TONGA DEVELOPMENT BANK

Annual Report for the Year Ended 30 June 2017

'AVE PA'ANGA PAU

Voucher Remittance Product

TDB
Tonga's Bank

29th September 2017

Hon. Minister for Finance & National Planning
Ministry of Finance & National Planning
Nuku'alofa

Hon. Minister

I have the pleasure to present, on behalf of the Board of Directors, the Annual Report and Statement of Accounts of the Tonga Development Bank for the financial year ended 30 June 2017, as required under the Tonga Development Bank Act, 2014 Section 18 (6) and the Public Enterprises Act 2002 Section 20 (1).

Respectfully

Lord Matoto
Chairman

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BACKGROUND

Tonga Development Bank was established on 1st September 1977 under the Tonga Development Bank Act 1977 and incorporated under the Companies Act, 1995 and registered again in 2001. The Tonga Development Bank Act was reviewed and re-enacted in 2014.

The TDB Act 2014 stipulates the mandate for TDB which may be summed up as promoting the social and economic development of the people and enterprises in Tonga through loans, savings, investments and advisory services which are provided on sound professional banking principles and ensuring such loans are repaid. With the TDB Act 2014 in force and within the following years TDB is focusing on innovation and customer service by providing existing customers with services offered by commercial banks and where all their banking needs are met.

The Tonga Government is the sole shareholder of TDB since 1998. A Board of five Directors appointed by the Government oversees the policy management of the Bank. The Board includes a Managing Director and CEO to oversee the day to day management of the business.

VISION

"To be recognized as Tonga's outstanding provider of development and commercial finance which employs prudent banking principles to meet customer needs, demonstrates integrity and operates profitably"

MISSION

"To be committed to promoting Tonga's economic and social advancement by providing high quality development and commercial banking products and responsive professional services, while operating profitably as a financially sound banking institution"

BOARD OF DIRECTORS AS AT JUNE 2017

LORD MATOTO
Former Managing Director of the Bank and former Minister for Finance & National Planning. Chairman of the Board since February 2013.

MR PAULA TAUMOEPEAU

Business man and has been a Director of the Bank since September 2009.

MRS LEPAOLA VAEA

Deputy CEO of the Ministry of Revenue & Customs. Director of the Board in February 2014 (resigned 14 June 2017)

MRS LETA HAVEA KAMI
She was appointed in September 2013 as Managing Director & CEO.

MR OBEY NIU SAMATE
Highly experienced commercial banker and was appointed in September 06, 2017.

CHAIRMAN'S REPORT

"TDB achieving its 40th anniversary this year is a biblical milestone as it has undergone transformation, achieved continued growth, expanded its products and services and now a commercial bank to continuously serve the public's banking needs successfully in the long run."

It is always a pleasure for me to address shareholders when it comes to the end of any financial year. Yet this financial year is different because it is the Bank's first 12 months financial year period after aligning its calendar year period with an 18 months financials last year in order to be the same with the Government's financial year. It posed its own challenges with system changes required and compliance issues while going commercial.

Appointments
The Board has been strengthened with the new appointment of Mr Obey Samate on 6th September 2016 who brings onboard a wealth of experience in the banking sector. This has added a balance in experience at the Board level in the relevant areas. Although, we had to farewell Ms Lepaola Vaea who resigned on 14 June 2017 due to new career opportunities and work commitments.

New appointments to the Senior Management team with a strong gender composition with the retirement of Mr Hasiloni Fungavai after 30 years with TDB on the 27 March 2017 and Ms Loi Turaga Mateiwai replacing him as the new Chief Finance Officer. Ms Mateiwai has background in business and commercial banking experience. Ms Seini Vaiola Movete took over the Chief Credit Officer role in March 2017 from Mr Sitino Maka who also retired. Seini has been with the Bank for 24 years and had led the transformation programme over last 2 years.

Operation Highlights
The year was a busy one for the Bank in seeing most of its new products and services complete a full year of operation and competing fairly well in the market. The impact of costs realized and few improvements identified to be addressed as changes come with challenges and need to be managed quickly at the right time. Changes towards more automation are ongoing and expect more to be taken up during the next financial year. Growth is noted in savings and deposits as well in lending.

Our own unique Tongan online remittance product, 'Ave Pa'anga Pau was launched in February 2017. It supports Government's vision to keep remittance costs low to support RSE workers and Tongan communities in NZ who help to prop up almost 30% of our GDP with remittances.

Decisions undertaken during the year were made in light of the competitive environment to improve our services, customer care and efficiency across all operations taking into account expectations of our shareholders, regulators and key stakeholders.

The financial statement for the period shows a slight downward trend from the past. TDB had grown however there are operating activities which needs to be controlled and tightened. This is an indication that commercialization of our operations brings on new revenue streams and a range of new banking activities also brings various and different expense structures to be managed carefully. Overall, the Bank has basically achieved just below targets set for this period in terms of profitability and other development goals but fell short in terms of operating activities and income. Net Profit After Tax for the period was $1.44 million against an expected final budget of $1.54 million. Improvements need to be made in various areas of the Bank which will contribute to continuing strong performance by TDB in the long run.

Transformation and changes can be disruptive due to new challenges, also new and innovative activities require adjustments and trainings. The Bank's staffs have generally been very committed to the transformation and have responded well to the challenges which enabled the Bank to perform quite credibly in all aspects. Of course there are improvements to make which will receive attention as we move ahead.

The Bank will continue to provide more products in trade finance, ATMs and cards. However, before decisions are made proper business cases will be built around each product and timelines too. Meantime, continued staff training, roll out of new products, customer services upgrade and improvements will ensure the Bank's core functions receive proper ongoing attention. There are ongoing amendments on policies and work processes, and at the same time the Bank will ensure full compliance with both statutory and regulatory requirements.

Productivity and efficiency are important aspects the Bank drives and emphasizes through good people management practices as these are vital to the transformation of the Bank and its growth. All staff remuneration are reviewed and if necessary the Bank seeks advice from the Korn Ferry/Hay Group (New Zealand). The Bank had also sponsored a full scholarship for one of its IT staff to complete a degree in NZ to increase staff productivity and ensure succession planning. Also, TDB encourages staff continued education and will look for staff with good tertiary qualification and relevant work experience.

The Bank continues to provide agency services to Government with Sub-Treasury functions for the Niuas but in Vava'u, 'Eua and Ha'apai the Government has re-established its sub-treasuries there.

To stimulate economic activity, the Government requires the bank to manage its Government Development Loan (GDL) funds which is provided to the public on terms stipulated by the Government at low interest and no fees. The GDL directly competes with the TDB loan products and negatively impacted the performance of the Bank because Government refuses to pay the proper fees under the GPO policy to cover costs for managing the GDL and does not always pay on time.

For this financial period the Bank would not pay any dividend because of a breach of the regulatory requirement on single borrower limit. The Bank is obliged to restructure it's capital to meet the requirements by March 2018 and is working with it's shareholder to address this issue. The return on equity for 2016/17 is around 5.8% a slight reduction on the 18 months period by 0.09%.

With Tonga withdrawing from hosting the South Pacific Games in 2019, it is expected that the FX Levy Act will be repealed as the money was specifically for the Games. As the Bank absorbs the levy in its FX margin, it would like to see this cost abolished.

As a good citizen of the Kingdom, the TDB has supported and is continuing to support a diverse-range of activities within the community which promote health, education, sports, community activities and charitable purposes. The bank has granted a number of scholarships to local vocational training institutions to promote knowledge, skills based training and economic development in the country.

Future Outlook

In the coming year we will continue to revamp and improve services and all areas of the Bank. We will continue to explore all avenues for improvement, including the ongoing improvement on performance.

Changes in technology and the market will continue to drive the structure and operations of Bank, therefore we will always review the need to constantly adapt and ensure that the Bank is aligned with the latest technology to support the expansion as well to meet the needs of customers and the market. This will drive the demand of service we provide.

Acknowledgement

I would like to take this opportunity to acknowledge, on behalf of the Board of TDB, the continuing support received from the NRBT Governor and his team, the Minister of Finance and National Planning, Hon Dr 'Aisake Eke and later Hon Tevita Lavemaau, the Minister for Public Enterprises Hon Poasi Tei, the CEO and staff of the Ministry of Public Enterprises, other CEOs and staff of Government Ministries, the Directors, CEOs and staff of public enterprises, the Governors of Vava'u and Ha'apai and Government Representations and staff of ministries in the outer islands. The TDB Board is fully appreciative of the hard work and effort made by the CEO of the TDB, the Manager for Transformation, Managers and staff during this financial year. I am grateful to my fellow directors for their valuable contributions, support, expertise and maintaining the best interests of the Bank, shareholders, stakeholders, customers and staff of TDB at all times.

Last to mention but important at all times to the Bank, we extend and express our sincere appreciation and gratitude to our highly valued customers for their support, trust and continuing confidence in TDB. Together in this partnership we can grow and reach new heights.

Malo ʻaupito

Lord Matoto
Chairman

CEO'S REPORT

"A unified TDB team working together and striving for continuous improvement, can bring about the change needed to deliver customer service excellence, achieve strong long term results and make a lasting positive impact on Tonga's economic development."

I am sincerely grateful to our Almighty God for bringing us through a very difficult and challenging financial year.

As the only bank with 100% Tongan ownership and branded as "Tonga's Bank," has served as one of our greatest strength, especially in the challenges that we face as a new entrant into the commercial banking arena. Our 2016/2017 results indicated growth in loans in all sectors and savings where we deliver our services.

We are proud that TDB was set up by His Majesty King Taufa'ahau Tupou IV in 1977 and his vision for a sustainable institution driving social and economic development in the country has been achieved in its 40th anniversary this year. Moreover, TDB is linking up with the Tongan diaspora in New Zealand through its newest remittance voucher product called 'Ave Pa'anga Pau or "TDB Apps" which is a truly Tongan product providing low cost remittance service and a first time achievement in the Pacific region. We hope to further enhance and expand the service to other countries too.

CHALLENGES

Overall loan and advances portfolio stood at $59.17m on 30th June 2017, reflecting a 16% growth. More importantly the shareholders equity has grown from $20.916m in 2016 to $24.843m as at 30th June 2017. Shareholders' equity was only $329,793 in 1977 within 40 years the shareholder value has increased by $24.513m or on average of $612,845 in every year. In the process of portfolio diversification, TDB has introduced different commercial products whilst we do monitor, follow up and take corrective actions where necessary as we remain vigilant to the possibility of added risk and costs in some areas.

The Bank experience rapid change with our transformation programme in 2016-2017 to commercialization. At the same time, there were other changes which we had to cope with and incorporate into our plans. For example, our shareholder required a change of financial year from December to June which impacted our system capability in absorbing the changes. The changes that we went through had indicated some shortfalls and technical issues in our current operating system but we are successfully addressing the issues. The cost of the full depreciation of our intangible assets had caused the major impact in our financial results.

It was a challenging year, yet the Bank remains confident and focused on it's ability to strategically expand its business interests to deliver services consistently and adding value throughout its extensive branch network locally. Whilst we want to compete and offer attractive products to the public, we are also restricted in lending by certain prudential requirements by the regulator and legislation. Our current capital base needs to be restructured to enable the Bank to meet the needs of larger customers and be more competitive in the market. We are working with our regulators and potential investors to address this issue.

YEAR IN REVIEW

Lending Sector

a. TDB Portfolio Growth

The Bank's gross loan portfolio has increased by $8.44m (16 %) from $52.69m in 2016 to $61.13m in 2017. The overall portfolio consists of Agriculture/Fisheries Sector $5.19m in 2017 (increased by 20% from $4.30m in 2016), Industry & Business $32.09m (increased by 48% from $21.67m in 2016), Housing & Personal $21.09m (decreased by 16% from $24.39m in 2016) and Staff loan $2.77m (increased by 19% from $2.33m in 2016).

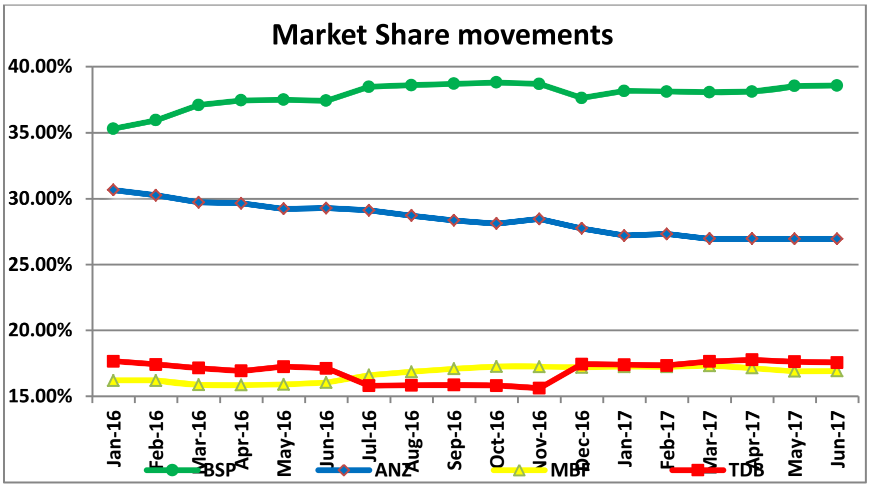
The overall growth in portfolio in the last 12 months was satisfactory given the lending to Agriculture/Fisheries, Industries & Business sectors directly competes with the low cost Government Development Loan (GDL) offered at 1% and 4%. However, there are rooms for growth in these sectors but we need to improve marketing, client visitation programme and service delivery in order to increase lending.

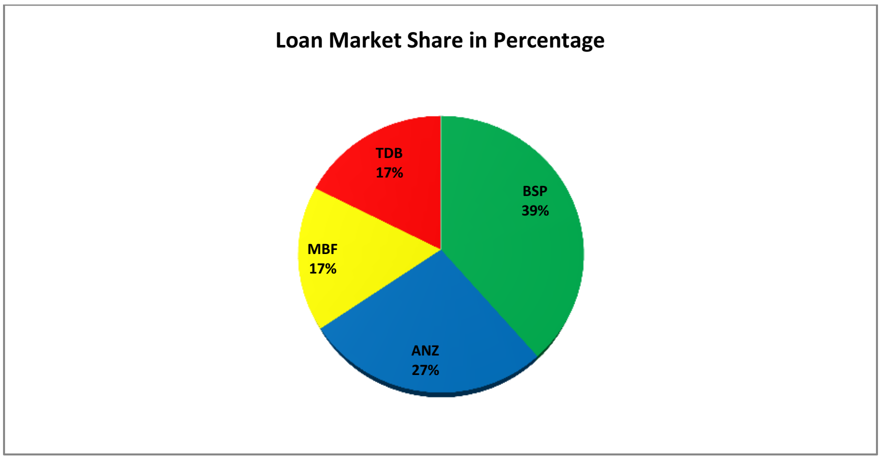
Lending to the Housing & Personal sector has decreased as it is a highly competitive sector in which all commercial banks participate and including the Retirement Fund Board for their members only. The GDL also affects Personal Loans for educational purposes.

b. GDL portfolio Growth

The GDL Portfolio has increased by $9,339 from $9.10m in 2016 to $9.11m in 2017. The GDL programme is a revolving fund with low interest rates of 1% and 4% to key productive sectors (ie: Agriculture, Fisheries, Tourism, Education and others). TDB has been managing the total GDL fund of $13.05m over the last 3 years for Government according to an Implementation Agreement and receives an annual service fee. In May 2017, Government provided an additional $1m to the Agriculture & Fisheries sectors taking total funding to $14.05m.

Graphs below indicate TDB's Market Share in Gross Loans





Banking Sector

a. Portfolio Growth for Branch Operations

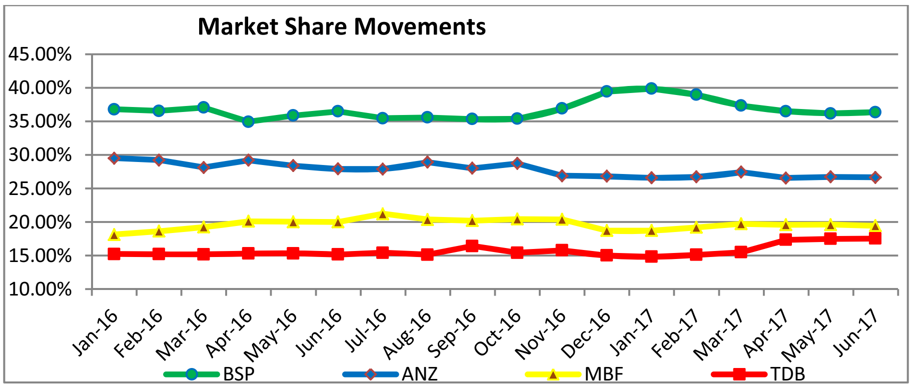
The newly formed Operations Department which covered the Branch Office of Hahake, Hihifo, 'Eua, Ha'apai, Vava'u, Niuatoputapu and Niuafo'ou had grown within the financial year:

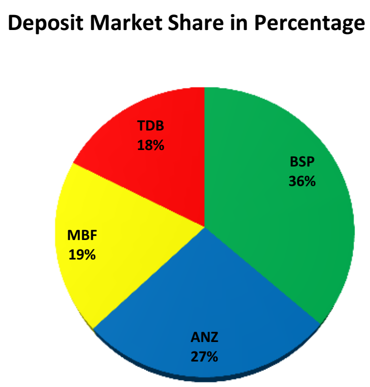
i. The Branch Operations Portfolio grew in value by $978,242 or 7.1% compared to June 2016. In June 2017, the portfolio stands at $14.67m in comparison to $13.69m at end of June 2016. However, the number of accounts had declined by 143 accounts or 7.4% from 1,929 accounts to 1,786 compared to the eighteen months last year. This was basically due to the re-opening of the BSP branches in 'Eua and Ha'apai late last year after 3 years agency service provided by TDB.

ii. GDL Portfolio grew by 23.6%. The amount increased from $2.67m in 2016 to $3.32m at the end of June 2017. The total number of accounts also increased by 206 or 53.5% from 385 accounts to 591 accounts compared to the eighteen months last year.

iii. All Offices portfolio grew except Hihifo Office which had declined by $29,439 or 1.9% from July 2016 to June 2017.

Graphs below indicate TDB's Market Share in Deposits





b. Online Banking

Online Banking was launched to the public in September 2016. With Online Banking services, the Bank offers an easy and effective way for clients to access information on their accounts anytime, keep track of their finances and make transactions anytime 24 hours and seven days a week and from any place with internet access.
Online Banking enables our clients to perform all routine transactions such as:

(a) view account information, balances and transactions;

(b) view and print bank statements;

(c) transfer funds between designated accounts within the Bank, and

(d) transfer funds to other local Banks.

Online Banking is in full operation now with a total of 291 Personal customers and 37 Business customers of whom 36 are personal customers and 2 business customers are from the Branches.

c. TDB APP (ʻAve Paʻanga Pau Voucher Remittance Product)

We acknowledge the technical assistance provided by IFC over the last two years in the development of our newest product aiming to provide low cost remittance from New Zealand to Tonga. The ʻAve Paʻanga Pau product was successfully launched by the Prime Minister of Tonga, Hon. Samiuela ʻAkilisi Pohiva on 14 February 2017.

At the end of June 2017, we have 248 active clients using this product which include the outer branches as well. This new low cost product has a lot of growth potential to support the Tongan community in New Zealand and RSE workers programme and the Tongan diaspora overseas.

PM Hon. Samiuela ʻAkilisi Pohiva launching the TDB APP

d. Outer Islands Banking Services

In Haʻapai, our banking services includes twelve (12) outer-islands which are visited regularly on a monthly basis to complete loan applications, site inspections of security assets, receipting loan repayments, verify project implementation and marketing TDB products and services.

The regular monthly trip is carried out by one (1) bank officer and normally takes only 2 days, but it may be a bit longer depending on the weather. We have been hiring local boats to carry out this work but have been very wary of risks. Therefore, the Bank is working closely with the Ministry of Police as we are keen on capitalizing on the opportunity for better security and safety in our service delivery.

Vava'u outer-islands visit is carried out on a quarterly basis offering the same services as Ha'apai. However, Vava'u people easily accessed our services as there are more boat transportation available on a weekly basis from the islands to Neiafu.

PERFORMANCE TARGETS AND MEASURES

a. Credit Risk Management (CRM)

We continued to apply prudent credit risk management principles and it is an ongoing process aimed at maintaining and improving the quality of the Loan Portfolio.

The loan grading system continued to be a valuable tool in assessing the overall health of the loan portfolio during the year.

b. Liquid Asset Ratio

The Reserve Bank continues to impose a threshold Liquid Asset Ratio (LAR) of 18% to ensure that sufficient liquidity is available in the system. The Bank's LAR as at end of June 2017 was 42.50% a growth of 3.12% from 39.38% in the previous year.

c. Arrears

The arrears ratio was recorded at 2.40% at year end 30 June 2017 as compared to target of 4.5%. It is a significant reduction of arrears ratio from 12.5% in 30 June 2016.

The 2016/17 target for the number of accounts in arrears was 500. However, the actual number of account in arrears was 275 at year end 30 June 2017 indicating a good proactive arrears process and active portfolio management practices.

d. Funding

The Bank's lending are funded by internal sources which provides 87% of the funding requirements.

e. Net Interest Margin (NIM)

The Bank's NIM is reviewed on a quarterly basis. This includes matching of the average lending interest rates with the average interest cost of funds. As at end June 2017, the Net Interest Margin was 4.79%.

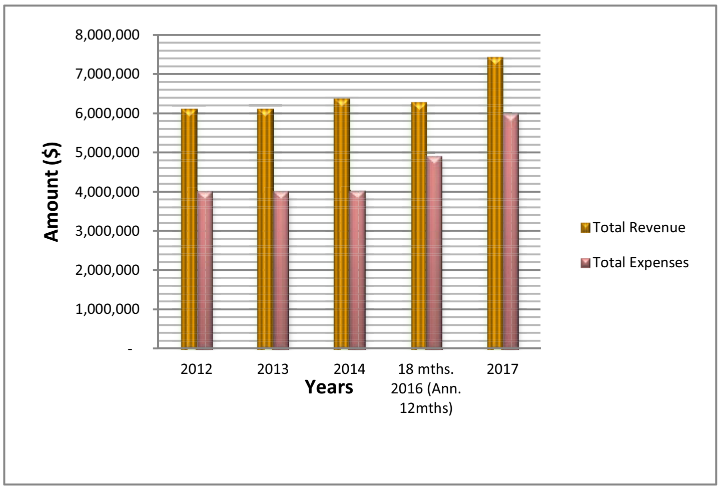
FINANCIAL PEROFRMANCE

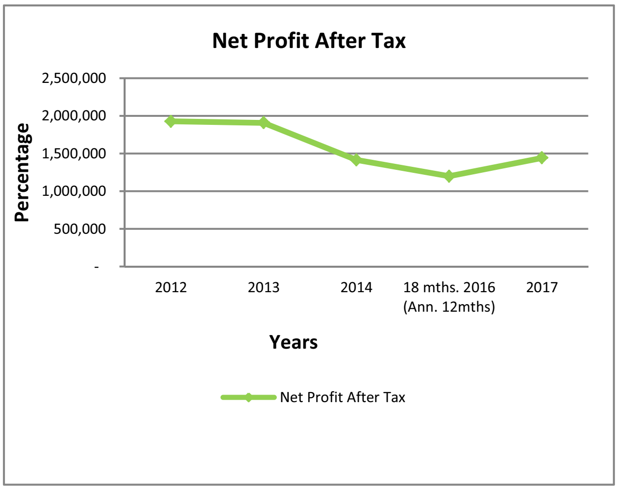
(All figures are in Tongan Pa'anga)

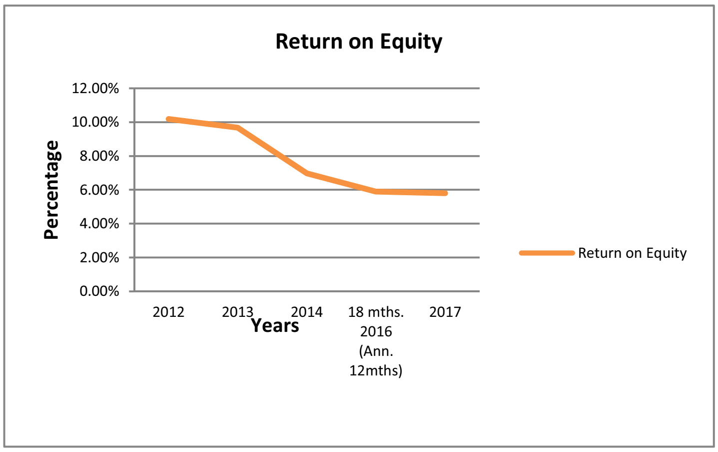
Tonga Development Bank recorded operating revenue of $7.43m. We recorded a net profit before tax at $1.298m for the year ended 30th June 2017, compared to $1.795m achieved in the eighteen months period year. Annualizing the growth in the last financial year to 12 months in this financial had increased by $598,562 which represents a growth of 20%. We continue to successfully support the economic development on the country by assisting the Government in delivering its low cost GDL loan facility to the public on a revolving basis. As at 30th June 2017, the total revolving funds lent to the public reached $22m with more than 1,000 account holders in different development sectors. At the same time, we are managing the GDL loan facility carefully since it completes with the Bank's products.

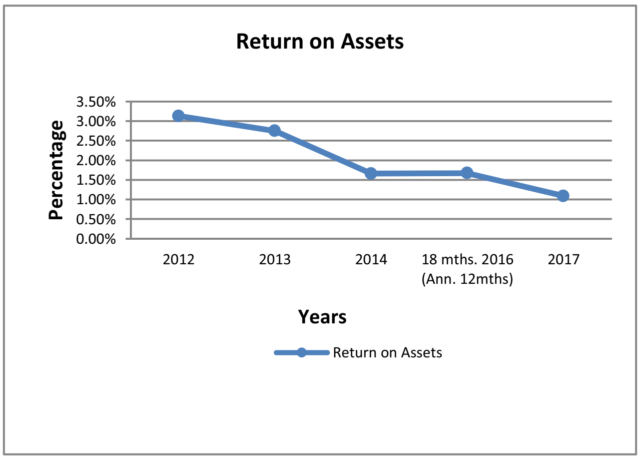
	2012	2013	2014	18 mths. 2016 (Ann. 12mths)	2017
Total Revenue	$ 6,114,457	$ 6,127,343	$ 6,368,496	$ 6,270,512	$ 7,426,778
Net Profit After Tax	1,925,885	1,907,535	1,414,055	1,197,124	1,440,664
Total Assets	61,536,744	69,406,509	85,140,268	107,371,040	132,214,371
Total Liabilities	42,633,347	49,684,228	64,852,365	86,454,647	107,370,779
Retained Earnings	8,373,207	9,192,091	6,287,903	6,916,393	8,357,057
Total Shareholder's Equity	18,903,397	19,722,281	20,287,903	20,317,831	24,843,592
Earnings Per Share	$ 1.83	$ 1.81	$ 1.01	$ 0.86	$ 1.03
Dividend Per Share	0.63	0.78	0.61	0.56	-
Profitability Measures	**2012**	**2013**	**2014**	**18 mths. 2016 (Ann. 12mths)**	**2017**
Return on Assets	3.13%	2.75%	1.66%	1.11%	1.09%
Return on Equity	10.19%	9.67%	6.97%	5.89%	5.80%
Profit Margin	31.50%	31.13%	22.20%	19.09%	19.40%
Liquidity Measures					
Current Ratio	1.44	1.40	1.31	1.24	1.23
Quick Ratio	1.13	1.15	1.70	1.08	1.42
Financial Measures					
Debt Ratio	0.69	0.72	0.76	0.81	0.81
Debt/Equity Ratio	2.26	2.52	3.20	4.26	4.32

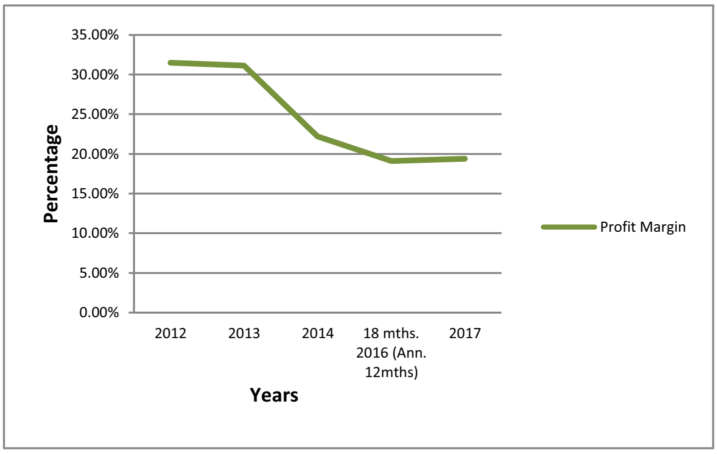
FINANCIAL TRENDS











The Bank had a feasibility study done in November 2013 and approved by Government to commence the transformation and expansion of its services in 2014 from development banking to Commercial Banking. In 2015/2016 the bank changed it's financial year end from December to June to be in line with the Government. This had an impact on the operations as there were key risk areas to be addressed. Due to Single Borrower Limit exceeded, no dividends will be paid out. However, a possible Dividend Bonus payout will be paid when the requirement is fulfilled. This is reflected in the graph above.

Return on Assets had decreased due to growth in Loans and Advances during the period against the Net Profit.

PEOPLE CAPITAL
We value our 123 full time staff as well as 26 casual staff who have made our transformation possible. The total 149 staff are the most important assets of our business. Thus, we provide ongoing training and encourage further education and scholarships to encourage staff to obtain higher skills and to broaden and keep current their knowledge.

The people we take on board are the lifeblood of the organization. Our employees are the most important assets in our business. They run the organization and provide the end results. The average age of staff is 34 years and staff turnover remains low at 14% at the end of June 2017.

Staff are given opportunity and practical training with other commercial banks and relevant institutions on an ongoing basis. In-house training on SWIFT, TDB APPs, and Customer Services were conducted to equip the staff with the skills and knowledge to deliver service standards required. Relevant training will continue to be done on an ongoing basis to create a product knowledge based culture within the organisation.

FUTURE OUTLOOK
Our journey is never being easy. We continue to strive for progress and transformation as we explore the commercial banking sectors. The Bank has been well positioned for growth with savings and lending to enhance capacity and operational efficiency of the existing operation. We will realign our resources to address potential threats and remain focused on what we intent to achieve in the long run.

We remain focused on what we plan to do and confident of improving our growth in creating value as we move to the year ahead.

APPRECIATION
I wish to take this opportunity to express my sincere appreciation to the Chairman and Board of Directors for their valuable advice and excellent guidance helping Management to navigate successfully through the required changes and risk management during the year. Moreover, I would like to convey my sincere gratitude for the commitment of the unified management team and staff of the Bank – "Takanga 'etau Fohe." Without their commitment to paddle our canoe as one and move forward strongly together, the results achieved this year would not be possible.

I am also very grateful to our loyal customers who have placed their trust and belief in the Bank and embarking on the expansion journey with us. We thank you for your feedback and support to help us to be a better business partner going forward. May God bless TDB and everyone who has a relationship with this key institution to sustain it going forward for another successful 40 years and more to come.

Malo

Leta Havea Kami
Chief Executive Officer

FIVE YEARS SUMMARY

Profit & Loss TOP $'000s	2012	2013	2014	June 2016 (18months)	2017	Movement 2016/June 2017
Interest Income	4,603	4,511	4,706	7,186	5,065	-30%
Interest Expense	1,095	1,189	1,473	2,979	2,421	-19%
Net Interest Income	3,509	3,322	3,233	4,207	2,643	-37%
Fees & commission income	2,266	2,362	2,556	3,694	2,410	-35%
Other Operating Income	339	443	580	1,504	1,615	7%
Losses on loans & advances	383	389	694	(188)	229	-222%
Bad Debts	73	4	31	32	56	75%
Income Tax Expense	597	270	406	542	(143)	-126%
Operating Profit after tax	1,329	1,638	1,414	1,796	1,441	-20%
Earnings per share	1.26	1.56	1.01	1.28	1.03	-20%
Balance Sheet **TOP $'000s**	**2012**	**2013**	**2014**	**June 2016 (18months)**	**2017**	**Movement 2016/June 2017**
Average assets	61,589	65,472	77,273	96,256	119,793	24%
Total Assets	61,537	69,407	85,140	107,371	132,214	23%
Gross Loans	42,328	47,329	51,379	50,881	59,174	16%
Saving Deposits	6,885	9,246	10,888	20,855	30,607	47%
Shareholder's Equity	18,903	19,722	20,288	20,916	24,843	19%
Performance Ratios	**2012**	**2013**	**2014**	**June 2016 (18months)**	**2017**	**Movement 2016/June 2017**
Return on Assets	2.20%	2.50%	1.80%	1.90%	1.09%	-42.6%
Return on Equity	7.00%	8.30%	6.97%	8.59%	5.80%	-32.5%
Operating Costs to Total Income	70.80%	71.10%	70.10%	78.23%	80.58%	3.0%
Operating Income to Average Portfolio	15.20%	16.30%	18.80%	23.8%	17.3%	-27.3%

DIRECTORS' REPORT

In accordance with a resolution of the Board of Directors, the directors herewith submit the balance sheet as at 30 June 2017, statement of profit or loss and other comprehensive income, statement of changes in equity and statement of cash flows for the year ended on that date and report as follows:

1. DIRECTORS

The following persons were directors of the Bank at any time during the year and up to the date of this report:

- Lord Matoto (Chairman)
- Paula Taumoepeau
- Leta Havea Kami
- Lepaola Vaea (Resigned 14 June 2017)
- Obey Samate (Appointed 6 September 2016)

2. PRINCIPAL ACTIVITY

The principal activity of the Bank is the provision of development and selected commercial banking services in the Kingdom of Tonga.

During the year ended 30 June 2017 there has been no material change in the nature of the Bank's business or in the classes of business in which the Bank has an interest.

3. TRADING RESULTS

The net profit after income tax for the year ended 30 June 2017 was $1,440,664 (period ended 30 June 2016: $1,795,686).

4. PROVISIONS

There were no material movements in provisions, other than provisions for losses on loans and advances, and employee entitlements.

5. DIVIDENDS

No dividend was declared for the year ended 30 June 2017.

DIRECTORS' REPORT – CONTINUED

6. RESERVES

The directors recommend that revaluation surplus on property, plant and equipment be transferred to asset revaluation reserves in respect of the year ended 30 June 2017.

7. BASIS OF ACCOUNTING

The directors believe the basis of the preparation of financial statements is appropriate and the Bank will be able to continue in operation for at least 12 months from the date of this report. Accordingly the directors believe the classification and carrying amounts of assets and liabilities as stated in these financial statements to be appropriate.

8. BAD AND DOUBTFUL DEBTS

The directors took reasonable steps before the Bank's statement of profit or loss and other comprehensive income and balance sheet were made out to ascertain that all known bad debts were written off and adequate provision was made for doubtful debts.

At the date of this report, the directors are not aware of any circumstances which would render the amount written off for bad debts, or the amount of the provision for doubtful debts, inadequate to any substantial extent.

9. EVENTS SUBSEQUENT TO BALANCE DATE

The Bank had amended its Articles of Association during the year to increase its authorised capital as part of a capital restructuring exercise. The Bank has identified potential investors including seeking additional injection of capital from its current shareholder, which is yet to eventuate.

The intent of this exercise is to increase the Bank's capital base to remedy a breach in the single borrower limit during the current financial year as well as take on board more significant loans in the future in order to be more competitive in the market.

10. UNUSUAL OR SIGNIFICANT TRANSACTIONS

The results of the Bank's operations for the year ended 30 June 2017 have not in the opinion of the directors been substantially affected by any item, transaction or event of a material and unusual nature other than those disclosed in the financial statements. The Bank however had breached the 25% single borrower limit under regulatory requirements and is under one (1) year Government guarantee from March 2017.

11. OTHER CIRCUMSTANCES

At the date of this report, the directors are not aware of any circumstances not otherwise dealt with in this report or financial statements which render any amounts stated in the financial statements misleading.

12. RELATED PARTY TRANSACTIONS

All related party transactions have been adequately recorded in the financial statements. The transactions with related parties are on normal commercial terms and conditions.

13. **DIRECTORS' BENEFITS**

No director has, since the end of the previous financial year, received or become entitled to receive a benefit (other than loans and advances given in the normal course of operation or benefit included in the total amount of emoluments received or due and receivable by directors as shown in the Bank's financial statements) by reason of contract made by the Bank or related entity with the director or with a firm of which he is a member or with a company in which he has substantial financial interest.

Signed in accordance with a resolution of the directors this 30th day of August 2017.

....
Leta Havea Kami
Chief Executive Officer

....
Lord Matoto
Chairman of the Board

STATEMENT BY DIRECTORS

In the opinion of the directors:

(a) the accompanying statement of profit or loss and other comprehensive income is drawn up so as to give a true and fair view of the results of the Bank for the year ended 30 June 2017,

(b) the accompanying balance sheet is drawn up so as to give a true and fair view of the state of affairs of the Bank as at 30 June 2017;

(c) the accompanying statement of changes in equity is drawn up so as to give a true and fair view of the movement in shareholder's funds for the year ended 30 June 2017; and

(d) the accompanying statement of cash flows is drawn up so as to give a true and fair view of the cash flows of the Bank for the year ended 30 June 2017.

....	....
Leta Havea Kami	**Lord Matoto**
Chief Executive Officer	**Chairman of the Board**

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Independent Auditor's Report

To the Shareholder of Tonga Development Bank Limited

Report on the Audit of the Financial Statements

Opinion

We have audited the accompanying financial statements of Tonga Development Bank Limited (the 'Bank'), which comprise the balance sheet as at 30 June 2017, and the statement of profit or loss and other comprehensive income, statement of changes in equity and statement of cash flows for the year then ended, and notes to the financial statements, including a summary of significant accounting policies.

In our opinion, the accompanying financial statements give a true and fair view of the financial position of the Bank as at 30 June 2017, and of its financial performance and its cash flows for the year then ended in accordance with International Financial Reporting Standards.

Basis for Opinion

We conducted our audit in accordance with International Standards on Auditing (ISAs) Our responsibilities under those standards are further described in the *Auditor's Responsibilities for the Audit of the Financial Statements* section of our report.

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

Independence

We are independent of the Bank in accordance with the ethical requirements of the International Ethics Standards Board for Accountant's Code of Ethics for Professional Accountants (IESBA Code) that are relevant to our audit of the financial statements in Tonga, and we have fulfilled our other ethical responsibilities in accordance with these requirements and the IESBA Code.

Responsibilities of Directors and management for the financial statements

Directors and management are responsible for the preparation and fair presentation of the financial statements in accordance with International Financial Reporting Standards and with the requirements of the Tonga Companies Act, 1995 and the Tonga Development Bank Act, 2014, and for such internal control as the directors and management determine is necessary to enable the preparation of financial statements that are free from material misstatement, whether due to fraud or error.

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

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

PricewaterhouseCoopers Level 8 Civic Tower, 272 Victoria Parade, Suva Fiji
GPO Box 200 Suva, Fiji.
T (679)3313955 / 3315199 F (679) 3300947

pwc

Auditor's Responsibilities for the Audit of the Financial Statements

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

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

- Identify and assess the risks of material misstatement of the financial statements, whether due to fraud or error, design and perform audit procedures responsive to those risks, and obtain audit evidence that is sufficient and appropriate to provide a basis for our opinion. The risk of not detecting a material misstatement resulting from fraud is higher than for one resulting from error, as fraud may involve collusion, forgery, intentional omissions, misrepresentations, or the override of internal control

- Obtain an understanding of internal control relevant to the audit in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Bank's internal control.

- Evaluate the appropriateness of accounting policies used and the reasonableness of accounting estimates and related disclosures made by the directors and management.

- Conclude on the appropriateness of the directors and managements use of the going concern basis of accounting and, based on the audit evidence obtained, whether a material uncertainty exists related to events or conditions that may cast significant doubt on the Bank's ability to continue as a going concern If we conclude that a material uncertainty exists, we are required to draw attention in our auditor's report to the related disclosures in the financial statements or, if such disclosures are inadequate, to modify our opinion. Our conclusions are based on the audit evidence obtained up to the date of our auditor's report. However, future events or conditions may cause the Bank to cease to continue as a going concern

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

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

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Report on Other Legal and Regulatory Requirements

In accordance with the requirements of the Tonga Companies Act 1995, in our opinion:

a) proper books of account have been kept by the Bank, so far as it appears from our examination of those books, and

b) the accompanying financial statements are in agreement with the books of account and to the best of our information and according to the explanations given to us give the information required by the Tonga Companies Act, 1995 and the Tonga Development Bank Act, 2014, in the manner so required

We have obtained all the information and explanations which to the best of our knowledge and belief were necessary for the purposes of our audit.

Restriction on Distribution or Use

This report is made solely to the Bank's shareholder, as a body. Our audit work has been undertaken so that we might state to the Bank's shareholder those matters we are required to state to them in an auditor's report and for no other purpose. To the fullest extent permitted by law, we do not accept or assume responsibility to anyone other than the Bank and the Bank's shareholder as a body, for our audit work, for this report, or for the opinions we have formed.

30 August 2017
Suva, Fiji

PricewaterhouseCoopers
PricewaterhouseCoopers
Chartered Accountants

TONGA DEVELOPMENT BANK

STATEMENT OF PROFIT OR LOSS AND OTHER COMPREHENSIVE INCOME YEAR ENDED 30 JUNE 2017

	Notes	Year ended 30 June 2017 $	18 months ended 30 June 2016 $
Interest income	6	5,065,071	7,186,450
Interest and other borrowing expenses	6	(2,421,537)	(2,979,213)
Net interest income		2,643,534	4,207,237
Fees and commission income	7	2,410,715	3,694,189
Other operating income	8	1,615,568	1,504,342
Fair value gains on investment property	18	756,961	-
Net operating income		7,426,778	9,405,768
Losses on loans and advances	13	(229,888)	187,517
Bad debts written off		(56,287)	(32,150)
Bad debts recovered/reversed		142,529	134,534
Other operating expenses	9	(5,984,565)	(7,358,462)
Profit before income tax		1,298,567	2,337,207
Income tax benefit/ (expense)	20	142,097	(541,521)
Profit for the year/period from continuing operations		1,440,664	1,795,686
Other comprehensive income		2,486,535	-
Total comprehensive income for the year/period		$ 3,927,199	$ 1,795,686
Earnings per share	29	$ 1.03	$ 1.28

The above statement of profit or loss and other comprehensive income should be read in conjunction with the accompanying notes.

TONGA DEVELOPMENT BANK

BALANCE SHEET
AS AT 30 JUNE 2017

	Notes	30 June 2017 $	30 June 2016 $
ASSETS			
Cash on hand and at bank	10	47,283,807	35,239,900
Due from other financial institutions		521,914	305,474
Investment securities – held to maturity	12	7,588,757	7,776,302
Loans and advances	13	59,174,531	50,881,032
Other assets	14	1,215,627	1,284,599
Amounts receivable from shareholder	15	1,104,937	10,946
Statutory reserve deposit	16	4,645,000	3,758,000
Property, plant and equipment	17	9,784,803	6,738,754
Investment property	18	200,000	436,497
Intangible assets	19	-	294,582
Deferred tax asset	20(c)	694,995	644,954
Total assets		$ 132,214,371	$ 107,371,040
LIABILITIES			
Savings deposits		30,607,057	20,855,083
Other liabilities	21	3,056,075	4,736,876
Amount payable to NRBT	16	111,000	100,000
Borrowings	22	65,456,440	57,440,947
Current tax liability	20(a)	337,637	104,441
Managed funds	23	7,107,575	1,955,325
Deferred tax liability	20(d)	694,995	1,094,779
Dividends payable	28	-	167,196
Total liabilities		107,370,779	86,454,647
SHAREHOLDERS' EQUITY			
Share capital	24(b)	14,000,000	14,000,000
Retained earnings		8,357,057	6,916,393
Asset revaluation reserve	24(c)	2,486,535	-
Total shareholders' equity		24,843,592	20,916,393
Total equity and liabilities		$ 132,214,371	$ 107,371,040

The above balance sheet should be read in conjunction with the accompanying notes.

Signed in accordance with a resolution of the directors this 30th day of August 2017.

Leta Havea Kami
Chief Executive Officer

Lord Matoto
Chairman of the Board

TONGA DEVELOPMENT BANK

STATEMENT OF CHANGES IN EQUITY
YEAR ENDED 30 JUNE 2017

	Notes	Share Capital	Retained Earnings	Asset Revaluation Reserve	Total
		$	$	$	$
Balance at 1 January 2015		14,000,000	6,287,903	-	20,287,903
Comprehensive income					
Profit for the period		-	1,795,686	-	1,795,686
Other comprehensive income		-	-	-	-
Total comprehensive income		-	1,795,686	-	1,795,686
Transactions with owners					
Dividend declared for the period	28	-	(1,167,196)	-	(1,167,196)
Total transactions with owners		-	(1,167,196)	-	(1,167,196)
Balance at 30 June 2016		14,000,000	$ 6,916,393	-	$ 20,916,393
Comprehensive income					
Profit for the year		-	1,440,664	-	1,440,664
Revaluation surplus	24(c)	-	-	2,486,535	2,486,535
Other comprehensive income		-	-	-	-
Total comprehensive income		-	1,440,664	2,486,535	3,927,199
Transactions with owners					
Dividends declared in 2017	28	-	-	-	-
Balance at 30 June 2017		$14,000,000	$8,357,057	$2,486,535	$ 24,843,592

The above statement of changes in equity should be read in conjunction with the accompanying notes.

TONGA DEVELOPMENT BANK

STATEMENT OF CASH FLOWS
YEAR ENDED 30 JUNE 2017

	Note	Year ended 30 June 2017 $	18 months ended 30 June 2016 $
Cash flows from operating activities			
Interest received		5,066,849	7,185,556
Interest payment		(2,231,180)	(2,816,225)
Fees and commission received		2,410,715	3,694,189
Other income		1,615,568	1,581,962
Income tax paid	20(a)	(74,538)	(846,504)
Payment to employees and suppliers		(4,846,776)	(6,336,870)
Cash flows from operating activities before changes in operating assets and liabilities		1,940,638	2,462,108
Changes in operating assets and liabilities:			
Disbursements of loans		(23,623,620)	(23,644,619)
Repayments of loans		20,338,725	23,249,803
(Increase) in other debtors and prepayments		67,194	(822,485)
(Increase) in amounts receivable from shareholder		(1,093,991)	(7,368)
(Decrease) / Increase in other liabilities		(1,996,342)	2,419,600
Net cash (used in)/ generated from operating activities		(4,367,396)	3,657,039
Cash flows from investing activities			
Purchase of property, plant and equipment	17, 18	(284,073)	(983,559)
Purchase of intangible assets	19	-	(412,833)
Net (increase) in investment securities		(61,455)	(1,668,301)
Net (increase) in statutory deposits	16	(876,000)	(909,000)
Net (decrease) in government bonds	12	249,000	(2,810,000)
Net cash (used) in investing activities		(972,528)	(6,783,693)
Cash flows from financing activities			
Net increase in TDB promissory notes		8,378,152	9,331,783
Net increase in savings deposits		9,751,974	9,967,212
Dividends paid		(167,196)	(1,848,433)
Repayment of borrowings		(362,659)	(439,731)
Net cash generated from financing activities		17,600,271	17,010,831
Net increase in cash and cash equivalents		12,260,347	13,884,177
Cash and cash equivalents at beginning of year/ period		35,545,374	21,661,197
Cash and cash equivalents at end of year/ period	11	$ 47,805,721	$ 35,545,374

The above statement of cash flows should be read in conjunction with the accompanying notes.

1 GENERAL INFORMATION

Tonga Development Bank Limited (the "Bank") provides development and selected commercial Banking services in the Kingdom of Tonga.

The Bank was established in the Kingdom of Tonga by the Tonga Development Bank Act 1977 which was replaced by TDB Act 2014, and is incorporated under the Tonga Companies Act 1995. The address of its registered office is at Fatafehi Road, Nuku'alofa, Tonga.

The financial statements were approved for issue by the Directors on 30th August 2017.

2 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

The principal accounting policies applied in the preparation of these financial statements are set out below. These policies have been consistently applied to all the years presented, unless otherwise stated.

(a) Basis of preparation

The Bank's financial statements have been prepared in accordance with International Financial Reporting Standards (IFRS) and requirements of the Tonga Companies Act 1995 and Tonga Development Bank Act 2014. The financial statements have been prepared under the historical cost convention, as modified by the revaluation of available-for-sale financial assets and fair value measurement of certain classes of property, plant and equipment and investment property. The preparation of financial statements in conformity with IFRS requires the use of certain critical accounting estimates. It also requires management to exercise its judgment in the process of applying the Bank's accounting policies. The areas involving a higher degree of judgment or complexity, or areas where assumptions and estimates are significant to the financial statements are disclosed in Note 4.

The bank changed its financial year from 31 December to 30 June during the previous financial period.

(i) New and amended standards adopted by the Bank

There are no IFRSs or IFRIC interpretations that are effective for the first time for the financial period beginning on or after 1 July 2016 that would be expected to have a material impact on the Bank.

(ii) New standards and interpretations not yet adopted

A number of new standards and amendments to standards and interpretations are effective for annual periods beginning after 1 July 2017, and have not been applied in preparing these financial statements. None of these is expected to have a significant effect on the financial statements of the Bank, except the following set out below.

IFRS 9, 'Financial Instruments' – addresses the classification, measurement and recognition of financial assets and financial liabilities. The complete version of IFRS 9 was issued in September 2014. It replaces the guidance in IAS 39 that relates to the classification and measurement of financial instruments. IFRS 9 retains but simplifies the mixed measurement model and establishes three primary measurement categories for financial assets: amortised cost, fair value through other comprehensive income and fair value through profit or loss. The basis of classification depends on the entity's business model and the contractual cash flow characteristics of the financial asset. Investments in equity instruments are required to be measured at fair value through profit or loss with the irrevocable option at inception to present changes in fair value in other comprehensive income not recycling. There is now a new expected credit losses model that replaces the incurred loss impairment model used in IAS 39.

2 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES – CONTINUED

(a) Basis of preparation - continued

(ii) New standards and interpretations not yet adopted - continued

For financial liabilities there were no changes to classification and measurement except for the recognition of changes in own credit risk in other comprehensive income, for liabilities designated at fair value through profit or loss. IFRS 9 relaxes the requirements for hedge effectiveness by replacing the bright line hedge effectiveness tests. It requires an economic relationship between the hedged item and hedging instrument and for the 'hedged ratio' to be the same as the one management actually use for risk management purposes. Contemporaneous documentation is still required but is different to that currently prepared under IAS 39.The standard is effective for accounting periods beginning on or after 1 January 2018. Early adoption is permitted. The Company intends to adopt IFRS 9 on its effective date and has yet to assess its full impact

IFRS 15, 'Revenue from contracts with customers' – This standard deals with revenue recognition and establishes principles for reporting useful information to users of financial statements about the nature, amount, timing and uncertainty of revenue and cash flows arising from an entity's contracts with customers. Revenue is recognised when a customer obtains control of a good or service and thus has the ability to direct the use and obtain the benefits from the good or service. The standard replaces IAS 18 'Revenue' and IAS 11 'Construction contracts' and related interpretations. The standard has an effective date from annual periods beginning on or after 1 January 2018.

IFRS 16, 'Leases' – replaces the current guidance in IAS 17. Under IFRS 16, a contract is, or contains, a lease if the contract conveys the right to control the use of an identified asset for a period of time in exchange for consideration. Under IAS 17, a lessee was required to make a distinction between a finance lease (on balance sheet) and an operating lease (off balance sheet). IFRS 16 now requires a lessee to recognise a lease liability reflecting future lease payments and a 'right-of-use asset' for virtually all lease contracts. Included is an optional exemption for certain short-term leases and leases of low-value assets; however, this exemption can only be applied by lessees. The standard is effective for accounting periods beginning on or after 1 January 2019. Early adoption is permitted but only in conjunction with IFRS 15, 'Revenue from contracts with customers'.

The Bank is yet to assess the impact of the above standards and intends to adopt the standards no later than the accounting period in which it becomes effective.

(b) Segment Reporting

Operating segments are reported in a manner consistent with the internal reporting provided to the chief operating decision-maker. The chief operating decision-maker, who is responsible for allocating resources and assessing performance of the operating segments, has been identified as the Chief Executive Officer and Chief Finance Officer who make strategic decisions.

For segment analysis, refer note 5.

2 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES – CONTINUED

(c) Foreign currency translation

(i) Functional and presentation currency

Items included in the financial statements of the Bank are measured using the currency of the primary economic environment in which the entity operates ('the functional currency').

The financial statements are presented in Tongan Pa'anga, which is the Bank's functional and presentation currency.

(ii) Transactions and balances

Foreign currency transactions are translated into the functional currency using the exchange rates prevailing at the dates of the transactions. Foreign exchange gains and losses resulting from the settlement of such transactions and from the translation at year-end exchange rates of monetary assets and liabilities denominated in foreign currencies are recognised in the statement of profit or loss and other comprehensive income.

(d) Financial assets

The Bank classifies its financial assets in the following categories: loans and receivables, held-to-maturity investments and available-for-sale financial assets. Management determines the classification of its investments at initial recognition.

(i) Loans and receivables

Loans and receivables are non-derivative financial assets with fixed or determinable payments that are not quoted in an active market, other than: (a) those that the entity intends to sell immediately or in the short term, which are classified as held for trading, and those that the entity upon initial recognition designates as at fair value through profit or loss; (b) those that the entity upon initial recognition designates as available for sale; or (c) those for which the holder may not recover substantially all of its initial investment, other than because of credit deterioration.

(ii) Held-to-maturity financial assets

Held-to-maturity investments are non-derivative financial assets with fixed or determinable payments and fixed maturities that the Bank's management has the positive intention and ability to hold to maturity. If the Bank were to sell other than an insignificant amount of held-to-maturity assets, the entire category would be reclassified as available for sale.

2 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES – CONTINUED

(d) Financial assets - continued

(iii) Available-for-sale financial assets

Available-for-sale investments are those intended to be held for an indefinite period of time, which may be sold in response to needs for liquidity or changes in interest rates, exchange rates or equity prices. Regular way purchases and sales of financial assets at fair value through profit or loss, held to maturity and available for sale are recognised on trade-date – the date on which the Bank commits to purchase or sell the asset.

Financial assets are initially recognised at fair value plus transaction costs for all financial assets not carried at fair value through profit or loss. Financial assets carried at fair value through profit and loss are initially recognised at fair value, and transaction costs are expensed in the statement of profit or loss and other comprehensive income. Financial assets are derecognised when the rights to receive cash flows from the financial assets have expired or where the Bank has transferred substantially all risks and rewards of ownership.

Available-for-sale financial assets and financial assets at fair value through profit or loss are subsequently carried at fair value. Loans and receivables and held-to-maturity investments are carried at amortised cost using the effective interest method.

Gains and losses arising from changes in the fair value of the 'financial assets at fair value through profit or loss' category are included in the statement of profit or loss and other comprehensive income in the period in which they arise. Gains and losses arising from changes in the fair value of available-for-sale financial assets are recognised directly in equity, until the financial asset is derecognised or impaired. At this time, the cumulative gain or loss previously recognised in equity is recognised in profit or loss. However, interest calculated using the effective interest method and foreign currency gains and losses on monetary assets classified as available for sale are recognised in the statement of profit or loss and other comprehensive income. Dividends on available-for-sale equity instruments are recognised in the statement of profit or loss and other comprehensive income when the entity's right to receive payment is established.

The fair values of quoted investments in active markets are based on current bid prices. If there is no active market for a financial asset, the Bank establishes fair value using valuation techniques. These include the use of recent arm's length transactions, discounted cash flow analysis, option pricing models and other valuation techniques commonly used by market participants.

(e) Offsetting financial instruments

Financial assets and liabilities are offset and the net amount reported in the balance sheet when there is a legally enforceable right to offset the recognised amounts and there is an intention to settle on a net basis, or realise the asset and settle the liability simultaneously.

2 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES – CONTINUED

(f) Interest income and expense

Interest income and expense for all interest-bearing financial instruments are recognised within 'interest income' and 'interest expense' in the statement of profit or loss and other comprehensive income using the effective interest method.

The effective interest method is a method of calculating the amortised cost of a financial asset or a financial liability and of allocating the interest income or interest expense over the relevant period. The effective interest rate is the rate that exactly discounts estimated future cash payments or receipts through the expected life of the financial instrument or, when appropriate, a shorter period to the net carrying amount of the financial asset or financial liability. When calculating the effective interest rate, the Bank estimates cash flows considering all contractual terms of the financial instrument but does not consider future credit losses.

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

(g) Fee and commission income

Fees and commissions are generally recognised on an accrual basis when the service has been provided. Service fees charged by the Bank for servicing a loan are recognised as revenue as the services are provided. Loan establishment fees are recognised as income in the accounting period in which it is earned rather than received. The amount received is deferred over the term of the financial asset other than the earned amount which is recognised as income in the current accounting period.

Commission and fees arising from negotiating or participating in the negotiation of, a transaction for a third party – such as arrangement or renewal of insurance policies – are recognised on completion of underlying transaction. Performance linked fees or fee components are recognised when the performance criteria are fulfilled.

(h) Impairment of financial assets

Assets carried at amortised cost

The Bank assesses at each balance sheet date whether there is objective evidence that a financial asset or group of financial assets is impaired. A financial asset or a group of financial assets is impaired and impairment losses are incurred only if there is objective evidence of impairment as a result of one or more events that occurred after the initial recognition of the asset (a 'loss event') and that loss event (or events) has an impact on the estimated future cash flows of the financial asset or group of financial assets that can be reliably estimated.

2 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES – CONTINUED

(h) Impairment of financial assets - continued

Assets carried at amortised cost - continued

The criteria that the Bank uses to determine that there is objective evidence of an impairment loss include:

- Delinquency in contractual payments of principal or interest;
- Cash flow difficulties experienced by the borrower;
- Breach of loan covenants or conditions;
- Initiation of legal proceedings;
- Deterioration in the value of collateral.

The estimated period between a loss occurring and its identification is determined by the Bank's management for each identified portfolio. In general, the periods used vary between 3 months and 12 months; in exceptional cases, longer periods are warranted.

The Bank first assesses whether objective evidence of impairment exists individually for financial assets that are individually significant, and individually or collectively for financial assets that are not individually significant. Assets that are individually assessed for impairment and for which an impairment loss is, or continues to be, recognised are not included in a collective assessment of impairment. The assessment normally encompasses collateral held and the anticipated receipts for that individual account.

The amount of the loss is measured as the difference between the asset's carrying amount and the estimated value of collateralised security discounted by the Bank's security values. The carrying amount of the asset is reduced through the use of an allowance account and the amount of the loss is recognised in the statement of profit or loss and other comprehensive income.

When a loan is uncollectible, it is written off against the related provision for loan impairment. Such loans are written off after all the necessary procedures have been completed and the amount of the loss has been determined.

If, in a subsequent period, the amount of the impairment loss decreases and the decrease can be related objectively to an event occurring after the impairment was recognised (such as an improvement in the loans credit rating), the previously recognised impairment loss is reversed by adjusting the doubtful loan account. The amount of the reversal is recognised in the statement of profit or loss and other comprehensive income in impairment charge for loan losses.

(i) Property, plant and equipment

Land and buildings comprise mainly Bank offices located in the Kingdom of Tonga. All property, plant and equipment are stated at cost less depreciation. Cost includes expenditure that is directly attributable to the acquisition of the items.

Subsequent costs are included in the asset's carrying amount or are recognised as a separate asset, as appropriate, only when it is probable that future economic benefits associated with the item will flow to the Bank and the cost of the item can be measured reliably. All other repairs and maintenance are charged to other operating expenses during the financial period in which they are incurred.

2 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES – CONTINUED

(i) Property, plant and equipment - continued

Depreciation is calculated on a straight line basis so as to write off the cost or revalued amount of each property, plant and equipment over its expected useful life. The expected useful life of each asset is as follows:

	Years
Leasehold land	Life of lease
Buildings	25 - 40
Furniture and equipment	8
Library	8
Machines	8
Computers	4
Vehicles	4 - 5

The assets' residual values and useful lives are reviewed, and adjusted if appropriate, at each balance sheet date. Assets that are subject to amortisation are reviewed for impairment whenever events or changes in circumstances indicate that the carrying amount may not be recoverable. An asset's carrying amount is written down immediately to its recoverable amount if the asset's carrying amount is greater than its estimated recoverable amount. The recoverable amount is the higher of the asset's fair value less costs to sell and value in use.

Gains and losses on disposals are determined by comparing proceeds with carrying amount. These are included in the statement of profit or loss and other comprehensive income.

Change in accounting policy

During the year, the measurement basis had changed for the class of assets under leasehold land and buildings from cost method to revaluation method. These are now recognised at fair value based on periodic valuations by external independent valuers, less subsequent depreciation for leasehold land and buildings. A revaluation surplus is credited to asset revaluation reserves in shareholders' equity. All other property, plant and equipment is recognised at historical cost less depreciation.

(j) Investment property

Investment property, principally comprising residential leasehold land and buildings, is held for long term rental yields and is occupied by third parties.

Investment property is shown at cost less subsequent depreciation and impairment. Cost includes expenditure that is directly attributable to the acquisition of the items.

Subsequent costs are included in the asset's carrying amount or recognised as a separate asset, as appropriate, only when it is probable that future economic benefits associated with the item will flow to the Bank and the cost of the item can be measured reliably. All other repairs and maintenance are expensed in the statement of profit or loss and other comprehensive income during the financial period in which they are incurred.

Depreciation is calculated using the straight line method to allocate the cost of each asset to its residual value over its estimated useful life. The estimated useful lives in use are:

	Years
Leasehold land	Term of lease
Buildings - residential	25 – 40

2 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES – CONTINUED

(j) Investment property – continued

Change in accounting policy

During the year, the measurement basis had changed for investment properties from cost method to fair value method. Changes in fair values are presented in profit or loss as fair value gains on investment property. Valuations are performed by professional valuers who hold recognised and relevant professional qualifications and have recent experience in the location and category of the investment property being valued.

If an investment property becomes owner-occupied, it is reclassified as property, plant and equipment. Its fair value at the date of reclassification becomes its cost for subsequent accounting purposes. Investment properties are derecognised when they have been disposed.

Rental income from investment property is recognised in the statement of profit or loss and other comprehensive income on a straight-line basis over the term of the lease.

(k) Intangible assets

Costs incurred to develop and enhance the Bank's computer systems are capitalised to the extent that benefits do not relate solely to revenue that already has been brought to account and will contribute to the future earning capacity of the economic entity. The cost of intangible assets is amortised over the economic life on a straight line basis. The amortisation rate is at 50%. Costs associated with maintaining computer software programs are recognised as an expense when incurred.

(l) Impairment of non-financial asset

Assets that have an indefinite useful life are not subject to amortisation and are tested annually for impairment. Assets that are subject to amortisation are reviewed for impairment whenever events or changes in circumstances indicate that the carrying amount may not be recoverable. An impairment loss is recognised for the amount by which the asset's carrying amount exceeds its recoverable amount. The recoverable amount is the higher of an asset's fair value less costs to sell and value in use. For the purposes of assessing impairment, assets are grouped at the lowest levels for which there are separately identifiable cash flows (cash-generating units). Non-financial assets other than goodwill that suffered impairment are reviewed for possible reversal of the impairment at each reporting date.

(m) Leases

Bank is the lessee

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

2 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES – CONTINUED

(n) Cash and cash equivalents

For the purposes of the statement of cash flows, cash and cash equivalents comprise balances with less than three months' maturity from the date of acquisition, including cash and non-restricted balances with Central Banks, amounts due from other financial institutions and short-term government securities.

(o) Provisions

Provisions are recognised when the Bank has a present legal or constructive obligation as a result of past events, it is more likely than not that an outflow of resources will be required to settle the obligation and the amount has been reliably estimated.

(p) Employee benefits

(i) Employee leave entitlements

Employee entitlements to annual leave are recognised when they accrue to employees. A provision is made for the estimated liability for annual leave as a result of services rendered by employees up to the balance sheet date. Employee entitlements to sick leave and casual leave are not recognised until the time of leave.

(ii) Pension obligations

The Bank makes contributions to the National Retirement Benefit Fund for all permanent employees at a rate of 7.5%. These contributions are charged to the statement of profit or loss and other comprehensive income in the periods to which the contributions relate.

(q) Deferred income tax

Deferred income tax is provided in full, using the liability method, on temporary differences arising between the tax bases of assets and liabilities and their carrying amounts in the financial statements. Deferred income tax is determined using tax rates (and laws) that have been enacted or substantively enacted by the balance sheet date and are expected to apply when the related deferred income tax asset is realised or the deferred income tax liability is settled.

The principal temporary differences arise from depreciation of property, plant and equipment, revaluation of property, plant and equipment, provisions for loan losses, unrealised exchange gains/losses and other provisions for staff entitlements.

The rates enacted or substantively enacted at the balance sheet date are used to determine deferred income tax.

Deferred tax assets are recognised where it is probable that future taxable profit will be available against which the temporary differences can be utilised.

The tax effects of income tax losses available for carry-forward are recognised as an asset when it is probable that future taxable profits will be available against which these losses can be utilised.

2 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES – CONTINUED

(r) Borrowings

Borrowings are recognised initially at fair value 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 statement of profit or loss and other comprehensive income over the period of the borrowings using the effective interest method.

(s) Share capital

Ordinary shares are classified as equity and carried at the Bank's financial statements at par value.

(a) Share issue costs
Incremental costs directly attributable to the issue of new shares or options or to the acquisition of a business are shown in equity as a deduction, net of tax, from the proceeds. No additional shares were issued during the financial period.

(b) Dividends on ordinary shares
Dividends on ordinary shares are recognised in equity in the period in which they are approved by the Bank's shareholders.

Dividends for the period that are declared before the balance sheet date are dealt with in the statement of changes in equity.

(t) Reserves

The asset revaluation reserve records increments and decrements on revaluation of leasehold land and buildings.

(u) Earnings per share

Basic earnings/loss per share is determined by dividing the profit after tax by the weighted average number of ordinary shares outstanding during the financial period

(v) Fiduciary activities

Assets and income arising thereon together with related undertakings to return such assets to third parties or customers are excluded from these financial statements where the Bank acts in a fiduciary capacity.

(w) Comparatives

Current year results are for the year ended 30 June 2017, while the comparative is for the 18 months period ended 30 June 2016.

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

(x) Rounding

Amounts have been rounded to the nearest dollar except where otherwise noted.

3 FINANCIAL RISK MANAGEMENT

The Bank's activities expose it to a variety of financial risks and those activities involve the analysis, evaluation, acceptance and management of some degree of risk or combination of risks. Taking risk is core to the development banking business. The Bank's aim is therefore to achieve an appropriate balance between risk and return and minimise potential adverse effects on the Bank's financial performance.

The Bank's risk management policies are designed to identify and analyse these risks, to set appropriate risk limits and controls, and to monitor the risks and adherence to limits by means of reliable and up-to-date information systems. The Bank regularly reviews its risk management policies and systems to reflect changes in markets, products and emerging best practice.

Risk management is carried out by a Risk Management department under policies approved by the Board of Directors and prudential guidelines issued by the National Reserve Bank of Tonga. Bank Treasury identifies and evaluates financial risks in close co-operation with the Bank's operating units. The Board provides written principles for overall risk management, as well as written policies covering specific areas, such as foreign exchange risk, interest rate risk and credit risk. In addition, internal audit is responsible for the independent review of risk management and the control environment. The most important types of risk are credit risk, liquidity risk, market risk and other operational risk. Market risk includes currency risk and interest rate risk.

3.1 Credit risk

The Bank takes on exposure to credit risk, which is the risk that a counterparty will cause a financial loss for the Bank by failing to discharge an obligation. Credit risk is the most important risk for the Bank's business; management therefore carefully manages its exposure to credit risk. Credit exposures arise principally in lending activities that lead to loans and advances, and investment activities that bring debt securities into the Bank's asset portfolio. There is also credit risk in off-balance sheet financial instruments, such as loan commitments. The credit risk management and control are centralised in the credit risk management team and reported to the Board of Directors and Assets and Liabilities Committee regularly.

3 FINANCIAL RISK MANAGEMENT – CONTINUED

3.1 Credit risk - continued

(a) Loans and advances

In measuring credit risk of loans and advances to customers and to Banks at a counterparty level, the Bank reflects three components (i) the 'probability of default' by the client or counterparty on its contractual obligations; (ii) current exposures to the counterparty and its likely future development, from which the Bank derive the 'exposure at default'; and (iii) the likely recovery ratio on the defaulted obligations (the 'loss given default').

These credit risk measurements are embedded in the Bank's daily operational management.

(i) The Bank assesses the probability of default of individual counterparties using internal rating tools tailored to the various categories of counterparty. They have been developed internally and are also based on prudential guidelines issued by National Reserve Bank of Tonga. The Bank clients are segmented into seven rating classes. The Bank's rating scale, which is shown below, reflects the range of default probabilities defined for each rating class. The rating tools are kept under review and upgraded as necessary.

Bank's Ratings	Description of the grade
A	Customers with well conducted loans, fully secured and operational & financial stability.
B	Accounts where arrangements are generally observed but lending is not considered at risk, a minor degree of concern during general economic pressures, reasonable financial condition and adequate security.
C1	Fully productive accounts but not generating sufficient income to meet repayment, repayments from other sources may be required, partial or full security and arrears may occur for up to 3 months.
S	Special mention will be a loan in excess of $250,000 and current rating will be A, B, or C1; moved into arrears of 30 to 60 days and requires special attention and monitoring, repayment difficulties and showing high degree of risk.
C2	Accounts of doubtful quality requiring active management supervision, projects have failed, arrears between 3 to 6 months and no financial data.
D	Sub standard and doubtful customers whose loans have been classified non-accrual and partial loss of interest and fee is expected, doubt about ability to service the debt; realisable value of security is insufficient to cover principal and interest, breach of repayment arrangements and accounts in arrears over 6 months.
E	Loss of principal and interest is expected, accounts under legal action and accounts may be written off if no improvements over 12 months.

3.2 Risk limit control and mitigation policies

The Bank manages limits and controls concentrations of credit risk wherever they are identified – in particular, to individual counterparties and Banks, and to industries.

The Bank structures the levels of credit risk it undertakes by placing limits on the amount of risk accepted in relation to one borrower, or groups of borrowers, and to industry segments. Such risks are monitored on a revolving basis and subject to an annual or more frequent review, when considered necessary. Limits on the level of credit risk by product and industry sector's are approved by the Board of Directors.

Exposure to credit risk is also managed through regular analysis of the ability of borrowers and potential borrowers to meet interest and capital repayment obligations and by changing these lending limits where appropriate.

3 FINANCIAL RISK MANAGEMENT – CONTINUED

3.2 Risk limit control and mitigation policies - continued

Some other specific control and mitigation measures are outlined below.

(a) Collateral

The Bank employs a range of policies and practices to mitigate credit risk. The most traditional of these is the taking of security for funds advances, which is common practice. The Bank implements guidelines on the acceptability of specific classes of collateral or credit risk mitigation. The principal collateral types for loans and advances are:

- Mortgages over residential and commercial properties;
- Charges over business assets such as premises, inventory and accounts receivable;
- Guarantees by the shareholders/directors; and
- Charges over financial instruments such as debt securities and equities.

In order to minimise the credit loss the Bank will seek additional collateral from the counterparty as soon as impairment indicators are noticed for the relevant individual loans and advances or will seek to increase repayments.

3.3 Impairment and provisioning policies

The internal rating systems described in Note 3.1 focus more on credit-quality mapping from the inception of the lending. In contrast, impairment provisions are recognised for financial reporting purposes only for losses that have been incurred at the balance sheet date based on objective evidence of impairment.

The impairment provision shown in the balance sheet at year end is derived from each of the seven internal rating grades. The table below shows the percentage of the Bank's balances relating to loans and advances and the associated impairment provision for each of the Banks' internal rating categories:

Bank's rating	30 June 2017		30 June 2016	
	Loans and Advances (%)	Impairment Provision (%)	Loans and Advances (%)	Impairment Provision (%)
A	13.54	-	13.81	-
B	18.99	-	24.02	-
C1	61.28	36.03	43.33	23.91
S	-	-	10.01	5.52
C2	4.92	36.78	7.31	40.34
D	0.81	12.58	0.84	11.54
E	0.46	14.61	0.68	18.69
	100.00	100.00	100.00	100.00

3 FINANCIAL RISK MANAGEMENT – CONTINUED

3.3 Impairment and provisioning policies - continued

The internal rating tool assists management to determine whether objective evidence of impairment exists, based on the following criteria set out by the Bank:

- Delinquency in contractual payments of principal or interest;
- Cash flow difficulties experienced by the borrower;
- Breach of loan covenants or conditions;
- Initiation of legal proceedings;
- Deterioration of the borrower's competitive position;
- Deterioration in the value of collateral; and
- Downgrading below C1 grade level.

The Bank's policy requires the review of individual financial assets based on the Bank's guidelines at least annually or more regularly when individual circumstances require. Impairment allowances on individually assessed accounts are determined by an evaluation of the incurred loss at balance-sheet date on a case-by-case basis, and are applied to all individually significant accounts. The assessment normally encompasses collateral held (including re-confirmation of its enforceability) and the anticipated receipts for that individual account.

3.4 Maximum exposure to credit risk before collateral held as categorised by the industry sectors:

	30 June 2017 $	%	30 June 2016 $	%
Industry sector:				
Agriculture	5,187,617	8.49	4,303,120	8.16
Industry and Business	32,084,507	52.48	21,666,026	41.11
Housing and Personal	21,092,630	34.50	24,394,075	46.29
Staff	2,771,206	4.53	2,330,981	4.44
	61,135,960	100.00	52,694,202	100.00

Management is confident in its ability to continue to control and sustain minimal exposure of credit risk to the Bank resulting from its loan and advances portfolio based on the following:

- Mortgage loans, which represent the biggest group in the portfolio, are backed by collateral;
- Risk assessment review by the Manager Risk Management; and
- The Bank has a stringent selection process before granting loans and advances.

3 FINANCIAL RISK MANAGEMENT – CONTINUED

3.5 Loans and advances

(i) Loans and advances are summarised as follows:

	Agriculture	Industry & Business	Housing & personal	Staff	Total
	$	$	$	$	$
As at 30 June 2017					
Neither past due nor impaired	4,685,696	29,867,966	20,033,247	2,762,572	57,349,481
Past due but not impaired	180,634	1,963,175	866,515	-	3,010,324
Individually impaired	321,287	253,366	192,868	8,634	776,155
Gross	5,187,617	32,084,507	21,092,630	2,771,206	61,135,960
Less: allowance for impairment	(358,303)	(1,023,264)	(548,266)	(31,596)	(1,961,429)
Net	$ 4,829,314	$31,061,243	$20,544,364	$ 2,739,610	$ 59,174,531

	Agriculture	Industry & Business	Housing & personal	Staff	Total
	$	$	$	$	$
As at 30 June 2016					
Neither past due nor impaired	3,814,778	13,903,308	23,267,329	2,322,705	43,308,120
Past due but not impaired	154,689	7,551,825	902,240	-	8,608,754
Individually impaired	333,653	210,893	224,506	8,276	777,328
Gross	4,303,120	21,666,026	24,394,075	2,330,981	52,694,202
Less: allowance for impairment	(193,302)	(891,817)	(724,211)	(3,840)	(1,813,170)
Net	$ 4,109,818	$20,774,209	$23,669,864	$ 2,327,141	$ 50,881,032

The total impairment provision for loans and advances is specific provision based on review of all specific individual accounts in the past due but not impaired and individually impaired categories, and group provisions based on the portfolio balance of risk rating groupings for all loans that are not specifically provisioned. These accounts are subject to regular monitoring by the Bank.

3 FINANCIAL RISK MANAGEMENT – CONTINUED

3.5 Loans and advances – continued

(ii) Loans and advances neither past due nor impaired are summarised as follows:

The credit quality of the portfolio of loans and advances that were neither past due nor impaired can be assessed by reference to the internal rating system adopted by the Bank.

	Agriculture	Industry & Business	Housing & personal	Staff	Total
	$	$	$	$	$
As at 30 June 2017					
Grades					
A	156,726	5,908,822	1,847,308	364,447	8,277,303
B	264,244	4,820,909	5,190,067	1,335,297	11,610,517
C1	4,264,726	19,138,235	12,995,872	1,062,828	37,461,661
S	-	-	-	-	-
	$ 4,685,696	$ 29,867,966	$20,033,247	$ 2,762,572	$57,349,481

	Agriculture	Industry & Business	Housing & personal	Staff	Total
	$	$	$	$	$
As at 30 June 2016					
Grades					
A	268,625	4,843,721	7,927,278	304,431	13,344,055
B	106,710	1,585,549	5,991,305	1,435,798	9,119,362
C1	3,439,443	2,385,549	9,348,746	582,476	15,756,214
S	-	5,088,489	-	-	5,088,489
	$ 3,814,778	$ 13,903,308	$23,267,329	$23,322,705	$43,308,120

(iii) Loans and advances past due but not impaired are summarised as follows:

Loans and advances less than 90 days past due are not considered impaired, unless other information is available to indicate the contrary. Gross amount of loans and advances by class to customers that were past due but not impaired were as follows:

	Agriculture	Industry & Business	Housing & personal	Staff	Total
	$	$	$	$	$
As at 30 June 2017					
Past due up to 30 days	162,278	1,957,469	736,382	-	2,856,129
Past due 30 – 60 days	118	5,706	19,081	-	24,905
Past due 60 – 90 days	18,238	-	111,052	-	129,290
	$ 180,634	1,963,175	866,515	-	3,010,324
Fair value of collateral	$ 5,786,751	$ 8,794,458	$ 1,877,405	-	$ 16,458,614

3 FINANCIAL RISK MANAGEMENT – CONTINUED

3.5 Loans and advances – continued

(iii) *Loans and advances past due but not impaired are summarised as follows (continued):*

	Agriculture	Industry & Business	Housing & personal	Staff	Total
	$	$	$	$	$
As at 30 June 2016					
Past due up to 30 days	134,028	6,575,403	403,427	-	7,112,858
Past due 30 – 60 days	20,661	-	151,514	-	172,175
Past due 60 – 90 days	-	976,422	347,299	-	1,323,721
	$ 154,689	$ 7,551,825	$ 902,240	$ -	$ 8,608,754
Fair value of collateral	$ 1,790,330	$ 8,944,984	$ 3,372,072	-	$ 14,107,386

(iv) Loans and advances renegotiated

Restructuring activities include extended payment arrangements, approved external management plans, modification and deferral of payments. Following restructuring, a previously overdue customer account is reset to a normal status and managed together with other similar accounts. Restructuring policies and practices are based on indicators or criteria which, in the judgement of management, indicate that payment will most likely continue. These policies are kept under continuous review.

Renegotiated loans that would otherwise be past due or impaired are as follows:

	Agriculture	Industry & Business	Housing & personal	Staff	Total
	$	$	$	$	$
As at 30 June 2017					
Term loans	1,538,430	10,982,065	3,597,676	333,288	16,451,459
As at 30 June 2016					
Term loans	643,030	2,897,399	1,126,746	8,276	4,675,451

(v) Repossessed collateral

During the period, the Bank obtained assets by taking possession of collateral held as security, as follows:

Nature of assets	Carrying amount 30 June 2017	30 June 2016
	$	$
Land - tax allotment	2,489,490	3,035,000

Repossessed properties are sold as soon as practicable, with the proceeds used to reduce the outstanding indebtedness.

3 FINANCIAL RISK MANAGEMENT – CONTINUED

3.5 Loans and advances - continued

(vi) Loans and advance exposure by categories:	30 June 2017 $	30 June 2016 $
Large corporate entities	28,412,188	19,144,385
SMEs	27,283,633	29,631,308
Other	5,440,139	3,918,509
	$ 61,135,960	$ 52,694,202

3.6 Market risk

The Bank takes on exposure to market risks, which is the risk that the fair value or future cash flows of financial instruments will fluctuate because of changes in market prices. Market risks arise from open positions in interest rate and currency, all of which are exposed to general and specific market movements and changes in the level of volatility of market rates or prices such as interest rates, credit spreads and foreign exchange rates.

3.6.1 Foreign exchange risk

The Bank takes on exposure to the effects of fluctuations in the prevailing foreign currency exchange rates on its financial position and cash flows. The Bank's risk management policy is designed to identify situations requiring active management and also to enable the Bank to develop strategies for managing foreign exchange exposure.

The Bank's assets and liabilities are mainly in local currency except to the extent shown below:

	30 June 2017 $	30 June 2016 $
Assets		
Due from other financial institutions	$ 521,914	$ 305,474
Liabilities		
Borrowings – foreign	$ 1,794,775	$ 1,819,905

3.6.2 Interest rate risk

The Bank takes on exposure due to the effects of fluctuations in the prevailing levels of market interest rates on its financial position and cash flows. Interest margins may increase or decrease as a result of such changes. The Bank monitors the level of interest rate risk on a quarterly basis. Interest rates are reviewed annually or earlier if warranted.

3.7 Liquidity risk

Liquidity risk is the risk that the Bank is unable to meet its payment obligations associated with its financial liabilities when they fall due and to replace funds when they are withdrawn. The consequence may be the failure to meet obligations to repay depositors and fulfil commitments to lend.

The Bank is exposed to daily calls on its available cash resources from current accounts, maturing deposits and loan draw downs. The Bank does not maintain cash resources to meet all of these needs as experience shows that a minimum level of reinvestment of maturing funds can be predicted with a high level of certainty. The Bank monitors the level of liquidity on a daily basis.

The table on next page analyses assets and liabilities into relevant maturity groupings based on the remaining period at balance sheet date to the contractual maturity date.

3 FINANCIAL RISK MANAGEMENT – CONTINUED

3.7 Liquidity risk - continued

	Up to 1 month	2 - 3 months	4 - 12 months	2 - 5 years	Over 5 years	No specific maturity	Total
As at 30 June 2017	$	$	$	$	$	$	$
Assets							
Cash on hand and at bank	47,283,807	-	-	-	-	-	47,283,807
Due from other financial institutions	521,914	-	-	-	-	-	521,914
Investment securities- held to maturity	-	-	1,574,927	6,013,830	-	-	7,588,757
Loans and advances	6,323,442	4,836,611	15,158,057	32,856,421	-	-	59,174,531
Statutory reserve deposit	-	-	-	-	-	4,645,000	4,645,000
Property, plant and equipment	-	-	-	-	-	9,784,803	9,784,803
Investment property	-	-	-	-	-	200,000	200,000
Intangible assets	-	-	-	-	-	-	-
Other assets	2,165,835	31,444	64,073	57,441	694,995	1,771	3 015,559
Total assets	56,294,998	4,868,055	16,797,057	38,927,692	694,995	14,631,574	132,214,371
Liabilities							
Saving deposits	30,607,057	-	-	-	-	-	30,607,057
Borrowings	95,359	43,687	354,280	1,520,140	1,284,449	-	3,297,915
Promissory notes	1,996,434	5,844,840	14,889,329	21,032,643	18,395,279	-	62,158,525
TDB bonds	-	-	-	-	-	-	-
Other liabilities	897,581	876,047	1,063,152	8,058,063	412,439	-	11,307,282
Total liabilities	33,596,431	6,764,574	16,306,761	30,610,846	20,092,167	-	107,370,779
Net liquidity gap	$ 22,698,567	($ 1,896,519)	$ 490,296	$ 8,316,846	($ 19,397,172)	$ 14,631,574	$ 24,843,592
As at 30 June 2016							
Total Assets	37,987,996	4,496,794	13,433,774	24,943,522	15,281,121	11,227,833	107,371,040
Total Liabilities	25,413,515	9,517,015	7,648,657	29,347,867	14,527,593	-	86,454,647
Net Liquidity Gap	$ 12,574,481	($ 5,020,221)	$ 5,785,117	($ 4,404,345)	$ 753,528	$ 11,227,833	$ 20,916,393

3 FINANCIAL RISK MANAGEMENT – CONTINUED

3.8 Off-balance sheet items

(a) Loan commitments
The dates of the contractual amounts of the Bank's off-balance sheet financial instruments that commit it to extend credit to customers and other facilities, are summarised in the table below.

(b) Operating lease commitments
Where the Bank is the lessee, the future minimum lease payments under non-cancellable operating leases, as disclosed in note 26, are summarised in the table below.

(c) Capital commitments
Capital commitments (note 26) are summarised in the table below.

	No later than 1 year	**1 – 5 years**	**Over 5 years**	**Total**
	$	$	$	$
At 30 June 2017				
Loan commitments	6,264,460	-	-	6,264,460
Operating lease commitments	8,320	33,280	138,673	180,273
Capital commitments	1,312,000	-	-	1,312,000
Total	$ 7,584,780	$ 33,280	$ 138,673	$ 7,756,733
At 30 June 2016				
Loan commitments	3,900,325	-	-	3,900,325
Operating lease commitments	8,320	33,280	147,000	188,600
Capital commitments	-	-	-	-
Total	$ 3,908,645	$ 33,280	$ 147,000	$ 4,088,925

3.9 Fair value of financial assets and liabilities

The fair value is the amount for which an asset could be exchanged, or a liability settled between knowledgeable, willing parties in an arm's length transaction.

The valuation of the Bank's financial assets and liabilities is discussed below:

(i) Term deposits
The carrying values of term deposits are considered to approximate their fair values as they are denominated in cash and these amounts are repayable on demand.

(ii) Investment securities
Investment securities comprise interest bearing bonds which are being held to maturity. The fair value of the investment securities of $5,859,000 (30 June 2016: $6,108,000) is based on the indicative pricing using the prevailing interest rates.

(iii) Loans and advances to customers
Loans and advances are net of provisions for impairment. The carrying values of loans and advances are considered to approximate their fair values as all doubtful accounts have been provided for.

(iv) Savings deposits
The carrying values of savings deposits are considered to approximate their fair values as they are repayable on demand.

3 FINANCIAL RISK MANAGEMENT – CONTINUED

3.9 Fair value of financial assets and liabilities – continued

(v) Borrowings
The carrying values of borrowings are considered to approximate their fair value as they are repayable on demand.

(vi) Other financial assets and liabilities
The reported values of other financial assets and liabilities are considered to be their fair value.

3.10 Capital management

The Bank's objectives when managing capital are:

- To comply with the capital requirements set by the regulators of the Banking markets where the Bank operates;
- To safeguard the Bank's ability to continue as a going concern so that it can continue to provide returns for shareholders and benefits for other stakeholders; and
- To maintain a strong capital base to support the development of its business.

Capital adequacy and the use of regulatory capital are monitored daily by the Bank's management, based on the guidelines developed by the National Reserve Bank of Tonga (NRBT), for supervisory purposes. The required information is filed with the NRBT on a quarterly basis.

The NRBT requires the Bank to: (a) hold the minimum level of regulatory capital, and (b) maintain a ratio of total regulatory capital to the risk-weighted asset at or above the agreed minimum of 18%.

The Bank's regulatory capital as managed by its Treasury comprises of:

- Tier 1 capital: share capital, retained earnings and reserves created by appropriations of retained earnings.

The risk-weighted assets are measured by means of a hierarchy of five risk weights classified according to the nature of and reflecting an estimate of credit, market and other risks associated with each asset and counterparty, taking into account any eligible collateral or guarantees. A similar treatment is adopted for off-balance sheet exposure, with some adjustments to reflect the more contingent nature of the potential losses.

The table below summarises the composition of regulatory capital and the ratios of the Bank for the year ended 30 June 2017 and for the period ended 30 June 2016. During that period, the Bank complied with all of the externally imposed capital requirements to which they are subject.

Tier 1 Capital	30 June 2017 $	30 June 2016 $
Share capital	14,000,000	14,000,000
Retained earnings	8,357,057	6,916,393
Total	$ 22,357,057	$ 20,916,393
Risk weighted assets	$ 59,174,531	$ 50,881,032
Ratio	37.78%	41.10%

4 CRITICAL ACCOUNTING ESTIMATES AND JUDGMENTS

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 based on historical experience and other factors, including expectations of future events that are believed to be reasonable under the circumstances.

Impairment losses on loans and advances

The Bank reviews its loan portfolios to assess impairment at least on a quarterly basis. In determining whether an impairment loss should be recorded in the statement of profit or loss and other comprehensive income, the Bank makes judgments as to whether there is any observable data indicating that there is a measurable decrease in the estimated values of collateralised security values. This evidence may include observable data indicating that there has been an adverse change in the payment status of borrowers, or local economic conditions that correlate with defaults on assets in the industry sectors. The methodology and assumptions used for reviewing impairment are reviewed regularly.

Property valuations

Leasehold land and buildings held under investment property and property, plant and building had been revalued during the current financial year. The market values have been arrived at on the basis of the valuations carried out by Landcare Solutions Limited, independent valuers not related to the bank. The valuers have appropriate qualifications and recent experience in the valuation of properties in Tonga. The valuation was arrived at by reference to finding recent comparable transactions for sale of similar property. A limitation in performing the valuation was inconsistency in identifying true market value since there was limited information for the land market, and non-existence of the town planning zoning.

5 SEGMENT ANALYSIS

Industry segment

The Bank operates predominantly in the financial services industry.

Geographical segment

The Bank operates in Tonga and is, therefore, one geographical area for reporting purposes.

6 NET INTEREST INCOME

	Year ended 30 June 2017 $	18 months ended 30 June 2016 $
Interest income		
Loans and advances	4,811,116	6,919,911
Term deposits and securities	253,955	266,539
	$ 5,065,071	$ 7,186,450
Interest and other borrowing expenses		
Borrowings	53,877	106,728
TDB promissory notes	2,104,155	2,609,431
Savings deposits	245,990	261,667
Bank charges	17,515	1,387
	$ 2,421,537	$ 2,979,213

7 FEES AND COMMISSION INCOME

	Notes	Year ended 30 June 2017 $	18 months ended 30 June 2016 $
Service fees		2,227,790	3,497,080
Commissions		182,925	197,109
		$ 2,410,715	$ 3,694,189

8 OTHER OPERATING INCOME

	Notes	Year ended 30 June 2017 $	18 months ended 30 June 2016 $
Rent		127,905	303,643
Net foreign exchange fees and earnings		656,188	413,449
Other	(a)	831,475	787,250
		$ 1,615,568	$ 1,504,342

(a) Other operating income includes the following:

	2017	2016
Cost of operations and government policy obligations	459,000	688,500
BSP agency agreement fee	-	55,000
Government development loan managed fees	286,058	-
Other income	76,122	43,750
Gain on sale of property, plant & equipment	10,295	-
	$ 831,475	$ 787,250

9 OTHER OPERATING EXPENSES

	Notes	Year ended 30 June 2017 $	18 months ended 30 June 2016 $
Staff costs	(a)	2,946,406	3,839,444
Administrative expenses		1,094,472	1,396,969
Amortisation expense		294,582	118,251
Auditor's remuneration – audit fee		26,370	33,000
Depreciation - Property, plant and equipment		675,628	841,242
- Investment property		41,353	62,100
Premises		365,828	397,002
Travel		209,992	301,211
Others	(b)	329,934	369,243
		$ 5,984,565	$ 7,358,462

(a) Staff costs comprise:

	2017	2016
Wages and salaries and other staff costs	2,733,160	3,544,318
Retirement fund	213,246	295,126
	$ 2,946,406	$ 3,839,444

(b) Others include:

	2017	2016
Staff training	52,063	72,078
Bad debts	80,000	80,000
Director fees	148,196	155,732
Others	49,675	61,433
	$ 329,934	$ 369,243

9 **OTHER OPERATING EXPENSES – CONTINUED**

The Bank makes contributions to the National Retirement Benefit Fund for all permanent employees at a rate of 7.5%.

10 **CASH ON HAND AND AT BANK**

	30 June 2017 $	30 June 2016 $
Cash on hand	2,295,281	5,682,288
Cash at bank	44,988,526	29,557,612
	$ 47,283,807	$ 35,239,900

11 **CASH AND CASH EQUIVALENTS**

For the purposes of the statement of cash flows, cash and cash equivalents comprise the following:

	30 June 2017 $	30 June 2016 $
Cash on hand and at bank	47,283,807	35,239,900
Due from other financial institutions	521,914	305,474
Investment securities	-	-
	$ 47,805,721	$ 35,545,374

Mandatory reserve deposits are not available for use in the Bank's day-to-day operations. Cash on hand, balances with the reserve bank and mandatory reserve deposits are non-interest-bearing. Other money-market placements are floating-rate assets.

12 **INVESTMENT SECURITIES – HELD TO MATURITY**

	30 June 2017 $	30 June 2016 $
BSP Bank	574,830	556,281
ANZ Bank	451,455	447,428
MBF Bank	703,472	664,593
Government of Tonga Local Development Bonds	5,859,000	6,108,000
	$ 7,588,757	$ 7,776,302

The year ended 30 June 2017 interest rate receivable on term deposits range from 1.0% to 5.0% (Period ended 30 June 2016: 1.0% to 6.5%per annum) and the interest rate for the Government of Tonga Local Development Bond range from 3.0% to 4.0% (Period ended 30 June 2016: 3.0% to 4.0% per annum).

The interest is receivable on maturity for term deposits and annually after one year from the date of issue for the Government of Tonga Local Development Bonds.

13 LOANS AND ADVANCES

	30 June 2017 $	30 June 2016 $
Gross loans and advances	61,135,960	52,694,202
Less: Allowance for losses on loans and advances	(1,961,429)	(1,813,170)
Net loans	$ 59,174,531	$ 50,881,032
Loans and advances approved but not yet disbursed amounted to	$ 6,264,460	$ 3,900,325

Allowance for losses on loans and advances:

Movements in allowance for losses on loans and advances are as follows:

	30 June 2017 $	30 June 2016 $
Balance at beginning of the year/ period	1,813,170	2,304,612
Provision for loan impairment	270,150	998,690
Provisions written back	(40,262)	(1,186,207)
Loans written off during the year/ period	(81,629)	(303,925)
Balance at end of year/ period	$ 1,961,429	$ 1,813,170

	30 June 2017 $	30 June 2016 $
Composition of allowance for losses on loans and advances:		
Specific provisions	843,671	777,503
Collective provisions	1,117,758	1,035,667
	$ 1,961,429	$ 1,813,170

The losses on loans and advances as shown in the statement of profit or loss and other comprehensive income is arrived as follows:

	30 June 2017 $	30 June 2016 $
Provision for loan impairment	270,150	998,690
Provisions written back	(40,262)	(1,186,207)
	$ 229,888	($ 187,517)

Non accrual loans and advances

	30 June 2017 $	30 June 2016 $
Non accrual loans and advances	3,452,632	3,534,686
Less: specific provision for impairment	(819,397)	(1,032,833)
	$ 2,633,235	$ 2,501,853

Loans to directors and director related entities are disclosed in note 25 (a) (iii).

13 LOANS AND ADVANCES – CONTINUED

The directors have adopted of a collective provisioning policy based on the existing internal credit risk rating system. The following percentages are assigned to each loan grade for the purposes of assessing collective provisions for those assets that share similar credit risk characteristics, and for which no specific provisions are made:

Grade	% for collective provisions
A	-
B	-
C1	2%
S	2%
C2	20%
D	50%
E	100%

14 OTHER ASSETS

	30 June 2017 $	30 June 2016 $
Prepayments	805,980	640,183
Accrued interests	103,301	105,079
Other assets	306,346	539,337
	$ 1,215,627	$ 1,284,599

Other assets include the following:		
Robbery recovery	56,941	56,941
Lawyers suspense	59,709	59,709
Digicel mobile money receivable	140,392	229,118
Others	49,304	193,569
	$ 306,346	$ 539,337

15 AMOUNTS RECEIVABLE FROM SHAREHOLDER

Comprises the following:	30 June 2017	30 June 2016
Claims for EEC	18,799	10,946
Interest receivable on Tonga Forest Product Limited loan	942,694	-
PPSA & mortgage fees – government development loan	6,738	-
Managed fund LPCI	136,706	-
	$ 1,104,937	$ 10,946

16 STATUTORY RESERVE DEPOSIT

	30 June 2017	30 June 2016
National Reserve Bank of Tonga (NRBT)	$ 4,645,000	$ 3,758,000
	===========	===========

The Statutory Reserve Deposit with National Reserve Bank of Tonga (NRBT) is not available for use in the Bank's day to day operations. The Statutory Reserve Deposit rate at 30 June 2017 was 5% (30 June 2016: 5%).

	30 June 2017	30 June 2016
Amounts payable to NRBT	($ 111,000)	($ 100,000)
	===========	===========

Amounts receivable from/(payable to) NRBT represent surplus/(shortfall) in the statutory reserve deposit at year end.

17 PROPERTY, PLANT AND EQUIPMENT

	Leasehold Land and Buildings	Fixtures, fittings and equipment	Motor vehicles	Computers	Total
	$	$	$	$	$
At 1 January 2015					
Cost	7,333,485	1,005,062	661,215	2,761,143	11,760,905
Accumulated depreciation	(1,508,170)	(859,616)	(498,426)	(2,296,876)	(5,163,088)
Net book amount	$ 5,825,315	$ 145,446	$ 162,789	$ 464,267	$ 6,597,817
For the 18 months ended 30 June 2016					
Opening net book amount	5,825,315	145,446	162,789	464,267	6,597,817
Additions	275,673	75,246	70,105	561,155	982,179
Disposals	-	-	-	-	-
Depreciation charge	(314,326)	(72,999)	(112,020)	(341,897)	(841,242)
Closing net book amount	$ 5,786,662	$ 147,693	$ 120,874	$ 683,525	$ 6,738,754
At 30 June 2016					
Cost	7,609,158	1,080,308	731,320	3,322,298	12,743,084
Accumulated depreciation	(1,822,496)	(932,615)	(610,446)	(2,638,773)	(6,004,330)
Net book amount	$ 5,786,662	$ 147,693	$ 120,874	$ 683,525	$ 6,738,754
For the year ended 30 June 2017					
Opening net book amount	5,786,662	147,693	120,874	683,525	6,738,754
Additions	12,988	47,405	-	223,680	284,073
Revaluation surplus	2,486,535	-	-	-	2,486,535
Transfer from investment property at fair value	950,000	-	-	-	950,000
Transfers from investment property	-	2,105	-	-	2,105
Transfers	(82,588)	81,552	-	-	(1,036)
Disposals	-	-	-	-	-
Depreciation charge	(218,597)	(72,449)	(59,032)	(325,550)	(675,628)
Closing net book amount	$ 8,935,000	$ 206,306	$ 61,842	$ 581,655	$ 9,784,803
At 30 June 2017					
Cost or fair value	8,935,000	1,211,370	653,334	2,854,354	13,654,058
Accumulated depreciation	-	(1,005,064)	(591,492)	(2,272,699)	(3,869,255)
Net book amount	$ 8,935,000	$ 206,306	$ 61,842	$ 581,655	$ 9,784,803

The accounting policy adopted in respect of the above is set out in Note 2 (i).

18 INVESTMENT PROPERTY

	Land and Building $	Total $
At 1 January 2015		
Cost	829,248	829,248
Accumulated depreciation	(332,031)	(332,031)
Net book amount	$ 497,217	$ 497,217
For the 18 months ended 30 June 2016		
Opening net book amount	497,217	497,217
Additions	1,380	1,380
Disposals	-	-
Depreciation charge	(62,100)	(62,100)
Closing net book amount	$ 436,497	$ 436,497
At 30 June 2016		
Cost	830,628	830,628
Accumulated depreciation	(394,131)	(394,131)
Net book amount	$ 436,497	$ 436,497
For the year ended 30 June 2017		
Opening net book amount	436,497	436,497
Additions	-	-
Disposals	-	-
Fair value gains on revaluation	756,961	756,961
Depreciation charge	(41,353)	(41,353)
Transfer to property, plant and equipment	(952,105)	(952,105)
Closing net book amount	$ 200,000	$ 200,000
At 30 June 2017		
Fair value of investment property	$ 200,000	$ 200,000

(a) The accounting policy adopted in respect of the above is set out in Note 2 (j).

(b) The following amounts have been recognised in the statement of profit or loss and other comprehensive income:

	Year ended 30 June 2017 $	18 months ended 30 June 2016 $
Rental income	12,741	57,595
Direct operating expenses arising from investment properties	30,996	21,120
Fair value gains on investment property	756,961	-

19 INTANGIBLE ASSETS

	Computer Systems $	Total $
For the year ended 30 June 2016		
Opening net book amount	-	-
Additions	412,833	412,833
Disposals	-	-
Amortisation charge	(118,251)	(118,251)
Closing net book amount	$ 294,582	$ 294,582
At 30 June 2016		
Cost	412,833	412,833
Accumulated amortisation	(118,251)	(118,251)
Net book amount	$ 294,582	$ 294,582
For the year ended 30 June 2017		
Opening net book amount	294,582	294,582
Additions	-	-
Disposals	-	-
Amortisation charge	(294,582)	(294,582)
Closing net book amount	$ -	$ -
At 30 June 2017		
Cost	294,582	294,582
Accumulated amortisation	(294,582)	(294,582)
Net book amount	$ -	$ -

The amortisation policy adopted in respect of the above is set out in Note 2 (k).

20 TAXATION

	Year ended 30 June 2017 $	18 months ended 30 June 2016 $
Income tax is brought to account using the liability method of tax effect accounting.		
(a) Operating profit before income tax	1,298,567	2,337,207
Prima facie income tax charge on the operating profit at 25%	324,642	584,302
Tax effect of non-deductible expenditure:		
Grant exempt income	(66,955)	(42,781)
Deferred tax liability reversed	(399,784)	-
Income tax (benefit)/ expense	(142,097)	541,521
Temporary differences –deferred tax	449,831	(129,741)
	307,734	411,780
Add: opening current tax liability	104,441	539,165
Less tax paid	(74,538)	(846,504)
Current tax liability	$ 337,637	$ 104,441

20 TAXATION – CONTINUED

	Year ended 30 June 2017 $	18 months ended 30 June 2016 $
(b) Income tax expense comprises:		
Current tax expense	307,734	411,780
Deferred tax liability reversed	(399,784)	-
Deferred tax expense – net	(50,047)	129,741
Income tax (benefit)/ expense	($ 142,097)	$ 541,521

(c) Deferred tax asset

(i) Deferred tax asset comprises the net effect of the following (amounts recognised in profit or loss):

	30 June 2017 $	30 June 2016 $
Allowance for loan losses	490,357	453,293
Other provisions	67,164	48,963
Unearned revenue	137,474	142,698
	$ 694,995	$ 644,954

(ii) The movement in deferred tax asset is as follows:

Balance at beginning of period	644,954	774,695
Credited/ (charged) to statement profit or loss and other comprehensive income	50,041	(129,741)
Balance at end of period	$ 694,995	$ 644,954

(d) Deferred tax liability

	30 June 2017	30 June 2016
(i) The balance comprises temporary differences attributable to:		
Depreciation	$ 694,995	$ 1,094,779

(ii) The movement in deferred tax liability is as follows:

Balance at beginning of period	1,094,779	1,094,779
Deferred tax liability reversed	(399,784)	-
Balance at end of period	$ 694,995	$ 1,094,779

20 TAXATION – CONTINUED

The bank had been booking deferred tax liabilities arising from differences in accounting and tax depreciation up until the 2014 financial year. For the 2014 financial year, the bank had requested the Ministry of Revenue and Customs (MRC) for the use of one fixed asset register for tax and accounting purposes. The MRC approved this request and the bank has since then lodged tax returns using the accounting depreciation for financial years 2014 and onwards, which has been assessed and approved by the MRC.

During the current financial year, management and directors have assessed that deferred tax liabilities which has been carried forward in the financial statements is no longer valid given that there are no differences arising from depreciation for tax purposes. As such, the bank has used a conservative approach and reversed off deferred tax liabilities to the extent of existing deferred tax assets in the current year, with a view to write off the remaining balance in the next financial year.

21 OTHER LIABILITIES

	30 June 2017 $	30 June 2016 $
Accrued interest	608,111	798,468
Provisions for annual leave and staff bonus	125,185	77,620
Deferred income	549,895	570,791
Other creditors and accruals	1,772,884	3,289,997
	$ 3,056,075	$ 4,736,876

	30 June 2017 $	30 June 2016 $
Other creditors and accruals include the following:		
Accruals and creditors	1,184,104	773,775
Credit holding accounts	127,836	526,527
Foreign currency purchase	460,944	1,987,632
Withholding tax payable	-	2,063
	$ 1,772,884	$ 3,289,997

22 BORROWINGS

		30 June 2017 $	30 June 2016 $
Comprises:			
Borrowings	(a)	3,297,915	3,660,574
Tonga Development Bank promissory notes	(b)	62,158,525	53,780,373
Tonga Development Bank bonds		-	-
		$ 65,456,440	$ 57,440,947

22 BORROWINGS - CONTINUED

(a) Borrowings comprise the following:

	Principal repayment term	Interest rate	30 June 2017 $	30 June 2016 $
Government of the Kingdom of Tonga				
Asian Development Bank	1993 – 2023	3.0%	279,966	326,627
International Fund for Agriculture Development 3	1999 – 2020	3.0%	572,155	762,873
International Development Association	1998 – 2023	3.0%	651,019	751,169
			1,503,140	1,840,669
Other borrowings				
European Investment Bank VI	2009 – 2026	5.5%	64,637	87,262
European Union	1988 – 2019	1.5%	6,775	9,280
Private Sector Reconstruction Facility	2011 – 2025	0.0%	1,723,363	1,723,363
			1,794,775	1,819,905
			$ 3,297,915	$ 3,660,574

The Government of the Kingdom of Tonga has arranged loans and grants from the Asian Development Bank, the International Development Association and the International Fund for Agricultural Development all of which are fully drawn.

The Government of the Kingdom of Tonga has guaranteed the repayment of the fully drawn loan from the European Union. These loans together with the loans from the European Investment Bank are in various currencies.

	30 June 2017	30 June 2016
(b) Tonga Development Bank promissory notes	$ 62,158,525	$ 53,780,373

The interest rate at year end on promissory notes ranged from 1.0% per annum to 6.25% per annum. Interest is paid out on maturity and semi-annually for terms over 180 days.

23 MANAGED FUNDS

The Bank manages these funds on behalf of Government agencies and at year end the balances for the respective funds were as follows:

	Total Funds $	Advance to Projects $	30 June 2017 $	30 June 2016 $
Other Managed Fund				
Livelihood Reactivation Project - Niuatoputapu	94,401	(251,721)	(157,320)	(63,638)
New Zealand Borrower Diversification Fund	287,639	(304,597)	(16,958)	(74,628)
ADB Microfinance Revolving Fund	359,652	(220,659)	138,993	182,284
Total of Other Managed Funds	741,692	(776,977)	(35,285)	44,018
Government Development Loan				
Agriculture Marketing fund-1%	1,437,250	(486,453)	950,797	89,934
Fisheries Development & Export Fund -1%	170,000	(94,201)	75,799	37,603
Tourism Loan Fund -1%	500,000	(191,650)	308,350	247,138
Manufacturing Fund -1%	322,940	(110,952)	211,988	149,009
Student Loan Scheme Fund -1%	1,688,630	(667,897)	1,020,733	612,428
Agriculture Marketing & Production Fund -4%	5,158,499	(3,096,277)	2,062,222	(283,998)
Fisheries Development & Export Fund -4%	2,157,218	(1,706,260)	450,958	318,319
Tourism Loan Fund -4%	701,204	(500,077)	201,127	(163,946)
Manufacturing Fund -4%	730,000	(504,687)	225,313	(1,942)
Development of Livestock -4%	250,000	(96,360)	153,640	152,954
Development of Forestry -4%	10,004	(9,101)	903	(400,000)
Construction -4%	1,400,000	(453,460)	946,540	971,668
Retailer & Wholesaler Fund -4%	590,000	(420,335)	169,665	109,781
Other Priority Sector Funds-4%	60,000	(10,891)	49,109	41,117
Education - 4%	721,378	(636,276)	85,102	-
Overseas Medical Cover -4%	60,000	(13,416)	46,584	31,242
Micro Loans Women - 4%	300,000	(115,970)	184,030	-
Total of Government Development Loan	$16,257,127	($9,114,263)	$7,142,860	$1,911,307
Total Managed Fund	$16,998,815	($9,891,240)	$7,107,575	$1,955,325

Percentage noted above represent the interest rate at which government development loan managed funds are on lent.

24 CAPITAL

(a) Authorised

	$
At 1 January 2015 – 1,400,000 ordinary shares @ $10 each	14,000,000
Increase during the period – 600,000 ordinary shares@ $10 each	6,000,000
At 30 June 2016 – 2,000,000 ordinary shares @ $10 each	20,000,000
Increase during the year – 3,000,000 ordinary shares @ $10 each	30,000,000
At 30 June 2017 – 5,000,000 ordinary shares @ $10 each	$ 50,000,000

Based on the TDB Articles of Association adopted on 31st March 2017 authorised capital of the Bank has increased to $50,000,000 divided into 5,000,000 ordinary shares each of $10.

(b) Issued and fully paid

	30 June 2017 $	30 June 2016 $
1,400,000 ordinary shares of $10 each	$ 14,000,000	$ 14,000,000

(c) Asset revaluation reserve

	30 June 2017 $	30 June 2016 $
Balance at beginning of financial year	-	-
Revaluation surplus for the year	2,486,535	-
Balance at end of financial year	$ 2,486,535	-

25 RELATED PARTY TRANSACTIONS

(a) Directors

(i) The following persons were directors of the Bank at any time during this period and up to the date of this report:

- Lord Matoto (Chairman)
- Paula Taumoepeau
- Leta Havea Kami
- Lepaola Vaea (Resigned 14 June 2017)
- Obey Samate (Appointed 6 September 2016)

25 RELATED PARTY TRANSACTIONS - Continued

(ii) Directors' fees and emoluments and key management compensation during the period/ year were:

	Year ended 30 June 2017 $	18 months ended 30 June 2016 $
Directors' fees and retirement benefit	148,196	155,732
Management salaries and other short term employee benefits	379,966	570,536
Total	$ 528,162	$ 726,268

(iii) There were no transactions with related parties in terms of loans and advances to directors or director related entities during the year ended 30 June 2017 (period ended 30 June 2016: Nil).

(b) Shareholder

In the normal course of its operations, the Bank enters into transactions with the shareholder, the Government of the Kingdom of Tonga. These transactions include guarantee and financing transactions which are carried out on normal trading terms. The Government of the Kingdom of Tonga owns 100% of the shares in the Bank.

(i) Borrowings

	Year ended 30 June 2017 $	18 months ended 30 June 2016 $
Interest paid/payable on borrowings	53,894	70,405
Repayments of borrowings during the period	337,529	195,343
Borrowings from the Government of the Kingdom of Tonga are disclosed in note 22(a)	1,503,140	1,840,669
The Government purchased TDB bonds and promissory notes during the period and the balances at period end are as follows:		
TDB promissory notes	11,185,427	10,692,119
Interest paid/payable on TDB bonds and promissory notes	490,852	2,610,155

Interest payable on the bonds and promissory notes range from 2% to 4% per annum.

(ii) Term deposits

	Year ended 30 June 2017 $	18 months ended 30 June 2016 $
Interest received/receivable on Government of Tonga Local Development Bonds	252,595	272,244
Government of Tonga Local Development Bonds at year end - refer note 12.	5,859,000	6,108,000

(iii) The shareholder has provided a guarantee on behalf of the bank to the central bank for a breach in the single borrower limit. Refer note 31.

26 COMMITMENTS AND CONTINGENT LIABILITY

	30 June 2017 $	30 June 2016 $
(a) Capital commitment	$ 1,312,000	-
(b) Contingent liability	-	-
(c) Operating lease commitments	$ 180,273	$ 188,600

(i) The Bank has leases over various leasehold properties in the Kingdom for a maximum term of 50 years. The minimum operating lease payments at balance sheet date are as follows:

	30 June 2017 $	30 June 2016 $
Not later than one year	8,320	8,320
Later than one year but not later than five years	33,280	33,280
Later than five years	138,673	147,000
	$ 180,273	$ 188,600

(ii) The Bank has entered into lease agreements to rent out its various properties for terms ranging from one to five years. The minimum lease payments receivable at balance sheet date are as follows:

	30 June 2017 $	30 June 2016 $
Not later than one year	26,773	32,551
Later than one year but not later than five years	8,073	43,377
Later than five years	-	8,423
	$ 34,846	$ 84,350

27 FINANCING ARRANGEMENTS

	30 June 2017 $	30 June 2016 $
Arrangements with Bank of South Pacific Tonga Limited are as follows:		
(i) Documentary letter of credit limit secured by letter of negative pledge	-	500,000
(ii) Forward exchange contract limit	-	1,000,000
	$ -	$ 1,500,000

28 DIVIDENDS

	30 June 2017 $	30 June 2016 $
(a) No dividends were declared for the year ended 30 June 2017.	-	-
(b) The directors declared a dividend of 65% of net profit for the year ended 30 June 2016. This amounted to $1,167,196 or $0.83 per issued share of which $1,000,000 interim dividend has been paid to the shareholder as at 30 June 2016.	-	167,196

29 EARNINGS PER SHARE

	Year ended 30 June 2017 $	18 months ended 30 June 2016 $
Net profit after tax	1,440,664	1,795,686
Number of issued shares	1,400,000	1,400,000
Earnings per share	$ 1.03	$ 1.28

30 RETURN ON EQUITY

	Year ended 30 June 2017 $	18 months ended 30 June 2016 $
Net profit after tax	1,440,664	1,795,686
Shareholder's equity	24,843,592	20,916,393
Return on equity	5.80%	8.59%

31 BREACH IN SINGLE BORROWER LIMIT

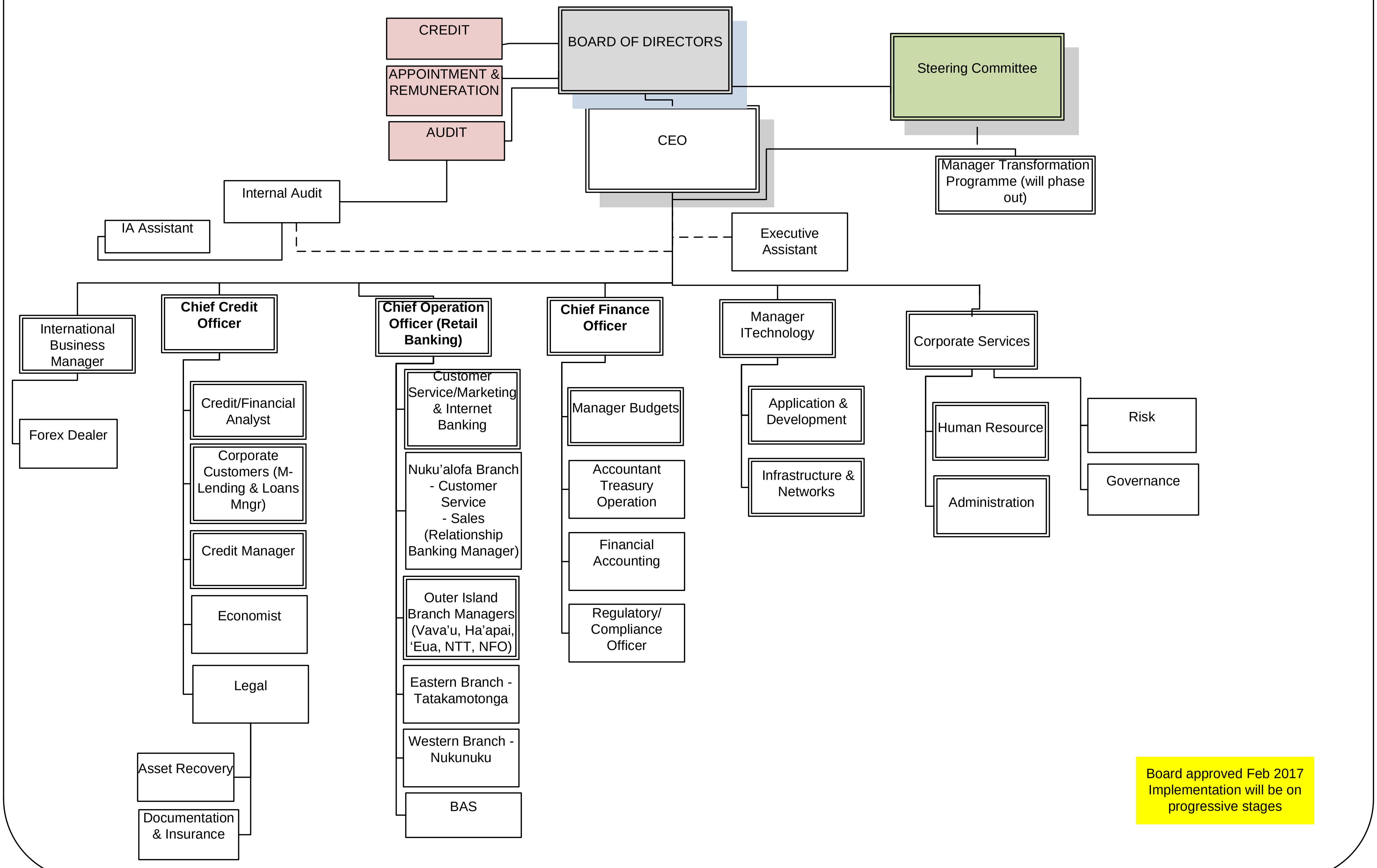
During the current financial year, the bank had approved a loan which was in excess of 25% of its capital base and therefore constituted a breach in the single borrower limit (SBL) under Prudential Statement 10 on Large Exposures. The bank's shareholder has provided a guarantee to the regulator, the central bank, for a period of 1 year from the date of the breach to cover excess of the loan over the banking single borrower limit.

32 SUBSEQUENT EVENTS

The Bank had amended its Articles of Association during the year to increase its authorised capital as part of a capital restructuring exercise. The Bank has identified potential investors including seeking additional injection of capital from its current shareholder.

The intent of this exercise is to increase the Bank's capital base to remedy the breach in the single borrower limit during the current financial year as well as take on board more significant loans in the future in order to be more competitive in the market.

PROPOSED OVERALL TDB STRUCTURE: Effective date 1st March 2017



Senior Management Team as at 30 June 2017

SENIOR EXECUTIVES

Managing Director & CEO	Mrs Leta Kami
Deputy Managing Directors	
• Finance	Mr Hasiloni Fungavai (Retired 28 April 2017) Mrs Loi Mateiwai (Appointed 27 March 2017)
• Credit & Risk	Mr Sitino Maka (Retired 28 February 2017) Mrs Seini Movete (Appointed 16 March 2017)

HEAD OFFICE

Managers

• Manager Operations	Mrs Lata Kava
• Lending- Tongatapu	Mrs ‘Elisapesi Fineanganofo
• Loans District 1 & 2	Mr Saia Talau
• Manager International	Mr Tevita Tu’inauvai
• Asset Recovery	Mr Samisoni Masila
• Credit and Operations Support	Mr Folaufisi Vaea
• Finance & Budgeting	Mrs ‘Ofeina Filimoehala
• Information Services	Mr Siokatame Havili Movete
• System Operations	Mrs Silia Tupou
• Human Resource	Mrs Siosina Paongo
• Administration	Mrs Mele Fonua
• Senior Economist	Mrs Piula Tangataevaha
• Senior Internal Auditor	Mr Samiu Fifita

BRANCH OFFICES

Managers

• Vava’u Branch	Mr ‘Eliki ‘Ofa
• Ha’apai Branch	Mr Viliami Fifita
• ‘Eua Branch	Mrs Lesieli Hala’ufia
• Niuatoputapu Branch	Mrs Milika Tolungamaka
• Niuafo’ou Branch	Mr Senituli Koloi
• Hahake District Office	Mr Tau’atevalu Mafi
• Hihifo District Office	Mr Mosese Fifita