EAST AFRICAN DEVELOPMENT BANK

Annual Report and Accounts 2007

Contents

Letter of transmittal

The Honourable Minister for Finance,
The Republic of Kenya;

The Honourable Minister for Finance,
The United Republic of Tanzania;

The Honourable Minister for Finance, Planning and Economic Development,
The Republic of Uganda;

In accordance with Articles 26 and 35 of the Bank's Charter, the Board of Directors herewith submit to the Honourable Members of the Governing Council and to the Members of the Bank the Annual Report of the East African Development Bank for the period 1st January to 31st December, 2007.

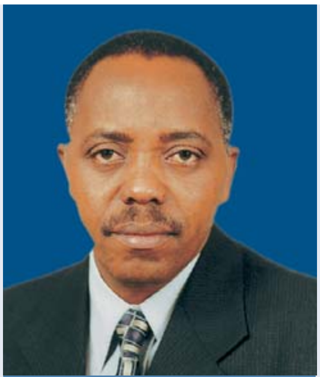
This Report describes the activities of the East African Development Bank during the year, shows the Bank's financial condition as at 31st December 2007, and includes commitments made during the year. The Report also shows the activities relating to the East African Community and a review of the economic performance of the Member States.

Honourable Members of the Governing Council, please accept the assurances of my highest considerations.

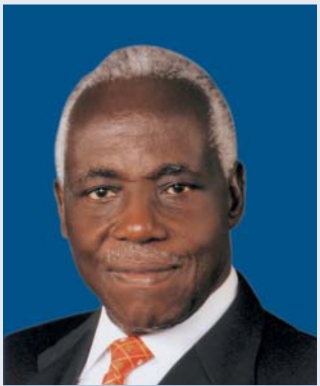
Joseph K. Kinyua

CHAIRMAN
BOARD OF DIRECTORS
EAST AFRICAN DEVELOPMENT BANK

Board of Directors



Joseph K. Kinyua
Chairman



James Mulwana

Christopher M. Kassami

Khadija L. Simba

Mukaila Ojelade

Francis N. Karuiru

Gray S. Mgonja

"A leading development finance institution with an overriding objective of promoting development in East Africa."

Chairman's Statement

The Bank's operations in 2007 were undertaken on the backdrop of impressive performance by the Member States economies.

Joseph K. Kinyua

The economies of Uganda and Tanzania registered strong recovery the previous year's slowdown while Kenya sustained its growth trend. The regional economy performance was in line with the robust performance of the global economy which, according to the IMF's World Economic Outlook (October 2007), registered a commendable real growth of 5.2%, although that represented a mild decline from 5.4% realised the previous year.

The buoyant global economic performance presented both opportunities and challenges to the business community in East Africa. The good performance of the sub-Saharan Africa economy, whose real growth was 6.1% compared with the previous year's 5.7%, was principally driven by the significant rise in oil prices. Although the high oil prices adversely affected oil importers such as the Bank's Member States, there was a compensatory effect arising from an increase in the international prices of non-fuel commodities such as coffee, one of the main exports of the East African economies.

The accommodative policy environment characterised by a pursuit of macroeconomic stability by the Member States underpinned the business growth and profitability of enterprises. The business community, however, remained responsive to the sentiments that occasioned the mild slowdown in the global economy such as the consequences of the sub-prime mortgage market crisis in the developed financial markets generally, and particularly the American market. The Bank's operations during the year had to contend with the inherent challenges of project risks associated with such sentiments.

The Bank's Member States continued to underscore the need for accelerated structural reforms. Such reforms, especially those entailing the liberalisation of the infrastructure provision and consequently the Governments' continued divestiture from the sector, accorded the Bank increased opportunity for direct intervention where such provision is amenable to commercially oriented enterprises. As this report indicates, the Bank continued supporting infrastructure projects, especially those in the energy and transport and communication sectors, cognisant of the fact that these sectors' enhancement spurs greater regional development.

Out of the Bank's USD 84.6 million worth of investments approved in 2007, about 42.0% were in the infrastructure category comprised of Transport, Storage and Communication, and Electricity Water, Gas and Oil sector. Manufacturing, Construction, Hotels and Restaurants, Financial Intermediation, and Education, Health and other Community and Social Services accounted for 13.4%, 28.4%, 6.8%, 4.0% and 5.8%, respectively. During the year, an additional USD 61.5 million was disbursed to various projects. Besides lending operations, the Bank continued enhancing its treasury management function for purposes of better management of its liquidity as well as revenue generation.

The financial performance for the review year manifested a difficult period for the Bank. After progressive trend in profitability in the previous three years, and despite posting an operating income before provisions of USD 19.3m, the Bank recorded a loss of USD 8.9 million compared to net profit of USD 4.6 million in 2006. The decline in performance was occasioned by an increase in impairment losses on loans and advances. The loss notwithstanding, the Bank's interest income of USD 25.3 million was a 39% increase from the previous year's level.

There was a 15% increase in interest charge and similar expenses, arising mainly from full charges on increased drawdown on commercial banks swap transactions of 2006 being booked in 2007, and the US dollar – the Bank's reporting currency – depreciating vis-à-vis other major currencies. Despite the increase, the Bank registered a net interest income of USD 13.6 million, which was 69% above the 2006 level. The Bank's balance sheet grew by 7% from USD 262.2 million as at 31st December 2006 to USD 279.9 million as at 31st December 2007.

The Bank takes full cognisance of the challenges it has to surmount regarding its operational efficiency, and the expectations of the business community. To address these challenges, the Bank is taking a variety of measures aimed at improving the quality of its portfolio. The thrust of the measures include a careful screening of the quality of the projects entering the Bank's portfolio, strengthening risk management and control, and enhancing project supervision and debt collection.

Backed by the support of Member States who remain committed to enhancing the Bank's capital base, I am confident that there is capacity to harness the ensuing opportunities. The positive signal arising from the Member States gesture of commitment to the Bank through additional equity injection will enhance its capacity to attract investment resources. Besides the shareholders, the Bank continues to benefit from the support of its lenders. During the review year, the Bank concluded negotiations for lines of credit from the European Investment Bank (Euro 25 million), China Development Bank (USD30 million) and Export-Import Bank of India (USD 5 million).

The Bank maintains its active participation in activities aimed at enhancing regional integration in the context of the East African Community (EAC), in concurrence with the Member States' strong belief that they have much to gain through co-operation among themselves than through separate development pursuits. Similarly, having recognised the importance of a vibrant and diversified regional capital market in accelerating growth and sustainable economic development, the Bank continues to promote the region's capital markets through its local currency resource mobilisation programmes.

On behalf of the members of the Board of Directors, I wish to express my appreciation for the continued support and guidance of the Governing Council and the Advisory Panel. I also wish to thank our international partners, especially the various multilateral and international institutions that have continuously supported us in our resource mobilisation efforts, the Bank's members and clients for their support during the year, and management and staff for their continued dedication and commitment to the Bank's course. I am optimistic that with the continued support, the Bank will remain on course in its endeavour to meet the expectations of its stakeholders.

Joseph K. Kinyua

CHAIRMAN
BOARD OF DIRECTORS
EAST AFRICAN DEVELOPMENT BANK

East African Community Activities

The East Africa Community (EAC) Customs Union entered its third year in 2007 with a number of notable milestones attained. Notably, two new Member States – Republics of Rwanda and Burundi – joined the regional integration arrangement. The entry of the two new Member States signifies progress towards attaining the overriding goal of creating a single market of over 120 million people and a combined income of more than USD 50 billion.

The thrust of the EAC activities during the review year was the ongoing consolidation of the Customs Union. Such activities entailed the leveraging of the regional programmes in the promotion of trade and investments as well as the development of regional infrastructure. Consequently, positive progress was reported in increased intra-EAC trade and growth of revenue. The direction of intra-regional trade continued to manifest the disparities in the Member States' industrial development, consequently being skewed in favour of Kenya given its relatively better development industrial sector.

The registered progress was a manifestation of determination by the Partner States to address the implementation challenges of the Customs Union, especially regarding the rules of origin under the gradual elimination of internal tariffs as well as the elimination of non-tariff barriers. At the same time, there was a deliberate emphasis on physical infrastructure development as a trade facilitating mechanism. Steady progress was maintained on the East African Road Network Project, particularly the Mombasa – Katuna road (Northern Corridor) and the Dar es Salaam – Mutukula road (Central Corridor), which moved from the planning to implementation stage and is expected to be completed in the next two years.

There was continued recognition that an efficient railway network is not only a cost effective way of facilitating trade in the region but also one of the ways of easing the burden on the road network and therefore road maintenance expenses. Subsequent to the handover of Kenya Railways Corporation and Uganda Railways Corporation to Rift Valley Railways Company in November 2006, the EAC member States embarked on the East African Railways Master Plan study. Following the concession agreement between RITES of India and the Government of Tanzania in November 2007, the latter, together with the Government of Zambia, is studying the recommendations of a study on the way forward for the concessioning of the Tanzania – Zambia Railways (TAZARA).

In the civil aviation sub-sector, the EAC Civil Aviation Safety and Security Oversight Agency (CASSOA) was established in April 2007. The agency's establishment, the first of its kind in Africa, being in line with Convention on International Air Transport, is meant to support the Member States in implementing the best practice and recommended standards in civil aviation. The establishment of CASSOA manifested the important role that the EAC Member States have attached to a safe and secure aviation industry as a stimulant of investment and productivity, development of tourism and international trade.

In view of the adverse effects of the drought on the regional economy, especially in Uganda and Tanzania, in 2006, there was concerted attention on measures to redress the energy deficit in the region. The implementation of the East Africa Power Master Plan, which is estimated to cost USD 1.2 billion and USD 600 million in generation and transmission respectively, envisages a time frame of up to seven years for the realisation of a full fledged regional power system. The 3rd East African Petroleum Conference was held in March 2007 on the backdrop of positive progress in oil exploration registered amongst the Member States during the previous year.

In the spirit of promoting the region as a single investment and tourism destination, EAC participated in the International Tourism Fair in Berlin in March 2007 at which the Partner States held joint promotion under one common exhibition area for the first time in the international tourism fair. The EAC further participated in the World Travel Market (WTM) in London in November 2007, having participated in a similar event in November 2006. These events were considered a prelude to planned joint promotion and marketing activities to Asian and American markets.

The EAC Partner States continued to explore the modalities of optimally exploiting shared resources. The launch of the Lake Victoria Basin Commission in July 2007 was one such modality. The Commission is set to roll out the development programme on the lake, including safety of navigation, environmental protection and conservation and overall sustainable development of the Lake Victoria Basin. The attendant activities include the management of the Mount Elgon Regional Ecosystem Conservation Programme (MERECP) which embraces part of Kenya and Uganda, as well as the Lake Victoria Region water and Sanitation Initiative project that is being implemented in partnership with UN-HABITAT.

As has been the tradition in recent years, there was continued harmonisation of the Member States fiscal and monetary policies. Underlying such endeavours was the objective of achieving convergence on both macroeconomic and fiscal regimes. Officials of the member states central banks continued to meet regularly in an effort to coordinate the macroeconomic policies and ensure maintenance prudential norms of banking supervision and regulation in the region.

High Point Hotel, Kenya

HL Developers, Uganda

Hood Transport, Tanzania

East African Community Activities

As a continuation of the past years' symbolic gesture of harmonisation, the budgets of the member states were delivered in the respective parliaments on June 14th June 2007. These developments manifested the confidence in the ongoing preparations for the establishment of a Common Market by 2010. The EAC Summit of August 2007 decided that the EAC move towards a monetary union by 2012, thus necessitating the initiation of technical studies on the creation of such union.

The EAC member states continued making strides in creating a conducive environment for the deepening of the capital markets, with the capital markets development committee (CMDC) steering the process of harmonising policies relating to financial markets with a view to developing a regional capital market. The CMDC continued to harmonise trading policies in the three stock exchanges in the region. At the same time, there was continued endeavour by the EAC secretariat to ensure self-reliance in the financing of projects and programmes. This was against the background of the EAC's development partners maintaining their support for the promotion of the Secretariat's capacity. The secretariat made strides in coordinating the process of seeking to establish the EAC Development Fund that can assure the EAC of sustainable sources of funding its activities. At the same the Secretariat continued to put in place mechanisms aimed at ensuring that the Development Strategy (2006 – 2010) is effectively implemented on a timely basis.

The Bank continued to play its part in furthering the regional integration process. Its contribution to the process was particularly in recognition of the fact that savings in the region are low against the background of financial sector reforms not being complete, necessitating enterprises in the region to rely on foreign savings. Bank remained keen in identifying and supporting projects with a regional orientation, which characteristically are either sponsored by investors from more than one Member State; have comparative advantage in raw material utilisation and production of output for local consumption or export; or utilise resources common to the Member States. The Bank was particularly keen in identifying such projects in the infrastructure sectors. The Bank continued to be a keen participant of EAC activities as well as sponsor integration-enhancing endeavours with the sustainable development of Lake Victoria basin remaining an area of interest to the Bank and other development partners.

Member States Economies

The Bank's Member States economies were characterised by impressive performance during 2007. Both Uganda and Tanzania, which had experienced slowdowns during the previous year on account of adverse effects of weather conditions on agriculture and electricity generation capacity, manifested strong recovery while the Kenyan economy sustained its robust growth trend.

The Member States' positive performance was in line with the global economy's strong performance during the year. According to the IMF's World Economic Outlook (October 2007), the global economy's real growth for 2007 was estimated an impressive 5.2%, although it represented a decline from the previous year's 5.4% growth. Sub-Saharan Africa equally sustained positive performance, realising a real growth of 6.1% compared to 5.7% registered the previous year.

The continent's performance continued to be buoyed by increased commodity production, especially oil, on the back of significant rise in oil prices. Even with the oil prices adversely affecting oil importers like the Bank's Member States, the increase in the international prices of non-fuel commodities had a compensatory effect. The increase in metal prices benefiting economics such as Mozambique, Zambia and South Africa and the increase coffee prices benefited Ethiopia, Sierra Leone and the East African economies.

The member states continued to pursue the policy of maintaining macroeconomic stability as a prerequisite for sustainable growth. Member States' central banks' pursuance of monetary policy remained focused on combating the inflationary pressure experienced during the year. This move was supported by prudent fiscal policies underpinned by disciplined and streamlined public expenditure, coupled with enhanced revenue mobilisation. A summary of the Member States' Key Macroeconomic indicators is given in **Table 1**.

By the end of the review year, the Bank's Member States had been operating for three years under the East African Customs Union that commenced in January 2005. Under the integration arrangement, the Member States have been working towards the convergence of key macroeconomic variables, which necessitated the harmonisation of macroeconomic policies among the partner states, with emphasis on exchange rates, and monetary and fiscal policies.

Table 1: A Summary of Selected Macroeconomic Indicators - 2007

	Kenya	Tanzania	Uganda
Real GDP Growth (%)	7.0	7.1	6.0
Nominal GDP (USD bn)	27.3	15.5	11.9
Population (m)	36.9	39.4	30.3
Headline Inflation (%)*	6.1	9.8	6.7
Exchange Rate (Local Currency/USD)*	63.3	1,147.3	1,711.6
91-Day Treasury Bills Rate*	6.9	9.9	8.0
External Debt (USD bn)*	6.7	5.4	1.9

Source: Central Banks of respective economies; Economist Intelligence Unit (EIU); CIA World Fact book;
** end of period.*

The policy harmonisation is premised on the fact that cooperation in monetary and financial matters and maintenance of convertibility of currencies of the Member States will ultimately result in the establishment of a single currency. The underlying quantifiable parameters, which form the convergence criteria, are as follows:

- Achieving and maintaining a real GDP growth of 7%
- Achieving and maintaining and underlying inflation rate of less than 5%
- Attaining sustainability in current account deficit as a percentage of GDP levels
- Reducing the budget deficit, excluding grants, as a percentage of GDP to sustainable levels of less than 5%
- Raising the ratio of gross national savings to GDP to at least 20%
- Building up foreign reserves to a level equivalent to 6 months of goods and non-factor services imports.

The Member States remained committed to undertaking measures that will enable the attainment of the convergence. The commitment was manifest in both the non quantifiable policy aspects and the quantifiable criteria. The Member States performance on the quantifiable convergence criteria during the year as summarised in **Table 2** was mixed. All the three economies registered positive real GDP growth, with Kenya realising and Tanzania surpassing the 7% target. It is notable that the economies growth trend is towards that target. The general inflationary pressure experienced in the three economies resulted in the underlying inflation target being missed by the end of the year although in the case of Kenya the target was met for much of the year. Accordingly, the Member States central banks continued to pursue monetary policies focussed on addressing the inflationary pressure.

Uganda and Tanzania were able meet the foreign reserves target equivalent to 6 months of import cover of foreign reserve while Kenya missed the target although it attained its budgetary expectations. The three economies continued to put in place measures aimed at enhancing the depth of their financial systems with a view to promoting an increase in domestic savings mobilisation. Not only did the gross national savings remain well below the 20% target, but so did the gross fixed investments as a percentage of GDP at 22%, 24.5% and 18.4% for Kenya, Uganda and Tanzania respectively, implying that the economies remained significantly dependent on foreign savings to finance domestic investments.

An overview of the respective Member States economies as well as the bearing of the macroeconomic developments during the review period on the private sector's investment environment is discussed overleaf.

Table 2: Macroeconomic Performance on the Convergence Criteria - 2007

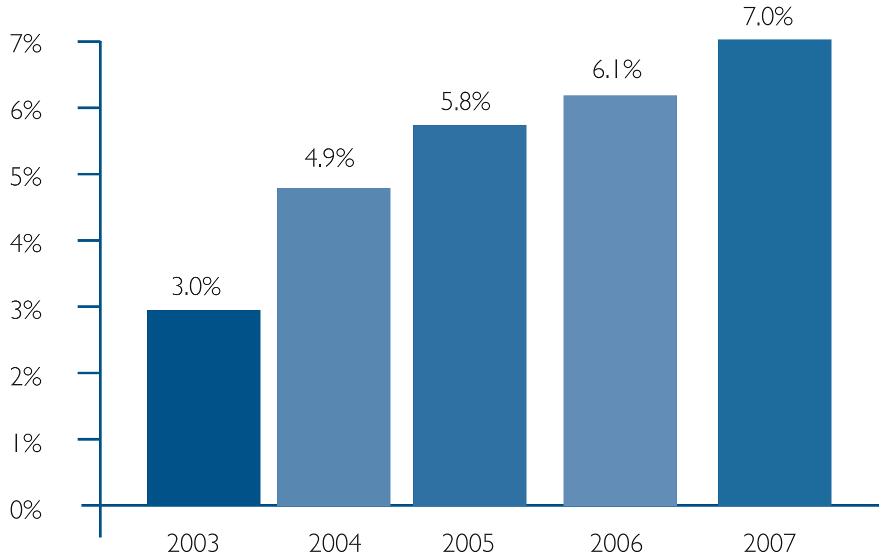
	Kenya	Tanzania	Uganda
Underlying Inflation (%)	5.2	6.1	6.7
Current Account Deficit (% of GDP)	4.4	13.3	3.1
Budget Deficit - Excluding Grants (% of GDP)*	2.8	9.1	8.4
Gross National Savings (% of GDP)**	10	11.2	11.2
Foreign Reserves (Months of Imports Cover)	4.3	6.6	7.0

Source: Central Banks of respective economies; Economist Intelligence Unit (EIU); World Bank;
** fiscal year 2006/07; ** beginning of period*

Kenya

The performance of the Kenyan economy during the review year was characterised by a continuation of the growth momentum experienced during the preceding four years. The economy's real growth for 2007 is estimated at 7.0% compared to 6.1% realised in 2006 (**Figure 1**).

Figure 1: Real GDP Growth



Source: Central Bank of Kenya;

Growth was evident across all major sectors of the economy. The agricultural sector that accounts for about a quarter of the economy's income realised a 7.6% growth during the first eleven months of the year compared to 5.5% during the previous year's corresponding period **(Table 3).** The sector's growth was mainly driven by faster growth in the production of tea and horticulture, which expanded by 23% and 17% respectively. Notwithstanding their relatively modest share of GDP, hotels and restaurants, and building and construction sectors realised robust growth during the review year, even though the former registered a decline in growth compared to the previous year. Both the manufacturing and financial services sectors maintained a five-year growth trajectory in line with the overall economic performance.

Like in the recent past years, the economy continued to register impressive performance in tourism, telecommunication, energy, construction and manufacturing, reflecting an increase in investor confidence. The economy recorded a 9.9% increase

Table 3: Share of GDP and Real Growth

	Share of Real GDP (%) - 2006	Growth (%)	
		2006	2007
Agriculture, Forestry & Fishing	25.9	5.5	7.6
Manufacturing	9.9	6.9	8.3
Wholesale &Retail Trade; Repairs	9.4	11.5	7
Hotels & Restaurants	1.4	17.1	12.6
Financial Services	3.7	5.5	7.9
Building & Construction	3.0	6.3	10.3
Transport and Communication	10.9	10.8	8.5

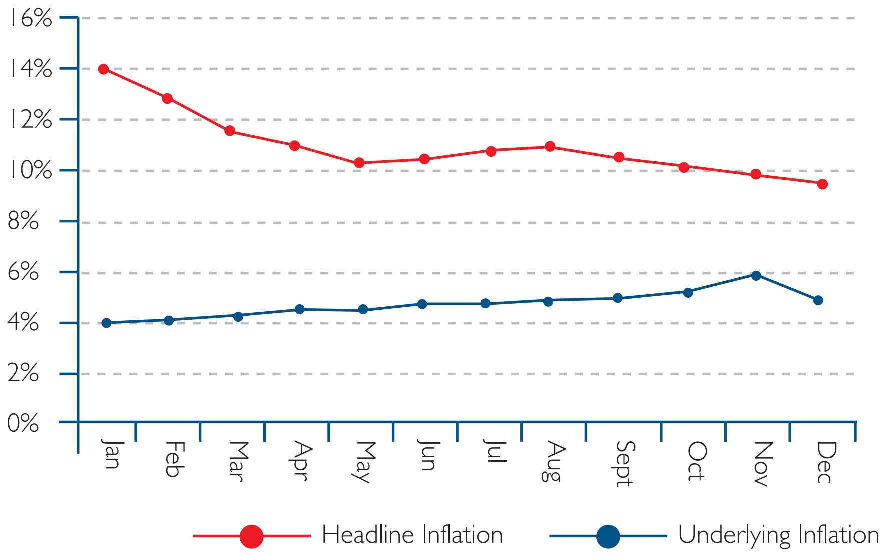
Source: Central Bank of Kenya

in tourist arrival during the year while the vibrancy of activity in the telecommunication industry as reflected by airtime excise duty increased by 28.6%. Similarly, energy generation and transportation, as represented by the volume of cargo through the port of Mombasa as well as total volume of throughput by Kenya Pipeline Company, increased during the year.

Following the pursuit of prudent monetary and fiscal policies by the Government of Kenya, the Underlying inflation, which excludes food and non-alcoholic beverages, energy and transport and communication indices from the overall Consumer Price Index (CPI), was largely contained within the 5% target except for the last three months of the year when the target was marginally missed **(Figure 2)**. However, the average annual headline inflation remained above 10 % for much of the year. Like the previous year, inflationary pressure during 2007 was predominantly driven by food and energy prices.

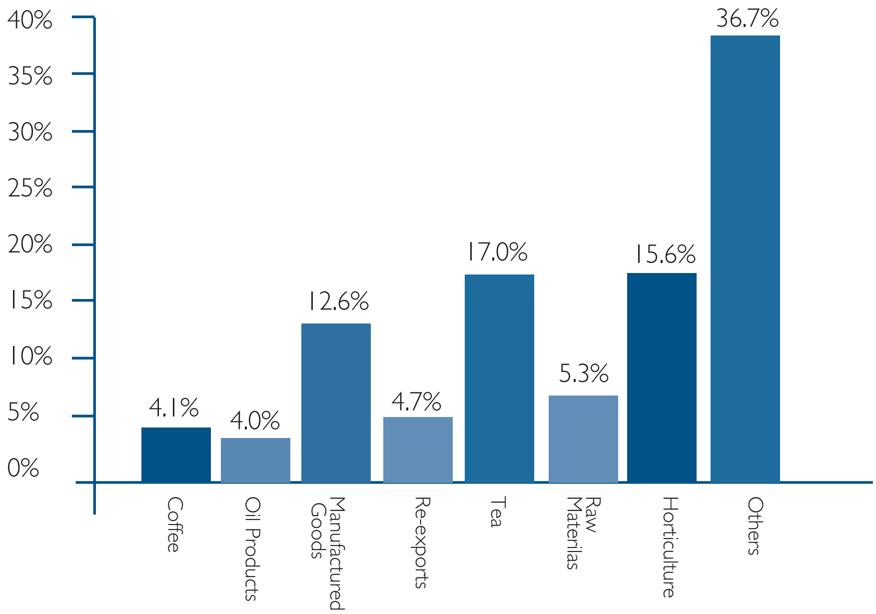
The value of the economy's merchandise export for the year increased by 16.5% from the previous year's USD 3.5 billion to USD4.1 billion buttressed by strengthened external demand occasioned by favourable growth in regional trading partners' economies. The exports continued being dominated by manufactured goods, tea and horticulture that collectively accounted for 45.2% of the total value of the exports for the year

Figure 2: Average Annual Inflation – 2007



Source: Central Bank of Kenya

Figure 3: Composition of Exports



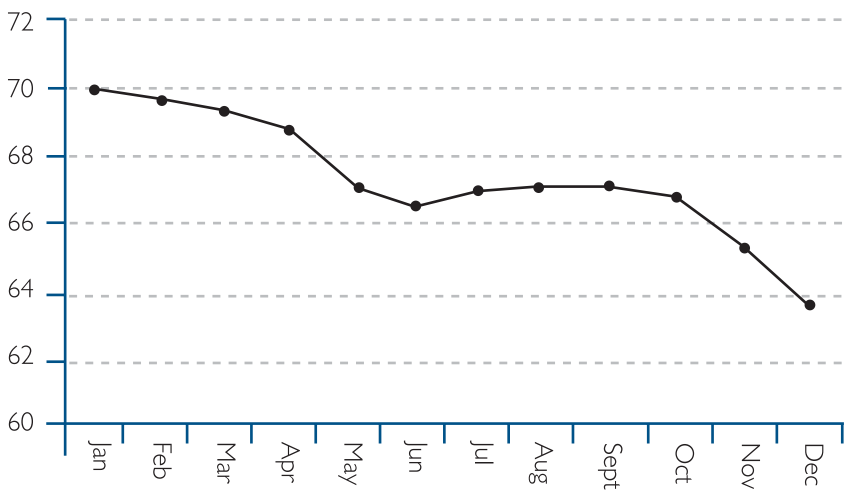
Source: Central Bank of Kenya

(Figure 3). The export main destination for Kenya's exports during the year were Uganda, United Kingdom, Netherlands, Tanzania, United States of America, Pakistan, Sudan, Egypt and Democratic Republic of Congo, with African countries absorbing about 45% of the total merchandise export. Uganda remained Kenya's leading export destination. The economy's imports, mainly comprising chemicals, machinery and transport equipment, oil, and manufactured goods, increased by 22.6% from the previous year's level to USD 9 billion. Consequently, the trade deficit widened from USD 3.8 billion in 2006 to USD 4.9 billion in 2007.

The Kenya Shilling (KES) exchange rate remained stable though with a tendency of appreciating against major international currencies, especially the USD **(Figure 4).** The economy's continued impressive performance and strong balance of payment position occasioned by improved export earnings and tourism as well as private capital inflows and remittances buttressed the KES' appreciation.

The KES' strong position especially during the first and last quarters of the review year resulted in exporters calling for the CBK's intervention, arguing that a strong KES was adversely affecting export competitiveness.

Figure 4: Nominal Exchange Rate (KES/USD) - 2007



Source: Central Bank of Kenya

The CBK however maintained that the appreciation of the shilling was driven by economic fundamentals and that any interventions in the foreign exchange would contradict the Government policy whereby the exchange rate is determined by the forces of demand and supply. The KES' exchange rate therefore continued to be market determined in order to balance the conflicting exporter importer interest and the interventions in the foreign exchange market where limited to smoothing out fluctuations arising from speculative tendencies.

On the back of a stable but generally appreciating KES was a current account position characterised by a widening deficit occasioned by an increase in the trade deficit that was not fully compensated for by the increase in the net service account **(Table 4)**. The increase in the value of exports was more than off set by the increase in imports of oil, manufactured goods, chemicals and machinery and transport equipments. Receipts from non-factor services and current transfers boosted the services account. The overall balance of payment position represented a surplus increase from a USD 675 million in 2006 to USD 882 million in 2007.

There was a deliberate endeavour to synchronise the monetary policy with the fiscal policy, the latter's thrust being disciplined and streamlined public expenditure accompanied by enhanced revenue mobilisation to support the economy's growth. The 2007/08 budget projected that the domestic revenue as a proportion of GDP will remain at the previous fiscal year's level of about 21% **(Figure 5)**. With the provisional revenue outturn of KES 373 billion, the projected revenue of KES 427 billion represents an absolute increase in total revenue. The increase is attributable to the on going reforms in tax administration and protection of the revenue base through the streamlining of the exemption regime under the East African Community customs union arrangement.

The projected expenditure equivalent to 26.7% of GDP in 2007/8 fiscal year compared to the previous fiscal year's 23.5% represents an increase in expenditure to in expenditure to support infrastructure development and core poverty reduction programmes in line with the Government of Kenya's policy of shifting resources from recurrent to development expenditure. The resultant budget deficit on commitment basis (including grants) was estimated to be equivalent to 6.2% of GDP compared to the previous fiscal year's 2.8%.

Owing to the continued positive performance, the economy's public and publicly guaranteed debt as a percentage of GDP declined from 47% in December 2006 to 44% by December 2007. However, in absolute terms the debt increased from KES 793 billion to KES 845 billion for the corresponding period. Even with the appreciation of the KES against the USD, its relatively weaker position vis-à-vis the Pound Sterling, Euro and Japanese Yen resulted in an increase in the foreign debt component as a significant portion of the country's debt is held in these currencies. The domestic debt increase was due to planned domestic borrowing.

Table 4: Current Account (USD m)

	2006	2007*
Trade Account	**-3,830**	**-4,910**
Exports	3,502	4,080
Imports	7,332	8,989
Services Account (net)	**3,302**	**3,755**
Non-factor Services	1,593	1,980
Income Account	-72	-71
Current Transfers	1,781	1,846
Current Account Balance	**-529**	**-1,155**

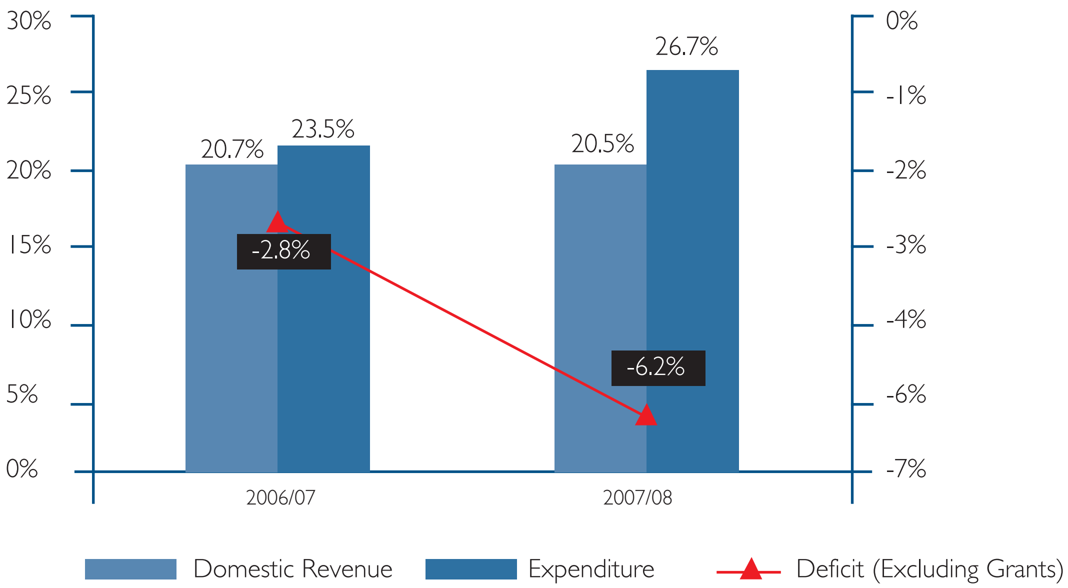
*Source: Central Bank of Kenya; * = Provisional*

Pricing in the money market during the year was influenced not only by the monetary and fiscal positions, but also by the level of market liquidity. The interest regime was generally stable with the high level of liquidity obviating upward pressure on the key interest rates. Like during the previous year, the average liquidity in the banking system remained more than double the 20% minimum requirement. Short term interest rates maintained a declining trend with the 91-day TB rates rising marginally from 6% in January 2007 to 7.6% by March 2007 before declining to 6.9% by December 2007 while the 182-Day TB rate declined from 8.2% in January 2007 to 7.0% in December 2007 **(Table 5)**.

The Central Bank of Kenya (CBK) reduced the Central Bank Rate (CBR) rate to 8.5% in June 2007 from the 10% level that had prevailing from the beginning of the year before increasing it to 8.75% in August 2007. The CBR, introduced in 2006, is the policy rate based on the inter bank rate, the repurchase (REPO) rate and a discretionary margin, and is reviewed every two months in line with the recommendations of the CBK's Monetary Policy Advisory Committee. Although the CBR is intended to be a benchmark rate independent of fiscal influence therefore replacing the 91-day Treasury Bills (TB) rate, it has taken time for the financial sector to fully adopt it as a pricing benchmark. Consequently, the 91-day TB rate is still widely used as the benchmark rate. Therefore, the adjustments of the CBR during the review year, although primarily intended to implicitly signal the direction of open market operations (OMO) – the mopping up of liquidity through sale or purchase of treasury bills, represented the continuous fine tuning of the new framework.

The average inter bank rates trend was influenced by the CBK's monetary policy conduct, especially the liquidity mop up operations. The aggressive behaviour amongst banks in terms of savings mobilisation efforts and lending, especially personal loans, was a superficial indication of competitive market behaviour, as imperfections continued to manifest through the high interest rate spreads.

Figure 5: Fiscal Indicators (% of GDP)



Source: Ministry of Finance; Budget Outlook Paper, 2008/09 – 2010/11, January 2008

Although the Kenyan economy's growth is expected to remain on course, the momentum was checked by the post December 2007 elections violence. The resulting disruption of production, distribution and consumption patterns is expected to result in a slow down in 2008. With the economic fundamentals remaining largely intact, the medium term outlook is not undermined. With the endeavour to maintain macroeconomic stability, sustenance of policy reforms meant to improve the business environment, and the continued investment in infrastructure, the economy remains on course to setting the base for the attainment of the targets of the long term strategy, "Vision 2030".

Table 5: Selected Interest Rates - KES Transactions (%)

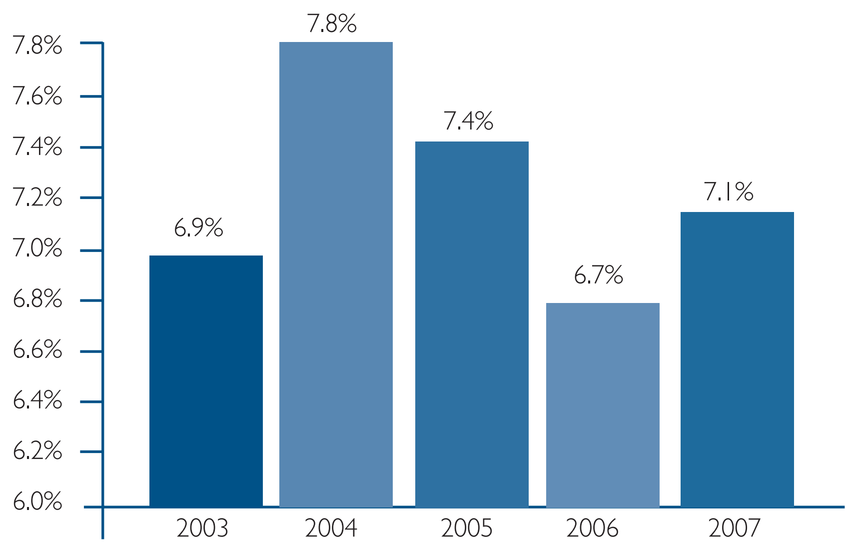
	Jan - 07	Mar - 07	June - 07	Sep – 07	Dec – 07
91– Day TB rate	6.00	6.32	6.53	7.32	6.87
182 – Day TB rate	8.28	7.97	7.19	7.82	7.87
Inter-bank rate	6.43	6.70	6.98	7.59	7.05
Average lending rate	13.78	13.56	13.14	12.87	13.32
Average deposit rate	4.35	4.19	4.18	4.48	4.32
Spread	9.43	9.37	8.96	8.39	9.00

Source: Central Bank of Kenya

Tanzania

The Tanzanian economy's performance during the review year was characterised by recovery underpinned by a rebound in agriculture and improved electricity supply especially as the economy recovered from the drought in 2006. The economy's real GDP for 2007, computed at market prices as opposed to factor prices in the old series, grew at 7.1% compared with the growth of 6.7% in 2006 **(Figure 6).** Economic activities that demonstrated strong growth during the year include, trade and repairs (9.8%), manufacturing (8.7%), mining (10.7%), construction (9.7%), communication (20.1%), real estate and business services (7.0%), which together contributed about 45 percent of GDP.

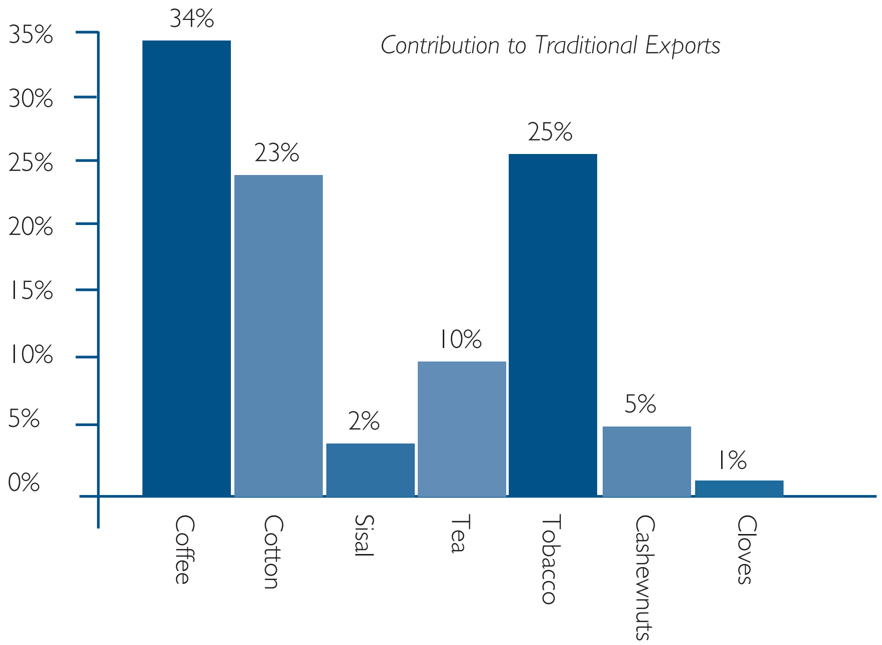
Figure 6: Real GDP Growth

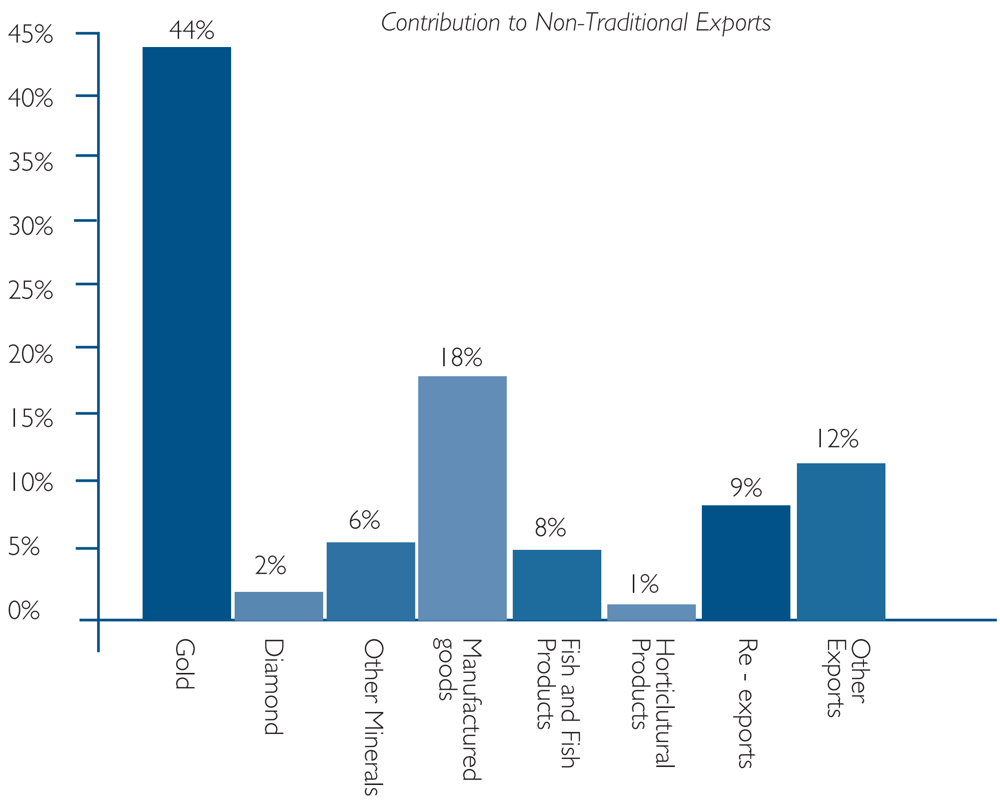


Source: National Bureau of Statistics

The economy's growth was also reflected in the improvement in exported goods and services. Export of goods increased by about 18 % during the year, reflecting mainly a very rapid increase in manufactured exports, and an improvement of traditional as well as non-traditional exports over the previous year. The traditional and non-traditional exports rose by 8.6% and 16.7 % respectively. Coffee, tobacco and cotton were the dominant traditional exports while gold dominated non-traditional exports **(Figure 7).** At the same time, imports grew at a rapid pace, nearly 25 percent during the first 7 months of the year, driven mainly by higher fuel costs and increased capital goods. As a result, between July and December 2007, the current account deficit widened to USD 938.4 million, compared with USD 589.9 million registered during the same period, in 2006. The Tanzanian Government continued to put in place measures aimed at encouraging the private sector to diversify the export base, such as improving the investment environment and providing one-stop centre facilitation service to prospective investors.

Figure 7: Traditional and Non-traditional Exports – December 2007





Source: Bank of Tanzania

The Government policies continued to support a stable macroeconomic environment as a prerequisite for sustained growth. Inflation was maintained at single digits, but largely remained above the target of 5 % due to inflationary pressures emanating mainly from increase in fuel costs and food prices **(Figure 8).**

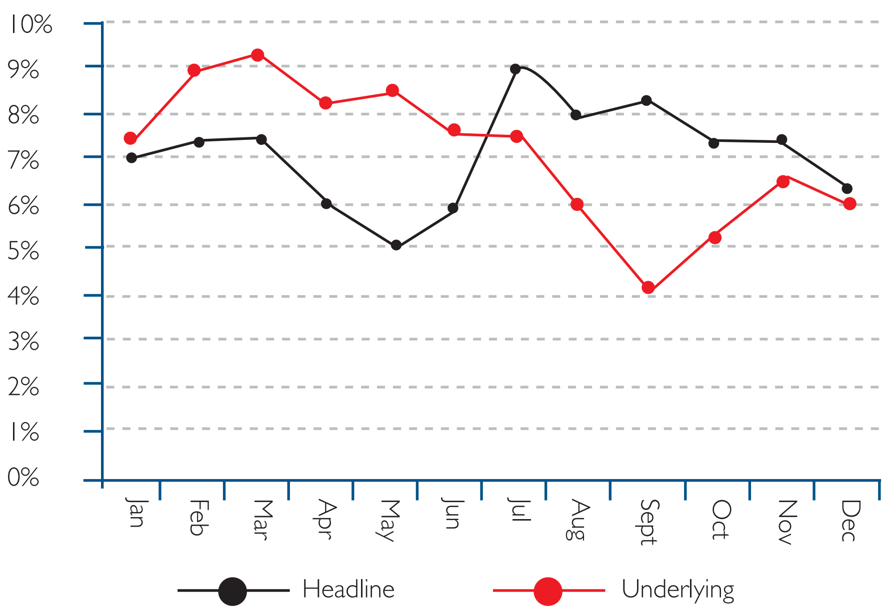
The annual headline rate which was 7 % in January dropped to 5.9 % in June before rising again to 7.8 % in August and easing to 6.4 % by the end of December, 2007. The sudden rise in inflation during July and September 2007 was a result of sharp increase in food prices. In view of the general inflationary pressure, the Bank of Tanzania (BOT) maintained a tight monetary policy stance which was complemented by sound government financing in order to anchor macroeconomic stability. To ensure that the substantial increase in public spending to meet pressing social and infrastructural needs had limited impact on demand, the Government of Tanzania has targeted zero net domestic financing of its 2007/08 budget.

Strong domestic revenue performance was recorded, with revenue rising from 14.5 percent of GDP in 2006/07 to 16.4 % of GDP in 2007/08 **(Figure 9).** Actual domestic revenue collections during the six months to December 2007 were 2 % above target and 35 % above actual collection during the corresponding period in 2006. Revenue collections from excise duty on petroleum products, VAT, and income tax, exceeded targets for the period. However, non tax revenues have performed poorly mainly on account of a downward adjustment of some fee rates envisaged during the 2007/08 budget.

Measures taken by the TRA to enhance revenue collection performance included extending the gains achieved in TRA's large taxpayers department to medium sized taxpayers; promoting electronic tax filing; improving customs processes; improving non tax revenue collection and reviewing the fiscal regime in the mining sector with a view to broadening the tax base. Donor support also increased from 9 % of GDP in 2006 to 12 % of GDP in 2007.

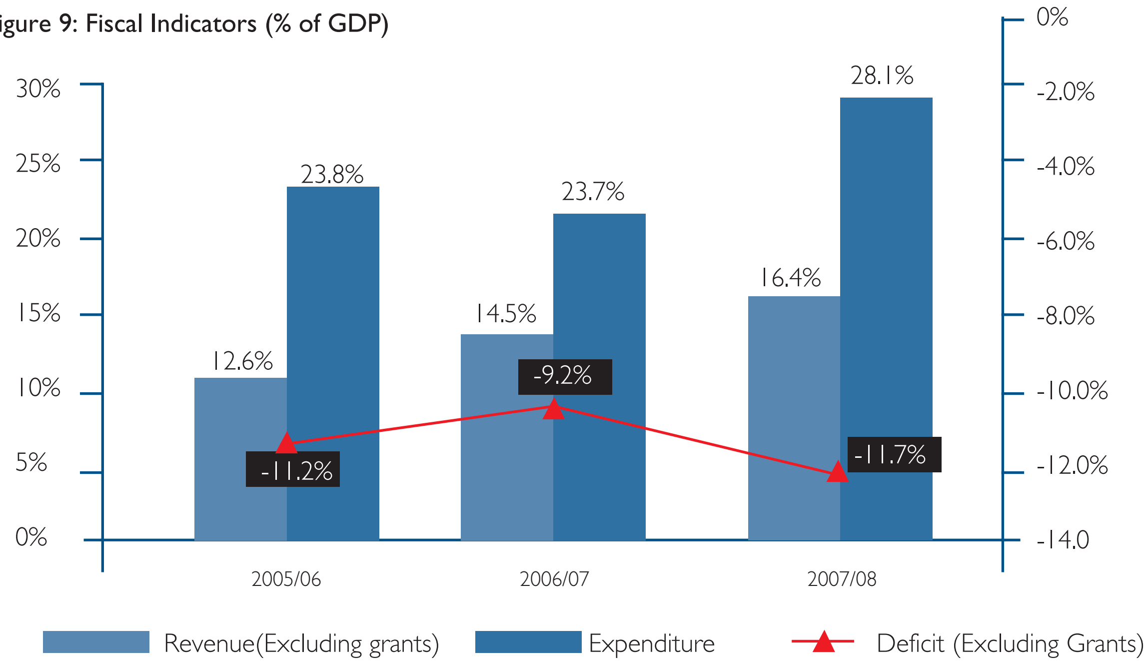
The programmed increase in expenditure to 28.1% in the 2007/08 budget **(Figure 9)** reflects the spending priorities outlined in the National Strategy for Growth and Reduction of Poverty (NSGRP) and is concentrated in development expenditure, especially in infrastructure, education and health. The expenditure will be financed by improvement in domestic revenue collection and increased donor support. All major recurrent expenditure categories were below projections during

Figure 8: Inflation - 2007



Source: Bank of Tanzania

Figure 9: Fiscal Indicators (% of GDP)



Source: Ministry of Finance

the half year to December 2007, mainly on account of slow procurement and recruitment processes. Development expenditure benefited from accelerated disbursement of foreign project financing.

The money and foreign exchange markets continued to be influenced by fiscal and monetary policy conduct as well as the developments in the external environment. In light of the observed inflationary pressure and fiscal spending, the BOT undertook a sterilization programme focused on ensuring that money supply remained broadly within the targeted range. During the year, the rate of growth of broad money supply declined from the previous year's 22% to 21%. These developments, together with a financial system that continued to portray signs of a shallow and thin market such that deposit rates characterized by sticky low single digit level while the lending rates remained high, influenced the interest rates structure **(Table 6).**

Reserve money remained on track, while at the same time Treasury Bill yields declined during the last quarter of the year. In addition to relying more on other instruments for liquidity management, the BOT enhanced competition in the market for government securities by first exercising strict discipline in limiting sales to the amounts offered for all maturities.

Table 6: Selected Interest Rates for TZS Transactions (%)

	Dec-06	Mar-07	Jun-07	Sep-07	Dec-07
Overall inter-bank rates	7.1	7.6	7.2	12.3	5.8
REPO Rates	6.3	6.9	6.3	11.6	5.1
Discount Rates	20.1	20.6	21.4	20.6	16.4
Overall Treasury Bill rates	15.0	16.0	17.1	15.6	11.4
Savings deposit rates	2.6	2.6	2.6	2.6	2.7
Time deposit rates	7.2	7.7	7.7	8.2	8.3
Lending rates	16.4	16.4	15.7	15.9	15.3
Interest Rates Spread	13.8	13.8	13.1	13.3	12.6

Source: Bank of Tanzania

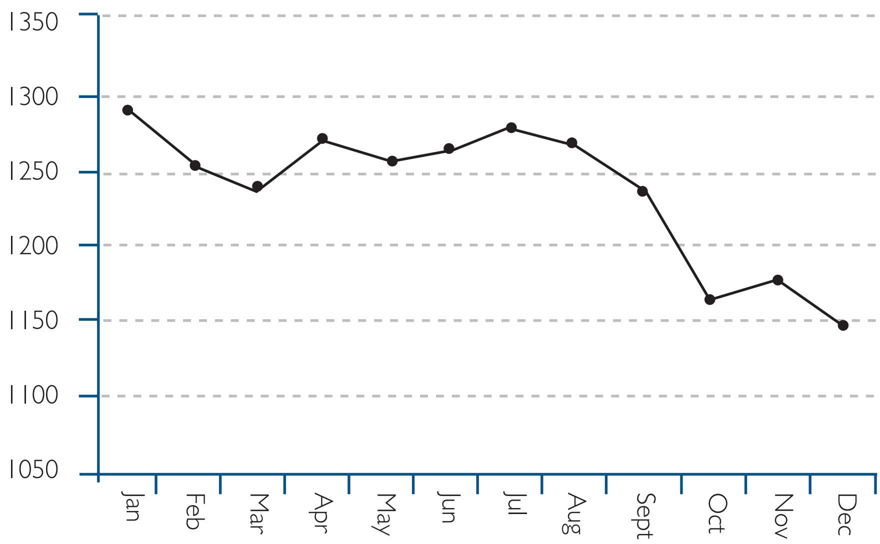
The BOT is committed to a freely floating exchange rate regime with market intervention limited to addressing any erratic market movements that are not in line with market fundamentals, subject to concerns about the potential impact of an appreciation on export competitiveness. The Bank will continue to conduct its foreign exchange sales for sterilization operations, systematically on a daily basis, to maintain an orderly market and minimize the influence on the exchange rate. Following the announcement of its new strategy for monetary and foreign exchange operations, the Tanzanian shilling experienced an initial appreciation of about 10% against major currencies, but has since traded within a fairly narrow range **(Figure 10).** The modest appreciation of the shilling provided a partial cushion against the sharp rise in the price of oil and dampened inflation on most of the consumer goods.

The economy's current account position represented a widening deficit from the previous year's position (**Table 7**). This was principally occasioned by a huge increase in imports that could not be matched by the corresponding increase in exports. The import of goods and services increased by 23%, where as exports grew by 15% of the previous year's level. The surge in imports was not necessarily a negative development considering that much of it was towards improving the economy's production capacity.

The importation of capital goods increased from USD 1.4 billion in 2006 to USD 1.7 billion in 2007 in line with the growth in economic activities. Capital goods imported were mainly transportation equipment, machinery and building and construction materials. Intermediate goods worth USD 1.9 billion constituted the economy's largest imports, principally comprising oil and industrial raw materials. The increase in oil imports was mainly as a result of a rise in quantities imported at high prices while the industrial raw materials surge was associated with the growth of the manufacturing sector following macroeconomic reforms that have attracted investments to the sector. Consumer goods imports worth USD 1.1 billion were mainly foods and pharmaceutical products, paper and textile apparels.

Tanzanian's debt stock as at the end of December 2007 was USD 7.0 billion, comprising of USD 5.4 billion external debt and USD 1.6 billion domestic debts. The Government of Tanzania continues to undertake both policy and structural reforms aimed at enhancing its growth potential. The Government is committed to sustaining the policies and strategies that have delivered the good macroeconomic performance in the recent past. The review year's strong performance underlies the recognition that there is scope for even higher growth as the economy taps opportunities of global integration. Real GDP growth is projected to reach 7.8 % in 2008.

Figure 10: Nominal Exchange Rate (TZS/USD) - 2007



Source: Bank of Tanzania

Table 7: Current Account Balance (USD millions)

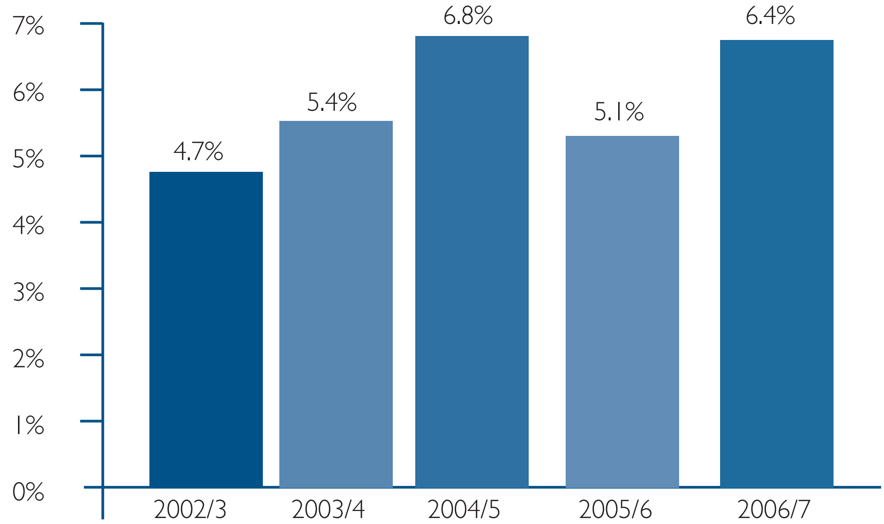
	Dec-06	Dec-07
Trade Account	**-2,128**	**-2,820**
Exports	1,736	2,007
Imports	- 3,864	- 4,827
Service Account	**245**	**218**
Receipts	1,494	1,697
Payments	-1,249	-1,479
Income Account	**- 84**	**- 68**
Receipts	81	109
Payments	- 165	-177
Current Transfers	**588**	**615**
Inflows	654	687
Outflows	-66	- 72
Current Account Balance	**-1,379**	**-2,055**

Source: Bank of Tanzania

Uganda

The Uganda economy manifested strong signs of recovery underpinned by improved weather conditions and increased power generation capacity, attributes that boosted the agricultural and industrial sectors. Consequently, the economy's real growth improved from 5.1% in 2005/06 to 6.4% in 2006/07 **(Figure 11)**. The year's performance followed the previous year's slow down principally occasioned by prolonged drought that not only affected agriculture production but also negatively influenced hydro-electricity generation capacity resulting in major load shedding.

Figure 11: Real GDP Growth



Source: Ministry of Finance, Planning and Economic Development; Background to the Budget 2007/08 Fiscal year

The agricultural sector maintained its dominance in terms of its contribution to GDP although its growth was modest **(Table 8)**. Robust performance was evident in the transport and communication sector, driven mainly by growth in the telecommunication sub-sector that benefited from the continued popularity of mobile telephones, and mining and quarrying whose growth benefited from the increased demand in construction due to increased public sector construction (roads) and private sector construction (commercial properties, especially hotels). Growth in the manufacturing sector was boosted by the improvement in the electricity supply as a result of a rise in the water levels in Lake Victoria during the year.

Uganda's exports during 2007 continued to be dominated by coffee, fish and fish products and accounted for 17% and 10% respectively of total merchandise export **(Figure 12).**

Table 8: GDP Composition and Growth

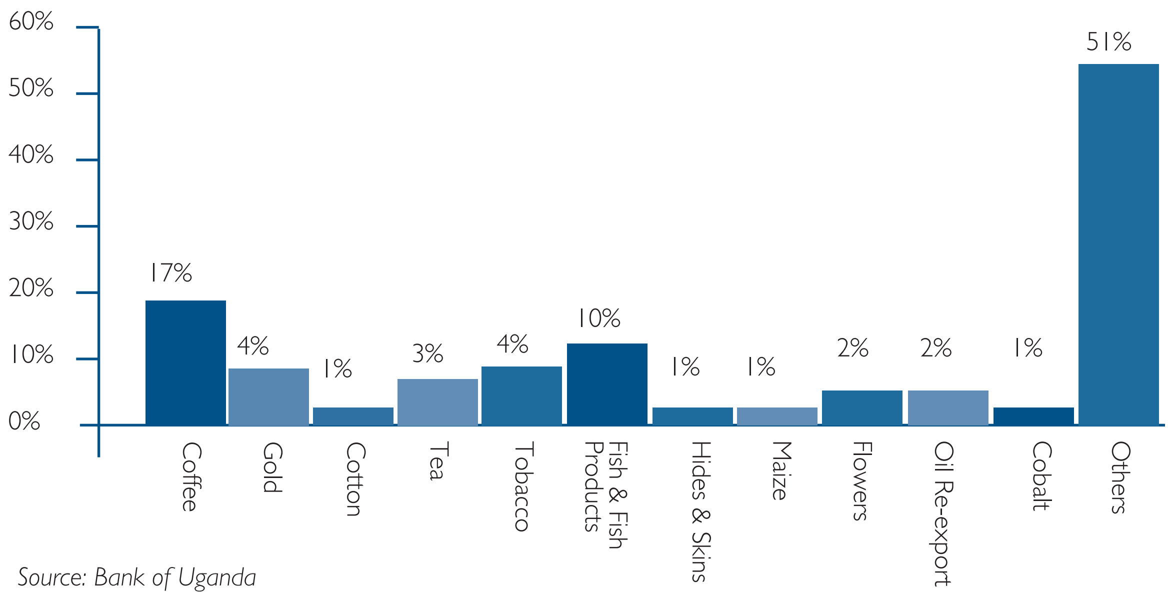
	Share of Real GDP (%) - 2006/07	Real Growth (%)	
		2005/06	2006/07
Agriculture	29	-0.6	1.9
Mining & Quarrying	0.8	8.5	14.2
Manufacturing	8.2	-0.1	2.9
Electricity & Water	1.1	-2.2	3
Construction	8.9	13.5	11.3
Wholesale & Retail Trade	10.7	6.6	9.7
Hotels and Restaurants	3	7.7	5.4
Transport and Communication	9.4	19.8	22.3
Community Services	16.5	8.1	3.7

Source: Ministry of Finance, Planning and Economic Development; Background to the Budget 2007/08 Fiscal year

The good performance of coffee exports was on account of stronger world prices. A major contributor to non-coffee merchandise exports, categorized as "others", accounted for 51% of the year's total merchandise export. This category includes the re-exports of manufactured goods such as vehicles and manufacturing equipment, basic domestic manufactures, and food and drinks. Exports to Democratic Republic of Congo and Sudan were boosted during the calendar year by improvement in security as well as increased demand in these economies.

The Government of Uganda continued to put in place measures aimed at diversifying the export base, cognizant of the fact that the economy's locally produced exports are commodity dominated. The foreign direct investments (FDI) promotion endeavours emphasized on value addition, with the end products preferably targeting the export market. Some of the infrastructural developments during the year were aimed at promoting the quality of FDI. Examples include the development of three industrial and business parks, namely Kampala Industrial and Business Park, Luzira Industrial and Business Park and Bweyogerere Industrial Estate.

Figure 12: Contribution to Goods Exports



Source: Bank of Uganda

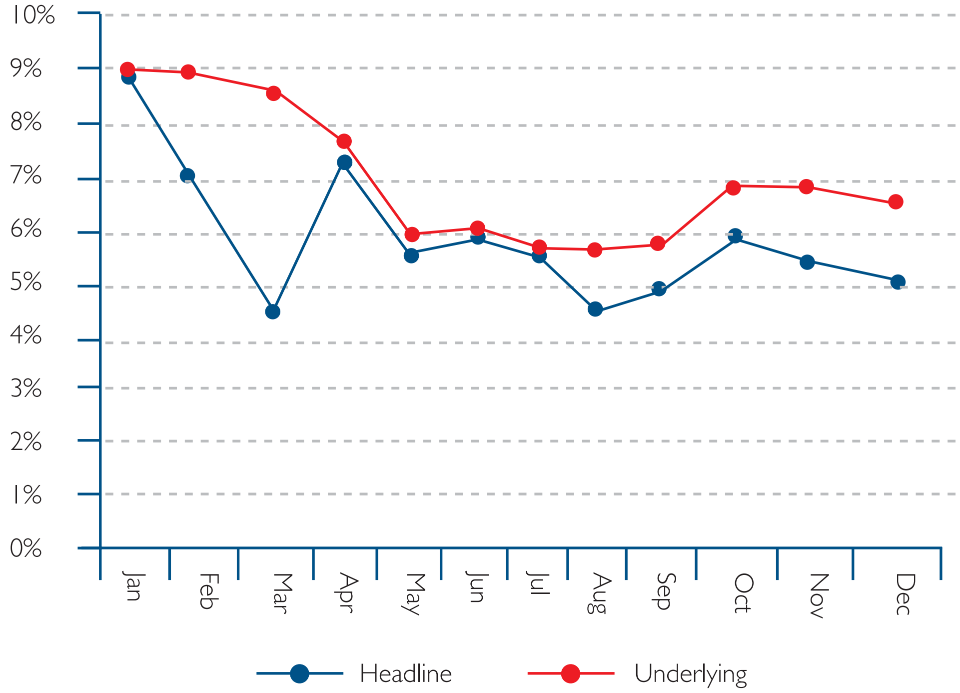
As an integral growth promoting strategy the Government of Uganda continued to pursue the policy of maintaining stable prices of goods and services. The Bank of Uganda (BOU) remained focused on containing inflation at low and stable levels, while ensuring that its monetary policy conduct did not result in instability in the money and foreign exchange markets. The annual headline inflation declined from 8.6% in January 2007 to 5.1% in December 2007 **(Figure 13)**. This was mainly attributable to the decline in the prices of staple food items, fruits and vegetables and a reduction in sugar prices. The decline would have been greater, but high international oil prices and increases in electricity tariffs had an offsetting effect. Headline inflation also demonstrated a declining trend during the period from 9.3% in January 2007 to 4.9% in December 2007.

In order to ensure that the consumer price index (CPI) reflects contemporary consumption patterns, the Uganda Bureau of Statistics (UBOS) rebased the index from 1997/98 to 2005/06. The restructuring included the changes in the reduction in the weighting of food crops and the introduction of a new category, electricity, fuel and utilities (EFU). With these modifications, underlying inflation – which previously excluded food prices – was replaced by a measure designated as "core" inflation that excludes food crop prices and EFU. The core inflation is expected to replace underlying inflation as the target measure in economic policy.

With the recognition that fiscal policy is the complementary pillar policy for maintenance of macroeconomic stability, the Government of Uganda continued to emphasize on expenditure restraint and domestic revenue mobilisation enhancement. Although total government revenue remained significantly lower than the level of public expenditure, domestic revenue as a proportion of GDP maintained a gradual upward trend **(Figure 14).** As a percentage of GDP Government expenditure increased from 21.4% in 2005/06 to 22.1% in 2006/07, this was mainly due to increased spending in the energy sector, specifically on the thermal electricity subsidy and on infrastructure.

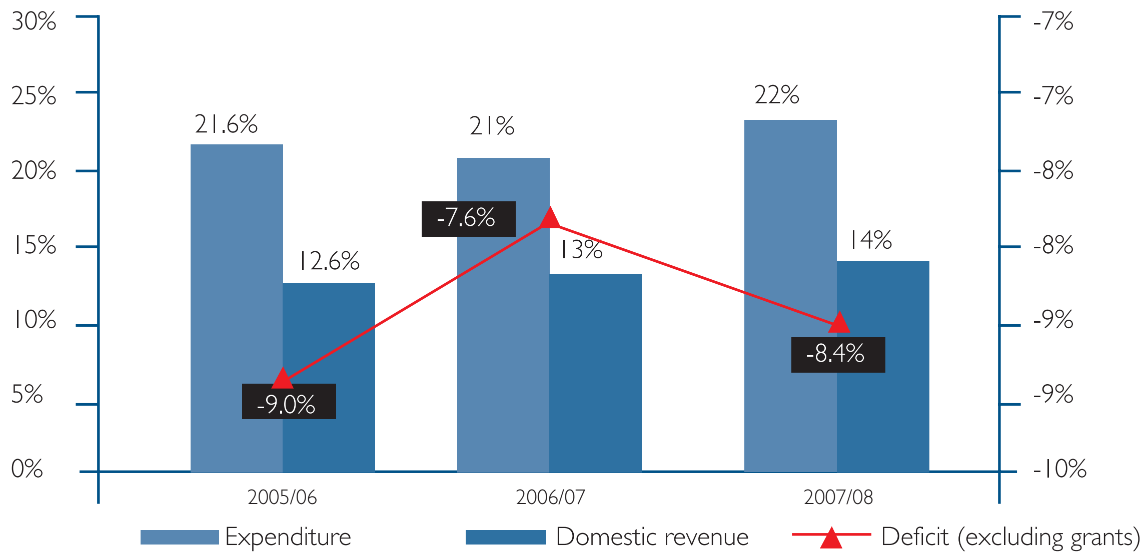
The portion of the budget financed by domestic revenue was 62.7% in 2006/7 representing a slight decline from the 63% level in 2005/6. This implies that a substantial proportion of the budget continues to be externally financed, although in the recent past years

Figure 13: Inflation - 2007



Source: Bank of Uganda

Figure 14: Fiscal Indicators (% of GDP)



Source: Ministry of Finance, Planning and Economic Development; Background to the Budget 2007/08 Fiscal year

there has been a gradual process of increasing the share of the budget that is domestically financed.

Even with budget deficit primarily financed by high concessional external resources, the financing mode continued to pose macroeconomic challenges, especially considering that the resulting liquidity increase necessitated sterilisation so as in order to avoid pressure on commodity prices, interest rates and exchange rates. The Government's 2007/08 fiscal policy thrust, announced in June 2007, was to reorient expenditure towards "prosperity for all" in the context of the Poverty Eradication Action Plan (PEAP). Even though expenditure was expected to rise especially in priority areas such as ensuring that there is improved energy supply, it was equally expected that domestic revenue mobilisation will improve on the back of anticipated strong growth.

The monetary and fiscal policies' stance as well as the financial system's imperfectly competitive structure continued to influence the pricing in the money market during the review period. Commercial banks lending rates were fairly stable. They remained high, while savings rates remained at the low single digit level **(Table 9).** The perception of high risks in lending to the private sector in an economy whose structure manifests the dominance of the agricultural sector persisted. Even with the Treasury Bill yields taking a declining trend, banks remained keen in investing in risk-free government securities rather as an alternative to lending to the private sector. Even with the anticipation that market competitiveness will be enhanced with the BOU licensing new banks, the existing market players seemed content to serve "niche market segments" as they try to modernise their operations and expand outreach.

During the review year, the foreign exchange market remained stable, albeit with the local currency portraying an appreciation bias **(Figure 15).** The Uganda Shilling (UGX) was subject to mild appreciation from UGX 1,792/USD in January to UGX 1,644/USD in June before depreciating to UGX 1763/USD in September and subsequently appreciating to UGX 1,711.61 per USD by the end of December 2007. The appreciation trend during the first half of the year, although backed by fundamentals, was partly influenced by speculative market tendencies. The BOU's action of cancelling its Treasury Bills auctions in July to obviate off-shore

Table 9: Selected Interest Rates (%) – UGX Transactions

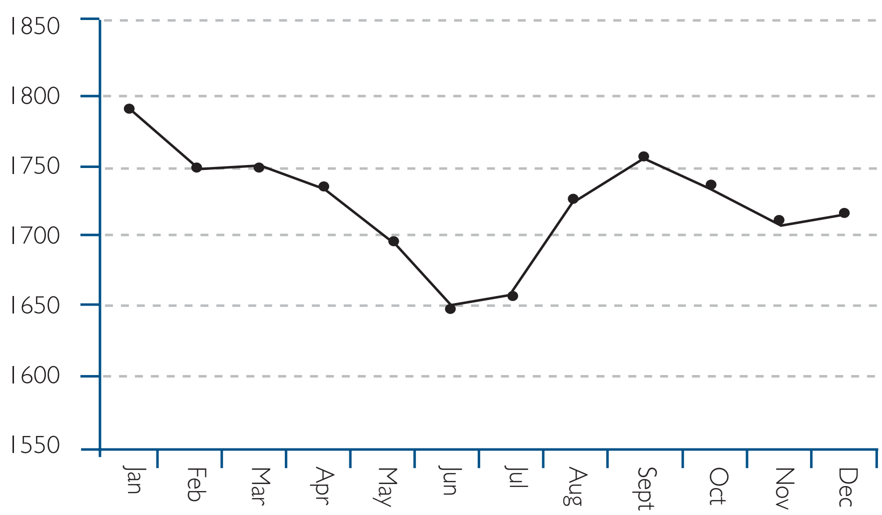
	Jan-07	Mar-07	Jun-07	Sep-07	Dec-07
Savings deposit rate	2.17	2.08	2.79	2.60	2.66
Lending rate	18.92	19.17	19.38	18.98	18.20
91-day TB rate	10.06	9.28	9.1	7.56	8.02
182-day TB rate	11.62	16.83	12.9	9.62	11.04
364-day TB rate	11.06	10.77	12.4	10.31	11.62
Rediscount rate	16.42	15.57	15.6	13.76	13.68
Bank rate	17.42	16.57	16.60	14.76	14.68

Source: Bank of Uganda

speculators coming to the market in pursuit of opportunities presented by interest rates differential led to slight depreciation of the UGX from June to September. However, the subsequent appreciation was attributed to buoyant export earnings and remittances.

The economy's current account for the year 2006/07 represented a widening deficit relative to that of the previous fiscal year **(Table 10).** Although there was registered growth in exports, the gains were outweighed by further imports growth driven mainly by capital imports for the power sector, high fuel prices and general increase in demand stemming from higher economic growth. The service account deficit widened despite modest improvements in banking, tourism and information technology receipts, as higher imports resulted in increased trade-related costs. The income account remained in deficit, although at a marginally lower level than that of the previous fiscal year's, reflecting reduced interest payments on the economy's external debt following the write-offs granted by major multilateral creditors. The net current transfers continued to show a large surplus as donors remained engaged in the country and private remittances remained high.

Figure 15: Nominal Exchange Rate (UGX/USD) – 2007



Source: Bank of Uganda

Table 10: Current Account (USD millions)		
	2005/06	**2006/07**
Trade Account	**-1,101.8**	**-1,242.3**
Exports	889.4	1,204.6
Imports	-1,991.2	-2,446.9
Service Account	**-359.6**	**-588.8**
Receipts	505.0	500.6
Payments	-864.6	-1,089.4
Income Account	**-136.6**	**-134.6**
Receipts	53.5	86.0
Payments	-190.1	-220.6
Current Transfers	**1,334.9**	**1,592.7**
Inflows	1,610.6	2,051.9
Outflows	-275.7	-459.2
Current Account Balance	**-263.1**	**-373.0**

Source: Bank of Uganda

The economy's external debt by the end of 2006/07 fiscal year was about USD 1.85 billion compared to the previous fiscal year's USD 4.6 billion. The 57% reduction was largely due to debt write-offs by the Multilateral Debt Relief Initiative (MRDI). The percentage of debt service to export of goods and services was 6.1% in 2006/07 compared to the previous fiscal year's 13.1%, an improvement attributed to higher performance in exports of goods and services and lower debt service due to USD 2.7 billion debt forgiveness. The economy performance with regard to maintenance of macroeconomic stability has generally been satisfactory. With the agricultural and industrial sectors expected to maintain their positive performance, the economy is projected attain a 7% real growth in 20007/08 fiscal year.

Private Sector Investment Environment

The Bank's Member States maintained the two pronged approach towards promoting a private sector led growth. First, they continued to pursue the policy of maintaining macroeconomic stability with a view to ensuring that there are minimum distortions to the private sector's savings, investment and production decisions. Second, the stable macroeconomic environment continued to be complemented by careful interventions aimed at mitigating business risks and market imperfections.

The provision of public goods requisite for a thriving private sector was high on the Member States' agenda. This was particularly evident in the public expenditure programmes aimed at revamping physical infrastructure. The fiscal strategy of resource reorientation towards capital expenditure and not recurrent expenditure was observed. The emphasis on infrastructure was underpinned by the recognition that the private sector's competitiveness was substantially compromised by either the dilapidated nature, or lack of basic infrastructure meant to mitigate the costs of doing business.

Notwithstanding the public intervention in the provision of private sector promoting infrastructure and utilities, electricity supply inadequacy remained a binding constraint to the Member States' industrial and commercial sectors, resulting in failure to realise their full growth potential. Even then, the review year was characterised by further strides in ensuring that additional generation capacity was realised. The infrastructure challenges were increasingly being recognised as potential opportunities by the private sector, especially in the non-public goods type of infrastructure that is amenable to private sector participation.

The measures taken by the Member States individually and collective during the review year towards the promotion of private sector development hinged on the objective of enhancing competitiveness and ensuring that there is ease to doing business. Good intentions notwithstanding, the Member States, like much of the continent, continued to lag behind when it came to promoting the ease of doing business. **Table 11** gives a summary of how the Bank's Member States performed in the 2007 World Bank IFC Survey, Doing Business - 2008, amongst 178 countries.

The Doing Business 2008 ranking, based on a ten stage criterion, ranked Kenya 72 while Tanzania and Uganda were ranked 130 and 118 respectively, out of the 178 countries surveyed. The ranking criteria ranged from starting a business, dealing with licences and employing of workers to registering properties, getting credit, protecting investors, paying taxes, trading across borders, entering contracts and closing a business. The detailed ranking for the Bank's Member States is given in **Table 11.**

One of the key attributes to the ease of doing business in East Africa was accessibility and affordability of credit. It's noteworthy that like the recent past years, the accessibility and affordability of long term credit, especially local currency finance, continued to constrain the private sector's realisation of its full potential. This, according to the ranking, was particularly the case in Uganda and Tanzania. The liberalisation of the financial markets implied that the Member States would continue to intensify the efforts towards reducing distortions that retard financial sector development such as government interventions

Table 11: Current Account (USD millions)			
	Kenya	Tanzania	Uganda
Ease of Doing Business (Rank)	**72**	**130**	**118**
1. Starting Business (Rank)	112	95	114
Procedures (Number)	12	12	18
Time (Days)	44	29	28
Cost (%of per capita income)	46.1	47.1	92
Minimum capital (% of per capita income)	0	0	0
2. Dealing with Licenses (Rank)	**9**	**170**	**81**
Procedures (Number)	10	21	16
Time (Days)	100	308	143
Cost (% of per capita income)	58.8	2,365.5	811.8
3. Employing Workers (Rank)	**66**	**151**	**11**
Difficult of hiring index (0 - 100)	33	89	0
Rigidity of hours Index (0 - 100)	0	40	0
Difficult of firing index (0 - 100)	30	60	10
Rigidity of employment Index (0 - 100)	21	63	3
Non wages labour cost (% of salary)	4	16	10
Firing cost (Weeks of salary)	47	32	13
4. Registering Property (Rank)	**114**	**160**	**163**
Procedures (Number)	8	10	13
Time (Days)	64	119	227
Cost (% of property value)	4.2	5.3	4.6
5. Getting Credit	**13**	**115**	**158**
Strength of legal rights index (0 - 100)	8	5	3
Depth of credit information index (0 - 100)	4	0	0
Public registry coverage (% of adults)	0	0	0
Private registry coverage (% of adults)	1.5	0	0
6. Protecting Investors (Rank)	**83**	**83**	**122**
Extent of disclosure index (0 - 100)	3	3	2
Extend of director liability index (0 - 100)	2	4	5
Ease of shareholder suits index (0 - 100)	10	8	5
Strength of investor protection index (0 - 100)	5	5	4
7. Paying Taxes (Rank)	**154**	**104**	**55**
Payments (Number per year)	41	48	33
Time (Hours per year)	432	172	237
Total tax rate (% of profit)	50.9	44.3	32.3
8. Trading Across Borders (Rank)	**148**	**100**	**141**
Documentation to export (Number)	9	5	6
Time to export (Days)	29	24	39
Cost to export (USD per container)	1,955	1,212	2,940
Documentation to import (Number)	8	7	7
Time to import (Days)	37	30	37
Cost to import (USD per container)	1,995	1,425	2,990
9. Enforcing contracts	**107**	**35**	**119**
Procedures (Number)	44	38	38
Time (Days)	465	462	535
Cost (% of claim)	26.7	14.3	44.9
10. Closing a business (Rank)	**76**	**109**	**48**
Time (Years)	4.5	3	2.2
Cost (% of estate)	22	22	30
Recovery rate (US cents on the USD)	31	20.5	41

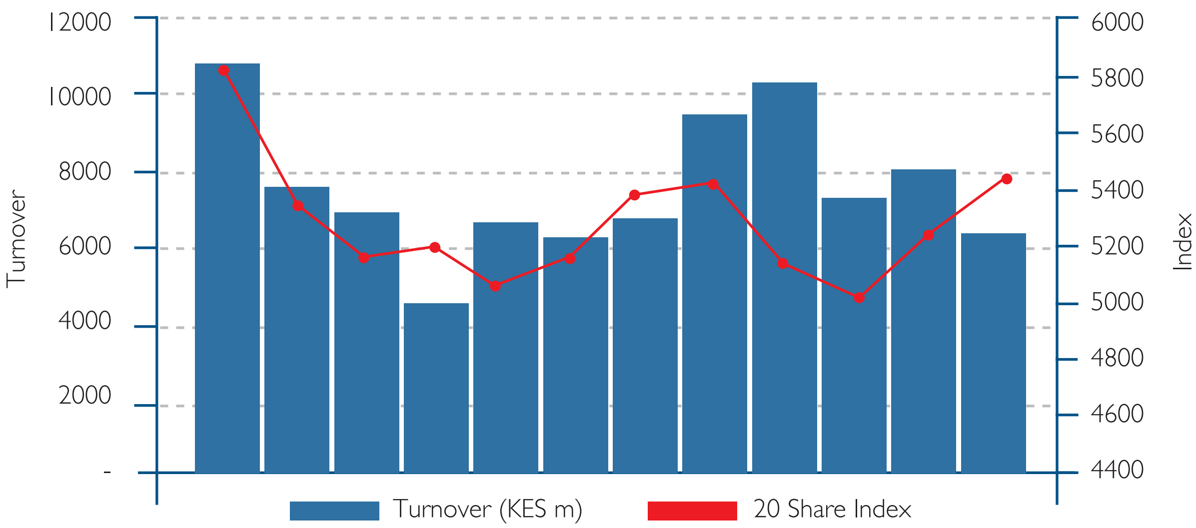
Source: Doing Business 2008; World Bank and IFC Co publication, 2007 through state ownership, barriers to competition, and directed or subsidized credit. The financial markets' pricing structure continued to reflect the persistence of market imperfections, especially with regard to competition. Endeavours such as the licensing of new banks, mergers and acquisition, and encouragement of the expansion of the banks' branch network were seen to be promoting competitive market behaviour.

The Member States continued with their treasury bond programmes with the anticipation that the longer tenures securities will provide appropriate benchmarking for longer term corporate bonds. Activity, however, remained concentrated on the short-end of the market, resulting in corporate bonds being benchmarked by short term money market instruments. Even with continued issuance of bonds, their secondary trading in the respective stock markets remained fairly inactive relative to the equities.

The evolution of activities at the Nairobi Stock Exchange (NSE), Dar es Salaam Stock Exchange (DSE) and the Uganda Securities Exchange (USE) during the review year continued to mirror the perceptions and expectations of corporate and individual investors on the overall economic performance and that of the listed corporation **(Figures 16, 17, and 18).** With increased awareness of opportunities in the stock market among households, there was marked interest and participation particularly in the initial public offerings (IPOs) in Kenya.

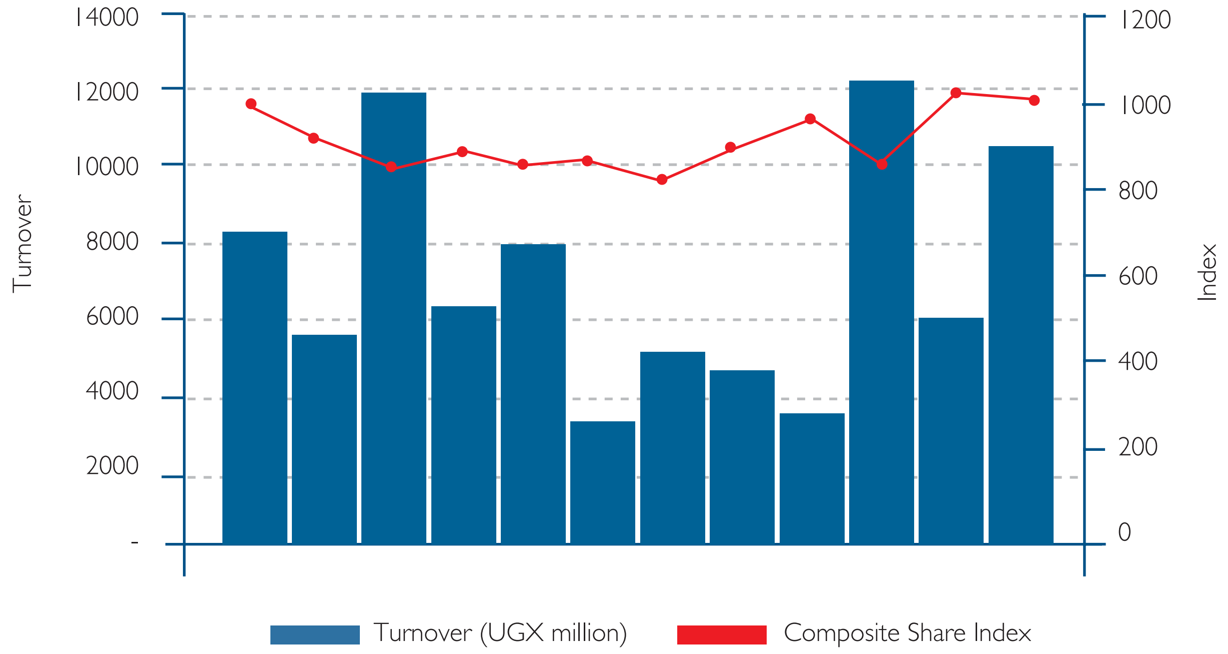
Although by international standards the three stock exchanges portray the characteristics of a shallow capital market, the NSE is relatively well developed compared to the USE and DSE. The relative underdevelopment of the latter two markets is observable from the turnover trends **(Figures 17 and 18)** characterised by activity swings occasioned by one off participation of corporate investors.

Figure 16: Nairobi Stock Exchange Turnover and Index Evolution - 2007



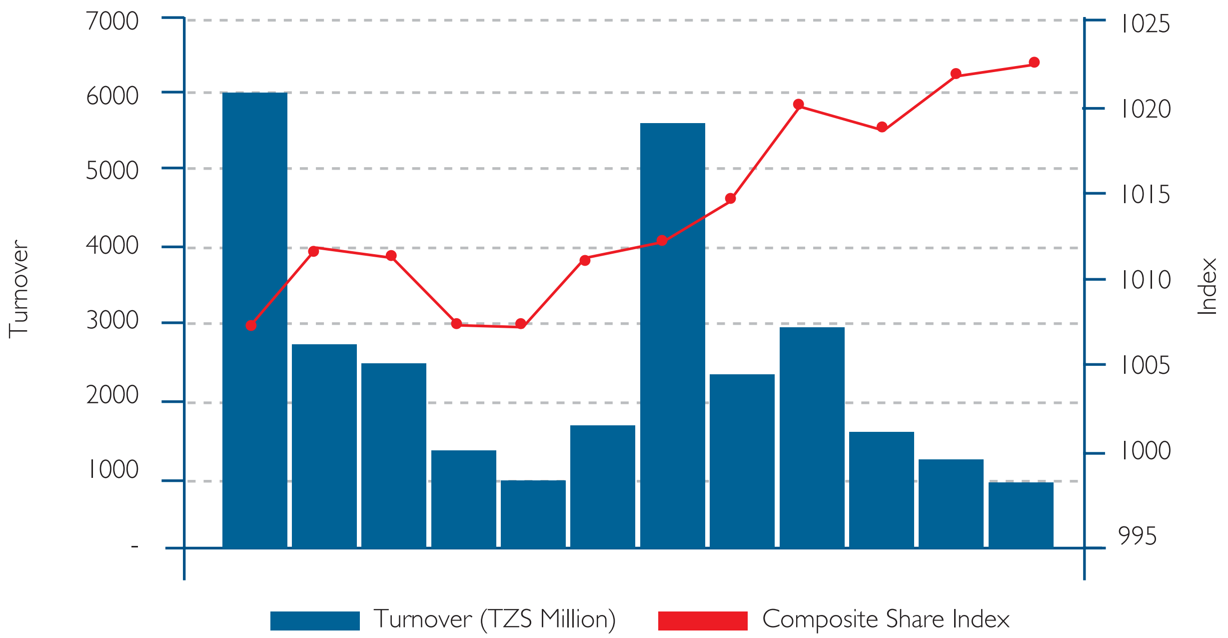
Source: Nairobi Stock Exchange

Figure 17: Uganda Securities Exchange Turnover and Index Evolution – 2007



Source: Uganda Securities Exchange

Figure 18: Dar-es-Salaam Stock Exchange Turnover & Index Evolution (TZS m) – 2007



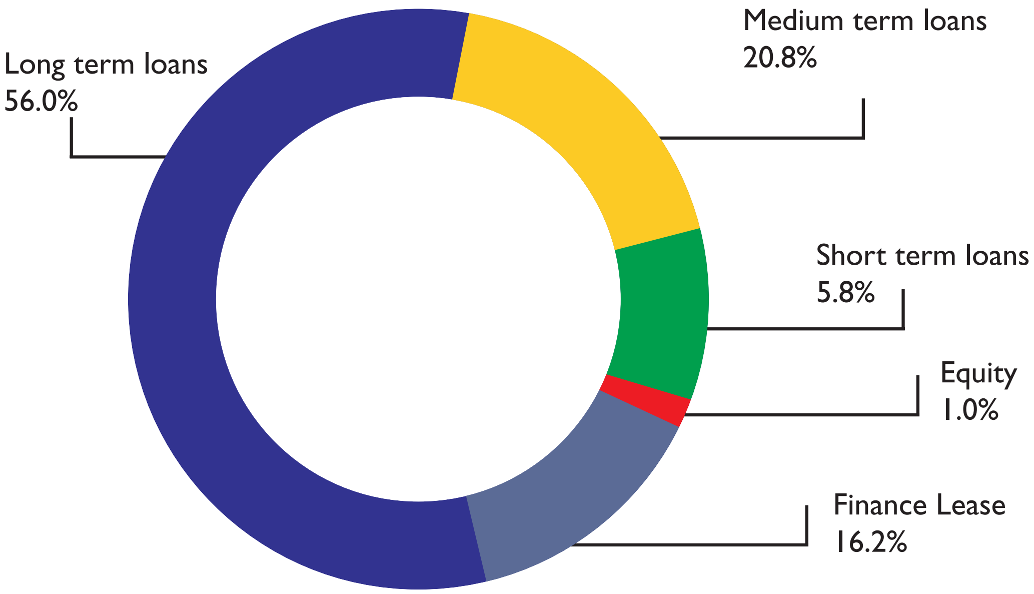
Source: Dar-es-Salaam Stock Exchange

Overview of the Year's Activities

Project Approvals

The Bank approved investments worth USD 84.6 million compared to the previous year's USD 108.61 million. The approvals comprised of USD 13.7 million in asset leasing, USD 0.8 million in equity investments, USD 69.9 million in short, medium and long term loans **(Figure 19).**

Figure 19: Uganda Securities Exchange Turnover and Index Evolution – 2007



The sector distribution of the investment approvals is given in Table 12.

Table 12: Sector Distribution of Investment Approvals

	DISAGGREGATED SECTOR	AMOUNT (USD)%
Manufacturing	11,303,288.00	13.4%
Construction	24,028,937.00	28.4%
Hotels and Restaurants	5,754,398.00	6.8%
Transport, Storage and Communication	18,609,189.00	22.0%
Financial Intermediation	3,370,941.00	4.0%
Electricity, Water, Gas and Oil	16,609,848.00	19.6%
Education, Health and other Community and		
Social Services	4,925,881.00	5.8%
Total	**84,602,482.00**	**100.0%**

Disbursements

Disbursements for the year amounted to USD 61.5 million compared to the previous year's USD 89.00 million. The level of disbursements for the year represented a 31% decline from the previous year's level. The ratio of approvals to disbursements during the review year was 1.38 : 1 compared to 1.2 : 1 in 2006.

Collections

Collections for the year amounted to USD 64.9 million, representing a 69% increase from the previous year's level of USD 38.33 million. The collections were realised largely from normal billing, bad debt recoveries and prepayments.

Portfolio Distribution

The Bank's portfolio remained dominated by Long Term loans, which accounted for about 83% of the gross portfolio. Asset Leasing accounted for 9.3% of the gross portfolio while equity investments, medium term loans and short term loans accounted for 1.8%, 4.5% and 1.8% respectively **(Table 13).**

Resource Mobilisation

The Bank continued its efforts to mobilise additional funds for investing in viable projects in the Member States. During the year under review, negotiations for a line of credit of USD 10 million with Japan Bank for International Co-operation were started while those on direct participation in local currency facilities with European Investment Bank were at advanced

Table 13: Gross Portfolio by Product

PRODUCT	GROSS BALANCES	%
Equity Investments	3,813,385.29	1.8%
Finance Leases	19,507,998.77	9.3%
Long Term Loans	173,449,589.67	82.6%
Medium Term Loans	9,428,193.87	4.5%
Short Term Loans	3,790,024.07	1.8%
Total	**209,989,191.67**	**100.0%**

The sector distribution of the Bank's gross portfolio is given in **Table 14.**

Table 14: Sector Distribution of Gross Portfolio

SECTOR	GROSS BALANCES	%
Agriculture and Fisheries	12,475,915.18	5.9%
Mining and Quarrying	1,178,635.63	0.6%
Manufacturing	57,763,942.94	27.5%
Construction	26,469,866.29	12.6%
Hotels and Restaurants	26,803,412.69	12.8%
Transport, Storage and Communication	34,526,565.88	16.4%
Financial Intermediation	13,603,630.38	6.5%
Electricity and Water	8,373,091.71	4.0%
Oil and Gas	1,905,927.27	0.9%
Education, Health and other Community Services	13,155,565.50	6.3%
General Trading	13,732,638.21	6.5%
Total	**209,989,191.67**	**100.0%**

stages at year end. Some of the negotiations started in the previous years were concluded. The agreement for a line of credit of EUR 25 million with European Investment Bank was signed in February and that for USD 30 million with China Development Bank in October 2007. A USD 5 million line of credit from Export Import Bank of India came into effect in June 2007.

By the year end, negotiations for direct participation in local currency facilities with European Investment Bank were at advanced stages. Discussions were also continuing with African Development Bank for a financial package consisting of a line of credit of USD 80 million and some technical assistance grant for the Bank's capacity building. The Bank continued accessing European Investment Bank Apex IV local and foreign currency facilities channelled through the Bank of Uganda as well as special facilities created by the central bank to cater for specific programmes e.g. the Energy for Rural Transformation Refinance Fund. During the year a sum of USD 2.3 million was drawn under these facilities.

By the year end, contributions of USD 3 million per Member State towards the recapitalization of the Bank for the fourth successive year was expected from the respective Governments of Kenya, Uganda and Tanzania. The payments for the year are part of the Bank's USD 45 million recapitalization program approved in 2003. Meanwhile, further capital injection is expected from Rwanda following its admission and from 2009 onwards Member States have committed themselves to USD 90 million capital injection to run equity and housing projects in the region.

Financial Performance

The financial performance for the review year manifested a difficult period for the Bank. After progressive trend in profitability in the previous three years, and despite posting an operating profit before provisions of USD 19.3 million, the Bank recorded a loss of USD 8.9 million compared to net profit of USD 4.6 million in 2006.The decline in performance was occasioned by a charge on non performing loans of USD 20.9 million. The Bank's staff costs and administration expenses increased from the previous year's USD 5.2 million to USD 6.6 million.

During the year, interest income amounted to USD 25.3 million, an increase of 39% from the previous year's level. The notable improvement in interest income is attributable to record disbursements made in the last quarter of 2006 with full year's income effect in 2007. The Bank also had a significant portion of its portfolio on fixed interest rate terms which cushioned the income against the drop in interest rates. Interest charge and similar expenses amounted to USD 11.7million, being 16% above 2006 level. The increase was accounted for by drawdown on commercial banks' Swap transactions in the second half of 2006 with full charges being booked in 2007 and the strengthening of the other currencies against the dollar, the Bank's reporting currency. With the substantial redemption of expensive lines of credit and the cut in interest rates, especially the dollar rates, the Bank's borrowing charges remained at the 2006 despite additional draw-downs of USD 21m during the year. The resultant net interest income of USD13.7 million was 69% above the 2006 level. The Bank's balance sheet grew by 5% from USD 262.2 million as at 31st December 2006 to USD 275.6 million as at 31st December 2007. A summary of the year's financial performance follows:

Profit and loss account for the year ended 31 December 2007

	2007 USD'000	2006 USD'000
Interest income		
Interest income on loans to projects	19,769	13,049
Interest income from lease rentals	1,654	782
Interest income from unimpaired loans to other banks	759	413
Interest on deposits	3,163	3,941
Subtotal	25,345	18,185
Interest expense		
Interest on loans from banks	(1,452)	(163)
Bond issue costs	(71)	(246)
Interest on bonds	(3,712)	(3,678)
Interest on medium and long term borrowings	(6,459)	(6,040)
Subtotal	(11,694)	(10,127)
Net interest income	13,651	8,058
Fee and commission income:		
Commission received	882	1,298
Commission from letters of credit	70	139
Commitment fees	365	168
Net income/(loss) arising from foreign exchange	739	(164)
Dividend income	144	288
Other income	3,428	1,884
Operating income	**19,279**	**11,671**
General operating expenses		
Staff administration expenses	(6,570)	(5,235)
Depreciation and amortization	(647)	(281)
Impairment loss on loans and advances	(20,917)	(1,530)
	(28,134)	(7,046)
(Loss)/profit before taxation	**(8,855)**	**4,625**
Taxation	-	-
Net (loss)/ profit for the year	**(8,855)**	**4,625**
Basic (loss)/ earnings per share	**(1.38)**	**0.81**

Balance Sheet as at 31 December 2007

	2007	2006
	USD'000	USD'000
ASSETS		
Cash and bank balances	9,812	4,186
Deposits due from banks	60,341	63,844
Other assets receivable	10,860	11,473
Loans and advances at amortized costs	184,725	173,780
Equity investments - Available for sale	1,919	965
Other investments at cost	1,918	1,858
Capital work in progress	255	-
Intangible assets	1,510	1,558
Property and equipment	4,264	4,568
TOTAL ASSETS	**275,604**	**262,232**
SHAREHOLDERS' FUNDS AND LIABILITIES		
LIABILITIES		
Dividends payable	35	35
EADB bonds at amortized cost	34,376	37,458
Other accounts payable	1,556	1,333
Medium and long term loans	137,655	121,412
	173,622	160,238
Special funds	13,841	13,841
Grants	1,103	1,271
Capital fund	7,479	7,479
Advance share capital contribution	40	31
	22,463	22,622
TOTAL LIABILITIES	**196,085**	**182,860**
CAPITAL & RESERVES		
Share capital	86,549	77,558
Fair value adjustment of available for sale assets	11	-
Special reserve	9,356	8,474
Accumulated losses	(16,397)	(6,660)
TOTAL SHAREHOLDERS EQUITY	**79,519**	**79,372**
TOTAL SHAREHOLDERS EQUITY & LIABILITIES	**275,604**	**262,232**

Risk Management Policies and Processes

During the year, the risk management function was strengthened through the appointment of a Risk Manager. The Bank continued to focus on managing risk exposures assumed in the normal course of providing development banking services. These risks are broadly categorized into credit, compliance/legal, interest rate, currency, liquidity and operational risks. Credit risk, remains the Bank's core business risk and is managed using a set of credit policies, guidelines and processes.

The day-to-day operational responsibilities for implementing risk management policies and guideline are delegated to the relevant business units while the Risk Management and Control Unit has oversight for all risk management functions. The highest level of risk management is assured by the Bank's Board of Directors, which approves all risk management policies

Baobab School, Tanzania

Corporate Governance

Governing Council

At its 33rd meeting held on 04th May 2007 in Dar es Salaam, Tanzania, the Governing Council considered and approved the Bank's Annual Report and the Audited Annual Financial Statements for the year ended 31st December 2006. The financial results showed that the Bank made a profit of USD 4.62 million compared to USD 1.42 million in 2005. The Governing Council commended the Bank's management on the positive results. The Governing Council also noted the following key activities of the East African Community (EAC) which had been acknowledged in the year.

- Finalization and adoption of the 3rd EAC Development Strategy 2006-2010 and commencement of the implementation.
- The admission of Rwanda and Burundi to the EAC with effect from 1st July 2007

At its 34th Meeting held on 21st July 2007 in Nairobi, Kenya the Governing Council approved commitments amounting to USD90 million in new capital injections into the Bank over the next five years. Out of these contributions, the Governing Council approved to invest USD30 million in an In-house Venture Capital Fund as Seed Capital and USD60 million for financing of housing in East Africa. The Governing Council approved the re-appointment of the Director General for a term of three (3) years commencing 02nd January 2008.

Advisory Panel

The Advisory Panel comprises eminent persons in international finance who provide the Bank with strategic guidance on its mandate in formal sessions that are held concurrently with the meetings of the Governing Council. Although there were no formal meetings of the Advisory Panel during the year, individual members of the Panel continued to give regular advice on various aspects of the Bank's business.

Board of Directors

During 2007, Mr. Sheku S. Sesay who represented the African Development bank (AfDB) on the Board resigned his Board position to take up a senior appointment in the Government of Sierra Leone. Pending the appointment of a substantive Director, the AfDB was represented by Mrs. Vivienne Apopo, the Alternate Director. In September 2007 the AfDB appointed Mr. Mukaila Ojelade as its representative on the Board.

Between January and December 2007, the Board had five (5) meetings in the months of January, May, July, September and November. The Board approved the Operations, Administration and Capital Budgets for the year 2007. The Board also approved the revival of the Young Professionals program and authorized the recruitment of 11 Young Professionals to undertake the program.

The following policy papers were tabled, discussed and approved by the Board:

- Environmental and Social Policy;
- Procurement of Goods and Services;
- Disposal of Assets Regulations;
- Guidelines for the Selection and Employment of Consultants by Borrowers of EADB.

The Board on various occasions discussed the proposal to establish an External East African Venture Capital Fund. It was ultimately decided that the Bank should enhance its In-house Equity Fund. Consistent with its mandate, the Board discussed and approved various investment financing proposals in several sectors of the region's economy.

Audit Sub-Committee of the Board

During the year the Audit Sub committee of the Board held three meetings in January, May and September 2007. The Sub Committee considered the draft accounts and Management Letter for the year ended 31st December 2006 and subsequently recommended their submission to the Board. The Sub committee received and discussed Internal Audit reports for a number of audits performed during the period. The Sub Committee commissioned special audits in the following areas; Internal controls to identify gaps and deficiencies in the internal control systems as benchmarked against the Committee of Sponsoring Organisations of the Treadway Commission (COSO) framework; Information technology (IT) post implementation to ensure that the new IT system was implemented in accordance with the intended objectives, evaluate adequacy of controls and procedures in the systems operation, ensure data integrity and identify potential weaknesses and risks. The reports issued by the consultants are under review by the Sub Committee. Upon the recommendation of the Sub Committee the Bank adopted a Risk Based Audit Framework to commence in 2008.

Management and staff

During the year under review, further strides were made towards aligning the Bank's human resource activities to the key Strategic Plan objectives as is spelt out in the five year Strategic Plan (2006 – 2010). The key initiatives undertaken during the year included the recruitment of new staff under the Bank's Young Professionals Programme, upgrading of the performance management system, and streamlining and automating the core human resource and administration through integrating its processes into the new Information Technology systems that were being implemented across the Bank. The number of permanent employees of the Bank as at the end of 2007 was 76 compared to 78 by the end of the previous year.

The Bank moved beyond administrative implementation of human resource activities to a more strategic focus, with attention being on performance enhancing processes. Consequently, these initiatives underpinned the Bank's performance in terms of the levels of approvals and disbursements realised during the year. In order to ensure optimal utilisation of the human resources, training and staff development was given priority especially in areas of effective marketing of the Bank's products and services.

Financial Statements for the year ended 31 December 2007

Statement Of Directors' Responsibilities

The Bank's directors are responsible for the preparation and fair presentation of the financial statements, comprising the balance sheet at 31 December 2007, the income statement, the statement of changes in equity and cash flow statement for the year then ended, and the notes to the financial statements, which include a summary of significant accounting policies and other explanatory notes, in accordance with International Financial Reporting Standards, and the Bank's Charter.

The directors' responsibility includes: designing, implementing and maintaining internal control relevant to the preparation and fair presentation of these financial statements that are free from material misstatement, whether due to fraud or error; selecting and applying appropriate accounting policies; and making accounting estimates that are reasonable in the circumstances. They are also responsible for safe guarding the assets of the Bank.

The directors accept responsibility for the financial statements set out on pages 43 to 77 which have been prepared using appropriate accounting policies supported by reasonable and prudent judgments and estimates, in conformity with International Financial Reporting Standards and the Bank's Charter. The directors are of the opinion that the financial statements give a true and fair view of the state of the financial affairs and of the loss for the year ended 31 December 2007. The directors further accept responsibility for the maintenance of accounting records that may be relied upon in the preparation of financial statements, as well as adequate systems of internal financial control.

The directors have made an assessment of the Bank's ability to continue as a going concern and have no reason to believe the business will not be a going concern for the next twelve months from the date of this statement.

Approval of the financial statements

The financial statements, as indicated above, were approved by the board of directors on 4th July 2008 and were signed on its behalf by:

Chairman

Director General

Date: 7th July 2008

Financial Statements for the year ended 31 December 2007

Report Of The Independent Auditors To The Members Of East African Development Bank

Report on the Financial Statements

We have audited the financial statements of East African Development Bank which comprise the balance sheet at 31 December 2007, the income statement, the statement of changes in equity and cash flow statement for the year then ended and the notes to the financial statements, which include a summary of significant accounting policies and other explanatory notes as set on pages 47 to 77.

Directors' Responsibility for the Financial Statements

As stated on page 41, the Bank's directors are responsible for the preparation and fair presentation of these financial statements in accordance with International Financial Reporting Standards and the Bank's Charter. This responsibility includes: designing, implementing and maintaining internal control relevant to the preparation and fair presentation of financial statements that are free from material misstatement, whether due to fraud or error; selecting and applying appropriate accounting policies; and making accounting estimates that are reasonable in the circumstances.

Auditors' responsibility

Our responsibility is to express an opinion on these financial statements based on our audit. We conducted our audit in accordance with International Standards on Auditing. Those standards require that we comply with ethical requirements and plan and perform the audit to obtain reasonable assurance whether the financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation and fair presentation of the financial statements 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 entity's internal control. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of accounting estimates made by management, as well as evaluating the overall presentation of the financial statements.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinion.

Opinion

In our opinion, the financial statements give a true and fair view of the state of affairs of East African Development Bank at 31 December 2007 and of its financial performance and cash flows for the year then ended in accordance with International Financial Reporting Standards.

KPMG
Certified Public Accountants
P O Box 3509
Kampala
Uganda

Date: 7th July 2008

Financial Statements for the year ended 31 December 2007

Profit And Loss Account For The Year Ended 31 December 2007

	Notes	2007 USD'000	2006 USD'000
Interest income			
Interest income on loans to projects	3 (a)	19,769	13,049
Interest income from lease rentals	3 (b)	1,654	782
Interest income from unimpaired loans to other banks		759	413
Interest on deposits	3 (c)	3,163	3,941
Subtotal		25,345	18,185
Interest expense			
Interest on loans from banks		(1,452)	(163)
Bond issue costs	4	(71)	(246)
Interest on bonds		(3,712)	(3,678)
Interest on medium and long term borrowings		(6,459)	(6,040)
Subtotal		(11,694)	(10,127)
Net interest income		**13,651**	**8,058**
Fee and commission income:			
Commission received		882	1,298
Commission from letters of credit		70	139
Commitment fees		365	168
Net income/(loss) arising from foreign exchange	5	739	(164)
Dividend income		144	288
Other income	6	3,428	1,884
Operating income		**19,279**	**11,671**
General operating expenses			
Staff administration expenses	7	(6,570)	(5,235)
Depreciation and amortization		(647)	(281)
Impairment loss on loans and advances	14 (i)	(20,917)	(1,530)
		(28,134)	(7,046)
(Loss)/profit before taxation	8	**(8,855)**	**4,625**
Taxation	9	-	-
Net (loss)/ profit for the year		**(8,855)**	**4,625**
Basic (loss)/ earnings per share	10	**(1.38)**	**0.81**

The notes set out on pages 47 to 77 form an integral part of these financial statements.

Financial Statements for the year ended 31 December 2007

Balance Sheet As At 31 December 2007

	Notes	2007 USD'000	2006 USD'000
ASSETS			
Cash and bank balances	11	9,812	4,186
Deposits due from banks	12	60,341	63,844
Other assets receivable	13	10,860	11,473
Loans and advances at amortized costs	14	184,725	173,780
Equity investments - Available for sale	15	1,919	965
Other investments at cost	16	1,918	1,858
Capital work-in-progress	17	255	-
Intangible assets	18	1,510	1,558
Property and equipment	19	4,264	4,568
TOTAL ASSETS		**275,604**	**262,232**
SHAREHOLDERS' FUNDS AND LIABILITIES			
LIABILITIES			
Dividends payable	20	35	35
EADB bonds at amortized cost	21	34,376	37,458
Other accounts payable	22	1,556	1,333
Medium and long term loans	23	137,655	121,412
		173,622	160,238
Special funds	24	13,841	13,841
Grants	25	1,103	1,271
Capital fund	26	7,479	7,479
Advance share capital contribution	27	40	31
		22,463	22,622
TOTAL LIABILITIES		196,085	182,860
CAPITAL & RESERVES			
Share capital	28	86,549	77,558
Fair value adjustment of available for sale assets	29	11	-
Special reserve	30	9,356	8,474
Accumulated losses		(16,397)	(6,660)
TOTAL SHAREHOLDERS EQUITY		**79,519**	**79,372**
TOTAL SHAREHOLDERS EQUITY & LIABILITIES		**275,604**	**262,232**
Off balance sheet items and contingents	36	25,159	40,121

The financial statements set out on pages 43 to 77 were approved by the Board of Directors on 4th July 2008 and were signed on its behalf by:

Chairman: Director General:

Financial Statements for the year ended 31 December 2007

Cash Flow Statement For The Year Ended 31 December 2007

	Note	2007 USD'000	2006 USD'000
Reconciliation of operating (loss)/profit to net cash flows from operating activities			
(Loss)/ profit before tax		(8,855)	4,625
Depreciation		468	252
Amortization of intangible assets		497	29
Amortization of grants		(318)	-
Gain on sale of property and equipment		-	(738)
Gain on sale equity investment		(2,772)	(480)
Operating (loss)/profit before changes in operating assets		**(10,980)**	**3,688**
Adjustment for changes in working capital			
Increase in deposits with banks maturing after 3 months		-	(7,000)
Increase in loans and other receivables at amortized cost		(10,945)	(63,262)
Increase in equity investments		(1,229)	-
(Increase)/ decrease in other investments		(60)	391
Decrease/ (increase) in other assets receivables		613	(3,303)
Increase/(decrease) in other accounts payable		223	(78)
Increase in advance share contribution		9	9
Increase in medium and long term loans		**16,243**	**24,794**
Net cash flows from operating activities		**(6,126)**	**(44,761)**
Cash flows from investing activities			
Proceeds from sale of equity investments		3,058	964
Capital work-in-progress additions		(255)	-
Purchase of property and equipment		(613)	(1,462)
Proceeds from sale of property and equipment		-	765
Net cash flows from investing activities		**2,190**	**267**
Cash flows from financing activities			
Increase in share capital		8,991	8,991
EADB bond payments		(3,082)	(3,104)
Increase in grants		150	1,014
Net cash flows from financing activities		**6,059**	**6,901**
Net increase/(decrease) in cash and cash equivalents		**2,123**	**(37,593)**
Cash and cash equivalents at the beginning of the year		61,030	98,623
Cash and cash equivalents at the end of the year	**31**	**63,153**	**61,030**

Financial Statements for the year ended 31 December 2007

Statement Of Changes In Equity For The Year Ended 31 December 2007

	Share capital USD '000	Fair value adjustment USD '000	Special reserves USD '000	Accumulated losses USD '000	Total equity USD '000
At 1 January 2006	68,567	422	7,176	(9,987)	66,178
Increase in share capital	8,991	-	-	-	8,991
Fair value reserve realized on sale of available - for-sale investments	-	(422)	-	-	(422)
Net profit for the year	-	-	-	4,625	4,625
Transfer of commission and guarantee fees from profit and loss account	-	-	1,298	(1,298)	-
At 31 December 2006	**77,558**	**-**	**8,474**	**(6,660)**	**79,372**
Increase in share capital	8,991	-	-	-	8,991
Surplus on revaluation of available for sale investments	-	11	-	-	11
Net loss for the year	-	-	-	(8,855)	(8,855)
Transfer of commission and guarantee fees from profit and loss account	-	-	882	(882)	-
At 31 December 2007	**86,549**	**11**	**9,356**	**(16,397)**	**79,519**

Notes to the financial statements for the year ended 31 December 2007

1. REPORTING ENTITY

East African Development Bank (the "Bank") is a corporation domiciled in the three East African Countries (Uganda, Kenya and Tanzania) with its head office in Kampala, Uganda. The Bank is primarily involved in development finance lending and the provision of related services as stipulated under the Bank's Charter of 1980.

2. PRINCIPAL ACCOUNTING POLICIES

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

a) Basis of preparation

The financial statements are prepared in accordance with and comply with International Financial Reporting Standards.

The financial statements are prepared under the historical cost convention as modified by the carrying of the available-for-sale investments at fair values and impaired assets at their recoverable amounts.

The preparation of financial statements in conformity with the International Financial Reporting Standards requires the use of judgments, estimates and assumptions that affect the application of policies and reported amounts of assets and liabilities and disclosures of contingent assets and liabilities at the date of financial statements and reported amounts of revenues and expenses during the reported period. The estimates and associated assumptions are based on historical experiences and the Directors' best knowledge of current events and actions, the results of which forms the basis of making judgment about the carrying value of liabilities and assets that are not readily apparent from other sources. Actual results ultimately may differ from these estimates.

Management identifies all significant accounting policies and those that involve high judgment as documented in note 32.

b) Functional and presentation currency

These financial statements are presented in United States Dollars (USD), which is the Bank's functional currency, except as indicated the financial information has been rounded off to the nearest a thousand. Assets and liabilities expressed in various currencies are translated into US Dollars at rates of exchange ruling at the balance sheet date. Transactions during the year are converted at exchange rates ruling at the transaction date. At balance sheet date the translation rates between one United States Dollars (USD) and the other currencies were as follows:-

		2007	2006
Kenya	KES	62.68	69.40
Tanzania	TZS	1,132.09	1,261.64
Uganda	UGX	1,696.29	1,739.60
Denmark	DKK	5.08	5.66
Japan	JPY	114.00	118.95
Norway	NOK	5.41	6.26
Sweden	SEK	6.47	6.87
U.K.	GBP	0.50	0.51
E.U.	EUR	0.68	0.76
Special Drawing Rights	SDR	0.63	0.66

The resulting differences from the conversion and translation of all transactions and balances are dealt with in the profit and loss account in the period in which they arise.

c) Revenue recognition

Income is recognised on accrual basis.

(i) Interest income

Interest income and interest expense are recognized on an accrual basis taking into account the effective interest rate of the interest earning asset or the interest bearing liability.

Interest income and expense include the amortization of any discount or premium or other differences between the initial carrying amount of an interest bearing instrument and its amount of maturity calculated on an effective interest rate basis. The effective interest rate is the rate that exactly discounts the estimated future cash payments and receipts through the expected life of the financial asset or liability (or, where appropriate, a shorter period) to the carrying amount of the financial asset or liability. The effective interest rate is established on initial recognition of the financial asset and liability and is not revised subsequently.

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

Interest income and expense presented in the income statement include:

- Interest on financial assets and liabilities at amortised cost on an effective interest rate basis; and
- Interest on available-for-sale investment securities on an effective interest basis.

(ii) Fees and commission income

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

Other fees and commission income including account servicing fees are recognized as the service s performed.

(iii) Dividend income

Dividend income is recognised when the right to receive dividends is established.

(iv) Other income

Other income comprises gains less loss related to trading assets and liabilities, and includes all realised and unrealized fair value changes, and interest.

d) Property and equipment

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

Management and directors review the residual value and useful life of an asset at the year end and any change considered to be appropriate in accounting estimate is recorded through the income statement.

Depreciation is calculated to write off the cost of the property and equipment on a straight-line basis over the expected useful lives of the assets concerned. The rates for depreciation used are as follows: -

Buildings	5.0%
Motor vehicles	25.0%
Office equipment	10.0% -25.0%
Furniture	12.5%

Gains and losses on disposal of property and equipment are determined by reference to their carrying amount and are taken into account in determining the result for the year.

e) Intangible assets

Computer software costs which are clearly identifiable and controlled by the Bank and have probable benefits exceeding the costs beyond one year are recognised as an intangible asset. Intangible assets are stated at cost net of accumulated amortization and impairment losses.

Subsequent expenditure on software is capitalized only when it increases the future economic benefits embodied in specific assets to which it relates. All other expenditure is expensed as incurred.

Amortization is recognized in profit and loss on a straight line basis over an estimated useful life of software from the date that it is available for users. The estimated useful life of the software is four years.

f) Operating leases

Leases, where a significant portion of the risks and rewards of ownership are retained by the lessor are classified as operating leases. Payments made under operating leases are charged to the profit and loss account on a straight line basis over the period of the lease.

g) Capital work-in-progress

Assets in the course of construction (capital work-in-progress) are not depreciated. Upon completion of the project the accumulated cost is transferred to an appropriate asset category where it is depreciated according to the policy.

h) Leased assets

Leases in terms of which the Bank assumes substantially all the risks and rewards of ownership are classified as finance leases.

Equipment leased out under finance lease arrangements is recognised as investments at the date of the agreement at an amount equal to the net investment in the lease. The interest element of each installment is recognised as income to the profit and loss account at the time each installment falls due. Provision is made for lease payments receivable considered to be uncollectible.

i) Recognition and measurement of financial instruments

A financial instrument is a contract that gives rise to both a financial asset of one enterprise and a financial liability of another. Management determines the appropriate classification of the financial instrument at the time of purchase and evaluates its portfolio on a regular basis to ensure that all financial instruments are appropriately classified.

(i)Recognition

The Bank recognises financial assets held for trading and available for sale assets on the date it commits to purchase the assets. From this date, any gains and losses arising from changes in fair value of the assets are recognised.

Trading assets and liabilities are those assets and liabilities that the Bank acquires or incurs principally for the purpose of selling or repurchasing in the near term, or holds as part of a portfolio that is managed together for short-term profit or position taking. Trading assets and iabilities are initially recognised and subsequently measured at fair value in the balance sheet with transaction costs taken directly to profit or loss. All changes in fair value are recognised as part of net trading income in profit or loss.

Held-to-maturity investments and Loans and advances are recognised on the date they are transferred to the Bank.

(ii)Measurement

Financial instruments are measured initially at cost, including transaction costs.

Subsequent to initial recognition all trading instruments and all available-for-sale assets are measured at fair value, except that any instrument that does not have a quoted market price in an active market and whose fair value cannot be reliably measured is stated at cost, including transaction costs, less impairment losses.

The determination of fair values of financial assets and financial liabilities is based on quoted market prices or dealer price quotations for financial instruments traded in active markets.

For all other financial instruments fair value is determined by using valuation techniques. Valuation techniques include net present value techniques, the discounted cash flow method, comparison to similar instruments for which market observable prices exist, and valuation models. The Bank use widely recognised valuation models for determining the fair value of common and more simple financial instruments like options and interest rate and currency swaps. For these financial instruments, inputs into models are market observable.

All non-trading financial liabilities, Loans and advances and held-to-maturity assets are measured at amortised cost less impairment losses. Amortised cost is calculated on the effective interest rate method. Premiums and discounts, including initial transaction costs, are included in the carrying amount of the related instrument and amortised based on the effective interest rate of the instrument.

Amortised 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 amortisation using the effective interest method of any difference between the initial amount recognised and the maturity amount, minus any reduction for impairment.

Gains and losses arising from a change in the fair value of available-for-sale assets and trading instruments are recognised in the equity reserve and income statement respectively.

(iii)Derecognition

A financial asset is derecognized when the Bank loses control over the contractual rights that comprise that asset. This occurs when the rights are realized, expire or are surrendered. A financial liability is derecognized when it is extinguished.

Available-for-sale assets and assets held for trading that are sold are derecognized and corresponding receivables from the buyer for the payment are recognised as of the date the Bank commits to sell the asset. The Bank uses the specific identification method to determine the gain or loss on derecognition. All gains and losses previously recognized directly in equity are recognized in profit and loss account.

Held to maturity instruments and loans and receivables are derecognized on the date they are transferred by the Bank.

(iv)Derivative instruments

Financial future contracts, forward rate agreements and interest rate swap agreements are stated at fair value. Fair values are obtained from quoted market prices and dealer price quotations. Gains and losses on fair value measurement are recognized in the income statement.

j) Impairment of non financial assets

The carrying amounts of the Bank's assets are reviewed at each balance sheet date to determine whether there is any indication of impairment. If such a condition exists, the assets' recoverable amount is estimated and an impairment loss recognised in the income statement whenever the carrying amount of an asset exceeds the recoverable amount.

k) Impairment losses on loans and advances

Loans and advances are recognised when cash is advanced to borrowers. Loans originated by the Bank by providing money to borrowers, other than those created with the intention of short term profit taking are classified as loans and receivables. These are carried at amortised cost, which is the present value of the expected future cash-flows, discounted at the instruments' original effective interest rate. Loan origination fees together with related direct costs are treated as part of the cost of the transaction.

Identification and measurement of impairment

At each balance sheet 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 that 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. All significant assets found not to be specifically impaired are then collectively assessed for any impairment that has been incurred but not yet identified. Assets that are not individually significant are then collectively assessed for impairment by grouping together financial assets (carried at amortised cost) with similar risk characteristics.

- objective evidence that financial assets (including equity securities) are impaired can include:
- significant financial difficulty of the issuer or obligor;
- a breach of contract, such as default or delinquency in interest or principal repayments;
- the Bank granting to the borrower, for economic or legal reasons relating to the borrower's financial difficulty, a concession that the lender would not otherwise consider;
- it becoming probable that the borrower will enter bankruptcy or other financial reorganization;
- the disappearance of an active market for that financial asset because of financial difficulties; or
- observable data indicating that there is a measurable decrease in the estimated future cash flows from a group of financial assets since the initial recognition of those assets, although the decrease cannot yet be identified with the individual financial assets in the group, including:

i.) adverse changes in the payment status of borrowers in the group; or
ii.) National or local economic conditions that correlate with defaults on the assets in the group.

In assessing collective impairment the Bank uses statistical modelling of historical trends of the probability of default, timing of recoveries and the amount of loss incurred, adjusted for management's judgement 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 modelling. Default rates, loss rates and the expected timing of future recoveries are regularly benchmarked against actual outcomes to ensure that they remain appropriate.

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

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

Loans and advances are shown at gross amount adjusted for any provision for impairment losses. A provision for loan impairment is established if there is objective evidence that the Bank will not be able to collect all amounts due according to the original contract terms of the loans. The amount of the provision is the difference between the carrying amount and the estimated recoverable amount. When a loan is deemed uncollectible, it is written off against the related provision for impairment. Subsequent recoveries are credited to the provision for loan losses in the profit and loss account.

l) Investment securities

Investment securities are initially measured at fair value plus incremental direct transaction costs and subsequently accounted for depending on their classification as either held-to-maturity, fair value through profit or loss, or available-for-sale.

Fair value through profit and loss

For Investment securities that are designated at fair value on initial recognition, their fair value changes are recognized immediately as a profit or loss.

Available-for-sale

Available-for-sale investments are non-derivative investments that are not designated as another category of financial assets. Unquoted equity securities whose fair value cannot be reliably measured are carried at cost. All other available-for-sale investments are carried at fair value.

m) Other assets receivable

Other assets receivable are stated at cost less impairment losses for amounts considered to be irrecoverable.

n) Other accounts payable

Other accounts payable are carried at cost, which is the fair value of the consideration to be paid in the future for goods and services received.

o) Fiduciary assets

Assets held in a fiduciary capacity are not treated as assets of the Bank on the balance sheet.

p) Offsetting

Financial assets and liabilities are only offset and the net amount reported in the balance sheet where there is a legally enforceable right to set off the recognised amounts and the Bank intends to either settle on a net basis, or realize the asset and settle the liability simultaneously.

Income and expenses are presented on a net basis when permitted by the accounting standard or for gains and losses arising from a group of similar transactions.

q) Borrowings

Borrowings are recognised initially at fair value, being their issue proceeds (fair value of consideration received) net of transaction costs incurred. Borrowings are subsequently stated at amortised cost; any difference between proceeds net of transaction costs and the redemption value is recognised in the income statement over the period of the borrowings using the effective interest method

Charges on borrowings are accrued when they are incurred.

r) Liquidity

The Bank maintains a minimum of 1.33 times coverage of designated liabilities for the coming twelve months in liquid assets. Designated liabilities include repayments of principal and interest, budgeted administrative and staff expenses for the year.

s) 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. Where the Bank expects a provision to be reimbursed, for example under an insurance contract, the reimbursement is recognised as a separate asset but only when the reimbursement is virtually certain.

t) Retirement obligations

The Bank operates a defined contribution retirement benefit scheme to which employees contribute 10% of their basic salary and the Bank contributes 10%, 12.5% or 15% of the employees' basic salary depending on his/her length of service.

The Bank also makes contributions to a statutory pension scheme, the National Social Security Fund (NSSF). This is a defined contribution scheme registered under the National Social Security Act. The Bank's obligations under the scheme are limited to specific contributions legislated from time to time and are currently 10% of the employees' gross salary for Uganda and Kenya Shillings 200 for Kenyan employees resident in Kenya.

The Bank's contributions to both schemes are charged to the profit and loss account in the year in which they are made.

Costs relating to early retirement are charged to the profit and loss account in the year in which they are incurred.

u) Cash and cash equivalents

For the purposes of the cash flow statement, cash and cash equivalents comprise of cash with Banks held as demand and time deposits with less than 90 days maturity from the balance sheet date.

v) Contingent liabilities

Letters of credit acceptances and guarantees are accounted for as Off Balance Sheet transactions and described as contingent liabilities. Estimation of the outcome and financial effect of contingent liabilities made by management based on the information available up to the date the financial statements are approved for issue by the directors. Any expected loss is charged to the profit and loss account.

w) Taxation

No provision is made for taxation as the Bank is exempt from income tax under Article 49 of the Bank's Charter.

x) New standards and interpretations not yet adopted

A number of new standards, amendments to standards and interpretations are not yet effective for the year ended 31 December 2007, and have not been applied in preparing these financial statements:

IFRIC 11 (IFRS 2) Group and Treasury Share Transactions
This interpretation is required to be applied for annual periods beginning on or after 1 March 2007 but is not expected to have a significant impact on the activities of the Bank.

IFRIC 12 Service Concession arrangements
This interpretation is required to be applied for annual periods beginning on or after 1 January 2008 but is not expected to have a significant impact on the activities of the Bank.

IFRS 8 Operating segments

This interpretation is required to be applied for annual periods beginning on or after 1 January 2009 but is not expected to have a significant impact on the activities of the Bank.

IAS 23 Revised Borrowing Costs

This interpretation is required to be applied for annual periods beginning on or after 1 January 2009 but is not expected to have a significant impact on the activities of the Bank.

IFRIC 13 Customer Loyalty Programmes

This interpretation is required to be applied for annual periods beginning on or after 1 July 2008 but is not expected to have a significant impact on the activities of the Bank.

IFRIC 14 (IAS 19) The limit on a Defined Benefits Asset, Minimum Funding Requirements and their Interaction

This interpretation is required to be applied for annual periods beginning on or after 1 January 2008 but is not expected to have a significant impact on the activities of the Bank.

y) Comparatives

Where necessary, comparative figures have been adjusted to conform to changes in presentation in the current year. In particular, interest income and impaired losses have been adjusted to take into account suspended interest on impaired loans and advances.

3. INTEREST INCOME

(a) Interest income on loans to project

	2007 USD '000	2006 USD '000
Interest income on unimpaired loans and advances measured at amortized cost	15,852	12,368
Interest income on impaired loans and advances measured at amortized cost	3,917	681
	19,769	**13,049**

(b) Interest income from lease rentals

	2007 USD '00 0	2006 USD '000
Interest income on unimpaired lease receivables measured at amortized cost	1,513	782
Interest income on impaired lease receivables measured at amortized cost	141	-
	1,654	**782**

(c) Interest from deposits

	2007 USD '000	2006 USD '000
Interest income from short term deposits	2,804	3,941
Interest income from long term deposits	359	-
	3,163	**3,941**

4. BOND ISSUE COSTS

	2007 USD '000	2006 USD '000
Amortization charge	31	226
Other bond issue costs	40	20
	71	**246**

These relate to costs incurred on issue of EADB bonds and are written off over the period of the bond.

5. NET GAIN /(LOSS) FROM FOREIGN EXCHANGE

	2007 USD '000	2006 USD '000
Exchange gain/(loss) on currency translations	372	(155)
Realised gain/(loss) on foreign exchange dealings	367	(9)
	739	**(164)**

6. OTHER INCOME

	2007 USD '000	2006 USD '000
Rent income	505	479
Gain on sale of property and equipment	-	738
Directors fees	11	19
Staff loans interest	31	37
Gain on sale of equity investments	2,772	480
Guarantee fees	-	68
Miscellaneous income	109	63
	3,428	**1,884**

7. STAFF AND ADMINISTRATION EXPENSES

	2007 USD '000	2006 USD '000
Salaries and wages	3,032	2,386
Pension and gratuity	350	303
Rent and housing allowance	183	244
Other staff costs	487	607
Staff duty travel	285	261
Directors expenses	157	175

Insurance	226	218
Advertising and publicity	91	64
Legal fees	57	4
Other administrative expenses	1,702	973
	6,570	**5,235**

8. (LOSS)/PROFIT BEFORE TAXATION

(Loss)/profit before taxation is stated after charging the following:

	2007 USD '000	2006 USD '000
Directors emoluments:		
- Fees and allowances	106	70
- Other expenses	51	105
Depreciation and amortization of intangible asset and grants	647	281
Auditors remuneration	33	30

9. TAXATION

In accordance with Article 49 of the Bank's Charter, the Bank is exempt from income tax. Therefore, no amounts for corporation and deferred tax have been provided for in the financial statements.

10. BASIC (LOSS)/EARNINGS PER SHARE

Basic (loss)/ earnings per share is calculated by dividing the net (loss)/profit for the year attributable to ordinary shareholders by the weighted average number of ordinary shares outstanding during the year.

	2007 USD '000	2006 USD '000
Net (loss)/profit attributable to ordinary shareholders	(8,855)	4,625
Weighted average number of ordinary shares in issue during the year	6,411	5,745
Basic (loss)/ earnings per share	(1.38)	0.81
Diluted (loss)/ earnings per share	(1.38)	0.81

There were no potentially dilutive shares/instruments outstanding as at 31 December 2007 and 2006.

11. CASH AND BANK BALANCES

	2007 USD '000	2006 USD '000
Commercial Bank of Africa	33	1,115
Standard Chartered Bank Uganda Limited	(103)	146
Stanbic Bank Uganda Limited	461	202
CRDB Bank Limited – Tanzania	3	2
Standard Chartered Bank London	3,554	501
Standard Chartered Bank Kenya Limited	800	(160)
Standard Chartered Bank-Tanzania Limited	8	247
Citibank Uganda Limited	104	45
Citibank – London	-	505
Citibank USA	1,496	-
The Hongkong and Shanghai Banking Corporation Limited (HSBC)	3,295	1,558
Cooperative Bank of Kenya	161	-
Others	-	25
	9,812	**4,186**

12. DEPOSITS DUE FROM BANKS

	2007 USD '000	2006 USD '000
Standard Chartered Bank London	-	5,268
Crown Agents Financial Services	4,099	3,065
Standard Chartered Bank Kenya Limited	257	3,170
Fortis Bank	10,760	13,313
Citibank – London	341	7,739
Citibank Uganda Limited	8,801	-
The Hongkong and Shanghai Banking Corporation Limited (HSBC)	9,188	12,100
Standard Chartered Bank Uganda	-	1,725
Barclays Bank Uganda Limited	11,103	6,709

Kenya Commercial Bank Limited	4,165	-
CFC Bank Limited	4,627	3,755
The Cooperative Bank of Kenya	7,000	7,000
	60,341	**63,844**

The above amount is analysed as follows:

	2007 USD '000	**2006 USD '000**
Amounts due within 3 months	53,341	56,844
Amounts due after 3 months	7,000	7,000
	60,341	**63,844**

The weighted average effective interest rates on deposits due from Banks was 4.8% (2006: 4.7%)

13. OTHER ASSETS RECEIVABLES

	2007 USD '000	**2006 USD '000**
Local debtors	495	1,816
Due from Government of Uganda	5,141	1,333
Due from Government of Kenya	3,000	3,000
Due (to)/ from Government of Tanzania	(120)	3,000
AfDB Information Technology grant receivable	501	553
Other receivables	446	313
Derivative asset arising from forward contract	111	235
Rent receivable	142	67
Payments in advance	-	98
Staff advances and loans	1,020	903
Un amortized bond issue costs	124	155
	10,860	**11,473**

14. LOANS AT AMORTISED COST

	Note	**2007 USD '000**	**2006 USD '000**
Loans to other Banks		14,012	15,920
Loans to other projects		204,664	177,152
Finance lease receivable		19,534	12,981
Gross loans		**238,210**	**206,053**
Impairment losses on loans and advances	14 (i)	(53,485)	(32,273)
		184,725	**173,780**

The weighted average effective interest rates on loans from Banks, loans to projects and finance lease receivable was 5.12%, 8.50% and 10.96% respectively.

(i) Impairment losses on loans

The movement in the allowance for impairment in respect of Loans and advances to customers during the year was as follows:

	2007 USD '000	**2006 USD '000**
At 1 January	32,273	21,477
Accrued impaired interest for prior years	-	12,377
Exchange loss/ rate movement	91	77
New provisions created	18,608	2,820
Impairment on suspended interest	3,917	681
Recoveries and provisions no longer required	(1,404)	(1,971)
Net increase in provisions	**21,121**	**1,530**
Bad debts written off during the year	-	(3,188)
At 31 December	**53,485**	**32,273**
Charge to profit and Loss account		
Net increase in provisions as above	21,121	1,530
Recovery of previously written off loans	(204)	-
Net charge to profit and loss	**20,917**	**1,530**

(ii) Distribution of investments, accrued interest and loan charges receivable by sector

	2007 USD '000	2006 USD '000
Agriculture and fisheries	4,728	3,035
Forestry and paper	5,089	3,734
Mining and quarrying	-	1,094
General industrial manufacturing	5,795	9,815
Consumer industrial manufacturing	7,587	14,138
Agro-marine food and processing	23,158	26,117
Construction, building materials and real estate	24,355	20,076
Hotel, tourism, leisure and entertainment	26,534	18,102
Transport and storage	18,695	6,302
Telecommunication services and information technology	11,881	15,561
Commercial banks	23,230	23,892
Investment companies	165	157
Micro finance institutions	2,326	3,924
Electricity and water	8,154	7,746
Oil and gas	94	-
Education, health and other community services	11,987	9,955
General trading (wholesale, retail and repairs)	10,947	10,132
	184,725	**173,780**

Commitments existed in respect of which disbursements had not been made. These commitments amounted to USD 18.19 million (2006-USD 30.90 million).

Loans advances to projects in which Directors have an interest	**15**	**73**

(iii) Analysis of finance leases

	2007 USD '000	2006 USD '000
Lease rentals within one year	7,144	3,686
Lease rentals after one year but before five years	12,390	9,295
Less Impairment losses	(1,480)	(541)
	18,054	**12,440**

15. EQUITY INVESTMENTS

	Currency	Equity amount '000	Impairment amount '000	Equity amount '000	2007 USD '000	2006 USD '000
Central Depository & Settlement Corporation	KES	5,000	-	5,000	80	72
Industrial Promotion Services	UGX	280,000	-	280,000	165	161
Nile Bank Limited	UGX	-	-	-	-	287
Plastic and Rubber Industries Limited	KES	536	-	536	9	8
Azania Bancorp Limited	TZS	550,000	-	550,000	486	437
Karen Hospital	KES	36,135	-	36,135	577	-
Pan Paper Mills	USD	76	(76)	-	-	-
Leather Industries Uganda	USD	175	(175)	-	-	-
Gaba Airport View Hotel Limited	UGX	400,000	-	400,000	236	-
Stanbic Bank Uganda Limited	UGX	27,715	-	16	16	-
New Forest Limited	USD	350	-	350	350	-
Total					**1,919**	**965**

16 OTHER INVESTMENTS

	2007 USD '000	2006 USD '000
Bonds	-	576
Preference shares in Crown Beverages Limited	787	767
Preference shares in Savings and Finance Limited	574	515
Investment Business Partners International (Kenyan SME Fund) Limited	352	-
Preference shares in Gulu Church Hill Courts Limited	205	-
	1,918	**1,858**

17. CAPITAL WORK-IN-PROGRESS

	2007 USD '000	2006 USD '000
Building work in progress	**255**	**-**

Capital work in progress relates to costs incurred in renovation and reconstruction of the conference centre at EADB headquarters as at 31 December 2007.

18. INTANGIBLE ASSETS

	2007 USD '000	2006 USD '000
Cost		
At 1 January	1,733	-
Reclassification from property and equipment	-	319
Transfer from work in progress	-	131
Additions	449	1,283
At 31 December	**2,182**	**1,733**
Amortization		
At 1 January	175	-
Reclassification from property and equipment	-	146
Charge for the year	497	29
At 31 December	672	175
Net book Value		
At 31 December	**1,510**	**1,558**

19. PROPERTY AND EQUIPMENT

	Land and buildings USD '000	Office equipment USD '000	Motor vehicles USD '000	Furniture and fittings USD '000	Total Cost USD '000
Cost					
At 1 January 2006	10,702	1,333	385	578	12,998
Additions	21	87	32	39	179
Reclassification to intangible assets	-	(319)	-	-	(319)
Disposals	(114)	(6)	(18)	-	(138)
31 December 2006	10,609	1,095	399	617	12,720
Additions	1	131	-	32	164
Disposals	-	-	-	-	-
At 31 December 2007	**10,610**	**1,226**	**399**	**649**	**12,884**
Depreciation					
At 1 January 2006	6,802	818	261	276	8,157
Reclassifications to intangible assets	-	(146)	-	-	(146)
Disposals	(88)	(5)	(18)	-	(111)
Charge for the year	71	80	45	56	252
At 31 December 2006	6,785	747	288	332	8,152
Disposals	-	-	-	-	-
Charge for the year	303	66	40	59	468
At 31 December 2007	**7,088**	**813**	**328**	**391**	**8,620**
Net book Value:					
At 31 December 2007	3,522	413	71	258	4,264
At 31 December 2006	3,824	348	111	285	4,568

The gross carrying value of fully depreciated property and equipment that are still in use is USD 5,709,102 (2006 – USD 5,487,335). Such assets would have attracted a notional depreciation of USD 457,525 (2006 – USD 274,367).

Leasehold land on which the Bank's buildings are built was donated by the respective governments free of charge. As such, no cost has been assigned to land component and all such land has been disclosed together with the cost of buildings.

As at 31 December 2007, there were no assets pledged by the Bank to secure liabilities.

20. DIVIDENDS PAYABLE

	2007 USD '000	2006 USD '000
Dividends payable	**35**	**35**

The balance above represents dividends due to class A members to be ploughed back as share capital. The amounts have not yet been converted to shares.

21. EADB BONDS AT AMORTISED COST

	Note	2007 USD '000	2006 USD '000
Uganda Shilling Medium Term Note	(i)	11,837	11,543
Kenya Shilling Long Term Note	(ii)	10,596	11,875
Tanzania Shilling Medium Term Note	(iii)	-	2,077
Tanzania Shilling Long Term Note	(iv)	11,943	11,963
		34,376	**37,458**
Maturity analysis of EADB bonds			
Amounts payable within one year		7,395	10,663
Amounts payable after one year and within five years		26,981	24,490
Amounts payable after five years		-	2,305
		34,376	**37,458**

(i) In December, 2005 the Bank issued Uganda Shilling floating rate bonds redeemable in ten equal installments starting June 2008 and ending in December, 2012. Interest is payable at a semi-annual interval at a rate determined by the most recent 182-day Bank of Uganda Treasury Bill rate plus 1% margin.

(ii) In August, 2004 the Bank issued Kenya Shilling bond under its Medium Term Notes. The Bonds are trading on the Nairobi Stock Exchange. Interest is payable semi-annually at a fixed rate of 7.50% pa.

(iii) The Bank issued Tanzania shilling floating rate bonds on the Tanzania market in January 2002. Interest is payable at a semi-annual interval at a rate determined by the most recent 182 day weighted average yield treasury bills issued by the Bank of Tanzania, plus 0.75% margin. The original capital was fully redeemed in January 2007.

(iv) In July, 2005 the Bank issued Tanzania shilling bonds redeemable in ten semi-annual installments after a grace period of 2 years. Interest is payable semi-annually at a fixed rate of 12.7% p.a.

22. OTHER ACCOUNTS PAYABLE

	2007 USD '000	2006 USD '000
Deposits on asset leasing	609	656
Pay As You Earn	402	392
Value Added Tax	(344)	(652)
Staff payables	22	49
Legal fees	-	131
Other creditors	850	730
Rent received in advance	17	27
	1,556	**1,333**

23. MEDIUM AND LONG-TERM BORROWINGS

	Currency	Equity amount '000	Impairment amount '000	Equity amount '000	2007 USD '000	2006 USD '000
AfDB V/VI/VII	USD	46,012	1,174	47,186	47,186	47,191
AfDB V/VI	EUR	1,113	44	1,157	1,703	1,966
DEG	EUR	2,383	76	2,459	3,620	5,644
EIB GPE (BOU)	UGX	31,298,273	-	31,298,273	18,451	17,483
EIB GPE (BOU)	USD	537	-	537	537	730
EIB Facility (CBK)	KES	48,034	322	48,356	772	1,045
EIB GBPE (BOT)	EUR	500	(8)	492	724	1,002
Sida	SEK	32,750	-	32,750	5,064	5,857
FMO, Euro	EUR	908	21	928	1,366	2,441
EXIM BANK-India	USD	262	13	275	275	1,116
OPEC	USD	3,636	121	3,757	3,757	5,636
NDF	EUR	10,022	8	10,030	14,766	14,182
Standard Chartered Bank, Kenya Limited	KES	1,000,000	3,186	1,003,186	16,006	9,842
Cooperative Bank of Kenya Limited	KES	500,000	-	500,000	7,978	7,211
DBSA, South Africa	USD	14,895	555	15,450	15,450	66
					137,655	**121,412**

Maturity analysis of long and medium term loans		
Amounts payable within one year	23,682	14,103
Amounts payable after one year but within five years	67,090	56,877
Amounts payable after five years	46,883	50,432
	137,655	**121,412**

All lines of credit are secured by the callable shares. The weighted average effective interest rate on medium and long term loans was 6.9% (2006: 6.3%).

24. SPECIAL FUNDS

	Norwegian EADB fund for rehabilitation USD '000	DANIDA/EADB funds for rehabilitation of Uganda industries USD '000	SIDA/EADB funds for rehabilitation USD '000	SIDA/EADB venture capital fund USD '000	Total USD '000
31 December 2007	2,404	5,045	4,222	2,170	13,841
31 December 2006	2,404	5,045	4,222	2,170	13,841

a) The Norwegian/EADB fund for rehabilitation in Uganda represents a grant of NOK 30 million from the Norwegian Government. The fund revolved twice as per the grant agreement and subsequently reverted to EADB.

b) The DANIDA/EADB fund represents a grant of DKK 49 million *(USD 7.941 million) for the rehabilitation of industries in Uganda. Part of the DANIDA funds amounting to *USD 0.948 million was converted to share capital in 1996. In 1998 funds amounting to *USD 2.163 million from DANIDA funds were converted into share capital on behalf of the three member states in equal amounts. All DANIDA shares in Class B have been transferred to Member States under Class A. This is in accordance with conditions contained in the Danish Grant agreements with EADB, on disbursement of funds.

c) The SIDA/EADB fund represents a grant of SEK 20 million (*USD 2.724 million) for the rehabilitation of Uganda industries.

d) The SIDA/BOU venture capital fund represents funds received for equity investments.

25. GRANTS

	Note	2007 USD '000	2006 USD '000
African Development Bank (AfDB)	(i)	953	1,271
Housing finance feasibility study grant	(ii)	150	-
		1,103	**1,271**

(i) This represents funds received from AfDB for acquisition of a new computer Information System under a non-repayable grant agreement signed in 2005 for USD 1.36 million. The amount is not repayable. The grant is being amortized over the useful life of the information system of four years.

(ii)This represents funds received from the Government of Tanzania to fund the housing finance feasibility study.

26. CAPITAL FUND

	2007 USD '000	2006 USD '000
Norwegian Government	7,479	7,479

This represents funds received from the Norwegian Government, in 1982 and 1987 amounting to SDR 7.1 million from which SDR 2.2 million was utilized for the allocation of fully paid shares to the Governments of Kenya, Tanzania and Uganda in 1988. The balance of USD 7.5 million equivalent is interest free and is not repayable by the Bank.

27. ADVANCE SHARE CAPITAL CONTRIBUTION

	2007 USD '000	2006 USD '000
Government of Tanzania	16	13
Government of Kenya	12	9
Government of Uganda	12	9
	40	**31**

In their annual meeting in 2002 and 2003, the Governing Council approved increase of paid up share capital of the Bank. The three Member States of Uganda, Kenya and Tanzania were to inject USD 45m into the Bank with payments spread over five years starting from 2004. The amount is to be paid in installments of USD 3m per shareholder Member State annually which entitles a Member State to 222 shares at nominal value of USD 13,500. Thus the balance of USD 40,000 (2006: USD 31,000) as at 31 December 2007 was classified as advance share capital contribution in accordance with the Bank's Charter.

28. SHARE CAPITAL

a) Authorised share capital under Article 3 of the Charter

	Number of shares				Value per share	Total value
	Paid in shares	Callable shares	Unsubscribed shares	Total	USD	USD '000
At 1 January 2007						
Class A shares	4,704	23,520	43,776	72,000	13,500	972,000
Class B shares	1,041	-	6,959	8,000	13,500	108,000
	5,745	**23,520**	**50,735**	**80,000**	**-**	**1,080,000**
Increase in share capital:						
Class A	-	-	-	-	-	-
Class B	-	-	-	-	-	-
Transfer to Class A shares	666	3,330	(3,996)	-	-	-
At 31 December 2007	**6,411**	**26,850**	**46,739**	**80,000**	**-**	**1,080,000**
Analysed as follows:						
Class A shares	5,370	26,850	39,780	72,000	13,500	972,000
Class B shares	1,041	-	6,959	8,000	13,500	108,000
	6,411	**26,850**	**46,739**	**80,000**	**-**	**1,080,000**

b) Issued and fully paid share capital

	Number of shares			Value per share	Total value
	Paid in shares	Callable shares	Total	USD	USD '000
At 1 January 2007					
Class A shares	4,704	-	4,704	13,500	63,504
Class B shares	1,041	-	1,041	13,500	14,054
	5,745	**-**	**5,745**	**13,500**	**77,558**
Class A, issued and fully paid during the year	666	-	666	13,500	8,991
At 31 December 2007	6,411	-	6,411	13,500	86,549
Class A shares	5,370	-	5,370	13,500	72,495
Class B shares	1,041	-	1,041	13,500	14,054
	6,411	-	6,411	13,500	86,549

Payment of dividends to members is made to subscribers of Class B shares in proportion to the number of shares held by such members. Dividends to Class A shares are paid in proportion to the number of shares held by each member but only after Class B dividend is paid.

The voting power of each member during annual and general meetings of the Bank is equal to the number of shares of the paid-in-capital stock of the Bank held by that member.

29. FAIR VALUE ADJUSTMENT RESERVE

	2007 USD '000	2006 USD '000
Equity investment-quoted	11	-

This relates to fair value adjustment on Stanbic Bank Uganda Limited equity investments which are classified as available for sale and measured at fair value.

30. SPECIAL RESERVE

	2007 USD '000	2006 USD '000
At 1 January	8,474	7,176
Transfer of commission and guarantee fees from profit and loss account	882	1,298
	9,356	**8,474**

The transfer to the special reserve is made in accordance with Article 17 of the Bank's Charter, the reserve being credited with commissions earned. The special reserve is to enable the Bank meet its liabilities on borrowings or guarantees chargeable. The reserve is not available for distribution.

31. CASH AND CASH EQUIVALENTS

Cash and cash equivalents included in the cash flow statement comprise the following balance sheet amounts:

	Note	2007 USD '000	2006 USD '000
Net balances with banks	11	9812	4,186
Balances due from banks within 3 months	12	53,341	56,844
		63,153	**61,030**

32. USE OF ESTIMATES AND JUDGEMENTS

The Bank makes estimates and assumptions that affect the reported amounts of assets and liabilities within the next financial year. Estimates and judgments are continually evaluated and are based on historical experience and other factors, including expectations of future events that are believed to be reasonable under the circumstances.

The Bank regularly reviews its assets and makes judgments in determining whether an impairment loss should be recognized in respect of observable data that may impact on future estimated cash flows. The methodology and assumptions used for estimating both the amount and timing of future cash flows are reviewed regularly to reduce any differences between loss estimates and actual loss experience.

Impairment losses on loans and advances

The specific counterparty component of the total allowances for impairment applies to claims evaluated individually for impairment and is based upon management's best estimate of the present value of the cash flows that are expected to be received. In estimating these cash flows, management makes judgments about counterparty's financial situation and the net realizable value of any underlying collateral. Each impaired asset is assessed on its merits, and the workout strategy and estimate of cash flows considered recoverable are independently reviewed by the Credit Risk function.

Collectively assessed impairment allowances cover credit losses inherent in portfolios of claims with similar economic characteristics when there is objective evidence to suggest that they contain impaired claims, but the individual impaired items cannot yet be identified. In assessing the need for collective loan loss allowances, management considers factors such as credit quality, portfolio size, concentrations, and economic factors. In order to estimate the required allowance, assumptions are made to define the way inherent losses are modelled and to determine the required input parameters, based on historical experience and current economic conditions. The accuracy of the allowances depends on how well the estimated future cash flows for specific counterparty allowances and the model assumptions and parameters used in determining collective allowances.

Determining fair values

The determination of fair value for financial assets and liabilities for which there is no observable market price requires the use of valuation techniques. For financial instruments that trade infrequently and have little price transparency, fair value is less objective, and requires varying degrees of judgment depending on liquidity, concentration, uncertainty of market factors, pricing assumptions and other risks affecting the specific instrument.

33. FINANCIAL RISK MANAGEMENT

(a) Introduction and overview

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

- Credit risk;
- Liquidity risk; and
- Market risk

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.

Risk management framework

The Bank's board of directors has overall responsibility for the establishment and oversight of the Bank's risk management framework. The board has established the Asset and Liability Committee (ALCO), Project Committee and the Risk Management Department which are responsible for developing and monitoring the risk management policies in their specified areas. The Board Audit Committee has both executive and non executive members and report regularly to the Board of Directors on their activities.

The Bank's risk management policies are 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 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 Audit Committee is assisted in these functions by Internal Audit. Internal Audit undertakes both regular and adhoc reviews of risk management controls and procedures,the results of which are reported to the Audit Committee.

(b) Credit risk

Credit risk is the risk of financial loss to the Bank if a customer or counterparty to a financial instrument fails to meet its contractual obligations, and arises principally from the Bank's loans and advances to ustomers, other Banks and investment securities. For risk management reporting purposes, the Bank considers all elements of credit risk exposure such as individual obligator default risk and sector risk.

In the normal course of its business, the Bank incurs credit risk from financial institutions and advances to customers. The credit risk exposure is, however, managed through constant monitoring of the status of financial institutions where deposits are maintained. As a policy the Bank places its deposits with internationally well rated financial institutions. Credit risk is also minimized by the Bank's policy of diversification. The Bank does not invest in a single project more than 50% of the project's net worth and this would not exceed 15% of the Bank's net worth. The Bank also endeavors to maintain a well-balanced loan portfolio distributed prudently among the sectors of the economy falling within its target activities. The Bank's total exposure to a single sector should not exceed 20% of the total investment portfolio save for telecommunications and energy sectors at 30%. The Bank also limits the total outstanding loans to at three times the aggregate of the unimpaired subscribed capital, reserves and surplus of the Bank.

Management of credit risk

The Board of Directors has partly delegated responsibility for the management of credit risk to its project committee for credit exposures below USD 1 million. The Board is involved directly for loan exposure above USD 1 million and any equity investments above USD 700,000. The management committee is responsible for oversight of the Bank's credit risk, including, formulating credit policies, covering collateral requirements and credit assessments, risk grading and reporting. Documentary, legal procedures and compliance with regulatory and statutory requirements is done in consultation with the Bank's Legal and Compliance department, establishing the authorization structure for the approval and renewal of credit facilities with concurrence of the board of directors, reviewing and assessing credit risk. The Bank assesses all credit exposures, prior to facilities being committed to customers by the Operations Department and Risk Department. Renewals and reviews of facilities are subject to the same review process, limiting concentrations of exposure to counterparties, products and industries (for loans and advances). New loan project requests are subject to Bank's risk grading in order to ensure that only viable projects are taken into the books.

The current risk grading framework consists of nine grades reflecting the varying degrees of projects viability, with the first five grades being desirable.

The Bank also has a Credit Administration Manager who is responsible for monitoring the credit quality of loans and ensuring appropriate corrective action is taken. The credit administration also provides advice, guidance and specialist skills to Operations Department to promote best practice in the management of credit risk.

The Credit Administration Manager prepares regular reports for Management and the Board's consideration on the performance of the loan portfolio.

The Operations Departments is required to implement the Bank's credit policies and procedures, and ensure that credit approval authorities delegated from the Bank's Project Committee are observed. The Operations Department is responsible for the quality and performance of its credit portfolio and for monitoring and controlling all credit risks in its portfolio, including those subject to Board approval.The regular audits of Operations Department and the Bank's credit processes are undertaken by Internal Audit.

Exposure to credit risks

	Loans and advances to projects		Loans and advances to banks	
	2007 USD '000	2006 USD '000	2007 USD '000	2006 USD '000
Carrying amount				
Individually impaired:	61,229	38,374	-	-
Allowance for impairment	(51,165)	(30,600)	-	-
Carrying amount	10,064	7,774	-	-
Collectively Impaired:				
Allowance for impairment	(2,320)	(1,673)	-	-
Past due but not impaired:				
Carrying amount	26,140	24,188	-	-
Past due comprises:				
Watch (0 to 60 days)	907	5,386	-	-
Substandard (61 to 180) days	3,999	11,522	-	-
Doubtful (181 to 365) days	21,234	7,280	-	-
Carrying amount	26,140	24,188	-	-
Neither past due nor impaired:				
Carrying amount	136,829	127,571	14,012	15,920
Total carrying amount	**170,713**	**157,860**	**14,012**	**15,920**

Impaired loans and advances

Impaired loans and advances are those 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 internally classified as loss accounts.

Past due but not impaired loans and advances

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. These loans are internally classified as watch, when the account is 61 days in arrears, substandard if the account is between 91 and 181 days in arrears for accounts with monthly and other terms of payment and doubtful for loans between 181 and 360 days in arrears.

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 for monitoring purposes independent of satisfactory performance after restructuring, for at least two scheduled payments as a way of demonstrating positive performance.

Allowances for impairment

The Bank establishes an allowance for impairment losses that represents its estimate of incurred losses in its loan portfolio taking to account prudential guidelines of International Financial Reporting Standards (IFRS). The main components of this allowance are a specific loss component that relates to individually significant exposures and a collective loan loss allowance established for groups of homogeneous assets in respect of losses that have been incurred on a collective basis.

Write off policy

The Bank writes off a loan balance and any related allowances for impairment losses when the Bank's Project committee determines that the loans are uncollectible. This determination is reached after considering information such as the occurrence of significant changes in the borrower's financial position such that the borrower can no longer pay the obligation, or that the proceeds from collateral will not be sufficient to pay back the entire exposure. All loans write off are approved by the Board of Directors.

The Bank holds collateral against loans and advances to customers in the form of mortgage interest over property. Estimates of fair value are based on the value of the collateral assessed at the time of borrowing, and generally are not updated except when a loan is individually assessed as impaired. Collateral generally is not held over loans and advances to Banks.

An estimate of fair value of collateral and other security enhancements held against financial assets is shown below:

	2007 **USD '000**
Legal mortgage over individually impaired assets	90,426
Legal mortgage held over other loans and advances to customers	199,882
	290,308

The Bank maintains a minimum of 1.5 times collateral value against the committed loan amount.

Settlement risk

The Bank's activities may give rise to risk at the time of settlement of transactions and trades. Settlement risk is the risk of loss due to the failure of a company to honour its obligations to deliver cash, securities or other assets as contractually agreed. Settlement limits form part of the credit approval/limit monitoring process described earlier.

(c) Liquidity risk

Liquidity risk is the risk that the Bank will encounter difficulty in meeting obligations on its financial liabilities. It includes both the risk of being unable to fund assets at appropriate maturities and rates and the risk of being unable to liquidate an asset at a reasonable price and in an appropriate time frame.

Management of liquidity risk

The Bank has access to a diverse funding base. Funds are raised mainly from borrowings and share capital. This enhances funding flexibility, limits dependence on any one source of funds and generally lowers the cost of funds. The Bank strives to maintain a balance between continuity of funding and flexibility through the use of liabilities with a range of maturities. The Bank continually assesses liquidity risk by identifying and monitoring changes in funding required in meeting business goals and targets set in terms of the overall Bank strategy. In addition, the Bank has an Asset and Liability Committee that meet on a regular basis to monitor liquidity risk, review and approve liquidity policies and procedures.

Exposure to Liquidity risk

The Bank maintains a liquidity policy of 1.33 times the designated liabilities for the next twelve months. Designated liabilities consist of liabilities and budgeted commitments that are due in the twelve months.

Details of the liquidity policy ratio as at the end of the year is as follows:

	2007 USD '000	2006 USD '000
Cash and cash equivalents as per liquidity policy	70,153	68,030
Designated liabilities	50,487	41,793
Surplus per liquidity policy	19,666	26,237
Liquidity ratio	**1.39**	**1.63**
Designated liabilities		
Redemption of bonds	7,395	10,101
Repayment of term loans	21,255	12,328
Interest on borrowings	12,961	12,312
Budgeted acquisition of fixed assets	884	783
Budgeted staff and administration expenses	7,992	6,269
Total	**50,487**	**41,793**

The liquidity policy of the bank defines cash and cash equivalent as operational and strategic liquidity pool.

The Bank registered a liquidity ratio of 1.39 (2006: 1.63) which is above the required liquidity ratio as per the policy of 1.33%.

The table below analyses assets and liabilities into relevant maturity groupings based on the remaining period at 31 December 2007 to the contractual maturity date.

Matured	<6 Months	>6 Months	>1 Year	>3Years	>5Years	>7 Years		
			<1 Year	<3 Years	<5 Years	<7 Years		Total
	USD '000	USD '000	USD '000	USD '000	USD '000	USD '000	USD '000	USD '000
Assets								
Cash and bank balances	9,812	-	-	-	-	-	-	**9,812**
Deposits due from banks	1,817	51,524	-	-	7,000	-	-	**60,341**
Loans to Banks	-	200	1,381	4,143	5,525	2,763	-	**14,012**
Other current assets	10,350	386	-	-	-	-	124	**10,860**
Loans and advances to project loans	4,243	9,486	19,123	67,348	44,278	22,390	3,845	**170,713**
Investments in equity	-	-	-	-	-	-	1,919	**1,919**
Other investments	-	-	-	-	-	-	1,918	**1,918**
Capital work in progress	-	-	-	-	-	-	255	**255**
Intangible assets	-	-	-	-	-	-	1,510	**1,510**
Property and equipment	-	-	-	-	-	-	4,264	**4,264**
Total assets	**26,222**	**61,596**	**20,504**	**71,491**	**56,803**	**25,153**	**13,835**	**275,604**
Liabilities								
Dividends	35	-	-	-	-	-	-	**35**
Sundry accounts payable	1,556	-	-	-	-	-	-	**1,556**
Bonds	-	3,835	3,560	9,328	9,328	5,794	2,531	**34,376**
Medium and long term loans	-	9,242	12,013	28,479	21,858	23,281	18,815	**113,688**
Loans from Banks	-	34	2,393	7,180	9,573	4,787	-	**23,967**
Special funds	-	-	-	-	-	-	13,841	**13,841**
Grants	-	-	-	-	-	-	1,103	**1,103**
Capital funds	-	-	-	-	-	-	7,479	**7,479**
Share capital funds in advance	-	-	-	-	-	-	40	**40**
Shareholders' funds	-	-	-	-	-	-	79,519	**79,519**
Total liabilities	**1,591**	**13,111**	**17,966**	**44,987**	**40,759**	**33,862**	**123,328**	**275,604**
Net liquidity gap at 31 Dec 2007	24,631	48,485	2,538	26,504	16,044	(8,709)	(109,493)	**-**
Net liquidity gap at 31 Dec 2006	27,190	58,813	7,522	19,388	11,352	(3,305)	(120,960)	**-**

The matching and controlled mismatching of the maturities and interest rates of assets and liabilities is fundamental to the management of the Bank. It is unusual for Banks ever to be completely matched since business transacted is often of uncertain terms and of different types. An unmatched position potentially enhances profitability but can also increase the risk of losses. The maturities of assets and liabilities and the ability to replace at an acceptable cost, interest bearing liabilities as they mature, are important factors in assessing the liquidity of the Bank and its exposure to changes in interest rates and exchange rates.

(d) Market risk

Market risk is the risk that changes in market prices, such as interest rate and foreign exchange rates 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 the acceptable parameters, while optimising the return on risk.

Management of market risks

Overall authority for market risk is vested in Asset and Liability Committee (ALCO). ALCO is responsible for the development of detailed risk management policies and for the day to day review of their implementation.

Interest rate risk

In broad terms the interest rate risk is the risk that concerns the sensitivity of the Bank's financial performance to changes in the interest rates. The Bank's operations are subject to the risk of interest rate fluctuations to the extent that interest earning assets and interest bearing liabilities mature or reprice at different times or in differing amounts. Risk management activities are aimed at optimizing net interest income, given market interest rates levels consistent with the Bank's business strategies. In order to minimize interest risk, the Bank has a policy where the approved lending commitments are matched to specific lines of credit or source of funds, including adopting the funding interest rate characteristics (fixed or variable) to its on lending activities.

The following table summarizes the exposure to interest rate risks. Included in the table are the Bank's assets and liabilities at carrying amounts, categorized by the earlier of contractual re-pricing or maturity dates. The Bank does not bear an interest rate risk on off balance sheet items.

INTEREST RATE RISK

	Up to 1 month USD '000	1 to 3 months USD '000	3 to 6 months USD '000	6 to 12 months USD '000	1 to 5 years USD '000	Over 5 years USD '000	Non-interest bearing USD '000	Total USD '000
Assets								
Cash and bank balances	9,812	-	-	-	-	-	-	9,812
Deposits due from banks	32,173	28,168	-	-	-	-	-	60,341
Loans to Banks	-	13,812	-	-	-	-	200	14,012
Loans and advances to customers	9,867	146,766	5,428	1,355	7,297	-	-	170,713
Other current assets	-	-	-	-	-	-	10,860	10,860
Investments in equity	-	-	-	-	-	-	1,919	1,919
Other investments	-	-	-	-	-	-	1,918	1,918
Capital work in progress	-	-	-	-	-	-	255	255
Intangible asset	-	-	-	-	-	-	1,510	1,510
Property & equipment	-	-	-	-	-	-	4,264	4,264
Total assets	**51,852**	**188,746**	**5,428**	**1,355**	**7,297**	**-**	**20,926**	**275,604**
Liabilities								
Dividends	-	-	-	-	-	-	35	35
Sundry accounts payable							1,556	1,556
Bonds	-	-	11,790	-	10,386	11,925	275	34,376
Term loans	66,746	1,791	14,758	-	7,227	21,075	2,091	113,688
Loans from other Banks	-	23,933	-	-	-	-	34	23,967
Capital funds	-	-	-	-	-	-	7,479	7,479
Special funds	-	-	-	-	-	-	13,841	13,841
Technical grants	-	-	-	-	-	-	1,103	1,103
Share capital contribution in advance	-	-	-	-	-	-	40	40
Shareholders' funds	-	-	-	-	-	-	79,519	79,519
Total liabilities	**66,746**	**25,724**	**26,548**	**-**	**17,613**	**33,000**	**105,973**	**275,604**
Interest sensitivity gap at 31 Dece 2007	**(14,894)**	**163,022**	**(21,120)**	**1,355**	**(10,316)**	**(33,000)**	**(85,047)**	**-**
Interest sensitivity gap at 31 Dec 2006	**(23,823)**	**125,409**	**(13,552)**	**2,543**	**787**	**(10,842)**	**(80,522)**	**-**

Exchange rate risk

Exchange risk arises from a mismatch between the value of the assets and that of capital and liabilities denominated in foreign currency. The Bank does not actively engage in dealing and trading operations in currencies and so the Bank's exposure mainly involves assets, liabilities and off balance sheet items denominated in foreign currency. To minimize exchange rate risk in a multi currency environment, the Bank matches it's borrowing in one currency with its assets in the currency.

Currency risk

The Bank is exposed to currency risk through transactions in foreign currencies. The Bank's transactional exposures give rise to foreign currency gains and losses that are recognized in the income statement. In respect of monetary assets and liabilities in foreign currencies, the Bank ensures that its net exposure is kept to an acceptable level by buying and selling foreign currencies at spot rates when considered appropriate. The Bank had the following significant currency positions at year end.

	EUR	USD	GBP	UGX	KES	SDR	TZS	Others	USD'000
Assets									
Cash at bank	1,153	8,120	52	(488)	413	-	9	553	9,812
Deposits from banks	18,732	39,119	76	-	2,414	-	-	-	60,341
Other current assets	-	10,359	284	187	30	-	-	-	10,860
Finance lease receivable	247	10,764	-	2,776	4,298	-	-	-	18,085
Loans to projects	1,551	78,189	-	30,820	29,899	-	12,169	-	152,628
Investments in loans to other Banks	-	14,012	-	-	-	-	-	-	14,012
Equity investments	-	350	-	420	664	-	485	-	1,919
Other investments	-	351	-	993	-	-	574	-	1,918
Capital work in progress	-	255	-	-	-	-	-	-	255
Fixed assets	-	4,264	-	-	-	-	-	-	4,264
Intangible assets	-	1,510	-	-	-	-	-	-	1,510
Total assets	**21,683**	**167,293**	**412**	**34,708**	**37,718**	**-**	**13,237**	**553**	**275,604**
Liabilities									
Dividends payable	-	(35)	-	-	-	-	-	-	(35)
EADB Bond	-	-	-	(11,837)	(10,596)	-	(11,943)	-	(34,376)
Sundry accounts payable	-	(930)	-	(337)	(119)	-	(170)	-	(1,556)
Medium and long – term loan	(22,179)	(67,206)	-	(18,451)	(24,755)	-	-	(5,064)	(137,655)
Special Funds	-	(13,841)	-	-	-	-	-	-	(13,841)
Technical grants	-	(1,103)	-	-	-	-	-	-	(1,103)
Capital funds	-	(7,479)	-	-	-	-	-	-	(7,479)
Share capital funds in advance	-	(40)	-	-	-	-	-	-	(40)
Share holder's funds	-	(79,519)	-	-	-	-	-	-	(79,519)
Total liabilities	**(22,179)**	**(170,153)**	**-**	**(30,625)**	**(35,470)**	**-**	**(12,113)**	**(5,064)**	**(275,604)**
Net Currency Position 31 Dec 2007	**(496)**	**(2,860)**	**412**	**4,083**	**2,248**	**-**	**1,124**	**(4,511)**	**-**
Net Currency Position 31 Dec 2006	**(1,691)**	**(795)**	**155**	**3,046**	**680**	**7**	**1,313**	**(2,715)**	**-**

34. EMPLOYEE RETIREMENT BENEFIT PLAN

	Note	2007 USD '000	2006 USD '000
Contribution to the retirement benefit plan	(i)	350	303
Contribution to the statutory pension scheme (NSSF)	(ii)	6	1
		356	**304**

(i) The Bank operates a defined contribution retirement benefit scheme to which employees contribute 10% of their basic salary and the Bank contributes 10%, 12.5% or 15% of the employees' basic salary depending on his/her length of service. A Board of Trustees manages the scheme and Crown Agents Asset Management Ltd invested the funds on its behalf until December 2006 when they were transferred to Stanbic Investment Management Services. An amount of USD 292,228 (2006: 254,858) has been charged in the 2007 profit and loss account in respect of the Bank's contributions.

(ii) The Bank also makes contributions to a statutory pension scheme, the National Social Security Fund. The contributions and obligations under the scheme are limited to specific contributions legislated from time to time and the Bank's contribution is currently 10% of the employees' gross salary and Kenya Shillings 200 for Kenyan employees resident in Kenya.

Other staff benefits

The Bank ensures proper welfare of its staff by providing welfare schemes such as car loan purchase scheme, educational assistance, housing and medical schemes.

Under the housing scheme, the Bank set aside a revolving fund amounting to USD 1.36 million for this purpose. A general purpose loan scheme is also availed to staff that qualify for it.

The Bank pays for professional membership and subscription fees for staff that belong to professional bodies.

Employees are eligible for a car loan up to two years' basic salary, less the employee's contribution, where applicable.

The Bank operates a medical insurance scheme which covers Bank employees appointed either on permanent, contract, consultancy, or trainee terms, including spouses and children.

35. CAPITAL COMMITMENTS

	2007	2006
Authorized but not contracted for	804	114
Authorized and contracted for	106	-
	910	**114**

36. OFF BALANCE SHEET ITEMS AND CONTIGENTS

The Bank conducts business involving guarantees, performance bonds and indemnities. The following are the commitments and contingencies outstanding as at year-end.

	Note	2007 USD '000	2006 USD '000
Letters of credit	(a)	6,9539,	212
Bank guarantees	(b)	13	13
Un-disbursed commitments	(c)	18,193	30,896
		25,159	**40,121**

Nature of contingent liabilities

(a) Letters of credit commit the Bank to make payments to suppliers of equipment to approved projects, on production of shipping documents.

(b) Bank guarantees are mainly written by the Bank to support performance by a staff to third parties. The Bank will only be required to meet these obligations in the event of the staff's default.

(c) Commitments to lend are agreements to lend to a customer in future subject to certain conditions. Such commitments are normally made for a fixed period.

Other contingent liabilities – Litigation

(i) The Bank is involved in a court case in Tanzania challenging an Arbitral Award of USD 61 million against it. The case has been ongoing since 1994. Following this award, the Bank in November 2006 applied for an interim stay of execution of the award. That application is yet to be heard. The Bank then filed a petition to set aside the Award. The petition was dismissed by the High court in June 2007 on the grounds of limitation. The Bank has subsequently filed an application to the High Court for extension of the limitation period to enable the Bank file a new petition to set aside the Award. The application has been set for hearing on 9 July, 2008. In the event the application is not granted at the High Court, the Bank still has a right of appeal to the Court of Appeal. The Directors have received a legal advice which indicates that the Bank has sufficient grounds to set aside the Arbitral Award provided the obstacle of limitation is overcome.

There are several applications pending before the Court in Tanzania contesting the legal costs due to the Decree Holder in various miscellaneous applications arising out of the above case.

Meanwhile, the assets of the Bank in Tanzania are by virtue of the East African Development Act 1984 (as amended by the Finance Act 2005) fully protected from any form of execution before the delivery of a final judgment against the Bank by the Court of Appeal as final appellate court.

(ii) The Bank has made a claim against an insurance company for approximately USD 572,400, with interest from February, 2002, for breach under a performance bond issued by it for the delivery of motor vehicles by one of its clients. The suit is to be heard on 10 November, 2008. The case has good prospects of success; however, the potential liability in costs from a loss would amount to USD 32,260. Meanwhile, the Bank has appealed against the decision to join a third party as co-defendant in the suit and the appeal is yet to be fixed for hearing.

(iii) The Bank has filed a claim for USD 3.5 million against the guarantors of a former customer following the failure by the customer to pay, and the sale of the customers assets having failed to realize the full debt due to the Bank. The hearing of the case is pending before the courts.

(iv) The Bank is involved in a case where one of the creditors of its former customer has filed a suit challenging the Bank's security and prayed for an injunction restraining the Bank from realizing the security. The hearing of the Plaintiff's application for injunction has been fixed for 17 June, 2008. The parties are pursing a settlement out of court.

v). As at 31 December, 2007, the Bank was involved in a case where a former client and its guarantors sued the Bank for a declaration that the guarantees issued to secure the financing had been frustrated and therefore the Bank should not charge interest on the loan, and for further orders that an injunction be issued against the Bank restraining it from realizing the securities held. The case has been fixed for hearing on 6 June, 2008

37. RELATED PARTY TRANSACTIONS

	2007 USD '000	2006 USD '000
Staff loans and advances	1,002	903
Loans advanced to projects in which directors have an interest	15	73
Bank balances held with banks that are shareholders of the Bank and related banks.	15,753	18,924
Long and medium term loans advanced to the Bank by shareholders.	**48,890**	**55,541**

No provision has been made for any loans to related parties. Loans to employees are given at concessionary rates while those to directors and to projects where directors have an interest are at market rates.

38. POST BALANCE SHEET EVENTS

The directors are not aware of post balance sheet events that require disclosure or adjustment to the financial statements as at the date of this report.

39. EMPLOYEES

The number of permanent employees of the Bank at the year-end was 76 (2006: 78).

40. INCORPORATION

The Bank was created under the Treaty for the East African Co-operation of 1967, which was amended and re-enacted as a Bank Charter in 1980.

41. CURRENCY

These financial statements are expressed in Unites States Dollars (USD)

Annexes

Annex A: EADB Share Capital Subscription 2007

	SUBSCRIPTION				
	CALLABLE				
Members	Paid in No	Amount	Paid-up	No. of	Amount
	of Shares	USD '000	Capital	Shares	USD '000
CLASS A					
Kenya Government	1790	24,165	27.92%	8950	120825
Tanzania Government	1790	24,165	27.92%	8950	120825
Uganda Government	1790	24,165	27.92%	8950	120825
TOTAL CLASS A	**5370**	**72,495**	**83.76%**	**26850**	**362475**
CLASS B					
African Development Bank	500	6,750	7.80%		
FMO - Netherlands	375	5,062.50	5.85%		
DEG - Germany	100	1,350	1.60%		
Consortium of Yugoslav Institutions	28	378	0.44%		
SBIC - Africa Holdings	24	324	0.37%		
Commercial Bank of Africa, Nairobi	5	67.5	0.07%		
Nordea Bank Sweden, AB (publ)	2	67.5	0.07%		
Standard Chartered Bank, London	2	27	0.02%		
Barclays Bank PLC, London	2	27	0.02%		
Total Subscribed	1,041	14,053.50	16.24%		
Unsubscribed	6,959	93,946.50			
TOTAL CLASS B	**8,000**	**108,000**			
AUTHORISED CAPITAL STOCK (USD '000)					
Total Class A					
1. Subscribed & paid in	72,495				
2. Callable	362,475				
3. Unsubscribed	537,030				
Total Class B (Subscribed & Unsubscribed)	**108,000**				
TOTAL AUTHORISED CAPITAL STOCK	**1,080,000**				

Annex B: Governing Council, Advisory Panel, Board of Directors and Auditors

GOVERNING COUNCIL	
Hon. Dr. Ezra Suruma	Minister for Finance, Planning and Economic Development; Republic of Uganda **Chairman**
Hon. Zakia Meghji	Minister for Finance; United Republic of Tanzania
Hon. Amos Kimunya	Minister for Finance, Republic of Kenya

ADVISORY PANEL	
Mr. Mahesh K. Kotecha	President, Structured Credit Corporation and Vice Chairman Capital Markets Assurance Corporation, New York
Mr. Toyoo Gyohten	President, The Institute for International Monetary Affairs, Japan and Senior Adviser, Bank of Tokyo – Mitsubishi, Limited
Mr. Lars Ekengren	Former Deputy Director General, Sida
Mr. Jannik Lindbaek	Former Executive Vice President and CEO of the International Finance Corporation (IFC)
Mr. Robert McNamara	Former President of the World Bank

BOARD OF DIRECTORS	
Mr. Joseph K. Kinyua	Director, Kenya – (Chairman)
Mr. Gray S. Mgonja	Director, Tanzania
Mr. Christopher Kassami	Director, Uganda
Mr. Sheku S. Sesay	Director, AfDB (Retired 31st March 2007)
Mr. Mukaila Ojelade	Director, AfDB (Appointed 7th April 2007)
Mr. Francis N. Karuiru	Director, Kenya
Mr. James Mulwana	Director, Uganda
Mrs. Khadija I. Simba	Director, Tanzania

AUDITORS
KPMG, P.O. Box 3509, Kampala, Uganda

Annex C: Management

MANAGEMENT	
Mr. G. Tumusiime	Director General
Mr. W. Kasozi	Director of Legal Affairs/ Secretary
Mr. P. Opande	Director of Finance
Mr. Passwell Shapi	Director of Operations
Mr. B. Mboha	Resident Manager, Uganda
Mr. A.Mwakalyelye	Resident Manager, Tanzania
Mr. H. Olaka	Resident Manager, Kenya

Annex D: Addresses of the Headquarters and Country Offices

HEADQUARTERS:	**KAMPALA, UGANDA**	
	East African Development Bank Building	
	4 Nile Avenue, P. O. Box 7128, Kampala, Uganda	
	Telephones:	+256-414-230021 / 5
	Fax:	+256-414-259763
	E-mail:	admin@eadb.org
COUNTRY OFFICES:	**NAIROBI, KENYA**	
	2nd Floor, Rahimtulla Tower, P O Box P.O. Box 47685-00100, Nairobi, Kenya	
	Telephones:	+254-20-340642 / 340656
	Fax:	+254-20-2731590
	E-mail:	cok@eadb.org
	DAR ES SALAAM, TANZANIA	
	7th Floor, NSSF Waterfront House, P. O. Box 9401, Dar es Salaam, Tanzania	
	Telephones:	+255-22-2113195 / 2116981
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