,129,000 (\$795,000 – 2001) was overdue. Loans in nonaccrual status resulted in \$231,000 (\$307,000 – 2001) not being recognized as income from public sector loans for the year ended 31 December 2002. The accumulated interest and other charges on these loans that were not recognized as income as of 31 December 2002 would have totaled \$745,000 (\$514,000 – 2001).

Thirteen private sector loans were in nonaccrual status as of 31 December 2002 (twelve – 2001). The principal outstanding at that date was \$83,874,000 (\$75,449,000 – 2001) of which \$69,891,000 (\$52,141,000 – 2001) was overdue. Loans in nonaccrual status resulted in \$7,930,000 (\$7,676,000 – 2001) not being recognized in income from private sector loans for the year ended 31 December 2002. The accumulated interest and other charges on these loans that were not recognized as of 31 December 2002 would have totaled \$30,131,000 (\$29,380,000 – 2001).

Loan Loss Provision

ADB has not suffered any losses of principal on public sector loans. No loan loss provisions have been made against outstanding public sector loans, but loan loss provisions have been made against private sector loans during the year (see Note K).

Information pertaining to loans which were subject to loan loss provisions at 31 December 2002 and 2001 is as follows:

	<u>2002</u>	<u>2001</u>
Loans not subject		
to loss provisions	\$29,141,349,000	\$28,629,075,000
Loans subject to		
loss provisions	93,054,000	109,899,000
Total	<u>\$29,234,403,000</u>	<u>\$28,738,974,000</u>
Average amount of		
loans subject to		
loss provisions	\$ 91,945,000	\$ 113,060,000
Related interest		
income on such		
loans	\$ 2,262,000	\$ 3,182,000
Cash received on		
related interest		
income on such		
loans	\$ 1,385,000	\$ 3,591,000

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The changes in the allowance for loan losses during 2002 and 2001 are as follows:

	2002	2001
Balance - 1 January	\$ 80,128,000	\$75,610,000
Provision during the year	3,909,000	4,994,000
Provision written back	(11,894,000)	-
Translation adjustments	334,000	(476,000)
Balance - 31 December	<u>\$ 72,477,000</u>	<u>\$80,128,000</u>

Loan Guarantees

ADB extends guarantees to public sector and private sector borrowers which are not reflected in the financial statements. Such guarantees include (i) partial credit guarantees where only certain principal and/or interest payments are covered; and (ii) political risk guarantees, which provide coverage against well-defined sovereign risks. While ADB's guarantees do not necessarily require applicable

government's counterguarantees, all ADB's outstanding guarantees as of 31 December 2002 were counterguaranteed by its concerned government. A counterguarantee takes the form of a member government agreement to indemnify ADB for any payments it makes under the guarantee. Guaranteed payments under partial credit guarantees are generally due 10 or more years from the loan inception date. ADB's political risk guarantee is callable when a guaranteed event has occurred and such an event has resulted in debt service default to the guaranteed lender. The present value of the contingent future payment obligations of all outstanding partial credit guarantees and the nominal value of political risk guaranteed obligation at 31 December 2002 and 2001 are used to calculate ADB's lending limitation. None of these amounts were subject to call as of that date (nil - 31 December 2001). ADB estimates that the present value of guarantees outstanding at 31 December 2002 approximates their fair value.

As at 31 December 2002 and 2001, the outstanding amount and present value of ADB's guarantee obligations covered:

	2002		2001	
	Outstanding Guaranteed Amount	Present Value	Outstanding Guaranteed Amount	Present Value
Partial Credit Guarantees				
Complementary Loans				
China, People's Rep. of	\$ 28,496,000	\$ 22,532,000	\$ 27,966,000	\$ 21,039,000
India	63,326,000	46,590,000	57,235,000	39,935,000
Indonesia	24,055,000	18,870,000	21,741,000	16,174,000
Papua New Guinea	-	-	505,000	494,000
Subtotal	<u>115,877,000</u>	<u>87,992,000</u>	<u>107,447,000</u>	<u>77,642,000</u>
Bond Issue				
Philippines	800,481,000	324,439,000	91,575,000	44,148,000
Term Loans				
Sri Lanka	114,513,000	86,659,000	112,636,000	80,839,000
Subtotal	<u>1,030,871,000</u>	<u>499,090,000</u>	<u>311,658,000</u>	<u>202,629,000</u>
Political Risk Guarantees				
Bangladesh	60,269,000	35,748,000	28,735,000	16,147,000
Pakistan*	850,000	850,000	8,662,000	8,220,000
Sri Lanka	25,820,000	17,464,000	6,118,000	3,936,000
Subtotal	<u>86,939,000</u>	<u>54,062,000</u>	<u>43,515,000</u>	<u>28,303,000</u>
Total	<u>\$1,117,810,000</u>	<u>\$553,152,000</u>	<u>\$355,173,000</u>	<u>\$230,932,000</u>

* Reported at face value being a revolving facility in nature.

The outstanding guaranteed amounts represent the amounts utilized under the related loans which have been disbursed as of the end of a reporting period. At 31 December 2002, the nominal amount of the partial credit guarantees and

political risk guarantees facilities were \$1,030,871,000 and \$251,000,000, respectively (\$317,596,000 and \$251,000,000, respectively - 31 December 2001).

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Cofinancing

ADB functions as lead lender in cofinancing arrangements with other participating financial institutions who also provide funds to ADB's public and private sector borrowers. In such capacity, ADB provides loan administration services,

which include loan disbursements and loan collections. The participating financial institutions have no recourse to ADB for their outstanding loan balances.

Loans administered by ADB on behalf of participating institutions as at 31 December 2002 and 2001 are as follows:

	2002		2001	
	Amount	No. of Loans	Amount	No. of Loans
Public sector loans	\$ 946,069,000	43	\$ 994,709,000	39
Private sector loans	267,477,000	11	277,284,000	15
Total	<u>\$1,213,546,000</u>	<u>54</u>	<u>\$1,271,993,000</u>	<u>54</u>

During the year ended 31 December 2002, a total of \$389,000 (\$532,000 - 2001) was received as compensation for arranging and administering such loans. This amount has been included in "Income from other sources."

NOTE F—EQUITY INVESTMENTS

ADB's investments in equity securities issued by private enterprises located in DMCs include a \$13,620,000 (\$13,874,000 - 2001) 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. ADB also holds 100% of AFIC issued convertible noncumulative preference shares in the amount of \$25,000,000 (\$25,000,000 - 2001). In October 2002, ADB together with other financiers, renewed the revolving credit facility up to a maximum aggregate principal amount outstanding at any time of \$36,000,000 (\$45,000,000 - 2001). ADB's obligations amount to \$16,000,000, of which, at 31 December 2002, the outstanding loan is \$4,444,000 (\$4,444,000 - 2001). This amount has been included in "LOANS OUTSTANDING" (see Note E).

Unrealized gains on equity investments reported at market value were \$4,335,000 at 31 December 2002 (\$2,269,000 - 2001) and were reported in "CAPITAL AND RESERVES" as part of "Accumulated other comprehensive income."

Approved equity investment facility that has not been disbursed was \$197,928,000 at 31 December 2002 (\$176,739,000 - 2001).

NOTE G—PROPERTY, FURNITURE, AND EQUIPMENT

In 1991, under the terms of an agreement with the Philippines (Government), ADB returned the former headquarters pre-

mises which had been provided by the Government. In accordance with the agreement as supplemented by a memorandum of understanding, ADB 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. The amortization for the year ended 31 December 2002 amounted to \$511,000 (\$567,000 - 2001) reducing depreciation expense for the new headquarters building from \$4,492,000 (\$4,414,000 - 2001) to \$3,981,000 (\$3,847,000 - 2001). At 31 December 2002, the unamortized deferred compensation balance (included in "ACCOUNTS PAYABLE AND OTHER LIABILITIES - Miscellaneous") was \$9,653,000 (\$10,225,000 - 2001). At 31 December 2002, accumulated depreciation for property, furniture, and equipment was \$91,195,000 (\$82,614,000 - 2001).

NOTE H—BORROWINGS AND SWAP TRANSACTIONS

ADB 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 ADB's major operational currencies, taking advantage of the opportunities offered in different financial markets. Such currency swaps enable ADB 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.

ADB issues structured debt which includes embedded currency and/or interest rate derivatives in order to decrease

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its cost of borrowing. However, ADB enters into simultaneous currency and/or interest rate swaps to hedge fully against the effects of such embedded derivatives.

ADB has a potential risk of loss if the swap counterparty fails to perform its obligations. In order to reduce such credit risk, ADB only enters into long-term swap transactions with counterparties eligible under ADB's swap guidelines which include a requirement that the counterparties have a credit rating of double A or higher.

The fair value of outstanding currency swap agreements, interest rate swap agreements, and borrowings is determined at the estimated amount that ADB would receive or pay to terminate the agreements using a market-based valuation model. The basis of valuation is the present value of expected cash flows based on appropriate market data.

Interest rate swaps: Under a typical interest rate swap agreement used by ADB, 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. The terms of ADB'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 the currency swapped out, and a payable is created for the currency swapped in. The terms of ADB's currency swap agreements specifically match the terms of particular borrowings.

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 ADB as of the end of 2002 and 2001 consists of 3,490,994 shares, of which 3,487,017 shares (3,474,627 – 2001) have been subscribed by members. Of the subscribed shares, 3,241,762 (3,230,244 – 2001) are “callable” and 245,255 (244,383 – 2001) are “paid-in.” The “callable” share capital is subject to call by ADB only as and when required to meet ADB'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, ADB 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 ADB for the conduct of its operations. The settlement of such amounts is not determinable and, accordingly, it is not practicable to determine a fair value for these receivables.

As of 31 December 2002, all matured installments amounting to \$3,311,328,000 (\$3,049,555,000 – 2001) were received except for \$2,815,000 (\$4,353,000 – 2001) from one country (two – 2001). Installments not due aggregating \$10,848,000 (\$18,967,000 – 2001) are receivable as follows:

For the Year ending 31 December:

2003	\$5,038,000	2004	\$2,905,000	2005	\$2,905,000
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Payments in respect of capital subscription installments in advance of due dates are shown in the Balance Sheet (under “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 ADB 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 ADB. The resources so set aside amounting to \$64,491,000 as of 31 December 2002 (\$59,780,000 – 2001) expressed in terms of the SDR on the basis of \$1.35458 (\$1.25562 – 2001) 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, ADB implemented maintenance of

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value (MOV) 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. Since then, settlement of MOV has been put in abeyance.

Inasmuch as the valuation of ADB's capital stock and the basis of determining possible MOV 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. In view thereof, the notional MOV amounts of receivables and payables are offset against one another and shown as net notional amounts to maintain value of currency holdings in the "CAPITAL AND RESERVES" portion of the Balance Sheet. The timing of the establishment and settlement of such amounts is uncertain and, accordingly, it is not practicable to determine a fair value for such receivables and payables.

One country made an arrangement with ADB that has the effect of continuing the settlement of their MOV obligation. The "Amounts required to maintain value of currency holdings" under "RECEIVABLE FROM MEMBERS" represents the amount receivable from changes in exchange rates of the member's currency in relation to the United States dollar.

The net notional amounts as of 31 December 2002 consisted of (a) the increase of \$334,457,000 (\$148,847,000 - 2001) 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 2002 and (b) the net decrease of \$153,999,000 (\$313,609,000 - 2001) in the value of such currency holdings in relation to the United States dollar during the same period. In terms of receivable from and payable to members, they are as follows:

	<u>2002</u>	<u>2001</u>
Notional MOV Receivables	\$718,212,000	\$657,940,000
Notional MOV Payables	229,756,000	195,484,000
Total	<u>\$488,456,000</u>	<u>\$462,456,000</u>

Membership

As of 31 December 2002, ADB is owned by 61 member countries, 44 countries from the region and 17 countries from outside the region (see OCR-7). During 2002, Portugal and Timor-Leste have subscribed 12,040 and 350 shares of ADB's capital stock respectively, and remitted the required paid-in portion of their subscriptions.

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 2002, \$714,464,000 of the net income for the year ended 31 December 2001 was allocated to the Ordinary Reserve (\$625,716,000 - 2001).

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 \$56,808,000 to the Ordinary Reserve during the year ended 31 December 2002 (credit of \$20,236,000 - 2001). 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.

Cumulative Revaluation Adjustments Account

In May 2002, the Board of Governors approved the allocation of \$147,501,000 of the 31 December 2001 net income to a separate category of Reserves - "Cumulative Revaluation Adjustments Account." This represents the cumulative FAS 133 adjustment.

Special Reserve

The Special Reserve includes 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 2002, guarantee fees amounting to \$861,000 (\$1,295,000 - 2001) were appropriated to Special Reserve.

Surplus

Surplus represents funds for future use to be determined by the Board of Governors. No amounts were allocated by the Board of Governors out of Surplus during 2002 and 2001.

ASIAN DEVELOPMENT BANK—ORDINARY CAPITAL RESOURCES

NOTES TO FINANCIAL STATEMENTS

31 December 2002 and 2001

Comprehensive Income and Accumulated Other Comprehensive Income

Comprehensive income has two major components: net income and other comprehensive income comprising gains and losses affecting equity that, under generally accepted accounting principles, are excluded from net income. Other comprehensive income includes such items as the effects of the implementation of FAS 133, unrealized gains and losses on available-for-sale securities and listed equity investments, and currency translation adjustments.

NOTE K—INCOME AND EXPENSES

Total income from loans for the year ended 31 December 2002 was \$1,709,943,000 (\$1,813,640,000 – 2001). The average yield on the loan portfolio during the year was 5.93% (6.42% – 2001). Premium on prepaid loans collected during 2002 amounted to \$62,521,000 (\$2,841,000 – 2001).

Total income from investments for the year ended 31 December 2002 was \$330,448,000 (\$403,436,000 – 2001). 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 4.26% (5.91% – 2001). If unrealized gains and losses were included, the annualized rate of return would have been 5.34% (6.18% – 2001).

Income from other sources primarily includes dividends received for the year ended 31 December 2002 amounted to \$8,603,000 (\$13,229,000 – 2001), gain on sale of equity investments of \$7,078,000 (loss of \$345,000 – 2001), net of the share in the net losses of an equity investment of \$363,000 (share in net profit of \$1,478,000 – 2001) accounted for on the equity method.

Total interest expense incurred for the year ended 31 December 2002 amounted to \$1,138,660,000 (\$1,416,830,000 – 2001). Other financial expenses consist of amortization of borrowings' issuance costs and other expenses of \$16,507,000 (\$17,282,000 – 2001).

Administrative expenses (other than those pertaining directly to ordinary operations and special operations) for the year ended 31 December 2002 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 \$254,372,000 (\$223,313,000 – 2001), \$144,379,000 (\$129,481,000 – 2001) was accordingly charged to the Asian Development Fund. The balance of administrative expenses after allocation was reduced by the deferral of direct loan origination costs of \$19,440,000 (\$34,793,000 – 2001) related

to new loans for the year ended 31 December 2002 (see Notes B and E).

In April 2001, the Board of Directors approved financing of technical assistance (TA) directly from current income and outlined a 4-year financing framework for TA operations. The full amount of TA commitments is to be charged to OCR current income as "TECHNICAL ASSISTANCE TO MEMBER COUNTRIES" in the year of commitment. As at 31 December 2002, the amount of TA commitments amounted to \$75,960,000 (\$19,962,000 – 2001) out of which \$11,115,000 (\$209,000 – 2001) had been disbursed.

For the year ended 31 December 2002, the provision for losses totaled \$4,476,000 (\$3,909,000 for private sector loans and \$567,000 for equity investments). For the year ended 31 December 2001, the provision for losses totaled \$9,838,000 (\$4,994,000 for private sector loans and \$4,844,000 for equity investments).

FAS 133 adjustment of \$224,756,000 (\$112,845,000 – 2001) was made up of mark to market gains on derivatives of \$242,051,000 (\$153,560,000 – 2001) offset by amortization of the FAS 133 transition adjustments of \$17,295,000 (\$40,715,000 – 2001).

NOTE L—OTHER ASSETS AND LIABILITIES— MISCELLANEOUS

Included in miscellaneous assets and liabilities are as follows:

	<u>2002</u>	<u>2001</u>
Amounts Receivable from: Asian Development Fund (Note K)	\$20,474,000	\$6,103,000
Technical Assistance Special Fund	60,000	–
Japan Special Fund	230,000	143,000
Asian Development Bank Institute Special Fund	<u>72,000</u>	<u>107,000</u>
Total	<u>\$20,836,000</u>	<u>\$6,353,000</u>
Amounts Payable to: Staff Retirement Plan	<u>\$12,150,000</u>	<u>\$4,166,000</u>

NOTE M—STAFF RETIREMENT PLAN AND POSTRETIREMENT MEDICAL BENEFITS

Staff Retirement Plan

ADB 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

CONTINUED

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 ADB, 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 salary to the Plan and may also make additional voluntary contributions. ADB'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, ADB adopted a cost-sharing plan for retirees' medical insurance premiums. Under the plan, ADB is obligated to pay 75% 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 medical benefits at 31 December 2002 and 2001:

	Pension Benefits		Postretirement Medical Benefits	
	2002	2001	2002	2001
Change in benefit obligation:				
Benefit obligation at beginning of year	\$ 714,365,000	\$576,014,000	\$ 105,789,000	\$ 61,231,000
Service cost	25,121,000	19,014,000	4,884,000	4,252,000
Interest cost	51,157,000	44,165,000	7,680,000	6,964,000
Participants' contributions	39,752,000	29,898,000	-	-
Amendments	-	40,392,000	-	-
Actuarial loss (gain)	36,507,000	32,295,000	6,733,000	34,460,000
Benefits paid	(33,355,000)	(27,413,000)	(1,087,000)	(1,118,000)
Benefit obligation at end of year	<u>\$ 833,547,000</u>	<u>\$714,365,000</u>	<u>\$ 123,999,000</u>	<u>\$ 105,789,000</u>
Change in plan assets:				
Fair value of plan assets at beginning of year	\$ 692,875,000	\$729,822,000	\$ -	\$ -
Actual return on plan assets	(62,054,000)	(49,607,000)	-	-
Employer's contribution	10,826,000	10,175,000	1,087,000	1,118,000
Plan participants' contributions	39,752,000	29,898,000	-	-
Benefits paid	(33,355,000)	(27,413,000)	(1,087,000)	(1,118,000)
Fair value of plan assets at end of year	<u>\$ 648,044,000</u>	<u>\$692,875,000</u>	<u>\$ -</u>	<u>\$ -</u>
Funded status	<u>\$(185,503,000)</u>	<u>\$(21,490,000)</u>	<u>\$(123,999,000)</u>	<u>\$(105,789,000)</u>
Unrecognized actuarial loss	166,234,000	2,605,000	36,731,000	32,190,000
Unrecognized prior service cost	37,118,000	42,185,000	(3,312,000)	(3,697,000)
Unrecognized transition obligation	(1,112,000)	(2,217,000)	5,297,000	7,706,000
Net amount recognized	<u>\$ 16,737,000</u>	<u>\$ 21,083,000</u>	<u>\$ (85,283,000)</u>	<u>\$ (69,590,000)</u>
Amounts recognized in the balance sheet consist of:				
Prepaid benefit cost	17,124,000	21,409,000	-	-
Accrued benefit liability	(403,000)	(326,000)	(85,283,000)	(69,590,000)
Intangible asset	-	-	N/A	N/A
Accumulated other comprehensive income	16,000	-	N/A	N/A
Net amount recognized	<u>\$ 16,737,000</u>	<u>\$ 21,083,000</u>	<u>\$ (85,283,000)</u>	<u>\$ (69,590,000)</u>
Weighted-average assumptions as of 31 December				
Discount rate	6.75%	7.00%	6.75%	7.00%
Expected return on plan assets	8.00%	8.00%	N/A	N/A
Rate of compensation increase varies with age and averages	5.75%	6.00%	5.75%	6.00%

ASIAN DEVELOPMENT BANK—ORDINARY CAPITAL RESOURCES

NOTES TO FINANCIAL STATEMENTS

31 December 2002 and 2001

For measurement purposes, a 7.75% annual rate of increase in the per capita cost of covered health care benefits was assumed for the valuation as at 31 December 2002. The

rate was assumed to decrease gradually to 5.75% for 2009 and remain at that level thereafter.

	Pension Benefits		Postretirement Medical Benefits	
	2002	2001	2002	2001
Components of net periodic benefit cost:				
Service cost	\$ 25,121,000	\$ 19,014,000	\$ 4,884,000	\$ 4,252,000
Interest cost	51,157,000	44,165,000	7,680,000	6,964,000
Expected return on plan assets	(63,001,000)	(58,746,000)	-	-
Amortization of prior service cost	5,067,000	982,000	(385,000)	(385,000)
Amortization of transition obligation	(1,105,000)	(1,105,000)	2,409,000	2,409,000
Recognized actuarial (gain) loss	(2,067,000)	(8,349,000)	2,192,000	1,998,000
Net periodic benefit cost	<u>\$ 15,172,000</u>	<u>\$ (4,039,000)</u>	<u>\$ 16,780,000</u>	<u>\$ 15,238,000</u>

A one-percentage-point change in assumed health care trend rates would have the following effects:

	1- Percentage-Point Increase	1- Percentage-Point Decrease
Effect on total service and interest cost components	\$ 3,007,000	\$ (2,310,000)
Effect on postretirement benefit obligation	24,405,000	(19,298,000)

NOTE N—FAIR VALUE OF FINANCIAL INSTRUMENTS

The carrying amounts and estimated fair values of ADB's significant financial instruments as of 31 December 2002 and 2001 are summarized as follows:

	2002		2001	
	Carrying Amount ^a	Estimated Fair Value	Carrying Amount ^a	Estimated Fair Value
On-balance sheet financial instruments:				
ASSETS:				
Due from banks	\$ 473,360,000	\$ 473,360,000	\$ 68,823,000	\$ 68,823,000
Investments (Note D)	9,028,741,000	9,028,741,000	8,264,915,000	8,264,915,000
Loans outstanding (Note E)	29,145,236,000	31,922,103,000	28,658,846,000	30,697,150,000
Equity investments (Note F)	211,267,000	211,267,000	208,018,000	208,018,000
Other assets				
Nonnegotiable, noninterest-bearing demand obligations	313,416,000	178,361,000	333,047,000	185,090,000
Receivable from swaps - investments (Note D)	511,937,000	511,937,000	-	-
Receivable from swaps - borrowings (Note H)	9,231,868,000	9,231,868,000	6,379,403,000	6,379,403,000
LIABILITIES:				
Borrowings (Note H)	26,236,013,000	28,645,177,000	25,252,189,000	26,734,750,000
Other liabilities				
Payable for swaps - investments (Note D)	548,218,000	548,218,000	-	-
Payable for swaps - borrowings (Note H)	9,027,166,000	9,027,166,000	6,784,076,000	6,784,076,000
	Outstanding Amount	Present Value	Outstanding Amount	Present Value
Off-balance sheet financial instruments:				
Guarantees (Note E)	1,117,810,000	553,152,000	355,173,000	230,932,000

^a The carrying amount for borrowings and swaps are inclusive of accrued interest.

CONTINUED

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 amount.

If available, quoted market values are used to determine fair values. Financial instruments for which market quotations are not readily available are valued using a market-based valuation model. The basis of valuation is the expected cash flows discounted at the applicable market yield curves or appropriate market data.

NOTE O—OFF-BALANCE SHEET CREDIT RISK

ADB is a party to off-balance sheet financial instruments on guarantees. Guarantees involve elements of credit risk which are not reflected on the balance sheet. Credit risk represents the maximum potential accounting loss due to possible non-performance by obligors and counterparties under the terms of the contract. The amount of credit risks on guarantees as at 31 December 2002 was \$1,117,810,000 (\$355,173,000 – 31 December 2001).

NOTE P—SPECIAL AND TRUST FUNDS

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

In addition, ADB, alone or jointly with donors, administers on behalf of the donors, including members of ADB, their agencies and other development institutions, projects/programs supplementing ADB's operations. Such projects/programs are funded with external funds administered by ADB and with external funds not under ADB's administration. The funds are restricted for specific uses including technical assistance to borrowers and technical assistance for regional programs. The responsibilities of ADB 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 ADB 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 2002 and 2001 is as follows:

	2002		2001	
	Total Net Assets	No. of Funds	Total Net Assets	No. of Funds
Special Funds				
Asian Development Fund	\$22,852,571,000	1	\$19,887,498,000	1
Technical Assistance Special Fund	68,338,000	1	81,271,000	1
Japan Special Fund	188,167,000	1	268,129,000	1
Asian Development Bank Institute Special Fund	10,397,000	1	9,857,000	1
Subtotal	23,119,473,000	4	20,246,755,000	4
Trust Funds				
Funds administered by ADB	463,977,000	32	219,626,000	30
Funds not administered by ADB	5,455,000	1	6,900,000	1
Subtotal	469,432,000	33	226,526,000	31
Total	\$23,588,905,000	37	\$20,473,281,000	35

During the year ended 31 December 2002, a total of \$638,000 (\$411,000 – 2001) was received as compensation for

administering projects/programs under Trust Funds. The amount has been included in "Income from other sources."

REPORT OF INDEPENDENT AUDITORS

Asian Development Bank

We have audited the accompanying special purpose statement of assets, liabilities and fund balances of the Asian Development Bank—Asian Development Fund as of 31 December 2002 and 2001 and the related special purpose statements of revenues and expenses, cash flows and changes in fund balances for the years then ended. These financial statements are the responsibility of the management of the Asian Development Bank. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with auditing standards generally accepted in the United States of America. 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 disclosure in the financial statements, assessing the accounting principles used and significant estimates made by management, and evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

As discussed in Notes B and D, the Board of Directors approved in May 2001 the adoption of special purpose financial statements for the Asian Development Bank—Asian Development Fund in 2001. With the adoption of the special purpose financial statements, loan loss provisioning has been eliminated. The accompanying financial statements are not intended to be a presentation in conformity with accounting principles generally accepted in the United States of America.

In our opinion, the special purpose financial statements referred to above present fairly, in all material respects, the assets, liabilities and fund balances of Asian Development Bank—Asian Development Fund at 31 December 2002 and 2001, and the revenues and expenses and cash flows for the years then ended, on the basis of accounting explained in Notes B and D.

Our audits were conducted for the purpose of forming an opinion on the special purpose financial statements taken as a whole. The accompanying special purpose statements of loans as at 31 December 2002 and 2001, and of resources as at 31 December 2002 are presented for purposes of additional analyses and are not required parts of the special purpose financial statements. Such information has been subjected to the auditing procedures applied in the audits of the special purpose financial statements and in our opinion is fairly stated in all material respects in relation to the special purpose financial statements taken as a whole.

This report is intended solely for the information and use of the Board of Governors, Board of Directors, management and members of the Asian Development Bank—Asian Development Fund. However, under the Agreement Establishing the Asian Development Fund, this report is included in the Annual Report of the Asian Development Bank and is therefore a matter of public record and its distribution is not limited.

PriceWaterhouseCoopers LLP

Detroit, Michigan
10 March 2003

ASIAN DEVELOPMENT BANK—ASIAN DEVELOPMENT FUND

SPECIAL PURPOSE STATEMENT OF ASSETS, LIABILITIES, AND FUND BALANCES

31 December 2002 and 2001

Expressed in Thousands of United States Dollars (Note B)

ASSETS	2002		2001	
DUE FROM BANKS (Note B)	\$	10,205	\$	6,293
INVESTMENTS (Notes B and C)				
Government and government-guaranteed obligations	\$	1,158,631	\$	932,477
Time deposits		727,676		386,344
Corporate bonds		1,276,190		1,197,736
Securities transferred under securities lending arrangement		112,293	3,274,790	69,569
				2,586,126
LOANS OUTSTANDING (ADF-5) (Notes B and D)		17,232,780		14,832,323
ACCRUED REVENUE				
On investments		37,675		28,508
On loans		40,478		36,066
		78,153		64,574
DUE FROM CONTRIBUTORS (Notes B and E)		2,465,316		2,476,215
OTHER ASSETS				
Investment related receivables		56,007		160
Others		3,056	59,063	2,803
				2,963
TOTAL		\$23,120,307		\$19,968,494
LIABILITIES AND FUND BALANCES				
PAYABLE TO ORDINARY CAPITAL RESOURCES	\$	20,474	\$	6,103
ADVANCE PAYMENTS ON CONTRIBUTIONS (ADF-6)		16,472		2,651
OTHER LIABILITIES				
Investment related payables	\$	170,009	\$	70,842
Others (ADF-6)		60,781	230,790	1,400
				72,242
FUND BALANCES				
Amounts available for loan commitments (ADF-6)				
Contributed Resources (Note B)		20,790,249		18,180,486
Set-Aside Resources (Note G)		64,491		59,780
Transfers from Ordinary Capital Resources and Technical Assistance Special Fund (Note A)		232,951		232,553
		21,087,691		18,472,819
Accumulated surplus (ADF-4)		1,755,189		1,608,532
Accumulated other comprehensive income (ADF-4) (Notes B and H)		9,691	22,852,571	(193,853)
				19,887,498
TOTAL		\$23,120,307		\$19,968,494

The accompanying notes are an integral part of these special purpose financial statements (ADF-7).

ASIAN DEVELOPMENT BANK—ASIAN DEVELOPMENT FUND

SPECIAL PURPOSE STATEMENT OF REVENUE AND EXPENSES

For the Years Ended 31 December 2002 and 2001

Expressed in Thousands of United States Dollars (Note B)

	2002		2001	
REVENUE				
From loans (Notes B and D)		\$156,370		\$146,763
From investments (Notes B and C)				
Interest	\$125,772		\$120,018	
Net gain on sales	8,768	134,540	1,015	121,033
From other sources—net		<u>152</u>	<u>260</u>	\$ 268,056
		\$ 291,062		
EXPENSES				
Administrative expenses (Note F)		<u>144,405</u>		<u>129,517</u>
EXCESS OF REVENUE OVER EXPENSES		\$146,657		\$138,539

The accompanying notes are an integral part of these special purpose financial statements (ADF-7).

ASIAN DEVELOPMENT BANK—ASIAN DEVELOPMENT FUND

SPECIAL PURPOSE STATEMENT OF CASH FLOWS
For the Years Ended 31 December 2002 and 2001

Expressed in Thousands of United States Dollars (Note B)

	2002	2001
CASH FLOWS FROM OPERATING ACTIVITIES		
Interest charges on loans received	\$ 136,842	\$ 126,324
Interest on investments received	132,439	116,773
Cash received from other sources	152	121
Administrative expenses paid	(130,983)	(131,456)
Net Cash Provided by Operating Activities	\$ 138,450	\$ 111,762
CASH FLOWS FROM INVESTING ACTIVITIES		
Sales of investment	447,477	362,994
Maturities of investment	55,394,621	49,239,054
Purchases of investment	(56,183,290)	(49,935,316)
Principal collected on loans	262,261	219,334
Loans disbursed	(1,115,613)	(1,005,975)
Net Cash Used in Investing Activities	\$ (1,194,544)	\$ (1,119,909)
CASH FLOWS FROM FINANCING ACTIVITIES		
Contributions received and encashed ¹	1,057,054	1,006,117
Net Cash Provided by Financing Activities	\$ 1,057,054	\$ 1,006,117
Effect of Exchange Rate Changes on Due from Banks	2,952	732
Net Increase (Decrease) in Due from Banks	3,912	(1,298)
Due from Banks at Beginning of Period	6,293	7,591
Due from Banks at End of Period	\$ 10,205	\$ 6,293
RECONCILIATION OF EXCESS OF REVENUE OVER EXPENSES TO NET CASH PROVIDED BY OPERATING ACTIVITIES:		
Excess of revenue over expenses (ADF-2)	\$ 146,657	\$ 138,539
Adjustments to reconcile excess of revenue over expenses to net cash provided by operating activities:		
Capitalized charges on loans	(18,683)	(20,162)
Amortization of discounts/premiums	15,834	(2,564)
Change in accrued/prepaid administrative expenses	13,422	(1,939)
Change in accrued revenue on investments and loans	(10,012)	(958)
Net gain on sales of securities	(8,768)	(1,015)
Changes in receivables/payables	-	(139)
Net Cash Provided by Operating Activities	\$ 138,450	\$ 111,762

¹ In addition, nonnegotiable, noninterest-bearing demand promissory notes amounting to \$763,484 (\$558,674 – 2001) were received from contributing members.

The accompanying notes are an integral part of these special purpose financial statements (ADF-7).

ASIAN DEVELOPMENT BANK—ASIAN DEVELOPMENT FUND

SPECIAL PURPOSE STATEMENT OF CHANGES IN FUND BALANCES

For the Years Ended 31 December 2002 and 2001

Expressed in Thousands of United States Dollars (Note B)

	Contributed Resources	Set-Aside Resources	Transfers from OCR & TASF	Accumulated Surplus	Accumulated Other Comprehensive Income	Total
Balance—						
1 January 2001	\$19,319,810	\$62,031	\$232,670	\$1,469,993	\$ (85,276)	\$20,999,228
Comprehensive income for the year 2001 (Note H)				138,539	(108,577)	29,962
Change in amount of contributed resources available for loan commitments	(1,139,324)					(1,139,324)
Change in SDR value of set-aside resources		(2,251)				(2,251)
Change in value of transfers from Technical Assistance Special Fund			(117)			(117)
Balance—						
31 December 2001	\$18,180,486	\$59,780	\$232,553	\$1,608,532	\$(193,853)	\$19,887,498
Comprehensive income for the year 2002 (Note H)				146,657	203,544	350,201
Change in amount of contributed resources available for loan commitments	2,609,763					2,609,763
Change in SDR value of set-aside resources		4,711				4,711
Change in value of transfers from Technical Assistance Special Fund			398			398
Balance—						
31 December 2002	\$20,790,249	\$64,491	\$232,951	\$1,755,189	\$ 9,691	\$22,852,571

Accumulated Other Comprehensive Income (Note H)

For the Years Ended 31 December 2002 and 2001

Expressed in Thousands of United States Dollars (Note B)

	Accumulated Translation Adjustments		Unrealized Investment Holding Gains		Accumulated Other Comprehensive Income	
	2002	2001	2002	2001	2002	2001
Balance, 1 January	\$(208,980)	\$ (87,242)	\$ 15,127	\$ 1,966	\$(193,853)	\$ (85,276)
Other comprehensive income for the year	198,551	(121,738)	4,993	13,161	203,544	(108,577)
Balance, 31 December	\$ (10,429)	\$(208,980)	\$20,120	\$15,127	\$ 9,691	\$(193,853)

The accompanying notes are an integral part of these special purpose financial statements (ADF-7).

ASIAN DEVELOPMENT BANK—ASIAN DEVELOPMENT FUND

SPECIAL PURPOSE SUMMARY STATEMENT OF LOANS

31 December 2002 and 2001

Expressed in Thousands of United States Dollars (Note B)

Borrower/Guarantor ¹	Loans Outstanding	Undisbursed Balances of Effective Loans ²	Loans Not Yet Effective ²	Total Loans	Percent of Total Loans
Afghanistan	\$ 116,050	\$ 51,246	\$ –	\$ 167,296	0.70
Bangladesh	4,406,296	776,008	276,317	5,458,621	22.97
Bhutan	70,074	20,213	–	90,287	0.38
Cambodia	325,036	199,405	119,544	643,985	2.71
Cook Islands	20,873	2,110	–	22,983	0.10
Indonesia	660,045	330,162	134,158	1,124,365	4.73
Kazakhstan	49,971	5,065	–	55,036	0.23
Kiribati	6,256	6,404	–	12,660	0.05
Kyrgyz Republic	341,822	163,735	–	505,557	2.13
Lao PDR	666,736	217,003	89,110	972,849	4.09
Maldives	40,861	28,283	5,122	74,266	0.31
Marshall Islands	52,818	8,722	7,185	68,725	0.29
Micronesia, Fed. States of	30,741	1,155	22,193	54,089	0.23
Mongolia	362,697	150,120	–	512,817	2.16
Myanmar	452,131	–	–	452,131	1.90
Nepal	1,154,890	332,664	109,816	1,597,370	6.72
Pakistan	4,201,579	920,626	320,957	5,443,162	22.91
Papua New Guinea	260,842	53,557	5,803	320,202	1.35
Philippines	854,774	56,613	–	911,387	3.84
Samoa	73,675	15,681	–	89,356	0.38
Solomon Islands	46,006	10,760	–	56,766	0.24
Sri Lanka	1,704,922	650,624	92,344	2,447,890	10.30
Tajikistan	39,021	80,344	56,371	175,736	0.74
Thailand	52,717	–	–	52,717	0.22
Tonga	39,773	5,636	–	45,409	0.19
Tuvalu	3,972	–	1,888	5,860	0.02
Uzbekistan	13,309	6,066	–	19,375	0.08
Vanuatu	48,248	12	–	48,260	0.20
Viet Nam	1,136,645	960,142	237,956	2,334,743	9.83
BALANCE – 31 December 2002	\$17,232,780	\$5,052,356	\$1,478,764	\$23,763,900	100.00
BALANCE – 31 December 2001	\$14,832,323	\$4,362,802	\$1,376,618	\$20,571,743	

¹ Loans other than those made directly to a member or to its central bank have been guaranteed by the member with the exception of loans to the private sector amounting to \$5,502 (\$8,836 – 2001).

² Loans negotiated before 1 January 1983 were denominated in current United States dollars. Loans negotiated after that date are denominated in Special Drawing Rights (SDR) for the purpose of commitment. The undisbursed portions of such SDR loans are translated into United States dollars at the applicable exchange rates as of the end of a reporting period. Of the undisbursed balances, ADB has entered into irrevocable commitments to disburse various amounts totaling \$49,706 (\$90,393 – 2001).

The accompanying notes are an integral part of these special purpose financial statements (ADF-7).

MATURITY OF EFFECTIVE LOANS

<u>Twelve Months</u> <u>Ending 31 December</u>	<u>Amount</u>	<u>Five Years</u> <u>Ending 31 December</u>	<u>Amount</u>
2003	\$454,909	2012	3,841,931
2004	399,341	2017	4,599,639
2005	432,187	2022	4,696,122
2006	472,362	2027	3,646,090
2007	521,467	2032	2,347,742
		2037	815,637
		2042	<u>57,709</u>
		Total	<u>\$22,285,136</u>

SUMMARY OF CURRENCIES RECEIVABLE ON LOANS OUTSTANDING

<u>Currency</u>	<u>2002</u>	<u>2001</u>	<u>Currency</u>	<u>2002</u>	<u>2001</u>
Australian dollar	\$ 335,615	\$ 350,116	New Zealand dollar	17,785	17,340
Canadian dollar	773,930	771,606	Norwegian krone	30,689	30,386
Danish krone	75,045	68,359	Pound sterling	220,161	227,914
Euro	2,619,263	2,271,650	Singapore dollar	447	-
Japanese yen	10,206,797	8,768,144	Swedish krona	95,082	88,962
Korean won	27,584	14,034	Swiss franc	258,485	189,745
Malaysian ringgit	3,363	-	Thai baht	1,283	-
			United States dollar	<u>2,567,251</u>	<u>2,034,067</u>
			Total	<u>\$17,232,780</u>	<u>\$14,832,323</u>

ASIAN DEVELOPMENT BANK—ASIAN DEVELOPMENT FUND

SPECIAL PURPOSE STATEMENT OF RESOURCES

31 December 2002

Expressed in Thousands of United States Dollars (Note B)

	Effective Amounts Committed During 2002	Effective Amounts Committed		Amounts Not Yet Available For Loan Commitments	Amounts Available For Loan Commitments	Amounts Received	Amounts Receivable
		At Exchange Rates Per Resolutions	At 31 Dec 2002 Exchange Rates				
CONTRIBUTED RESOURCES							
Australia	\$ -	\$ 1,324,951	\$ 922,727	\$ 82,412	\$ 840,315	\$ 840,315	\$ -
Austria	-	169,562	178,491	14,267	164,224	164,224	-
Belgium	21,310	159,126	155,526	10,655	144,871	144,871	-
Canada	-	1,413,316	1,124,824	61,804	1,063,020	1,063,020	-
Denmark	26,372	179,656	172,906	13,178	159,728	159,728	-
Finland	14,798	114,676	95,387	7,399	87,988	87,988	-
France	-	957,755	894,089	73,753	820,336	820,336	-
Germany	171,035	1,297,647	1,369,090	96,022	1,273,068	1,273,068	-
Hong Kong, China	-	36,550	36,550	8,140	28,410	28,410	-
Indonesia	-	14,960	14,960	-	14,960	14,960	-
Italy	-	707,302	483,231	-	483,231	483,231	-
Japan	-	7,502,667	11,017,233	473,891	10,543,342	10,543,342	-
Korea, Rep. of	-	158,580	137,574	39,459	98,115	98,115	-
Malaysia	-	10,000	6,708	506	6,202	6,202	-
Nauru	-	1,933	1,933	-	1,933	1,433	500
The Netherlands	-	496,350	516,722	42,916	473,806	473,806	-
New Zealand	-	90,472	73,482	10,440	63,042	63,042	-
Norway	-	165,600	154,586	15,719	138,867	138,867	-
Portugal	53,640	47,142	53,640	8,879	44,761	44,761	-
Singapore	-	4,000	3,888	1,944	1,944	1,944	-
Spain ¹	29,628	132,540	113,413	14,799	98,614	98,614	-
Sweden	-	288,985	209,895	18,941	190,954	190,954	-
Switzerland	-	250,051	304,145	20,081	284,064	284,064	-
Taipei, China	-	46,508	42,882	6,933	35,949	35,949	-
Thailand	2,335	6,642	4,671	1,168	3,503	3,503	-
Turkey	-	105,386	105,386	2,500	102,886	102,886	-
United Kingdom	-	862,613	795,281	67,935	727,346	727,346	-
United States	-	2,924,928	2,924,928	30,158	2,894,770	2,894,770	-
Total	319,118	19,469,898	21,914,148	1,123,899	20,790,249	20,789,749²	500
SET-ASIDE RESOURCES							
(Note G)	-	-	64,491	-	64,491	-	-
TRANSFER FROM							
ORDINARY CAPITAL RESOURCES	-	-	230,000	-	230,000	-	-
TRANSFERS FROM							
TECHNICAL ASSISTANCE SPECIAL FUND ³	-	-	2,951	-	2,951	-	-
TOTAL	\$319,118	\$19,469,898	\$22,211,590	\$1,123,899	\$21,087,691	\$20,789,749	\$500

¹ Excludes \$59,424 equivalent of additional contribution which was not yet made effective as of 31 December 2002 pending receipt of instrument of contribution.

² Excludes \$16,472 equivalent representing advance payments received but not yet available for loan commitments as of 31 December 2002.

³ Includes translation adjustments amounting to \$520 as of 31 December 2002.

The accompanying notes are an integral part of these special purpose financial statements (ADF-7).

ASIAN DEVELOPMENT BANK—ASIAN DEVELOPMENT FUND

NOTES TO SPECIAL PURPOSE FINANCIAL STATEMENTS

31 December 2002 and 2001

NOTE A—NATURE OF OPERATIONS

The Asian Development Fund (ADF) was established on 28 June 1974 to more effectively carry out the special operations of the Asian Development Bank (ADB) by providing resources on concessional terms which are made available almost exclusively to the least developed borrowing countries.

The resources of ADF have been subsequently augmented by seven replenishments, the most recent of which became effective in June 2001 in a total amount equivalent to \$2,791,483,000 to cover the operational requirements for the four-year period from January 2001. The last allocation from the surplus account of ADB's ordinary capital resources to ADF in the amount of \$230,000,000 was in 1997.

NOTE B—SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

In May 2001, the Board of Directors approved the adoption of the special purpose financial statements for ADF. With the adoption of the special purpose financial statements, loan loss provisioning has been eliminated.

Due to the nature and organization of ADF, these financial statements have been prepared for the specific purpose of reflecting the sources and applications of member subscriptions and are not intended to be a presentation in accordance with generally accepted accounting principles. These special purpose financial statements have been prepared to comply with Article IV, Section 4.01 of the Regulations of ADF.

Functional Currencies and Reporting Currency

The currencies of contributing member countries are functional currencies. The reporting currency is the United States dollar, and the special purpose financial statements are expressed in thousands of current United States dollars.

Translation of Currencies

Assets, liabilities, amounts available for loan commitments and advance payments on contributions are translated from their functional currencies to the reporting currency, generally at the applicable rates of exchange at the end of a reporting period. Revenue and expense amounts are translated for each semimonthly 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 relating to set-aside resources (see Note G) are recorded as notional amounts receivable from or payable to ordinary capital resources. Other

translation adjustments are charged or credited to "Accumulated translation adjustments" and reported in "FUND BALANCES" as part of "Accumulated other comprehensive income." Exchange gains or losses on currency transactions among functional currencies are included in revenue.

Investments

All investment securities and negotiable certificate of deposits held by ADF are considered by Management to be "Available for Sale" and are reported at estimated fair value, with unrealized gains and losses excluded from revenue and reported in "FUND BALANCES" as part of "Accumulated other comprehensive income." Estimated fair value generally represents market value. Time deposits are classified as "Held-to-Maturity" and are reported at cost. Realized gains and losses are included in revenue from investments and are measured by the difference between amortized cost and the net proceeds of sales.

Securities Transferred Under Securities Lending Arrangement

ADB accounts for transfers of financial assets in accordance with FAS 140, "Accounting for Transfers and Servicing of Financial Assets and Extinguishments of Liabilities—a replacement of FAS 125." In general, transfers are accounted for as sales under FAS 140 when ADB has relinquished control over the transferred assets. Transfers that are not accounted for as sales are accounted for as repurchase agreements and collateralized financing arrangements.

Loans

It is the policy of ADF to place in nonaccrual status loans made to eligible borrowing member countries if the principal or interest with respect to any such loans is overdue by six months. Interest on nonaccruing loans is included in revenue only to the extent that payments have actually been received by ADF. ADB follows a policy of not taking part in debt rescheduling agreements with respect to public sector loans. In the case of private sector loans, ADB may agree to debt rescheduling only after alternative courses of action have been exhausted. When ADB decides that a particular loan is no longer collectible, the entire amount will be expensed during the period.

Contributed Resources

Contributions by member countries are included in the financial statements as amounts committed from the date

ASIAN DEVELOPMENT BANK—ASIAN DEVELOPMENT FUND

NOTES TO SPECIAL PURPOSE FINANCIAL STATEMENTS

31 December 2002 and 2001

Instruments of Contribution are deposited and related formalities are completed.

Contributions are generally paid or to be paid in the currency of the contributor either in cash or notes.

Accounting Estimates

The preparation of special purpose financial statements 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.

Special Purpose Statement of Cash Flows

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

Reclassification and Restatement

Certain 2001 amounts have been restated to conform with the 2002 presentation.

NOTE C—INVESTMENTS

The main investment management objective is to maintain security and liquidity. Subject to these parameters, ADB seeks the highest possible return on its investments. Investments are governed by the Investment Authority approved by the Board of Directors in 1999. ADB is restricted by its Investment Authority to invest in investment instruments which are obligations of a limited class of issuers, primarily government or government-guaranteed obligations and corporate obligations.

The currency compositions of the investment portfolio as of 31 December 2002 and 2001 expressed in United States dollars are as follows:

Currency	2002	2001
Australian dollar	\$ 582,983,000	\$ 355,074,000
Canadian dollar	320,404,000	240,118,000
Danish krone	80,490,000	50,268,000
Euro	1,057,178,000	555,904,000
Japanese yen	56,025,000	53,693,000
Norwegian krone	141,777,000	87,934,000
Pound sterling	606,242,000	450,718,000
Swedish krone	75,990,000	38,403,000
United States dollar	309,416,000	710,052,000
Others	44,285,000	43,962,000
Total	<u>\$3,274,790,000</u>	<u>\$2,586,126,000</u>

The estimated fair value and amortized cost of the investments by contractual maturity at 31 December 2002 are as follows:

	Estimated Fair Value	Amortized Cost
Due in one year or less	\$1,820,903,000	\$1,816,509,000
Due after one year through five years	<u>1,453,887,000</u>	<u>1,438,161,000</u>
Total	<u>\$3,274,790,000</u>	<u>\$3,254,670,000</u>

Time deposits at cost approximates its fair value. Additional information relating to investments in government and government-guaranteed obligations and corporate bonds is as follows:

	2002	2001
As of 31 December		
Amortized cost	\$2,526,994,000	\$2,184,655,000
Estimated fair value	2,547,114,000	2,199,782,000
Gross unrealized gains	20,232,000	15,156,000
Gross unrealized losses	112,000	29,000
For the years ended 31 December		
Change in net unrealized gains	4,993,000	13,161,000
Proceeds from sales	447,477,000	362,994,000
Gross gains	8,824,000	1,019,000
Gross losses	56,000	4,000

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 4.50% (4.84% – 2001). If unrealized gains and losses were included, the annualized rate of return would have been 4.65% (5.35% – 2001).

NOTE D—LOANS AND LOAN LOSS PROVISION

Loans

Prior to 1 January 1999, loans of ADF were extended to eligible borrowing member countries, which bore a service charge of 1% and required repayment over periods ranging from 35 to 40 years. On 14 December 1998, the Board of Directors approved an amendment to ADF loan terms, as follows: (i) for loans to finance specific projects, the maturity was shortened to 32 years including an 8-year grace period; (ii) for program loans to support sector development, the

CONTINUED

maturity was shortened to 24 years including an 8-year grace period; and (iii) all new loans bear a 1% interest charge during the grace period, and 1.5% during the amortization period, with equal amortization. The new ADF lending terms took effect on 1 January 1999 and apply only to new loans for which formal loan negotiations were completed on or after 1 January 1999. ADF requires borrowers to absorb exchange risks attributable to fluctuations in the value of the currencies disbursed.

ADB believes that there is no comparable market, nor ADB intends to sell its loans. The use of market data to arrive at the loan at fair value will give meaningless results. As such, the fair value of loans is determined using an entry value method. Under this method, fair value is determined based on the terms at which a similar loan would currently be made by ADB to a similar borrower. For such loans, fair value approximates the carrying amount. The estimated fair value of loans is not affected by credit risks because the amount of any such adjustment is not considered to have a material effect based on ADB's experience with its borrowers.

Undisbursed loan commitments and an analysis of loans by country as of 31 December 2002 are shown in ADF-5.

The principal amount outstanding of public sector loans in nonaccrual status as of 31 December 2002 was \$498,137,000 (\$442,146,000 – 2001) of which \$80,420,000 (\$69,994,000 – 2001) was overdue. Loans in nonaccrual status resulted in \$5,009,000 (\$4,712,000 – 2001) not being recognized as income from loans for the year ended 31 December 2002. The accumulated interest on these loans that was not recognized as income as of 31 December 2002 would have totaled \$24,361,000 (\$22,882,000 – 2001). The loans in nonaccrual status as of 31 December 2002 were 28 loans made to Myanmar and 14 loans to Solomon Islands. (Four loans to Afghanistan and 28 loans to Myanmar – 2001).

No private sector loan was in nonaccrual status as of 31 December 2002 (one for \$5,234,000 – 2001).

Private sector loans outstanding as of 31 December 2002 were \$5,502,000 (\$8,836,000 – 2001), and there were no undisbursed loan commitments (nil – 2001).

NOTE E—NOTES OF CONTRIBUTORS

Notes of contributors are nonnegotiable, noninterest-bearing and, subject to certain restrictions imposed by applicable Board of Governors' resolutions, encashable by ADB at par upon demand.

ADB currently expects that the notes outstanding at 31 December 2002 will be encashed in varying amounts over a nine-year period ending 31 December 2011.

The fair value of notes of contributors is determined using an entry value method, whereby fair value is determined based on the terms at which notes are currently being accepted from contributors. On this basis, the fair value of outstanding notes of contributors approximates their carrying amount.

NOTE F—ADMINISTRATIVE EXPENSES AND ADMINISTRATION CHARGE

Administrative expenses for 2002 included an administration charge from ordinary capital resources amounting to \$144,379,000 (\$129,481,000 – 2001). The charge represents an apportionment of all administrative expenses of ADB (other than those pertaining directly to ordinary operations and special operations), based on the number of loans and equity investments approved during the year.

NOTE G—SET-ASIDE RESOURCES

Pursuant to the provisions of Article 19, paragraph 1(i) of the Articles of Agreement Establishing the Asian Development Bank (the Charter), the Board of Governors has authorized the setting aside of 10% of the unimpaired "paid-in" capital paid by member countries pursuant to Article 6, paragraph 2(a) of the Charter and of the convertible currency portion paid by member countries 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 ADB. The capital so set aside was allocated and transferred from the ordinary capital resources to ADF as Set-Aside Resources.

The capital stock of ADB 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). Therefore, Set-Aside Resources had historically been translated into the current United States dollar (ADB'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 had par values in terms of gold. Pending ADB's selection of the appropriate successor to the 1966 dollar, the Set-Aside Resources have been valued for purposes of the accompanying financial statements in terms of the Special Drawing Right (SDR), at the value in current United States dollars as computed by the IMF. As of 31 December 2002, the value of the SDR in terms of the current United States dollar was \$1.35458 (\$1.25562 – 2001). On this basis, Set-Aside Resources amounted to \$64,491,000 (\$59,780,000 – 2001). If the capital stock of ADB as of 31 December 2002 had been

ASIAN DEVELOPMENT BANK—ASIAN DEVELOPMENT FUND**NOTES TO SPECIAL PURPOSE FINANCIAL STATEMENTS**

31 December 2002 and 2001

valued in terms of \$12,063.50 per share, Set-Aside Resources would have been \$57,434,000.

NOTE H—COMPREHENSIVE INCOME AND ACCUMULATED OTHER COMPREHENSIVE INCOME

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 currency translation adjustments.

NOTE I—FAIR VALUE OF FINANCIAL INSTRUMENTS

Fair value of a financial instrument is defined as the amount at which the instrument could be exchanged in a current

transaction between willing parties, other than in a forced or liquidation sale.

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

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 carrying amounts of ADF's assets, liabilities, and fund balances are considered to approximate fair values for all significant financial instruments. See Notes B, C, D, and E for discussions relating to investments, loans, and notes of contributors.

REPORT OF INDEPENDENT AUDITORS

Asian Development Bank

In our opinion, the accompanying statements of financial position and the related statements of activities and changes in net assets and cash flows present fairly, in all material respects, in terms of United States dollars, the financial position of the Asian Development Bank—Technical Assistance Special Fund at 31 December 2002 and 2001, and the results of its activities and changes in net assets and its cash flows for the years then ended, in conformity with accounting principles generally accepted in the United States of America. These financial statements are the responsibility of the management of the Asian Development Bank; 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 auditing standards generally accepted in the United States of America 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, assessing the accounting principles used and significant estimates made by management, and evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

Our audits were conducted for the purpose of forming an opinion on the basic financial statements taken as a whole. The accompanying statement of resources as at 31 December 2002 and summary statement of technical assistance approved and effective for the year ended 31 December 2002 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

Detroit, Michigan
10 March 2003

ASIAN DEVELOPMENT BANK—TECHNICAL ASSISTANCE SPECIAL FUND

STATEMENT OF FINANCIAL POSITION

31 December 2002 and 2001

Expressed in Thousands of United States Dollars (Note B)

	2002	2001
ASSETS		
DUE FROM BANKS (Note B)	\$ 1,792	\$ 1,467
INVESTMENTS (Notes B and C)		
Government and government-guaranteed obligations	\$60,508	\$ 60,678
Time deposits	<u>94,457</u> 154,965	<u>124,275</u> 184,953
ACCRUED REVENUE	1,143	991
OTHER ASSETS	7,168	7,052
TOTAL	\$165,068	\$194,463
LIABILITIES AND UNCOMMITTED BALANCES		
PAYABLE TO ORDINARY CAPITAL RESOURCES	\$ 60	\$ -
ACCOUNTS PAYABLE AND OTHER LIABILITIES	70	177
UNDISBURSED COMMITMENTS (Notes B and E)	96,600	113,015
UNCOMMITTED BALANCES (TASF-2 and TASF-4) (Note B)		
Unrestricted net assets	68,338	81,271
TOTAL	\$165,068	\$194,463

The accompanying notes are an integral part of these financial statements (TASF-6).

ASIAN DEVELOPMENT BANK—TECHNICAL ASSISTANCE SPECIAL FUND

STATEMENT OF ACTIVITIES AND CHANGES IN NET ASSETS

For the Years Ended 31 December 2002 and 2001

Expressed in Thousands of United States Dollars (Note B)

	2002	2001
CHANGES IN UNRESTRICTED NET ASSETS		
CONTRIBUTIONS (TASF-4) (Notes B and D)	\$ 1,117	\$ 117
REVENUE		
From investments (Notes B and C)		
Interest	\$ 5,908	\$ 9,103
Unrealized investment (losses) gains	(1,117)	1,844
	4,791	10,947
From other sources—net (Note E)	2,743	447
Total	8,651	11,394
EXPENSES		
Technical assistance (TASF-5) (Notes B and E)	27,931	34,744
Financial expenses	11	3
Total	27,942	34,747
CONTRIBUTIONS AND REVENUE LESS THAN EXPENSES	(19,291)	(23,236)
EXCHANGE GAINS (LOSSES)—net (Note B)	6,358	(10,950)
DECREASE IN NET ASSETS	(12,933)	(34,186)
NET ASSETS AT BEGINNING OF YEAR	81,271	115,457
NET ASSETS AT END OF YEAR	\$ 68,338	\$ 81,271

The accompanying notes are an integral part of these financial statements (TASF-6).

ASIAN DEVELOPMENT BANK—TECHNICAL ASSISTANCE SPECIAL FUND

STATEMENT OF CASH FLOWS

For the Years Ended 31 December 2002 and 2001

Expressed in Thousands of United States Dollars (Note B)

	2002	2001
CASH FLOWS FROM OPERATING ACTIVITIES		
Contributions received	\$ 520	\$ 70
Interest on investments received	5,847	11,227
Cash received from other activities	2,929	563
Technical assistance disbursed	(43,907)	(56,382)
Financial expenses paid	(11)	(3)
Net Cash Used in Operating Activities	<u>(34,622)</u>	<u>(44,525)</u>
CASH FLOWS FROM INVESTING ACTIVITIES		
Sales of investment	27,275	523
Maturities of investment	1,256,924	2,952,122
Purchases of investment	(1,249,279)	(2,907,548)
Net Cash Provided by Investing Activities	<u>34,920</u>	<u>45,097</u>
Effect of Exchange Rate Changes on Due from Banks	<u>27</u>	<u>(261)</u>
Net Increase in Due from Banks	325	311
Due from Banks at Beginning of Year	<u>1,467</u>	<u>1,156</u>
Due from Banks at End of Year	<u>\$ 1,792</u>	<u>\$ 1,467</u>
RECONCILIATION OF DECREASE IN NET ASSETS TO NET CASH USED IN OPERATING ACTIVITIES:		
Decrease in net assets (TASF-2)	\$ (12,933)	\$ (34,186)
Adjustments to reconcile decrease in net assets to net cash used in operating activities:		
Change in undisbursed commitments	(16,415)	(22,761)
Translation adjustments	(6,172)	11,066
Unrealized investment losses (gains)	1,117	(1,844)
Change in contributions receivable	(596)	(47)
Change in accrued interest receivable and others	468	1,920
Change in advances for technical assistance to member countries	(182)	1,568
Amortization of discounts/premiums	<u>91</u>	<u>(241)</u>
Net Cash Used in Operating Activities	<u>\$ (34,622)</u>	<u>\$ (44,525)</u>

The accompanying notes are an integral part of these financial statements (TASF-6).

ASIAN DEVELOPMENT BANK—TECHNICAL ASSISTANCE SPECIAL FUND

STATEMENT OF RESOURCES

31 December 2002

Expressed in Thousands of United States Dollars (Note B)

	Contributions Committed During 2002	Direct Voluntary Contributions	Regularized Replenishment	Total Contributions
DIRECT VOLUNTARY CONTRIBUTIONS				
Australia	\$ –	\$ 2,484	\$ 15,318	\$ 17,802
Austria	–	159	2,207	2,366
Bangladesh	–	47	–	47
Belgium	–	1,394	1,808	3,202
Canada	–	3,346	17,185	20,531
China, People's Rep. of	1,000	1,600	–	1,600
Denmark	–	1,963	2,283	4,246
Finland	–	237	1,007	1,244
France	–	1,697	12,900	14,597
Germany	–	3,315	15,249	18,564
Hong Kong, China	–	100	120	220
India	47	2,857	–	2,857
Indonesia	–	250	40	290
Italy	–	774	8,795	9,569
Japan	–	47,710	97,279	144,989
Korea, Rep. of	–	1,900	600	2,500
Malaysia	–	909	–	909
Nauru	–	–	67	67
The Netherlands	–	1,338	5,978	7,316
New Zealand	–	1,096	715	1,811
Norway	–	3,279	2,021	5,300
Pakistan	70	1,526	–	1,526
Singapore	–	1,100	–	1,100
Spain	–	190	1,651	1,841
Sri Lanka	–	6	–	6
Sweden	–	861	4,129	4,990
Switzerland	–	1,035	3,137	4,172
Taipei, China	–	200	500	700
Turkey	–	–	2,354	2,354
United Kingdom	–	5,617	8,344	13,961
United States	–	1,500	34,352	35,852
Total	1,117	88,490	238,039	326,529
Transfers to Asian Development Fund				(3,472)
Allocation from OCR Net Income (Note D)				501,000
Other Resources ¹				95,560
TOTAL				\$919,617

¹ Other resources represent income and replenishments accruing to TASF since 1 April 1980, including unrealized investment holding gains. The accompanying notes are an integral part of these financial statements (TASF-6).

ASIAN DEVELOPMENT BANK—TECHNICAL ASSISTANCE SPECIAL FUND

SUMMARY STATEMENT OF TECHNICAL ASSISTANCE APPROVED AND EFFECTIVE
For the Year Ended 31 December 2002

Expressed in Thousands of United States Dollars (Note B)

Recipient	Project Preparation	Project Implementation/ Advisory	Total
Azerbaijan	\$ -	\$ 762	\$ 762
Bangladesh	(24)	-	(24)
Bhutan	-	(5)	(5)
Cambodia	-	650	650
China, People's Rep. of	-	6,922	6,922
Cook Islands	-	(41)	(41)
Fiji Islands	-	(150)	(150)
India	1,500	1,341	2,841
Indonesia	200	486	686
Kazakhstan	-	(36)	(36)
Kiribati	-	(52)	(52)
Kyrgyz Republic	-	1,289	1,289
Lao PDR	-	900	900
Maldives	-	230	230
Marshall Islands	-	594	594
Micronesia, Fed. States of	5	785	790
Mongolia	-	1,350	1,350
Nauru	-	(71)	(71)
Nepal	-	(10)	(10)
Pakistan	820	700	1,520
Papua New Guinea	-	(77)	(77)
Philippines	-	922	922
Samoa	-	(4)	(4)
Solomon Islands	(40)	(148)	(188)
Sri Lanka	-	133	133
Thailand	(150)	(27)	(177)
Timor-Leste	-	(21)	(21)
Tuvalu	-	(54)	(54)
Uzbekistan	250	797	1,047
Vanuatu	-	(11)	(11)
Viet Nam	-	155	155
Total	<u>\$2,561</u>	<u>\$17,309</u>	19,870
Regional Activities			8,061
TOTAL			\$27,931

Negative amounts represent net undisbursed commitments written back to balances available for future commitments (Notes B and E).

The accompanying notes are an integral part of these financial statements (TASF-6).

ASIAN DEVELOPMENT BANK—TECHNICAL ASSISTANCE SPECIAL FUND

NOTES TO FINANCIAL STATEMENTS

31 December 2002 and 2001

NOTE A—NATURE OF OPERATIONS

The Technical Assistance Special Fund (TASF) was established to provide technical assistance on a grant basis to developing member countries of the Asian Development Bank (ADB) and for regional technical assistance. TASF resources consist of direct voluntary contributions by members, allocations from the net income of ordinary capital resources (OCR) and Asian Development Fund (ADF) contributions, and revenue from investments and other sources.

NOTE B—SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Presentation of the Financial Statements

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

TASF reports contributed cash and other assets as restricted support if they are received with donor stipulations that limit the use of the donated assets. When a 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. There were no restricted net assets at 31 December 2002 and 2001.

Investments

All investment securities held by TASF are reported at estimated fair value, with realized and unrealized gains and losses included in revenue. Estimated fair value generally represents market value. Time deposits are classified as "Held-to-Maturity" and are reported at cost.

Contributions

Contributions from members are included in the financial statements from the date contribution agreements become effective. Contributions from donors which are restricted by them to technical assistance (TA) projects/programs with specified procurement sources are classified as temporarily restricted contributions. Those without any stipulations as to specific use are accounted for as unrestricted contributions.

Technical Assistance to Member Countries

Technical assistance is recognized in the financial statements when the related project is approved and becomes

effective. Upon completion of the TA project, any undisbursed amount is written back as a reduction in technical assistance for the period and the corresponding undisbursed commitment is eliminated accordingly.

Reporting Currency

The financial statements of TASF are expressed in thousands of current United States dollars. As a matter of convenience, the United States dollar is the functional and reporting currency and is used to measure exchange gains and losses.

Translation of Currencies

Assets, liabilities, and uncommitted balances in currencies other than United States dollars are translated at the applicable rates of exchange at the end of a reporting period. Contributions included in the financial statements during the year are recognized at applicable exchange rates as of the respective dates of commitment. Revenue and expense amounts in currencies other than United States dollars are translated for each semimonthly 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 are accounted for as exchange gains or losses and are charged or credited to operations.

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 TASF considers that its cash and cash equivalents are limited to "DUE FROM BANKS."

NOTE C—INVESTMENTS

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

ASIAN DEVELOPMENT BANK—TECHNICAL ASSISTANCE SPECIAL FUND

NOTES TO FINANCIAL STATEMENTS

31 December 2002 and 2001

by the Board of Directors in 1999. ADB is restricted by its Investment Authority to invest in investment instruments which are obligations of a limited class of issuers, primarily government or government-guaranteed obligations and corporate obligations.

The currency compositions of the investment portfolio as of 31 December 2002 and 2001 expressed in United States dollars are as follows:

Currency	2002	2001
Australian dollar	\$ 6,027,000	\$ 5,147,000
Canadian dollar	124,352,000	132,725,000
Euro	12,354,000	10,078,000
Swiss franc	–	33,918,000
Others	12,232,000	3,085,000
Total	<u>\$154,965,000</u>	<u>\$184,953,000</u>

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 2.86% (5.26% – 2001).

NOTE D—FUNDING

Since inception in 1967, direct contributions have been made by 29 member countries. In 1986 and 1992, the Board of Governors, in authorizing a replenishment of the ADF, provided for an allocation to the TASF in an aggregate amount equivalent to \$72,000,000 and \$140,000,000, respectively, to be used for technical assistance to ADF borrowing developing member countries and for regional technical assistance.

In addition, an aggregate amount equivalent to \$501,000,000 had been allocated to TASF out of OCR net income in 1992 to 1995 and in 1998 to 2000.

Some of the direct contributions received were subject to restricted procurement sources, while some were given on condition that the technical assistance be made on a reim-

bursable basis. The total contributions received for the years ended 31 December 2002 and 2001 were without restrictions.

NOTE E—UNDISBURSED COMMITMENTS

Undisbursed commitments are denominated in United States dollars and represent effective ongoing grant-financed TA projects/programs which are not yet disbursed as of the end of the year. During 2002, an amount of \$3,870,000 (\$5,471,000 – 2001) representing completed and canceled TA projects has been written back as a reduction in technical assistance of the period and the corresponding undisbursed commitment has been eliminated. The fair value of undisbursed commitments approximates the amounts undisbursed because ADB expects that grants will be made for all projects/programs covered by the commitments. When TA provided as a project preparatory grant leads to an ADB loan, the amount of the grant exceeding \$250,000 will be refunded by the borrower through the loan proceeds under the terms of that ADB loan. Refinanced amount of \$2,625,000 (\$346,000 – 2001) was charged to such loans and credited to revenue from other sources of the TASF during the year ended 31 December 2002.

NOTE F—FAIR VALUE OF FINANCIAL INSTRUMENTS

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

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

The carrying amounts of TASF's assets, liabilities, and uncommitted balances are considered to approximate fair values for all significant financial instruments. See Notes B and E for discussions with respect to investments and undisbursed commitments, respectively.

REPORT OF INDEPENDENT AUDITORS

Asian Development Bank

In our opinion, the accompanying statements of financial position and the related statements of activities and changes in net assets and cash flows present fairly, in all material respects, in terms of United States dollars, the financial position of the Asian Development Bank—Japan Special Fund at 31 December 2002 and 2001, and the results of its activities and changes in net assets and its cash flows for the years then ended, in conformity with accounting principles generally accepted in the United States of America. These financial statements are the responsibility of the management of the Asian Development Bank; 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 auditing standards generally accepted in the United States of America 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, assessing the accounting principles used and significant estimates made by management, and evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.



Detroit, Michigan
10 March 2003

ASIAN DEVELOPMENT BANK—JAPAN SPECIAL FUND

STATEMENT OF FINANCIAL POSITION

31 December 2002 and 2001

Expressed in Thousands of United States Dollars (Note B)

	2002			2001		
	ACCSF	JSF Regular & Supplementary	Total	ACCSF	JSF Regular & Supplementary	Total
ASSETS						
DUE FROM BANKS (Note B)	\$ 656	\$ 711	\$ 1,367	\$ 1,315	\$ 663	\$ 1,978
INVESTMENTS (Notes A, B, and C)						
Government and government-guaranteed obligations	2,016	41,021	43,037	35,967	–	35,967
Time deposits	15,163	12,104	27,267	80,964	96,085	177,049
Other securities	43,490	189,746	233,236	64,546	181,676	246,222
	<u>60,669</u>	<u>242,871</u>	<u>303,540</u>	<u>181,477</u>	<u>277,761</u>	<u>459,238</u>
EQUITY INVESTMENTS (Notes A, B, and D), net	–	106	106	–	105	105
ACCRUED REVENUE	710	4,992	5,702	431	1,335	1,766
OTHER ASSETS (Note E)	98	6,306	6,404	23	6,170	6,193
TOTAL	\$62,133	\$254,986	\$317,119	\$183,246	\$286,034	\$469,280
LIABILITIES AND UNCOMMITTED BALANCES						
ACCOUNTS PAYABLE AND OTHER LIABILITIES						
Payable to Ordinary Capital Resources	\$ –	\$ 230	\$ 230	\$ –	\$ 143	\$ 143
Other liabilities (Note E)	14,625	187	14,812	10,327	43	10,370
	<u>14,625</u>	<u>417</u>	<u>15,042</u>	<u>10,327</u>	<u>186</u>	<u>10,513</u>
UNDISBURSED COMMITMENTS (Notes B and F)						
Technical assistance	19,479	94,431	113,910	14,918	117,605	132,523
Interest payment assistance	–	–	–	58,115	–	58,115
	<u>19,479</u>	<u>94,431</u>	<u>113,910</u>	<u>73,033</u>	<u>117,605</u>	<u>190,638</u>
NET ASSETS (JSF-2) (Note B), represented by:						
Uncommitted balances (Notes A, G, and H)						
Unrestricted	–	160,138	160,138	–	8,505	8,505
Temporarily restricted	26,211	–	26,211	99,366	57,794	157,160
	<u>26,211</u>	<u>160,138</u>	<u>186,349</u>	<u>99,366</u>	<u>66,299</u>	<u>165,665</u>
Net accumulated investment income (Notes A and H)						
Temporarily restricted	1,818	–	1,818	520	101,944	102,464
	<u>28,029</u>	<u>160,138</u>	<u>188,167</u>	<u>99,886</u>	<u>168,243</u>	<u>268,129</u>
TOTAL	\$62,133	\$254,986	\$317,119	\$183,246	\$286,034	\$469,280

The accompanying notes are an integral part of these financial statements (JSF-4).

ASIAN DEVELOPMENT BANK—JAPAN SPECIAL FUND

STATEMENT OF ACTIVITIES AND CHANGES IN NET ASSETS

For the Years Ended 31 December 2002 and 2001

Expressed in Thousands of United States Dollars (Note B)

	2002			2001		
	ACCSF	JSF Regular & Supplementary	Total	ACCSF	JSF Regular & Supplementary	Total
CHANGES IN UNRESTRICTED NET ASSETS						
CONTRIBUTIONS (Notes B and H)	\$ -	\$ 22,550	\$ 22,550	\$ -	\$ 30,929	\$ 30,929
REVENUE FROM INVESTMENTS (Notes B and C)	-	5,810	5,810	-	-	-
REVENUE FROM OTHER SOURCES	-	43	43	-	74	74
UNREALIZED INVESTMENT GAINS ON EQUITY INVESTMENTS (Note D)	-	-	-	-	205	205
NET ASSETS RELEASED FROM RESTRICTIONS (Notes B and H)	72,994	159,738	232,732	8,779	894	9,673
Total	72,994	188,141	261,135	8,779	32,102	40,881
TRANSFER TO JAPAN FUND FOR POVERTY REDUCTION (Note A)	(90,000)	-	(90,000)	-	-	-
EXPENSES						
Interest payment assistance written back (Notes B and F)	(33,251)	-	(33,251)	-	-	-
Technical assistance (Notes B and F)	16,157	34,554	50,711	8,700	64,227	72,927
Administrative expenses	88	1,349	1,437	79	1,413	1,492
Provision for losses (Notes B and D)	-	-	-	-	431	431
Total	(17,006)	35,903	18,897	8,779	66,071	74,850
CONTRIBUTIONS AND REVENUE IN EXCESS OF (LESS THAN) EXPENSES	-	152,238	152,238	-	(33,969)	(33,969)
EXCHANGE LOSSES (Note B)	-	(606)	(606)	-	(992)	(992)
INCREASE (DECREASE) IN UNRESTRICTED NET ASSETS BEFORE TRANSLATION ADJUSTMENTS	-	151,632	151,632	-	(34,961)	(34,961)
TRANSLATION ADJUSTMENTS (Note B)	-	1	1	-	(3)	(3)
INCREASE (DECREASE) IN UNRESTRICTED NET ASSETS	-	151,633	151,633	-	(34,964)	(34,964)
CHANGES IN TEMPORARILY RESTRICTED NET ASSETS						
REVENUE FROM INVESTMENTS AND OTHER SOURCES (Notes B and C)	1,392	-	1,392	252	14,110	14,362
NET ASSETS RELEASED FROM RESTRICTIONS (Notes B and H)	(72,994)	(159,738)	(232,732)	(8,779)	(894)	(9,673)
EXCHANGE LOSSES (Note B)	(1,471)	-	(1,471)	(218)	-	(218)
TRANSLATION ADJUSTMENTS (Note B)	1,216	-	1,216	(28,353)	(2)	(28,355)
(DECREASE) INCREASE IN TEMPORARILY RESTRICTED NET ASSETS	(71,857)	(159,738)	(231,595)	(37,098)	13,214	(23,884)
DECREASE IN NET ASSETS	(71,857)	(8,105)	(79,962)	(37,098)	(21,750)	(58,848)
NET ASSETS AT BEGINNING OF YEAR	99,886	168,243	268,129	136,984	189,993	326,977
NET ASSETS AT END OF YEAR	\$ 28,029	\$ 160,138	\$ 188,167	\$ 99,886	\$ 168,243	\$ 268,129

The accompanying notes are an integral part of these financial statements (JSF-4).

ASIAN DEVELOPMENT BANK—JAPAN SPECIAL FUND

STATEMENT OF CASH FLOWS

For the Years Ended 31 December 2002 and 2001

Expressed in Thousands of United States Dollars (Note B)

	2002			2001		
	ACCSF	JSF Regular & Supplementary	Total	ACCSF	JSF Regular & Supplementary	Total
CASH FLOWS FROM OPERATING ACTIVITIES						
Contributions received	\$ -	\$ 22,550	\$ 22,550	\$ -	\$ 30,929	\$ 30,929
Transfer to Japan Fund for Poverty Reduction	(90,000)	-	(90,000)	-	-	-
Interest on investments received	1,603	4,878	6,481	536	18,096	18,632
Technical assistance disbursed	(10,000)	(57,723)	(67,723)	(7,010)	(62,893)	(69,903)
Interest assistance paid	(22,225)	-	(22,225)	(12,398)	-	(12,398)
Administrative expenses paid	(101)	(1,274)	(1,375)	(55)	(1,470)	(1,525)
Others—net	(1,464)	(549)	(2,013)	(218)	(902)	(1,120)
Net Cash Used in Operating Activities	(122,187)	(32,118)	(154,305)	(19,145)	(16,240)	(35,385)
CASH FLOWS FROM INVESTING ACTIVITIES						
Sales of investment	108,343	-	108,343	8,419	29,966	38,385
Maturities of investment	3,935,023	9,553,289	13,488,312	3,733,758	6,864,848	10,598,606
Purchases of investment	(3,924,828)	(9,521,124)	(13,445,952)	(3,721,982)	(6,878,441)	(10,600,423)
Net Cash Provided by Investing Activities	118,538	32,165	150,703	20,195	16,373	36,568
Effect of Exchange Rate Changes on Due from Banks	2,990	1	2,991	204	(7)	197
Net (Decrease) Increase in Due from Banks	(659)	48	(611)	1,254	126	1,380
Due from Banks at Beginning of Year	1,315	663	1,978	61	537	598
Due from Banks at End of Year	\$ 656	\$ 711	\$ 1,367	\$ 1,315	\$ 663	\$ 1,978
RECONCILIATION OF DECREASE IN NET ASSETS TO NET CASH USED IN OPERATING ACTIVITIES:						
Decrease in net assets (JSF-2)	\$ (71,857)	\$ (8,105)	\$(79,962)	\$ (37,098)	\$ (21,750)	\$(58,848)
Adjustments to reconcile decrease in net assets to net cash used in operating activities:						
Change in undisbursed commitments	(53,554)	(23,174)	(76,728)	(16,251)	3,189	(13,062)
Amortization of discounts/premiums	610	2,982	3,592	623	(1,401)	(778)
Translation adjustments	(1,216)	(1)	(1,217)	28,353	5	28,358
Unrealized investment (gains) losses	(101)	(258)	(359)	45	(203)	(158)
Net (gain) loss from sales of investments	(12)	-	(12)	-	19	19
Provision for losses charged	-	-	-	-	431	431
Others—net	3,943	(3,562)	381	5,183	3,470	8,653
Net Cash Used in Operating Activities	\$ (122,187)	\$ (32,118)	\$ (154,305)	\$ (19,145)	\$ (16,240)	\$ (35,385)

The accompanying notes are an integral part of these financial statements (JSF-4).

ASIAN DEVELOPMENT BANK—JAPAN SPECIAL FUND

NOTES TO FINANCIAL STATEMENTS

31 December 2002 and 2001

NOTE A—NATURE OF OPERATIONS

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

In March 1999, the Board approved the acceptance and administration by ADB of a new facility, the Asian Currency Crisis Support Facility (ACCSF) to assist Asian currency crisis-affected member countries (CAMCs). Funded by Japan, ACCSF was established within JSF to assist in the economic recovery of CAMCs through interest payment assistance (IPA) grants, TA grants, and guarantees. With the general fulfillment of the purpose of the facility, Japan and ADB agreed to terminate the ACCSF on 22 March 2002. An amount of \$90 million in the ACCSF account, upon request of Japan, was transferred to the Japan Fund for Poverty Reduction (JFPR). JFPR, established by Japan in May 2000 supporting innovative poverty reduction and related social development activities, is one of the trust funds managed by ADB. The ACCSF account is to be kept open until the completion of all TA and IPA disbursements and the settlement of all administrative expenses.

NOTE B—SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Presentation of the Financial Statements

The financial statements of JSF are presented on the basis of unrestricted and temporarily restricted net assets. ACCSF funds are separately reported in the financial statements.

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. Time deposits are classified as "Held-to-Maturity" and are reported at cost.

Contributions

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

Technical Assistance and Interest Payment Assistance

Technical assistance and interest payment assistance are recognized in the financial statements when the related project or assistance is approved and becomes effective. Upon completion of the TA project or cancellation of a grant, any undisbursed amount is written back as a reduction in TA or IPA for the year and the corresponding undisbursed commitment is eliminated, 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 respective dates of commitment. Revenue and expense amounts in Japanese yen are translated for each semimonthly period at the applicable rates of exchange at the beginning of each period; such practice approximates the application of average rates in effect during the period. Exchange gains or losses on currency transactions arise on exchange differences between the date a project/program is

ASIAN DEVELOPMENT BANK—JAPAN SPECIAL FUND

NOTES TO FINANCIAL STATEMENTS

31 December 2002 and 2001

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 reserve against losses is established 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 main investment management objective is to maintain security and liquidity. Subject to these parameters, ADB seeks the highest possible return on its investments. Investments are governed by the Investment Authority approved by the Board of Directors in 1999. ADB is restricted by its Investment Authority to invest in investment instruments which are obligations of a limited class of issuers, primarily government or government-guaranteed obligations and corporate obligations.

The currency compositions of the investment portfolio as of 31 December 2002 and 2001 expressed in United States dollars are as follows:

Currency	2002			2001		
	ACCSF	JSF Regular and Supplementary	Total	ACCSF	JSF Regular and Supplementary	Total
Japanese yen	\$ –	\$ –	\$ –	\$181,477,000	\$ –	\$181,477,000
United States dollar	60,669,000	242,871,000	303,540,000	–	277,761,000	277,761,000
Total	\$60,669,000	\$242,871,000	\$303,540,000	\$181,477,000	\$277,761,000	\$459,238,000

The annualized rates of return on the average investments held under ACCSF and JSF funds during the year, based on the portfolio held at the beginning and end of each month were 1.54% and 2.15%, respectively (0.12% and 4.76%, respectively - 2001).

NOTE D—EQUITY INVESTMENTS

ADB used JSF resources to make an equity investment in India in 1990. Commencing May 2001, due to the unavailability of a reliable market for the investment, ADB reported the investment at its written down value of \$106,000 (\$105,000 - 2001).

NOTE E—OTHER ASSETS AND LIABILITIES

Included in other assets and liabilities are interfund balances between JSF and ACCSF. As at 31 December 2002,

an amount of \$2,089,000 (\$431,000 - 2001) was receivable from ACCSF. The said amount is reflected as other assets under JSF and other liabilities under ACCSF.

NOTE F—UNDISBURSED COMMITMENTS

Undisbursed commitments are denominated in United States dollars and represent TA projects/programs and IPA grants which have become effective but not yet disbursed. During 2002, an amount of \$3,010,000 (\$2,960,000 - 2001) and \$33,251,000 (nil - 2001), representing completed and partially canceled TA projects and IPA grants, respectively, have been written back as a reduction in TA and IPA for the year, and the corresponding undisbursed commitments have been eliminated. The fair value of undisbursed commitments approximates the amounts outstanding because ADB expects that disbursements will substantially be made for all the projects/programs covered by the commitments.

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NOTE G—UNCOMMITTED BALANCES

Uncommitted balances comprised of amounts which have not been committed by ADB as at 31 December 2002. These

balances include TA projects/programs that had been approved but not yet become effective.

As of 31 December 2002 and 2001 these balances are as follows:

	2002			2001		
	ACCSF	JSF Regular and Supplementary	Total	ACCSF	JSF Regular and Supplementary	Total
Uncommitted balances	\$26,211,000	\$160,138,000	\$186,349,000	\$99,366,000	\$66,299,000	\$165,665,000
TA projects/programs approved by Japan and ADB but not yet effective	(2,500,000)	(22,820,000)	(25,320,000)	(7,540,000)	(23,555,000)	(31,095,000)
TA projects/programs approved by Japan and not yet effective	—	(1,900,000)	(1,900,000)	(2,750,000)	(3,440,000)	(6,190,000)
Uncommitted balances available for new commitments	<u>\$23,711,000</u>	<u>\$135,418,000</u>	<u>\$159,129,000</u>	<u>\$89,076,000</u>	<u>\$39,304,000</u>	<u>\$128,380,000</u>

NOTE H—CONTRIBUTIONS AND TEMPORARILY RESTRICTED NET ASSETS

All contributions for the years ended 31 December 2002 and 2001 were received during the respective years. Some of the contributions received were with restriction that were to be utilized for specific TA projects/programs. Such contributions were classified as temporarily restricted support.

Effective 31 December 2002, all remaining temporarily restricted net assets under JSF were transferred and integrated into the regular net assets, as concurred by Japan, in order to optimize the use of JSF. Temporarily restricted uncommitted balances are available for the following purposes as of 31 December 2002 and 2001:

	2002	2001
Asian Currency Crisis Support Facility	<u>\$26,211,000</u>	<u>\$ 99,366,000</u>
Japan Special Fund		
Environment-Related Activities	—	29,365,000
Financial Sector	—	11,009,000
Private Sector Promotion	—	9,916,000
Gender and Development Training/Symposium	—	7,110,000
	—	394,000
	—	<u>57,794,000</u>
Total	<u>\$26,211,000</u>	<u>\$157,160,000</u>

Accumulated investment income net of accumulated administrative expenses for 31 December 2001 was categorized as temporarily restricted net assets. Under the terms of the agreement between ADB and Japan, accumulated investment income may only be used for defraying of the JSF's administrative expenses. Effective 31 December 2002, Japan agreed to use the investment income amounting to \$106,405,000 for JSF as additional resources for funding future ADB's TA operations, as well as for defraying administrative expenses.

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

NOTE I—GUARANTEES

To assist in the economic recovery of CAMCs, a guarantee facility is provided under ACCSF. In the absence of any concluded guarantee, the noninterest-bearing, nonnegotiable note of ¥360 billion made available to support the guarantee facility under ACCSF was returned to Japan on 25 March 2002.

ASIAN DEVELOPMENT BANK—JAPAN SPECIAL FUND**NOTES TO FINANCIAL STATEMENTS**

31 December 2002 and 2001

NOTE J—FAIR VALUE OF FINANCIAL INSTRUMENTS

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

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

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 carrying amounts of JSF's assets, liabilities, and uncommitted balances are considered to approximate fair values for all significant financial instruments. See Notes B, C, D, and F for discussions relating to investments, equity investments, and undisbursed commitments.

REPORT OF INDEPENDENT AUDITORS

Asian Development Bank

In our opinion, the accompanying statements of financial position and the related statements of activities and changes in net assets, and cash flows present fairly, in all material respects in terms of United States dollars, the financial position of the Asian Development Bank—Asian Development Bank Institute Special Fund at 31 December 2002 and 2001, and the results of its activities and changes in net assets and its cash flows for the years ended 31 December 2002 and 2001, in conformity with accounting principles generally accepted in the United States of America. These financial statements are the responsibility of the management of the Asian Development Bank Institute; 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 auditing standards generally accepted in the United States of America 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, assessing the accounting principles used and significant estimates made by management, and evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

Price Waterhouse Coopers LLP

Detroit, Michigan
10 March 2003

ASIAN DEVELOPMENT BANK—ASIAN DEVELOPMENT BANK INSTITUTE SPECIAL FUND
STATEMENT OF FINANCIAL POSITION
31 December 2002 and 2001

Expressed in Thousands of United States Dollars (Note B)

	2002	2001
ASSETS		
DUE FROM BANKS (Note B)	\$ 6,300	\$ 2,161
INVESTMENTS (Notes B, C, and D)		
Time deposits and government securities	2,955	5,975
PROPERTY, FURNITURE, AND EQUIPMENT (Notes B and F)		
Leasehold Improvements	\$1,689	\$1,526
Less—allowance for depreciation	<u>926</u> 763	<u>672</u> 854
Furniture and Equipment	2,614	2,609
Less—allowance for depreciation	<u>2,281</u> 333	<u>2,257</u> 352
OTHER ASSETS	1,849	1,711
TOTAL	\$12,200	\$11,053
LIABILITIES AND UNCOMMITTED BALANCES		
ACCOUNTS PAYABLE AND OTHER LIABILITIES (Note G)	\$ 1,803	\$1,196
UNCOMMITTED BALANCES (ADBISF-2)		
Unrestricted net assets	10,397	9,857
TOTAL	\$12,200	\$11,053

The accompanying notes are an integral part of these financial statements (ADBISF-4).

ASIAN DEVELOPMENT BANK—ASIAN DEVELOPMENT BANK INSTITUTE SPECIAL FUND

STATEMENT OF ACTIVITIES AND CHANGES IN NET ASSETS

For the Years Ended 31 December 2002 and 2001

Expressed in Thousands of United States Dollars (Note B)

	<u>2002</u>	<u>2001</u>
CHANGES IN UNRESTRICTED NET ASSETS		
CONTRIBUTIONS (Note B)	\$ 9,779	\$18,476
REVENUE		
Income from investments (Notes B and C)	–	5
Income from other sources—net	<u>6</u>	<u>3</u>
Total	<u>9,785</u>	<u>18,484</u>
EXPENSES		
Administrative expenses	8,580	10,191
Program expenses	<u>1,957</u>	<u>4,647</u>
Total	<u>10,537</u>	<u>14,838</u>
CONTRIBUTIONS AND REVENUE (LESS THAN) IN EXCESS OF EXPENSES	(752)	3,646
EXCHANGE LOSSES—NET	49	(88)
TRANSLATION ADJUSTMENTS (Note B)	<u>1,243</u>	<u>(1,315)</u>
INCREASE IN UNRESTRICTED NET ASSETS AFTER TRANSLATION ADJUSTMENTS	540	2,243
NET ASSETS AT BEGINNING OF YEAR	9,857	7,614
NET ASSETS AT END OF YEAR	\$10,397	\$ 9,857

The accompanying notes are an integral part of these financial statements (ADBISF-4).

ASIAN DEVELOPMENT BANK—ASIAN DEVELOPMENT BANK INSTITUTE SPECIAL FUND
STATEMENT OF CASH FLOWS
For the Years Ended 31 December 2002 and 2001

Expressed in Thousands of United States Dollars (Note B)

	<u>2002</u>	<u>2001</u>
CASH FLOWS FROM OPERATING ACTIVITIES		
Contributions received	\$ 9,779	\$ 18,476
Interest on investments received	-	5
Expenses paid	<u>(9,642)</u>	<u>(14,415)</u>
Net Cash Provided by Operating Activities	<u>137</u>	<u>4,066</u>
CASH FLOWS FROM INVESTING ACTIVITIES		
Maturity and sales of investment	148,400	155,002
Purchases of investment	<u>(144,649)</u>	<u>(158,094)</u>
Net Cash Provided by (Used In) Investing Activities	<u>3,751</u>	<u>(3,092)</u>
Effect of Exchange Rate Changes on Cash	<u>251</u>	<u>247</u>
Net Increase in Due From Banks	4,139	1,221
Due from Banks at Beginning of Year	<u>2,161</u>	<u>940</u>
Due from Banks at End of Year	<u>\$ 6,300</u>	<u>\$ 2,161</u>
RECONCILIATION OF INCREASE IN UNRESTRICTED NET ASSETS TO NET CASH PROVIDED BY OPERATING ACTIVITIES:		
Increase in net unrestricted assets (ADBISF-2)	\$ 540	\$ 2,243
Adjustments to reconcile increase in net unrestricted assets to net cash provided by operating activities:		
Translation adjustments	(1,243)	1,315
Depreciation	226	545
Others—net	<u>614</u>	<u>(37)</u>
Net Cash Provided by Operating Activities	<u>\$ 137</u>	<u>\$ 4,066</u>

The accompanying notes are an integral part of these financial statements (ADBISF-4).

ASIAN DEVELOPMENT BANK—ASIAN DEVELOPMENT BANK INSTITUTE SPECIAL FUND

NOTES TO FINANCIAL STATEMENTS

31 December 2002 and 2001

NOTE A—NATURE OF OPERATIONS

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

NOTE B—SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES*Presentation of the Financial Statements*

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

The Institute reports donor's contributions of cash and other assets as unrestricted support as these are made available to the Institute without conditions other than for the purposes of pursuing the objectives of the Institute.

Investments

All investment securities held by the Institute are reported at estimated fair value, with realized and unrealized gains and losses included in revenue. Estimated fair value generally represents market value. Time deposits are classified as "Held-to-Maturity" and are reported at cost.

Property, Furniture, and Equipment

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

Contributions

Contributions from donors are included in the financial statements from the date committed.

Functional Currency and Reporting Currency

The functional currency of the Institute is the Japanese yen. The reporting currency is the United States dollar and the

financial statements are expressed in thousands of current United States dollars.

Translation of Currencies

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

Accounting Estimates

The preparation of 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 as at the end of the year and the reported amounts of income and expenses during the year. Actual results could differ from those estimates.

Statement of Cash Flows

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

Reclassifications

Certain reclassifications of the financial statements and related footnote amounts in the year ended 31 December 2001 have been made to conform to the presentation in the year ended 31 December 2002.

NOTE C—INVESTMENTS

The investment portfolio was composed wholly of investments denominated in Japanese yen. As of 31 December 2002 and 2001, the estimated fair value of the investments approximated cost or amortized cost. All such investments are due within one year.

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 0.01% (0.07% - 2001).

NOTES TO FINANCIAL STATEMENTS

31 December 2002 and 2001

Investments are governed by the Investment Authority approved by the Board of Directors in 1999. The Investment Authority allows investment in higher-yielding investment instruments, such as high-quality corporate bonds, mortgage-backed securities, and asset-backed securities. The main investment management objective is to maintain security and liquidity. Subject to these parameters, ADB administers the Institute's investment and seeks the highest possible return on its investments.

NOTE D—FAIR VALUE OF FINANCIAL INSTRUMENTS

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

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

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

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

Staff Retirement Plan

The Institute participates in the contributory defined benefit Staff Retirement Plan (the Plan) of ADB. Every member of

the professional staff, as defined under the Plan, shall, as a condition of service, become a participant from the first day of service, provided that at such a date, the staff has not reached the normal retirement age of 60. Retirement benefits are based on length of service and highest average remuneration during two years of eligible service. The Plan assets are segregated and are not included in the statement of financial position. The costs of administering the Plan are absorbed by ADB, 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 salary to the Plan and may also make voluntary contributions. The Institute's contribution is determined at a rate sufficient to cover that part of the costs of the Plan not covered by the participants' contributions.

Postretirement Medical Benefits Plan

The Institute participates in the cost-sharing plan of ADB for retirees medical insurance premiums of ADB. Under the plan, the Institute is obligated to pay 75% of the Group Medical Insurance Plan premiums for retirees and their eligible dependents who elect 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.

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The following table sets forth the pension and postretirement benefits at 31 December 2002 and 31 December 2001:

	Pension Benefits		Postretirement Medical Benefits	
	2002	2001	2002	2001
Change in benefit obligation:				
Benefit obligation at beginning of year	\$ 1,220,000	\$ 750,000	\$ 290,000	\$ 252,000
Service cost	313,000	270,000	108,000	84,000
Interest cost	113,000	84,000	28,000	28,000
Plan participants' contributions	116,000	124,000	-	-
Amendments	-	45,000	-	-
Actuarial gain	(272,000)	(53,000)	(61,000)	(58,000)
Benefits paid	(84,000)	-	(17,000)	(16,000)
Benefit obligation at end of year	<u>\$ 1,406,000</u>	<u>\$ 1,220,000</u>	<u>\$ 348,000</u>	<u>\$ 290,000</u>
Change in plan assets:				
Fair value of plan assets at beginning of year	\$ 869,000	\$ 651,000	\$ -	\$ -
Actual return on plan assets	(84,000)	(53,000)	-	-
Employer's contribution	137,000	147,000	17,000	16,000
Plan participants' contributions	116,000	124,000	-	-
Benefits paid	(84,000)	-	(17,000)	(16,000)
Fair value of plan assets at end of year	<u>\$ 954,000</u>	<u>\$ 869,000</u>	<u>\$ -</u>	<u>\$ -</u>
Funded status	\$ (452,000)	\$ (351,000)	\$ (348,000)	\$ (290,000)
Unrecognized actuarial gain	(328,000)	(235,000)	(182,000)	(135,000)
Unrecognized prior service cost	40,000	45,000	(13,000)	(15,000)
Net amount recognized	<u>\$ (740,000)</u>	<u>\$ (541,000)</u>	<u>\$ (543,000)</u>	<u>\$ (440,000)</u>
Amounts recognized in the statement of financial position consist of:				
Accrued benefit liability	\$ (740,000)	\$ (541,000)	\$ (543,000)	\$ (440,000)
Net amount recognized	<u>\$ (740,000)</u>	<u>\$ (541,000)</u>	<u>\$ (543,000)</u>	<u>\$ (440,000)</u>
Weighted-average assumptions as of 31 December				
Discount rate	6.75%	7.00%	6.75%	7.00%
Expected return on plan assets	8.00%	8.00%	N/A	N/A
Rate of compensation increase varies with age and averages	5.75%	6.00%	5.75%	6.00%

For measurement purposes, a 7.75% annual rate of increase in the per capita cost of covered health care benefits was assumed for the valuation as at 31 December 2002. The rate

was assumed to decrease gradually to 5.75% for 2009 and remain at that level thereafter.

	Pension Benefits		Postretirement Medical Benefits	
	2002	2001	2002	2001
Components of net periodic benefit cost:				
Service cost	\$ 313,000	\$ 270,000	\$ 108,000	\$ 84,000
Interest cost	113,000	84,000	28,000	28,000
Expected return on plan assets	(78,000)	(65,000)	-	-
Amortization of prior service cost	5,000	-	(2,000)	(2,000)
Recognized actuarial loss	(17,000)	(34,000)	(14,000)	(2,000)
Net periodic benefit cost	<u>\$ 336,000</u>	<u>\$ 255,000</u>	<u>\$ 120,000</u>	<u>\$ 108,000</u>

ASIAN DEVELOPMENT BANK—ASIAN DEVELOPMENT BANK INSTITUTE SPECIAL FUND

NOTES TO FINANCIAL STATEMENTS

31 December 2002 and 2001

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

	<u>1-Percentage- Point Increase</u>	<u>1-Percentage- Point Decrease</u>
Effect on total service and interest cost components	\$30,000	\$(24,000)
Effect on postretirement benefit obligation	69,000	(56,000)

NOTE F —LEASED ASSETS

The Institute leases office space and other assets. Rental expenses under operating leases for the years ended 31 December 2002 and 2001 were \$2,855,000 and \$2,953,000, respectively. The minimum rental payments required under operating leases that have initial or noncancelable lease terms in excess of one year at 31 December 2002 follow:

<u>Year ending 31 December</u>	<u>Minimum future rentals</u>
2003	\$2,232,000

NOTE G—DUE TO ADB

Accounts payable and other liabilities include amounts due to ADB of \$72,000 and \$107,000 at 31 December 2002 and 2001, respectively.