

ANNUAL **2011** REPORT

PACIFIC ISLANDS DEVELOPMENT BANK



CHUUK CNMI GUAM KOSRAE MARSHALL ISLANDS PALAU POHNPEI YAP

mission&purpose

To contribute to the acceleration of the process of economic and social development of the member States and nations, individually and collectively, and to promote economic cooperation among them.

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TRANSMITTAL LETTER

March 15, 2012

Board of Governors

Pacific Islands Development Bank

Dear Governors:

I have the honor of transmitting the Annual Report of the Pacific Islands Development Bank for the year ended December 31, 2011, pursuant to Section 12 of Article 13 of the *Articles of Agreement Establishing the Pacific Islands Development Bank*, and Section 7 of Article II of the Bank's *Bylaws*, as amended.

Respectfully,



Aren B. Palik

President & CEO

Chairman, PIDB Board of Directors

MESSAGE

from the President and Chairman of the Board of Directors

2011 was an historic year for the Pacific Islands Development Bank as the Republic of the Marshall Islands joined the bank as a member and shareholder. We congratulate and welcome RMI to our PIDB family. Further, Kosrae State infused \$30,000 in additional equity increasing its shares to 730 valued at \$730,000. We also thank Kosrae for its payment and continued commitment to the bank.

2011 also marked the third year of operation under the Bank's Five Year Strategic Plan covering the period 2009 to 2013. During the year, we aggressively pursued strategic initiatives and actions relating to resource mobilization and capacity enhancement as called for in the Strategic Plan. Overall, 2011 was another great year for the Bank (refer to "2011 Highlight of Events and Accomplishments" on page 5).

While the Bank has enjoyed sustained and consistent growth and improved earnings over the past years, it remains very fragile and susceptible. The bank still faces many challenges, most critical of which is its limited capitalization and lack of loanable funds. While some progress has been made in securing additional capital and funding, the fact that the major donor countries are facing economic, financial, and budgetary challenges reduces our chances of securing external funding, especially grants and soft loans. Nevertheless, the bank's *Capitalization and Funding Task Force* remains aggressive in its pursuit of external funding. The assistance of all board members and management in securing increased capitalization is crucial to PIDB's continued growth and eventual fulfillment of its mandate. Other challenges and impediments to regional development and progress, among others, include air and sea transportation, inadequate and poor infrastructure, remoteness of the member islands to major markets, lack of quality education and trained/skilled labor force, land issues, lack of capital, and US federal regulations and requirements. PIDB will continue to collaborate with its member governments, development partners, and other financial institutions in addressing the above issues and developmental constraints.

Internally, the Bank is continually updating its lending and operational policies and manuals in response to a growing loan operation and a challenging operating environment. The Bank needs to assess its loan platform and accounting software program, and invest in its human resources and staff development and training with the ultimate objective of delivering quality customer service to our clients and customers. Responding to the bank's operational growth over the years, the Board of Directors has approved the lease of a more spacious office in the new Nanbo Building in Hagatna with actual relocation scheduled for May 2012.

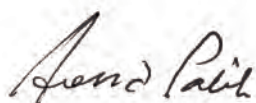
MESSAGE

from the President and Chairman of the Board of Directors

As we close this year and look ahead, it is imperative that we continue to use our Strategic Plan (2009-2013) as our roadmap and guide. Strategic planning has proven to be an effective planning and implementation tool, vital to the overall success of the bank or any organization. The overarching goals and objectives outlined in our Strategic Plan remain clear: (1) increase the bank's financial, human, and technical resources, (2) effectively manage credit risks, (3) manage and increase return on securities investment, (4) diversify and expand products and services, (5) manage our margins by increasing revenue and controlling expenses; and (6) secure new members/shareholders. Annually, through our annual budget process, we will continue to monitor our performance and progress in these areas and make the necessary adjustments.

Finally, the cover of this year's Report displays a canoe sailing. The canoe is one thing that all the PIDB member islands have in common and it has always been an important part of our island culture, heritage, and history. The Bank's corporate logo also displays a canoe with a sail. The canoe, metaphorically, represents PIDB on its journey with a purpose and mission. The Bank has already charted its course and has begun its journey. At this juncture, our canoe (PIDB) needs additional fuel and provision. Let us work together, with commitment and perseverance, and prepare our canoe for its continued journey and seize the opportunities that lie ahead.

We express our sincere gratitude and appreciation to our shareholders for their commitment to PIDB and for their continued support. We also acknowledge and thank all the members of the Board of Governors, Board of Directors, and our staff for their diligence and dedicated services without which our remarkable achievements in 2011 would not have been possible. Thank you.



Aren B. Palik

President & CEO

Chairman, Board of Directors

PART I

General Information

A. 2011 Highlight of Events & Accomplishments

Following are some of key accomplishments and highlight of events during the period under review:

- Republic of the Marshall Islands (RMI) joined PIDB with \$250,000 capital payment
- Kosrae State infused an additional \$30,000 capital
- Received a clean “unqualified” audit opinion
- Approved four (4) scholarships under PIDB Scholarship Program
- Contributed/donated \$5,000 to Association of Pacific Island Legislatures (APIL)
- Total Loans outstanding grew by 15% or \$952,247 to \$7.3 million
- Total Assets grew by 7.6% or \$643,545 to \$9.0 million
- Stockholders’ Equity grew by 5.6% or \$362,791 to \$6.8 million
- Achieved a 2.4% Return on Assets on a \$216,227 net income
- Increased Retained Earnings by \$216,227 or 46% to \$685,469
- Achieved a low loan delinquency ratio of 0.9%
- Recorded zero loan charge-offs
- Was approved 4th IRP application for \$750,000 but pending federal funding

B. PIDB Members & Capitalization

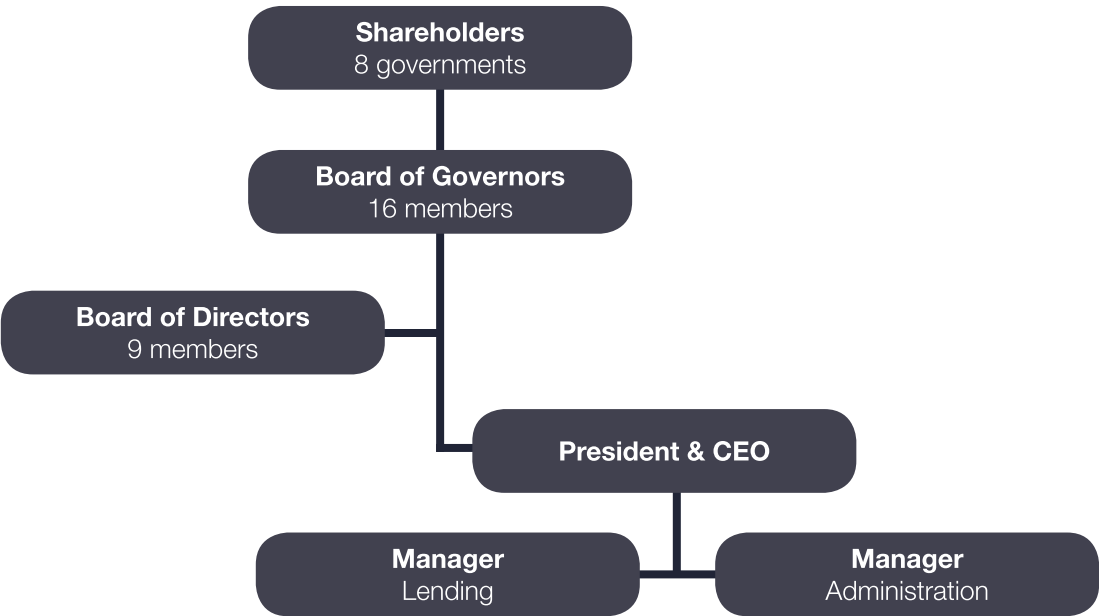
The shareholders of the Bank with number of shares owned and their corresponding values in 2011 compared to 2010 are as follows:

SHAREHOLDERS	2011 No. of Shares	Value (\$)	2010 No. of Shares	Value (\$)
Chuuk	251	251,783	251	251,783
CNMI	1,000	1,000,000	1,000	1,000,000
Guam	1,000	1,000,000	1,000	1,000,000
Kosrae	730	730,000	700	700,000
Marshall Is.	250	250,000	0	0
Palu	1,000	1,000,000	1,000	1,000,000
Pohnpei	1,000	1,000,000	1,000	1,000,000
Yap	1,000	1,000,000	1,000	1,000,000
Total	6,231	\$6,231,783	5,951	\$5,951,783

PART I

General Information

C. Organizational Chart



D. The Board of Governors

The *Articles of Agreement Establishing the Pacific Islands Development Bank*, as amended, stipulates that each member shall appoint two Governors (one representing the Executive and one representing the Legislative branch) to the Board of Governors. The members of the Board for the period under review are as follows:

SHAREHOLDERS	Executive Branch Representative	Legislative Branch Representative
Chuuk	Vacant	Vacant
CNMI	Benigno Fitia, <i>Governor</i>	Diego Benavente, <i>Representative</i>
Guam	Eddie Calvo, <i>Governor</i>	Judith Won Pat, <i>Speaker</i>
Kosrae	Carson Sigrah, <i>Lt. Governor</i>	Lyndon Abraham, <i>Speaker</i>
Marshall Is.	Pending	Pending
Palu	Kerai Mariur, <i>Vice President</i>	Secilil Eldebechel, <i>Delegate</i>
Pohnpei	John Ehsa, <i>Governor</i>	Thomas Pablo, <i>Director of Treasury</i>
Yap	Sebastian Anefal, <i>Governor</i>	Henry Falan, <i>Speaker</i>

PART I

General Information

During its regular meeting on February 28, 2011 in Yap, the Board reorganized and elected Governors John Ehsa and Kerai Mariur as Chairman and Vice Chairman, respectively. The Board also opted to allow the CNMI governors (Benigno Fitial and Diego Benavente) to select one of them to serve as Board Secretary. The Bank extends its gratitude and appreciation to the outgoing officers, Chairman Sebastian Anefal, Vice Chairman John Ehsa, and Secretary Kerai Mariur, for their invaluable services.

E. The Board of Directors

The *Articles of Agreement Establishing the Pacific Islands Development Bank*, as amended, stipulates that the two Governors representing each member shall appoint, subject to the approval of a majority of the Board of Governors, one person to serve as a Director. The Bank President & CEO serves as Chairman of the Board of Directors.

The following individuals served on the Board of Directors during the year under review:

PALAU Secilil Eldebechel Member House of Delegates	CNMI Diego Benavente Representative CNMI Legislature	KOSRAE Ilai Abraham Former Senator Kosrae State Legislature
POHNPEI Thomas Pablo Director Dept. of Treasury/Admin.	GUAM Lourdes Leon Guerrero President & CEO Bank of Guam	YAP John Masiwemai Senator Yap State Legislature
CHUUK Vacant	Aren Palik President & CEO Chairman of the Board	RMI Pending

The Board and management congratulate and welcome Ilai Abraham, John Masiwemai, and Lourdes Leon Guerrero who were appointed to the Board during the period under review. The Board also extend sincere gratitude and appreciation to those they replaced, namely, Gibson Siba, Michael Gaan, and Lourdes Perez, respectively.

PART I | PART II

General Information | 2011 Loans/Lending Report

F. The Management

The Bank's management team for the period under review comprised the following:

NAME	Position/Title	Date of Hire	Years of Service
Aren Palik	President/CEO	October 22, 2002	9.3 years
Rosa Weilbacher	Manager of Admin.	June 1, 1999	11.7 years
Antonio John	Manager of Lending	April 1, 2010	1.8 years

G. Professional Service Providers

The Bank utilizes the services of the following professionals during the period under review:

Investment Consultant - Morgan Stanley Smith Barney

Independent Auditor - Deloitte & Touche LLP

Legal Counsel - Berman O' Conner & Mann (on needs basis)

PART II: 2011 Loans/Lending Report

A. Approved Loans

Loan Type	2011 Number	Amount	2010 Number	Amount
Commercial Loans				
Agriculture	0	0	0	0
Fisheries	0	0	0	0
Tourism	3	525,000	0	0
Manufacturing	0	0	0	0
Services	12	581,905	12	1,098,937
Commercial	18	463,728	2	42,799
Sub Total	33	1,570,634	14	1,141,736
Residential Home Loans	3	260,000	1	56,800
Consumer Loans	42	524,423	42	426,112
Total	78	2,355,057	57	1,624,648

PART II

2011 Loans/Lending Report

B. Outstanding Loans by Loan Type

Loan Type	2011 Number	Amount	2010 Number	Amount
Commercial Loans				
Agriculture	1	11,753	1	14,556
Fisheries	1	64,885	1	70,826
Tourism	10	1,739,306	8	1,218,164
Manufacturing	1	18,650	1	20,640
Services	37	2,923,694	37	2,876,472
Commercial	29	1,148,842	18	1,305,715
Sub Total	79	5,907,130	66	5,506,374
Residential Home Loans	7	586,339	4	336,681
Consumer Loans	88	839,586	56	537,753
Total	174	7,333,055	126	6,380,808

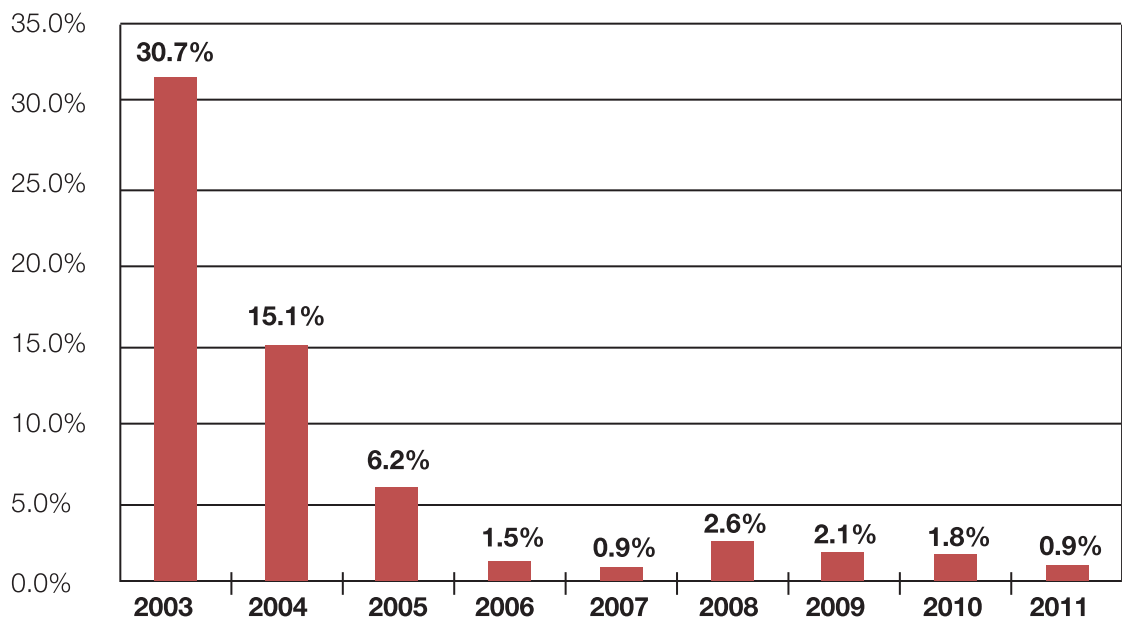
C. Outstanding Loans by Shareholder

Outstanding Loans by Shareholder and Loan Type							
Shareholder	Commercial		Consumer		Housing		Total
	#	\$	#	\$	#	\$	# \$
Guam	9	1,132,492	8	63,448	2	224,044	19 1,437,984
Palau	8	1,155,225	2	32,004	1	93,962	11 1,281,190
Pohnpei	12	1,070,431	17	207,344	1	31,641	30 1,309,417
Yap	8	856,219	39	314,377	1	54,597	48 1,225,194
Kosrae	26	733,393	22	222,413	1	24,095	49 979,901
CNMI	6	650,964	0	0	1	140,000	7 790,964
Chuuk	1	71,937	0	0	0	0	1 71,937
RMI	0	0	0	0	0	0	0 0
FSMD/Export	9	236,469	0	0	0	0	9 236,469
Total	79	5,907,130	88	839,586	7	586,339	174 7,333,055

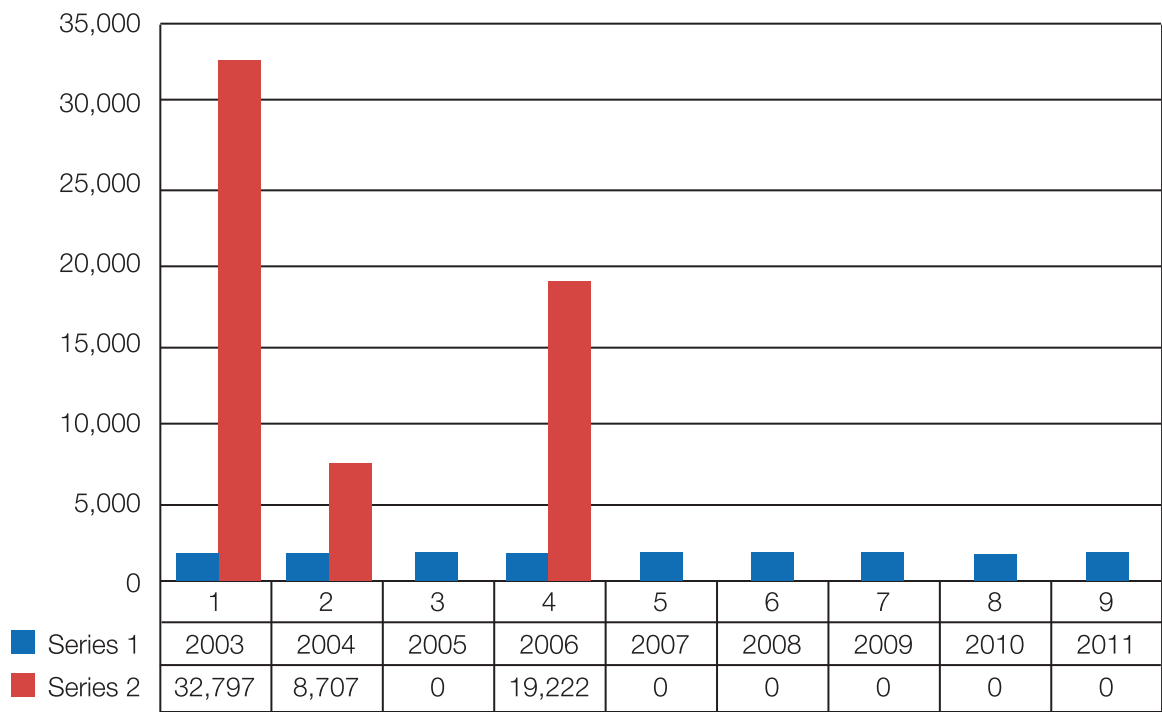
PART II

2011 Loans/Lending Report

D. Loan Delinquency



E. Loan Charge Offs



PART III

2011 Financial Report

A. Performance Against Budget

The Table below shows the Bank's performance against its 2011 budget and targets. Variance in Loans Receivable of \$189,945 is due primarily to a combination of lack of bankable loans and limited capital. Total Assets was short by \$241,677 as we were unable to fully draw the IRP funds and equity/capital injection from current members was slightly lower than the budgeted amount. The bank prudently managed its margins resulting in a net income of \$216,277 against a budget of \$170,000.

Selected Key Items	2011 Budget	2011 Actual	Variance (\$)
Loans Receivable	7,523,000	7,333,055	-189,945
Total Assets	9,314,074	9,072,397	-241,677
Stockholders' Equity	7,004,074	6,802,579	-201,495
Retained Earnings (Deficit)	661,017	685,469	24,452
Gross Revenue	783,000	734,497	-48,503
Total Operating Expenses	512,700	478,270	-34,430
Provision for Loan Losses	100,000	40,000	-60,000
Net Income	170,000	216,227	46,227

B. Performance Against Previous Year (2010)

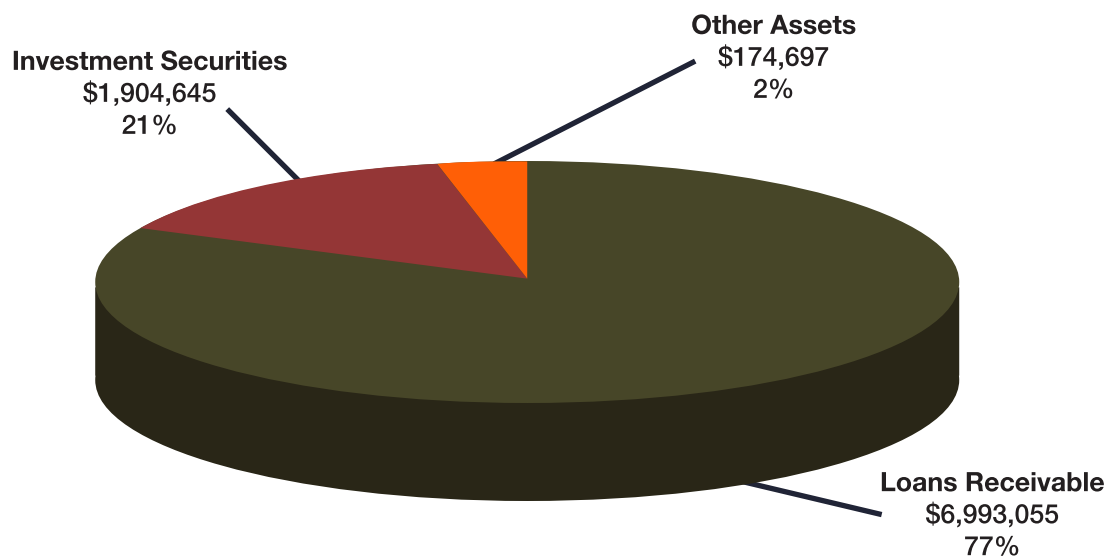
The Table below compares the bank's 2011 financial performance against 2010 in selected key performance indicators. The bank mostly exceeded and outperformed previous year's performance.

Selected Key Items	2011 Actual	2010 Actual	Variance (\$)
Loans Receivable	7,333,055	6,380,808	952,247
Total Assets	9,072,397	8,428,852	643,545
Stockholders' Equity	6,802,579	6,439,788	362,791
Retained Earnings (Deficit)	685,469	469,242	216,227
Gross Revenue	734,497	662,382	72,115
Total Operating Expenses	478,270	439,667	38,603
Provision for Loan Losses	40,000	100,000	-60,000
Net Income	216,227	122,715	93,512

PART III

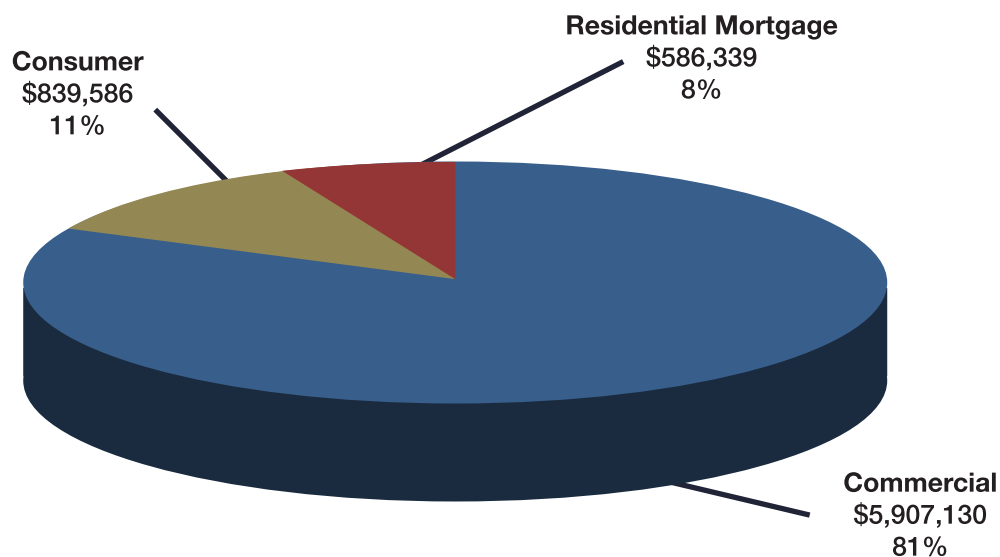
2011 Financial Report

C. Asset Mix



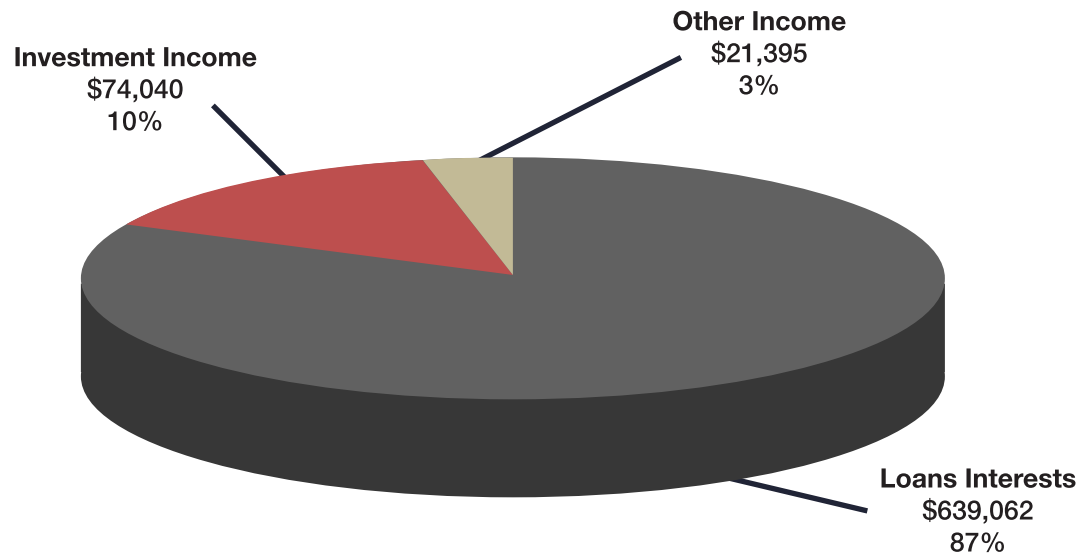
Loans Receivable is net of Loan Loss Reserve of \$340,000

D. Loan Mix

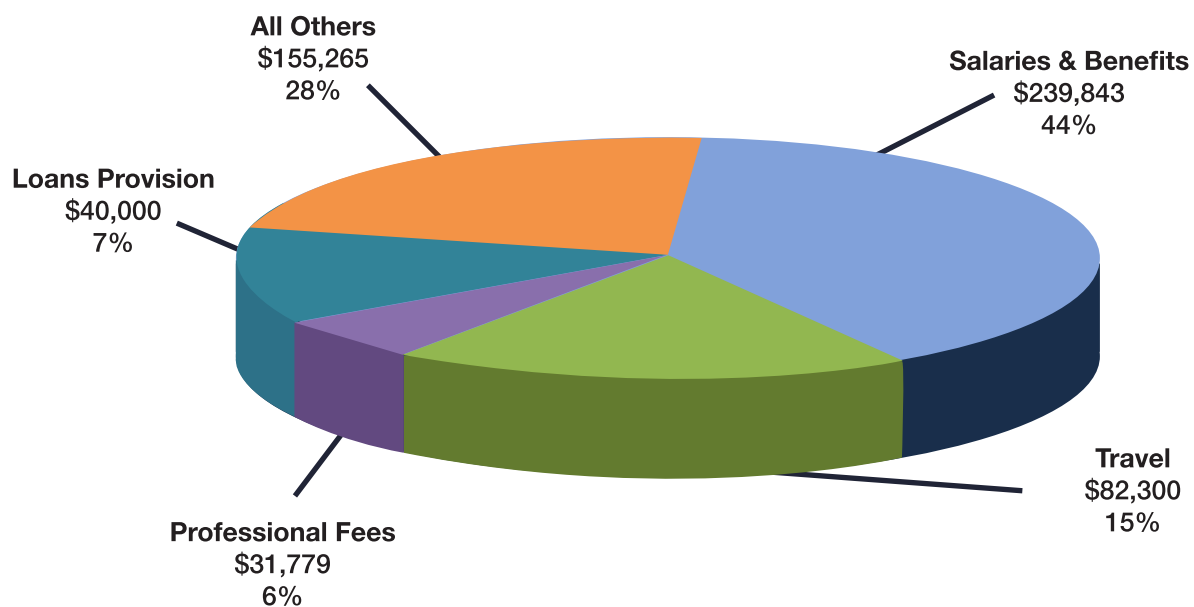


Loan amounts is inclusive of the Loan Loss Reserve

E. Revenue by Source



F. Major Expenses

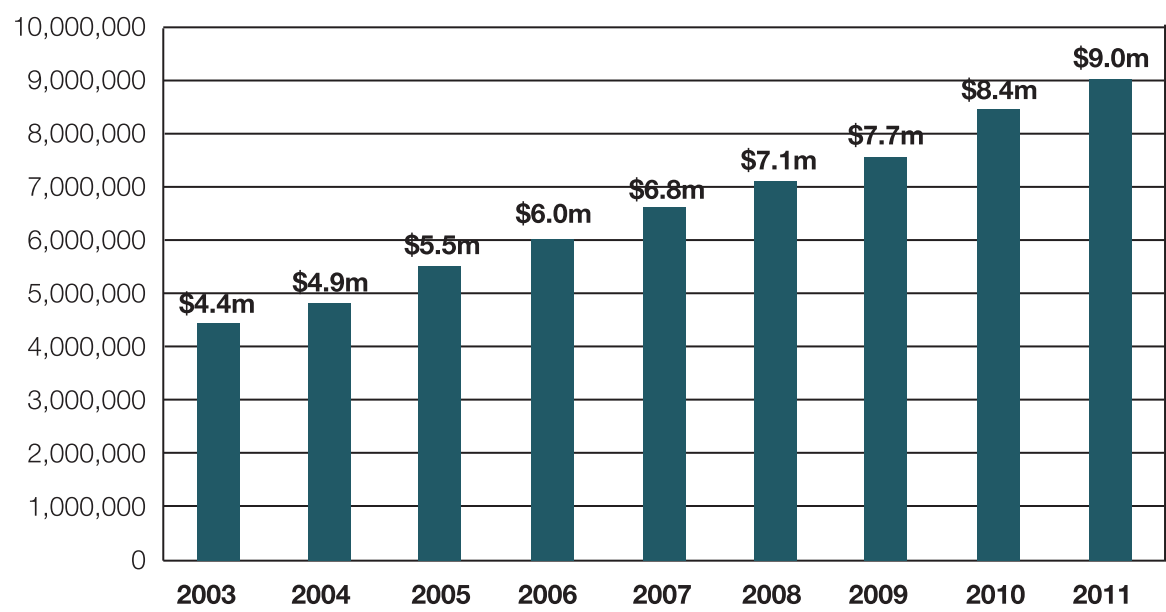


PART IV

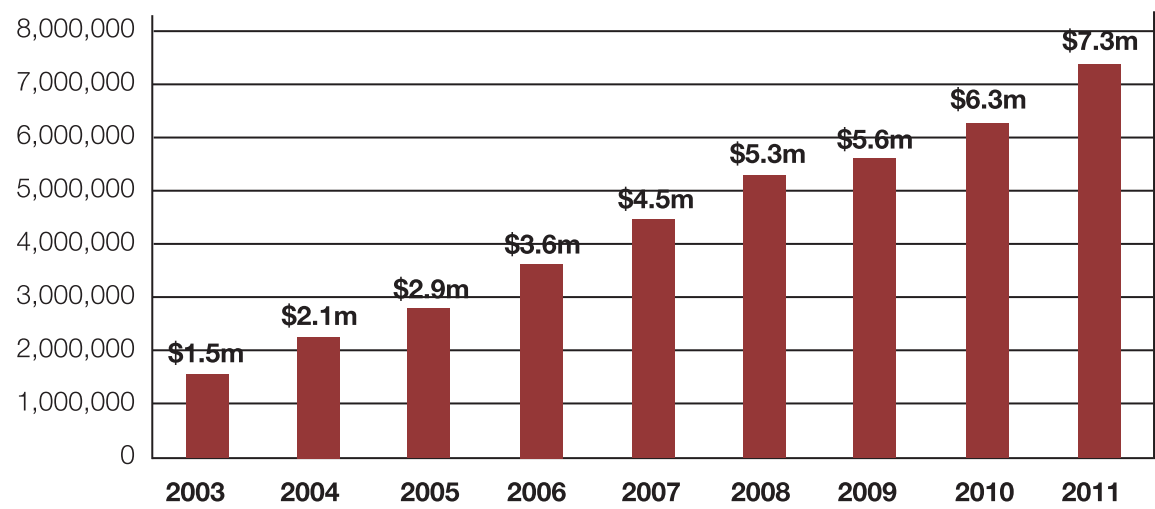
Historical Performance

The following graphs show the historical financial performance of the Bank from 2003 to 2011 on selected key performance indicators.

Total Assets



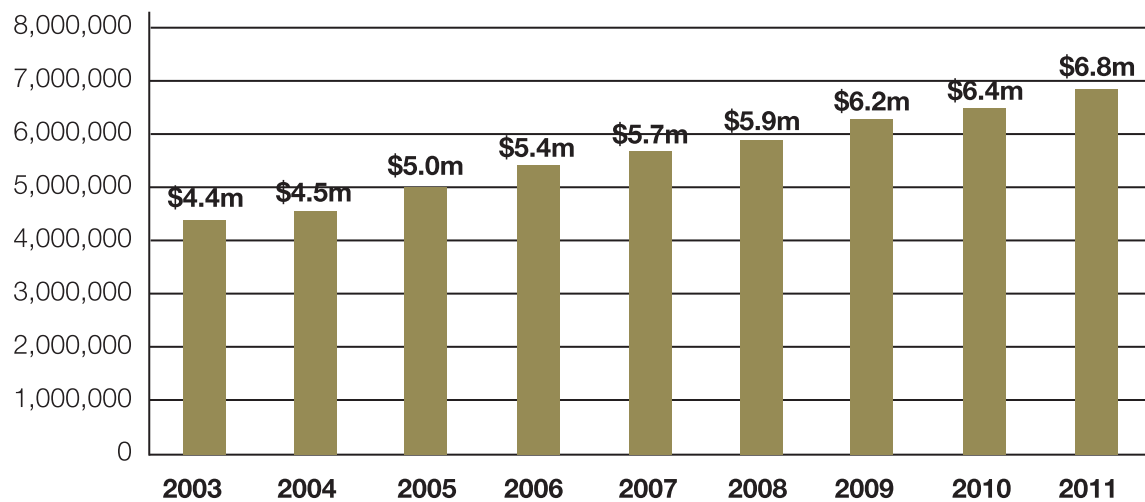
Loans Receivable



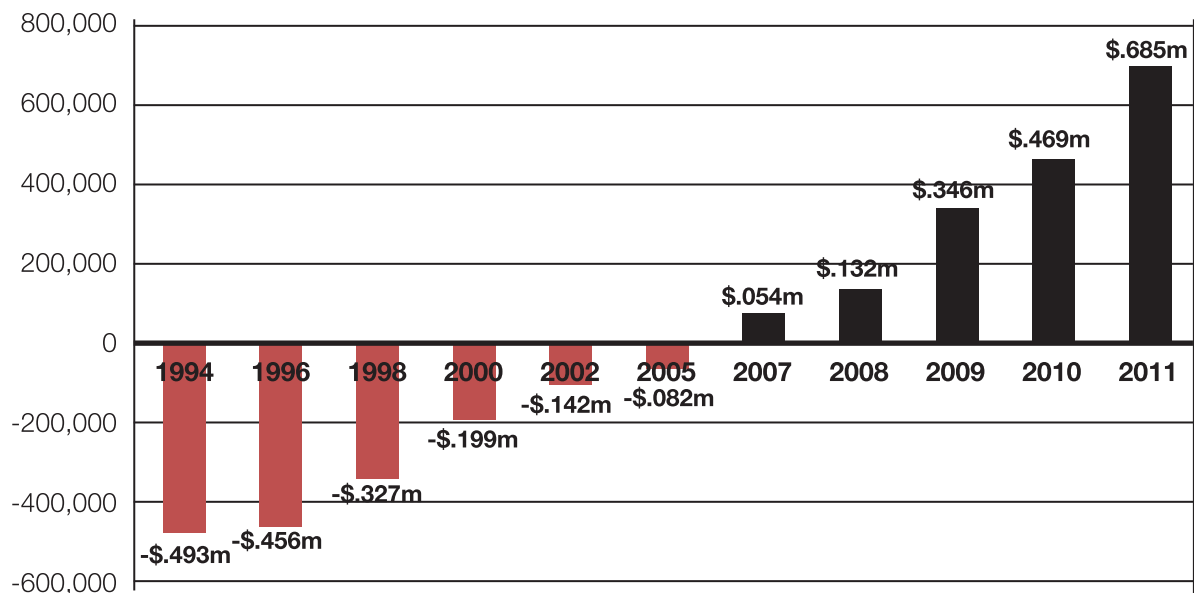
PART IV

Historical Performance

Stockholder's Equity



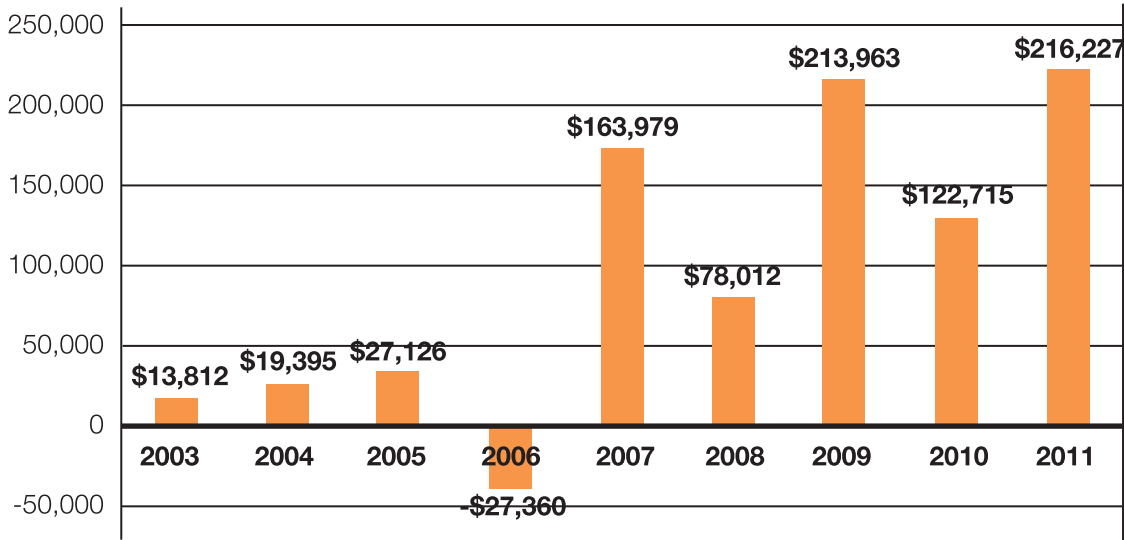
Retained Earnings/Deficit



PART IV | PART V

Historical Performance | Financial Ratios

Net Income/Losses



PART V: Financial Ratios

Selected Ratios	2006	2007	2008	2009	2010	2011
GROWTH						
Total Asset Growth	10%	13%	4%	8%	9%	8%
Loans Growth	22%	23%	18%	6%	12%	15%
Long Term Debt Growth	49%	72%	3%	21%	35%	14%
Net Worth Growth	6%	6%	4%	5%	3%	6%
PROFITABILITY						
Return on Assets	-0.45%	2.4%	1.1%	2.8%	1.5%	2.4%
Return on Equity	-0.51%	2.9%	1.3%	3.4%	1.9%	3.1%
Net Margin	9%	30%	17%	32%	20%	30%
LEVERAGE						
Net Worth	\$5.5M	\$5.7M	\$5.9M	\$6.2M	\$6.4M	\$6.8M
Debt/Worth	13%	21%	21%	24%	31%	33%
Total Liabilities/Total Assets	11%	17%	17%	19%	24%	25%
LIQUIDITY						
Working Capital	\$2.4M	\$2.4M	\$1.9M	\$2.1M	\$2.3M	\$2.0M
Current Ratio	120	n/a	947	1,037	3.444	2,683

PART VI

Board Activities Report

A. Board of Governors

The Board of Governors held its annual regular meeting in Yap in February 2011 with only two members excused due to prior commitments. Key decisions made and actions taken in that meeting include:

- Elected John Ehsa as Board Chairman and Kerai Mariur as Vice Chairman
- Reviewed the Bank's 2010 Annual Report;
- Reviewed the Bank's 2010 Audit Report;
- Reviewed the Bank's 2011 Budget and Goals;
- Helped in securing RMI membership;
- Approved nomination of Mr. Ilai Abraham of Kosrae to Board of Directors;
- Adopted eight (8) Board Resolutions;
- Addressed membership obligations & non-payment of shares; and
- Conducted the President's 2010 performance review.

B. Board of Directors

The Board of Directors, during the period under review, held three (3) regular meetings in January, July, and October 2011. Key decisions made and actions taken by the Board during the period under review include:

- Approved loans over and above the President's lending authority;
- Prepared and transmitted 2010 Annual Report to the Board of Governors;
- Reviewed and approved the 2011 Budget & Goals;
- Quarterly review of the Allowance for Loan Loss reserves;
- Reviewed and continually revised bank policies and procedures;
- Prepared various Resolutions requested by the Board of Governors;
- Selected PIDB scholarships recipients;
- Approved relocation of bank's corporate office to new location in Guam; and
- Worked on membership capital and new membership.

PACIFIC ISLANDS DEVELOPMENT BANK

**FINANCIAL STATEMENTS AND
INDEPENDENT AUDITOR'S REPORT**

YEARS ENDED DECEMBER 31, 2011 AND 2010



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Independent Auditors' Report

The Board of Governors and the Board of Directors
Pacific Islands Development Bank:

We have audited the accompanying statements of condition of Pacific Islands Development Bank (the Bank) as of December 31, 2011 and 2010, and the related statements of earnings, changes in stockholders' equity and cash flows for the years then ended. These financial statements are the responsibility of the Bank's management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with auditing standards generally accepted in the United States of America. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes consideration of internal control over financial reporting as a basis for designing 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 over financial reporting. Accordingly, we express no such opinion. An audit also includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements, assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, such financial statements present fairly, in all material aspects, the financial positions of Pacific Islands Development Bank as of December 31, 2011 and 2010, and the results of its operations and its cash flows for the years then ended in conformity with accounting principles generally accepted in the United States of America.

March 13, 2012

Member of
Deloitte Touche Tohmatsu Limited

PACIFIC ISLANDS DEVELOPMENT BANK

Statements of Condition December 31, 2011 and 2010

<u>ASSETS</u>	<u>2011</u>	<u>2010</u>
Cash	\$ 245,881	\$ 155,212
Money market funds	363,178	584,918
Cash and cash equivalents	609,059	740,130
Time certificates of deposit	150,507	250,000
Investment securities	1,190,960	1,256,439
Loans receivable, net of an allowance of \$340,000 and \$300,000 at December 31, 2011 and 2010, respectively	6,993,055	6,080,808
Interest receivable	119,173	88,292
Security deposit	1,074	1,074
Property and equipment, net	8,569	12,109
	<u>\$ 9,072,397</u>	<u>\$ 8,428,852</u>
 <u>LIABILITIES AND STOCKHOLDERS' EQUITY</u>		
Liabilities:		
Other payables	\$ 778	\$ 678
Long-term debt	2,269,040	1,988,386
Total liabilities	<u>2,269,818</u>	<u>1,989,064</u>
Commitments		
Stockholders' equity:		
Capital stock	6,231,783	5,951,783
Retained earnings	685,469	469,242
Accumulated other comprehensive (loss) income	(114,673)	18,763
Total stockholders' equity	<u>6,802,579</u>	<u>6,439,788</u>
	<u>\$ 9,072,397</u>	<u>\$ 8,428,852</u>

See accompanying notes to financial statements.

PACIFIC ISLANDS DEVELOPMENT BANK

Statements of Earnings Years Ended December 31, 2011 and 2010

	2011	2010
Interest income	\$ 639,062	\$ 560,920
Dividend income	40,156	11,314
Realized gain from investment	33,884	32,987
	<u>713,102</u>	<u>605,221</u>
Provision for loan losses	<u>40,000</u>	<u>100,000</u>
	<u>673,102</u>	<u>505,221</u>
Operating expenses:		
Salaries and related expenses	239,843	219,653
Conference and travel	82,300	100,236
Professional fees	31,779	9,796
Insurance	28,912	27,609
Office rental	20,543	20,377
Trust fees	15,898	11,405
Depreciation	8,638	10,053
Communications	8,513	9,018
Business development and marketing	7,651	4,171
Board meetings	7,037	7,054
Automobile	4,220	4,285
Office supplies	4,112	3,485
Miscellaneous	18,824	12,525
Total operating expenses	<u>478,270</u>	<u>439,667</u>
Operating income	<u>194,832</u>	<u>65,554</u>
Other income:		
Other income	52,312	70,760
Interest expense	<u>(30,917)</u>	<u>(13,599)</u>
Total other income	<u>21,395</u>	<u>57,161</u>
Net earnings	<u>\$ 216,227</u>	<u>\$ 122,715</u>

See accompanying notes to financial statements.

PACIFIC ISLANDS DEVELOPMENT BANK

Statements of Changes in Stockholders' Equity Years Ended December 31, 2011 and 2010

	Shares of Common Stock	Common Stock	Retained Earnings	Accumulated Other Comprehensive (Loss) Income	Total
Balance at December 31, 2009	5,901	5,901,783	346,527	(13,145)	6,235,165
Issuance of common stock	50	50,000	-	-	50,000
Comprehensive income:					
Net earnings	-	-	122,715	-	122,715
Net unrealized holding gains on available-for-sale securities net of reclassification adjustments	-	-	-	31,908	31,908
Total comprehensive income					154,623
Balance at December 31, 2010	5,951	5,951,783	469,242	18,763	6,439,788
Issuance of common stock	280	280,000	-	-	280,000
Comprehensive income:					
Net earnings	-	-	216,227	-	216,227
Net unrealized holding losses on available-for-sale securities net of reclassification adjustments	-	-	-	(133,436)	(133,436)
Total comprehensive income					82,791
Balance at December 31, 2011	<u>6,231</u>	<u>\$ 6,231,783</u>	<u>\$ 685,469</u>	<u>\$ (114,673)</u>	<u>\$ 6,802,579</u>

See accompanying notes to financial statements.

PACIFIC ISLANDS DEVELOPMENT BANK

Statements of Cash Flows Years Ended December 31, 2011 and 2010

	2011	2010
Cash flows from operating activities:		
Net earnings	\$ 216,227	\$ 122,715
Adjustments to reconcile net earnings to net cash provided by operating activities:		
Depreciation	8,638	10,053
Provision for loan loss	40,000	100,000
Realized gain on sale of investment securities	(33,884)	(32,987)
Gain on sale of equipment	(11,000)	-
Increase (decrease) in interest receivables	(30,880)	31,077
Decrease in security deposit	-	2,000
Increase in other payables	100	678
Net cash provided by operating activities	189,201	233,536
Cash flows from investing activities:		
Decrease (increase) in time certificates of deposit	99,493	(250,000)
Loan originations and repayments, net	(941,248)	(695,349)
Investment securities purchases and sales, net	(34,073)	(188,470)
Additions to property and equipment	(5,098)	(68)
Net cash used in investing activities	(880,926)	(1,133,887)
Cash flows from financing activities:		
Proceeds from issuance of capital stock	280,000	50,000
Proceeds from note payable	322,898	556,250
Repayment of note payable	(42,244)	(42,201)
Net cash provided by financing activities	560,654	564,049
Net change in cash and cash equivalents	(131,071)	(336,302)
Cash and cash equivalents at beginning of year	740,130	1,076,432
Cash and cash equivalents at end of year	\$ 609,059	\$ 740,130
Supplemental disclosure of cash flow information:		
Cash paid during the year for:		
Interest	\$ 30,917	\$ 13,599
Supplemental information relating to noncash investing and financing activities:		
Sale of property through PIDB direct loan	11,000	-

See accompanying notes to financial statements.

PACIFIC ISLANDS DEVELOPMENT BANK

Notes to Financial Statements
December 31, 2011 and 2010

(1) Organization and Summary of Significant Accounting Policies

Organization

Pacific Islands Development Bank (the Bank) was created on July 5, 1989 to provide financial and technical expertise to persons and businesses within the Pacific Island region.

The accounting and reporting policies of the Bank are in accordance with accounting principles generally accepted in the United States of America and conform to general practices within the banking industry. The more significant of the principles used in preparing the financial statements are briefly described below.

In August 2001, the Bank was recognized as a non-profit 501c(3) corporation by the Government of Guam. However, the Bank's characterization of its capital stock has yet to be resolved with Guam authorities. Therefore, the Bank has continued its historic financial statement presentation and has yet to adopt not-for-profit financial reporting.

Cash and Cash Equivalents

For the purposes of the statements of condition and cash flows, cash and cash equivalents is defined as cash on hand, in banks and in money market funds. Time certificates of deposit with initial maturities in excess of ninety days are separately classified.

Investment Securities

Debt securities that management has the positive intent and ability to hold to maturity are classified as "held to maturity" and recorded at amortized cost, adjusted for premiums and discounts that are recognized in interest income using the straight-line method over the period to maturity. This method does not differ materially from the interest method. Securities not classified as held to maturity or trading, including equity securities with readily determinable fair values, are classified as "available for sale" and recorded at fair value, with unrealized gains and losses excluded from earnings and reported in other comprehensive income. Declines in the fair value of held-to-maturity and available-for-sale securities below their cost that are deemed to be other than temporary are reflected in earnings as realized losses.

At December 31, 2011 and 2010, the Bank has classified all of its investment securities as available for sale.

Loans

Loans are stated at unpaid principal balance less the allowance for loan losses. Interest income is recognized on an accrual basis. Other credit-related fees are recognized as fee income, a component of noninterest income, when earned.

Non-Performing Loans

Generally, loans are placed on non-accrual status upon becoming contractually past due 90 days as to principal or interest (unless loans and leases are adequately secured by collateral, are in the process of collection, and are reasonably expected to result in repayment), when terms are renegotiated below market levels, or where substantial doubt about full repayment of principal or interest is evident.

PACIFIC ISLANDS DEVELOPMENT BANK

Notes to Financial Statements
December 31, 2011 and 2010

(1) Organization and Summary of Significant Accounting Policies, Continued

Non-Performing Loans, Continued

When a loan is placed on non-accrual status, the accrued and unpaid interest receivable is reversed and the loan is accounted for on the cash or cost recovery method until qualifying for return to accrual status. All payments received on non-accrual loans are applied against the principal balance of the loan. A loan may be returned to accrual status when all delinquent interest and principal become current in accordance with the terms of the loan or lease agreement and when doubt about repayment is resolved. At December 31, 2011 and 2010, the Bank has not placed any loans on non-accrual status.

Impaired Loans

A loan is considered impaired when, based on current information and events, it is probable that the Bank will not be able to collect all amounts due from the borrower in accordance with the contractual terms of the loan, including scheduled interest payments. Impaired loans include all non-accruing loans, all loans modified in a troubled debt restructuring and loans classified as doubtful (see note 4).

When a loan has been identified as being impaired, the amount of impairment is measured based on the present value of expected future cash flows discounted at the loan's effective interest rate, the loan's observable market price, or the estimated fair value of the collateral, less any selling costs, if the loan is collateral-dependent. If the measurement of the impaired loan is less than the recorded investment in the loan (including accrued interest), an impairment is recognized by establishing or adjusting an existing allocation of the Allowance.

Loans Modified in a Troubled Debt Restructuring (TDRs)

Loans are considered to have been modified in a troubled debt restructuring when, due to a borrower's financial difficulties, the Bank makes certain concessions to the borrower that it would not otherwise consider. Modifications may include interest rate reductions, principal or interest forgiveness, forbearance, and other actions intended to minimize economic loss and to avoid foreclosure or repossession of collateral. A modification that results in an insignificant delay in contractual cash flows is not considered to be a concession. During the years ended December 31, 2011 and 2010, the Bank granted loan modifications and temporary payment deferments that are not considered to be TDRs.

Allowance for Loan Losses

The Bank maintains an Allowance adequate to cover management's estimate of probable credit losses as of the balance sheet date. Changes to the level of the Allowance are recognized through charges or credits to provisions for loan losses. Loans that are charged-off reduce the Allowance while recoveries of loans previously charged-off increase the Allowance. During the years ended December 31, 2011 and 2010, the Bank did not charge off any loans or recover any previously charged-off loans.

The Bank does not disaggregate its loan portfolio by segments for the purposes of determination of the Allowance. The level of Allowance is generally based on analyses of individual borrowers and historical loss experience supplemented as necessary by credit judgment to address observed changes in trends and conditions, and other relevant environmental and economic factors that may affect the collectability of loans. On a quarterly basis, the Bank performs an analysis of individual loans based on its internal risk rating methodology.

PACIFIC ISLANDS DEVELOPMENT BANK

Notes to Financial Statements
December 31, 2011 and 2010

(1) Summary of Significant Accounting Policies, Continued

Allowance for Loan Losses, Continued

In July 2010, the Financial Accounting Standards Board (FASB) issued Accounting Standards Update ("ASU") 2010-20, *"Disclosures about the Credit Quality of Financing Receivables and the Allowance for Credit Losses,"* which requires the Bank to provide a greater level of disaggregated information about the credit quality of the Bank's loans and the Allowance for Loan and Lease Losses (the "Allowance"). This ASU will also require the Bank to disclose additional information related to credit quality indicators, nonaccrual and past due information, and information related to impaired loans and loans modified in a troubled debt restructuring. The provisions of this ASU are effective for the Bank as of and for the year ended December 31, 2011. As this ASU amends only the disclosure requirements for loans and the Allowance, the adoption had no impact on the Bank's financial position or results of operations.

Property and Equipment

Property and equipment are stated at cost less accumulated depreciation. Depreciation on all property and equipment is computed under the straight-line method over the estimated useful lives of the assets.

Taxation

The Bank is not subject to taxation within Guam and therefore, no provision for taxes is included within the accompanying financial statements.

Comprehensive Income

Accounting principles generally accepted in the United States of America require that recognized revenue, expenses, gains and losses be included in net income. Although certain changes in assets and liabilities, such as unrealized gains and losses on available-for-sale securities, are reported as a separate component of the equity section of the statements of condition, such items, along with net income, are components of comprehensive income.

Estimates

The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates. Material estimates that are particularly susceptible to significant change in the near term relate to the determination of the allowance for loan losses.

Significant Group Concentration of Credit Risk

All of the Bank's lending activities are with individuals and businesses located within Guam, the Commonwealth of the Northern Mariana Islands, the Federated States of Micronesia, the Republic of the Marshall Islands, and the Republic of Palau. The types of securities that the Bank invests in are included in note 2. The Bank does not have any significant concentrations in any one industry or customer.

PACIFIC ISLANDS DEVELOPMENT BANK

Notes to Financial Statements
December 31, 2011 and 2010

(1) Summary of Significant Accounting Policies, Continued

Risks and Uncertainties

In the normal course of its business, the Bank encounters the three components of economic risks: interest rate risk, credit risk and market risk. The Bank is subject to interest rate risk to the degree that its interest-bearing liabilities mature or re-price at different speeds, or on a different basis, than its interest-earning assets. Incorporated into interest rate risk is prepayment risk. Prepayment risk is the risk associated with the prepayment of assets, and the write-off of premiums associated with those assets, if any, should interest rates fall significantly. Credit risk is the risk of default, primarily in the Bank's loan portfolio that results from the borrower's inability or unwillingness to make contractually required payments. Market risk reflects changes in the value of securities, the value of collateral underlying loans receivable. Credit and market risks can be affected by a concentration of business within the Pacific Island region.

Subsequent Events

Management has evaluated subsequent events through March 13, 2012, which is the date that the financial statements are available to be issued. There were no material subsequent events that would require recognition or disclosure in the financial statements for the year ended December 31, 2011.

(2) Investment Securities

At December 31, 2011 and 2010, all of the Bank's investment securities are maintained by a fund manager. During the years ended December 31, 2011 and 2010, the Bank incurred net realized gains of \$33,884 and \$32,987, respectively, from the sale of securities by the fund manager. Net cumulative unrealized (losses) gains at December 31, 2011 and 2010 amounted to (\$114,673) and \$18,763, respectively.

The amortized cost and fair value of investment securities, with gross unrealized gains and losses, follows:

		2011		
	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value
Debt securities				
U.S. treasury notes	\$ 151,753	\$ 469	\$ (69)	\$ 152,153
U.S. government agency and sponsored Agencies (GSE) debt securities	116,626	181	(67)	116,740
International bonds	6,198	188	-	6,386
Domestic bonds	82,873	306	(139)	83,040
	357,450	1,144	(275)	358,319
Other marketable equity securities	948,183	20,116	(135,658)	832,641
	<u>\$ 1,305,633</u>	<u>\$ 21,260</u>	<u>\$ (135,933)</u>	<u>\$ 1,190,960</u>

PACIFIC ISLANDS DEVELOPMENT BANK

Notes to Financial Statements
December 31, 2011 and 2010

(2) Investment Securities, Continued

	<u>2010</u>			
	<u>Amortized Cost</u>	<u>Gross Unrealized Gains</u>	<u>Gross Unrealized Losses</u>	<u>Fair Value</u>
Debt securities				
U.S. treasury notes	\$ 128,867	\$ 3,142	\$ -	\$ 132,009
U.S. government agency and sponsored Agencies (GSE) debt securities	112,927	4,861	(596)	117,192
International bonds	6,256	-	(67)	6,189
Domestic bonds	<u>78,224</u>	<u>3,284</u>	<u>(45)</u>	<u>81,463</u>
	326,274	11,287	(708)	336,853
Other marketable equity securities	<u>911,402</u>	<u>25,882</u>	<u>(17,698)</u>	<u>919,586</u>
	<u>\$ 1,237,676</u>	<u>\$ 37,169</u>	<u>\$ (18,406)</u>	<u>\$ 1,256,439</u>

The amortized cost and fair value of investment securities by contractual maturity at December 31, 2011, follows:

	<u>Amortized Cost</u>	<u>Fair Value</u>
Due within one year	\$ 74,985	\$ 75,312
Due after one but within five years	233,689	234,142
Due after five but within ten years	<u>48,776</u>	<u>48,865</u>
	357,450	358,519
Other marketable equity securities	<u>948,183</u>	<u>832,641</u>
	<u>\$ 1,305,633</u>	<u>\$ 1,190,960</u>

(3) Loans Receivable

The loan portfolio consists of direct loans. The interest rates on commercial loans, consumer loans and residential loans are predominately at a fixed rate of 10%, 12% and 7%, respectively. Loans have been collateralized by various forms of collateral.

A summary of the balances of loans at December 31, 2011 and 2010 follows:

	<u>2011</u>	<u>2010</u>
Commercial – PIDB direct	\$ 3,012,410	\$ 3,593,923
Commercial – USDA Intermediary Relending Program (IRP)	2,658,251	1,912,347
Consumer	839,586	537,863
Residential mortgages	586,339	336,675
Commercial – FSMDB import/export	<u>236,469</u>	<u>-</u>
Gross loans	7,333,055	6,380,808
Less: allowance for loan losses	<u>(340,000)</u>	<u>(300,000)</u>
Net loans	<u>\$ 6,993,055</u>	<u>\$ 6,080,808</u>

PACIFIC ISLANDS DEVELOPMENT BANK

Notes to Financial Statements
December 31, 2011 and 2010

(3) Loans Receivable, Continued

In the ordinary course of business, the Bank has entered into transactions with its employees, directors and their affiliates. Such transactions were made on substantially the same terms and conditions, including interest rates and collateral, as those prevailing at the same time for comparable transactions with other customers. The aggregate amount of loans outstanding to such related parties at December 31, 2011 and 2010 was \$235,000 and \$179,000, respectively.

(4) Allowance for Loan Losses

A summary of the changes in the allowance for loan losses for the years ended December 31, 2011 and 2010, follows

	<u>2011</u>	<u>2010</u>
Balance at beginning of year	\$ 300,000	\$ 200,000
Loans charged-off, net of recoveries	-	-
Provision for loan losses	<u>40,000</u>	<u>100,000</u>
Balance at end of year	\$ <u>340,000</u>	\$ <u>300,000</u>

Credit Quality Indicators

The Bank uses an internal credit risk rating system that categorizes loans into pass, special mention, substandard or doubtful categories. Credit risk ratings are applied individually to each loan on a quarterly basis.

The following are the definitions of the Bank's credit quality indicators:

Pass: Loans in this category have a high probability of being paid as agreed. The credit carries a level of risk commensurate with the returns provided without placing the Bank in any exposure.

Special Mention: Loans in this category have potential weaknesses that deserve management's close attention. If left uncorrected, these potential weaknesses may result in deterioration of the repayment prospects for default of loan. Special mention loans are not adversely classified and do not expose the Bank to significant risk to warrant such adverse classification.

Substandard: Loans in this category are inadequately protected by the current worth and paying capacity of the obligors or of the collateral pledged. Loans so classified must have a well-defined weakness or weaknesses that jeopardize the liquidation of the debt. They are characterized by the distinct possibility that the Bank may sustain some losses if the deficiencies are not corrected.

Doubtful: Loans classified in this category have all the weaknesses inherent in those classified Substandard with the added characteristic that the weaknesses make collection or liquidation in full, on the basis of currently known facts, conditions and values, highly questionable and improbable. Loans classified as Doubtful are considered to be impaired.

PACIFIC ISLANDS DEVELOPMENT BANK

Notes to Financial Statements
December 31, 2011 and 2010

(4) Allowance for Loan Losses, Continued

The Bank's credit quality indicators are periodically updated on a case-by-case basis. The following presents by class and by credit quality indicator, the recorded investment in the Bank's loans as of December 31, 2011:

	<u>Pass</u>	<u>Special mention</u>	<u>Sub- standard</u>	<u>Doubtful</u>	<u>Total</u>
PIDB direct	\$ 2,869,371	\$ 89,415	\$ -	\$ 53,624	\$ 3,012,410
IRP	1,962,352	282,165	124,643	289,091	2,658,251
Consumer	835,215	4,371	-	-	839,586
Residential	586,339	-	-	-	586,339
Import/export	<u>236,469</u>	<u>-</u>	<u>-</u>	<u>-</u>	<u>236,469</u>
Total	\$ <u>6,489,746</u>	\$ <u>375,951</u>	\$ <u>124,643</u>	\$ <u>342,715</u>	\$ <u>7,333,055</u>

The following presents by class, an aging analysis of the Bank's loan portfolio as of December 31, 2011:

	<u>Current</u>	<u>30 – 59 Days Past Due</u>	<u>60 – 89 Days Past Due</u>	<u>Past Due 90 Days or More</u>	<u>Total</u>
PIDB direct	\$ 2,958,786	\$ -	\$ -	\$ 53,624	\$ 3,012,410
IRP	2,646,498	-	11,753	-	2,658,251
Consumer	838,358	-	1,228	-	839,586
Residential	586,339	-	-	-	586,339
Import/export	<u>236,469</u>	<u>-</u>	<u>-</u>	<u>-</u>	<u>236,469</u>
Total	\$ <u>7,266,450</u>	\$ <u>-</u>	\$ <u>12,981</u>	\$ <u>53,624</u>	\$ <u>7,333,055</u>

At December 31, 2011, impaired loans of \$341,715 represent two loans classified as doubtful, both with a recorded allowance totaling \$222,765.

(4) Long-Term Debt

On October 7, 2003, the Bank was awarded an Intermediary Relending Program (IRP) loan by the U.S. Department of Agriculture in the amount of \$500,000. The loan requires interest only payments for the first three years; thereafter, principal and interest is payable in equal annual installments beginning on October 7, 2007. The loan matures on October 7, 2033. The loan bears a fixed interest rate of one percent per annum. At December 31, 2011 and 2010, outstanding balances were \$415,592 and \$432,591, respectively.

On June 27, 2006, the Bank was awarded supplemental funds of \$750,000 under the same program. The loan requires interest only payments for the first three years; thereafter, principal and interest is payable in equal annual installments beginning on June 27, 2010. The loan matures on June 27, 2036. The loan bears a fixed interest rate of one percent per annum. At December 31, 2011 and 2010, outstanding balances were \$700,499 and \$725,744, respectively.

PACIFIC ISLANDS DEVELOPMENT BANK

Notes to Financial Statements
December 31, 2011 and 2010

(4) Long-Term Debt, Continued

On September 8, 2008, the Bank was awarded additional supplemental funds of \$750,000 under the same program. The loan requires interest only payments for the first three years; thereafter, principal and interest is payable in equal annual installments beginning on September 8, 2012. The loan matures on September 8, 2038. The loan bears a fixed interest rate of one percent per annum. At December 31, 2011 and 2010, outstanding balances were \$652,949 and \$330,051, respectively, with \$97,051 and \$419,949, respectively, available for future drawdowns.

On September 16, 2010, the Bank entered into a \$500,000 loan agreement with the FSM Development Bank mainly for relending in the forms of business development loans to FSM citizens on Guam. The loan requires interest only payments for the first three years; thereafter, principal and interest is payable in equal quarterly installments beginning on September 15, 2013. The loan matures on September 15, 2023. The loan bears a fixed interest rate of four percent per annum. At December 31, 2011 and 2010 outstanding balance was \$500,000.

The loans are collateralized by all repayments, interest, fees, investments and other revenues collected or generated from the IRP loans.

The Bank's future maturities of long-term debt are as follows:

Year ending December 31,

2012	\$ 62,525
2013	76,713
2014	105,801
2015	108,152
2016	110,580
Thereafter	<u>1,805,269</u>
	<u>\$ 2,269,040</u>

The Bank is required to match 50% of the IRP loan. Therefore, as of December 31, 2011, cash restricted for this purpose approximated \$1,412,000. The Bank has designated cash in money market funds and investment securities as restricted for this purpose.

(5) Property and Equipment

A summary of property and equipment as of December 31, 2011 and 2010, is as follows:

<u>Description</u>	<u>Estimated Useful Lives</u>	<u>2011</u>	<u>2010</u>
Office furniture and equipment	10 years	\$ 10,644	\$ 20,781
Computer equipment	5 years	44,255	41,554
Vehicles	5 years	<u>32,089</u>	<u>52,588</u>
		86,988	114,923
Less accumulated depreciation		<u>(78,419)</u>	<u>(102,814)</u>
		<u>\$ 8,569</u>	<u>\$ 12,109</u>

PACIFIC ISLANDS DEVELOPMENT BANK

Notes to Financial Statements
December 31, 2011 and 2010

(6) Stockholders' Equity

Under the "Articles of Agreement Establishing The Pacific Islands Development Bank" (the Articles), each member is to contribute \$1,000,000 for the purchase of shares in the Bank. If all eligible governments participate, equity contributions of \$10,000,000 would result. As of December 31, 2011 and 2010, the Bank has received \$6,231,783 and \$5,951,783 of equity contributions, respectively. Authorized capital stock is 18,000 shares of \$1,000 par value. As of December 31, 2011 and 2010, respectively, 6,231 and 5,951 shares have been issued and are outstanding.

This under-capitalization has delayed the Bank in expanding its operating activities. In order for the Bank to engage in operations of the size contemplated, significant capital infusions are required from existing and prospective members.

(7) Commitments

The Bank does not have any undisbursed loan commitments at December 31, 2011.

(8) Leases

The Bank operates from rented premises under an operating lease agreement that expired July 31, 2011 and is currently on a month-to-month extension, at a monthly rent of \$1,705. The Bank will be moving into a new location during 2012.

(9) Related Party Transactions

As explained in note 3, the Bank has made certain loans to related parties.

(10) Employee Benefit Plan

The Bank has a 401(k) Plan whereby substantially all employees participate in the Plan after meeting certain eligibility requirements, namely, completion of one year of continuous employment. Contributions to the Plan are 10% of gross salaries and are 100% vested after three years of service. During the years ended December 31, 2011 and 2010, the Bank contributed \$12,991 and \$12,582, respectively, to the Plan.

(11) Fair Value Measurements

The Bank uses fair value measurements to record fair value adjustments to investments and to determine fair value disclosures. In accordance with FASB Accounting Standards Codification (ASC) Topic 820 "*Fair Value Measurements and Disclosures*," the fair value of a financial instrument is the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date. Fair value is best determined based upon quoted market prices. FASB ASC 820 establishes a fair value hierarchy that prioritizes the use of inputs used in valuation methodologies into the following three levels:

Level 1: Quoted prices in active markets for identical assets or liabilities. Level 1 assets and liabilities include debt and equity securities and derivative contracts that are traded in an active exchange market, as well as certain U.S. Treasury securities that are highly liquid and are actively traded in over-the-counter markets.

PACIFIC ISLANDS DEVELOPMENT BANK

Notes to Financial Statements
December 31, 2011 and 2010

(11) Fair Value Measurements, Continued

Level 2: Observable inputs other than Level 1 prices, such as quoted prices for similar assets or liabilities; quoted prices in markets that are not active; or other inputs that are observable or can be corroborated by observable market data for substantially the full term of the assets or liabilities.

Level 3: Unobservable inputs that are supported by little or no market activity and that are significant to the fair value of the assets or liabilities. Level 3 assets and liabilities include financial instruments whose value is determined using pricing models, discounted cash flow methodologies, or similar techniques, as well as instruments for which the determination of fair value requires significant management judgment and estimation.

The Bank's investments in available-for-sale securities are stated at fair value. Quoted market prices are used to value investments. The Bank has determined that all of its investments are Level 1 assets. Additionally, the Bank does not have other financial or nonfinancial assets and liabilities that are measured at fair value on a recurring or nonrecurring basis and therefore do not have disclosure requirements under FASB ASC 820.



PACIFIC ISLANDS DEVELOPMENT BANK

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