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BOARD OF AUDITORS  
NEW YORK  
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10 March 2008

Ms. Karen Koning AbuZayd  
Commissioner General  
United Nations Relief and Works Agency for Palestine Refugees  
in the Near East (UNRWA)  
PO Box 140157  
Amman 11814 Jordan

Dear Ms. Koning AbuZayd,

Please find attached the report of the Board of Auditors on the United Nations Relief and Works Agency for the Palestinian Refugees in the Near East – Microfinance and Microenterprise Department (MMD) for the year ended 31 December 2006.

Yours sincerely,

  
Swatantra A. Goolsarran  
Executive Secretary  
United Nations Board of Auditors

cc: Mr. Michael Kingsley-Nyinah  
Mr. Ramadan Al-Omari  
Mr. Mukesh Arya  
Ms. Jane Giacaman  
Imran Vanker

Enc.

## **Audit report on the UNRWA Microfinance and Microenterprise Department (MMD)**

We have audited the accompanying financial statements of the United Nations Relief and Works Agency for Palestine Refugees in the Near East (UNRWA) Microfinance and Microenterprise Department, comprising statements A to D, and the supporting notes to the financial statements for the financial year ended 31 December 2006. The financial statements are the responsibility of the Commissioner-General. Our responsibility is to express an opinion on the financial statements based on our audit.

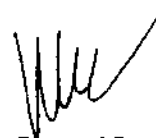
We conducted our audit in accordance with the International Standards on Auditing. Those standards require that we plan and perform the audit to obtain reasonable assurance as to whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing accounting principles used and significant estimates made by the Commissioner-General, as well as evaluating the overall financial statement presentation. We believe that our audit provides a reasonable basis for the audit opinion.

In our opinion, these financial statements present fairly, in all material respects, the financial position of UNRWA Microfinance and Microenterprise Department as of 31 December 2006 and the results its operations and its cash flows for the year then ended, in accordance with International Financial Reporting Standards.

Furthermore, in our opinion, the transactions of the UNRWA Microfinance and Microenterprise Department that have come to our notice or that we have tested as part of our audit have in all significant respects been in accordance with the Financial Regulations and legislative authority.



**Imran Vanker**  
Director of External Audit (South Africa)  
Lead auditor



**Bernard Levallois**  
Director of External Audit (France)  
Chairman: Audit Operations Committee  
United Nations Board of Auditors



**Roland A. Rey**  
Director of External Audit (Philippines)

10 March 2008

UNITED NATIONS  
RELIEF AND WORKS AGENCY FOR  
PALESTINE REFUGEES IN THE NEAR EAST



NATIONS UNIES  
OFFICE DE SECOURS ET DE TRAVAUX POUR LES  
REFUGIES DE PALESTINE DANS LE PROCHE-ORIENT

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## CERTIFICATION OF THE FINANCIAL STATEMENTS

### Microfinance and Microenterprise Programme

FI 540

17 January 2008

Pursuant to financial regulations 11.4 and 12.1, and further to my letter same reference dated 25 April 2007, I have the honour to resubmit UNRWA's Microfinance and Microenterprise Programme (MMP) Financial Statements for the year ended 31 December 2006.

These statements have been revised as per United Nation Board of Auditors recommendations, where all agreed adjustment entries were posted.

I certify that all transactions have been properly recorded in the accounting records and properly reflected in the MMP's revised financial accounts and appended statements, which I hereby certify as accurate and representative of the MMP's operating activities and the financial state of affairs as at 31 December 2006.

Ramadan Al Omari  
Comptroller

**United Nations Relief and Works Agency  
For Palestine Refugees in the Near East**

**Microfinance and Microenterprise Department**

**Gaza, West Bank, Jordan and Syria**

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**Consolidated Financial Statements  
and  
Notes**

**31 December 2006**

**With Comparative Figures as of 31 December 2005**

**United Nations Relief and Works Agency  
For Palestine Refugees in the Near East**

**Microfinance and Microenterprise Department**

**Gaza, West Bank, Jordan and Syria**

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**United Nations Relief Works Agency**  
**For Palestine Refugees in the Near East**  
*Microfinance and Microenterprise Department*

**Consolidated Balance Sheet**  
**As of 31 December 2006**  
**With Comparative Figures for 2005**

Assets	Note	2006 USD	2005 USD
<b>Non-Current Assets</b>			
Property, Plant and Equipment	5	479,952	429,868
Loans Receivable, Net	4	599,176	159,680
		<u>1,079,128</u>	<u>589,548</u>
<b>Current Assets</b>			
Loans Receivable, Net	4	5,143,747	7,859,641
Pledges Receivable	8.1-4	275,814	943,396
Prepayments and Other Receivables		104,233	3,916
Cash and Cash Equivalents	3	10,372,931	7,494,612
		<u>15,896,725</u>	<u>16,301,565</u>
<b>Total Assets</b>		<u><b>16,975,853</b></u>	<u><b>16,891,113</b></u>
<b>Equity</b>			
General Undesignated		(6,637,236)	(4,660,194)
Fund Held For Training		62,253	19,296
Temporary Restricted	8.1.1-4	1,158,038	2,927,978
Board Designated Fund/MIS System		36,976	45,000
Loan Revolving Fund	9	19,208,157	14,619,249
<b>Total Equity ( Statement-C )</b>		<u><b>13,828,189</b></u>	<u><b>12,951,329</b></u>
<b>Non-Current Liabilities :</b>			
Retirement Benefit Obligations		83,665	73,650
	2.4.b.	<u>83,665</u>	<u>73,650</u>
<b>Current Liabilities :</b>			
Payables and Accruals		344,426	46,612
Bills Payable to UNRWA	6	344,573	1,444,522
Liability to UNRWA – OPEC Pal Trust Fund	7	2,375,000	2,375,000
<b>Total Current Liabilities</b>		<u>3,063,999</u>	<u>3,866,134</u>
<b>Total Liabilities</b>		<u>3,147,664</u>	<u>3,939,784</u>
<b>Total Equity and Liabilities</b>		<u><b>16,975,853</b></u>	<u><b>16,891,113</b></u>

See Notes to Financial Statements

**United Nations Relief Works Agency  
For Palestine Refugees in the Near East  
Microfinance and Microenterprise Department**

**Consolidated Statement of Profit and Loss  
For the Year Ended 31 December 2006  
With Comparative Figures for 2005**

Note	Financial Services	Training Service	Total	
	Note 1.a	Note 1.b	2006	2005
	2006	2006	2006	2005
	USD	USD	USD	USD
<b>Interest and Other Operating Income:</b>				
	2,369,341		2,369,341	2,372,630
	48,096		48,096	
	271,542		271,542	44,529
		137,155	137,155	45,291
	<b>2,688,979</b>	<b>137,155</b>	<b>2,826,134</b>	<b>2,462,450</b>
<b>Impairment Losses On Loans</b>				
	1,929,390		1,929,390	732,168
	471,894		471,894	655,384
	<b>1,457,496</b>		<b>1,457,496</b>	<b>76,784</b>
<b>Operating Expense:</b>				
	2,413,381	49,633	2,463,014	2,129,801
	92,395	23,475	115,870	126,850
	152,242	-	152,242	151,291
	64,940	-	64,940	58,653
	182,081	9,560	191,641	73,087
	19,226	1,049	20,275	14,894
	117,503	-	117,503	112,557
	118,501	-	118,501	93,989
	43,970	-	43,970	52,580
	-	-	-	5,610
	34,720	10,482	45,202	5,459
	5,353	-	5,353	52,639
	<b>3,244,312</b>	<b>94,199</b>	<b>3,338,511</b>	<b>2,877,410</b>
		<b>42,956</b>		<b>(491,744)</b>
	20,917	-	20,917	130
	<b>(1,991,912)</b>	<b>42,956</b>	<b>(1,948,956)</b>	<b>(491,614)</b>

See Notes to Financial Statements

**United Nations Relief Works Agency  
For Palestine Refugees in the Near East  
Microfinance and Microenterprise Department**

**Profit and Loss For  
Small Micro Enterprise Training Program  
As of 31 December 2006  
With Comparative Figures for 2005**

	Training Service	
	<u>2006</u>	<u>2005</u>
Note	<u>USD</u>	<u>USD</u>
<i>Interest and Other Operating Income:</i>		
Training Income	137,155	45,291
<i>Total Operating Revenues</i>	<u>137,155</u>	<u>45,291</u>
<i>Operating Expense:</i>		
Salaries and Related Expenses	49,633	27,678
Special Service Contracts	23,475	-
Stationary and Supplies	9,560	-
Minor Equipment and Maintenance	1,049	-
Training	10,482	-
Other Cost	-	41,303
<i>Total Operating Expense</i>	<u>94,199</u>	<u>68,981</u>
Operating Gain (Loss) for the Year	1.b <u>42,956</u>	<u>(23,690)</u>

See Notes to Financial Statements

**United Nations Relief Works Agency  
For Palestine Refugees in the Near East  
Microfinance and Microenterprise Department**

**Statement of Changes in Net Assets  
Year Ended 31 December 2006**

	General Undesignated Fund		Temporary Restricted Fund		Board Designated Fund		Revolving Loan Fund	Total
	USD		USD		USD			
Net Assets as at 1 <sup>st</sup> January 2005	(4,158,445)		42,986		45,000		13,138,028	9,067,569
Opening Loss for Year 2005 (Statement - B)	(467,924)		(23,690)					(491,614)
Additional general reserves for bad debts	(33,825)							(33,825)
Grants designated to Capital			4,409,199					4,409,199
Releases to Revolving Loan Fund			(1,481,221)				1,481,221	-
Net Assets at Beginning of Year 2006	(4,660,194)		2,927,978		45,000		14,619,249	12,951,329
Operating Loss for Year 2006 (Statement - B)	(1,991,912)							(1,948,956)
Adjustments to Prior Years	14,871							14,872
Additional ( Releases ) Fund for the Period					(8,024)		2,818,969	2,810,944
Releases to Revolving Loan Fund			(1,769,940)				1,769,940	-
Net assets at end of year (Statement -A)	(6,637,236)		1,158,038		36,976		19,208,157	13,828,189

See Notes to Financial Statements

**United Nations Relief Works Agency**  
**For Palestine Refugees in the Near East**  
*Microfinance and Microenterprise Department*

**Statement of Cash Flows**  
**Year Ended 31 December 2006**  
**With Comparative Figures for 2005**

	2006	2005
	USD	USD
<b>Cash Flows from Operating Activities:</b>		
Contribution Received	2,787,177	3,465,802
Interest on Loans and Other Revenues	3,183,040	3,117,834
Loans Issued net of Collections	347,010	(3,000,967)
Cash Paid to Employees and Suppliers	(3,270,321)	(1,902,875)
<b>Net cash Provided by operating activities</b>	<b>3,046,905</b>	<b>1,679,794</b>
<b>Cash Flows from Investing Activities:</b>		
Procurement of Fixed Assets	(168,586)	(321,248)
	<b>(168,586)</b>	<b>(321,248)</b>
<b>Cash Flows from Financing Activities:</b>		
Liability to UNRWA - OPEC Pal Trust Fund	-	1,900,000
	<b>-</b>	<b>1,900,000</b>
<b>Increase in Cash and Banks During the Period</b>	<b>2,878,319</b>	<b>3,258,546</b>
Cash at Beginning of the Year	7,494,612	4,236,066
<b>Cash on Hand and Deposits With Banks at the end of Year</b>	<b>10,372,931</b>	<b>7,494,612</b>
<b>Adjustments to Reconcile Changes in Net Assets</b>		
<b>to Net Cash Provided by Operating Activities:</b>		
Change in Net Assets	876,860	3,883,760
Provision for Loans Losses	1,095,041	732,168
Change in general provisions for bad debts	834,349	33,825
Depreciation	118,501	93,989
Loans Extended	(15,318,588)	(23,367,190)
Loans Collection	15,665,598	20,366,223
Decrease (Increase) in Pledges receivable	667,582	(943,397)
Decrease (Increase) in Prepaid Expenses	(100,317)	(3,214)
(Decrease) Increase in Payables and Accruals	297,814	3,112
(Decrease) Increase in Bills Payable to UNRWA	(1,099,949)	872,083
(Decrease) Increase in Termination Benefits Obligations	10,015	8,435
	<b>3,046,905</b>	<b>1,679,794</b>

See Notes to Financial Statements

**United Nations Relief and Works Agency  
For Palestine Refugees in the Near East  
Microfinance and Microenterprise Department**

**Notes to Financial Statements  
31 December 2006**

(Amounts are expressed in US Dollars)

**1. Background**

**A- Microfinance and Microenterprise Department**

Since June 1991, UNRWA's Microfinance and Microenterprise Department (MMD) in the West Bank and Gaza has helped promote small business development, create employment, improve the income of micro enterprises and reduce poverty through the establishment of a number of targeted credit products aimed at small businesses, microenterprises, women, youth, consumers and householders. Since 2003 the department has also expanded its microfinance operations to Jordan and Syria. The MMD organizes its lending activities through a revolving loan fund that serves the operations in all fields. The department supports businesses varying in size from micro vending, employing just one or two individuals to small industrial firms and aims to satisfy a variety of needs such as capital funding and working capital financing. It also provides non-business financial services to working class consumers and poor households.

MMD's funds are disbursed to borrowers under five credit products. These are the Small-Scale Enterprise (SSE) product, the Solidarity-Group Lending (SGL) product, the Consumer Lending Product (CLP), the Microenterprise Credit (MEC) product and the Housing Lending Product (HLP).

The Small-Scale Enterprise (SSE) product was the original credit instrument that the programme began with in 1991. Its objective is to provide loans to new and existing small-scale enterprises. This product has been restricted in recent years due the critical economic situation facing most medium and small-scale enterprise in the oPt.

Microenterprise Credit (MEC) product is now the core financial instruments of the department. This was introduced in Gaza in 1996, in the West Bank in 1998 and in Jordan and Syria in 2003. This product is designed to meet the working capital needs of the microenterprise sector that is unable to secure credit from banks and other formal financial institutions due primarily to lack of required collateral. This product is retailed to both formal and informal enterprises.

The Solidarity-Group Lending (SGL) product was introduced in Gaza in 1994 to enable Palestinian women to participate in the local community. This product focuses primarily on women-based informal enterprises.

The Consumer Lending Product (CLP) was established in 2002 in Gaza. This product aims to help workers and employees to purchase household assets and

provide financing for education, health and family emergencies. Target clients are people who have fixed monthly income.

The Housing Lending Product (HLP) was introduced in Gaza in 2006 with the aim to provide financial resources to Palestine refugees build improve and develop their housing and living conditions.

These financial services are retailed through a network of 13 branch offices, of which two are located in Syria, two in Jordan, three in Gaza and six in the West Bank. Three of these offices are new ones which were established in 2006, including the al-Balad branch office in Amman, Jordan, the al-Amin branch office in Damascus, Syria and the Bethlehem branch office in the West Bank.

## **1. Background (continued)**

### **B- Small Micro Enterprise Training Program (SMET)**

UNRWA's MMD also provides business training through its Small Micro Enterprise Training Programme (SMET). The main goal of the training programme is to contribute to the economic development of the Gaza Strip, through supporting small businesses and encouraging entrepreneurs. Without a natural resource base, Palestinians have to rely on their skill, entrepreneurship and industriousness to promote economic growth. The programme has its own separated expenses and budget. The program income is generated from trainee's fees and funds from donors as indicated in statement B1 and related notes.

To achieve this goal, the training programme aims:

- To provide a wide range of business training courses to the business community in Gaza;
- To promote an entrepreneurial spirit and the requisite skills;
- To develop a local training capacity through a team of trainers able to deliver courses using participatory, non-formal adult-education training techniques and technologies with up-to-date subject matter;
- To develop a business curriculum that is relevant to the state of the local economy and to make training material and resources more readily available;
- To encourage trainers who have developed training skills in the programme to transfer their experience in both teaching methodology and curriculum development to the universities and vocational training institutions where they teach;
- To promote co-operation and co-ordination among institutions engaged in small and micro-enterprise development, through contact groups and workshops;
- To enable small businesses in the Gaza Strip to compete in regional and global markets.

To achieve these objectives, the programme includes the following activities:

1. **Business Training:** This is the core activity of the SMET program. It provides a range of business training courses that meet the practical training needs of the small business community in Gaza. The business service model adopted pursues a demand-

led approach that is relevant to the business needs of clients. The training style is participatory and based on adult learning techniques and methodologies.

**2. Start up Your Own Business:** This training programme aims to encourage new business start-ups amongst women and new graduates from technical and vocational colleges and from universities. The encouragement of entrepreneurship and self-employment is an important tool for business development and both for economical and social development.

**3. Curriculum Development:** In order to meet the goal of establishing best practice in the training process, the programme strives to incorporate relevance and participation in developing training manuals and curricula based. The use of participatory and adult education techniques in developing curricula leads to the development of training courses that are most attractive to clients.

**4. Building Local Training Capacity:** The SMET programme works with a pool of more than 40 trainers who deliver almost 100 training courses. Twenty of these trainers form the core trainer's pool that conducts the bulk of the courses offered. The programme continues to build the team of trainers capable of delivering courses in participatory, non-formal adult education training techniques and technologies, with up-to-date subject matter.

The financial activities of the programme comprising training fees charged and direct costs of the programme, are presented separately in the Statement of Activities for the year ended 31 December.

## **2. Summary of Significant Accounting Policies**

The financial statements have been prepared in conformity with International Financial Reporting Standards and on the accrual basis of accounting.

Summary of significant accounting policies is described below.

### **2.1 Basis of Presentation:**

Funds of MMD and changes therein are classified and reported as follows:

- *General Undesignated net assets* – Utilization of net assets by MMD is not subject to donor-imposed restrictions. It includes retained earnings or losses from operations
- *Temporary restricted net assets* - Net assets whose use by MMD is limited by donor-imposed stipulations that either expire by passage of time or can be fulfilled and released by actions of MMD pursuant to those donor-imposed stipulations.
- *Revolving Loan Fund* - Restricted contributions received for on lending purposes, which were expended in term of loans, are included in the Revolving Loan Fund.
- *Grants and Donations* – The MMD records grants and donations for operations and loan funds for use in the current operating period, in the income statement below the net income from operation. Grants and donations for periods beyond the current operating period are recorded under liabilities as deferred grant revenue, to achieve that objective, grants and contributions:
  - Are first recorded under deferred revenues:

- At end of each year the deferred revenue account is adjusted for grant funds that should have been released during the period. The amounts related to the year are credited to the Income Statement;
- Grants for Fixed Assets are recorded as deferred grant revenue, i.e. fixed assets recorded in the balance sheet and an amount for depreciation is transferred to income statement over the useful life of the asset acquired.
- Accrual basis of accounting - Accrual accounting recognizes the effects of transactions and other events when they occur, recording them in the accounting records and reporting them in the financial statements of the periods to which they relate.

## 2.2 Loans Receivable and Allowance for Loan Losses

### 2.2.1. Allowance for loan losses

During 2005 management changed its policy and determined that impairment loss on the loan portfolio was represented by loans written off that were over 360 days past due, and accordingly booked these amounts by charging the statement of the profit and loss and by crediting the loan asset.

At the same time, management continued the policy of calculating provisions on the basis of loan aging categories as described below, by charging "general undesignated net assets" and by crediting the allowance for loan losses.

Loan Status	Allowance (percent)
1 – 30 days overdue	5 %
31 – 60 days overdue	10 %
61 – 90 days overdue	25 %
91 – 120 days overdue	50 %
121 – 180 days overdue	75 %
181 – 360 days overdue	100%

However, as the Department moved its accounting approach to the full accrual method, during year 2006 management adjusted FTI No. 42 in order that the provision for bad debts is based of a new "aged portfolio at risk report" (see below) that makes the provision for bad debt on the total amount outstanding on the loan. Based upon the historical experience of the MMD it was determined that the following loan loss provision is required for delinquent and the defaulting.

Loan Status	Allowance (percent)	
Current	1 %	General Provision
1 – 30 days overdue	5 %	General Provision
31 – 60 days overdue	10 %	General Provision
61 – 90 days overdue	25 %	General Provision
91 – 120 days overdue	50 %	General Provision
121 – 180 days overdue	75 %	General Provision
181 – 360 days overdue	100%	General Provision

Based upon the above percentages, if a loan is not serviced an increasing reserve should be provided for. This provision will be shown in the income statement for the

period. On monthly basis adjustment to be made to reflect the changes in the General provisions.

#### 2.2.2. Related-Party (“insider”) Loans

During the financial period no loans were given to the MMD management, board members, MMD staff or any other related-party as per the department rules and regulations.

#### 2.2.3. Accrued Interest on loans

Effective year 2006 the interest income on loans provided is accounted for on the accrual basis in compliance with IAS 18. This is done by accruing interest up to 90 days by debiting accrual receivables and crediting interest revenue. After 90 days all uncollected accrual receivables are transferred to Interest in Suspense by debiting the interest revenue and crediting interest in suspense. After 360 days all bad debts that have past due will be written off.

The Accrued Interest Revenue recorded for year 2006 was:           \$ 48,096.00  
MIS calculation for accrued interest revenue for year 2005 was:   \$ 18,301.00

#### 2.2.4. Recoveries

Any recoveries of previously written off loans are taken to the statement of profit and loss in the period they are received

### 2.3 Property Plant and Equipment:

A-Fixed assets are stated at cost net of accumulated depreciation. Depreciation is computed on a straight-line basis over the estimated useful lives of the respective assets as follows:

	<u>Years</u>
Furniture and Equipment	10
Computers and Printers	3
Vehicles	7
Leasehold Improvements	5

B- No in-kind donations were received during the financial year 2007.

### 2.4 Employee Separation Benefits

#### a- Provident Fund

All area staff members of MMD/UNRWA staff participate in the provident fund (PF) contributory scheme. Staff monthly contributions into the scheme are set at 7.5% of basic salaries and UNRWA share contribution is set at 15%. Under the PF rules, staff members are allowed to make additional voluntary contributions up to a maximum of 50% of monthly payroll. All participants receive the lower of book or market value return on the fund for the period of membership in the PF. The PF is administered by the Provident Fund Secretariat (PFS) jointly with the

supervision and guidance provided by two committees, the Provident Fund Committee and the Investment Advisory Committee.

#### b- Retirement Benefit Obligation

Starting with the year 2005, the Microfinance Microenterprise Department booked provisions for "retirement benefits obligations" towards its "A" category staff and according to the policy described below.

UNRWA staffs are categorized under three categories of employment. These are  
"A" category: Staff contracted before the year 1990  
"X" category: Staff contracted between the years 1990 and 1995  
"Z" category: Staff contracted after 1 September 1999

The MMD program includes 9 staff members under the "A" category, and the rest under the X and Z categories.

Only the "A" staff category is entitled to end of service benefits as follows:

For Termination Indemnity we have 3 groups:

Group 1: Less than 10 years of service or age less than 46  
Group 2: More than or equal 10 years of service and age between 46 and 55  
Group 3: Early voluntary Retirement

The indemnity for each group is as follow:

Group 1: If Total Service = 1 --> 1 \* Base Salary  
If Total Service between 1.01 and 8.99 --> (Total Service - 1) \* Base Salary  
If Total Service >= 9 --> 8 \* Base Salary

Group 2: If Age = 46 --> 8.25 \* Base Salary  
If Age = 47 --> 8.50 \* Base Salary  
If Age = 48 --> 8.75 \* Base Salary  
If Age = 49 --> 9.00 \* Base Salary  
If Age = 50 --> 9.25 \* Base Salary  
If Age = 51 --> 9.50 \* Base Salary  
If Age = 52 --> 9.75 \* Base Salary  
If Age = 53 --> 10.00 \* Base Salary  
If Age = 54 --> 10.25 \* Base Salary  
If Age = 55 --> 10.50 \* Base Salary

Group 3: 0.085 \* Total Years in Service \* Annual Base Salary

Movement in the liability for the years 2006 and 2005 is as follows:

	<u>USD</u>
Balance as at 31 December 2005	73,650
Additional provision for 2006	<u>10,015</u>
Balance as at 31 December 2006	<u>83,665</u>

## 2.5 Foreign Currency Transactions:

The books of accounts are maintained in U.S. Dollar. Transactions in other currencies are translated to USD at UN exchange rate ruling at the date of the transaction. Monetary assets and liabilities denominated in other currencies at the balance sheet date are translated to USD at the exchange rate ruling at that date. Exchange differences arising on translation are recognized in the statement of operating activities. All other assets and liabilities are presented in USD equivalent at their historical values.

	<u>2006</u>	<u>2005</u>	<u>Change</u>
	<u>USD</u>	<u>USD</u>	<u>%</u>
One Jordanian Dinar	0.708	0.708	0.00 %
One Israeli Shekel	4.22	4.600	-8.17 %
One Syrian Pound	52.21	52.00	0.40 %

## 3. Cash and Cash Equivalents

### Composition:

	<u>31 December</u>	
	<u>2006</u>	<u>2005</u>
	<u>USD</u>	<u>USD</u>
Deposits with Banks in Jordanian Dinar	1,453,144	652,179
Deposits with Banks in New Israeli Shekel	160,315	82,548
Deposits with banks in US Dollar	8,515,998	6,634,016
Deposits with Banks in Syrian Pound	243,474	125,869
	<u>10,372,931</u>	<u>7,494,162</u>

Deposit with Banks in US Dollar as at 31 December 2006 and 2005 include an amount of \$ 1,184,811 and \$ 1,217,562 respectively from funds received from UNRWA designated for OPEC Pal Trust Revolving Fund.

## 4. Loans Receivable, Net

Loans Receivable includes loans outstanding from funds disbursed through both initial donor contribution (first time loans) and from revolving loan funds.

Composition of loans receivable net of allowance for bad debts by maturity as at 31 December is as follows:

	<u>2006</u>	<u>2005</u>
	<u>Net Loans</u>	<u>Net Loans</u>
	<u>USD</u>	<u>USD</u>
Maturities less than 1 year	5,143,746	7,859,641
Maturities over than 1 year	599,176	159,680
<b>Total</b>	<u>5,742,922</u>	<u>8,019,321</u>

4.1 Net Loans Receivable is as Follows:

	<u>31 December 2006</u>			<u>31 December 2005</u>		
	<u>Loans</u> <u>USD</u>	<u>Allowance</u> <u>USD</u>	<u>NET</u> <u>USD</u>	<u>Loans</u> <u>USD</u>	<u>Allowance</u> <u>USD</u>	<u>NET</u> <u>USD</u>
SSE Loans	362,183	(163,741)	198,442	699,827	(140,585)	559,242
MEC Loans	5,582,498	(1,151,730)	4,430,768	6,332,973	(711,982)	5,620,991
SGL Loans	566,926	(356,878)	210,048	1,424,321	(155,531)	1,268,790
CLP Loans	331,428	(223,857)	107,571	632,098	(61,800)	570,298
HLP Loans	804,134	(8,041)	796,093			
<b>Total</b>	<b><u>7,647,169</u></b>	<b><u>(1,904,247)</u></b>	<b><u>5,742,922</u></b>	<b><u>9,089,219</u></b>	<b><u>(1,069,898)</u></b>	<b><u>8,109,321</u></b>

Net loans receivable represent outstanding balance as of December 31, 2006 and 2005 less the calculated provision for un-collectable loans as of the same date. Net loans receivable is the net realizable value of loans disbursed.

4.2 Changes in Loan Balances during year 2006 are as follows:

	<u>Beginning</u> <u>USD</u>	<u>Issued</u> <u>USD</u>	<u>Repaid</u> <u>USD</u>	<u>Written Off</u> <u>USD</u>	<u>Total</u> <u>USD</u>
<b><u>Gaza</u></b>					
SSE Loans	699,828	118,500	332,114	124,031	362,183
MEC Loans	2,221,182	2,137,200	2,954,668	388,285	1,015,439
SGL Loans	1,424,321	1,055,091	1,603,733	170,142	566,926
CLP Loans	632,097	470,050	668,459	102,260	331,428
HLP Loans		<u>891,000</u>	<u>86,866</u>		<u>804,134</u>
<b>Sub Total</b>	<b><u>4,838,828</u></b>	<b><u>4,671,841</u></b>	<b><u>5,645,841</u></b>	<b><u>784,718</u></b>	<b><u>3080,110</u></b>
<b><u>West Bank</u></b>					
MEC Loans	<u>2,705,055</u>	<u>5,754,728</u>	<u>5,748,309</u>	<u>256,844</u>	<u>2,454,630</u>
<b>Sub Total</b>	<b><u>2,705,055</u></b>	<b><u>5,754,728</u></b>	<b><u>5,748,309</u></b>	<b><u>256,844</u></b>	<b><u>2,454,630</u></b>
<b><u>Jordan</u></b>					
MEC Loans	<u>952,965</u>	<u>2,904,594</u>	<u>2,475,236</u>	<u>44,328</u>	<u>1,337,995</u>
<b>Sub Total</b>	<b><u>952,965</u></b>	<b><u>2,904,594</u></b>	<b><u>2,475,236</u></b>	<b><u>44,328</u></b>	<b><u>1,337,995</u></b>
<b><u>Syria</u></b>					
MEC Loans	<u>592,371</u>	<u>1,987,425</u>	<u>1,796,212</u>	<u>9,151</u>	<u>774,434</u>
<b>Sub Total</b>	<b><u>592,371</u></b>	<b><u>1,987,425</u></b>	<b><u>1,796,212</u></b>	<b><u>9,151</u></b>	<b><u>774,434</u></b>
<b>Grand Total</b>	<b><u>9,089,219</u></b>	<b><u>15,318,588</u></b>	<b><u>15,665,598</u></b>	<b><u>1,095,041</u></b>	<b><u>7,647,169</u></b>

Percentage of Loans Receivable by Area:

	<u>31 December 2006</u>		<u>31 December 2005</u>	
	<u>USD</u>	<u>%</u>	<u>USD</u>	<u>%</u>
Gaza	3,080,110	40 %	4,838,828	53 %
West Bank	2,454,630	32 %	2,705,055	30 %
Jordan	1,337,995	18 %	952,965	10 %
Syria	774,434	10 %	592,371	7 %
	<b><u>7,647,169</u></b>	<b><u>100 %</u></b>	<b><u>9,089,219</u></b>	<b><u>100 %</u></b>

Percentage of Loans Receivable by Type:

	<u>31 December 2006</u>		<u>31 December 2005</u>	
	<u>USD</u>	<u>%</u>	<u>USD</u>	<u>%</u>
SSE Loans	362,183	5 %	699,828	7 %
MEC Loans	5,582,498	73 %	6,332,973	70 %
SGL Loans	566,926	7 %	1,424,321	16 %
CLP Loans	331,428	4 %	632,097	7 %
HLP Loans	804,134	11 %	-	-
	<u>7,647,169</u>	<u>100 %</u>	<u>9,089,219</u>	<u>100 %</u>

4.3 Changes in the allowance for loan losses during year 2006 are as follows:

	<u>Beginning</u>	<u>Additions</u>	<u>Total</u>
	<u>USD</u>	<u>(Releases)</u>	<u>USD</u>
	<u>USD</u>	<u>USD</u>	<u>USD</u>
<b>Gaza</b>			
SSE Loans	140,584	23,156	163,741
MEC Loans	343,943	177,170	521,113
SGL Loans	155,531	201,347	356,878
CLP Loans	61,800	162,057	223,857
HLP Loans	-	8,041	8,041
Sub Total	<u>701,858</u>	<u>571,772</u>	<u>1,273,630</u>
<b>West Bank</b>			
MEC Loans	319,394	225,503	544,897
Sub Total	<u>319,394</u>	<u>225,503</u>	<u>544,897</u>
<b>Jordan</b>			
MEC Loans	40,960	14,443	55,403
Sub Total	<u>40,960</u>	<u>14,443</u>	<u>55,403</u>
<b>Syria</b>			
MEC Loans	7,686	22,631	30,317
Sub Total	<u>7,686</u>	<u>22,631</u>	<u>30,317</u>
Grand Total	<u>1,069,898</u>	<u>834,349</u>	<u>1,904,247</u>

Percentage of Written Off Loans

	<u>31 December 2006</u>		<u>31 December 2005</u>	
	<u>USD</u>	<u>%</u>	<u>USD</u>	<u>%</u>
SSE Loans	124,031	11 %	13,890	2 %
MEC Loans	698,608	64 %	622,987	85 %
SGL Loans	170,142	16 %	79,010	11 %
CLP Loans	102,260	9 %	16,281	2 %
HLP Loans	-	-	-	-
	<u>1,095,041</u>	<u>100 %</u>	<u>732,168</u>	<u>100 %</u>

4.4 Loans Receivable, as at 31 December 2006, Distributed by Sector are as follows:

	Agriculture	Commerce	Industry	Service	Consuming	Housing	Total
	<u>USD</u>	<u>USD</u>	<u>USD</u>	<u>USD</u>	<u>USD</u>	<u>USD</u>	<u>USD</u>
SSE	6,745		200,038	155,400			362,183
MEC	99,778	430,141	75,207	410,312			1,015,439
SGL	153,293	273,863	102,581	37,190			566,926
HLP						804,134	804,134
CLP					331,428		331,428
Sub-Total	<u>259,816</u>	<u>704,004</u>	<u>377,826</u>	<u>602,902</u>	<u>331,428</u>	<u>804,134</u>	<u>3,080,110</u>
<b>West Bank</b>							
MEC	<u>17,378</u>	<u>918,381</u>	<u>252,557</u>	<u>1,266,314</u>			<u>2,454,630</u>
Sub Total	<u>17,378</u>	<u>918,381</u>	<u>252,557</u>	<u>1,266,314</u>			<u>2,454,630</u>
<b>Jordan</b>							
MEC	<u>186</u>	<u>637,912</u>	<u>158,776</u>	<u>541,121</u>			<u>1,337,995</u>
Sub Total	<u>186</u>	<u>637,912</u>	<u>158,776</u>	<u>541,121</u>			<u>1,337,995</u>
<b>Syria</b>							
MEC		435,175	96,816	242,443			774,434
Sub Total		<u>435,175</u>	<u>96,816</u>	<u>242,443</u>			<u>774,434</u>
Grand Total	<u>277,380</u>	<u>2,695,472</u>	<u>885,975</u>	<u>2,652,780</u>	<u>331,428</u>	<u>804,134</u>	<u>7,647,169</u>

Percentage of Loans Receivables Distributed by Sector are as follows:

	<u>31 December 2006</u>		<u>31 December 2005</u>	
	<u>USD</u>	<u>%</u>	<u>USD</u>	<u>%</u>
Agriculture	277,380	4 %	673,865	7 %
Commerce	2,695,472	35 %	3,315,121	36 %
Industry	885,975	12 %	1,333,012	15 %
Service	2,652,780	34 %	3,135,124	35 %
Consuming	331,428	4 %	632,097	7 %
Housing	804,134	11 %		
	<u>7,647,169</u>	<u>100 %</u>	<u>9,089,219</u>	<u>100 %</u>

\*CLP and HLP loans are disbursed to individuals for household improvements and development and are not distributed among any sector.

4.5 Loans Receivable, as at 31 December 2006 distributed by Geographical Area are as follows:

	SSE	MEC	SGL	CLP	HLP	Total
<u>Gaza</u>	<u>USD</u>	<u>USD</u>	<u>USD</u>	<u>USD</u>	<u>USD</u>	<u>USD</u>
Gaza Area	159,377	546,704	271,898	287,528	308,709	1,574,216
Middle Area	126,879	129,444	114,635	43,900	262,918	677,776
Southern Area	<u>75,927</u>	<u>339,291</u>	<u>180,393</u>	0	<u>232,508</u>	<u>828,118</u>
Total Gaza	<u>362,183</u>	<u>1,015,439</u>	<u>566,926</u>	<u>331,428</u>	<u>804,135</u>	<u>3,080,110</u>
<b>West Bank</b>						
Nablus		603,791				603,791

Tulkarm	-	284,745	-	-	-	284,745
Ramallah	-	884,596	-	-	-	884,596
Jenin	-	82,506	-	-	-	82,506
Hebron	-	331,746	-	-	-	331,746
Bethlehem	-	<u>267,246</u>	-	-	-	<u>267,246</u>
Total W.B	-	<u>2,454,630</u>	-	-	-	<u>2,454,630</u>
<b>Jordan</b>	-	<u>1,337,995</u>	-	-	-	<u>1,337,995</u>
	-	<u>1,337,995</u>	-	-	-	<u>1,337,995</u>
<b>Syria</b>	-	<u>774,434</u>	-	-	-	<u>774,434</u>
	-	<u>774,434</u>	-	-	-	<u>774,434</u>
Grand Total	<u>362,183</u>	<u>5,582,498</u>	<u>566,926</u>	<u>331,428</u>	<u>804,135</u>	<u>7,647,169</u>

### 5. Property, Plant and Equipment

#### Composition:

	Furniture And Equipment <u>USD</u>	Computers And Hardware <u>USD</u>	Vehicles <u>USD</u>	Leasehold Improvements <u>USD</u>	Total <u>USD</u>
<b>Cost :</b>					
Balance Jan. 1	222,903	179,275	203,134	166,779	772,091
Additions	46,166	83,625	10,831	27,963	168,585
Disposals					
Balance Dec. 31	<u>269,069</u>	<u>262,900</u>	<u>213,965</u>	<u>194,742</u>	<u>940,676</u>
<b>Accumulated Depreciation</b>					
Balance Jan. 1	83,366	109,362	88,317	61,178	342,223
Additions	22,664	44,789	23,196	27,852	118,501
Disposals					
Balance Dec. 31	<u>106,030</u>	<u>154,151</u>	<u>111,513</u>	<u>89,030</u>	<u>460,724</u>
Net Book Value	<u>163,039</u>	<u>108,749</u>	<u>102,452</u>	<u>105,712</u>	<u>479,952</u>

### 6. Bills Payable to UNRWA

Represents expenses paid by UNRWA on behalf of MMD in respect of operating expenses incurred by MMD, billed on a monthly basis and advances against donor's pledges as follows:

	<u>2006</u>	<u>2005</u>
Expenses Paid on Behalf of MMD	344,573	484,779
Advances against donor's pledges		<u>959,743</u>
Total amount due to UNRWA	<u>344,573</u>	<u>1,444,522</u>

## **7. Liability to UNRWA - OPEC Pal Trust Fund**

On 15 June 2004, United Nations Relief and Works Agency "UNRWA" for Palestine Refugees in the Near East had signed an "Administration Agreement" with the OPEC Fund for International Development (OFID) through which the fund will make available to UNRWA, as an administrator, an amount of US \$2,500,000 to be used exclusively for the promotion of micro enterprise through loans for the Palestinians in the occupied territories.

In consideration of the Administrator performing the services specified in the agreement, the administrator may deduct program support costs of up to 5% from amounts disbursed by OFID into the Pal Fund. The administrator may also charge such reasonable fees or other charges under the Loan Agreement to cover such costs of the administrator as may directly and reasonably be incurred, in connection with the conclusion of loan agreements. UNRWA passed on the administration of the trust activities to the MMD.

As of 31 December 2004, one instalment in the amount of US \$500,000 was received by UNRWA. Program support costs of US \$25,000 were deducted by UNRWA and the balance of \$ 475,000 was loaned to the MMD to manage program activities.

During year 2005 UNRWA/MMD received a total of USD 2,000,000. An amount of USD 500,000 was received by Gaza Branch, and another USD 1,500,000 was received by the West Bank Branch. The amount of USD 100,000 was paid to UNRWA as Program Support Cost (PSC) calculated at 5% of the amount received. The balance of \$ 1,900,000 represents the net liability to UNRWA under the second instalment bringing the total accumulated liability to \$ 2,375,000 as of 31 December 2005.

## **8. Grants and Donations**

Summary of grants and donations during 2004 to 2006 is as follows:

### **8.1.1- Netherlands Minister for Development Cooperation**

According to the Grant Agreement number RAM0064625 Activity number 13168 signed on December 1, 2005 between the Netherlands Minister for Development Cooperation and United Nations Relief and Works Agency for Palestine Refugees in the Near East (UNRWA), the amount of \$4,800,000 was earmarked to support UNRWA project proposal "Microfinance and disengagement: supporting economic recovery and rehabilitation through microenterprise and housing credit, for the period from 1 December 2005 up to and including 1 December 2006. The funds shall be transferred in advance in instalments amounting to a maximum of 72% of the total contribution of \$4,800,000 (not exceeding Euro 4 million). The final instalment shall be paid after the definitive amount of the contribution has been determined in the final narrative and financial report.

The funds shall be administered and accounted for in accordance with UNRWA financial regulations and other applicable rules, procedures and practices and a separate records and accounts of the programme shall be maintained. In accordance with these regulations, UNRWA deducts 7% from funds available to MMD to cover program support costs (PSC).

According to the Grant budget, funding to MMD is as follows excluding UNRWA, PSC of 7%:

	<u>USD</u>
Total MMD Portion	4,800,000
Less UNRWA PSC	<u>314,019</u>
<b>Net to MMD</b>	<b><u>4,485,981</u></b>
Allocated to Revolving Fund Capital	4,285,981
Allocated to Operating costs-Bethlehem branch	200,000
Amount Spend during 2006-Bethlehem branch	93,487
Balance carried forward for year 2007(pledges Receivable)	106,513
Value of amount received funded for loans	
For Gaza MMD	2,551,869
For West Bank MMD	<u>1,676,816</u>
Total Restricted Fund	4,228,685
Gaza Distributed Year 2005-2006(Note 9)	(2,275,691)
West bank Distributed Year 2006(Note 9)	<u>1,676,695</u>
Net of Fund Temporary Restricted	276,299
Add: Pledges Receivables	<u>74,415</u>
Balance Available for year 2007 ( Temporary Restricted )	<b><u>\$ 350,714</u></b>

#### 8.1.2- The Government of Canada

According to the Grant Agreement number 7041359 Project number Z-020711 signed on February 28, 2006 between the "Government of Canada as represented by the Minister for International Cooperation, acting through the Canadian International Development Agency (CIDA) and United Nations Relief and Works Agency for Palestine Refugees in the Near East (UNRWA), for the provision of micro-credit, job creation, and shelter rehabilitation activities that form part of UNRWA contribution to the Gaza Disengagement Plan. According to the budget, the amount allocated to the MMD programme was as follows:

Microfinance lending	\$1,000,000
Microenterprise training (12 months)	\$ 200,000

The duration of implementation under the agreement was from date of signature on 28 February 2006 through 31 December 2007, however, management represented that CIDA allowed charging to the grant as from November 2005 on the Microfinance component.

According to UNRWA financial policies and guidelines, the amount of 6% from MMD allocation is charged by UNRWA as Program Support Cost (PSC). The following is a detail of the pledge receivable that was recorded in the books as at 31 December 2005.

	<u>USD</u>
Micro-finance lending	1,000,000
P.S.C	(56,650)
Disbursed During 2006 ( Note 9 )	(943,350)
Balance Available	.0
Micro-enterprise training ( 12 months)	200,000
P.S.C	(11,321)
Amount Spend During 2006	(103,783)
Balance Available for year 2007 " Pledges Receivables "	(84,896)
Net Balance	0

#### 8.1.3- Arab Gulf Program for United Nations Development Organizations

In June 2003, UNRWA and the AGFUND concluded a grant agreement by which the donor pledged to contribute \$80,000 towards "Solidarity Group Lending Product / Palestine. The amounts shown below represent MMD allocation net of UNRWA program support costs of 12%. The project is implemented and the full amounts shown below have been released to Loan Revolving Fund Capital

2005	\$31,250
2006	\$40,150
Total	<u>\$71,400</u>

#### 8.1.4 Arab Authority for Agricultural Investment and Development (AAAID)

The Arab Authority for Agricultural Investment and Development (hereinafter referred to as "AAAID") undertakes to make available to the United Nations Relief and Works Agency for Palestine Refugees in the Near East (hereinafter referred to as "UNRWA") a financial contribution in the amount of USD 2 million (USD two million). UNRWA will utilize the financial contribution for the project in the Microfinance and Income Generation entitled: "Supporting Sustainable Live hoods and Durable Income through Microenterprise Credit" which is managed by Microfinance and Microenterprise Department (MMD) - UNRWA.

According to the contract agreement UNRWA will administer the contribution and it will receive 6% from the contribution as Programme Support Cost (PSC) and Microfinance and Microenterprise Department will manage the fund.

Following is the contribution detail as at 31 December 2006.

	<u>USD</u>
Total Fund Received	2,000,000
Less : P.S.C %	(113,253)
Amount Received :	<u>1,886,747</u>
Gaza Field Received	735,759
West Bank Field Received	1,150,988

Spent to 31/12/2006 by Gaza Field ( Note 9 )	(331,400)
Spent to 31/12/2006 by West Bank Field ( Note 9 )	(748,023)
Balance Available temporary restricted	<u>807,324</u>

The AAAID funded regional office in Jordan for furniture and equipment which will be used in 2007.

<b>Pledges Receivables</b>	<b>9,990</b>
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#### **9. Revolving Loan Fund**

*Revolving Loan Fund* - Restricted contributions received for on lending purposes, which were expended in term of loans, are included in the Revolving Loan Fund.

Composition of this fund by funding source as at 31 December 2006 is as follows:

	<u>Gaza</u>	<u>West Bank</u>	<u>Syria</u>	<u>Total</u>
	<u>USD</u>	<u>USD</u>	<u>USD</u>	<u>USD</u>
Australia	619,272	-		619,272
Canada	200,370	170,220		370,590
Germany	1,682,252	1,276,323		2,958,575
Italy	725,750	218,500		944,250
Japan	357,142	223,199		580,341
New Zealand	122,822	-		122,822
Norway	2,794,013	340,968		3,134,981
UNRWA	80,000	-		80,000
AGFUND	131,400	-	53,571	184,971
CIDA	943,350	-		943,350
Netherlands	2,275,691	1,676,695		3,952,386
USAID	4,237,197	-		4,237,197
AAAID	331,400	748,023		1,079,423
<b>Grand Total</b>	<b>14,500,659</b>	<b>4,653,928</b>	<b>53,571</b>	<b>19,208,157</b>

#### **10. Geographical Segments**

MMD operates out of four principle field offices located in the West Bank, Gaza, Jordan, and Syria. In presenting information on the basis of geographical segments, segment revenue is based on the geographical location of borrowers. Segment assets are based on the geographical location of assets.

10.1 Statement of Balance Sheet by Geographical Segment

Assets	Gaza		West Bank		Jordan		Syria		Total	
	2006	2005	2006	2005	2006	2005	2006	2005	2006	2005
	USD	USD	USD	USD	USD	USD	USD	USD	USD	USD
<b>Non-Current Assets:</b>										
Property, Plant and Equipment	119,664	108,640	236,810	242,179	55,394	38,580	48,083	40,469	479,952	429,868
Loans Receivable, Net	599,177	159,680	-	-	-	-	-	-	599,177	159,680
	<b>718,841</b>	<b>268,320</b>	<b>236,810</b>	<b>242,179</b>	<b>55,394</b>	<b>38,580</b>	<b>48,083</b>	<b>40,469</b>	<b>1,079,129</b>	<b>589,548</b>
<b>Current Assets :</b>										
Loan Receivable, Net	1,207,304	3,977,290	1,909,733	2,385,661	1,282,591	912,004	744,117	584,686	5,143,747	7,859,641
Pledges Receivable	159,311	943,396	106,513	-	9,990	-	-	-	275,814	943,396
Prepayment and other Receivables	32,722	3,916	60,152	-	7,150	-	4,210	-	104,233	3,916
Cash and Cash Equivalents	7,108,561	5,170,847	2,780,590	1,789,381	226,722	238,692	257,059	275,692	10,372,931	7,494,612
	<b>8,507,898</b>	<b>10,095,449</b>	<b>4,856,988</b>	<b>4,175,042</b>	<b>1,526,453</b>	<b>1,170,696</b>	<b>1,005,386</b>	<b>860,378</b>	<b>15,896,724</b>	<b>16,101,565</b>
<b>Total Assets</b>	<b>9,226,739</b>	<b>10,363,769</b>	<b>5,113,798</b>	<b>4,417,221</b>	<b>1,581,847</b>	<b>1,209,276</b>	<b>1,053,470</b>	<b>900,847</b>	<b>16,975,853</b>	<b>16,891,113</b>
<b>Equity</b>										
General Undesignated Fund Held for Training	(3,221,289)	(1,427,992)	(3,417,990)	(3,163,236)	57,060	29,892	(55,016)	(98,838)	(6,637,236)	(4,660,194)
Temporary Restricted Fund	62,253	19,296	-	-	-	-	-	-	62,253	19,296
Board Designated Fund/MIS System	734,952	1,639,987	403,086	1,267,991	-	-	-	-	1,158,038	2,927,978
Revolving Loan Fund	36,976	45,000	-	-	-	-	-	-	36,976	45,000
	14,500,659	12,336,468	4,653,928	2,229,210	-	-	53,371	53,371	19,208,157	14,619,249
<b>Total Equity</b>	<b>12,133,551</b>	<b>12,632,759</b>	<b>1,639,024</b>	<b>333,965</b>	<b>57,060</b>	<b>29,892</b>	<b>(1,445)</b>	<b>(45,287)</b>	<b>13,828,189</b>	<b>12,951,329</b>
<b>Non-Current Liabilities</b>										
Retirement Benefit Obligations	46,983	40,980	36,682	32,670	-	-	-	-	83,665	73,650
	<b>46,983</b>	<b>40,980</b>	<b>36,682</b>	<b>32,670</b>	<b>-</b>	<b>-</b>	<b>-</b>	<b>-</b>	<b>83,665</b>	<b>73,650</b>
<b>Current Liabilities :</b>										
Payables and Accounts Inter-Office Accounts	108,434	10,875	212,241	12,700	19,168	12,112	4,583	10,925	344,426	46,613
Bills Payable to UNRWA	(4,800,099)	(4,815,923)	2,299,907	2,768,380	1,474,418	1,130,511	1,025,774	917,032	-	-
Liability to UNRWA-OPEC Pal Trust Fund	138,065	1,056,371	130,749	333,213	31,201	36,761	24,558	18,177	-	-
	1,599,805	1,438,707	775,195	936,293	-	-	-	-	344,573	1,444,522
<b>Total Current Liabilities</b>	<b>(2,953,795)</b>	<b>(2,309,970)</b>	<b>3,438,092</b>	<b>4,050,586</b>	<b>1,524,787</b>	<b>1,179,384</b>	<b>1,054,915</b>	<b>946,134</b>	<b>2,375,000</b>	<b>2,375,000</b>
<b>Total Liabilities</b>	<b>(2,906,812)</b>	<b>(2,268,990)</b>	<b>3,474,774</b>	<b>4,083,256</b>	<b>1,524,787</b>	<b>1,179,384</b>	<b>1,054,915</b>	<b>946,134</b>	<b>3,063,999</b>	<b>3,866,134</b>
<b>Total Equity and Liabilities</b>	<b>9,226,739</b>	<b>10,363,769</b>	<b>5,113,798</b>	<b>4,417,221</b>	<b>1,581,847</b>	<b>1,209,276</b>	<b>1,053,470</b>	<b>900,847</b>	<b>16,975,853</b>	<b>16,891,113</b>

10.2 Statement of Profit and Loss by geographical Segment

	Gaza		West Bank		Jordan		Syria		Central Office		Total	
	2006	2005	2006	2005	2006	2005	2006	2005	2006	2005	2006	2005
	USD	USD	USD	USD	USD	USD	USD	USD	USD	USD	USD	USD
<b>Interest and Other Operating Income :</b>												
Interest on Loans	760,214	1,208,916	906,150	699,751	417,905	313,122	285,072	150,841	-	-	2,369,341	2,372,630
Accrued Interest Revenue	14,117	-	27,854	-	5,831	-	294	-	-	-	48,096	-
Interest on Bank Deposit and other revenues	164,936	30,145	84,682	7,415	11,112	4,720	10,812	2,249	-	-	271,542	44,529
<b>Total Operating Revenues</b>	<b>939,267</b>	<b>1,239,061</b>	<b>1,018,686</b>	<b>707,166</b>	<b>434,848</b>	<b>317,842</b>	<b>296,178</b>	<b>153,090</b>	-	-	<b>2,688,979</b>	<b>2,417,159</b>
<b>Impairment Losses On Loans</b>												
Provision Expenses for Impaired Loans	1,356,498	294,987	482,347	391,140	58,773	42,609	31,773	3,432	-	-	1,929,390	732,168
Recoveries from Written Loans	179,192	311,467	277,946	339,128	12,342	4,620	2,414	169	-	-	471,894	655,384
<b>Net Impairment Losses On Loans</b>	<b>1,177,306</b>	<b>(16,480)</b>	<b>204,401</b>	<b>52,012</b>	<b>46,431</b>	<b>37,989</b>	<b>29,359</b>	<b>3,263</b>	-	-	<b>1,457,496</b>	<b>76,784</b>
<b>Operating Expense</b>												
Salaries and Related Exp.	1,105,833	1,029,220	760,760	647,096	142,691	94,835	68,274	55,369	335,823	275,603	2,413,381	2,102,123
Special Service Contracts	27,480	35,135	24,255	40,931	2,754	20,345	3,375	16,914	34,530	13,525	92,395	126,850
Occupancy	57,023	59,682	56,248	63,731	14,880	8,745	22,366	16,102	1,726	3,031	152,242	151,291
Communication	24,181	23,763	24,811	23,112	12,017	6,024	3,150	3,058	781	2,696	64,940	58,653
Stationary and Supplies	29,233	25,546	36,866	35,924	17,112	3,281	5,503	1,699	93,367	6,637	182,081	73,087
Minor Equipment & Maint.	13,167	6,220	3,844	6,821	689	827	813	1,026	734	-	19,226	14,894
Travel and Transportation	30,903	49,151	49,669	33,521	4,754	2,491	2,380	8,624	29,597	18,770	117,503	112,557
Depreciation	32,313	23,592	25,817	28,581	11,974	8,804	11,969	13,063	36,429	19,949	118,501	93,989
Loss on Exchange Difference	(6,469)	2,070	(1,521)	(4,382)	658	544	(13,585)	1,638	-	-	(20,917)	(130)
Program Support Cost	13,452	15,739	13,188	28,799	5,436	3,934	4,359	4,108	7,535	-	43,970	52,580
Cash Losses	-	-	-	385	-	-	-	-	-	-	-	-
Training	16,883	2,395	3,456	1,000	6,061	837	5,615	5,225	-	-	34,720	5,610
Others	780	2,476	986	1,463	872	1,436	2,715	1,227	2,704	-	5,353	11,336
<b>Total Operating Expenses</b>	<b>1,344,779</b>	<b>1,374,989</b>	<b>998,379</b>	<b>906,982</b>	<b>219,878</b>	<b>152,103</b>	<b>117,134</b>	<b>133,850</b>	<b>543,225</b>	<b>340,375</b>	<b>3,223,395</b>	<b>2,808,299</b>
Allocation of Central Office Operating Expenses	211,858	204,225	244,452	136,150	48,890	-	38,025	-	(543,225)	(340,375)	-	-
Allocation of Jerusalem Office	160,298	-	-	-	92,480	-	67,818	-	-	-	-	-
<b>Operating Income/(Loss) /Year</b>	<b>1,794,675</b>	<b>(223,673)</b>	<b>(268,348)</b>	<b>(387,978)</b>	<b>27,169</b>	<b>127,750</b>	<b>43,842</b>	<b>15,977</b>	<b>-</b>	<b>-</b>	<b>1,991,913</b>	<b>(467,924)</b>

## **Risk**

Risk is inherent in the microfinance industry. Effective risk management is seen as the only way for microfinance institutions to keep functioning.

Ultimate responsibility for effective management of risks rests with the Director of the Microfinance Microenterprise Department.

Several types of Risks apply to the MMD, these are:

- **Credit Risk** is the risk that counterparty will not settle its obligations in accordance with the agreed terms.
- **Country Risk** is the risks that counterparty is unable to meet its contractual obligations as a result of adverse economic conditions or actions taken by government in the relevant country.
- **Market Risk** is the exposure created by the potential changes in market prices.
- **Liquidity Risk** is the risk that funds will not be available to meet liabilities as they fall due.
- **Operational and Other Risks** is the risk of direct and indirect loss due to an event or action causing the risks having operational risk impact.
- **Political Risk** is the risk that an existing political situation makes it difficult for Microfinance Institutions to function for example war situations.

In occupied Palestinian Territories, because of the present circumstances, political risk, country risk and credit risk are very high, while country and political risk remains low in both Jordan and Syria. To mitigate the risk in the oPt, management did the following;

- a. SSE Loans were significantly reduced starting with 2001. In this category the amount of loans is relatively high, which bears a high risk factor because of the present situation. Management decided to significantly reduce its activities under this programme in both Gaza and West Bank and has currently ceased all SSE lending in the West Bank.
- b. Management concentrated on expanding activities under MEC and SGL products categories. These loans, range between \$1,000 to \$8,000 and \$400 to \$4,000 respectively, and aim at distributing the risk to a larger number of borrowers. However, even here management has to reduce lending in 2006 due to increasing risk in the oPt.
- c. Management introduced a new housing loan product in Gaza with very tight collateral conditions that mitigated the political and country risk.
- d. The currently effective internal control system and procedures were further tightened up. Constant follow-up and loan-monitoring procedures were introduced to reduce Credit Risk of borrowers. However, the department now has to operate in a market where policing and the enforcement of contract law through the courts are highly dysfunctional and barely operating.
- e. To reduce general portfolio risk, management is rapidly expanding the portfolio in Jordan and Syria where portfolio quality remains high and can offset risk in the oPt.

## 12. Portfolio Quality

### a. Portfolio at Risk Ratio:

Portfolio at risk ratio (balance of loans in arrears / value of loans outstanding) measures amount of default risk in portfolio. An increasing portfolio at risk is negative.

Value of loans in arrears = the outstanding balance (principal remaining to be paid) of loans that are at higher risk because a Payment is late

#### Portfolio at Risk

	2006		2005	
	Principal Outstanding	Portfolio at Risk Ratio	Principal Outstanding	Portfolio at Risk Ratio
	USD		USD	
Current	4,655,955		4,561,900	
1 to 30	691,721	9.05 %	2,340,629	25.75%
31 to 60	238,338	3.12 %	647,270	7.12 %
61 to 90	132,869	1.74 %	375,012	4.12 %
91 to 120	142,555	1.86 %	233,638	2.57 %
121 to 180	364,589	4.77 %	298,994	3.28 %
181 to 360	1,421,143	18.58 %	631,776	6.95 %
	<b>7,647,169</b>	<b>39.12 %</b>	<b>9,089,219</b>	<b>49.79 %</b>
<b>Portfolio at risk over 30 days</b>		<b>30.07 %</b>		<b>24.05%</b>

### b. Portfolio in Arrears Ratio:

Portfolio in arrears ratio (Value of Payments in Arrears / Value of Loans Outstanding), the ratio indicates amount of loan payments past due. An increasing portfolio in arrears is negative.

Value of loans in arrears = is the value of payments due (unpaid loan instalments).

#### Portfolio in Arrears

	2006		2005	
	Payments in Arrears	Portfolio in Arrears Ratio	Payments in Arrears	Portfolio in Arrears Ratio
	USD	Percent	USD	Percent
1 to 30	235,642	3.08 %	404,036	4.45 %
31 to 60	175,226	2.29 %	216,405	2.38 %
61 to 90	179,086	2.34 %	144,965	1.59 %
91 to 120	208,152	2.72 %	119,083	1.31 %
121 to 180	432,331	5.65 %	177,247	1.95 %
181 to 360	820,436	10.73 %	323,624	3.56 %
	<b>2,050,873</b>	<b>26.82 %</b>	<b>1,385,360</b>	<b>15.24 %</b>

**c. Operating Self Sufficiency Ratio:**

Operating Self Sufficiency ratio (Interest and Recovery / Operating expenses and additional provision for loan losses), the ratio measures how well the MMD covers its cost through its operating activities. An increasing operating self sufficiency ratio is positive.

	2006	2005
Interest and Recovery	2,889,330	3,028,014
Operating Expenses	5,152,785	3,540,467
<b>Operating Self Sufficiency Ratio</b>	<b>56 %</b>	<b>86 %</b>

The significant decline in the operating self-sufficiency (OSS) ratio in 2006 was mainly due to the significant increase in risk of the MMD's operations in Gaza where the OSS was just 32 percent. The performance of the MMD's West Bank operations improved in 2006 when the OSS reached 77 percent, while the OSS of the department's credit operations in Jordan and Syria were 104 and 113 percent respectively.

**d. Loan Officer Productivity:**

Loan Officer Productivity (Number of Active Borrowers / Number of Loan Officers), the ratio measures the average caseload of each loan officer. An increasing Loan Officer Productivity ratio is positive.

	2006	2005
Number of Active Borrowers	12,351	14,726
Number of Loan Officers	107	126
<b>Loan Officer Productivity</b>	<b>115</b>	<b>117</b>

Loan officer productivity fell as a result of the economic situation in the oPt, especially the reduced performance of activities in Gaza.