FINCA MICROFINANCE BANK LIMITED

ANNUAL REPORTS AND FINANCIAL STATEMENTS

31 DECEMBER 2020

FINCA MICROFINANCE BANK LIMITED

ANNUAL REPORTS AND FINANCIAL STATEMENTS
FOR THE YEAR ENDED 31 DECEMBER 2020

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FINCA MICROFINANCE BANK LIMITED

CORPORATE INFORMATION

DIRECTORS	**Name**	**Position**	**Nationality**	**Date of appointment / Resignation**
	Mike Gama-Lobo	Chairman	American	Resigned on 25 September 2020
	Nasama Massinda	Chairperson	Tanzanian	Appointed on 22 Oct 2019 as a Board member and as Chairperson on 1 October 2020
	Volker Renner	Member	Germany	Appointed on 31 May 2017
	Monica Joseph	Member	Tanzanian	Appointed on 2 September 2015
	Mary Pascal Mabiti	Member	Tanzanian	Appointed on 11 June 2019
	Barbara Wasmus	Member	Netherlands	Appointed on 23 June 2019

Key management chairperson	**Name**	**Position**	**Nationality**	**Appointment date**
	Edward Talawa	Chief Executive Officer	Tanzanian	Appointed on 10 June 2019

REGISTERED OFFICE
Plot No.34/1, 8th Floor, TAN House
Victoria, Bagamoyo Road
P.O. Box 78783
Dar es Salaam, Tanzania

AUDITOR
KPMG
Certified Public Accountants
2nd Floor, The Luminary,
Haile Selassie Road
P.O. Box 1160
Dar es Salaam, Tanzania

PRINCIPAL BANKERS
NMB Bank Plc

Head Office
Ohio/Ali Hassan Mwinyi Road
P.O. Box 9213
Dar es Salaam, Tanzania

NBC Bank Limited
Head Office
Sokoine Drive
P.O. Box 1863
Dar es Salaam, Tanzania

CRDB Bank Plc
Head Quarters
Azikiwe Street
P.O. Box 268
Dar es Salaam, Tanzania

Diamond Trust Bank (Tanzania) Limited
Samora avenue
P.O. Box 115
Dar es Salaam, Tanzania

CORPORATE INFORMATION (CONTINUED)

PRINCIPAL BANKERS	Citibank (Tanzania) Limited 36 Upanga Road P.O Box 71625 Dar es Salaam, Tanzania
	Bank of Tanzania, 2 Mirambo street P.O Box 11884 Dar es Salaam, Tanzania
LAWYERS	Mwema Advocates Bibi Titi/Morogoro Road P.O Box 4182 Dar es Salaam, Tanzania
	Lawfields Attorneys Plot No. 38, 6th Floor, Tanzanite Park, Ursino South P.O Box 35970 Dar es Salaam, Tanzania
	Leo Attorneys 21 Tunisia Rd, Ada Estate P.O Box 78572 Dar es Salaam, Tanzania
	KZR Law Chambers P.O Box 988 Mwanza, Tanzania
	Mwakingwe & Bank Advocates NHC Building, Uhuru Bendera Road P.O Box 92 Iringa, Tanzania
	E&S Associates Co. Limited Bunju A, Kilungule Street, House No.BNJ/KLGL/1329 P. O. Box 31570 Dar es Salaam, Tanzania
PRINCIPAL FINANCIERS	FINCA Microfinance Holdings (FMH) Global Partnerships Social Investment Fund 6.0 LLC

FINCA MICROFINANCE BANK LIMITED

REPORT OF THE DIRECTORS
FOR THE YEAR ENDED 31 DECEMBER 2020

The Directors present their annual report together with the audited financial statements for the year ended 31 December 2020, which disclose the state of affairs of FINCA Microfinance Bank Limited ("the Bank").

INCORPORATION

The Bank was incorporated on 12 September 2000 under the Companies Act, 2002 as a Bank limited by guarantee not having a share capital. However, in September 2011 the Bank converted to a Bank limited by shares.

PRINCIPAL ACTIVITIES

The principal activity of the Bank is the provision of banking and related financial services stipulated under the Banking and Financial Institutions Act, 2006.

The Bank's mission is to alleviate poverty through lasting solutions that help people build assets, create jobs and raise their standard of living and become number one financial institutions serving low income individuals and borrowers. The Bank is transforming business model to leverage technology and focusing on process improvements, while maintaining the human touch and warm relationships that define FINCA. The Bank is focused to provide innovative and impactful financial services to enable low-income individuals and communities to invest in their futures.

BANK SECRETARY

Bank Secretary during the year ended 31 December 2020 was Beatus Malawa.

CORPORATE GOVERNANCE

The Board of the Bank consists of five Directors. The Board takes overall responsibility for the Bank, including responsibility for identifying key risk areas, considering and monitoring investment decisions, considering significant financial matters, and reviewing the performance of management business plans and budgets. The Board is also responsible for ensuring that a comprehensive system of internal control policies and procedures is operative, and in compliance with sound corporate governance principles**.**

The Board is required to meet at least four times a year. The Board delegates day-to-day management of the business to the Chief Executive Officer who is assisted by senior management. Senior management is invited to attend board meetings and facilitate the effective control of all the Bank's operational activities, acting as a medium of communication and coordination between all the various business units**.**

The Bank is committed to the principles of effective corporate governance. The Directors also recognize the importance of integrity, transparency and accountability. During the year, the following board subcommittees were in place to ensure a high standard of corporate governance throughout the Bank:

Audit Committee

Name	**Position**	**Country of residence**	**Date of appointment**
Volker Renner	Chairperson	Germany	12 November 2017
Mary Mabiti	Member	Tanzania	11 June 2019
Barbara Wasmus	Member	Netherlands	23 June 2019

CORPORATE GOVERNANCE (CONTINUED)

Asset-Liability Committee

Name	Position	Country of residence	Date of appointment / resignation
Monica Joseph	Chairperson	Tanzania	1 December 2015
Barbara Wasmus	Member	Netherlands	25 June 2019
Nasama Massinda	Member	Tanzania	1 October 2020 removed from the committee after being appointed as the Board chairperson

Risk Committee

Name	Position	Country of residence	Date of appointment
Barbara Wasmus	Chairperson	Netherlands	25 June 2019
Monica Joseph	Member	Tanzania	1 December 2015
Volker Renner	Member	Germany	12 November 2017

Human Resources Committee

Name	Position	Country of residence	Date of appointment
Mary Mabiti	Chairperson	Tanzania	11 June 2019
Monica Joseph	Member	Tanzania	1 December 2015
Nasama Massinda	Member	Tanzania	Appointed as a member on 22 October 2019 and on 1 October 2020 removed from the committee after being appointed as the Board chairperson.

CAPITAL STRUCTURE

The Bank capital structure for the year under review is shown below.

	2020 TZS '000	2019 TZS '000
Authorized share capital		
35,000,000 ordinary shares of TZS 1,000 each	35,000,000	35,000,000
Issued and fully paid capital		
34,102,304 (2019: 31,574,605) ordinary shares of TZS 1,000 each	34,102,304	31,574,605

SHAREHOLDERS OF THE BANK

The total number of shareholders during the year 2020 was two. There were no Directors holding shares in the Bank.

Shareholding structure of the Bank was as follows:

	2020	2019
FINCA Microfinance Holding Bank LLC	34,102,303	31,574,604
FINCA International LLC	1	1
	34,102,304	31,574,605

MANAGEMENT

The Management of the Bank is under the Chief Executive Officer and is organized in the following departments:

- Banking Services.
- Finance and Administration.
- Credit.
- Human Resources.
- Legal and Compliance;
- Internal Audit.
- Risk Management.
- Information Systems; and
- Marketing.

FUTURE DEVELOPMENT PLANS

The Bank will continue focusing on the current core business, particularly the bottom of the pyramid to improve its profitability while being innovative in delivery mechanism to ensure sustainability and good customer experience through all the touch points.

RESULTS AND DIVIDEND

During the year, the Bank made loss after tax of TZS 9,258,929,000 (2019: Loss of TZS 7,123,881,000). The Directors do not propose payment of dividend for the year ended 31 December 2020 (2019: Nil).

PERFORMANCE FOR THE YEAR

The following is a summary highlighting the Bank's performance.

	2020	2019
Branches	19	23
Total number of staff	283	411
Gross outstanding portfolio (TZS `000)	37,394,381	60,348,363
Total current and demand accounts (TZS '000)	31,819,348	36,757,690
Total assets (TZS '000)	58,803,480	87,797,164
Portfolio At Risk > 1 day (PAR 1)	22.36%	11.18%
Portfolio At Risk over 30 days (PAR 30)	18.84%	8.45%
Portfolio yield	42.9%	50.0%
Debt/Equity	162.7%	180.4%
Total deposits/gross loans and advances	85.1%	60.9%
Capital/assets	58.0%	36.0%

The Bank's results are set out on page 14 of the financial statements. Performance of the Bank is consistent with the poor performance of financial sector that was mainly attributed by decline in loans and advances growth and deterioration of the quality of loan portfolio. Sector performance has been noted by the central Bank and they have been implementing various accommodative monetary stance to rectify the situation. The Bank is continuing to invest on technology and innovations to improve efficiency service delivery and thus improving ability to withstand both internal as well as external shocks.

RISK MANAGEMENT AND INTERNAL CONTROL

The Board accepts final responsibility for the risk management and internal control systems of the Bank. It is the task of management to ensure that adequate internal financial and operational control systems are developed and maintained on an ongoing basis in order to provide reasonable assurance regarding:

- The effectiveness and efficiency of operations;
- The safeguarding of the Bank's assets;
- Compliance with applicable laws and regulations;

RISK MANAGEMENT AND INTERNAL CONTROL (CONTINUED)

- The reliability of accounting records;
- Business sustainability under normal as well as adverse conditions; and
- Responsible behaviors towards all stakeholders.

The efficiency of any internal control system is dependent on the strict observance of prescribed measures. There is always a risk of non-compliance of such measures by staff. Whilst no system of internal control can provide absolute assurance against misstatement or losses, the Bank's system designed to provide the Board with reasonable assurance that the procedures in place are operating effectively. The Board assessed the internal control systems throughout the financial year ended 31 December 2020 and is of the opinion that they met acceptable criteria.

The Board carries risk and internal control assessment through the Audit and Risk Committees.

SOLVENCY

The Board confirms that applicable accounting standards have been followed and that the financial statements have been prepared on a going concern basis. The Board of Directors has reasonable expectation that the Bank has adequate resources to continue in operational existence for the fore seeable future.

As at 31 December 2020, the Bank stands in a negative liquidity position of TZS 16.6 billion for the assets and liabilities maturing in three months. This mainly results from borrowings payable to shareholder of the Bank, FINCA Microfinance Holding Bank LLC amounting to TZS 12.4 billion by which as at 31 December 2020, TZS 11.2 billion is maturing by 31 March 2021. Subsequent to year end, the shareholders of the Bank approved capital injection through borrowing conversion amounting to TZS 3.2 billion from February 2021 to August 2021. Up to the date of signing the financial statements TZS 1.4 billion had already been converted in line with the conversion forecast. In addition to that, the shareholders further approved to extend loan tenor for TZS 2.3 billion of the same borrowing to April 2022 to regularize the gap.

Accordingly, the financial statements are prepared on the basis of accounting policies applicable to a going concern.

EMPLOYEES' WELFARE

Management and Employees' Relationship

Relationship between employees and management continued to be cordial for the year 2020. There were no unresolved complaints received by management from the employees during the year. A healthy relationship continues to exist between management and the employee. The Bank is an equal opportunity employer. It gives equal access to employment opportunities and ensures that the best available person is appointed to any given position free from discrimination of any kind and without regard to factors like gender, marital status, tribes, religion and disability, which does not impair ability to discharge duties.

Training Facilities

Training programs have been and are continually being developed to ensure employees are adequately trained at all levels. All employees have some form of annual training to upgrade skills and enhance development both individually and as a group, with the goal to benefit both the organization and employees.
During the year the Bank spent TZS 38.8 million for staff training in order to improve employees' technical skills and hence effectiveness (2019: TZS 39 million).

Medical Assistance

All members of staff with a maximum number of four beneficiaries (dependents) for each employee were availed medical insurance. The Bank used National Health Insurance Fund (NHIF) as medical insurer during the year.

EMPLOYEES' WELFARE (CONTINUED)

Health and Safety

A safe working environment is ensured for all employees and contractors by providing adequate and proper personal protective equipment, training and supervision as necessary.

Financial Assistance to Staff

Loans are available to all confirmed employees depending on the assessment and the discretion of management as to the need and circumstances. Management has established a policy that provides loans to staff and these loans are limited by the size of the loan portfolio.

Persons with Disabilities

Applications for employment by disabled persons are always considered, bearing in mind the aptitudes of the applicant concerned. In the event of members of staff becoming disabled, the Bank makes necessary efforts to ensure that the respective staff's employment with the Bank continues and appropriate training is arranged. It is the policy of the Bank that training, career development and promotion of disabled persons should, as far as possible, be identical to that of other employees.

Employees Benefit Plan

All eligible employees are members of the National Social Security Fund (NSSF). The fund is a defined contribution pension scheme with the Bank having no legal or constructive obligation to pay further top-up contributions.

GENDER PARITY

The Bank had 283 employees, out of which 138 were female and 145 were male (2019: 411 employees).

RELATED PARTY TRANSACTIONS

All related party transactions and balances are disclosed in note 28 to these financial statements.

POLITICAL AND CHARITABLE DONATIONS

The Bank did not make any political or charitable donations during the year (2019: Nil).

ENVIRONMENTAL CONTROL PROGRAMME

The Bank subscribes to sustainable protection of the environment and as such always ensures that it does business with customers who observe laws of the country with respect to the protection of the environment.

AUDITORS

The auditor, KPMG have expressed their willingness to continue in office. A resolution proposing the appointment of auditor of the Bank for the financial year 2021 will be tabled at the Annual General Meeting.

BY ORDER OF THE BOARD

Monica Joseph
Director

Mary Pascal Mabiti
Director

12 April 2021

STATEMENT OF DIRECTORS' RESPONSIBILITIES

The Directors are responsible for the preparation and fair presentation of the financial statements of FINCA microfinance Bank Limited comprising the statement of financial position at 31 December 2020, and the statements of profit or loss and other comprehensive income, changes in equity and cash flows for the year then ended, and the notes to the financial statements, which include a summary of significant accounting policies and other explanatory notes, and the directors' report, in accordance with International Financial Reporting Standards and in the manner required by the Companies Act, 2002 as well as the Banking and Financial Institutions Act, 2006.

The Directors are also responsible for such internal control as the directors determine is necessary to enable the preparation of financial statements that are free from material misstatement, whether due to fraud or error, and for maintaining adequate accounting records and an effective system of risk management.

The Auditors are responsible for reporting on whether the annual financial statements are fairly presented in accordance with the applicable financial reporting framework.

As at 31 December 2020, the Bank stands in a negative liquidity position of TZS 16.6 billion for the assets and liabilities maturing in three months. This mainly results from borrowings payable to shareholder of the Bank, FINCA Microfinance Holding Bank LLC amounting to TZS 12.4 billion by which as at 31 December 2020, TZS 11.2 billion is maturing by 31 March 2021. Subsequent to year end, the shareholders of the Bank approved capital injection through borrowing conversion amounting to TZS 3.2 billion from February 2021 to August 2021. Up to the date of signing the financial statements TZS 1.4 billion had already been converted in line with the conversion forecast. In addition to that, the shareholders further approved to extend loan tenor for TZS 2.3 billion of the same borrowing to April 2022 to regularize the gap.

The Directors have made an assessment of the ability of the Bank to continue as going concern and have no reason to believe that the business will not be a going concern at least for the next twelve months from the date of approval of these financial statements.

Approval of financial statements

The financial statements of FINCA Microfinance Bank Limited as identified in the first paragraph, were approved and authorised for issue by the board of directors on 12-04-2021 and signed by:

Monica Joseph
Director

Mary Pascal Mabiti
Director

DECLARATION OF THE HEAD OF FINANCE
FOR THE YEAR ENDED 31 DECEMBER 2020

The National Board of Accountants and Auditors (NBAA) according to the power conferred under the Auditors and Accountants (Registration) Act. No. 33 of 1972, as amended by Act No. 2 of 1995, requires financial statements to be accompanied with a declaration issued by the Head of Finance responsible for the preparation of financial statements of the entity concerned.

It is the duty of a Professional Accountant to assist the Board of Directors to discharge the responsibility of preparing financial statements of an entity showing true and fair view of the entity position and performance in accordance with applicable International Financial Reporting Standards and statutory financial reporting requirements. Full legal responsibility for the preparation of financial statements rests with the Directors as under Directors Responsibility statement on an earlier page.

I, **Deusdedith Edward Mulindwa**, being the Head of finance of FINCA Microfinance Bank Limited hereby acknowledge my responsibility of ensuring that financial statements for the year ended 31 December 2020 have been prepared in compliance with applicable accounting standards and statutory requirements.

I thus confirm that the financial statements comply with applicable accounting standards and statutory requirements as on that date and that they have been prepared based on properly maintained financial records.

Deusdedith Edward Mulindwa
Head of Finance

NBAA Membership No.: ACPA 3834

12 April 2021

KPMG
Certified Public Accountants
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INDEPENDENT AUDITOR'S REPORT TO THE SHAREHOLDERS OF FINCA MICROFINANCE BANK LIMITED

Report on the Audit of the Financial Statements

Opinion

We have audited the financial statements of Finca Microfinance Bank Limited ("the Bank") set out on pages 14 to 70, which comprise the statement of financial position as at 31 December 2020, and the statement of profit or loss and other comprehensive income, statement of changes in equity and statement of cash flows for the year then ended, and notes to the financial statements, including a summary of significant accounting policies and other explanatory information.

In our opinion, the accompanying financial statements give a true and fair view of the financial position of Finca Microfinance Bank Limited as at 31 December 2020, and of its financial performance and its cash flows for the year then ended in accordance with International Financial Reporting Standards (IFRS) and in the manner required by the Companies Act, 2002 and Banking and Financial Institutions Act, 2006.

Basis for Opinion

We conducted our audit in accordance with International Standards on Auditing (ISAs). Our responsibilities under those standards are further described in the *Auditor's responsibilities for the audit of the financial statements* section of our report. We are independent of the Bank in accordance with International Ethics Standards Board for Accountants' *International Code of Ethics for Professional Accountants (including International Independence Standards) (IESBA Code)* together with the ethical requirements that are relevant to our audit of the financial statements in Tanzania, and we have fulfilled our other ethical responsibilities in accordance with these requirements and the IESBA Code. We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our opinion.

Key Audit Matters

Key audit matters are those matters that, in our professional judgment, were of most significance in our audit of the financial statements of the current period. These matters were addressed in the context of our audit of the financial statements as a whole, and in forming our opinion thereon, and we do not provide a separate opinion on these matters.

KPMG

INDEPENDENT AUDITOR'S REPORT TO THE SHAREHOLDERS OF FINCA MICROFINANCE BANK LIMITED (CONTINUED)

Report on the Audit of the Financial Statements (Continued)

Key Audit Matters (Continued)

<table>
<tr><th colspan="2">Impairment on loans and advances to customers – Refer to Note 6(b) and Note 19 to the financial statements</th></tr>
<tr><th>The key matter</th><th>How the matter was addressed in our audit</th></tr>
<tr><td>
Loans and advances to customers amounted to TZS 37,394 million as at 31 December 2020 and the total impairment allowance (expected credit losses (ECL)) amounted to TZS 5,067 million.
Measurement of impairment losses on loans and advances to customers is deemed a key audit matter as the determination of expected credit losses is highly subjective as it involves significant level of judgement applied by management and is a significant estimate.
The key areas where we identified significant levels of management judgement and therefore increased levels of audit focus on the Bank's impairment charge on loans and advances to customers are:
— Quantitative and qualitative criteria used in determining criteria for significant increase in credit risk and default for classification of loans and advances to customers;
— Inherently judgmental modelling is used to estimate ECL which involves determination of probabilities of default (PD), exposures at default (EAD) and loss given default (LGD) and ultimately measurement of Expected Credit Loss ("ECL");
— Establishing the number and relative weightings of forward-looking scenarios;
— Management overlays applied in response to the impact of Covid-19 to the bank portfolio;
— Estimation of cash flows from collateral realisation for secured facilities used in the determination of loss given default; and
— Estimation of time to recovery from the sale of collateral for secured facilities used in the determination of loss given default, collateral depreciation factor.
</td><td>
Our audit procedures in this area included:
— Obtaining an understanding of the credit management processes and assessing the design and operating effectiveness of controls over the credit review processes, approval of external collateral valuation vendors and review of controls over the approval of impairment;
— Assessing reasonableness and reliability of data inputs used for estimating probability of default and loss given default by evaluating the accuracy and completeness of monthly loan balances used in the computation of impairment and accuracy of collateral values used in establishing loss given default;
— Involving Financial Risk Management specialists in challenging management's selection of macroeconomic variables by inspecting results of regression analysis between the macroeconomic variables. Macro-economic variables selected in this case was Consumer Price Index ("CPI") and the Gross Domestic Product ("GDP");
— Evaluating the model documentation in line with the IFRS 9 model to understand the methodology applied on the computation of the PD as per the client methodology in comparison to the recomputed.
— Selecting a sample from the Bank's loan book at the reporting date and assessing whether the sampled facilities are correctly staged and valued based on IFRS 9 as well as regulatory considerations;
— Evaluating key assumptions impacting ECL calculations to assess accuracy and the reasonableness; such assumptions include the recovery rate for various collateral types held, realisation period, cure rate assumption, collateral depreciation factor, definition of default, discount factor and significant increase in credit risk by performing a retrospective in consideration with the current economic trends;
— Evaluating management method of determining groups of similar financial assets for purposes of measuring ECL to confirm that assets are properly stratified based on shared credit risk; and
— Evaluating the adequacy of financial statements disclosures in accordance with the requirements of IFRS 9, Financial Instruments, including disclosures of key assumptions and judgements relating to ECL.
</td></tr>
</table>

INDEPENDENT AUDITOR'S REPORT TO THE SHAREHOLDERS OF FINCA MICROFINANCE BANK LIMITED (CONTINUED)

Report on the Audit of the Financial Statements (Continued)

Other Information

The Directors are responsible for the other information. The other information comprises the information included in the document titled Finca Microfinance Bank Limited Annual Reports and Financial Statements 31 December 2020, but does not include the financial statements and our auditor's report thereon.

Our opinion on the financial statements does not cover the other information and we do not express any form of assurance conclusion thereon.

In connection with our audit of the financial statements, our responsibility is to read the other information and, in doing so, consider whether the other information is materially inconsistent with the financial statements or our knowledge obtained in the audit, or otherwise appears to be materially misstated. If, based on the work we have performed, we conclude that there is a material misstatement of this other information, we are required to report that fact. We have nothing to report in this regard.

Responsibilities of the Directors for the Financial Statements

The Directors are responsible for the preparation of financial statements that give a true and fair view in accordance with IFRSs and in the manner required by the Companies Act, 2002 and Banking and Financial Institutions Act, 2006, and for such internal control as the Directors determine is necessary to enable the preparation of financial statements that are free from material misstatement, whether due to fraud or error.

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

Auditor's Responsibilities for the Audit of the Financial Statements

Our objectives are to obtain reasonable assurance about whether the financial statements as a whole are free from material misstatement, whether due to fraud or error, and to issue an auditor's report that includes our opinion. Reasonable assurance is a high level of assurance but is not a guarantee that an audit conducted in accordance with ISAs will always detect a material misstatement when it exists. Misstatements can arise from fraud or error and are considered material if, individually or in the aggregate, they could reasonably be expected to influence the economic decisions of users taken on the basis of these financial statements.

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

- Identify and assess the risks of material misstatement of the financial statements, whether due to fraud or error, design and perform audit procedures responsive to those risks, and obtain audit evidence that is sufficient and appropriate to provide a basis for our opinion. The risk of not detecting a material misstatement resulting from fraud is higher than for one resulting from error, as fraud may involve collusion, forgery, intentional omissions, misrepresentations, or the override of internal control.
- Obtain an understanding of internal control relevant to the audit in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Bank's internal control.
- Evaluate the appropriateness of accounting policies used and the reasonableness of accounting estimates and related disclosures made by the Directors.
- Conclude on the appropriateness of the Directors' use of the going concern basis of accounting and, based on the audit evidence obtained, whether a material uncertainty exists related to events or conditions that may cast significant doubt on the Bank's ability to continue as a going concern. If we conclude that a material uncertainty exists, we are required to draw attention in our auditor's report to the related disclosures in the financial statements or, if such disclosures are inadequate, to modify our opinion. Our conclusions are based on the audit evidence obtained up to the date of our auditor's report. However, future events or conditions may cause the Bank to cease to continue as a going concern.

KPMG

INDEPENDENT AUDITOR'S REPORT TO THE SHAREHOLDERS OF FINCA MICROFINANCE BANK LIMITED (CONTINUED)

Report on the Audit of the Financial Statements (Continued)

Auditor's Responsibilities for the Audit of the Financial Statements (Continued)

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

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

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

Report on Other Legal and Regulatory Requirements

As required by the Companies Act, 2002 we report to you, based on our audit that:

- in our opinion, proper accounting records have been kept by Finca Microfinance Bank Limited;
- the individual accounts are in agreement with the accounting records of the Bank;
- we obtained all the information and explanations which, to the best of our knowledge and belief, are necessary for the purposes of our audit; and
- information specified by the law regarding Directors' emoluments and other transactions with the Bank is disclosed.

As required by Banking and Financial Institutions Act, 2006 and its regulations, we report to you based on our audit, that:

Nothing has come to our attention that causes us to believe that the Bank has not complied with the Banking and Financial Institutions Act, 2006 and its regulations including computation of its capital position. Capital ratios are included in Note 6 (f).

KPMG
Certified Public Accountants (T)

KPMG

Signed by: CPA Vincent Onjala (TACPA 2722)
Dar es Salaam

Date: 12-04-2021

FINCA MICROFINANCE BANK LIMITED

STATEMENT OF PROFIT OR LOSS AND OTHER COMPREHENSIVE INCOME
FOR THE YEAR ENDED 31 DECEMBER 2020

	Notes	2020 TZS '000	2019 TZS '000
Income			
Interest and similar income	7	17,839,857	25,894,925
Interest and similar expense	8	(6,053,530)	(6,607,813)
Net interest income		**11,786,327**	**19,287,112**
Impairment on financial instruments	19(b)(ii)	(5,756,974)	(4,174,464)
Net interest income after loan impairment charge		6,029,353	15,112,648
Fees and commission income	9	4,027,608	6,174,901
Fees and commission expense	10	(286,188)	(562,271)
Net fee and commission income		3,741,420	5,612,630
Net income from lending activities		**9,770,773**	**20,725,278**
Grant income	11	174,536	174,536
Other (losses)/income	12	(355,986)	185,072
Personnel expenses	13	(9,152,708)	(11,888,672)
Operating expenses	14	(6,519,911)	(8,433,323)
Depreciation and amortisation	22,23 & 24	(3,065,391)	(2,776,378)
Loss before tax		**(9,148,687)**	**(2,013,487)**
Income tax expense	15(a)	(110,242)	(5,110,394)
Loss for the year		**(9,258,929)**	**(7,123,881)**
Other comprehensive income		-	-
Total comprehensive loss for the year		**(9,258,929)**	**(7,123,881)**

Notes and related statements forming part of these financial statements appear on pages 18 to 70.

Auditor's report is on page 10 to 13.

FINCA MICROFINANCE BANK LIMITED

STATEMENT OF FINANCIAL POSITION
AS AT 31 DECEMBER 2020

	Notes	2020 TZS '000	2019 TZS '000
ASSETS			
Cash and bank balances	18	7,018,321	5,326,299
Investment in fixed deposits	17	9,245,099	11,589,424
Loans and advances to customers	19(a)	32,327,853	57,195,085
Due from related parties	27	6,951	14,482
Other assets	20	1,910,687	2,129,152
Work in progress	21	38,278	14,716
Property and equipment	22	1,707,590	2,525,282
Right of use asset	23(a)	3,279,045	4,780,539
Intangible assets	24	3,269,656	4,222,185
Total assets		**58,803,480**	**87,797,164**
LIABILITIES AND EQUITY			
LIABILITIES			
Deposits from customers	25	23,910,937	28,386,803
Deposits from banks	25	7,908,411	8,370,887
Borrowings	26	12,396,722	25,895,587
Amounts due to related parties	27	-	109,944
Deferred grants	28	576,836	751,373
Lease liabilities	23(b)	2,882,653	4,057,608
Tax payable	15(d)	95,885	138,492
Other payables	29	3,412,382	5,735,586
Total liabilities		**51,183,826**	**73,446,280**
Capital and reserves			
Share capital	30	34,102,304	31,574,605
Accumulated losses		(27,455,186)	(18,823,271)
Statutory reserve		972,536	1,599,550
Total equity		**7,619,654**	**14,350,884**
Total liabilities and equity		**58,803,480**	**87,797,164**

The financial statements on pages 14 to 70 were approved and authorised for issue by the Board of Directors on 12-04-2021 and were signed on its behalf by:

Monica Joseph
Director

Mary Pascal Mabiti
Director

Notes and related statements forming part of these financial statements appear on pages 18 to 70.
Auditor's report is on page 10 to 13.

STATEMENT OF CHANGES IN EQUITY
FOR THE YEAR ENDED 31 DECEMBER 2020

	Share capital TZS'000	Accumulated losses TZS'000	Regulatory reserve* TZS'000	General Reserve TZS'000	Total TZS'000
At 1 January 2019	**31,574,605**	**(12,208,092)**	**1,586,242**	**522,010**	**21,474,765**
Loss for the year	-	(7,123,881)	-	-	(7,123,881)
General provision reserve	-	522,010	-	(522,010)	-
Regulatory reserve*	-	(13,308)	13,308	-	-
At 31 December 2019	**31,574,605**	**(18,823,271)**	**1,599,550**	**-**	**14,350,884**
At 1 January 2020	**31,574,605**	**(18,823,271)**	**1,599,550**	**-**	**14,350,884**
Transactions with owners of the Bank					
Issue of shares	2,527,699	-	-	-	2,527,699
	34,102,304	**(18,823,271)**	**1,599,550**	**-**	**16,878,583**
Total comprehensive loss for the year					
Loss for the year	-	(9,258,929)	-	-	(9,258,929)
Regulatory reserve*	-	627,014	(627,014)	-	-
At 31 December 2020	**34,102,304**	**(27,455,186)**	**972,536**	**-**	**7,619,654**

*Regulatory reserve represents the surplus of loan provision computed as per Bank of Tanzania regulations over the impairment of loans and advances as per International Financial Reporting Standards. The reserve is not distributable.

Notes and related statements forming part of these financial statements appear on pages 18 to 70.

Auditor's report is on page 10 to 13.

FINCA MICROFINANCE BANK LIMITED

STATEMENT OF CASH FLOWS
FOR THE YEAR ENDED 31 DECEMBER 2020

	Notes	2020	2019
Cash flows from operating activities		**TZS '000**	**TZS '000**
Loss before tax		(9,148,687)	(2,013,487)
Adjustments for:			
Depreciation	22	999,116	1,182,538
Amortisation of intangible assets	24	1,255,608	537,663
Impairment on financial instruments	19(b)(ii)	5,756,974	4,174,464
Depreciation of right of use asset	23(a)	810,667	1,056,177
Grant income	11	(174,536)	(174,536)
Gain on disposal of property and equipment		(946)	(21,654)
Loss on disposal lease assets and liability	23(b)	85,544	-
Interest expense on term loans	8	2,195,251	3,249,177
Interest expense on lease liability	8	506,352	468,611
Write-off of WIP during the year	21	-	41,329
		2,285,343	**8,500,282**
Changes in:			
Decrease/ (increase) in loans and advances to customers		19,185,556	(4,588,866)
Decrease in other assets		182,273	442,803
(decrease)/ Increase in deposits		(4,938,342)	1,678,135
Decrease in other payables		(2,323,206)	(1,372,460)
Income tax paid	15(d)	(152,849)	(382,446)
Interest paid on term loans		(1,814,289)	(3,375,170)
Interest paid on lease liability	23(b)	(152,201)	(428,659)
Net movement in related party balances		(102,413)	109,384
Net cash generated from operating activities		**12,169,872**	**583,003**
Cash flows from investing activities			
Purchase of property and equipment	22	(288,287)	(371,924)
Purchase of intangible assets	24	(175,819)	(82,735)
Purchase of WIP	21	(150,822)	(554,028)
Proceeds from maturity of investment in fixed deposit		2,269,027	-
Proceeds from disposal of property and equipment		107,809	22,390
Net cash used in investing activities		**1,761,908**	**(986,297)**
Cash flows from financing activities			
Borrowings received during the year	26	-	12,016,914
Borrowings repaid during the year	26	(13,879,826)	(20,933,093)
Proceed of deferred grants	28	-	(35,209)
Payment of lease liabilities	23	(887,631)	(1,187,014)
Proceeds from issue of shares		2,527,699	-
Net cash used in financing activities		**(12,239,758)**	**(10,138,402)**
Net decrease in cash and cash equivalents		1,692,022	(10,541,696)
Cash and cash equivalents at beginning of the year		5,326,299	15,867,995
Cash and cash equivalents at the end of the year		**7,018,321**	**5,326,299**
Cash and cash equivalents:			
Cash and bank balance	18	7,018,321	5,326,299
		7,018,321	**5,326,299**

Notes and related statements forming part of these financial statements appear on pages 18 to 70.
Auditor's report is on page 10 to 13

1. REPORTING ENTITY

FINCA Microfinance Bank Limited ("the Bank”) is a Limited liability Bank incorporated in Tanzania under the Companies Act 2002 and domiciled in Tanzania. The microfinance bank licensed under the Banking and Financial Institutions (Microfinance Activities) Regulation, 2014 and regulated by the Bank of Tanzania. Details of the address of its registered office and principal place of business are disclosed on page one whilst its principal activities are described in the report of Directors.

2. BASIS OF PREPARATION

The financial statements have been prepared in accordance with IFRS Standards under the historical cost convention except for certain financial instruments that are measured at revalued amounts or fair values.The principal accounting policies applied in the preparation of these financial statements are set out below. These policies have been consistently applied to all the periods presented, unless otherwise stated.

Going concern

As at 31 December 2020, the Bank stands in a negative liquidity position of TZS 16.6 billion for the assets and liabilities maturing in three months. This mainly results from borrowings payable to shareholder of the Bank, FINCA Microfinance Holding Bank LLC amounting to TZS 12.4 billion by which as at 31 December 2020, TZS 11.2 billion is maturing by 31 March 2021. Subsequent to year end, the shareholders of the Bank approved capital injection through borrowing conversion amounting to TZS 3.2 billion from February 2021 to August 2021. Up to the date of signing the financial statements TZS 1.4 billion had already been converted in line with the conversion forecast. In addition to that, the shareholders further approved to extend loan tenor for TZS 2.3 billion of the same borrowing to April 2022 to regularize the gap.

Statement of compliance

The financial statements of FINCA Microfinance Bank Limited have been prepared in accordance with International Financial Reporting Standards (IFRSs), and in the manner required by the Companies Act, 2002 and Banking and Financial Institutions Act, 2006.

3. FUNCTIONAL AND PRESENTATION CURRENCY

The financial statements are measured using the currency of the primary economic environment in which the Bank operates (“the functional currency”). The financial statements are presented in Tanzania Shillings, which is also the functional currency. All amounts have been rounded to the nearest thousands, except when otherwise indicated.

4. USE OF JUDGEMENTS AND ESTIMATES

In preparing these financial statements, management has made judgements, estimates and assumptions that affect the application of the Bank’s accounting policies and the reported amounts of assets, liabilities, income and expenses. Actual results may differ from these estimates.

Estimates and underlying assumptions are reviewed on an ongoing basis. Revisions to estimates are recognised prospectively.

Judgements

In preparing these financial statements, management has made judgements, estimates and assumptions that affect the application of the Bank’s accounting policies and the reported amounts of assets, liabilities, income and expenses. Actual results may differ from these estimates.

Estimates and underlying assumptions are reviewed on an ongoing basis. Revisions to estimates are recognised prospectively.

4. USE OF JUDGEMENTS AND ESTIMATES (CONTINUED)

A. Judgements

Information about judgements made in applying accounting policies that have the most significant effects on the amounts recognised in the financial statements is included in the following notes.

Note 5 (d)(vi): establishing the criteria for determining whether credit risk on the financial asset has increased significantly since initial recognition, determining the methodology for incorporating forward-looking information into the measurement of ECL and selection and approval of models used to measure ECL.

Notes 5(d)(ii): classification of financial assets: assessment of the business model within which the assets are held and assessment of whether the contractual terms of the financial asset are SPPI on the principal amount outstanding.

B. Assumptions and estimation uncertainties

Information about assumptions and estimation uncertainties that have a significant risk of resulting in a material adjustment in the year ended 31 December 2020 is included in the following notes.

Note 5(d)(vii): Impairment of financial instruments, determination of inputs into the ECL measurement model, including key assumptions used in estimating recoverable cash flows and incorporation of forward-looking information.

Note 5(d)(vi): measurement of the fair value of financial instruments with significant unobservable inputs.

Note 5(e): critical estimates are made by the directors in determining depreciation rates for property and equipment and their residual values. The rates are set out in note 5(e).

The Bank has taken into consideration of COVID19 pandemic by moving all modifications/ restructured loans into Stage 2 and applying forbearance flag on those loans. For those loans which have gone through multiple modifications have been considered as defaults unless it was individually assessed and decided to leave them in Stage 2. Curing period was defined as six consecutive payments with no delays in payments.

5. SIGNIFICANT ACCOUNTING POLICIES

The principal accounting policies used in the preparation of these financial statements are set out below:

(a) Foreign currencies

Foreign currency transactions are translated into the functional currency of an entity using the exchange rates prevailing at the dates of the transactions. Monetary assets and liabilities denominated in foreign currencies are translated into the functional currency at the exchange rate at the reporting date. The foreign currency gain or loss on monetary items is the difference between the amortised cost in the functional currency at the beginning of the year, adjusted for effective interest, impairment and payments during the year, and the amortised cost in the foreign currency translated at the spot exchange rate at the end of the year.

Non-monetary assets and liabilities that are measured at fair value in a foreign currency are translated into the functional currency at the exchange rate when the fair value is determined. Non-monetary items that are measured based on historical cost in a foreign currency are translated at the exchange rate at the date of the transaction.

5. SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

(b) Income recognition

Income is derived substantially, from banking business and related activities and comprises net interest income and fee and commission income.

i) Net interest income

Effective interest rate

Interest income and expense are recognised in profit or loss using the effective interest method. The effective interest rate' is the rate that exactly discounts estimated future cash payments or receipts through the expected life of the financial instrument to:

- the gross carrying amount of the financial asset;
- or the amortised cost of the financial liability.

When calculating the effective interest rate for financial instruments other than purchased or originated credit-impaired assets, the Bank estimates future cash flows considering all contractual terms of the financial instrument, but not Expected Credit Loss (ECL). For purchased or originated credit impaired financial assets, a credit-adjusted effective interest rate is calculated using estimated future cash flows including ECL.

The calculation of the effective interest rate includes transaction costs and fees and points paid or received that are an integral part of the effective interest rate. Transaction costs include incremental costs that are directly attributable to the acquisition or issue of a financial asset or financial liability.

ii) Amortised cost and gross carrying amount

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

The ‘gross carrying amount of a financial asset’ is the amortised cost of a financial asset before adjusting for any expected credit loss allowance.

iii) Calculation of interest income and expense

The effective interest rate of a financial asset or financial liability is calculated on initial recognition of a financial asset or a financial liability. In calculating interest income and expense, the effective interest rate is applied to the gross carrying amount of the asset (when the asset is not credit impaired) or to the amortised cost of the liability. The effective interest rate is revised as a result of periodic re-estimation of cash flows of floating-rate instruments to reflect movements in market rates of interest.

However, for financial assets that have become credit-impaired subsequent to initial recognition, interest income is calculated by applying the effective interest rate to the amortised cost of the financial asset. If the asset is no longer credit-impaired, then the calculation of interest income reverts to the gross basis.

For financial assets that were credit-impaired on initial recognition, interest income is calculated by applying the credit-adjusted effective interest rate to the amortised cost of the asset. The calculation of interest income does not revert to a gross basis, even if the credit risk of the asset improves. For information on when financial assets are credit impaired.

5. SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

(b) Income recognition (Continued)

Presentation

- Interest income calculated using the effective interest method presented in the statement of profit or loss and OCI includes interest on financial assets and financial liabilities measured at amortised cost.
- Interest expense presented in the statement of profit or loss and OCI includes interest on financial liabilities measured at amortised cost.
- Interest income and expense on other financial assets and financial liabilities at FVTPL are presented in net income from other financial instruments at FVTPL.

iv) Net fee and commission income

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

If a loan commitment is not expected to result in the draw-down of a loan, then the related loan commitment fee is recognised on a straight-line basis over the commitment period.

Other fee and commission income – including account servicing fees and sales commissions – is recognised as the related services are performed. If a loan commitment is not expected to result in the draw-down of a loan, then the related loan commitment fee is recognised on a straight-line basis over the commitment period.

A contract with a customer that results in a recognised financial instrument in the bank's financial statements may be partially in the scope of IFRS 9 and partially in the scope of IFRS 15. If this is the case, then the bank first applies IFRS 9 to separate and measure the part of the contract that is in the scope of IFRS 9 and then applies IFRS 15 to the residual.

Other fee and commission expenses relate mainly to transaction and service fees, which are expensed as the services are received.

v) Net trading income

Net trading income comprises gains less losses related to trading assets and liabilities, and includes all fair value changes, interest, dividends and foreign exchange differences.

(c) Leases

At inception of a contract, the Bank assesses whether a contract is, or contains, a lease. A contract is, or contains, a lease if the contract conveys the right to control the use of an identified asset for a period of time in exchange for consideration.

The Bank as a lessee

At commencement or on modification of a contract that contains a lease component, the Bank allocates consideration in the contract to each lease component on the basis of its relative standalone price. However, for leases of branches and office premises the Bank has elected not to separate non-lease components and accounts for the lease and non-lease components as a single lease component.

5. SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

(c) Leases (continued)

The Bank as a lessee (continued)

The Bank recognises a right-of-use asset and a lease liability at the lease commencement date. The right-of-use asset is initially measured at cost, which comprises the initial amount of the lease liability adjusted for any lease payments made at or before the commencement date, plus any initial direct costs incurred and an estimate of costs to dismantle and remove any improvements made to branches or office premises.

The right-of-use asset is subsequently depreciated using the straight-line method from the commencement date to the end of the lease term. In addition, the right-of-use asset is periodically reduced by impairment losses, if any, and adjusted for certain remeasurements of the lease liability.

The lease liability is initially measured at the present value of the lease payments that are not paid at the commencement date, discounted using the interest rate implicit in the lease or, if that rate cannot be readily determined, the Bank's incremental borrowing rate. Generally, the Bank uses its incremental borrowing rate as the discount rate.

The Bank determines its incremental borrowing rate by analysing its borrowings from various external sources and makes certain adjustments to reflect the terms of the lease and type of asset leased.

Lease payments included in the measurement of the lease liability comprise the following:

– fixed payments, including in-substance fixed payments;

– variable lease payments that depend on an index or a rate, initially measured using the index or rate as at the commencement date;

– amounts expected to be payable under a residual value guarantee; and

– the exercise price under a purchase option that the Bank is reasonably certain to exercise, lease payments in an optional renewal period if the Bank is reasonably certain to exercise an extension option, and penalties for early termination of a lease unless the Bank is reasonably certain not to terminate early.

The lease liability is measured at amortised cost using the effective interest method. It is remeasured when there is a change in future lease payments arising from a change in an index or rate, if there is a change in the Bank's estimate of the amount expected to be payable under a residual value guarantee, if the Bank changes its assessment of whether it will exercise a purchase, extension or termination option or if there is a revised in-substance fixed lease payment.

When the lease liability is remeasured in this way, a corresponding adjustment is made to the carrying amount of the right-of-use asset, or is recorded in profit or loss if the carrying amount of the right-of-use asset has been reduced to zero.

From 1 January 2020, where the basis for determining future lease payments changes as required by interest rate benchmark reform, the Bank remeasures the lease liability by discounting the revised lease payments using the revised discount rate that reflects the change to an alternative benchmark interest rate.

The Bank presents right-of-use assets in 'property and equipment' and lease liabilities in 'other liabilities' in the statement of financial position.

5. SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

(c) Leases (continued)

The Bank as a lessee (continued)

Short-term leases and leases of low-value assets

The Bank applies the short-term lease recognition exemption to its short-term leases of machinery and equipment (i.e., those leases that have a lease term of 12 months or less from the commencement date and do not contain a purchase option). It also applies the lease of low-value assets recognition exemption to leases of office equipment that are considered to be low value. Lease payments on short-term leases and leases of low- value assets are recognised as expense on a straight-line basis over the lease term.

(d) Income tax expense

Income tax expense comprises current tax and change in deferred tax. Income tax expense is recognised in profit or loss except to the extent that it relates to items recognised directly in equity or other comprehensive income, in which case it is recognised in equity or in other comprehensive income.

The Bank has determined that interest and penalties related to income taxes, including uncertain tax treatments, do not meet the definition of income taxes, and therefore has accounted for them under IAS 37 Provisions, Contingent Liabilities and Contingent Assets and has recognised the related expenses in 'other expenses'

i) Current tax

Current tax comprises the expected tax payable or receivable on the taxable income or loss for the year and any adjustment to the tax payable or receivable in respect of previous years. The amount of current tax payable or receivable is the best estimate of the tax amount expected to be paid or received that reflects uncertainty related to income taxes, if any. It is measured using tax rates enacted or substantively enacted at the reporting date. Current tax assets and liabilities are offset only if certain criteria are met.

ii) Deferred tax

Deferred tax is recognised on all temporary differences between the carrying amounts of assets and liabilities for financial reporting purposes and the amounts used for taxation purposes, except for:

- temporary differences relating to the initial recognition of assets or liabilities in a transaction that is not a business combination and which affects neither accounting nor taxable profit
- temporary differences related to investments in subsidiaries to the extent that it is probable that they will not reverse in the foreseeable future; and
- taxable temporary differences arising on the initial recognition of goodwill

Deferred tax is measured at the tax rates that are expected to be applied to the temporary differences when they reverse, based on the laws that have been enacted or substantively enacted by the reporting date. A deferred tax asset is recognised only to the extent that it is probable that future taxable profits will be available against which the asset can be utilised.

5. SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

(d) Income tax expense (Continued)

ii) Deferred tax (continued)

The measurement of deferred tax reflects the tax consequences that would follow from the manner in which the Bank expects, at the reporting date, to recover or settle the carrying amount of its assets and liabilities. For this purpose, the carrying amount of investment property measured at fair value is presumed to be recovered through sale, and the Bank has not rebutted this presumption.

Deferred tax assets are recognised for unused tax losses, unused tax credits and deductible temporary differences to the extent that it is probable that future taxable profits will be available against which they can be used. Future taxable profits are determined based on the reversal of relevant taxable temporary differences. If the amount of taxable temporary differences is insufficient to recognise a deferred tax asset in full, then future taxable profits, adjusted for reversals of existing temporary differences, are considered, based on business plans for individual the Bank. Deferred tax assets are reviewed at each reporting date and are reduced to the extent that it is no longer probable that the related tax benefit will be realised; such reductions are reversed when the probability of future taxable profits improves.

Unrecognised deferred tax assets are reassessed at each reporting date and recognised to the extent that it has become probable that future taxable profits will be available against which they can be used.

Deferred tax assets and liabilities are offset if there is a legally enforceable right to offset current tax liabilities against current tax assets and they relate to income taxes levied by the same tax authority on the same taxable entity or on different tax entities, but they intend to settle current tax assets and liabilities on a net basis or their tax assets and liabilities will be realized simultaneously.

(e) Financial assets and liabilities

i) Recognition and initial measurement

The bank initially recognises loans and advances and deposits on the date at which they are originated. All other financial assets and liabilities are initially recognised on the trade date on which the bank becomes a party to the contractual provision of the assets or liabilities.

A financial asset or liability is initially measured at fair value plus (for an item not subsequently measured at fair value through profit or loss) transaction costs that are directly attributable to its acquisition or issue. Subsequent to initial recognition, financial liabilities (deposits and debt securities) are measured at their amortized cost using the effective interest method.

ii) Classification

On initial recognition, a financial asset is classified as measured at: amortised cost, FVOCI or FVTPL.

A financial asset is measured at amortised cost if it meets both of the following conditions and is not designated as at FVTPL:

— the asset is held within a business model whose objective is to hold assets to collect contractual cash flows; and

5. SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

(e) Financial assets and liabilities (continued)

ii) Classification (continued)

— the contractual terms of the financial asset give rise on specified dates to cash flows that are solely payments of principal and interest on the principal amount outstanding.

A debt instrument is measured at FVOCI only if it meets both of the following conditions and is not designated as at FVTPL:

— the asset is held within a business model whose objective is achieved by both collecting contractual cash flows and selling financial assets; and
— the contractual terms of the financial asset give rise on specified dates to cash flows that are solely payments of principal and interest on the principal amount outstanding.

On initial recognition of an equity investment that is not held for trading, the bank may irrevocably elect to present subsequent changes in fair value in OCI. This election is made on an investment-by-investment basis. All other financial assets are classified as measured at FVTPL.

In addition, on initial recognition, the bank may irrevocably designate a financial asset that otherwise meets the requirements to be measured at amortised cost or at FVOCI as at FVTPL if doing so eliminates or significantly reduces an accounting mismatch that would otherwise arise.

Business model assessment

The bank makes an assessment of the objective of a business model in which an asset is held at a portfolio level because this best reflects the way the business is managed and information is provided to management. The information considered includes:

— the stated policies and objectives for the portfolio and the operation of those policies in practice. In particular, whether management's strategy focuses on earning contractual interest revenue, maintaining a particular interest rate profile, matching the duration of the financial assets to the duration of the liabilities that are funding those assets or realising cash flows through the sale of the assets;
— how the performance of the portfolio is evaluated and reported to the bank's management;
— the risks that affect the performance of the business model (and the financial assets held within that business model) and how those risks are managed;
— how managers of the business are compensated – e.g. whether compensation is based on the fair value of the assets managed or the contractual cash flows collected; and
— the frequency, volume and timing of sales in prior periods, the reasons for such sales and its expectations about future sales activity. However, information about sales activity is not considered in isolation, but as part of an overall assessment of how the bank's stated objective for managing the financial assets is achieved and how cash flows are realised.

Financial assets that are held for trading or managed and whose performance is evaluated on a fair value basis are measured at FVTPL because they are neither held to collect contractual cash flows nor held both to collect contractual cash flows and to sell financial assets.

5. SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

(e) Financial assets and liabilities (continued)

ii) Classification (continued)

Assessment whether contractual cash flows are Solely Payments of Principal and Interest (SPPI Test)

For the purposes of this assessment, ‘principal’ is defined as the fair value of the financial asset on initial recognition. ‘Interest’ is defined as consideration for the time value of money and for the credit risk associated with the principal amount outstanding during a particular period of time and for other basic lending risks and costs (e.g. liquidity risk and administrative costs), as well as profit margin.

In assessing whether the contractual cash flows are solely payments of principal and interest, the bank considers the contractual terms of the instrument. This includes assessing whether the financial asset contains a contractual term that could change the timing or amount of contractual cash flows such that it would not meet this condition. In making the assessment, the bank considers:

— contingent events that would change the amount and timing of cash flows;

— leverage features;

— prepayment and extension terms;

— terms that limit the bank’s claim to cash flows from specified assets (e.g. non-recourse asset arrangements); and

— features that modify consideration of the time value of money – e.g. periodical reset of interest rates.

The bank holds a portfolio of long-term fixed rate loans for which the bank has the option to propose to revise the interest rate at periodic reset dates. These reset rights are limited to the market rate at the time of revision. The borrowers have an option to either accept the revised rate or redeem the loan at par without penalty.

The bank has determined that the contractual cash flows of these loans are solely payments of principal and interest because the option varies the interest rate in a way that is consideration for the time value of money, credit risk, other basic lending risks and costs associated with the principal amount outstanding.

The Bank’s financial assets classified into the measurement categories are as following;

Financial assets	Business Model	SPPI	Measurement Category
Cash and cash equivalents	Hold to collect contractual cash flows	Cash flows are solely payments of principal and interest	Amortized cost
Loans and advances to banks	Hold to collect contractual cash flows	Cash flows are solely payments of principal and interest	Amortized cost
Loans to customers	Hold to collect contractual cash flows	Cash flows are solely payments of principal and interest	Amortized cost
Investment in fixed deposits	Hold to collect contractual cash flows	Cash flows are solely payments of principal and interest	Amortized cost

Financial assets are not reclassified subsequently to their initial recognition, except in the period after the bank changes its business model for managing financial assets.

5. SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

(e) Financial assets and liabilities (continued)

iii) Derecognition

Financial assets

The Bank derecognises a financial asset when the contractual rights to the cash flows from the financial asset expire or it transfers the rights to receive the contractual cash flows in a transaction in which substantially all of the risks and rewards of ownership of the financial asset are transferred or in which the Bank neither transfers nor retains substantially all of the risks and rewards of ownership and it does not retain control of the financial asset.

On derecognition of a financial asset, the difference between the carrying amount of the asset (or the carrying amount allocated to the portion of the asset derecognised) and the sum of;

(i) the consideration received (including any new asset obtained less any new liability assumed) and
(ii) any cumulative gain or loss that had been recognised in Other Comprehensive Income (OCI) is recognised in profit or loss.

Any cumulative gain or loss recognised in Other Comprehensive Income in respect of equity investment securities designated as at Fair value through other comprehensive income (FVOCI) is not recognised in profit or loss on derecognition of such securities. Any interest in transferred financial assets that qualify for derecognition that is created or retained by the Bank is recognised as a separate asset or liability

When assets are sold to a third party with a concurrent total return swap on the transferred assets, the transaction is accounted for as a secured financing transaction similar to sale-and repurchase transactions, because the Bank retains all or substantially all of the risks and rewards of ownership of such assets.

In transactions in which the Bank neither retains nor transfers substantially all of the risks and rewards of ownership of a financial asset and it retains control over the asset, the Bank continues to recognise the asset to the extent of its continuing involvement, determined by the extent to which it is exposed to changes in the value of the transferred asset.

Financial liabilities

The bank classifies its financial liabilities, other than financial guarantees and loan commitments, as measured at amortised. The Bank derecognises a financial liability when its contractual obligations are discharged or cancelled or expire.

iv) Modifications of financial assets and financial liabilities

Financial assets

If the terms of a financial asset are modified, then the Bank evaluates whether the cash flows of the modified asset are substantially different.

If the cash flows are substantially different, then the contractual rights to cash flows from the original financial asset are deemed to have expired. In this case, the original financial asset is derecognised (see (iii)) and a new financial asset is recognised at fair value plus any eligible transaction costs. Any fees received as part of the modification are accounted for as follows:

5. SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

(e) Financial assets and liabilities (continued)

iv) Modifications of financial assets and financial liabilities (continued)

Financial assets (continued)

– fees that are considered in determining the fair value of the new asset and fees that represent reimbursement of eligible transaction costs are included in the initial measurement of the asset; And
– other fees are included in profit or loss as part of the gain or loss on derecognition.

If cash flows are modified when the borrower is in financial difficulties, then the objective of the modification is usually to maximise recovery of the original contractual terms rather than to originate a new asset with substantially different terms. If the Bank plans to modify a financial asset in a way that would result in forgiveness of cash flows, then it first considers whether a portion of the asset should be written off before the modification takes place (see below for write-off policy). This approach impacts the result of the quantitative evaluation and means that the derecognition criteria are not usually met in such cases.

If the modification of a financial asset measured at amortised cost or FVOCI does not result in derecognition of the financial asset, then the Bank first recalculates the gross carrying amount of the financial asset using the original effective interest rate of the asset and recognises the resulting adjustment as a modification gain or loss in profit or loss. For floating-rate financial assets, the original effective interest rate used to calculate the modification gain or loss is adjusted to reflect current market terms at the time of the modification. Any costs or fees incurred and modification fees received adjust the gross carrying amount of the modified financial asset and are amortised over the remaining term of the modified financial asset

If such a modification is carried out because of financial difficulties of the borrower (see (vii)), then the gain or loss is presented together with impairment losses. In other cases, it is presented as interest income calculated using the effective interest rate method (see (b)).

Financial liabilities

The Bank derecognises a financial liability when its terms are modified and the cash flows of the modified liability are substantially different. In this case, a new financial liability based on the modified terms is recognised at fair value. The difference between the carrying amount of the financial liability derecognised and the consideration paid is recognised in profit or loss. Consideration paid includes non-financial assets transferred, if any, and the assumption of liabilities, including the new modified financial liability.

If the modification of a financial liability is not accounted for as derecognition, then the amortised cost of the liability is recalculated by discounting the modified cash flows at the original effective interest rate and the resulting gain or loss is recognised in profit or loss. Any costs and fees incurred are recognised as an adjustment to the carrying amount of the liability and amortised over the remaining term of the modified financial liability by re-computing the effective interest rate on the instrument.

Interest rate benchmark reform (policy applied from 1 January 2020)

If the basis for determining the contractual cash flows of a financial asset or financial liability measured at amortised cost changes as a result of interest rate benchmark reform, then the Bank updates the effective interest rate of the financial asset or financial liability to reflect the change that is required by the reform. A change in the basis for determining the contractual cash flows is required by interest rate benchmark reform if the following conditions are met:

5. SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

(e) Financial assets and liabilities (continued)

iv) Modifications of financial assets and financial liabilities (continued)

Financial assets (continued)

– the change is necessary as a direct consequence of the reform; and

– the new basis for determining the contractual cash flows is economically equivalent to the previous basis – i.e. the basis immediately before the change.

If changes are made to a financial asset or financial liability in addition to changes to the basis for determining the contractual cash flows required by interest rate benchmark reform, then the Bank first updates the effective interest rate of the financial asset or financial liability to reflect the change that is required by interest rate benchmark reform. After that, the Bank applies the policies on accounting for modifications set out above to the additional changes.

v) Offsetting

Financial assets and financial liabilities are offset, and the net amount presented in the statement of financial position when, and only when, the Bank currently has a legally enforceable right to set off the amounts and it intends either to settle them on a net basis or to realise the asset and settle the liability simultaneously.

Income and expenses are presented on a net basis only when permitted under IFRS Standards, or for gains and losses arising from a group of similar transactions such as in the Bank's trading activity.

vi) Fair value measurement

Fair value' is the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date in the principal or, in its absence, the most advantageous market to which the Bank has access at that date. The fair value of a liability reflects its non-performance risk.

When one is available, the Bank measures the fair value of an instrument using the quoted price in an active market for that instrument. A market is regarded as 'active' if transactions for the asset or liability take place with sufficient frequency and volume to provide pricing information on an ongoing basis.

If there is no quoted price in an active market, then the Bank uses valuation techniques that maximise the use of relevant observable inputs and minimise the use of unobservable inputs. The chosen valuation technique incorporates all of the factors that market participants would take into account in pricing a transaction.

The best evidence of the fair value of a financial instrument on initial recognition is normally the transaction price – i.e. the fair value of the consideration given or received. If the Bank determines that the fair value on initial recognition differs from the transaction price and the fair value is evidenced neither by a quoted price in an active market for an identical asset or liability nor based on a valuation technique for which any unobservable inputs are judged to be insignificant in relation to the difference, then the financial instrument is initially measured at fair value, adjusted to defer the difference between the fair value on initial recognition and the transaction price.

5. SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

(e) Financial assets and liabilities (continued)

vi) Fair value measurement (continued)

Subsequently, that difference is recognised in profit or loss on an appropriate basis over the life of the instrument but no later than when the valuation is wholly supported by observable market data or the transaction is closed out.

If an asset or a liability measured at fair value has a bid price and an ask price, then the Bank measures assets and long positions at a bid price and liabilities and short positions at an ask price.

Portfolios of financial assets and financial liabilities that are exposed to market risk and credit risk that are managed by the Bank on the basis of the net exposure to either market or credit risk are measured on the basis of a price that would be received to sell a net long position (or paid to transfer a net short position) for the particular risk exposure.

Portfolio-level adjustments – e.g. bid-ask adjustment or credit risk adjustments that reflect the measurement on the basis of the net exposure – are allocated to the individual assets and liabilities on the basis of the relative risk adjustment of each of the individual instruments in the portfolio.

The fair value of a financial liability with a demand feature (e.g. a demand deposit) is not less than the amount payable on demand, discounted from the first date on which the amount could be required to be paid.

The Bank recognises transfers between levels of the fair value hierarchy as of the end of the reporting period during which the change has occurred.

vii) Impairment

The bank recognises loss allowances Expected Credit Losses (“ECL”) on the following financial instruments that are not measured at FVTPL:

- financial assets that are debt instruments;
- lease receivables;
- financial guarantee contracts issued; and
- loan commitments issued.

The Bank recognises loss allowances at an amount equal to lifetime ECLs, except for the following cases;

- for which the amount recognised will be 12-month ECLs.
- Other financial instruments for which credit risk has not increased significantly since initial recognition.

The impairment requirements of IFRS 9 are complex and require management judgements, estimates and assumptions, particularly in the following areas, which are discussed in details below:

- assessing whether the credit risk of an instrument has increased significantly since initial recognition; and
- incorporating forward-looking information into the measurement of ECLs

12-month ECL are the portion of ECL that result from default events on a financial instrument that are possible within the 12 months after the reporting date. Financial instruments for which a 12-month ECL is recognised are referred to as ‘Stage 1 financial instruments.

5. SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

(e) Financial assets and liabilities (continued)

vii) Impairment (Continued)

Financial instruments allocated to Stage 1 have not undergone a significant increase in credit risk since initial recognition and are not credit-impaired.

Lifetime ECL are the ECL that result from all possible default events over the expected life of the financial instrument or the maximum contractual period of exposure. Financial instruments for which lifetime ECL are recognised but that are not credit-impaired are referred to as ‘Stage 2 financial instruments’. Financial instruments allocated to Stage 2 are those that have experienced a significant increase in credit risk since initial recognition but are not credit-impaired.

Financial instruments for which lifetime ECL are recognised and that are credit-impaired are referred to as ‘Stage 3 financial instruments’.

Measurement of expected credit loss allowance

ECL are a probability-weighted estimate of credit losses. They are measured as follows:

– financial assets that are not credit-impaired at the reporting date: as the present value of all cash shortfalls (i.e. the difference between the cash flows due to the entity in accordance with the contract and the cash flows that the Bank expects to receive).

– financial assets that are credit-impaired at the reporting date: as the difference between the gross carrying amount and the present value of estimated future cash flows.

When discounting future cash flows, the following discount rates are used:

– financial assets other than purchased or originated credit-impaired (POCI) financial assets; the original effective interest rate or an approximation thereof;

– POCI assets: a credit-adjusted effective interest rate; and

Measurement of ECL is affected by the number of factors including how the Bank define certain terms referred into the standards as well as inputs used in measuring ECL. Below is the discussion of some of the key terms that will affect measurement of ECL as well discussion of key inputs to the ECL model.

Definition of default

Under IFRS 9, the Bank considers at a minimum both quantitative and qualitative information to determine financial asset that are in default. For term loans, the borrower who is more than 90 days past due will generally be regarded as being in default. Overdrafts are generally considered past due once the customer has breached an advised limit. This approach is largely consistent with the definition that is required by the Bank of Tanzania, the regulator.

Significant increase in credit risk

Under IFRS 9, when determining whether the credit risk (i.e. risk of default) on financial instrument has increased significantly since initial recognition, the Bank considers reasonable and supportable information that is relevant and available without undue cost or effort, including both quantitative and qualitative information and analysis based on the Bank’s historical experience, expert credit assessment and forward-looking information.

5. SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

(e) Financial assets and liabilities (continued)

vi) Impairment (Continued)

Significant increase in credit risk (continued)

Assessing whether credit risk has increased significantly since initial recognition of a financial instrument requires identifying the date of initial recognition of the instrument. For certain facilities e.g. overdraft, the date when the facility was first entered could be a long time ago. Modifying/restructuring the contractual terms of financial instrument may also affect this assessment.

Credit risk grade

The Bank allocates each exposure to a credit risk grade based on a variety of data that is determined to be predictive of the risk of default and applying experienced credit judgement. At transition, the Bank puts financial instruments without significant increase in credit risk in the 12-months ECL bucket irrespective of the obligor's credit risk rating at origination. However, where significant increase in credit risk has been observed, such credits shall be moved to Lifetime ECL. This is in line with the guidance issued by the Bank of Tanzania.

Restructured / Modified financial assets

If the terms of a financial asset are renegotiated or modified or an existing financial asset is replaced with a new one due to financial difficulties of the borrower, then an assessment is made of whether the financial asset should be derecognised (see (iv)) and ECL are measured as follows.

– If the expected restructuring will not result in derecognition of the existing asset, then the expected cash flows arising from the modified financial asset are included in calculating the cash shortfalls from the existing asset.

– If the expected restructuring will result in derecognition of the existing asset, then the expected fair value of the new asset is treated as the final cash flow from the existing financial asset at the time of its derecognition. This amount is included in calculating the cash shortfalls from the existing financial asset that are discounted from the expected date of derecognition to the reporting date using the original effective interest rate of the existing financial asset.

When the terms of financial assets are modified and the modification does not result in de-recognition, the determination of whether to the asset's credit risk has increased significantly is affected by the stage it was at the time of the modification. Financial assets restructured while under lifetime ECL shall not be moved to 12-months ECL unless it complies with the requirements of staging and migration referred and credit risk grade paragraph above. For financial assets which have been restructured while under 12-months ECL and there is evidence of significant increase credit risk the Bank treat those assets as originated credit impaired financial asset. This policy is in line with the Bank of Tanzania requirement.

Inputs into measurement of ECLs

The key inputs into measurement of ECL are like to be the term structure of the following variables which are derived from internally developed statistical models and other historical data that leverage Bank of Tanzania impairment requirements. The inputs are adjusted to reflect forward-looking information as described below;

5. SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

(e) Financial assets and liabilities (continued)

vii) Impairment (Continued)

Inputs into measurement of ECLs (continued)

Probability of Default (PD): PD are estimates at a certain date, which are calculated based on statistical models. The statistical model has been based on internally compiled data comprising both quantitative and qualitative factors. Where it is available, market data may also be used to derive the PD of certain customers. For portfolio in respect of which the Bank has limited historical data, external benchmark information has been used to supplement internally available data.

Loss given default (LGD): LGD is the magnitude of the likely loss if there is a default. The Bank estimates LGD parameters based on the history of recovery rates of claims against defaulted counterparties. The LGD models consider among others, the structure, and collateral, seniority of claims, counterparty industry and recovery costs of any collateral that is integral to the financial asset. Further, the Bank considers forecasts of future collateral valuations (including expected sale discount), time to realisation of collateral (and other recoveries), allocation of collateral across exposures where there are several exposures to the same borrower, recovery rates, haircuts, type of collateral and external costs of realisation of collateral in line with The Bank of Tanzania requirements.

Exposure at Default (EAD): EAD represents the expected exposure in the event of a default. The Bank derives EAD from the current exposure to the counterparty and potential changes to the current amount allowed under the contract including amortisation and prepayments. EAD of financial asset will be the gross carrying amount at default. For lending commitments and financial guarantees, the EAD considers the amount drawn, as well as potential future amounts that may be drawn or repaid under the contract which is been estimated based on historical observations and forward-looking forecast. The EAD is also in line with the Bank of Tanzania requirements.

As described above and subject to using a maximum of a 12-month PD for financial assets for which credit risk has not significantly increased, the Bank measures ECLs considering the risk of default over the maximum contractual period (including any borrower's extension options) over which it is exposed to credit risk, even if for risk management purpose the Bank considers a longer period.

Where modelling of a parameter is carried out on a collective basis, the financial instruments are grouped on the basis of shared risk characteristics that include industry, instrument type, collateral type and remaining term to maturity. The groupings are subject to regular review to ensure that the exposures within a particular group remain appropriately homogenous.

Incorporating Forward-looking information

Under IFRS 9, the Bank incorporates forward-looking information into both its assessment of whether the credit risk of an instrument has increased significantly since initial recognition and its measurement of ECLs. The Bank shall take into consideration the impact of Macroeconomic factors on how they relate to the inputs into ECLs models and how they impact them.

The Bank formulates one economic scenario, a base case as the there was no possibility of obtaining the other scenarios without undue cost and efforts. The base case is aligned with information used by the Bank for other purposes such as strategic planning and budgeting. External information considered includes economic data and forecasts published by governmental bodies and monetary authorities in the countries where the Bank operates, supranational organisations such as the OECD and the International Monetary Fund and selected the National Bureau of statistics.

5. SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

(e) Financial assets and liabilities (continued)

viii) Impairment (Continued)

Inputs into measurement of ECLs (continued)

Incorporating Forward-looking information (continued)

A comprehensive review is performed at least annually on the design of the scenario by a panel of experts that advises the Bank's senior management.

The Bank has identified and documented key drivers of credit risk and credit losses for each portfolio of financial instruments and, using an analysis of historical data, has estimated relationships between macro-economic variables and credit risk and credit losses. The key driver for credit risk for wholesale portfolios is GDP growth.

Year	2019	2020	2021	2022	2023
GDP-Base case	6.875	7.55	5.70%	6.10%	6.10%

COVID 19 Consideration

The Bank assessed the impact of COVID 19 pandemic since its confirmation in Tanzania in March 2020 and introduced measures to safeguard the business. The pandemic affected the business adversely where most of the customers business were affected which increased Non-performing loans and reduced disbursement significantly. The Bank witnessed the increase of the number of restructured loans which are captured by the ECL computation model.

Thus, the Bank has performed stress testing to assess the possible impact of COVID 19 pandemic for the foreseeable future and included the results in ECL computation model. The results includes low expected disbursement and low quality of disbursed loans which has increased the probability of default hence affected ECL computation.

Credit-impaired financial assets

At each reporting date, the bank assesses whether financial assets carried at amortised cost and debt financial assets carried at FVOCI are credit-impaired (referred to as stage 3 financial assets). A financial asset is 'credit-impaired' when one or more events that have a detrimental impact on the estimated future cash flows of the financial asset have occurred.

Evidence that a financial asset is credit-impaired includes the following observable data:

- significant financial difficulty of the borrower;
- a breach of contract such as a default or past due event;
- the restructuring of a loan or advance by the bank on terms that the bank would not consider otherwise;

5. SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

(e) Financial assets and liabilities (continued)

vi) Impairment (Continued)

Incorporating Forward-looking information (Continued)

Credit-impaired financial assets (continued)

- it is becoming probable that the borrower will enter bankruptcy or other financial reorganisation; or
- the disappearance of an active market for a security because of financial difficulties.

A loan that is overdue for 90 days or more is considered impaired. In addition, a loan that has been renegotiated due to a deterioration in the borrower's condition is usually considered to be credit-impaired unless there is evidence that the risk of not receiving contractual cash flows has reduced significantly and there are no other indicators of impairment.

Presentation of allowance for ECL in the statement of financial position

Loss allowances for ECL are presented in the statement of financial position as follows:

- financial assets measured at amortised cost: as a deduction from the gross carrying amount of the assets;
- debt instruments measured at FVOCI: no loss allowance is recognised in the statement of financial position because the carrying amount of these assets is their fair value. However, the loss allowance is disclosed and is recognised in the fair value reserve.

Write-off

Financial assets at both amortised and FVOCI are written off (either partially or in full) when there is no realistic prospect of recovery. This is generally the case when the bank determines that the borrower does not have assets or sources of income that could generate sufficient cash flows to repay the amounts subject to the write-off. However, financial assets that are written off could still be subject to enforcement activities in order to comply with the bank's procedures for recovery of amounts due.

vii) Designation at fair value through profit or loss (FVTPL)

Financial assets

On initial recognition, the Bank has designated certain financial assets as at FVTPL because this designation eliminates or significantly reduces an accounting mismatch, that would otherwise arise.

Financial liabilities

The Bank has designated certain financial liabilities as at FVTPL in either of the following circumstances:

– the liabilities are managed, evaluated and reported internally on a fair value basis; or
– the designation eliminates or significantly reduces an accounting mismatch that would otherwise arise.

Note 16 sets out the amount of each class of financial asset or financial liability that has been designated as at FVTPL. A description of the basis for each designation is set out in the note for the relevant asset or liability class.

5. SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

(f) Property and Equipment

i) Recognition and measurement

Items of property and equipment are measured at cost less accumulated depreciation and any accumulated impairment losses.

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

If significant parts of an item of property and equipment have different useful lives, then they are accounted for as separate items (major components) of property and equipment.

Any gain or loss on disposal of an item of property and equipment is recognised within other income in profit or loss.

ii) Subsequent costs

The cost of replacing part of an item of property or equipment is recognised in the carrying amount of the item if it is probable that the future economic benefits embodied within the part will flow to the Bank and its cost can be measured reliably. The costs of the day-to-day serving of property and equipment are recognised in profit or loss as incurred.

iii) Depreciation

Depreciation is recognised in profit or loss on a straight-line basis over the estimated useful lives of each part of an item of property and equipment. Leased assets are depreciated over the shorter of the lease term and their useful lives. Land is not depreciated. The estimated useful lives for the current and comparative periods are as stated:

Leasehold improvement over the term of the lease

Furniture and fittings, Motor vehicles and Computer equipment are depreciated at 5 years

(g) Intangible assets

Software

Software acquired by the Bank is measured at cost less accumulated amortisation and any accumulated impairment losses. Expenditure on internally developed software is recognised as an asset when the Bank is able to demonstrate: that the product is technically and commercially feasible, its intention and ability to complete the development and use the software in a manner that will generate future economic benefits, and that it can reliably measure the costs to complete the development. The capitalised costs of internally developed software include all costs directly attributable to developing the software and capitalised borrowing costs and are amortised over its useful life. Internally developed software is stated at capitalised cost less accumulated amortisation and any accumulated impairment losses.

Subsequent expenditure on software assets is capitalised only when it increases the future economic benefits embodied in the specific asset to which it relates. All other expenditure is recognised in profit or loss as it is incurred.

5. SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

(g) Intangible assets (continued)

Software is amortised on a straight-line basis in profit or loss over its estimated useful life, from the date on which it is available for use. The estimated useful life of software for the current and comparative periods is three to five years.

Amortisation methods, useful lives and residual values are reviewed at each reporting date and adjusted if appropriate.

(h) Impairment of non-financial assets

At each reporting date, the Bank reviews the carrying amounts of its non-financial assets to determine whether there is any indication of impairment. If any such indication exists, then the asset's recoverable amount is estimated. Goodwill is tested annually for impairment.

For impairment testing, assets are grouped together into the smallest group of assets that generates cash inflows from continuing use that is largely independent of the cash inflows of other assets. Goodwill arising from a business combination is allocated to CGUs or groups of CGUs that are expected to benefit from the synergies of the combination.

The recoverable amount of an asset or CGU is the greater of its value in use and its fair value less costs to sell. Value in use is based on the estimated future cash flows, discounted to their present value using a pre-tax discount rate that reflects current market assessments of the time value of money and the risks specific to the asset or CGU.

An impairment loss is recognised if the carrying amount of an asset or CGU exceeds its recoverable amount.

(i) Provisions

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

(j) Employee benefits

i) Pension obligations

The Bank subscribes to a defined contribution scheme and pays contributions to a publicly administered pension insurance plan on a statutory basis. The contributions are recognized as employee benefit expense when they are due.

The Bank's obligations under the scheme are limited to 10% of the employees' gross emoluments with the other 10% contribution being borne by the employees. The Bank's contributions in respect of retirement benefit costs are charged to profit or loss in the year to which they relate.

ii) Short term employee benefits

Short-term employee benefits are expensed as the related service is provided. A liability is recognised for the amount expected to be paid if the Bank has a present legal or constructive obligation to pay this amount as a result of past service provided by the employee and the obligation can be estimated reliably.

5. SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

(j) Employee benefits (continued)

iii) Termination benefits

Termination benefits are expensed at the earlier of when the Bank can no longer withdraw the offer of those benefits and when the Bank recognises costs for a restructuring. If benefits are not expected to be settled wholly within 12 months of the reporting date, then they are discounted.

(k) Grants

Grants received are mainly to support various strategic projects including credit scoring, Digital Fields Automation (DFA), mobile savings (Haloyako) and channels expansions (agent banking).

Grants to support strategic initiatives were recorded in the statement of income as grant income. Grants to finance lending operations or the purchase of fixed assets are shown as direct additions to equity and the corresponding asset account. Grants for future project implementation are deferred until the project implementation is effected, upon which they will be recognized in the income statement.

(l) Cash and cash equivalents

Cash and cash equivalents' include notes and coins on hand, unrestricted balances held with central banks and highly liquid financial assets with original maturities of three months or less from the date of acquisition that are subject to an insignificant risk of changes in their fair value, and are used by the Bank in the management of its short-term commitments. Cash and cash equivalents are carried at amortised cost in the statement of financial position.

(m) Comparatives

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

(n) New standards and interpretations

A. New standards, amendments, and interpretations effective during the year

New standard or amendments	Effective for annual periods beginning on or after on or after
— Amendments to references to conceptual framework in IFRS standards	1 January 2020
— Definition of material (amendments to IAS 1 and IAS 8)	1 January 2020
— Interest rate benchmark reform (amendments to IFRS 9, IAS 39 and IFRS 7)	1 January 2020

B. New and amended standards and interpretations in issue but not yet effective for the year ended 31 December 2020

The below standards are not expected to have a significant impact on the Company's financial statements

New standards or amendments	Effective for annual period beginning or after
— COVID-19 related rent concessions (Amendment to IFRS 16)	1 June 2020
— Interest rate benchmark reform –Phase 2 (Amendments to IFRS 9, IAS 39, IFRS 7, IFRS 4 and IFRS 16)	1 January 2021
— Onerous Contracts – cost of fulfilling a contract (Amendments to IAS 37)	1 January 2022
— Annual improvements to IFRS standards 2018-2020	1 January 2022
— Property, Plant and Equipment: Proceed before intended use (Amendments to IAS 16)	1 January 2022
— Classification of liabilities as current or non-current (Amendments to IAS 1)	1 January 2023

6. FINANCIAL RISK MANAGEMENT

The Bank's activities expose it to a variety of financial risks, including credit risk and the risks of changes in debt and equity market prices, foreign currency exchange rates, liquidity risk and interest rates.

FINANCIAL RISK MANAGEMENT FRAMEWORK

The Board has overall responsibility for the establishment and oversight of the Bank's risk management framework. The Board has established the Bank Asset and Liability Committee (ALCO) that is responsible for developing and monitoring Bank risk management policies in their specified areas. All Board committees have non-executive members and report regularly to the Board on their activities.

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

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

(a) Operational risk

Operational risk is the risk of direct or indirect loss arising from a wide variety of causes associated with the Bank's processes, personnel, technology and infrastructure, and from external factors other than credit, market and liquidity risks – e.g. those arising from legal and regulatory requirements and generally accepted standards of corporate behaviour. Operational risks arise from all the Bank's operations.

The Bank's objective is to manage operational risk so as to balance the avoidance of financial losses and damage to the Bank's reputation with overall cost effectiveness and innovation. In all cases, the Bank policy requires compliance with all applicable legal and regulatory requirements.

The Board of Directors is responsible for the development and implementation of controls to address operational risk. This responsibility is supported by the development of overall Bank standards for the management of operational risk in among others, the following areas:

- requirements for appropriate segregation of duties, including the independent authorisation of transactions.
- requirements for reconciliation and monitoring of transactions;
- compliance with regulatory and other legal requirements;
- documentation of controls and procedures;
- requirements for the periodic assessment of operational risks faced, and the adequacy of controls and procedures to address the risks identified;
- requirements for the reporting of operational losses and proposed remedial action;
- Development of a contingency plan; and
- Ethical and business standards.

6. FINANCIAL RISK MANAGEMENT (CONTINUED)

(b) Credit risk

Credit risk is the risk of financial loss to the Bank if a customer or counterparty to a financial Instrument fails to meet its contractual obligations and arises principally from the Bank's loans to customers. For risk management reporting purposes, the Bank considers and consolidates all elements of credit risk exposure.

Management of credit risk

The Board has delegated responsibility for the management of credit risk to its Bank Credit Committee. The Credit Committee is responsible for oversight of the Bank's credit risk, including:

- Formulating credit policies in consultation with branches, covering collateral requirements (for individual loans), credit assessment, risk grading and reporting, documentary and legal procedures.
- Reviewing and assessing credit risk. The Bank's Credit Committee assesses all credit exposures in excess of designated limits, prior to facilities being committed to customers by the branch concerned. Recapitalisation and reviews of facilities are subject to the same review process.
- Developing and maintaining the Bank's risk grading in order to categorise exposures according to the degree of risk of financial loss faced and to focus management on the attendant risks. The risk grading system is used in determining where impairment provisions may be required against the respective loan group credit exposures. The current risk-grading framework consists of five grades reflecting varying degrees of risk of default and the availability of collateral or other credit risk mitigation. The responsibility for setting risk grades lies with the final approving executive / committee as appropriate. Risk grades are subject to regular reviews by the Bank's Board of Directors.
- Reviewing compliance of branches with agreed exposure limits. Regular reports are provided to Bank operation manager/credit committee on the credit quality of local portfolios and appropriate corrective action is taken.
- Providing advice, guidance and specialist skills to branches to promote best practice throughout the Bank in the management of credit risk.

Each branch is required to implement Bank credit policies and procedures, with credit approval authorities delegated from the Bank credit committee.

Each branch manager reports on all credit related matters to management and the credit committee. Each branch is responsible for the quality and performance of its credit portfolio and for monitoring and controlling all credit risks in its portfolios.

Internal Audit undertakes regular audits of branches and the Bank's credit processes.

The Bank credit committee determines that the loans are uncollectible; internal audit does an independent review of these loans; final write-off proposal is compiled and submitted to Board for approval; and finally, the Board approves the write-off. The credit committee's determination is reached after considering information such as the occurrence of significant changes in the borrower financial position such that the borrower can no longer pay the obligation, or that proceeds from collateral will not be sufficient to pay back the entire exposure. For smaller balance standardised loans, charge off decisions generally are based on a product specific past due status.

6. FINANCIAL RISK MANAGEMENT (CONTINUED)

(a) Credit risk (continued)

Credit quality analysis

Compliance with the Bank standards is supported by a programme of periodic reviews undertaken by Internal Audit. The results of Internal Audit reviews are discussed with management and reported to the Audit Committee.

The following table sets out information about the credit quality of financial assets measures at amortised costs, FVOCI debt instruments (Unless specifically indicated, for financial assets, the amounts in the table represent gross carrying amounts.

	31 DECEMBER 2020			
	Stage 1 TZS'000	**Stage 2 TZS'000**	**Stage 3 TZS'000**	**Total TZS'000**
Loans and advances to customers				
Grade 1: Current	22,199,122	5,160,174	248,678	27,607,974
Grade 2: Especially mentioned	144,027	1,198,064	53,540	1,395,631
Grade 3: Substandard	-	665,333	129,675	795,008
Grade 4: Doubtful	-	731,438	37,713	769,151
Grade 5: Loss	-	-	6,826,617	6,826,617
	22,343,149	7,755,009	7,296,223	37,394,381
Less: Allowance for impairment	(495,399)	(534,218)	(4,036,911)	(5,066,528)
Carrying amount	**21,847,750**	**7,220,791**	**3,259,312**	**32,327,853**
Other financial assets (all at Grade 1: current)				
Cash and bank balances	6,931,157	-	-	6,931,157
Investment in fixed deposits	9,367,198	-	-	9,367,198
	16,298,355	**-**	**-**	**16,298,355**
Less: Allowance for impairment	(122,099)	-	-	(122,099)
Carrying amount	**16,176,256**	**-**	**-**	**16,176,256**

6. FINANCIAL RISK MANAGEMENT (Continued)

(b) Credit risk (Continued)

Credit quality analysis (Continued)

	31 DECEMBER 2019			
	Stage 1 TZS'000	**Stage 2 TZS'000**	**Stage 3 TZS'000**	**Total TZS'000**
Loans and advances to customers				
Grade 1: Current	51,079,503	577,130	1,319,596	52,976,229
Grade 2: Especially mentioned	95,114	1,742,925	400	1,838,439
Grade 3: Substandard	-	776,382	14,981	791,363
Grade 4: Doubtful	-	556,663	18,188	574,851
Grade 5: Loss	-	-	4,167,481	4,167,481
	51,174,617	3,653,100	5,520,646	60,348,363
Less: Allowance for impairment	(402,723)	(247,484)	(2,503,071)	(3,153,278)
Carrying amount	**50,771,894**	**3,405,616**	**3,017,575**	**57,195,085**
Other financial assets (all at Grade 1: current)				
Cash and bank balances	5,326,299	-	-	5,326,299
Investment in fixed deposits	11,636,225	-	-	11,636,225
	16,962,524	**-**	**-**	**16,962,524**
Less: Allowance for impairment	(46,802)	-	-	(46,802)
Carrying amount	**16,915,722**	**-**	**-**	**16,915,722**

Collateral held and other credit enhancements

The general creditworthiness of a corporate customer tends to the most relevant indicator of credit quality of a loan extended to it. However, collateral provides additional security and the Bank generally request corporate borrowers provide it.

The Bank uses a range of policies and practices to mitigate credit risk. The most traditional of these is the taking of security for funds advanced, which is common practice. The acceptability of collateral for credit risk mitigation is guided by the Bank's procedures and policies. The main types of collateral taken include mortgages both surveyed and un-surveyed, cash collaterals, fixed assets, inventories, motor vehicles and other household goods.

Valuation of collaterals

The Bank has a panel of valuers who undertake valuation of property and other assets to be used as Collateral. The valuers in the panel are qualified professional valuers with adequate experience in the field of property and machinery valuation. Valuation of collateral are performed between 3 to 5 year intervals. The bank has a policy of performing valuation to collaterals with a value of TZS 30 million and above.

6. FINANCIAL RISK MANAGEMENT (Continued)

(b) Credit risk (Continued)

Expected credit loss measurement

The Bank aligns the classification criteria for assets that are past due or impaired in line with regulatory guidelines. In the determination of the classification of accounts, performance is the primary consideration. The classification of an account reflects a judgment about risks of default and loss associated with the credit facility. The classification process establishes a consistent approach to problem recognition, problem labelling, remedial action and the initiation of credit write-offs.

IFRS 9, Financial Instruments, outlines a 'three-Stage' model for impairment based on changes in credit quality since initial recognition as summarised below:

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

Significant increase in credit risk

The Bank decision on whether expected credit losses are based on 12-month expected credit losses or lifetime expected credit losses depends on whether there has been a significant increase in credit risk since initial recognition. An assessment of whether credit risk has increased significantly is made at each reporting date. When making the assessment, the Bank uses the change in the risk of a default occurring over the expected life of the financial instrument instead of the change in the amount of expected credit losses. This form the basis of stage 1, 2 and 3 classification and subsequent migration.

The Bank applies qualitative and quantitative criteria for stage classification and for its forward and backward migration.

Quantitative criteria

The quantitative criteria is based on relative and not absolute changes in credit quality as stated in the table above driven by ratings and days past due.

The Bank considers that financial instruments for which default patterns are not concentrated at a specific point during the expected life of the financial instrument, changes in the risk of a default occurring over the next 12 months may be a reasonable approximation of the changes in the lifetime risk of a default occurring and could be used to determine whether credit risk has increased significantly since initial recognition.

6. FINANCIAL RISK MANAGEMENT (Continued)

(b) Credit risk (Continued)

Quantitative criteria (continued)

The Bank's quantitative credit grading, as compared to Bank of Tanzania (BOT) prudential guidelines, into five prudential guidelines categories is as follows:

Days past due	BOT Guidelines	IFRS 9 credit staging
0 to 5 days overdue	Current	Stage 1
6 to 30 days overdue	Especially mentioned	Stage 1
31 to 60 days overdue	Substandard	Stage 2
61 to 90 days overdue	Doubtful	Stage 2
More than 90 days	Loss	Stage 3

The appropriateness of using changes in the risk of a default occurring over the next 12 months to determine whether lifetime expected credit losses should be recognized depends on the specific facts and circumstances. Risk of default occurring over the next 12 months is not suitable basis for determining whether credit risk has increased on a financial instrument with a maturity of more than 12 months when:

- the financial instruments only have significant payment obligations beyond the next 12 months;
- changes in relevant macroeconomic or other credit-related factors occur that are not adequately reflected in the risk of a default occurring in the next 12 months; or
- changes in credit-related factors only have an impact on the credit risk of the financial instrument (or have a more pronounced effect) beyond 12 months.

In addition to the above, the Bank considers other qualitative factors in determining the classification above and may accelerate the classification of credit facilities where deemed appropriate. Qualitative factors include but not limited to the following:

- Significant changes in the terms of the same instrument if it were issued at the reporting date that indicate a change in credit risk since initial recognition, e.g.: increase in credit spread; more stringent covenants; increased amounts of collateral or guarantees; or higher income coverage.
- Significant changes in external market indicators of credit risk for the same financial instrument (or similar instrument of the borrower), e.g.: credit spread; credit default swap prices; length of time or the extent to which the fair value of a financial asset has been less than its amortized cost; other market information related to the borrower, such as changes in the price of a borrower's debt and equity instruments; or external credit rating (actual or expected).

- Changes in the Bank's credit management approach in relation to the financial instrument (e.g. based on emerging indicators of changes in the credit risk of the financial instrument, the bank's credit risk management practice is expected to become more active or focused on managing the instrument, including the instrument becoming more closely monitored or controlled, or the bank specifically intervening with the borrower).

- Expected changes in the loan documentation (e.g. breach of contract leading to covenant waivers or amendments, interest payment holidays, interest rate step-ups, requiring additional collateral or guarantees).

6. FINANCIAL RISK MANAGEMENT (Continued)

(b) Credit risk (Continued)

Expected credit loss measurement (Continued)

Qualitative criteria (continued)

- Actual or expected adverse changes in business, financial or economic conditions significantly affecting borrower's ability to meet its debt obligations (e.g. increase in interest rates or unemployment rates); operating results of the borrower e.g. declining revenues or margins, increasing operating risks, working capital deficiencies, decreasing asset quality, increased balance sheet leverage, liquidity, management problems or changes in the scope of business or organizational structure (such as the discontinuance of a segment of the business) that results in a significant change in the borrower's ability to meet its debt obligations; or regulatory, economic, or technological environment of the borrower that results in a significant change in the borrower's ability to meet its debt obligations (e.g. a decline in the demand for the borrower's sales product because of a shift in technology).
- Significant changes in the value of collateral or in the quality of third-party guarantees or credit enhancements, which are expected to reduce the borrower's economic incentive to pay or otherwise effect the probability of default (e.g. if the value of collateral declines because house prices decline, borrowers in some jurisdictions have a greater incentive to default on their mortgages); or quality of a guarantee provided by a shareholder (or an individual's parents) if the shareholder (or parents) have an incentive and financial ability to prevent default by capital or cash infusion.
- Significant changes in the expected performance and behaviour of the borrower, including changes in the payment status of borrowers in the group (e.g. increase in delayed contractual payments or number of credit card borrowers expected to approach or exceed their credit limit or who are expected to be paying the minimum monthly amount)

Definition of default

The Bank considers a financial asset to be in default when:

- The borrower is unlikely to pay its credit obligations to the Bank in full, without recourse by the Bank to actions such as realizing of security (if any is held)
- The borrower is more than 90 days past due on any material credit obligation to the Bank.
- It is becoming probable that the borrower will restructure the asset as a result of bankruptcy due to borrower's inability to pay its credit obligations.

The definition of default largely aligns with that applied by the Bank for regulatory capital purposes.

Incorporation of forward-looking information

The Bank incorporates forward-looking information into both the assessment of whether the credit risk of an instrument has increased significantly since initial recognition and the measurement of ECL. The Bank formulates three economic scenarios, best case, worst case and basic scenario and from the three the ECL is determined.

6. FINANCIAL RISK MANAGEMENT (Continued)

(b) Credit risk (Continued)

Modified financial assets

The contractual terms of a loan may be modified for a number of reasons, including changing market conditions, customer retention and other factors not related to a current or potential credit deterioration of the customer. An existing loan whose terms have been modified may be derecognised and the renegotiated loan recognised as a new loan at fair value in accordance with the accounting policy set out in Note 6(d).

When the terms of a financial asset are modified and the modification does not result in de-recognition, the determination of whether the asset's credit risk has increased significantly reflects comparison of:

- its remaining lifetime PD at the reporting date based on the modified terms; with
- the remaining lifetime PD estimated based on data on initial recognition and the original contractual terms.

When modification results in de-recognition, a new loan is recognised and allocated to Stage 1 (assuming it is not credit-impaired at that time).

The Bank renegotiates loans to customers in financial difficulties (referred to as 'forbearance activities') to maximise collection opportunities and minimise the risk of default. Under the Bank's forbearance policy, loan forbearance is granted on a selective basis if the debtor is currently in default on its debt or if there is a high risk of default, there is evidence that the debtor made all reasonable efforts to pay under the original contractual terms and the debtor is expected to be able to meet the revised terms.

The Bank sources macro-economic information from the National Bureau of Statistics and the Bank of Tanzania.

The revised terms usually include extending the maturity, changing the timing of interest payments and amending the terms of loan covenants. Both small and large loans are subject to the forbearance policy. The Bank's Credit Committee regularly reviews reports on forbearance activities.

For financial assets modified as part of the Bank's forbearance policy, the estimate of PD reflects whether the modification has improved or restored the Bank's ability to collect interest and principal and the Bank's previous experience of similar forbearance action. As part of this process, the Bank evaluates the borrower's payment performance against the modified contractual terms and considers various behavioural indicators.

Generally, forbearance is a qualitative indicator of a significant increase in credit risk and an expectation of forbearance may constitute evidence that an exposure is credit-impaired. A customer needs to demonstrate consistently good payment behaviour over a period of time before the exposure is no longer considered to be credit-impaired/in default or the PD is considered to have decreased such that it falls within the 12-month PD ranges for the asset to be considered Stage 1.

6. FINANCIAL RISK MANAGEMENT (Continued)

(b) Credit risk (Continued)

Measurement of ECL

The key inputs into the measurement of ECL are the term structure of the following variables: Probability of Default (PD), Loss Given Default (LGD) and Exposure at Default (EAD).

ECL for exposures in Stage 1 is calculated by multiplying the 12-PD by LGD and EAD. Lifetime ECL is calculated by multiplying the lifetime PD by the LGD and EAD.

Loss allowance

Loss allowances recognised is impacted by a variety of factors as described below;

- Transfers between Stage 1 and Stages 2 or 3 due to financial instruments experiencing significant increases (or decreases) of credit risk or becoming credit impaired in the period, and the consequent “step up” (or “step down”) between 12 month and Lifetime ECL;
- Additional allowances for new financial instruments recognised during the year, as well as releases for financial instruments de recognised in the year;
- Impact on the measurement of ECL due to changes in PDs, EADs and LGDs in the year, arising from regular refreshing of inputs to models;
- Impacts on the measurement of ECL due to changes made to models and assumptions.
- Financial assets derecognised during the period and write offs of allowances related to assets that were written off during the period.

6. FINANCIAL RISK MANAGEMENT (Continued)

(b) Credit risk (Continued)

Measurement of ECL (Continued)

Loans and advances to customers	2020			
Gross loans	**Stage 1 TZS'000**	**Stage 2 TZS'000**	**Stage 3 TZS'000**	**Total TZS'000**
Balance at 1 January	51,174,616	3,653,101	5,153,204	59,980,921
Transfer from Stage 1 to stage 2	(20,789,287)	20,789,287	-	-
Transfer from stage 2 to Stage 1	4,444,680	(4,444,680)	-	-
Transfer from Stage 2 to Stage 3	-	(7,800,433)	7,800,433	-
Transfer from Stage 3 to Stage 2	-	83,683	(83,683)	-
Transfer from Stage 1 to Stage 3	(11,367)	-	11,367	-
Write-offs	-	-	(3,944,606)	(3,944,606)
New financial assets originated	53,832,027	4,926,992	717,857	59,476,876
Repayment of principal amount	(65,301,277)	(7,228,832)	(1,997,821)	(74,527,930)
Changes in interest accrual	1,455,807	625,002	261,791	2,342,600
Modification of contractual cash flows of financial instruments	(41,843)	(11,810)	6,414	(47,239)
De-recognition during the period	(2,420,207)	(2,837,301)	(628,733)	(5,886,241)
Balance at 31 December 2020	**22,343,149**	**7,755,009**	**7,296,223**	**37,394,381**

Loss Allowance	**Stage 1 TZS'000**	**Stage 2 TZS'000**	**Stage 3 TZS'000**	**Total TZS'000**
Balance at 1 January	448,564	247,484	2,412,093	3,108,141
Transfer from Stage 1 to Stage 2	(420,191)	966,095	44,510	590,414
Transfer from Stage 2 to Stage 1	62,524	(349,969)	-	(287,445)
Transfer from Stage 2 to Stage 3	-	(1,317,399)	2,713,366	1,395,967
Transfer from Stage 3 to Stage 2	-	2,431	(2,202)	229
Transfer from Stage 1 to Stage 3	(493)	-	8,428	7,935
Write-offs	-	-	(3,944,606)	(3,944,606)
New financial assets originated	158,846	226,398	169,590	554,834
Financials assets derecognized	516,732	932,414	2,653,613	4,102,759
Changes in PDs/LGDs/EADs	(12,720)	(29,929)	3,761	(38,888)
Modification of contractual cash flows of financial instrument	(257,863)	(143,307)	(21,642)	(422,812)
Balance at 31 December 2020	**495,399**	**534,218**	**4,036,911**	**5,066,528**

6. FINANCIAL RISK MANAGEMENT (Continued)

(b) Credit risk (Continued)

Measurement of ECL (Continued)

Loans and advances to customers	2019			
Gross loans	**Stage 1 TZS'000**	**Stage 2 TZS'000**	**Stage 3 TZS'000**	**Total TZS'000**
Balance at 1 January	50,697,065	3,387,975	5,180,745	59,265,785
Transfer from Stage 1 to Stage 2	(14,534,817)	14,534,817	-	-
Transfer from Stage 2 to Stage 1	4,698,510	(4,698,510)	-	-
Transfer from Stage 2 to Stage 3	-	(5,281,602)	5,281,602	-
Transfer from Stage 1 to Stage 3	(20,271)	-	20,271	-
Transfer from Stage 3 to Stage 2	-	7,225	(7,225)	-
Write-offs			(3,561,711)	(3,561,711)
New financial assets originated	104,033,046	807,403	1,881,101	106,721,550
Financials assets derecognized	(88,692,737)	(5,620,876)	(3,393,357)	(97,706,970)
Changes in PDs/LGDs/EADs	(4,157,529)	186,160	(382,894)	(4,354,263)
Modification of contractual cash flows of financial instrument	(14,130)	(988)	(910)	(16,028)
Balance at 31 December 2019	**52,009,137**	**3,321,604**	**5,017,622**	**60,348,363**

Loss Allowance	Stage 1 TZS'000	Stage 2 TZS'000	Stage 3 TZS'000	Total TZS'000
Balance at 1 January	**353,472**	**201,138**	**1,919,259**	**2,473,869**
Transfer from Stage 1 to Stage 2	(112,730)	388,274	-	275,544
Transfer from Stage 2 to Stage 1	26,513	(292,316)	-	(265,803)
Transfer from Stage 2 to Stage 3	-	(1,133,556)	3,294,270	2,160,714
Transfer from Stage 3 to Stage 2	-	5,686	(7,161)	(1,475)
Transfer from Stage 1 to Stage 3	(503)	-	10,731	10,228
Write-offs	-	-	(3,561,711)	(3,561,711)
New financial assets originated	323,558	190,702	367,773	882,033
Financials assets derecognized	(314,416)	(130,384)	(26,984)	(471,784)
Changes in PDs/LGDs/EADs	129,397	958,116	600,183	1,687,696
Modification of contractual cash flows of financial instrument	(7,665)	(681)	(27,687)	(36,033)
Balance at 31 December 2019	**397,626**	**186,979**	**2,568,673**	**3,153,278**

(c) Liquidity risk

Liquidity risk' is the risk that the Bank will encounter difficulty in meeting obligations associated with its financial liabilities that are settled by delivering cash or another financial asset. Liquidity risk arises from mismatches in the timing and amounts of cash flows, which is inherent to the Bank's operations and investments.

6. FINANCIAL RISK MANAGEMENT (Continued)

(c) Liquidity risk (Continued)

Management of liquidity risk

The Bank's approach to managing liquidity is to ensure, as far as possible, that it will always have sufficient liquidity to meet its liabilities when due, under both normal and stressed conditions, without incurring unacceptable losses or risking damage to the Bank's reputation.

Treasury receives information from other business units regarding the liquidity profile of their financial assets and liabilities and details of other projected cash flows arising from projected future business. Treasury then maintains a portfolio of short-term liquid assets, largely made up of short-term liquid investment securities as well as loans and advances to customers, to ensure that sufficient liquidity is maintained within the Bank as a whole.

To manage the liquidity gap for the 3-months analysis which is mainly contributed by borrowings payable to shareholder of the Bank, FINCA Microfinance Holding Bank LLC amounting to TZS 12.4 billion by which as at 31st December 2020 TZS 11.2 billion is maturing by 31 March 2021. Subsequent to year end, the shareholders of the Bank have approved capital injection through borrowing conversion amounting to TZS 3.2 billion from February 2021 to August 2021. Up to the date of signing the financial statements TZS 1.4 billion had already been converted in line with the conversion forecast. In addition to that, the shareholders further approved to extend loan tenor for TZS 2.3 billion of the same borrowing to April 2022 to regularize the gap.

6. FINANCIAL RISK MANAGEMENT (CONTINUED)

(c) Liquidity risk (Continued)

Exposure to liquidity risk

Maturity profile of the carrying value financial instruments based on the contractual cash flows (i.e. undiscounted) including the impact of netting is as follows:

2020	Up to 3 months TZS'000	4 - 6 Months TZS'000	7 - 12 Months TZS'000	1 - 3 years TZS'000	More than 3 years TZS'000	Total TZS'000
ASSETS						
Cash and cash equivalents	7,018,321	-	-	-	-	7,018,321
Investment in fixed deposits	-	8,036,077	1,209,022	-	-	9,245,099
Loans and advances to customers	5,665,689	7,704,421	15,499,000	3,458,743	-	32,327,853
Due from related parties	6,951	-	-	-	-	6,951
Other assets (excluding non-financial assets)	1,129,188	-	-	-	-	1,129,188
Total assets	**13,820,149**	**15,740,498**	**16,708,022**	**3,458,743**	**-**	**49,727,412**
LIABILITIES						
Deposits from customers	14,883,619	4,955,292	3,647,131	424,895	-	23,910,937
Deposit from banks	199,659	6,384,273	162,109	1,162,371	-	7,908,411
Borrowings	11,244,813	1,151,908	-	-	-	12,396,721
Trade and other payables	578,949	-	-	-	-	578,949
Lease liabilities	849,528	188,769	422,752	1,118,401	303,203	2,882,653
Other payables (excluding non-financial liabilities)	2,655,030	-	-	-	-	2,655,030
Total liabilities	**30,411,598**	**12,680,243**	**4,231,991**	**2,705,666**	**303,203**	**50,332,701**
Net liquidity gap	**(16,591,449)**	**3,060,255**	**12,476,031**	**753,077**	**(303,203**	**(605,289)**
At 31 December 2019						
Total assets	18,731,445	22,209,000	25,994,383	8,389,876	-	75,324,704
Total liabilities	30,822,837	14,315,096	21,212,072	4,690,193	1,896,462	72,936,660
Net liquidity gap	**(12,091,392)**	**7,893,904**	**4,782,311**	**3,699,683**	**(1,896,462)**	**2,388,044**

6. FINANCIAL RISK MANAGEMENT (CONTINUED)

(d) Market risks

Market risk is the risk that changes in market prices, such as interest rate, equity prices, foreign exchange rates and credit spreads (not relating to changes in the obligor's / issuer's credit standing) will affect the Bank's income or the value of its holdings of financial instruments. The objective of market risk management is to manage and control market risk exposures within acceptable parameters, while optimising the return on risk.

Management of market risks

The Bank separates its exposure to market risk between trading and non-trading portfolios. Trading portfolios mainly are held by the Treasury unit, and include positions arising from market making and proprietary position taking, together with financial assets and liabilities that are managed on a fair value basis. Overall authority for market risk is vested in the Asset and Liability Committee (ALCO).

Interest rate risk

The Bank interest rate risk is the risk that the future cash flows of a financial instrument will fluctuate because of changes in the market interest rates. The fair value interest rate risk is the risk that the value of the financial instrument will fluctuate because of changes in market interest rates. The Bank takes on exposure to the effects of fluctuations in the prevailing levels of market interest rates on both the value and cash flow risks of its financial instruments.

Interest rate risk - stress tests

The Bank monitors the impact of risks associated with the effects of fluctuations in prevailing interest rates. The following table summarizes the estimated impact of an immediate hypothetical increase or decrease in interest rates of 100 basis points on profit before income tax expense, and current interest rate risk profile as at 31 December 2020.

	2020 TZS'000	2019 TZS'000
100 basis points increases or decrease in interest rates	**81,182**	**53,849**

The Bank's interest rate risk have reduced significantly, as most of the loans outstanding have fixed interest rates.

6. FINANCIAL RISK MANAGEMENT (CONTINUED)

(d) Market risks (Continued)

Interest rate risk (Continued)

The table below summarises the exposure to interest rate risk. Assets and liabilities are categorised by the earlier of contractual re-pricing or maturity dates. The Bank does not bear an interest rate risk on off balance sheet items except to the extent that interest rates affect foreign exchange rates.

2020	Up to 3 Months TZS'000	4 - 12 Months TZS'000	1 - 5 years TZS'000	Non-interest bearing TZS'000	Total TZS'000
ASSETS					
Cash and cash equivalents	-	-	-	7,018,321	7,018,321
Investment in fixed deposits	-	9,245,099	-	-	9,245,099
Loans and advances to customers	5,665,689	23,203,421	3,458,743	-	32,327,853
Due from related parties	-	-	-	6,951	6,951
Other assets (excluding non-financial assets)	-	-	-	1,129,188	1,129,188
Total assets	**5,665,689**	**32,448,520**	**3,458,743**	**8,154,460**	**49,727,412**
LIABILITIES					
Deposit from customers	14,883,619	8,602,423	424,895	-	23,910,937
Deposits from banks	199,659	6,546,382	1,162,371		7,908,411
Borrowings and interest payable	11,244,813	1,151,908	-	-	12,396,721
Lease liability	849,528	611,521	1,421,604	-	2,882,653
Trade and other payables-	-	-	-	578,949	578,949
Other payables (excluding non-financial liabilities)	2,655,030	-	-	-	2,655,030
Total liabilities	**29,832,649**	**16,912,234**	**3,008,869**	**578,949**	**50,332,701**
Interest rate sensitivity gap	**(24,166,960)**	**15,536,286**	**449,874**	**7,575,511**	**(605,289)**
At 31 December 2019					
Total assets	12,191,250	48,203,383	8,389,876	6,540,195	75,324,704
Total liabilities	25,789,684	15,800,539	25,120,662	4,899,289	71,610,174
Interest rate sensitivity gap	**(13,598,434)**	**32,402,844**	**(16,730,786)**	**1,640,906**	**3,714,530**

6. FINANCIAL RISK MANAGEMENT (CONTINUED)

(d) Market risks (Continued)

Currency risk

The Bank had no significant unhedged currency position at the end of the year. The Bank has an exposure to the effects of fluctuations in the prevailing foreign currency exchange rates on its financial position and cash flows. The table below summarizes the exposure to foreign currency exchange rate risk at 31 December 2020.

31 December 2020	**TZS '000**
Cash and cash equivalents	167,933
Placements	9,245,099
Borrowings	(12,396,722)
Hedging Value	13,296,085
Net balance sheet exposure	**10,312,395**
A sensitivity analysis in relation to the net exposure for a 10% strengthening/weakening of the TZS against USD:	
Increase in loss before tax	1,031,239
31 December 2019	
Cash and cash equivalents	1,947,710
Placements	11,589,424
Borrowings	(23,629,978)
Hedging Value	11,221,110
Lease liabilities	(3,313,863)
Net amount due to related parties	(109,948)
Net balance sheet exposure	**(2,295,545)**
A sensitivity analysis in relation to the net exposure for a 10% strengthening/weakening of the TZS against USD:	
Increase in profit before tax	(229,555)

(e) Fair value estimation

IFRS 13 requires the Bank to classify fair value measurements using a fair value hierarchy that reflects the significance of the inputs used in making the measurements.

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

- Level 1 fair value measurements are those derived from quoted prices (unadjusted) in active markets for identical assets or liabilities.
- Level 2 fair value measurements are those derived from inputs other than quoted prices included within Level 1 that are observable for the asset or liability, either directly (i.e. as prices) or indirectly (i.e. derived from prices).
- Level 3 fair value measurements are those derived from valuation techniques that include inputs for the asset or liability that are not based on observable market data (unobservable inputs).

This hierarchy requires the use of observable market data when available. The Bank considers relevant and observable market prices in its valuations where possible.

Fair value of the Bank's financial assets and financial liabilities that are measured at fair value on recurring basis. The Bank has considered the fair value to be approximately equal to amortization costs due to short term nature and the fact that they reprice in the short run.

6. FINANCIAL RISK MANAGEMENT (CONTINUED)

(e) Fair value estimation (Continued)

Financial instruments not measured at fair value:

The following table analyses within the fair value hierarchy the Bank's assets and liabilities (by class) measured at fair value at 31 December 2020.

31 December 2020	Financial assets at amortised cost	Financial liabilities at amortised cost	Total	Total Carrying Amount
ASSETS	**TZS'000**	**TZS'000**	**TZS'000**	**TZS'000**
Cash and bank balances	7,018,326	-	7,018,326	7,018,326
Investment in fixed deposit	9,245,099	-	9,245,099	9,245,099
Loans and advances to customers	32,327,853	-	32,327,853	32,327,853
Other assets	1,153,719	-	1,153,719	1,153,719
Due from related parties	6,951	-	6,951	6,951
	49,751,948	**-**	**49,751,948**	**49,751,948**
LIABILITIES				
Deposits from other banks	-	7,908,411	7,908,411	7,908,411
Deposits from customers	-	23,910,937	23,910,937	23,910,937
Borrowings		12,396,722	12,396,722	12,396,722
Lease liabilities	-	2,882,653	2,882,653	2,882,653
Other payables	-	2,655,030	2,655,030	2,655,030
	-	**49,753,753**	**49,753,753**	**49,753,753**

31 December 2019	Financial assets at amortised cost	Financial liabilities at amortised cost	Total	Total carrying amount
ASSETS	**TZS'000**	**TZS'000**	**TZS'000**	**TZS'000**
Cash and bank balances	5,326,299	-	5,326,299	5,326,299
Investment in fixed deposit	11,589,424	-	11,589,424	11,589,424
Loans and advances to customers	57,195,085	-	57,195,085	57,195,085
Other assets	1,199,414		1,199,414	1,199,414
Due from related parties	14,482	-	14,482	14,482
	75,324,704	**-**	**75,324,704**	**75,324,704**
LIABILITIES				
Deposits from other banks	-	8,370,887	8,370,887	8,370,887
Deposits from customers	-	28,386,803	28,386,803	28,386,803
Borrowings	-	25,895,587	25,895,587	25,895,587
Amounts due to related parties	-	109,944	109,944	109,944
Lease liabilities	-	4,057,608	4,057,608	4,057,608
Other payables	-	4,789,345	4,789,345	4,789,345
	-	**71,610,174**	**71,610,174**	**71,610,174**

6. FINANCIAL RISK MANAGEMENT (CONTINUED)

(f) Capital Management

Bank of Tanzania (the Central Bank) sets and monitors capital requirements for all banks and financial institutions in Tanzania.

The objective of the Bank of Tanzania is to ensure that a Bank maintains a level of capital which:

- is adequate to protect its depositors and creditors;
- is commensurate with the risks associated with its activities and profile; and
- promote public confidence in the Bank.

In implementing current capital requirements, the Bank of Tanzania requires banks to maintain a prescribed ratio of total capital to total risk-weighted assets.

Capital adequacy and use of regulatory capital are monitored regularly by management employing techniques based on the guidelines developed by the Basel Committee, as implemented by the Bank of Tanzania for supervisory purposes.

In accordance with the revised 2014 regulations, the Bank of Tanzania requires a bank to maintain at all times:

- a Core Capital of not less than 10% of its total risk-weighted assets and off balance sheet exposure; and
- a Total Capital of not less than 12% of its total risk-weighted assets and off balance sheet exposure.
- In addition, the Central Bank requires all banks and financial institutions to maintain a buffer of 2.5% above the core capital and total capital ratios by which its utilization will be advised by the Bank.

In addition, the Banking and Financial Institutions (Microfinance Activities) Regulation, 2014 requires a microfinance bank to maintain at all times a minimum core capital of not less than five billion shillings or such higher amount as the Bank may prescribe.

Capital is segregated into core capital (Tier 1) and supplementary capital (Tier 2).

Core capital includes ordinary share capital, irredeemable preference share capital, capital contribution reserve, share premium and retained earnings after deductions of goodwill, intangible assets, and prepayments and deferred charges.

Supplementary Capital on the other hand includes subordinated debt, general and other reserves.

Risk weighted assets are arrived at using a framework of five weights applied to both on-balance sheet and off-balance sheet items to reflect the relative risk of each asset and counterparty.

The table below summarises the composition of regulatory capital and the ratios of the Bank for the year ended 31 December 2020 and year ended 31 December 2019. During those two periods, the Bank complied with all the Bank of Tanzania imposed capital requirements to which it was subjected to.

6. FINANCIAL RISK MANAGEMENT (CONTINUED)

(f) Capital management (continued)

The Bank's regulatory capital position as at 31 December 2020 was as follows:

	2020 TZS '000	2019 TZS '000
Core capital (Tier 1)		
Share capital	34,102,304	31,574,605
Retained earnings (excluding loss for the year)	(18,196,257)	(11,699,391)
Qualifying year to date (loss)	(9,258,929)	(7,123,881)
	6,647,118	12,751,333
Less deductions from capital		
Regulatory adjustments:		
Prepayments	717,464	768,942
Deferred charges	-	-
Intangible assets	-	-
Total deductions from capital	717,464	768,942
Core capital	5,929,654	11,982,391
Supplementary capital (Tier 2)		
Total capital	5,929,654	11,982,391
Risk weighted assets		
On-balance sheet	37,193,582	63,426,243
Operational Risk	8,650,377	9,749,189
Total risk weighted assets	45,843,959	73,175,432

Capital ratios	**2020 %**	**2019 %**
Core capital /total risk weighted assets (BoT minimum 10%)	**12.93%**	**16.37%**
Total capital /total risk weighted assets (BoT minimum 12%)	**12.93%**	**16.37%**

6. FINANCIAL RISK MANAGEMENT (CONTINUED)

(f) Capital Management (Continued)

Capital allocation

The Bank's capital management approach is driven by its desire to maintain a sufficient capital base to support the development of its business and to meet regulatory capital requirements at all times.

Strategic business and capital plans are drawn up annually. The plan ensures that adequate levels of capital and optimum mix of the different components of capital are maintained by the Bank to support the strategy. This is integrated with the Bank's annual planning process that takes into consideration business growth assumptions across products and the related impact on capital resources.

The capital plan takes the following into account:

- regulatory capital requirements;
- increases in demand for capital due to business growth, market shocks or stresses;
- available supply of capital and capital raising options; and
- Internal controls and governance for managing the Bank's risk, performance and capital.

The allocation of capital between specific operations and activities is, to a large extent, driven by optimisation of the return achieved on the capital allocated. The amount of capital allocated to each operation or activity is based primarily upon the regulatory capital, but in some cases the regulatory requirements do not reflect fully the varying degree of risk associated with different activities. In such cases the capital requirements may be flexed to reflect differing risk profiles, subject to the overall level of capital to support a particular operation or activity not falling below the minimum required for regulatory purposes. The process of allocating capital to specific operations and activities is undertaken independently of those responsible for the operation, and is subject to review by the Asset and Liabilities Committee (ALCO).

Although maximisation of the return on risk-adjusted capital is the principal basis used in determining how capital is allocated within the Bank to particular operations or activities, it is not the sole basis used for decision-making. Account also is taken of synergies with other operations and activities, the availability of management and other resources, and the fit of the activity with the Bank's longer term strategic objectives. The Board of Directors reviews the Bank's policies in respect of capital management and allocation regularly.

7. INTEREST AND SIMILAR INCOME

	2020 TZS '000	2019 TZS '000
Interest from loans and advances	17,374,687	25,671,935
Interest income from investments	465,170	222,990
	17,839,857	**25,894,925**

8. INTEREST AND SIMILAR EXPENSE

	2020 TZS '000	2019 TZS '000
Interest expense on term loans	2,195,251	3,249,177
Interest expense on lease liabilities	506,352	468,611
Fees expense on term loan	30,809	74,814
Interest expense on deposits from customers	3,321,118	2,815,211
	6,053,530	**6,607,813**

9. FEES AND COMMISSION INCOME

	2020 TZS '000	2019 TZS '000
Application fees	1,405,598	3,123,303
Account maintenance fees	533,242	1,052,655
Recovery income	955,449	1,171,180
Ledger fees	1,133,319	827,763
	4,027,608	**6,174,901**

10. FEES AND COMMISSION EXPENSE

M-pesa charges	-	41,576
Commission expenses on agent banking	286,188	520,695
	286,188	**562,271**

11. GRANT INCOME

Master Card grant	164,283	164,283
Engine	5,000	5,000
Financial Sector Deepening Trust	5,253	5,253
	174,536	**174,536**

Grants received are mainly to support various strategic projects including credit scoring, Digital Fields Automation (DFA), mobile savings (Haloyako) and channels expansions (agent banking) amounting to USD 3,274,796 Million from 2013 to enhance financial inclusion.

Grants to support strategic initiatives were recorded in the statement of income as grant income. Grants to finance lending operations or the purchase of fixed assets are shown as direct additions to equity and the corresponding asset account. Grants for future project implementation are deferred until the project implementation is effected, upon which they will be recognized in the income statement.

12. OTHER (LOSSES) / INCOME

	2020 TZS '000	2019 TZS '000
Income from insurance claim	3,082	11,461
Net foreign exchange (loss)/gain	(217,653)	152,741
Other losses miscellaneous	(140,469)	(784)
(Loss)/ gain on disposal of Property and Equipment	(946)	21,654
	(355,986)	**185,072**

13. PERSONNEL EXPENSES

Salaries and wages	7,412,099	9,197,421
NSSF/PPF contributions	709,163	908,583
Training expenses	31,044	38,801
Medical insurance expenses	434,218	635,390
Skills and development levy	325,733	431,887
Other staff benefits	-	372,708
Workers Compensation Fund contribution	74,662	113,724
Directors' emoluments	165,789	139,158
Bonuses	-	51,000
	9,152,708	**11,888,672**

14. OPERATING EXPENSES

Operating expenses include the following:

	2020 TZS '000	2019 TZS '000
Transport and travel	800,705	1,273,150
Affiliation fees	433,240	664,996
Low value leases/Operating lease rentals	69,225	279,797
Professional and legal fees	349,884	793,536
Auditors' remuneration	284,783	335,572
Security and Insurance	780,540	1,073,681
Marketing and communication	559,948	725,571
Stationery, supplies and utilities	513,208	647,531
IT support	76,767	493,901
Recruitment and Retrenchment	1,024,431	136,196
Repair and maintenance	317,730	297,306
Other expenses	1,309,450	1,712,086
	6,519,911	**8,433,323**

15. INCOME TAX

a) Tax expense

	2020 TZS '000	2019 TZS '000
Alternative minimum tax	110,242	152,849
De-recognition of Deferred tax asset	-	4,957,545
	110,242	**5,110,394**

b) Reconciliation of accounting profit to tax expense

	%	2020 TZS '000	2019 TZS '000
Loss before tax		(9,148,687)	(2,013,487)
Tax expense at applicable rate of 30%	30.0%	(2,744,606)	(604,046)
Tax effect on items disallowed for tax purposes	-1.3%	116,687	212,570
Unrecognised deferred tax for 2019	-29.2%	2,673,213	697,174
Over provided in prior years	0.5%	(45,294)	-
De-recognised deferred tax	0.0%	-	4,957,545
Alternative minimum tax	-1.2%	110,242	(152,849)
	-1.2%	**110,242**	**5,110,394**

c) Derecognised deferred tax asset

Deferred taxes are calculated on all temporary differences under the liability method using enacted tax rate of 30%.The net deferred tax asset is attributable to the following:

	2020 TZS '000	2019 TZS '000
Accelerated capital allowances	156,647	82,238
Provisions	1,576,453	1,009,400
Tax losses carried forward	6,594,831	4,563,081
De-recognition of deferred tax asset	**7,957,884**	**8,327,931**

The Bank is in an assessed tax loss position. Consequently, deferred tax asset has not been recognised due to uncertainty regarding the timing of future taxable profits against which the deferred tax asset can be utilised.

15. INCOME TAX (Continued)

	2020 TZS '000	2019 TZS '000
d) Tax payable		
At beginning of year	(138,492)	(368,089)
Tax paid during the year	152,849	382,446
Current taxation charge for the year	(110,242)	(152,849)
At end of the year	**(95,885)**	**(138,492)**

16. Classification of financial assets and financial liabilities

The following table provides a reconciliation between line items in the statement of financial position and categories of financial instruments. See accounting policies in Notes 5(d)(ii).

31 December 2020

	Mandatorily at FVTPL TZS'000	Designated as at FVTPL TZS'000	FVOCI – debt instruments TZS'000	Amortised cost TZS'000	Total carrying amount TZS'000
Cash and cash equivalents	-	-	-	7,018,321	**7,018,321**
Loans and advances to customers:	-	-	-	32,327,853	**32,327,853**
Investment securities	-	-	-	9,245,099	**9,245,099**
Due to related parties	-	-	-	6,951	**6,951**
Other assets	-	-	-	1,910,687	**1,910,687**
Total financial assets	-	-	-	**50,508,911**	**50,508,911**
Deposits from banks	-	-	-	7,908,411	**7,908,411**
Deposits from customers	-	-	-	23,910,937	**23,910,937**
Borrowings	-	-	-	12,396,722	**12,396,722**
Lease liabilities	-	-	-	2,882,653	**2,882,653**
Total financial liabilities	-	-	-	**47,098,723**	**47,098,723**

16. Classification of financial assets and financial liabilities (continued)

31 December 2019

	Mandatorily at FVTPL TZS'000	Designated as at FVTPL TZS'000	FVOCI – debt instruments TZS'000	Amortised cost TZS'000	Total carrying amount TZS'000
Cash and cash equivalents	-	-	-	5,326,299	**5,326,299**
Loans and advances to Customers	-	-	-	57,195,085	**57,195,085**
Investment securities	-	-	-	11,589,424	**11,589,424**
Due to related parties	-	-	-	14,482	**14,482**
Other assets	-	-	-	2,129,152	**2,129,152**
Total financial assets	-	-	-	**76,254,442**	**76,254,442**
Deposits from banks	-	-		8,370,887	**8,370,887**
Deposits from customers	-	-	-	28,386,803	**28,386,803**
Borrowings	-	-	-	25,895,587	**25,895,587**
Lease liabilities	-	-	-	4,057,608	**4,057,608**
Total financial liabilities	-	-	-	**66,710,885**	**66,710,885**

17. INVESTMENTS IN FIXED DEPOSITS

	2020 TZS'000	2019 TZS'000
Fixed deposits	9,367,198	11,636,225
Impairment on investment	(122,099)	(46,801)
	9,245,099	**11,589,424**

18. CASH AND BANK BALANCES

Balance with Bank of Tanzania	5,361,642	2,329,574
Bank balances	1,656,679	2,996,725
	7,018,321	**5,326,299**

19. LOANS AND ADVANCES TO CUSTOMERS

Village Bank loans	535,755	129,466
Business loans	25,854,911	40,382,305
Small group loans	25,274	25,201
Salary loans	1,023,980	1,528,717
Shule loans	648,128	1,380,551
Parent Education Loan	67,592	129,254
Pamoja Loans	1,310,584	8,295,404
Pamoja Loans Plus	1,346,131	4,933,059
Insurance Claim	324,221	436,508
Micro Individual Lending Loan	3,631,935	923,551
Halo Credit overdraft account	45,841	45,841
Social Financial Group loan	1,225,100	2,138,506
Lien Loan	15,197	-
New Pamoja loan	1,339,732	-
Gross loans balances	**37,394,381**	**60,348,363**
Less: Provision for loan losses (Note 20(b)(i))	(5,066,528)	(3,153,278)
Net loans to customers	**32,327,853**	**57,195,085**

19. LOANS AND ADVANCES TO CUSTOMERS (CONTINUED)

	2020 TZS '000	2019 TZS '000
a) Analysis of net loans to customers by maturity		
Up to 3 months	5,665,689	12,191,250
Between 4 months and 6 months	7,704,421	14,144,748
Between 7 months and 12 months	15,499,000	22,469,211
Between 1 year and 3 years	3,458,743	8,389,876
	32,327,853	**57,195,085**
b) (i) Movement of provision for loan losses		
Balance brought forward	3,153,278	2,473,869
Provision charge for the year	5,858,483	4,241,120
Bad debts written off during the year	(3,945,233)	(3,561,711)
Balance carried forward	**5,066,528**	**3,153,278**
b) (ii) Impairment charge reported in the SOCI		
Impairment on loans and advances	5,858,483	4,241,120
Impairment on other financial instruments	75,298	46,801
Impairment (reversal) on stage 3 loans	(176,807)	(113,457)
Total impairment charge	**5,756,974**	**4,174,464**

The total write off during the year was TZS 3,945,233,000 (2019: TZS 3,561,711,000) and recovery of previous written off loan was TZS 955,449,000 (2019: TZS 1,020,197,402).

20. OTHER ASSETS

	2020 TZS '000	2019 TZS '000
Prepaid expenses	717,464	768,942
Staff advances	20,024	81,383
Stationary and office supplies	44,011	79,413
Other receivables	1,095,772	1,086,290
Mobile Banking - Nostro Accounts	33,416	113,124
	1,910,687	**2,129,152**

21. WORK IN PROGRESS

	2020 TZS '000	2019 TZS '000
COST		
At the beginning of the year	14,716	2,681,890
Additions	150,822	554,028
Total	**165,538**	**3,235,918**
Transfer to intangible assets	(127,260)	(3,111,775)
Transfer to Property and equipment	-	(68,098)
Write off to income statement	-	(41,329)
At 31 December	**38,278**	**14,716**

21. WORK IN PROGRESS (CONTINUED)

These are the payments made on refurbishment of 8th Floor when part of head office relocated from 9th floor to 8th Floor as part of cost control. Also other costs included other refurbishment for Mbagala cashless branch which were waiting for capitalization upon completion and start of operations. Most of the cost have been capitalized before end of the year. The remaining amount is related to Musoma branch refurbishment which is ongoing amounting to TZS 38million.

22. PROPERTY AND EQUIPMENT

	Leasehold Improvements TZS '000	Motor Vehicles TZS '000	Office Equipment TZS '000	Office Furniture and Fittings TZS '000	Total TZS '000
Cost					
At 1 January 2019	3,754,946	171,566	6,838,218	1,013,859	11,778,589
Additions	272,438	-	150,233	17,351	440,022
Disposals	-	(65,880)	(15,855)	(7,729)	(89,464)
At 31 December 2019	**4,027,384**	**105,686**	**6,972,596**	**1,023,481**	**12,129,147**
At 1 January 2020	4,027,384	105,686	6,972,596	1,023,481	12,129,147
Additions	139,065	-	148,026	1,196	288,287
Disposals	(650,991)	-	(25,999)	(14,783)	(691,773)
At 31 December 2020	**3,515,458**	**105,686**	**7,094,623**	**1,009,894**	**11,725,661**
Accumulated depreciation					
At 1 January 2019	2,530,558	171,566	5,026,712	780,682	8,509,518
Charge for the year	395,011	-	712,232	75,295	1,182,538
Eliminated on disposal	-	(65,880)	(14,583)	(7,728)	(88,191)
At 31 December 2019	**2,925,569**	**105,686**	**5,724,361**	**848,249**	**9,603,865**
At 1 January 2020	2,925,569	105,686	5,724,361	848,249	9,603,865
Charge for the year	297,182	-	631,132	70,802	999,116
Eliminated on disposal	(544,781)	-	(25,927)	(14,203)	(584,911)
At 31 December 2020	**2,677,970**	**105,686**	**6,329,566**	**904,848**	**10,018,070**
Net book value					
At 31 December 2020	**837,487**	**-**	**765,057**	**105,046**	**1,707,590**
At 31 December 2019	**1,101,815**	**-**	**1,248,235**	**175,232**	**2,525,282**

23. IFRS 16 - Leases

The Bank leases a number of branch and office premises. The lease terms are different depending on the strategic decision to operate in some of the branches, however on average the leases are for a period of 5 years with an option to renew the lease after that date. Some leases provide for additional rent payments that are based on changes in local price indices.

a) Right of use assets

	2020 TZS '000	2019 TZS '000
Cost		
At the beginning of year	5,836,716	5,455,665
Additions	150,992	381,051
Lease modification and derecognition during the year	(1,154,077)	-
At end of the year	**4,833,631**	**5,836,716**
Depreciation		
At beginning of the year	1,056,177	-
Amortization for the year	810,667	1,056,177
Lease modification and derecognition during the year**	(312,258)	-
At end of the year	**1,554,586**	**1,056,177**
Net book value	**3,279,045**	**4,780,539**

b) Lease liability

At 1 January	4,057,608	-
Impact on initial application of IFRS 16 as at 1 January 2019	-	4,820,514
Addition during the year	114,800	381,051
Interest expense accruals	506,352	468,611
Foreign exchange loss	-	3,105
Lease payments-principal	(887,631)	(1,187,014)
Lease payments-Interest	(152,201)	(428,659)
Lease modification and derecognition during the year**	(756,275)	-
31 December	**2,882,653**	**4,057,608**
Loss on disposal of lease		
Right of use adjustment/disposal due to closed branches	756,275	-
Lease liability adjustment/disposal due to closed branches	(841,819)	-
	(85,544)	-

**During the year 2020, the Bank closed four branches and released one floor at the head office. Also, the renegotiated the rental price for head office which resulted into modification of right of use and lease liability balances. In addition, the bank changed the currency of the lease from US dollars to Tanzanian shillings for Head office and Arusha branch. See note 7 (c) for maturity analysis of lease liability as at 31 December 2020.

c) Amounts recognised in the statement of cash flows.

	2020 TZS '000	2019 TZS '000
Principal payments	887,631	1,187,014
Interest payments	152,201	428,659
Total cash outflow for leases	**1,039,832**	**1,615,673**

23. IFRS 16 Leases (Continued)

d) Extension options

Some leases of office premises contain extension options exercisable by the Bank up to one year before the end of the non-cancellable contract period. Where practicable, the Bank seeks to include extension options in new leases to provide operational flexibility. The extension options held are exercisable only by the Bank and not by the lessors. The Bank assesses at lease commencement date whether it is reasonably certain to exercise the extension options. The Bank reassesses whether it is reasonably certain to exercise the options if there is a significant event or significant changes in circumstances within its control.

24. INTANGIBLE ASSETS

Computer software

	2020 TZS '000	2019 TZS '000
Cost		
At the beginning of year	6,988,073	3,793,563
Additions	303,079	3,194,510
At end of the year	**7,291,152**	**6,988,073**
Amortization		
At beginning of the year	2,765,888	2,228,225
Amortization for the year	1,255,608	537,663
At end of the year	**4,021,496**	**2,765,888**
Net book value	**3,269,656**	**4,222,185**

*Additions include TZS 127,260,000 capitalised from WIP – note 22 (2019: 3,111,775,000)

25. DEPOSITS FROM CUSTOMERS AND BANKS

	2020 TZS'000	2019 TZS'000
Deposits from customers	23,910,937	28,386,803
Deposits from banks	7,908,411	8,370,887
	31,819,348	**36,757,690**
Payable within 3 months or less	15,083,277	9,449,721
Payable within 4 to 6 months	11,339,566	7,796,248
Payable after 6 months	5,396,505	19,511,721
	31,819,348	**36,757,690**
Current and demand accounts		
Savings deposits	31,609,932	36,434,987
Collateral deposits	109,236	111,493
Others	100,180	211,210
	31,819,348	**36,757,690**

26. BORROWINGS

	2020 TZS '000	2019 TZS '000
Borrowings-Principal amounts	11,837,043	25,716,871
Interest payable	559,679	178,716
	12,396,722	**25,895,587**
Maturities of borrowings are as follows:		
Current - due within 12 months	**12,396,722**	**23,601,660**
Long term - due after 12 months	**-**	**2,293,927**

Analysis of principal amounts

	Balance as at 1 January 2020 TZS '000	**Payment TZS '000**	**Equity conversion Payment TZS '000**	**Foreign loss / (Gain) on mark to market TZS '000**	**Balance as at 31 December 2020 TZS '000**
Symbiotics Sicca (Lux.)	2,265,607	2,265,607	-		-
Global Partnerships Social Investment Fund 6.0 LLC	2,317,162	1,148,834	-	(19,100)	1,149,228
MCE Social Capital	1,149,139	1,149,139	-	-	-
FMH 26 JUNE 2018	2,281,231	2,297,619	-	16,388	-
FMH 28 JUNE 2018	3,421,846	-	804,459	25,836	2,643,223
FMH 17 JULY 2018	4,562,461	574,420	1,723,240	33,654	2,298,455
FMH 25 OCTOBER 2018	2,281,231	2,281,231	-		-
FMH 21 FEBRUARY 2019	3,432,100	-	-	15,582	3,447,682
FMH 14 MARCH 2019	1,716,565	1,723,259	-	6,694	-
FMH 22 MARCH 2019	2,289,529	-		8,926	2,298,455
	25,716,871	**11,440,109**	**2,527,699**	**87,980**	**11,837,043**

SYMBIOTICS SICAV (Lux.)

The loan from Symbiotics - SEB III MF is a shilling denominated loan amounting to TZS 4,531,216,600.00 equivalent to USD 2,000,000. A promissory note secures the loan and interest is fixed at 10.75%. The loan is repayable in two equal instalments of which 50% was paid on 30th November 2019 and another 50% was paid on 17th May 2020. Interest on the loan is payable semi-annually where the final interest payment was made on 17 May 2020.

GLOBAL PARTNERSHIPS SOCIAL INVESTMENT FUND 6.0 LLC

The original **loan** is a dollar denominated loan amounting to USD 1,000,000 which was received in August 2019. Interest is fixed at a rate of 7.78% per annum on the principal loan amount and it is payable in two equal instalments. The first instalment was paid on 20 December 2020 and the second one will be paid in 20th June 2021.

26. BORROWINGS (CONTINUED)

MCE Social Capital

This is a dollar denominated loan amounting to USD 1,000,000. Interest is fixed at a rate of 6.5% per annum on the principal loan amount and is payable semi-annually starting from 31 January 2018. The loan was payable in four equal instalments on 29 January 2019, 29 July 2019, 29 January 2020 and 29 July 2020. The last instalment of USD 250,000 was paid in July 2020.

FMH FUNDING

This is the loans received from FINCA Microfinance Holdings (FMH) on short term basis where a total of USD 8.7m were rolled over from the previous year on short term basis. During the year, a total of USD 3m was repaid while a total of USD 1.1m was converted in equity. All these loans were priced at 6% and is expected to keep on roll over at short term until the liquidity stabilizes.

BORROWING COVENANTS

As at 31st December 2020, the Bank was in breach of profitability and gross loan portfolio quality covenants with Global Partnership where the total exposure was less than 10% of total borrowings. Global Partnership borrowings USD 0.5M will mature in less than a year. The Bank obtained the waiver from the lender.

27. RELATED PARTY TRANSACTIONS AND BALANCES

In the ordinary course of business, transactions are entered into with FINCA International, the ultimate holding Company and other companies related to the Bank through common shareholding or common directorships. The relevant balances are shown below:

	2020 TZS '000	2019 TZS '000
Amount due from related parties		
FINCA International	-	7,531
FINCA Nigeria	5,021	5,021
Finca Africa IT Services Centre	1,930	1,930
	6,951	**14,482**
Amount due to related parties - FINCA International	**-**	**109,944**

	2020 TZS '000	2019 TZS '000
Transactions with related parties		
FINCA Microfinance Holding:		
Capital injection through debt conversion	2,527,699	-
Royalty fees	433,240	664,996
	2,960,939	**664,996**

Loans and advances to employees		
At 1 January	1,528,717	1,277,515
Net movement during the year	(504,737)	251,202
At 31 December, 2020	**1,023,980**	**1,528,717**

27. RELATED PARTY TRANSACTIONS AND BALANCES (CONTINUED)

Loans and advances to employees (continued)	2020 TZS'000	2019 TZS'000
Interest earned	**174,644**	**177,866**

Loans and advances to employees have been included under Note 17 - Loan and Advances to customers

Deposits from employees

	2020 TZS'000	2019 TZS'000
Opening balance	211,210	252,027
Net movement during the year	(111,030)	(40,817)
Closing balance	100,180	211,210

Key management personnel compensation

	2020 TZS'000	2019 TZS'000
Salaries and other benefits	1,622,027	1,245,890

Directors' emoluments

	2020 TZS'000	2019 TZS'000
Fees and allowances for services as Directors	165,789	139,158

Key management compensation is included in the personnel expenses for the year.

28. DEFERRED GRANT

	Balance as at 1 January 2020 TZS '000	Receipts TZS '000	Credited to profit or loss TZS '000	as at 31 December 2020 TZS '000
Engine	41,598	-	(5,000)	36,599
Financial Sector Deepening Trust	94,564	-	(5,253)	89,311
Master Card	615,209	-	(164,283)	450,926
	751,371	**-**	**(174,536)**	**576,836**

During the year no grant was received. As at year end, the deferred grant balance was TZS 576,836,000 (2019: TZS 751,373,000). The grants are credited to profit or loss to the extent that the agreed milestones in the memorandum of understanding have been achieved. The balance has been deferred pending implementation of the additional agreed milestones.

29. OTHER PAYABLES

	2020 TZS '000	2019 TZS '000
Accrued expenses	2,076,081	4,063,718
Provisions	278,489	320,746
Other payables	578,949	725,627
Employee bonus and leave days accrual	37,336	155,832
Deferred income on loans	441,527	469,663
	3,412,382	**5,735,586**

30. CAPITAL STRUCTURE

The Bank capital structure for the year under review is shown below.

	2020 TZS '000	2019 TZS '000
Authorized share capital		
35,000,000 ordinary shares of TZS 1,000 each	35,000,000	35,000,000
Issued and fully paid capital		
34,102,304** (2019: 31,574,605) ordinary shares of TZS 1,000 each	34,102,304	31,574,605

SHAREHOLDERS OF THE BANK

The total number of shareholders during the year 2020 was two. There were no Directors holding shares in the Bank.

Shareholding structure of the Bank was as follows:

	2020	2019
FINCA Microfinance Holding Bank LLC	34,102,303	31,574,604
FINCA International LLC	1	1
	34,102,304	31,574,605

**During the year the shareholders injected more capital by paying for 2,527,699 at TZS 1,000 per share which resulted into capital of TZS 2,527,699,000.

31. CONTINGENT LIABILITIES

Litigations

Litigations against the Bank relate to civil suits lodged against the Bank by customers and former employees in the normal course of business. The likely outcome of these suits cannot be determined as at the date of signing these financial statements. The Directors, however do not anticipate that significant liabilities will accrue from the pending suits and for those with likelihood of loss have been provided for.

32. COMMITMENTS

As at 31 December 2020 there were no capital commitments made.

33. CURRENCY

These financial statements are presented in Tanzania Shillings, rounded to the nearest thousand (TZS'000), which is also the functional currency unless explained otherwise.

34. EVENTS OCCURRING AFTER THE REPORTING PERIOD

The Directors are not aware of any other matter or circumstance arising since the end of the financial year not otherwise dealt with in these financial statements, which significantly affect the financial position of the Bank and results of its operations as at 31 December 2020.