

ASIAN INFRASTRUCTURE INVESTMENT BANK

AIIB PROJECT PREPARATION SPECIAL FUND

**AUDITOR'S REPORT AND FINANCIAL STATEMENTS
FOR THE PERIOD FROM 24 JUNE 2016 (DATE OF THE
ESTABLISHMENT OF THE SPECIAL FUND) TO 31 DECEMBER 2016**



Independent Auditor's Report

To the Board of Governors of the Asian Infrastructure Investment Bank (the "Bank"):

Opinion

What we have audited

The financial statements of AIIB Project Preparation Special Fund (the "Special Fund") set out on pages 1 to 12, which comprise:

- the statement of comprehensive income for the period from 24 June 2016 (date of the establishment of the Special Fund) to 31 December 2016;
- the statement of financial position as at 31 December 2016;
- the statement of changes in contributors' resources for the period from 24 June 2016 to 31 December 2016;
- the statement of cash flows for the period from 24 June 2016 to 31 December 2016; and
- the notes to the financial statements, which include a summary of significant accounting policies.

Our opinion

In our opinion, the financial statements give a true and fair view of the financial position of the Special Fund as at 31 December 2016, and of its financial performance and its cash flows for the period from 24 June 2016 to 31 December 2016 in accordance with International Financial Reporting Standards ("IFRS").

Basis for Opinion

We conducted our audit in accordance with International Standards on Auditing ("ISA"). 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 Special Fund in accordance with the International Ethics Standards Board for Accountants' Code of Ethics for Professional Accountants ("IESBA Code"), and we have fulfilled our other ethical responsibilities in accordance with the IESBA Code.

Responsibilities of Management and Board of Directors of the Bank for the Financial Statements

Management is responsible for the preparation of the financial statements that give a true and fair view in accordance with IFRS, and for such internal control as 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, management is responsible for assessing the Special Fund'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 management either intend to liquidate the Special Fund or to cease operations, or has no realistic alternative but to do so.

The Board of Directors is responsible for overseeing the Special Fund's financial reporting process.

Auditor's Responsibilities for the Audit of the Financial Statements

Our objectives are to obtain reasonable assurance about whether the financial statements as a whole are free from material misstatement, whether due to fraud or error, and to issue an auditor's report that includes our opinion. We report our opinion solely to you, as a body, in accordance with our agreed terms of engagement and for no other purpose. We do not assume responsibility towards or accept liability to any other person for the contents of this report. Reasonable assurance is a high level of assurance, but is not a guarantee that an audit conducted in accordance with ISA will always detect a material misstatement when it exists. Misstatements can arise from fraud or error and are considered material if, individually or in the aggregate, they could reasonably be expected to influence the economic decisions of users taken on the basis of these financial statements.

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

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

- Conclude on the appropriateness of management's 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 Special Fund'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 Special Fund to cease to continue as a going concern.
- Evaluate the overall presentation, structure and content of the financial statements, including the disclosures, and whether the financial statements represent the underlying transactions and events in a manner that achieves fair presentation.

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



PricewaterhouseCoopers
Certified Public Accountants

Hong Kong, 21 March 2017

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AIIB PROJECT PREPARATION SPECIAL FUND

Statement of Comprehensive Income

For the period from 24 June 2016 (Date of the Establishment of the Special Fund) to 31 December 2016


<i>In thousands of US Dollars</i>	Note	For the period from 24 June 2016 to 31 December 2016
Income		-
General and administrative expenses	3.1	(126)
Net loss and total comprehensive loss for the period		(126)
Attributable to:		
Contributors		(126)

The accompanying notes are an integral part of these financial statements.


AIIB PROJECT PREPARATION SPECIAL FUND
Statement of Financial Position
As at 31 December 2016

<i>In thousands of US Dollars</i>	Note	31 December 2016
Assets		
Cash and cash equivalents		9,900
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Total assets		9,900
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Liabilities		
Other liabilities	3.2	26
Contributors' resources		
Contribution	3.3	10,000
Accumulated losses		<u>(126)</u>
Total Contributors' resources		9,874
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Total liabilities and Contributors' resources		9,900
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The accompanying notes are an integral part of these financial statements.



 Mr. Jim Maqun
 President of the Bank



 Mr. Thierry de Longuemar
 Vice President
 and Chief Financial Officer of the Bank

AIIB PROJECT PREPARATION SPECIAL FUND
Statement of Changes in Contributors' Resources
For the period from 24 June 2016 (Date of the Establishment of the Special Fund) to 31 December 2016

In thousands of US Dollars

	Note	Contribution	Accumulated loss	Total
As at 24 June 2016		-	-	-
Contribution	3.3	10,000	-	10,000
Total comprehensive loss for the period		-	(126)	(126)
As at 31 December 2016		10,000	(126)	9,874

The accompanying notes are an integral part of these financial statements.

AIIB PROJECT PREPARATION SPECIAL FUND**Statement of Cash Flows**

For the period from 24 June 2016 (Date of the Establishment of the Special Fund) to 31 December 2016

<i>In thousands of US Dollars</i>	Note	For the period from 24 June 2016 to 31 December 2016
Cash flows from operating activity		
Net loss for the period		(126)
Adjustments for:		
Increase in other liabilities	3.2	26
Net cash used in operating activity		(100)
Cash flows from financing activity		
Contribution received	3.3	10,000
Net cash from financing activity		10,000
Net increase in cash and cash equivalents		9,900
Cash and cash equivalents as at 24 June 2016		-
Cash and cash equivalents as at 31 December 2016		9,900

The accompanying notes are an integral part of these financial statements.

AIIB PROJECT PREPARATION SPECIAL FUND

Notes to the Financial Statements

For the period from 24 June 2016 (Date of the Establishment of the Special Fund) to 31 December 2016
(All amounts in thousands of US Dollars unless otherwise stated)

1 GENERAL INFORMATION

On 24 June 2016, the AIIB Project Preparation Special Fund (the "Special Fund") was established as a special fund of the Asian Infrastructure Investment Bank (the "Bank" or "AIIB") in accordance with Article 17.1 of the Bank's Articles of Agreement (the "AOA").

The Special Fund is established as a multi-donor fund, which is open to contributions by all the Bank's members and others (the "Contributors"). The purpose of the Special Fund is to support and facilitate, on a concessional basis, the preparation of projects of low and middle income countries. The resources from the Contributors are accepted, held, managed, administered, used, committed, expended or otherwise disposed of by the Bank in accordance with the AOA, the Rules and Regulations of the Special Fund and the Contribution Agreements. On 25 June 2016, the Ministry of Finance of the People's Republic of China (the "China MOF") and the Bank signed a Contribution Agreement in respect of a contribution of USD 50 million. As of 31 December 2016, the first instalment of the contribution from the China MOF in an amount of USD 10 million has been received by the Special Fund.

These financial statements were signed by the President and the Vice President and Chief Financial Officer of the Bank on 21 March 2017.

2 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

2.1 Basis of preparation

These financial statements for the Special Fund have been prepared in accordance with International Financial Reporting Standards ("IFRS") as issued by the International Accounting Standards Board ("IASB"). Based on the By-Laws of the AIIB, the financial year of the Bank begins on 1 January and ends on 31 December of each year. The Special Fund follows the same financial year end as the Bank. For the year in which the Special Fund established, the financial year begins on the date of the establishment of the Special Fund and ends on 31 December of that year. The financial statements for the period from the date of the establishment of the Special Fund on 24 June 2016 to 31 December 2016 are the first annual financial statements of the Special Fund.

The Special Fund has adopted all the standards and interpretations effective for annual periods on 1 January 2016. In addition, the Special Fund has early adopted IFRS 9 *Financial Instruments* (full version issued in July 2014 and mandatorily effective on 1 January 2018), IFRS 15 *Revenue from Contracts with Customers* (mandatorily effective on 1 January 2018), and IFRS 16 *Leases* (mandatorily effective on 1 January 2019). The financial statements have been prepared under the historical cost convention, except for the financial assets measured at fair value.

AIIB PROJECT PREPARATION SPECIAL FUND

Notes to the Financial Statements

For the period from 24 June 2016 (Date of the Establishment of the Special Fund) to 31 December 2016
(All amounts in thousands of US Dollars unless otherwise stated)

2.2 New accounting pronouncements

Certain amendments to IFRS have been issued but are not mandatory for annual periods ended on 31 December 2016. The Special Fund has not early adopted those amendments and does not expect those amendments to have a material impact on the Special Fund. These amendments mainly include:

- (i) IFRIC 22 Foreign currency transactions and advance consideration; and
- (ii) IAS 7 Amendments disclosure initiative

2.3 Functional currency and foreign currency transactions

The functional currency and the presentation currency of the Special Fund is United States Dollar ("USD" or "US Dollar").

There were no foreign currency transactions for the period from 24 June 2016 to 31 December 2016.

2.4 Financial instruments

2.4.1 Financial assets

The Special Fund's financial assets are classified into three categories:

- (a) Amortised cost,
- (b) Fair value through other comprehensive income (FVOCI), or
- (c) Fair value through profit or loss (FVPL).

The basis of classification depends on the Special Fund's business model and the contractual cash flow characteristics of the financial asset.

(a) Classification of financial assets at amortised cost

The Special Fund classifies its financial assets at amortised cost only if both of the following criteria are met:

- (i) The financial asset is held within a business model with the objective of collecting the contractual cash flows, and
- (ii) The contractual terms give rise on specified dates to cash flows that are solely payments of principal and interest on the principal outstanding.

The Special Fund applies the effective interest method to the amortised cost of a financial asset.

AIIB PROJECT PREPARATION SPECIAL FUND

Notes to the Financial Statements

For the period from 24 June 2016 (Date of the Establishment of the Special Fund) to 31 December 2016
(All amounts in thousands of US Dollars unless otherwise stated)

(b) Classification of financial assets at FVOCI

Financial assets at FVOCI comprise:

- (i) Financial assets having contractual cash flows which reflect solely payments of principal and interest on outstanding principal, and for which the objective of the related business model is achieved both by collecting contractual cash flows and selling financial assets, and
- (ii) Investments in equity instruments which are neither held for trading nor contingent consideration, and for which the Special Fund has made an irrevocable election at initial recognition to recognise changes in fair value through OCI rather than profit or loss.

For (i) above, interest is calculated using the effective interest method and recognised in profit or loss. Except for gains or losses from impairment and foreign exchange, the financial asset is measured at FVOCI. When the financial asset is derecognised, the cumulative gain or loss previously recognised in OCI is reclassified to profit or loss.

For (ii) above, investments in equity instruments are required to be measured at FVPL with the irrevocable option at inception to present changes in fair value in OCI, in which case the accumulated fair value changes in OCI will not be reclassified to profit or loss in the future. Dividends on such investments are recognised in profit or loss, unless the dividend clearly represents a recovery of part of the cost of the investment.

(c) Classification of financial assets at FVPL

The Special Fund classifies the following financial assets at FVPL:

- (i) Financial assets that do not qualify for measurement at either amortised cost or at FVOCI, ,
- (ii) Financial assets that are designated at initial recognition as FVPL irrevocably, when such designation eliminates or significantly reduces a measurement or recognition inconsistency that would otherwise arise,
- (iii) Investment in equity instruments that are held for trading, and
- (iv) Investment in equity instruments for which the entity has not elected to recognise fair value gains and losses through OCI.

2.4.2 Financial liabilities

The Special Fund's financial liabilities are measured at amortised cost, using the effective interest method. The interest expenses, if any, are recognised in profit or loss.

AIIB PROJECT PREPARATION SPECIAL FUND

Notes to the Financial Statements

For the period from 24 June 2016 (Date of the Establishment of the Special Fund) to 31 December 2016
(All amounts in thousands of US Dollars unless otherwise stated)

2.4.3 Contributors' resources

The Special Fund recognises contributions received from Contributors as an equity on the basis that a contributor cannot choose to withdraw contributions from the Special Fund. Contributors are only entitled to a distribution of net assets on termination of the Special Fund in proportion to the contributions made available by them to the Special Fund.

2.4.4 Recognition and derecognition

The Special Fund recognises a financial asset or a financial liability in its statement of financial position when, and only when, the entity becomes party to the contractual provisions of the instrument.

At initial recognition, the Special Fund measures a financial asset or financial liability at its fair value plus or minus, in the case of a financial asset or financial liability not at fair value through profit or loss, transaction costs that are directly attributable to the acquisition or issue of the financial asset or financial liability.

Before evaluating whether, and to what extent, derecognition is appropriate, the Special Fund determines whether the derecognition analysis applied to a part of a financial asset or a financial liability in its entirety. The Special Fund derecognises a financial asset when the contractual rights to the cash flows from the asset expire, or when it transfers the financial asset and substantially all the risks and rewards of ownership of the asset to another entity. If the Special Fund neither transfers nor retains substantially all the risks and rewards of ownership and has not retained control of the transferred asset, the Special Fund derecognises the financial asset and recognises separately as assets or liabilities any rights and obligations created or retained in the transfer.

2.5 Statement of cash flows

The statement of cash flows is prepared using the indirect method. Cash and cash equivalents comprise balances with less than three months maturity from the date of the transaction, which are available for use at short notice and that are subject to insignificant risk of changes in value.

2.6 Cash and cash equivalents

Cash and cash equivalents are items which are readily convertible to known amounts of cash and which are subject to an insignificant risk of changes in value. Deposits with a maturity of three months or less are classified as cash and cash equivalents.

AIIB PROJECT PREPARATION SPECIAL FUND

Notes to the Financial Statements

For the period from 24 June 2016 (Date of the Establishment of the Special Fund) to 31 December 2016
(All amounts in thousands of US Dollars unless otherwise stated)

2.7 Interest income

Interest is recorded on an accrual basis. All interest income is recognised within 'interest income' in the statement of comprehensive income.

2.8 Administration fees and expenses

In accordance with the provisions of Section 4.05 of the Rules and Regulations of the Special Fund, the Bank shall receive an administration fee equal to one percent of the amount of the contribution. A proportionate amount of such administration fee shall be debited from each instalment of the contribution paid in by the Contributors and credited to the Bank's ordinary resources. Administration fees and expenses are recognised throughout the period to the satisfaction of the relevant services received.

2.9 Current and non-current presentation

All assets and liabilities in the statement of financial position are classified as current as at 31 December 2016.

2.10 Taxation

In accordance with Article 51 of the AOA, within the scope of its official activities, the Bank, its assets, property, income, and its operations and transactions, shall be exempt from all taxation and from all custom duties in its member countries. Article 51 of the AOA also exempts the Bank from any obligation for the payment, withholding, or collection of any tax or duty.

AIIB PROJECT PREPARATION SPECIAL FUND

Notes to the Financial Statements

For the period from 24 June 2016 (Date of the Establishment of the Special Fund) to 31 December 2016
(All amounts in thousands of US Dollars unless otherwise stated)

3 NOTES TO THE FINANCIAL STATEMENTS

3.1 General and administrative expenses

For the period from 24 June 2016 to 31 December 2016, general and administrative expenses are as follows:

AIIB administration fee	100
External auditor's remuneration	26
Total general and administrative expenses	126

3.2 Other liabilities

	31 December 2016
External auditor's remuneration payable	26
Total other liabilities	26

3.3 Contribution

As at 24 June 2016	-
Cumulative contribution received:	
China MOF	10,000
As at 31 December 2016	10,000

3.4 Fair value of financial assets and financial liabilities

The carrying amounts of financial assets and liabilities presented on the statement of financial position approximate their fair values.

AIIB PROJECT PREPARATION SPECIAL FUND

Notes to the Financial Statements

For the period from 24 June 2016 (Date of the Establishment of the Special Fund) to 31 December 2016
(All amounts in thousands of US Dollars unless otherwise stated)

3.5 Related parties

The Special Fund's related parties are the Bank and the Contributors.

The Bank is entitled to charge the Special Fund an administration fee of an amount equal to one percent of contributions received. An administration fee of USD 0.1 million was charged for the period from 24 June 2016 to 31 December 2016. There was no accrued administration fee payable by the Special Fund to the Bank as at 31 December 2016.

The contributions received from Contributors are outlined in Note 3.3.

3.6 Financial risk management

(a) Overview

The Special Fund follows the risk management framework and policies of the Bank. The Bank adopts a proactive and comprehensive approach to risk management that is instrumental to the Bank's financial viability and success in achieving its mandate. The ability to identify, mitigate, and manage risk begins with the Bank's policies being established with a strong risk culture. In addition to establishing appropriate risk parameters and a thorough project review and portfolio monitoring process, the risk management function provides an independent oversight of credit, market, liquidity, operational, and associated reputational risk in the Bank's activities, and ensure the integration of asset and liability management.

As the primary purpose of the Special Fund is to support and facilitate, on a concessional basis, the preparation of projects of low and middle income countries, rather than to generate a return on its assets, for the period ended 31 December 2016, the Special Fund was not exposed to most financial risks, with exception to credit risk associated with the financial institutions with which it deposits its cash resources.

(b) Credit risk

Credit risk management

The Special Fund takes on exposure to credit risk, which is the risk that one party to a financial instrument will cause a financial loss for the other party by failing to discharge an obligation.

In managing the Special Fund's credit exposure to financial institutions, AIIB applies the same rules and principles as in managing its own special funds. The credit rating of the financial institution counterparties is single A or higher.

The carrying amount of cash and cash equivalents presented on the statement of financial position represents the Special Fund's maximum exposure to credit risk as at 31 December 2016.

AIIB PROJECT PREPARATION SPECIAL FUND

Notes to the Financial Statements

For the period from 24 June 2016 (Date of the Establishment of the Special Fund) to 31 December 2016
(All amounts in thousands of US Dollars unless otherwise stated)

3.7 Events after the reporting period

On 28 February 2017, the China MOF made a second instalment amounted to USD 20 million in respect of its USD 50 million contribution to the Special Fund. There have been no other material events since the reporting date that would require disclosure or adjustment to these financial statements.