

FINCA MICROFINANCE BANK LIMITED

ANNUAL REPORTS AND FINANCIAL STATEMENTS
FOR THE YEAR ENDED 31 DECEMBER 2018

FINCA MICROFINANCE BANK LIMITED

ANNUAL REPORTS AND FINANCIAL STATEMENTS FOR THE YEAR ENDED 31 DECEMBER 2018

CONTENTS

	PAGES
Corporate information	1 - 2
Report of the Directors	3 - 7
Statement of Directors' responsibilities	8
Declaration of chief financial officer	9
Independent auditors' report	10 - 13
Financial statements:	
Statement of profit or loss and other comprehensive income	14
Statement of financial position	15
Statement of changes in equity	16
Statement of cash flows	17
Notes to the financial statements	18 - 75

FINCA MICROFINANCE BANK LIMITED

CORPORATE INFORMATION

DIRECTORS	Name	Position	Nationality	Date of appointment/ Resignation
	Mike Gama-Lobo	Chairman	American	Appointed on 1 October 2015
	Edward Talawa	Member	Tanzanian	Appointed on 16 March 2017
	Volker Renner	Member	Germany	Appointed on 31 May 2017
	Monica Joseph	Member	Tanzanian	Appointed on 2 September 2015
	Kelvin Twissa	Member	Tanzanian	Appointed on 1 October 2015

KEY MANAGEMENT	Name	Position	Nationality	Resignation date
	Issa Ngwegwe	Chief Executive Officer	Tanzanian	07 December 2018
	Bastiaan Nierop	Chief Executive Officer	Tanzanian	Appointed on 15 th March 2019

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

AUDITORS KPMG
Certified Public Accountants
2nd Floor, The Luminary,
Haile Selassie Road
P.O. Box 1160
Dar es Salaam, Tanzania
Telephone: +255 22 2600330
Fax No. +255 22 2600490

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

FINCA MICROFINANCE BANK LIMITED

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

Attorneys at Law and Management Consultants
477 Prince Street/Adjacent to Lugalo Golf Club
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

Octavian and Bank
2nd Floor, NIC Life House,
Sokoine Drive/Ohio Street,
P. O. Box 77353,
Dar es Salaam, Tanzania

PRINCIPAL FINANCIERS Blue Orchard Microfinance Fund
Symbiotics Sicav (Lux.)
MCE Social Capital
REFFA Fund
agRIF Cooperatief U.A.
Global Partnerships Social Investment Fund 6.0 LLC
Access Africa Fund LLC
Financial Sector Deepening Trust Tanzania (FSDT)

FINCA MICROFINANCE BANK LIMITED

REPORT OF THE DIRECTORS FOR THE YEAR ENDED 31 DECEMBER 2018

The Directors present their annual report together with the audited financial statements for the year ended 31 December 2018, 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 Finca Microfinance Bank is the provision of banking and related financial services stipulated under the Banking and Financial Institutions (Microfinance Activities) regulation 2014.

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. This is accomplished through offering financial services to individual entrepreneurs and principally through the creation of group lending representing peer groups of approximately 5 members to whom two critical services are provided as follows:

- a) Working capital loans to finance self-employment activities; and
- b) Mutual support for personal growth.

BANK SECRETARY

Bank Secretary during the year ended 31 December 2018 was Mr. 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 for 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
Monica Joseph	Member	Tanzania	12 November 2017
Edward Talawa	Member	Tanzania	12 November 2017

FINCA MICROFINANCE BANK LIMITED

REPORT OF THE DIRECTORS (CONTINUED)

CORPORATE GOVERNANCE (CONTINUED)

Asset-Liability Committee

Name	Position	Country of residence	Date of appointment
Monica Joseph	Chairperson	Tanzania	12 November 2017
Mike Gama-Lobo	Member	American	12 November 2017
Volker Renner	Member	Germany	12 November 2017

Risk Committee

Name	Position	Country of residence	Date of appointment
Edward Talawa	Chairperson	Tanzania	12 November 2017
Kelvin Twissa	Member	Tanzania	12 November 2017
Volker Renner	Member	Germany	12 November 2017

Human Resources Committee

Name	Position	Country of residence	Date of appointment
Kelvin Twissa	Chairperson	Tanzania	12 November 2017
Edward Talawa	Member	Tanzania	12 November 2017
Mike Gama-Lobo	Member	American	12 November 2017

CAPITAL STRUCTURE

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

	2018 TZS '000	2017 TZS '000
Authorized share capital		
35,000,000 ordinary shares of TZS 1,000 each	<u>35,000,000</u>	<u>25,000,000</u>
Issued and fully paid capital		
31,574,605 (2017: 23,030,150) ordinary shares of TZS 1,000 each	<u>31,574,605</u>	<u>23,030,150</u>

SHAREHOLDERS OF THE BANK

The total number of shareholders during the year 2018 was two. There were no Directors holding shares in the Bank.

Shareholding structure of the Bank was as follows:

	2018	2017
FINCA Microfinance Holding Bank LLC	31,574,604	23,030,149
FINCA International LLC	<u>1</u>	<u>1</u>
	<u>31,574,605</u>	<u>23,030,150</u>

FINCA MICROFINANCE BANK LIMITED

REPORT OF THE DIRECTORS (CONTINUED)

MANAGEMENT

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

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

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 of TZS 10,459,641,000 (2017: Loss of TZS 5,621,000,000). The Directors do not propose payment of dividend for the year ended 31 December 2018 (2017: Nil).

PERFORMANCE FOR THE YEAR

The following is a summary highlight of the Bank's performance.

	2018	2017
Branches	24	24
Total number of staff	488	528
Gross outstanding portfolio (TZS `000)	59,265,785	69,267,528
Total current and demand accounts (TZS `000)	35,079,755	45,155,021
Total assets (TZS `000)	100,103,798	108,351,319
Portfolio At Risk > 1 day (PAR 1)	9.72%	13.02%
Portfolio At Risk over 30 days (PAR 30)	6.66%	9.54%
Portfolio yield	45.6%	46.7%
Debt/Equity	162.2%	158.9%
Total deposits/gross loans and advances	59.2%	65.2%
Capital/assets	31.7%	19.9%

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 as expected 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 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;

FINCA MICROFINANCE BANK LIMITED

REPORT OF THE DIRECTORS (CONTINUED)

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 2018 and is of the opinion that they met accepted criteria.

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

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 foreseeable future.

EMPLOYEES' WELFARE

Management and Employees' Relationship

There were continued good relations between employees and management for the year 2018. 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 Forum. 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.

When presenting its annual budget for the year 2018, the Bank allocated a sum of TZS 170 million for staff training in order to improve employees' technical skills and hence effectiveness (2017: TZS 600 million).

Medical Assistance

All members of staff with a maximum number of four beneficiaries (dependents) for each employee were availed medical insurance. Currently AAR Health Insurance provides these services.

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 of 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.

FINCA MICROFINANCE BANK LIMITED

REPORT OF THE DIRECTORS (CONTINUED)

EMPLOYEES' WELFARE (CONTINUED)

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, every effort made to ensure that their 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 Parastatal Pension Fund (PPF), Local Authorities Pension Fund (LAPF) or National Social Security Fund (NSSF). The funds are defined contribution pension schemes with the Bank having no legal or constructive obligation to pay further top-up contributions.

The average number of employees during the year was 488 employees (2017: 528 employees).

GENDER PARITY

The Bank had 488 employees, out of which 252 were female and 236 were male (2017: 528 employees).

RELATED PARTY TRANSACTIONS

All related party transactions and balances are disclosed in note 24 to these financial statements.

POLITICAL AND CHARITABLE DONATIONS

The Bank did not make any political donations during the year (2017: Nil).

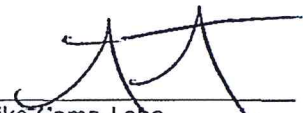
ENVIRONMENTAL CONTROL PROGRAMME

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 auditors, KPMG have expressed their willingness to continue in office. A resolution proposing the appointment of auditor of the Bank for the financial year 2018 will be tabled at the Annual General Meeting.

BY ORDER OF THE BOARD


Mike Gama-Lobo
Chairman
17th April 2019


Monica Joseph
Director

FINCA MICROFINANCE BANK LIMITED

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 2018, 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.

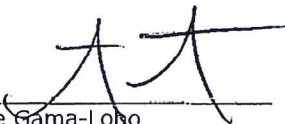
The Directors are also responsible for such internal control as the directors determine is necessary to enable the preparation of financial statements that are free from material misstatement, whether due to fraud or error, and for maintaining adequate accounting records and an effective system of risk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

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


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 in the year ahead.

Approval of financial statements

The financial statements of FINCA microfinance Bank Limited as identified in the first paragraph, were approved by the board of directors on 17th April 2019 and signed by:



Mike Gama-Lobo
Chairman



Monica Joseph
Director

FINCA MICROFINANCE BANK LIMITED

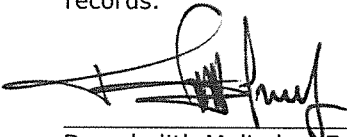
DECLARATION OF THE CHIEF FINANCIAL OFFICER

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, **Deusedith Mulindwa Edward**, being the Chief Financial Officer of Finca Microfinance Bank Limited hereby acknowledge my responsibility of ensuring that financial statements for the year ended 31 December 2018 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.



Deusedith Mulindwa Edward
Head of Finance

NBAA Membership No.: ACPA 30323

...17 April 2019



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Certified Public Accountants
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INDEPENDENT AUDITORS' 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 75, which comprise the statement of financial position as at 31 December 2018, the statements of profit or loss and other comprehensive income, changes in equity and cash flows for the year then ended, and a summary of significant accounting policies and other explanatory information.

In our opinion, the Banking financial statements give a true and fair view of the financial position of the FINCA Microfinance Bank Limited as at 31 December 2018, 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 Auditors' 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 Code of Ethics for Professional Accountants (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.



**INDEPENDENT AUDITORS' REPORT TO THE SHAREHOLDERS OF
FINCA MICROFINANCE BANK LIMITED (CONTINUED)**

Impairment of loans and advances (Refer to Note 6(F) and Note 17)	
The key matter	How the matter was addressed in our audit
<p>Loans and advances for the Bank amounted to TZS 56,791,916,000 at 31 December 2018 (TZS 64,059,610,000 at 31 December 2017), and the total impairment allowance for the Bank amounted to TZS 2,473,869,000 at 31 December 2018 (TZS 5,207,918,000 at 31 December 2017).</p> <p>On 1 January 2018, the Bank adopted IFRS 9, resulting in impairment charges being recognised when losses are expected rather than when they are incurred. Management has disclosed information regarding the transitional effect of this new standard in Note 5 (b).</p> <p>Measurement of loan impairment charges for loans 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.</p> <p>The key areas where we identified significant levels of management judgement and therefore increased levels of audit focus on the Bank's implementation of IFRS 9 are:</p> <ul style="list-style-type: none"> • Assumptions used in determining criteria for significant increase in credit risk. • Choosing appropriate models and assumptions for the 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 for each type of product/market and the associated impact on ECL • Establishing groups of similar financial assets for the purposes of measuring ECL 	<p>Based on our risk assessment and industry knowledge, we have examined the impairment charges for loans and advance and evaluated the methodology applied as well as the assumptions made according to the description of the key audit matter.</p> <p>Our audit procedures in this area, included, among others:</p> <ul style="list-style-type: none"> • Testing of controls over assumptions used in the expected credit loss models to assess the credit risk related to the exposure and the expected future cash flows. • Testing of controls over the compilation and review of the credit watch list, credit file review processes, approval of external collateral valuation vendors and review of controls over the approval of significant individual impairments. • Reviewing management model for establishing Stage 3 impairment amounts. This includes challenging reasonability of management assumptions through among others performing retrospective review of prior year assumptions and reviewing basis for write offs. • Selecting a sample from the Bank's loan book and carry out tests to establish whether significant facilities are correctly staged/classified and valued based on IFRS as well as regulatory considerations; • Testing of a sample of key data inputs and assumptions impacting ECL calculations to assess the reasonableness of economic forecasts and PD assumptions applied; • Evaluating the appropriateness of the Bank's IFRS 9 methodologies including the Significant Increase in Credit Risk (SICR) criteria used; • Testing the impairment calculations to check if the correct parameters – Probability of Default (PDs), Loss Given Default (LGDs), and Exposure at Default (EADs) were determined by considering local economic/portfolio factors; • Reviewing management method of determining groups of similar financial assets for purposes of measuring ECL to confirm that assets are properly stratified based on existing economic trends; and • Assessing whether the disclosures appropriately disclose the key judgements and assumptions used in determining the expected credit losses.



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

Other Information

The directors are responsible for the other information. The other information comprises the Corporate information, Report of the Directors as required by the Companies Act, 2002, Statement of Directors' responsibilities and Declaration of Head of Finance. The other information does not include the financial statements and our auditors' 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.

The financial statements of the Bank as at and for the year ended 31 December 2017 were audited by another auditor who expressed an unmodified opinion on those statements on 13 April 2018.

Responsibilities of Directors for the Financial Statements

As stated on page 8, the directors are responsible for the preparation of financial statements that give a true and fair view in accordance with International Financial Reporting Standards and in the manner required by the Companies Act, 2002 and Banking and Financial Institutions Act, 2006, and for such internal control as 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, 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 directors either intend to liquidate the Bank or to cease operations, or have no realistic alternative but to do so.

The directors are responsible for overseeing the Bank's financial reporting process.

Auditors' 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 auditors' 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 International Standards on Auditing ("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 scepticism 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.



**INDEPENDENT AUDITORS' REPORT TO THE SHAREHOLDERS OF
FINCA MICROFINANCE BANK LIMITED (CONTINUED)**

- 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 directors.
- Conclude on the appropriateness of 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 auditors' 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 auditors' report. However, future events or conditions may cause the Bank to cease to continue as a going concern.
- 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 those charged with governance 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 those charged with governance, 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 auditors' 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:

- proper records have been kept by Finca Microfinance Bank Limited;
- the individual accounts are in agreement with the accounting records of the Bank; and
- we obtained all the information and explanations which, to the best of our knowledge and belief, are necessary for the purposes of our audit.

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.

**KPMG
Certified Public Accountants (T)**

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

17 April 2019

FINCA MICROFINANCE BANK LIMITED

STATEMENT OF PROFIT OR LOSS AND OTHER COMPREHENSIVE INCOME
FOR THE YEAR ENDED 31 DECEMBER 2018

	Notes	2018 TZS '000	2017 TZS '000
Income			
Interest and similar income	8	25,676,147	30,466,536
Interest and similar expense	9	<u>(7,636,145)</u>	<u>(9,831,002)</u>
Net interest income		<u>18,040,002</u>	<u>20,635,534</u>
Impairment on loans and advances to customers	17	<u>(3,633,766)</u>	<u>(7,132,607)</u>
Net interest income after loan impairment charge		<u>14,406,236</u>	<u>13,502,927</u>
Fees and commission income	27	5,768,820	5,333,491
Fees and commission expense		<u>(612,350)</u>	<u>(491,543)</u>
Net fee and commission income		<u>5,156,470</u>	<u>4,841,948</u>
Net income from lending activities		<u>19,562,706</u>	<u>18,344,875</u>
Grant income	10	235,653	926,916
Other losses	11	(34,885)	(61,575)
Personnel expenses	12	(13,151,047)	(12,120,681)
Operating expenses	13	(15,737,655)	(13,782,883)
Depreciation and amortisation	20 & 21	<u>(2,076,570)</u>	<u>(1,475,929)</u>
Loss before tax		<u>(11,201,798)</u>	<u>(8,169,277)</u>
Income tax credit	14(a)	<u>1,706,684</u>	<u>2,548,277</u>
Loss for the year		<u>(9,495,114)</u>	<u>(5,621,000)</u>
Other comprehensive income		<u>-</u>	<u>-</u>
Total comprehensive loss for the year		<u>(9,495,114)</u>	<u>(5,621,000)</u>

Notes and related statements forming part of these financial statements appear on pages 18 to 75.

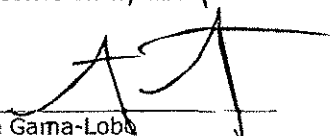
Report of the auditors is on page 10 to 13.


FINCA MICROFINANCE BANK LIMITED

STATEMENT OF FINANCIAL POSITION
AS AT 31 DECEMBER 2018

	Notes	2018 TZS '000	2017 TZS '000
ASSETS			
Cash and bank balances	16	16,024,342	6,995,694
Investment in fixed deposits	15	11,433,077	22,286,454
Loans and advances to customers	17	56,791,916	64,059,610
Due from related parties	24	128,233	62,777
Tax recoverable	14(d)	-	14,357
Other assets	18	3,252,385	3,162,255
Deferred tax assets	14(c)	4,957,545	3,215,105
Work in progress	19	2,681,890	4,417,588
Property and equipment	20	3,269,071	3,036,312
Intangible assets	21	1,565,339	1,101,167
Total assets		100,103,798	108,351,319
LIABILITIES AND EQUITY			
Liabilities			
Deposits from customers	22	28,359,996	24,852,821
Deposits from banks	22	6,719,759	20,302,200
Borrowings	23	34,937,760	34,352,369
Amounts due to related parties	24	114,311	562,847
Deferred grants	25	961,118	1,482,286
Tax payable	14(d)	368,089	-
Other payables	26	7,168,000	5,182,316
Total liabilities		78,629,033	86,734,839
Capital and reserves			
Share capital		31,574,605	23,030,150
Accumulated losses		(12,208,092)	(2,783,834)
General provision reserve		522,010	590,073
Statutory reserve		1,586,242	780,091
Total equity		21,474,765	21,616,480
Total liabilities and equity		100,103,798	108,351,319

The financial statements on pages 14 to 75 were approved and authorised for issue by the Board of Directors on 13th April 2019 and were signed on its behalf by:


Mike Gama-Loba
Chairman


Monica Joseph
Director

Notes and related statements forming part of these financial statements appear on pages 18 to 75.

FINCA MICROFINANCE BANK LIMITED

STATEMENT OF CHANGES IN EQUITY
FOR THE YEAR ENDED 31 DECEMBER 2018

	Share capital TZS'000	Accumulated losses/Retained earnings TZS'000	Regulatory reserve** TZS'000	General Reserve* TZS'000	Total TZS'000
At 1 January 2017	23,030,150	3,491,446	-	715,884	27,237,480
Issue of shares	-	(5,621,000)	-	-	(5,621,000)
Total comprehensive income for the year	-	125,811	-	(125,811)	-
General provision reserve*	-	(780,091)	780,091	-	-
Regulatory reserve**					
At 31 December 2017	<u>23,030,150</u>	<u>(2,783,834)</u>	<u>780,091</u>	<u>590,073</u>	<u>21,616,480</u>
At 1 January 2018	23,030,150	(2,783,834)	780,091	590,073	21,616,480
IFRS 9 impact net of tax	-	808,944	-	-	808,944
Adjusted balance at 1 January 2018	23,030,150	(1,974,890)	780,091	590,073	22,425,424
Transactions with owners of the Bank					
Issue of share	8,544,455	-	-	-	8,544,455
Total comprehensive loss for the year					
Loss for the year	-	(9,495,114)	-	-	(9,495,114)
General provision reserve*	-	68,063	-	(68,063)	-
Regulatory reserve**	-	(806,151)	806,151	-	-
At 31 December 2018	<u>31,574,605</u>	<u>(12,208,092)</u>	<u>1,586,242</u>	<u>522,010</u>	<u>21,474,765</u>

*General provision reserve represents a provision of 1% on current loans which is made as per The Banking and Financial Institutions (Management of Risk Assets) Regulation, 2014. The reserve is not distributable.

**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 75.

Report of the auditors is on page 10 to 13.

FINCA MICROFINANCE BANK LIMITED

STATEMENT OF CASH FLOWS
FOR THE YEAR ENDED 31 DECEMBER 2018

	Notes	2018 TZS '000	2017 TZS '000
Cash flows from operating activities			
Loss before tax		(11,201,798)	(8,169,277)
<i>Adjustments for:</i>			
Depreciation	20	1,234,778	1,173,266
Amortisation	21	841,792	302,663
Impairment loss on loans and advances to customers	17	3,633,766	2,880,675
Gain on disposal of property and equipment		(6,769)	-
Interest expense on term loans	9	3,337,724	6,016,553
Grant income	10	(235,653)	(926,916)
		(2,396,160)	1,276,964
<i>Working capital changes</i>			
Decrease in loans and advances to customers		4,789,562	7,139,005
Decrease/(Increase) in other assets		(90,130)	169,389
Increase in deposits from customers and banks		(10,075,266)	16,935,356
Increase in other payables		1,985,684	2,698,332
Income tax paid	14(d)	-	(178,316)
Net movement in related party balances		(513,991)	589,932
		(6,300,301)	28,630,662
Cash flows from investing activities			
Purchase of property and equipment	20	(1,467,538)	(814,953)
Purchase of intangible assets	21	(1,305,964)	(200,678)
Payments for work in progress	17	1,735,698	(3,336,030)
Proceeds from disposal of property and equipment		6,769	-
		(1,031,035)	(4,351,661)
Cash flows from financing activities			
Increase /(Decrease) in borrowings	23	1,140,300	(6,102,668)
Interest paid on term loans		(3,892,633)	(6,417,883)
Proceeds from deferred grants		(285,515)	1,672,415
Proceeds from issue of shares		8,544,455	-
		5,506,607	(10,848,136)
Net increase in cash and cash equivalents			
		(1,824,729)	13,430,865
Cash and cash equivalents at beginning of the year			
		<u>29,282,148</u>	<u>15,851,283</u>
Cash and cash equivalents at the end of the year			
		<u>27,457,419</u>	<u>29,282,148</u>
Cash and cash equivalents:			
Cash and bank balance	16	16,024,342	6,995,694
Investments in fixed deposits	15	11,433,077	22,286,454
		<u>27,457,419</u>	<u>29,282,148</u>

Notes and related statements forming part of these financial statements appear on pages 18 to 75.

Report of the auditors is on page 10 to 13

1. REPORTING ENTITY

FINCA Microfinance Bank Limited 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 under the historical cost convention except for certain financial instruments that are measured at revalued amounts or fair values. Historical cost is generally based on the fair value of the consideration given in exchange for assets.

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.

This is the first set of the annual financial statements in which IFRS 9 Financial Instruments and IFRS 15 Revenue from Contracts with Customers have been applied. Changes to significant accounting policies are described in Note 5.

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.

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

Applicable to 2018 only:

Note 6: 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.

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

4. USE OF JUDGEMENTS AND ESTIMATES (CONTINUED)

Applicable to 2018 and 2017:

(a) Fair value of financial instruments

The fair values of financial instruments that are not quoted in active markets are determined by using valuation techniques. Where valuation techniques (for example, models) are used to determine fair values, they are validated and periodically reviewed by qualified personnel independent of the area that created them. All models are certified before they are used, and models are calibrated to ensure that outputs reflect actual data and comparative market prices.

(e) Impairments of property and equipment

Property and equipment are reviewed for impairments whenever events or changes in circumstances indicate that the carrying amount may not be recoverable. An asset carrying amount is written down immediately to its recoverable amount if the asset's carrying amount is greater than estimated recoverable amount. Gains or losses on disposals are determined by comparing proceeds with the carrying amount. These are included in the profit and loss accounts.

5. CHANGES IN SIGNIFICANT ACCOUNTING POLICIES

The Bank initially applied IFRS 15 and IFRS 9 from 1 January 2018. A number of other new standards are also effective from 1 January 2018 but they do not have a material effect on the Bank's financial statements.

Due to the transition methods chosen by the Bank in applying these standards, comparative information throughout these financial statements has not been restated to reflect the requirements of the new standards. Any adjustments to the carrying amounts of financial assets and financial liabilities at the date of transition were recognised in the opening retained earnings and other reserves of the current period.

Consequently, for notes disclosures, the consequential amendments to IFRS 7 disclosures have also only been applied to the current period. The comparative period notes disclosures repeat those disclosures made in the year.

The adoption of IFRS 15 did not impact the timing or amount of fee and commission income from contracts with customers and the related assets and liabilities recognised by the Bank. Accordingly, the impact on the comparative information is limited to new disclosure requirements.

The effect of initially applying these standards is mainly attributed to an increase in impairment losses recognised on financial assets, additional disclosures related to IFRS 9 and additional disclosures related to IFRS 15.

(a) IFRS 15 Revenue from Contracts with Customers

IFRS 15 establishes a comprehensive framework for determining whether, how much and when revenue is recognised. It replaced IAS 18 Revenue, IAS 11 Construction Contracts and related interpretations. Under IFRS 15, revenue is recognised when a customer obtains control of the goods or services. Determining the timing of the transfer of control – at a point in time or over time – requires judgement.

The Bank has adopted IFRS 15 using the cumulative effect method (without practical expedients), with the effect of initially applying this standard recognised at the date of initial application (i.e. 1 January 2018). Accordingly, the information presented for 2017 has not been restated – i.e. it is presented, as previously reported, under IAS 18 and related interpretations. Additionally, the disclosure requirements in IFRS 15 have not generally been applied to comparative information.

There was no material impact on the Bank's statement of financial position as at 31 December 2018 and its statement of profit or loss and Other Comprehensive Income ("OCI") and statement of cash flows for the year then ended for each of the revenue line items affected.

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

5. CHANGES IN SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)**(b) IFRS 9 Financial Instruments**

IFRS 9 sets out requirements for recognising and measuring financial assets, financial liabilities and some contracts to buy or sell non-financial items. This standard replaces IAS 39 Financial Instruments: Recognition and Measurement.

The Bank has been presenting impairment of loans and advances (being the most significant financial asset) in a separate line item in the statement of profit or loss and OCI. Impairment losses on other financial assets such as trade receivables are presented under 'other operating expenses', similar to the presentation under IAS 39, and not presented separately in the statement of profit or loss and OCI due to materiality considerations.

Additionally, the Bank has adopted consequential amendments to IFRS 7 Financial Instruments: Disclosures that are applied to 2018 disclosures but have not been generally applied to comparative information.

The following table summarises the impact, net of tax, of transition to IFRS 9 on the opening balance of reserves and retained earnings (for a description of the transition method)

	Impact of adopting IFRS 9 on opening balance TZS'000
Retained earnings	
Recognition of expected credit losses under IFRS 9	1,155,634
Related tax	(346,690)
Impact at 1 January 2018	<u>808,944</u>

i. Classification and measurement of financial assets and financial liabilities

IFRS 9 contains three principal classification categories for financial assets: measured at amortised cost, Fair Value through Other Comprehensive Income ("FVTOCI") and Fair Value through Profit and Loss ("FVTPL"). The classification of financial assets under IFRS 9 is generally based on the business model in which a financial asset is managed and its contractual cash flow characteristics. IFRS 9 eliminates the previous IAS 39 categories of held to maturity, loans and receivables and available for sale. Under IFRS 9, derivatives embedded in contracts where the host is a financial asset in the scope of the standard are never separated. Instead, the hybrid financial instrument as a whole is assessed for classification.

IFRS 9 largely retains the existing requirements in IAS 39 for the classification and measurement of financial liabilities.

The adoption of IFRS 9 has not had a significant effect on the Bank's accounting policies related to financial liabilities. For an explanation of how the Bank classifies and measures financial liabilities under IFRS 9, see Note 6.

The following table and notes below explain the original measurement categories under IAS 39 and the new measurement categories under IFRS 9 for each class of the Bank's financial assets and financial liabilities as at 1 January 2018.

The effect of adopting IFRS 9 on the carrying amounts of financial assets at 1 January 2018 relates solely to the new impairment requirements.

5. CHANGES IN SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)**(b) IFRS 9 Financial Instruments (Continued)****i. Classification and measurement of financial assets and financial liabilities (Continued)**

	Original classification Under IAS 39	New classification Under IFRS 9	Original carrying amount under IAS 39 TZS'000	New carrying amount under IFRS 9 TZS'000
Financial assets				
Cash and balances with Bank of Tanzania	Loans and receivables	Amortised cost	3,168,280	3,168,280
Balances with other Banks	Loans and receivables	Amortised cost	3,827,414	3,827,414
Placements with Banks	Loans and receivables	Amortised cost	11,433,077	11,433,077
Loans and advances to customers	Loans and receivables	Amortised cost	64,059,610	65,215,244
Other assets	Amortised cost	Amortised cost	892,006	892,006
Total Financial assets			83,380,387	84,536,021
Financial liabilities				
Deposits from other banks	Amortised cost	Amortised cost	20,302,200	20,302,200
Deposits from customers	Amortised cost	Amortised cost	24,852,821	24,852,821
Other liabilities	Amortised cost	Amortised cost	3,919,616	3,919,616
Total financial liabilities			49,074,637	49,074,637

*FVOCI = Fair value through other comprehensive income

The Bank's accounting policies on the classification of financial instruments under IFRS 9 are set out in Note 5(b)(i). The application of these policies resulted in the reclassifications set out in the table above and explained below.

(a) Trade and other receivables that were classified as loans and receivables under IAS 39 are now classified at amortised cost. A decrease of TZS 1,248 million in the allowance for impairment over these receivables was recognised in opening retained earnings at 1 January 2018 on transition to IFRS 9 net of deferred tax.

The following table reconciles the carrying amounts of financial assets under IAS 39 to the carrying amounts under IFRS 9 on transition to IFRS 9 on 1 January 2018.

5. CHANGES IN SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)**(b) IFRS 9 Financial Instruments (Continued)****i. Classification and measurement of financial assets and financial liabilities (Continued)**

	IAS 39 carrying amount 31 December 2017 TZS'000	Reclassification TZS '000	Re- measurement TZS '000	IFRS 9 carrying amount 1 January 2018 TZS '000
Financial assets				
Loan and receivable				
Cash and cash equivalents:				
Opening balance	6,995,694	-	-	-
Re-measurement				
Closing balance:				6,995,694
Loans and advances to customers				
Opening balance	64,059,610	-		
Re-measurement			1,155,634	
Closing balance:				65,215,244
Total	71,055,304	-	1,155,634	72,210,938
Financial liabilities				
Amortised cost				
Deposits from other Banks:				
Opening balance:	20,302,200	-	-	
Closing balance				20,302,200
Deposits from customers:				
Opening balance:	24,852,821	-	-	
Closing balance				24,852,821
Other liabilities:				
Opening balance:	3,919,616	-	-	
Closing balance				3,919,616
Total amortised cost	<u>49,074,637</u>	<u>-</u>	<u>-</u>	<u>49,074,637</u>

5. CHANGES IN SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

IFRS 9 Financial Instruments (Continued)

ii. Impairment of financial assets

IFRS 9 replaces the 'incurred loss' model in IAS 39 with an 'expected credit loss' model. The new impairment model also applies to certain loan commitments and financial guarantee contracts but not to equity investments.

Under IFRS 9, credit losses are recognised earlier than under IAS 39. For an explanation of how the Bank applies the impairment requirements of IFRS 9, see Note 5(b) (iii).

iii. Transition

Changes in accounting policies resulting from the adoption of IFRS 9 have been applied retrospectively, except as described below.

- The Bank has used an exemption not to restate comparative information for prior periods with respect to classification and measurement (including impairment) requirements.
- Differences in the carrying amounts of financial assets and financial liabilities resulting from the adoption of IFRS 9 are recognised in retained earnings and reserves as at 1 January 2018. Accordingly, the information presented for 2017 does not generally reflect the requirements of IFRS 9, but rather those of IAS 39.
- The following assessments have been made on the basis of the facts and circumstances that existed at the date of initial application.
 - The determination of the business model within which a financial asset is held.
 - The designation and revocation of previous designations of certain financial assets and financial liabilities as measured at FVTPL.
 - The designation of certain investments in equity instruments not held for trading as at FVOCI.

(c) IFRS 15 Revenue from Contracts with Customers

IFRS 15 establishes a comprehensive framework for determining whether, how much and when revenue is recognised. It replaced IAS 18 revenue, IAS 11 construction contracts and related interpretations.

The Bank initially applied IFRS 15 on 1 January 2018 retrospectively in accordance with IAS 8 without any practical expedients. The timing or amount of the Bank's fee and commission income from contracts with customers was not impacted by the adoption of IFRS 15. The impact of IFRS 15 was limited to the new disclosure requirements.

The significant accounting policies applied in preparation of these financial statements are set out below.

6. SIGNIFICANT ACCOUNTING POLICIES

The principal accounting policies adopted 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. Foreign exchange gains and losses resulting from the settlement of such transactions and from the translation at year-end exchange rates of monetary assets and liabilities denominated in foreign currencies are recognised in the profit or loss in the year in which they arise.

6. SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

(a) Foreign currencies (continued)

Foreign currency non-monetary items measured at fair value are translated into functional currency using the rate of exchange at the date the fair value was determined. Foreign currency gains and losses on non-monetary items are recognized in profit or loss. Foreign currency differences arising from available for sale equity investments (before 1 January 2018) or equity instruments in respect of which an election has been made to present subsequent changes in fair value in OCI (from 1 January 2018) are recognized in OCI.

(b) Income recognition

Policy applicable from 1 January 2018

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

Gains and losses arising from changes in the fair value of financial assets and liabilities at fair value through profit or loss, as well as any interest receivable or payable, are included in profit or loss in the period in which they arise.

Gains and losses arising from changes in the fair value of FVOCI financial assets, other than foreign exchange gains or losses from monetary items, are recognised directly in other comprehensive income, until the financial asset is derecognised or impaired at which time the cumulative gain or loss previously recognised in other comprehensive income is recognised in profit or loss.

i) *Net interest income*

Policy applicable from 1 January 2018

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 ECL.

For 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.

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 (or impairment allowance before 1 January 2018).

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

6. SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

(b) Income recognition (continued)

Calculation of interest income and expense

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.

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.

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 on debt instruments measured at Fair Value through OCI;
- the effective portion of fair value changes in qualifying hedging derivatives designated in cash flow hedges of variability in interest cash flows, in the same period as the hedged cash flows affect interest income/expense; and
- the effective portion of fair value changes in qualifying hedging derivatives designated in fair value hedges of interest rate risk.

Interest income and expense on all trading assets and liabilities are considered to be incidental to the bank's trading operations and are presented together with all other changes in the fair value of trading assets and liabilities in net trading income.

Interest income and expense on other financial assets and financial liabilities at FVTPL are presented in net income from other financial instruments at FVTPL.

ii) *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.

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.

6. SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

(b) Income recognition (continued)

Policy applicable before 1 January 2018

iii) Net trading income and net income on financial assets at fair value through profit or loss

'Net trading income and net income on financial assets at fair value through profit or loss' comprises gains less losses related to trading assets and liabilities, and includes all fair value changes, interest, dividends and foreign exchange differences.

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

Gains and losses arising from changes in the fair value of financial assets and liabilities at fair value through profit or loss, as well as any interest receivable or payable, are included in profit or loss in the period in which they arise.

i) Net interest income

Interest income and expense on available-for-sale assets and financial assets or liabilities held at amortised cost is recognised in profit or loss using the effective interest method.

When calculating the effective interest rate, the bank estimates the cash flows considering all contractual terms of the financial instrument but does not consider future credit losses. The calculation includes all fees and points paid or received, between the parties to the contract that are an integral part of the effective interest rate, transaction costs and all other discounts and premiums. Transaction costs are incremental costs that are directly attributable to the acquisition, issue or disposal of a financial asset or liability.

Once a financial asset or a group of similar financial assets has been written down as a result of an impairment loss, interest income is recognised using the rate of interest used to discount the future cash flows for the purpose of measuring the impairment loss.

Interest income and expense on all trading assets and liabilities are considered to be incidental to the bank's trading operations are presented in net interest income.

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

(c) Other operating income

Other operating income comprises gains less losses related to trading assets and liabilities and includes all realised and unrealised fair value changes, interest and foreign exchange differences. It also includes rental income and gain on disposal of property and equipment.

6. SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

(d) Dividend income

Dividend income is recognised when the right to receive income is established. Dividends are reflected as a component of operating income.

(e) 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.

Current tax is the expected tax payable or receivable on the taxable income for the year using tax rates enacted or substantively enacted at the reporting date, and any adjustment to tax payable in respect of previous years.

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.

A deferred tax asset is recognised for unused tax losses, 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 utilised. 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 realized.

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.

(f) Financial assets and liabilities

Policy applicable from 1 January 2018

i) Recognition

The bank initially recognises loans and advances, deposits and debt securities on the date at which they are originated. All other financial assets and liabilities (including assets designated at fair value through profit or loss) are initially recognised on the trade date on which the bank becomes a party to the contractual provision of the instrument.

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.

6. SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

(f) Financial assets and liabilities (continued)

Policy applicable from 1 January 2018 (continued)

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
- 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.

6. SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)**(f) Financial assets and liabilities (continued)****Policy applicable from 1 January 2018 (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
Loans to customers	Hold to collect contractual cash flows	Cash flows are not solely payments of principal and interest	FVPL (Mandatory)
Trading assets	Hold to collect contractual cash flows	Cash flows are not solely payments of principal and interest	FVPL (Mandatory)
Derivative financial instruments	Other business model	Cash flows are not solely payments of principal and interest	FVPL (Mandatory)

6. SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

(f) Financial assets and liabilities (continued)

Policy applicable from 1 January 2018 (continued)

Reclassifications

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

Financial liabilities

The bank classifies its financial liabilities, other than financial guarantees and loan commitments, as measured at amortised.

iii) Impairment

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

- financial assets that are debt instruments (amortised cost and FVOCI) including loans and advances;
- lease receivables (rental income collected from Investment properties);

No impairment loss is recognised on equity investments.

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

- Investment in government securities that are determined to have low credit risk at the reporting date.
- 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'.

Life-time ECL are the ECL that result from all possible default events over the expected life of the financial instrument. Financial instruments for which a lifetime ECL is recognised but which are not credit-impaired are referred to as 'Stage 2 financial instruments'.

Measurement of expected credit loss allowance

The measurement of the ECL allowance for financial assets measured at amortized cost and FVOCI is an area that requires the use of complex models and significant assumptions about future economic conditions and credit behaviour (e.g., the likelihood of customers defaulting and the resulting losses).

6. SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

(f) Financial assets and liabilities (continued)

Policy applicable from 1 January 2018 (continued)

Measurement of expected credit loss allowance (continued)

A number of significant judgments are also required in applying the accounting requirements for measuring ECL, such as:

- Determining criteria for significant increase in credit risk;
- Choosing appropriate models and assumptions for the measurement of ECL;
- Establishing the number and relative weightings of forward-looking scenarios for each type of product/market and the associated ECL; and
- Establishing groups of similar financial assets for the purposes of measuring ECL. Financial guarantee: The present value of the expected payments to reimburse the holder less any amounts that Bank expect to recover.

Measurement of ECL is affected 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.

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.

6. SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

(f) Financial assets and liabilities (continued)

Policy applicable from 1 January 2018 (continued)

Credit risk grade (continued)

IFRS 9 allows credit exposures to migrate from higher credit risk categories to lower credit risk categories, that is, from stage 3 to stage 2 and from stage 2 to stage 1. Instruments falling under stage 1 applies 12 Months ECL model while those under stage 2 and stage 3 applies Life time ECL. Migration from stage 3 to stage 2 shall consider criteria for upgrading required by the Bank of Tanzania. On the other hand, credit exposures may migrate from stage 2 to stage 1 when there is a significant improvement of the credit exposure. Before upgrading instrument from stage 2 to stage 1, the Bank shall consider whether the facilities are Up-to-date with payments as well as the improvement of the quantitative and qualitative factors that caused significant increase of the credit risk.

Modified financial assets

The contractual terms of 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.

Under IFRS 9, 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 asset 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;

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, 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.

6. SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)**(f) Financial assets and liabilities (continued)****Policy applicable from 1 January 2018 (continued)****Inputs into measurement of ECLs (continued)**

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 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. 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	8.31	9.05	9.60

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.

6. SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

(f) Financial assets and liabilities (continued)

Policy applicable from 1 January 2018 (continued)

Credit-impaired financial assets (continued)

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

- significant financial difficulty of the borrower or issuer;
- 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;
- 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;
- loan commitments and financial guarantee contracts: generally, as a provision; (See note 31)
- where a financial instrument includes both a drawn and an undrawn component, and the bank cannot identify the ECL on the loan commitment component separately from those on the drawn component: the bank presents a combined loss allowance for both components. The combined amount is presented as a deduction from the gross carrying amount of the drawn component. Any excess of the loss allowance over the gross amount of the drawn component is presented as a provision; and
- 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.

Financial assets

iv) De-recognition of 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.

6. SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

(f) Financial assets and liabilities (continued)

Policy applicable from 1 January 2018 (continued)

Financial assets (continued)

iv) De-recognition of financial assets (continued)

On de-recognition 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 OCI is recognised in profit or loss.

From 1 January 2018 any cumulative gain/loss recognised in OCI in respect of equity investment securities designated as at FVOCI is not recognised in profit or loss on de-recognition of such securities. Any interest in transferred financial assets that qualify for de-recognition that is created or retained by the bank is recognised as a separate asset or liability.

The bank enters into transactions whereby it transfers assets recognised on its statement of financial position, but retains either all or substantially all of the risks and rewards of the transferred assets or a portion of them. In such cases, the transferred assets are not derecognised. Examples of such transactions are securities lending and sale-and-repurchase transactions.

When assets are sold to a third party with a concurrent total rate of 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.

In certain transactions, the bank retains the obligation to service the transferred financial asset for a fee. The transferred asset is derecognised if it meets the de-recognition criteria. An asset or liability is recognised for the servicing contract if the servicing fee is more than adequate (asset) or is less than adequate (liability) for performing the servicing.

The bank securitises various loans and advances to customers and investment securities, which generally result in the sale of these assets to unconsolidated securitisation vehicles and in the bank transferring substantially all of the risks and rewards of ownership. The securitisation vehicles in turn issue securities to investors. Interests in the securitised financial assets are generally retained in the form of senior or subordinated tranches, interest-only strips or other residual interests (retained interests). Retained interests are recognised as investment securities and carried at FVOCI. Gains or losses on securitisation are recorded in other revenue.

Financial liabilities

The bank derecognises a financial liability when its contractual obligations are discharged or cancelled, or expire.

v) Modifications of financial assets and financial liabilities

Financial assets Policy applicable from 1 January 2018

If the terms of a financial asset are modified, 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 and a new financial asset is recognised at fair value.

6. SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

(f) Financial assets and liabilities (continued)

v) *Modifications of financial assets and financial liabilities*

Financial assets Policy applicable from 1 January 2018 (continued)

If the cash flows of the modified asset carried at amortised cost are not substantially different, then the modification does not result in de-recognition of the financial asset. In this case, the bank recalculates the gross carrying amount of the financial asset and recognises the amount arising from adjusting the gross carrying amount as a modification gain or loss in profit or loss. If such a modification is carried out because of financial difficulties of the borrower, then the gain or loss is presented together with impairment losses. In other cases, it is presented as interest income.

The impact of modifications of financial assets on the expected credit loss calculation is discussed in Note 3(f) (iii).

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 extinguished and the new financial liability with modified terms is recognised in profit or loss.

vi) *Offsetting of financial assets and financial liabilities*

Financial assets and financial liabilities are offset and the net amount reported in the statement of financial position when there is a legally enforceable right to offset the recognized amounts and there is an intention to settle on a net basis, or to realize the asset and settle the liability simultaneously.

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

Policy applicable before 1 January 2018

i) *Recognition*

The Bank initially recognises loans and advances, deposits and debt securities on the date at which they are originated. All other financial assets and liabilities (including assets designated at fair value through profit or loss) are initially recognised on the trade date at which the Bank becomes a party to the contractual provision of the instrument.

ii) *Classification*

The Bank classifies its financial assets in the following categories: financial assets at fair value through profit or loss; loans and receivables; held-to-maturity investments; and available-for-sale financial assets. Management determines the classification of its investments at initial recognition.

Financial assets at fair value through profit or loss

This category has two sub-categories: financial assets held for trading, and those designated at fair value through profit or loss at inception. A financial asset is classified in this category if acquired principally for the purpose of selling in the short term or if so designated by management.

6. SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

(f) Financial assets and liabilities (continued)

Policy applicable before 1 January 2018 (continued)

Financial assets at fair value through profit or loss (continued)

Investments held for trading are those which were either acquired for generating a profit from short-term fluctuations in price or dealer's margin, or are securities included in a portfolio in which a pattern of short-term profit-taking exists. Investments held for trading are subsequently re-measured at fair value based on quoted bid prices or dealer price quotations, without any deduction for transaction costs. All related realized and unrealized gains and losses are included in profit or loss. Interest earned whilst holding held for trading investments is reported as interest income.

Foreign exchange forward and spot contracts are classified as held for trading. They are marked to market and are carried at their fair value. Fair values are obtained from discounted cash flow models which are used in the determination of the foreign exchange forward and spot contract rates. Gains and losses on foreign exchange forward and spot contracts are included in foreign exchange income as they arise.

Loans and receivables

Loans and receivables are non-derivative financial assets with fixed or determinable payments that are not quoted in an active market. They arise when the Bank provides money directly to a debtor with no intention of trading the receivable. Loans and advances are initially measured at fair value plus incremental direct transaction costs, and subsequently measured at amortized cost using the effective interest method. Loans and receivables compose of loans and advances and cash and cash equivalents.

ii) Identification and measurement of impairment of financial assets

At each reporting date the Bank assesses whether there is objective evidence that financial assets not carried at fair value through profit or loss are impaired. Financial assets are impaired when objective evidence demonstrates that a loss event has occurred after the initial recognition of the asset, and that the loss event has an impact on the future cash flows on the asset than can be estimated reliably.

The Bank considers evidence of impairment at both a specific asset and collective level. All individually significant financial assets are assessed for specific impairment. Significant assets found not to be specifically impaired are then collectively assessed for any impairment that may have been incurred but not yet identified. Assets that are not individually significant are collectively assessed for impairment by grouping together financial assets with similar risk characteristics.

Objective evidence that financial assets (including equity securities) are impaired can include default or delinquency by a borrower, restructuring of a loan or advance by the Bank on terms that the Bank would otherwise not consider, indications that a borrower or issuer will enter bankruptcy, the disappearance of an active market for a security, or other observable data relating to a group of assets such as adverse changes in the payment status of borrowers or issuers in the group, or economic conditions that correlate with defaults in the group.

In assessing collective impairment the Bank uses historical trends of the probability of default, timing of recoveries and the amount of loss incurred, adjusted for management's judgment as to whether current economic and credit conditions are such that the actual losses are likely to be greater or less than suggested by historical trends. Default rate, loss rates and the expected timing of future recoveries are regularly benchmarked against actual outcomes to ensure that they remain appropriate.

6. SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

(f) Financial assets and liabilities (continued)

Policy applicable before 1 January 2018 (continued)

Loans and receivables (continued)

ii) Identification and measurement of impairment of financial assets (continued)

Impairment losses on assets carried at amortized cost are measured as the difference between the carrying amount of the financial assets and the present value of estimated cash flows discounted at the assets' original effective interest rate. Losses are recognised in profit or loss and reflected in an allowance account against loans and receivables. Interest on the impaired asset continues to be recognised through the unwinding of the discount.

Impairment losses on available-for-sale securities are recognised by reclassifying the losses accumulated in the fair value reserve in equity to profit or loss. The cumulative loss that is reclassified from equity to profit or loss is the difference between the acquisition cost, net of any principal repayment and amortisation, and the current fair value, less any impairment loss recognised previously in profit or loss.

When a subsequent event causes the amount of impairment loss to decrease, the impairment loss is reversed through profit or loss.

iii) De-recognition

The Bank derecognizes a financial asset when the contractual rights to the cash flows from the financial asset expire, or when it transfers the rights to receive the contractual cash flows on the financial asset in a transaction in which substantially all the risks and rewards of ownership of the financial asset are transferred. Any interest in transferred financial assets that is created or retained by the Bank is recognized as a separate asset or liability.

The Bank derecognizes a financial liability when its contractual obligations are discharged or cancelled or expire.

On de-recognition of a financial asset, the difference between the carrying amount of the asset and the sum of (i) the consideration received and (ii) any cumulative gain or loss that had been recognised in other comprehensive income is recognised in profit or loss.

The Bank enters into transactions whereby it transfers assets recognized on its statement of financial position, but retains either all or substantially all of the risks and rewards of the transferred assets or a portion of them. If all or substantially all risks and rewards are retained, then the transferred assets are not derecognized from the statement of financial position. Transfers of assets with retention of all or substantially all risks and rewards include repurchase transactions.

iv) Offsetting of financial assets and financial liabilities

Financial assets and financial liabilities are offset and the net amount reported in the statement of financial position when there is a legally enforceable right to offset the recognized amounts and there is an intention to settle on a net basis, or to realize the asset and settle the liability simultaneously.

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

6. SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

(f) Financial assets and liabilities (continued)

Policy applicable before 1 January 2018 (continued)

v) *Fair value of financial assets and financial liabilities*

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.

When available, the Bank measures the fair value of an instrument using quoted prices in an active market for that instrument. A market is regarded as active if quoted prices are readily and regularly available and represent actual and regularly occurring market transactions on an arm's length basis.

If a market for a financial instrument is not active, the Bank establishes fair value using a valuation technique. Valuation techniques include using recent arm's length transactions between knowledgeable, willing parties (if available), reference to the current fair value of other instruments that are substantially the same, discounted cash flow analyses and option pricing models.

The chosen valuation technique makes maximum use of market inputs, relies as little as possible on estimates specific to the Bank, incorporates all factors that market participants would consider in setting a price, and is consistent with accepted economic methodologies for pricing financial instruments. Inputs to valuation techniques reasonably represent market expectations and measures of the risk-return factors inherent in the financial instrument. The Bank calibrates valuation techniques and tests them for validity using prices from observable current market transactions in the same instrument or based on other available observable market data.

The best evidence of the fair value of a financial instrument at initial recognition is the transaction price, i.e., the fair value of the consideration given or received, unless the fair value of that instrument is evidenced by comparison with other observable current market transactions in the same instrument (i.e., without modification or repackaging) or based on a valuation technique whose variables include only data from observable markets. When transaction price provides the best evidence of fair value at initial recognition, the financial instrument is initially measured at the transaction price and any difference between this price and the value initially obtained from a valuation model is subsequently recognised in profit or loss depending on the individual facts and circumstances of the transaction but not later than when the valuation is supported wholly by observable market data or the transaction is closed out.

Fair values reflect the credit risk of the instrument and include adjustments to take account of the credit risk of the Bank where appropriate. Fair value estimates obtained from models are adjusted for any other factors, such as liquidity risk or model uncertainties; to the extent that the Bank believes a third party market participant would consider them in pricing a transaction.

vi) *Amortized cost measurement*

The amortized cost of a financial asset or liability is the amount at which the financial asset or liability is measured at initial recognition, minus principal repayments, plus or minus the cumulative amortization using the effective interest method of any difference between the initial amount recognized and the maturity amount, minus any reduction for impairment.

6. SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

(g) Property and equipment

Recognition and measurement

Items of property and equipment measured at cost less accumulated depreciation.

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.

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

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.

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 4 - 5 years

Computer software

Software acquired by the Bank stated at cost less accumulated amortisation.

Expenditure on internally developed software recognised as an asset when the Bank is able to demonstrate its intention and ability to complete the development and use the software in a manner that will generate future economic benefits, and 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 are amortised over its useful life. Internally developed software stated at capitalised cost less accumulated amortisation and impairment.

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 expensed as incurred.

Amortisation recognised in profit or loss on a straight-line basis over the estimated useful life of the software, from the date that it is available for use. Estimated useful life for computer software is 2 - 5 years.

6. SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

(h) Leases

The leases entered into by the Bank are operating leases and total payments made under operating leases are charged to the income statement on a straight-line basis over the period of the lease. When an operating lease terminated before the lease period has expired, any payment required to be made to the lessor by way of a penalty recognised as an expense in the period in which termination takes place.

(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) Other benefits

Employee entitlements to annual leave are recognized when they accrue to employees. A provision is made for the estimated liability for annual leave as a result of services rendered by employees up to the balance sheet date.

(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) Comparatives

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

6. SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)**(m) New standards, amendments and interpretations effective and adopted during the year**

The Bank has adopted the following new standards and amendments during the year ended 31 December 2018, including consequential amendments to other standards with the date of initial application by the Bank being 1 January 2018. The nature and effects of the changes are as explained here in.

New standard or amendments	Effective for annual periods beginning on or after
— IFRS 15 Revenue from Contracts with Customers	1 January 2018
— IFRS 9 Financial Instruments (2014)	1 January 2018
— IFRIC 22 Foreign Currency Transactions and Advance Consideration	1 January 2018
— Annual improvements cycle (2014-2016)	1 January 2018

— IFRS 15: Revenue from Contracts with Customers

This standard replaces IAS 11 Construction Contracts, IAS 18 Revenue, IFRIC 13 Customer Loyalty Programmes, IFRIC 15 Agreements for the Construction of Real Estate, IFRIC 18 Transfer of Assets from Customers and SIC-31 Revenue – Barter of Transactions Involving Advertising Services.

The standard contains a single model that applies to contracts with customers and two approaches to recognising revenue: at a point in time or over time. The standard specifies how and when the Bank will recognise revenue as well as requiring such entities to provide users of financial statements with more informative, relevant disclosures.

The Bank applied IFRS 15 on 1 January 2018 using the modified retrospective approach in which the cumulative effect of initially applying this Standard is recognised at the date of initial application as an adjustment to the opening balance of retained earnings as at 1 January 2018 without restating comparative periods.

There was no material impact of application of IFRS 15 and no adjustment to retained earnings was required.

—IFRS 9: Financial Instruments (2014)

On 24 July 2014 the IASB issued the final IFRS 9 Financial Instruments Standard, which replaces earlier versions of IFRS 9 and completes the IASB's project to replace IAS 39 Financial Instruments: Recognition and Measurement.

The new standard brings fundamental changes to the accounting for financial assets and to certain aspects of the accounting for financial liabilities.

As a result of the adoption of IFRS 9, the Bank has adopted consequential amendments to IFRS 7 Financial Instruments: Disclosures that are applied to disclosures about 2018, but have not been applied to the comparative information.

The key changes to the bank accounting policies resulting from its adoption of IFRS 9 are summarised below. The full impact of adopting the standard is set out in Note 4(a) and Note 5(a).

Classification of financial assets and financial liabilities

IFRS 9 contains three principal classification categories for financial assets: measured at amortised cost, fair value through other comprehensive income (FVOCI) and fair value through profit or loss (FVTPL).

6. SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

(m) New standards, amendments and interpretations effective and adopted during the year (continued)

IFRS 9 classification is generally based on the business model in which a financial asset is managed and its contractual cash flows.

The standard eliminates the previous IAS 39 categories of held-to-maturity, loans and receivables and available-for-sale. Under IFRS 9, derivatives embedded in contracts where the host is a financial asset in the scope of the standard are never bifurcated. Instead, the whole hybrid instrument is assessed for classification. For an explanation of how the Bank classifies financial assets under IFRS 9, see Note 3(f) (ii).

IFRS 9 largely retains the existing requirements in IAS 39 for the classification of financial liabilities. However, although under IAS 39 all fair value changes of liabilities designated under the fair value option were recognised in profit or loss, under IFRS 9 fair value changes are generally presented as follows:

- the amount of change in the fair value that is attributable to changes in the credit risk of the liability is presented in OCI; and
- the remaining amount of change in the fair value is presented in profit or loss.

For an explanation of how the Bank classifies financial liabilities under IFRS 9, see Note 3(f) (ii).

Impairment of financial assets

IFRS 9 replaces the 'incurred loss' model in IAS 39 with an 'expected credit loss' model. The new impairment model also applies to certain loan commitments and financial guarantee contracts but not to equity investments.

Under IFRS 9, credit losses are recognised earlier than under IAS 39. For an explanation of how the Bank applies the impairment requirements of IFRS 9, see Note 3(f) (iii) and Note 5(a).

Transition

Changes in accounting policies resulting from the adoption of IFRS 9 have been applied retrospectively, except as described below.

Comparative periods generally have not been restated. Differences in the carrying amounts of financial assets and financial liabilities resulting from the adoption of IFRS 9 are recognised in retained earnings and reserves as at 1 January 2018. Accordingly, the information presented for 2017 does not reflect the requirements of IFRS 9 and therefore is not comparable to the information presented for 2018 under IFRS 9. The Bank used the exemption not to restate comparative periods.

The following assessments have been made on the basis of the facts and circumstances that existed at the date of initial application.

- The determination of the business model within which a financial asset is held.
- Determination of factors to consider in determining whether there has been a significant increase in credit risk.
- If a debt security had low credit risk at the date of initial application of IFRS 9, then the Bank has assumed that credit risk on the asset had not increased significantly since its initial recognition.

For more information and details on the changes and implications resulting from the adoption of IFRS 9, see Note 4(a).

- *IFRIC Interpretation 22 Foreign Currency Transactions and Advance Consideration*

6. SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)**(m) New standards, amendments and interpretations effective and adopted during the year (continued)***Transition (continued)*

This Interpretation applies to a foreign currency transaction (or part of it) when an entity recognises a non-monetary asset or non-monetary liability arising from the payment or receipt of advance consideration before the entity recognises the related asset, expense or income (or part of it).

This Interpretation stipulates that the date of the transaction for the purpose of determining the exchange rate to use on initial recognition of the related asset, expense or income (or part of it) is the date on which an entity initially recognises the non-monetary asset or non-monetary liability arising from the payment or receipt of advance consideration.

This Interpretation does not apply to income taxes, insurance contracts and circumstances when an entity measures the related asset, expense or income on initial recognition:

- a) fair value; or
- b) at the fair value of the consideration paid or received at a date other than the date of initial recognition of the non-monetary asset or non-monetary liability arising from advance consideration (for example, the measurement of goodwill applying IFRS 3 Business Combinations).

The amendments apply retrospectively for annual periods beginning on or after 1 January 2018, with early application permitted.

The adoption of this standard did not have a material impact on the bank's financial statements.

— *Annual improvement cycle (2014 – 2016) – various standards*

Standards	Amendments
IFRS 1 First-time Adoption of IFRS	Outdated exemptions for first-time adopters of IFRS are removed. The amendments apply prospectively for annual periods beginning on or after 1 January 2018.
IAS 28 Investments in Associates and Joint Ventures	A venture capital organisation, or other qualifying entity, may elect to measure its investments in an associate or joint venture at fair value through profit or loss. This election can be made on an investment-by-investment basis. A non-investment entity investor may elect to retain the fair value accounting applied by an investment entity associate or investment entity joint venture to its subsidiaries. This election can be made separately for each investment entity associate or joint venture. The amendments apply retrospectively for annual periods beginning on or after 1 January 2018; early application is permitted.

The adoption of these standards did not have a material impact on the amounts and disclosures of the bank's financial statements.

6. SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)**(m) New standards, amendments and interpretations effective and adopted during the year (continued)***Transition (continued)*

A number of new standards, amendments to standards and interpretations are not yet effective for the year ended 31 December 2018, and have not been applied in preparing these financial statements.

(n) New standards and interpretation in issue but not yet effective

The bank does not plan to adopt these standards early. These are summarised below:

— IFRS 16 Leases	1 January 2019
— IFRIC 23 Uncertainty over income tax treatments	1 January 2019
— IFRS 9 Prepayment Features with Negative Compensation	1 January 2019
— IAS 28 Long-term Interests in Associates and Joint Ventures	1 January 2019
— Annual improvements cycle (2015-2017)	1 January 2019
— IAS 19 Plan Amendment, Curtailment or Settlement (Amendments to IAS 19)	1 January 2019
— IFRS 3 Definition of a Business	1 January 2020
— Amendments to references to the Conceptual Framework in IFRS Standards	1 January 2020
— Amendments to IAS 1 and IAS 8 Definition of Material	1 January 2020
— IFRS 17 Insurance contracts	1 January 2022
— Sale or Contribution of Assets between an Investor and its Associate or Company (Amendments to IFRS 10 and IAS 28).	To be determined

All standards and interpretations will be adopted at their effective date (except for those standards and interpretations that are not applicable to the entity).

— IFRS 16: Leases

On 13 January 2016 the IASB issued IFRS 16 Leases, completing the IASB's project to improve the financial reporting of leases. IFRS 16 replaces the previous leases standard, IAS 17 Leases, and related interpretations.

IFRS 16 sets out the principles for the recognition, measurement, presentation and disclosure of leases for both parties to a contract, i.e. the customer ('lessee') and the supplier ('lessor'). The standard defines a lease as a contract that conveys to the customer ('lessee') the right to use an asset for a period of time in exchange for consideration.

A Company assesses whether a contract contains a lease on the basis of whether the customer has the right to control the use of an identified asset for a period of time.

The standard eliminates the classification of leases as either operating leases or finance leases for a lessee and introduces a single lessee accounting model. All leases are treated in a similar way to finance leases.

Applying that model significantly affects the accounting and presentation of leases and consequently, the lessee is required to recognise:

6. SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

(m) New standards and interpretation in issue but not yet effective (continued)

— *IFRS 16: Leases (continued)*

- a) assets and liabilities for all leases with a term of more than 12 months, unless the underlying asset is of low value. A Company recognises the present value of the unavoidable lease payments and shows them either as lease assets (right-of-use assets) or together with property, plant and equipment. If lease payments are made over time, a Company also recognises a financial liability representing its obligation to make future lease payments.
- b) depreciation of lease assets and interest on lease liabilities in profit or loss over the lease term; and
- c) separate the total amount of cash paid into a principal portion (presented within financing activities) and interest (typically presented within either operating or financing activities) in the statement of cash flows

IFRS 16 substantially carries forward the lessor accounting requirements in IAS 17. Accordingly, a lessor continues to classify its leases as operating leases or finance leases, and to account for those two types of leases differently. However, compared to IAS 17, IFRS 16 requires a lessor to disclose additional information about how it manages the risks related to its residual interest in assets subject to leases.

The standard does not require a Company to recognise assets and liabilities for:

- a) short-term leases (i.e. leases of 12 months or less) and;
- b) leases of low-value assets

The new standard is effective for annual periods beginning on or after 1 January 2019. Early application is permitted in so far as the recently issued revenue Standard, IFRS 15 Revenue from Contracts with Customers is also applied.

The Bank is currently in the process of assessing existing contractual relationships to identify the existing population of leases that would be recorded on the statement of financial position under the new standard. The Bank continues to evaluate the potential impact to the existing IT systems and processes and next steps include performing an initial quantification of the existing obligations and reviewing the additional disclosures required by the new standard. During 2019, the Bank will also complete its assessment of various practical expedients and formulate its accounting policies under IFRS 16.

— *IFRIC 23 Clarification on accounting for Income tax exposures*

IFRIC 23 clarifies the accounting for income tax treatments that have yet to be accepted by tax authorities, whilst also aiming to enhance transparency.

IFRIC 23 explains how to recognise and measure deferred and current income tax assets and liabilities where there is uncertainty over a tax treatment.

An uncertain tax treatment is any tax treatment applied by an entity where there is uncertainty over whether that treatment will be accepted by the tax authority.

If an entity concludes that it is probable that the tax authority will accept an uncertain tax treatment that has been taken or is expected to be taken on a tax return, it should determine its accounting for income taxes consistently with that tax treatment. If an entity concludes that it is not probable that the treatment will be accepted, it should reflect the effect of the uncertainty in its income tax accounting in the period in which that determination is made.

6. SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

(m) New standards and interpretation in issue but not yet effective (continued)

— *IFRIC 23 Clarification on accounting for Income tax exposures (continued)*

Uncertainty is reflected in the overall measurement of tax and separate provision is not allowed.

The entity is required to measure the impact of the uncertainty using the method that best predicts the resolution of the uncertainty (that is, the entity should use either the most likely amount method or the expected value method when measuring an uncertainty).

The entity will also need to provide disclosures, under existing disclosure requirements, about

- a) judgments made;
- b) assumptions and other estimates used; and
- c) potential impact of uncertainties not reflected.

The new Standard is effective for annual periods beginning on or after 1 January 2019. The Bank is assessing the potential impact on its financial statements resulting from the application of IFRIC 23.

— *Prepayment Features with Negative Compensation (Amendments to IFRS 9)*

The amendments clarify that financial assets containing prepayment features with negative compensation can now be measured at amortised cost or at fair value through other comprehensive income (FVOCI) if they meet the other relevant requirements of IFRS 9.

The amendments apply for annual periods beginning on or after 1 January 2019 with retrospective application, early adoption is permitted.

The adoption of these amendments will not have an impact on the financial statements of the Bank.

— *Long-term Interests in Associates and Joint Ventures (Amendment to IAS 28)*

The amendments clarify that an entity applies IFRS 9 to long-term interests in an associate and joint venture that form part of the net investment in the associate or joint venture but to which the equity method is not applied.

The amendments apply for annual periods beginning on or after 1 January 2019. Early adoption is permitted.

6. SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)**(m) New standards and interpretation in issue but not yet effective (continued)**

— *Long-term Interests in Associates and Joint Ventures (Amendment to IAS 28) (continued)*

The adoption of these standards will not have an impact on the financial statements of the Bank.

— *Annual improvement cycle (2015 – 2017) – various standards*

Standards	Amendments
IFRS 3 Business Combinations and IFRS 11 Joint Arrangements	Clarifies how a Company accounts for increasing its interest in a joint operation that meets the definition of a business: <ul style="list-style-type: none"> — If a party maintains (or obtains) joint control, then the previously held interest is not remeasured. — If a party obtains control, then the transaction is a business combination achieved in stages and the acquiring party remeasures the previously held interest at fair value.
IAS 12 Income taxes	Clarifies that all income tax consequences of dividends (including payments on financial instruments classified as equity) are recognised consistently with the transactions that generated the distributable profits – i.e. in profit or loss, OCI or equity.
IAS 23 Borrowing costs	Clarifies that the general borrowings pool used to calculate eligible borrowing costs excludes only borrowings that specifically finance qualifying assets that are still under development or construction. Borrowings that were intended to specifically finance qualifying assets that are now ready for their intended use or sale – or any non-qualifying assets – are included in that general pool. As the costs of retrospective application might outweigh the benefits, the changes are applied prospectively to borrowing costs incurred on or after the date an entity adopts the amendments.

The amendments are effective for annual reporting periods beginning on or after 1 January 2019 with earlier application permitted. The adoption of these amendments is not expected to affect the amounts and disclosures of the Bank's financial statements.

The Bank did not early adopt new or amended standards in the year ended 31 December 2018.

— *IAS 19 Plan Amendment, Curtailment or Settlement (Amendments to IAS 19)*

The amendments clarify that:

- on amendment, curtailment or settlement of a defined benefit plan, a Company now uses updated actuarial assumptions to determine its current service cost and net interest for the period; and
- the effect of the asset ceiling is disregarded when calculating the gain or loss on any settlement of the plan and is dealt with separately in other comprehensive income (OCI).

Consistent with the calculation of a gain or loss on a plan amendment, entities will now use updated actuarial assumptions to determine the current service cost and net interest for the period. Previously, entities would not have updated the calculation of these costs until the year-end.

Further, if a defined benefit plan is settled, any asset ceiling would be disregarded when determining the plan assets as part of the calculation of gain or loss on settlement.

6. SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

(m) New standards and interpretation in issue but not yet effective (continued)

— *IAS 19 Plan Amendment, Curtailment or Settlement (Amendments to IAS 19) (continued)*

The amendments apply for plan amendments, curtailments or settlements that occur on or after 1 January 2019, or the date on which the amendments are first applied. Earlier application is permitted.

The adoption of this standard will not have an impact on the financial statements of the Bank.

— *IFRS 3 Definition of a Business*

With a broad business definition, determining whether a transaction results in an asset or a business acquisition has long been a challenging but important area of judgement. These amendments to IFRS 3 Business Combinations seek to clarify this matter as below however complexities still remain.

— *Optional concentration test*

The amendments include an election to use a concentration test. This is a simplified assessment that results in an asset acquisition if substantially all of the fair value of the gross assets is concentrated in a single identifiable asset or a group of similar identifiable assets.

— *Substantive process*

If an entity chooses not to apply the concentration test, or the test is failed, then the assessment focuses on the existence of a substantive process.

The definition of a business is now narrower and could result in fewer business combinations being recognised.

The amendment applies to businesses acquired in annual reporting periods beginning on or after 1 January 2020. Earlier application is permitted. The adoption of this standard will not have an impact on the financial statements of the Bank.

— *Amendments to References to the Conceptual Framework in IFRS Standards*

This amendment sets out amendments to IFRS Standards (Standards), their accompanying documents and IFRS practice statements to reflect the issue of the International Accounting Standards Board (IASB) revised Conceptual Framework for Financial Reporting in 2018 (2018 Conceptual Framework).

Some Standards, their accompanying documents and IFRS practice statements contain references to, or quotations from, the IASB's Framework for the Preparation and Presentation of Financial Statements adopted by the IASB in 2001 (Framework) or the Conceptual Framework for Financial Reporting issued in 2010. Amendments to References to the Conceptual Framework in IFRS Standards updates some of those references and quotations so that they refer to the 2018 Conceptual Framework, and makes other amendments to clarify which version of the Conceptual Framework is referred to in particular documents.

6. SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

(m) New standards and interpretation in issue but not yet effective (continued)

— *Amendments to References to the Conceptual Framework in IFRS Standards (continued)*

These amendments are based on proposals in the Exposure Draft Updating References to the Conceptual Framework, published in 2015, and amend Standards, their accompanying documents and IFRS practice statements that will be effective for annual reporting periods beginning on or after 1 January 2020.

The adoption of these changes will not affect the amounts and disclosures of the Bank's financial statements.

— *IAS 1 and IAS 8 Definition of Material*

The amendment refines the definition of Material to make it easier to understand and aligning the definition across IFRS Standards and the Conceptual Framework.

The amendment includes the concept of 'obscuring' to the definition, alongside the existing references to 'omitting' and 'misstating'. Additionally, the amendments also adds the increased threshold of 'could influence' to 'could reasonably be expected to influence' as below.

"Information is material if omitting, misstating or obscuring it could reasonably be expected to influence decisions that the primary users of general purpose financial statements make on the basis of those financial statements, which provide financial information about a specific reporting entity."

However, the amendment has also removed the definition of material omissions or misstatements from IAS 8 Accounting Policies, Changes in Accounting Estimates and Errors. The amendments are effective from 1 January 2020 but may be applied earlier.

The Bank is assessing the potential impact on its financial statements resulting from the application of the refined definition of materiality.

— *IFRS 17 Insurance Contracts*

IFRS 17 Insurance Contracts sets out the requirements that an entity should apply in reporting information about insurance contracts it issues and reinsurance contracts it holds. An entity shall apply IFRS 17 Insurance Contracts to:

- a) insurance contracts, including reinsurance contracts, it issues;
- b) reinsurance contracts it holds; and
- c) investment contracts with discretionary participation features it issues, provided the entity also issues insurance contracts.

IFRS 17 requires an entity that issues insurance contracts to report them on the statement of financial position as the total of:

- a) the fulfilment cash flows—the current estimates of amounts that the entity expects to collect from premiums and pay out for claims, benefits and expenses, including an adjustment for the timing and risk of those amounts; and
- b) the contractual service margin—the expected profit for providing insurance coverage. The expected profit for providing insurance coverage is recognised in profit or loss over time as the insurance coverage is provided.

6. SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)**(m) New standards and interpretation in issue but not yet effective (continued)**

IFRS 17 requires an entity to recognise profits as it delivers insurance services, rather than when it receives premiums, as well as to provide information about insurance contract profits that the Company expects to recognise in the future. IFRS 17 requires an entity to distinguish between groups of contracts expected to be profit making and groups of contracts expected to be loss making. Any expected losses arising from loss-making, or onerous, contracts are accounted for in profit or loss as soon as the Company determines that losses are expected. IFRS 17 requires the entity to update the fulfilment cash flows at each reporting date, using current estimates of the amount, timing and uncertainty of cash flows and of discount rates. The entity:

- a) accounts for changes to estimates of future cash flows from one reporting date to another either as an amount in profit or loss or as an adjustment to the expected profit for providing insurance coverage, depending on the type of change and the reason for it; and
- b) chooses where to present the effects of some changes in discount rates—either in profit or loss or in other comprehensive income.

IFRS 17 also requires disclosures to enable users of financial statements to understand the amounts recognised in the entity's statement of financial position and statement of profit or loss and other comprehensive income, and to assess the risks the Company faces from issuing insurance contracts.

IFRS 17 replaces IFRS 4 Insurance Contracts. IFRS 17 is effective for financial periods commencing on or after 1 January 2021. An entity shall apply the standard retrospectively unless impracticable. A Company can choose to apply IFRS 17 before that date, but only if it also applies IFRS 9 Financial Instruments and IFRS 15 Revenue from Contracts with Customers.

The adoption of these changes will not affect the amounts and disclosures of the Bank's financial statements.

— *Sale or Contribution of Assets between an Investor and its Associate or Company (Amendments to IFRS 10 and IAS 28)*

The amendments require the full gain to be recognised when assets transferred between an investor and its associate or Company meet the definition of a 'business' under IFRS 3 Business Combinations. Where the assets transferred do not meet the definition of a business, a partial gain to the extent of unrelated investors' interests in the associate or Company is recognised. The definition of a business is key to determining the extent of the gain to be recognised.

The effective date for these changes has now been postponed until the completion of a broader review. The adoption of these changes will not affect the amounts and disclosures of the Bank's financial statements.

7. FINANCIAL RISK MANAGEMENT**Introduction and overview**

The Bank has exposure to the following risks from its use of financial instruments:

- Credit risk;
- Liquidity risk; and
- Market risks.

This note presents information about the Bank's exposure to each of the above risks, the Bank's objectives, policies and processes for measuring and managing risk, and the Bank's management of capital.

7. FINANCIAL RISK MANAGEMENT (CONTINUED)

RISK MANAGEMENT

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) 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.

7. FINANCIAL RISK MANAGEMENT (CONTINUED)**(a) Credit risk (Continued)****Management of credit risk (Continued)**

- 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.

Impaired loans

Impaired loans are loans for which the Bank determines that it is probable that it will be unable to collect all principal and interest due according to the contractual terms of the loan agreement(s). These loans are graded 1 day to 90+ days in the Bank's internal credit risk grading system.

Past due but not impaired loans

Loans where contractual interest or principal payments are past due but the Bank believes that impairment is not appropriate on the basis of the level of security / collateral available and / or the stage of collection of amounts owed to the Bank.

Loans with renegotiated terms

Loans with renegotiated terms are loans that have been restructured due to deterioration in the borrower's financial position and where the Bank has made concessions that it would not otherwise consider. Once the loan is restructured, it remains in this category independent of satisfactory performance after restructuring.

Allowances for impairment

The Bank establishes an allowance for impairment losses that represents its estimate of incurred losses in its loan portfolio. The main components of this allowance is a collective loan loss allowance established for the Bank of homogeneous assets in respect of losses that have been incurred but have not been identified on loans.

The table below provides details of exposure to credit risk:

	Loans and Advances to Customers	
	2018	2017
	TZS'000	TZS'000
Past due 0 to 7 days	53,098,293	60,976,514
Past due 8 to 30 days	1,855,462	1,827,787
Past due 31 to 60 days	724,269	1,445,942
Past due 61 to 90 days	616,504	1,110,410
Past due 90 + days	<u>2,971,257</u>	<u>3,906,875</u>
Gross loans and advances	59,265,785	69,267,528
Less: Provision for loan losses	<u>(2,473,869)</u>	<u>(5,207,918)</u>
Net loans and advances	<u>56,791,916</u>	<u>64,059,610</u>

7. FINANCIAL RISK MANAGEMENT (CONTINUED)

Allowances for impairment (Continued)

Write-off policy

The Bank writes off a loan balance in arrears equal to or greater than 180 days (and any related allowances for impairment losses) once the following actions have taken place:

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.

(a) Liquidity Risk

Liquidity risk is the risk that the Bank will encounter difficulty in meeting obligations from its financial liabilities.

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.

FINCA MICROFINANCE BANK LIMITED

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

7. FINANCIAL RISK MANAGEMENT (CONTINUED)

(a) 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:

2018	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	16,024,342	-	-	-	-	16,024,342
Investment in fixed deposits	11,433,077	-	-	-	-	11,433,077
Loans and advances to customers	18,714,966	7,293,933	22,525,471	8,257,546	-	56,791,916
Due from related parties	128,233	-	-	-	-	128,233
Other assets (excluding non-financial assets)	757,637	-	-	-	-	757,637
Total assets	47,058,255	7,293,933	22,525,471	8,257,546	-	85,135,205
LIABILITIES						
Deposits from customers and banks	19,882,366	3,306,896	11,890,493	-	-	35,079,755
Borrowings and Interest payable	22,635,485	782,229	4,606,897	6,913,149	-	34,937,760
Due to related parties	114,311	-	-	-	-	114,311
Other payables (excluding non-financial liabilities)	306,291	-	-	-	-	306,291
Total liabilities	42,938,453	4,089,125	16,497,390	6,913,149	-	70,438,117
Net liquidity gap	4,119,802	3,204,808	6,028,081	1,344,397	-	14,697,088
At 31 December 2017						
Total assets	32,983,319	19,312,646	27,867,817	14,085,625	47,136	94,296,543
Total liabilities and shareholders' fund	29,293,950	9,628,533	23,124,538	20,320,339	-	82,367,360
Net liquidity gap	3,689,369	9,684,113	4,743,279	(6,234,714)	47,136	11,929,183

7. FINANCIAL RISK MANAGEMENT (CONTINUED)**(b) 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 2018.

	2018	2017
	TZS'000	TZS'000
100 basis points increases or decrease in interest rates	<u>(17,925)</u>	<u>68,387</u>

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

FINCA MICROFINANCE BANK LIMITED

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

7. FINANCIAL RISK MANAGEMENT (CONTINUED)

(c) 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.

	Up to 3 Months TZS'000	4 - 12 Months TZS'000	1 - 5 years TZS'000	Non- interest bearing TZS'000	Total TZS'000
2018					
ASSETS					
Cash and cash equivalents	-	-	-	16,024,342	16,024,342
Investment in fixed deposits	11,433,077	-	-	-	11,433,077
Loans and advances to customers	18,714,966	29,819,404	8,257,546	-	56,791,916
Due from related parties	-	-	-	128,233	128,233
Other assets (excluding non-financial assets)	-	-	-	757,637	757,637
Total assets	30,148,043	29,819,404	8,257,546	16,910,212	85,135,205
LIABILITIES					
Deposit from customers and banks	22,635,485	5,389,126	6,913,149	-	34,937,760
Borrowings and interest payable	19,882,366	15,197,389	-	-	35,079,755
Due to related parties	-	-	-	114,311	114,311
Other payables (excluding non-financial liabilities)	-	-	-	306,291	306,291
Total liabilities	42,517,851	20,586,515	6,913,149	420,602	70,438,117
Interest rate sensitivity gap	(12,369,808)	9,232,889	1,344,397	16,489,600	14,697,088
At 31 December 2017					
Total assets	25,032,840	47,180,463	14,132,761	7,950,479	94,296,543
Total liabilities and shareholders' fund	26,433,980	32,753,071	20,320,339	2,859,970	82,367,360
Interest rate sensitivity gap	(1,401,140)	14,427,392	(6,187,578)	5,090,509	11,929,183

7. FINANCIAL RISK MANAGEMENT (CONTINUED)**(c) Market risks (Continued)****Currency risk**

The Bank had no significant hedged 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 2018.

31 December 2018	TZS '000
Cash and cash equivalents	12,304,883
Placements	11,433,077
Borrowings	(11,336,719)
Net amount due to related parties	<u>(13,921)</u>
Net balance sheet exposure	<u>12,387,320</u>

A sensitivity analysis in relation to the net exposure for a 10% strengthening/weakening of the TZS against USD:

Increase/(decrease) in profit before tax	<u>1,238,732</u>
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31 December 2017

Cash and cash equivalents	391,725
Net amount due to related parties	<u>(500,070)</u>
Net balance sheet exposure	<u>(108,345)</u>

A sensitivity analysis in relation to the net exposure for a 10% strengthening/weakening of the TZS against USD:

Increase/(decrease) in profit before tax	<u>(10,835)</u>
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d) 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 did not have any financial asset and financial liabilities that are measured at fair value on recurring basis.

7. FINANCIAL RISK MANAGEMENT (CONTINUED)**d) 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 2018.

	Level 1	Level 2	Level 3	Total fair Value	Financial asset not measured at fair value	Total Carrying Amount
31 December 2018						
ASSETS	TZS'000	TZS'000	TZS'000	TZS'000	TZS'000	TZS'000
Cash and balances	16,024,342	-	-	-	-	16,024,342
Placement with Bank	-	11,433,077	-	-	-	11,433,077
Loans and advances to customers – (net)	-	56,791,916	-	-	-	56,791,916
	<u>16,024,342</u>	<u>68,224,993</u>	<u>-</u>	<u>-</u>	<u>-</u>	<u>84,249,335</u>
LIABILITIES						
Deposits from other banks	-	6,719,759	-	-	-	6,719,759
Deposits from customers	-	28,359,996	-	-	-	28,359,996
	<u>-</u>	<u>35,079,755</u>	<u>-</u>	<u>-</u>	<u>-</u>	<u>35,079,755</u>
					Financial asset not measured at fair value	Total carrying amount
31 December 2017						
ASSETS	TZS'000	TZS'000	TZS'000	TZS'000	TZS'000	TZS'000
Cash and balances with Bank of Tanzania	6,995,694	-	-	-	-	6,995,694
Balances with other Bank	-	-	-	-	-	-
Placement with Bank	-	22,286,454	-	-	-	22,286,454
Loans and advances to customers – (net)	-	64,059,610	-	-	-	64,059,610
	<u>6,995,694</u>	<u>86,346,064</u>	<u>-</u>	<u>-</u>	<u>-</u>	<u>93,341,758</u>
LIABILITIES						
Deposits from other banks	-	20,302,200	-	-	-	20,302,200
Deposits from customers	-	24,852,821	-	-	-	24,852,821
	<u>-</u>	<u>45,155,021</u>	<u>-</u>	<u>-</u>	<u>-</u>	<u>45,155,021</u>

7. FINANCIAL RISK MANAGEMENT (CONTINUED)**d) Fair value estimation (Continued)**

At 31 December 2018	Carrying amount			Fair value
	Amortized cost	Other Financial Liabilities	Total	Total
	TZS'000	TZS'000	TZS'000	TZS'000
ASSETS				
Cash and balances with Bank of Tanzania	16,024,342	-	16,024,342	16,024,342
Placements	-	11,433,077	11,433,077	11,433,077
Balances with other Bank	-	-	-	-
Investment securities	-	-	-	-
Loans and advances to customers – (net)	56,791,916	-	56,791,916	56,791,916
	72,816,258	11,433,077	84,249,335	84,249,335
LIABILITIES				
Deposits from other Banks	-	6,719,759	6,719,759	6,719,759
Deposits from customers	-	28,359,996	28,359,996	28,359,996
	-	35,079,755	35,079,755	35,079,755

At 31 December 2017	Carrying amount			Fair Value
	Amortized cost	Other Financial Liabilities	Total	Total
	TZS'000	TZS'000	TZS'000	TZS'000
ASSETS				
Cash and balances with Bank of Tanzania	6,995,694	-	6,995,694	6,995,694
Placements	-	-	-	-
Balances with other Bank	-	-	-	-
Investment securities	-	22,286,454	22,286,454	22,286,454
Loans and advances to customers – (net)	64,059,610	-	64,059,610	64,059,610
	71,055,304	22,286,454	93,341,758	93,341,758
LIABILITIES				
Deposits from other Banks	-	20,302,200	20,302,200	20,302,200
Deposits from customers	-	24,852,821	24,852,821	24,852,821
	-	45,155,021	45,155,021	45,155,021

7. FINANCIAL RISK MANAGEMENT (CONTINUED)**d) Fair value estimation (Continued)**

31 December 2017:	Loans and receivables TZS '000	Financial assets and liabilities carried at amortised cost TZS '000	Total TZS '000
Assets			
Cash and cash equivalents	6,995,694	-	6,995,694
Investment in fixed deposits	-	22,286,454	22,286,454
Loans and advances to customers	64,059,610	-	64,059,610
Due from related parties	62,777	-	62,777
Other assets (excluding non-financial assets)	892,008	-	892,008
Total assets	<u>72,010,089</u>	<u>22,286,454</u>	<u>94,296,543</u>
Liabilities			
Deposits from customers and banks	-	45,155,021	45,155,021
Borrowings and Interest payable	-	34,352,369	34,352,369
Due to related parties	-	562,847	562,847
Other payables (excluding non-financial liabilities)	-	2,297,123	2,297,123
Total liabilities	<u>-</u>	<u>82,367,360</u>	<u>82,367,360</u>

e) 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 12.5% of its total risk-weighted assets and off balance sheet exposure; and
- a Total Capital of not less than 14.5% of its total risk-weighted assets and off balance sheet exposure.

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).

7. FINANCIAL RISK MANAGEMENT (CONTINUED)

e) Capital Management (continued)

Core capital includes ordinary share capital, irredeemable preference share capital, capital contribution reserve, share premium and retained earnings after deductions of goodwill, intangible assets, 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 2018 and year ended 31 December 2017. During those two periods, the Bank complied with all the Bank of Tanzania imposed capital requirements to which it was subjected to.

7. FINANCIAL RISK MANAGEMENT (CONTINUED)**e) Capital management (continued)**

The Bank's regulatory capital position as at 31 December 2018 was as follows:

	2018	2017
	TSZ '000	TSZ '000
Core capital (Tier 1)		
Share capital	31,574,605	23,030,150
Retained earnings (excluding (loss)/profit for the year)	(2,712,977)	2,837,166
Qualifying year to date (loss)/profit	<u>(9,495,114)</u>	<u>(5,621,000)</u>
	<u>19,366,514</u>	<u>20,246,316</u>
Less deductions from capital		
Regulatory adjustments:		
Prepayments	2,440,476	2,208,197
Deferred charges	4,957,545	3,215,105
Intangible assets	<u>1,565,339</u>	<u>1,101,167</u>
Total deductions from capital	<u>8,963,360</u>	<u>6,524,469</u>
Core capital	<u>10,403,154</u>	<u>13,721,847</u>
Supplementary capital (Tier 2)		
General Banking Risk reserve	<u>522,010</u>	<u>590,073</u>
Total capital	<u>10,925,164</u>	<u>14,311,920</u>
Risk weighted assets		
On-balance sheet	<u>74,687,491</u>	<u>76,987,636</u>
Total risk weighted assets	<u>74,687,491</u>	<u>76,987,636</u>
	2018	2017
Capital ratios	%	%
Core capital /total risk weighted assets (BoT minimum 12.5%)	13.93%	17.82
Total capital /total risk weighted assets (BoT minimum 14.5%)	<u>14.63%</u>	<u>18.59</u>

7. FINANCIAL RISK MANAGEMENT (CONTINUED)**e) Capital management (continued)****Capital allocation**

The Bank's capital management approach is driven by its desire to maintain a strong 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.

	2018	2017
	TZS '000	TZS '000
8. INTEREST AND SIMILAR INCOME		
Interest from loans and advances	25,071,464	29,237,455
Income from investments	598,636	1,219,028
Income from insurance claim	6,047	10,053
	<u>25,676,147</u>	<u>30,466,536</u>
	2018	2017
	TZS '000	TZS '000
9. INTEREST AND SIMILAR EXPENSE		
Interest on term loans	3,337,724	6,016,553
Fees on term loan	177,831	153,430
Interest on deposits from customers	<u>4,120,590</u>	<u>3,661,019</u>
	<u>7,636,145</u>	<u>9,831,002</u>

FINCA MICROFINANCE BANK LIMITED

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

10. GRANT INCOME

	2018 TZS '000	2017 TZS '000
Master Card grant	230,400	797,451
Donations received from FINCA International	-	129,465
Financial Sector Deepening Trust	<u>5,253</u>	<u>-</u>
	<u>235,653</u>	<u>926,916</u>

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*.

11. OTHER LOSSES

	2018 TZS '000	2017 TZS '000
Net foreign exchange loss	(41,654)	(61,575)
Earnings (Loss) on disposal of equipment	<u>6,769</u>	<u>-</u>
	<u>(34,885)</u>	<u>(61,575)</u>

12. PERSONNEL EXPENSES

Salaries and wages	10,122,038	9,461,507
NSSF/PPF contributions	1,005,464	933,402
Training expenses	211,965	307,830
Medical insurance expenses	665,908	535,597
Skills and development levy	464,482	434,024
Other staff benefits	286,850	274,720
Workers Compensation Fund contribution	103,149	93,997
Directors' emoluments	174,391	54,604
Bonuses	<u>116,800</u>	<u>25,000</u>
	<u>13,151,047</u>	<u>12,120,681</u>

13. OPERATING EXPENSES

Operating expenses include the following:

	2018	2017
	TZS '000	TZS '000
Transport and travel	1,910,472	1,892,486
Affiliation fees	722,997	907,027
Management fees	-	1,223,050
Operating lease rentals	2,311,812	2,015,686
Professional and legal fees	1,759,268	766,125
Auditors' remuneration	346,530	157,889
security and Insurance	1,530,812	1,784,721
Marketing and communication	1,790,661	1,528,139
Stationery, supplies and utilities	777,961	753,150
IT support	292,448	1,154,665
Recruitment	424,443	344,428
Repair and maintenance	182,481	141,738
Other expenses	3,687,770	1,113,779
	<u>15,737,655</u>	<u>13,782,883</u>

14. INCOME TAX**a) Tax expense**

Current tax at effective tax rate of 31.2% (2016:26.4%)	-	-
Deferred tax (credit)/charge (note 12 (d))	(2,089,130)	(2,436,127)
Prior year deferred tax over provision	-	(112,150)
Corporate tax charged for prior	382,446	-
	<u>(1,706,684)</u>	<u>(2,548,277)</u>

b) Reconciliation of accounting profit to tax expense

Loss before tax	<u>(11,201,798)</u>	<u>(8,169,277)</u>
Tax expense at applicable rate of 30%	(3,360,540)	(2,450,783)
Tax effect on items disallowed for tax purposes	1,653,856	14,656
Prior year deferred tax over provision	-	(112,150)
	<u>(1,706,684)</u>	<u>2,548,277</u>

14. INCOME TAX (Continued)**c) Deferred tax asset movement**

	Net balance at 1 January	Recognis ed in profit and loss from prior years	Recognised in profit or loss	Recognised in Retained Earnings	Net balance at 31 December
	TZS '000	TZS '000	TZS '000	TZS '000	TZS '000
2018					
Arising from:					
Property and equipment	(34,744)	-	82,130	-	47,386
Provision for loan losses	1,562,376	-	(820,215)	-	742,161
Accumulated tax losses	1,687,473	-	2,827,215	-	4,514,688
IFRS 9 transition adjustment	-	-	-	(346,690)	(346,690)
	<u>3,215,105</u>	<u>-</u>	<u>2,089,130</u>	<u>(346,690)</u>	<u>4,957,545</u>
2017					
Arising from:					
Property and equipment	31,344	-	3,400	-	34,744
Provision for loan losses	(698,172)	-	(864,204)	-	(1,562,376)
Accumulated tax losses	-	-	(1,687,473)	-	(1,687,473)
	<u>(666,828)</u>	<u>-</u>	<u>(2,548,277)</u>	<u>-</u>	<u>(3,215,105)</u>

d) Tax (payable)/recoverable

At beginning of year	14,357	(163,959)
Tax paid during the year	-	178,316
Current taxation charge for the year	(382,446)	-
At end of year	<u>(368,089)</u>	<u>14,357</u>

15. INVESTMENTS IN FIXED DEPOSITS

Fixed deposits	<u>11,433,077</u>	<u>22,286,454</u>
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16. CASH AND BANK BALANCES

Balance with Bank of Tanzania	12,834,798	3,168,280
Bank balances	<u>3,189,544</u>	<u>3,827,414</u>
	<u>16,024,342</u>	<u>6,995,694</u>

17. LOANS AND ADVANCES TO CUSTOMERS

a) Analysis of net loans to customers by maturity		
Up to 3 months	18,714,966	7,147,494
Between 4 months and 6 months	7,293,933	17,030,771
Between 7 months and 12 months	22,525,471	25,748,584
Between 1 year and 3 years	8,257,546	14,085,625
More than 3 years	-	47,136

	<u>56,791,916</u>	<u>64,059,610</u>
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17. LOANS AND ADVANCES TO CUSTOMERS (CONTINUED)

	2018	2017
	TZS '000	TZS '000
Village Bank loans	149,340	597,470
Business loans	39,134,792	49,167,911
Small group loans	30,361	18,347
Salary loans	1,277,515	1,178,039
Tigo pesa Agent loans	-	387
Group Agri-Loans	-	682
Shule loans	1,214,150	2,073,295
Parent Education Loan	283,112	315,206
Pamoja Loans	10,008,134	10,564,018
Pamoja Loans Plus	5,109,690	4,943,859
Insurance Claim	737,017	308,870
Micro Individual Lending Loan	238,460	-
Halo Credit overdraft account	33,197	-
Social Financial Group loan	<u>1,050,017</u>	<u>99,444</u>
Gross loans balances	59,265,785	69,267,528
Less: Provision for loan losses	<u>(2,473,869)</u>	<u>(5,207,918)</u>
Net loans to customers	<u>56,791,916</u>	<u>64,059,610</u>
b) Analysis of net loans to customers by maturity		
Up to 3 months	18,714,966	7,147,494
Between 4 months and 6 months	7,293,933	17,030,771
Between 7 months and 12 months	22,525,471	25,748,584
Between 1 year and 3 years	8,257,546	14,085,625
More than 3 years	<u>-</u>	<u>47,136</u>
	<u>56,791,916</u>	<u>64,059,610</u>
c) Movement of provision for loan losses		
Balance brought forward	5,207,918	2,327,243
Provision charge for the year	3,633,766	7,132,607
Bad debts written off during the year	(5,212,181)	(4,251,932)
IFRS 9 Impact	<u>(1,155,634)</u>	<u>-</u>
Balance carried forward	<u>2,473,869</u>	<u>5,207,918</u>

The total write off during the year was TZS 5,212,181,000 (2017: TZS 4,251,932,000) and recovery of previous written off loan was TZS 771,822,000 (2017: TZS 289,042,000).

	2018	2017
	TZS '000	TZS '000
18. OTHER ASSETS		
Prepaid expenses	2,240,477	2,208,197
Staff advances	131,275	355,048
Tax advance	200,000	-
Withholding tax receivable	-	-
Stationary and office supplies	54,272	62,052
Mobile Banking - Nostro Accounts	148,809	-
Other receivables	<u>477,552</u>	<u>536,958</u>
	<u>3,252,385</u>	<u>3,162,255</u>

19. WORK IN PROGRESS

	2018	2017
	TZS '000	TZS '000
Work in Progress - DFA Project	1,562,222	1,860,121
Work in Progress - Credit Scoring Project	9,132	341,951
Work in Progress - Haloyako Project	1,110,536	1,712,891
Work in Progress - Branch refurbishment	-	502,625
	<u>2,681,890</u>	<u>4,417,588</u>

These are payments towards Digital Field Automation (DFA), Credit scoring, Haloyako Project and Branch refurbishment. In the effort to make the business efficient and cost effective, the Bank introduced DFA project to enable transform current paper process into digital from client on-boarding, loan underwriting process to performance management. Each field staff will be provided with a tablet loaded with the DFA system. The project is expected to reduce turnaround time in serving the Banks clients by ensuring instant processing of loan application at field in which DFA system is integrated with core banking system. In the effort of reaching and including unbanked population the Bank introduced Haloyako project (Haloyako Savings and Loans) which is designed to mobilise savings and loans through mobile platform.

20. PROPERTY AND EQUIPMENT

	Leasehold Improvements	Motor Vehicles	Office Equipment	Office Furniture and Fittings	Total
	TZS '000	TZS '000	TZS '000	TZS '000	TZS '000
Cost					
At 1 January 2017	3,099,031	171,566	5,356,195	926,144	9,552,936
Additions	280,879	-	488,065	46,009	814,953
Disposals	-	-	-	-	-
At 31 December 2017	<u>3,379,910</u>	<u>171,566</u>	<u>5,844,260</u>	<u>972,153</u>	<u>10,367,889</u>
At 1 January 2018	3,379,910	171,566	5,844,260	972,153	10,367,889
Additions	375,036	-	997,813	94,689	1,467,538
Disposals	-	-	(3,855)	(52,983)	(56,838)
At 31 December 2018	<u>3,754,946</u>	<u>171,566</u>	<u>6,838,218</u>	<u>1,013,858</u>	<u>11,778,589</u>
Accumulated depreciation					
At 1 January 2017	1,784,208	171,566	3,556,792	645,745	6,158,311
Charge for the year	370,866	-	695,824	106,576	1,173,266
Eliminated on disposal	-	-	-	-	-
At 31 December 2017	<u>2,155,074</u>	<u>171,566</u>	<u>4,252,616</u>	<u>752,321</u>	<u>7,331,577</u>
At 1 January 2018	2,155,075	171,566	4,252,615	752,321	7,331,577
Charge for the year	375,483	-	777,952	81,343	1,234,778
Eliminated on disposal	-	-	(3,855)	(52,983)	(56,838)
At 31 December 2018	<u>2,530,558</u>	<u>171,566</u>	<u>5,026,712</u>	<u>780,681</u>	<u>8,509,517</u>
Net book value					
At 31 December 2018	<u>1,224,388</u>	<u>-</u>	<u>1,811,506</u>	<u>233,177</u>	<u>3,269,072</u>
At 31 December 2017	<u>1,224,836</u>	<u>-</u>	<u>1,591,644</u>	<u>219,832</u>	<u>3,036,312</u>

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

21. INTANGIBLE ASSETS**Computer software**

	2018 TZS '000	2017 TZS '000
Cost		
At the beginning of year	2,487,600	2,286,922
Additions	<u>1,305,963</u>	<u>200,678</u>
At end of the year	<u>3,793,563</u>	<u>2,487,600</u>
Amortization		
At beginning of the year	1,386,433	1,083,770
Amortization for the year	<u>841,792</u>	<u>302,663</u>
At end of the year	<u>2,228,225</u>	<u>1,386,433</u>
Net book value	<u>1,565,338</u>	<u>1,101,167</u>

22. DEPOSITS FROM CUSTOMERS AND BANKS

Deposits from customers	28,359,996	24,852,821
Deposits from banks	<u>6,719,759</u>	<u>20,302,200</u>
	<u>35,079,755</u>	<u>45,155,021</u>
Payable within 3 months or less	19,882,366	18,352,836
Payable within 4 to 6 months	3,306,896	15,091,916
Payable after 6 months	<u>11,890,493</u>	<u>11,710,269</u>
	<u>35,079,755</u>	<u>45,155,021</u>
Current and demand accounts		
Savings deposits	34,715,855	44,625,898
Collateral deposits	112,049	112,559
Others	<u>251,851</u>	<u>416,564</u>
	<u>35,079,755</u>	<u>45,155,021</u>

23. BORROWINGS

Borrowings-Principal amounts	34,633,050	33,492,751
Interest payable	<u>304,710</u>	<u>859,618</u>
	<u>34,937,760</u>	<u>34,352,369</u>
Maturities of borrowings are as follows:		
Current - due within 12 months	<u>28,024,611</u>	<u>16,279,309</u>
Long term - due after 12 months	<u>6,913,149</u>	<u>18,073,060</u>

23. BORROWINGS (CONTINUED)**Analysis of principal amounts**

	Balance as at 1 January 2018 TZS '000	Receipt TZS '000	Payment TZS '000	Balance as at 31 December 2018 TZS '000	Balance as at 31 December 2017 TZS '000
Symbiotics Sicav (Lux.)	3,604,000	-	3,604,000	-	3,604,000
Symbiotics Sicav (Lux.)	4,090,231	-	4,090,231	-	4,090,231
Blue Orchard Microfinance Fund	6,690,196	-	4,408,965	2,281,231	6,690,196
SELF Microfinance Fund Blue Orchard Microfinance Fund	-	1,500,000	750,000	750,000	-
Financial Sector Deepening Trust Fund Tanzania	4,350,000	-	4,350,000	-	4,350,000
Access Africa Fund LLC	123,434	332,812	-	456,246	123,434
REFFA Fund	2,567,422	-	2,567,422	-	2,567,422
Global Partnerships Social Investment Fund 6.0 LLC	917,143	-	917,143	-	917,143
MCE Social Capital FMH 26 JUNE 2018 FMH 28 JUNE 2018 FMH 17 JULY 2018	4,460,130	-	2,939,310	1,520,820	4,460,130
Symbiotics 10.75% FMH 25 OCTOBER 2018	2,230,065	51,165	-	2,281,230	2,230,065
FMH 05 DECEMBER 2018	-	2,281,231	-	2,281,231	-
FMH 05 DECEMBER 2018	-	3,421,846	-	3,421,846	-
FMH 05 DECEMBER 2018	-	4,562,461	-	4,562,461	-
AgRIF Cooperatief U.A.	-	4,531,217	-	4,531,217	-
	-	2,281,231	-	2,281,231	-
	-	2,281,231	-	2,281,231	-
	-	3,421,846	-	3,421,846	-
	4,460,130	102,330	-	4,562,460	4,460,130
	<u>33,492,751</u>	<u>24,767,370</u>	<u>23,627,071</u>	<u>34,633,050</u>	<u>33,492,751</u>

Blue Orchard Microfinance Fund

The original loan is a dollar denominated loan amounting to USD 4,000,000 and the loan balance as at 31 December 2018 was USD 3,000,000. Interest is fixed at a rate of 6.35% per annum on the principal loan amount and is payable every six months. The loan is payable in four equal instalments on 30 September 2017, 30 March 2018, 30 September 2018 and 30 March 2019.

GLOBAL PARTNERSHIPS SOCIAL INVESTMENT FUND 6.0 LLC

The original loan is a dollar denominated loan amounting to USD 2,000,000. Interest is fixed at a rate of 6.5% per annum on the principal loan amount and is payable quarterly starting from 20 June 2017. The loan is payable in three equal instalment on 20 March 2018, 20 September 2018 and 20 March 2019.

MCE Social Capital

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 is payable in four equal instalment on 29 January 2019, 29 July 2019, 29 January 2020 and 29 July 2020.

23. BORROWINGS (CONTINUED)

AGRIF Cooperatief U.A. (INCOFIN)

This is a dollar denominated loan amounting to USD 2,000,000. Interest rate is fixed at 6.5% per annum on the principal loan amount and is payable semi-annually starting from 7 May 2018. The loan is payable in two equal instalments on 07 May 2019 and 07 November 2019.

SELF-MICROFINANCE FUND.

This is a local currency denominated loan amounting to TZS 1,500,000,000. Interest rate is fixed at 11% per annum on the principal loan amount and is payable quarterly on each dates of 15 July 18, 15 October 18, 15 Jan 19, and 15 April 19

FMH FUNDING.

During 2018 FINCA microfinance bank received six short term loans totalled \$8m from the parent Bank (FMH) to address the liquidity needs. \$1m was received on 26th June, \$1.5m was received on 28th June, \$2m was received on 17th July, \$1m was received on 25th October and the last two loans one of \$1m and the other of \$1.5m was received on 5th December 2018. All these loans was priced at 6% and is expected to keep on roll over at short term until the liquidity is stabilized.

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 50% on 30th November 2019 and another 50% on 17th May 2020. Interest on the loan is payable semi-annually on each dates of 31 Nov 2018, 31 May 2019, 31 Nov 2019, and 17 May 2020

BORROWINGS COVENANTS

As at 31st December 2018, the Bank was in breach of profitability and gross loan portfolio quality covenants with two lenders, INCOFIN and Symbiotic where the total exposure was less than 20% of total borrowings. These borrowings are maturing in less than one year. The Bank applied for the waiver to all the lenders which were in breach and agreed with all the lenders that since the forecast and projections shows when exactly the breaches will be cured is not certain due to nature of the cause of breaches, the Bank will be updating all the lenders regularly on status of the major issues and performance of the business through skype meetings which the Bank has been doing. Therefore all the lenders are aware of the breaches and they have all the updates and the business plan and projections which shows the turnaround strategic plans. The breaches started about two year ago however none of them have demanded the prepayment or immediate payments.

24. RELATED PARTY TRANSACTIONS

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

	2018	2017
	TZS '000	TZS '000
Amount due from related parties		
FINCA International	121,281	3,023
FINCA Nigeria	5,021	5,020
FINCA Uganda	-	-
Finca Africa IT Services Centre	<u>1,931</u>	<u>54,734</u>
	<u>128,233</u>	<u>62,777</u>
Amount due to related parties - FINCA International	<u>114,311</u>	<u>562,847</u>
Transactions with related parties		
<i>FINCA Microfinance Holding:</i>		
Management fees	-	1,223,050
Capital injection	8,544,455	-
Royalty fees	<u>722,997</u>	<u>907,027</u>
	<u>9,267,452</u>	<u>2,130,077</u>
<i>FINCA Network Support, BV:</i>		
IT professional fees	<u>-</u>	<u>878,168</u>
Loans and advances to employees		
At 1 January	1,171,512	1,247,654
Net movement during the year	<u>106,003</u>	<u>(76,142)</u>
At 31 December, 2018	<u>1,277,515</u>	<u>1,171,512</u>
Interest earned	<u>187,038</u>	<u>151,157</u>
Loans and advances to employees have been included under Note 17 - Loan and Advances to customers		
Deposits from employees		
Opening balance	263,497	263,497
Net movement during the year	<u>(11,470)</u>	<u>153,115</u>
Closing balance	<u>252,027</u>	<u>416,612</u>
Key management personnel compensation		
Salaries and other benefits	<u>1,171,069</u>	<u>1,085,618</u>
Directors' emoluments		
Fees and allowances for services as Directors	<u>174,391</u>	<u>54,602</u>

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

25. DEFERRED GRANT

	Balance as at 1 January 2018 TZS '000	Receipts TZS '000	Credited to profit or loss TZS '000	Capitalized TZS'000	Balance as at 31 December 2018 TZS '000	Balance as at 31 December 2017 TZS '000
Net Hope Engine	446,839	-	-	(446,839)	-	446,839
Financial Sector Deepening Trust Tanzania	-	81,807	-	-	81,807	-
Master Card	105,070	-	(5,253)	-	99,817	105,070
	930,377	79,518	(230,400)		779,494	930,377
	<u>1,482,286</u>	<u>161,325</u>	<u>(235,653)</u>	<u>(446,839)</u>	<u>961,118</u>	<u>1,482,286</u>

During the year, Master card provided a grant of TZS 79,518,000 to the Bank to subsidise its operations. As at year end, the deferred grant balance was TZS 961,118,000 (2017: TZS 1,482,286,000). Engine provided a grant amounting to TZS 81,807,000. The grants were 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.

	2018 TZS '000	2017 TZS '000
26. OTHER PAYABLES		
Accrued expenses	5,854,339	1,622,493
Provisions	434,776	371,208
Other payables	306,291	2,297,123
Employee bonus and leave days accrual	244,353	137,098
Deferred income on loans	710,687	754,394
	<u>7,168,000</u>	<u>5,182,316</u>
27. FEES AND COMMISSION INCOME		
Application fees	2,705,482	3,244,305
Account maintenance fees	1,150,345	1,173,306
Recovery income	771,822	185,601
Other income	1,141,171	730,279
	<u>5,768,820</u>	<u>5,333,491</u>

28. 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 any liability will accrue from the pending suits.

Tax assessment

During the year, Tanzania Revenue Authority (TRA) reviewed the objection with the respect the tax assessment of years of income 2013, 2014 and 2015. A proposal statement of objection was issued relating to corporate tax, withholding tax, value added tax (VAT), employment taxes, excise duty and stamp duty. With adjustment of tax assessment of TZS 2,795 million, consequently provision has been made in these financial statements.

FINCA MICROFINANCE BANK LIMITED

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

29. COMMITMENTS

	2018	2017
	TZS '000	TZS '000
Capital commitments		
Budgeted and not contracted for	<u>7,128,129</u>	<u>6,800,000</u>
Operating lease commitments		
Future minimum lease payments in respect of lease of Bank equipment		
Payable within one year	<u>-</u>	<u>191,087</u>
Future minimum lease payments in respect of lease of Bank premises:		
Payable within one year	1,321,890	1,460,974
Payable between one year and 5 years	3,414,925	4,702,067
Payable after more than five years	<u>240,000</u>	<u>436,088</u>
	<u>4,976,815</u>	<u>6,599,129</u>

The rent paid under operating leases during the year period was TZS 2,311,812,000 (2017: TZS 1,673,598,000).

30. ASSETS PLEDGED AS SECURITY

As at 31 December 2018, a total of TZS 2 billion (2017: 4.3 billion) assets were pledged by the Bank to secure Bank liabilities.

31. CURRENCY

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

32. 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 2018.