ELECTRICITY SUPPLY CORPORATION
OF MALAWI LIMITED

Financial Statements for the year ended
30 June 2011

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ELECTRICITY SUPPLY CORPORATION OF MALAWI LIMITED
REPORT OF THE DIRECTORS
For the year ended 30 June 2011

The Directors have pleasure in presenting their report together with the statement of financial position of Electricity Supply Corporation of Malawi Limited together with the statement of comprehensive income, statement of changes in equity and statement of cash flows for the year ended 30 June 2011.

ACTIVITIES

The company is involved in the generation, transmission and distribution of electricity.

	2011 K'000	2010 K'000
FINANCIAL PERFORMANCE		
Profit for the year	5,806,197	86,457

SHARE CAPITAL

The issued share capital of the company is K110 million divided into 55 million Ordinary shares of K2 each.

The shareholders and their respective holdings are:	2011	2010
Malawi Government	99%	99%
MDC Limited in liquidation	1%	1%
	100%	100%

MDC Limited in liquidation holds 1% in trust for the Malawi Government.

AUDITOR

Deloitte, who were re-appointed during the year, have signified their willingness to continue in office.

REGISTERED OFFICE

The registered office and principal place of business of the company is situated at the company's premises in ESCOM House, 9 Haile Selassie Road, Blantyre, Malawi.

DIRECTORS

The following directors served in office during the year covered by the financial statements:

Mr K M Sadala - Chairman	
Dr E Kayambazinthu	
Mr G M Mtaula	
Mr D A Mphepo	
Mr L C Nazitwere	
Mr P M Kholongo	
Mr S Mikaya	
Mrs J Guga	
Secretary for Natural Resources, Energy and Environment	Ex officio
Secretary to the Treasury	Ex officio
Comptroller of Statutory Corporations	Ex officio

FOR AND ON BEHALF OF THE BOARD

Director: ____

Director: ____

STATEMENT OF DIRECTORS' RESPONSIBILITIES

For the year ended 30 June 2011

The Companies Act, 1984, requires the directors to prepare financial statements for each financial period, which give a true and fair view of the state of affairs of the company as at the end of the period and of the operating results for that period.

The Act also requires the directors to ensure that the company keeps proper accounting records which disclose with reasonable accuracy at any time the financial position of the company and enable them to ensure that the financial statements comply with the Companies Act, 1984.

In preparing the financial statements the directors accept responsibility for the following:

- Maintenance of proper accounting records;
- Selection of suitable accounting policies and applying them consistently;
- Making judgements and estimates that are reasonable and prudent;
- Compliance with applicable accounting standards, when preparing financial statements; and
- Preparation of financial statements on a going concern basis unless it is inappropriate to presume that the company will continue in business.

The directors also accept responsibility for taking such steps as are reasonably open to them to safeguard the assets of the company and to maintain adequate systems of internal controls to prevent and detect fraud and other irregularities.

The directors are of the opinion that the financial statements give a true and fair view of the state of the financial affairs of the company and of its operating results.

Director: ____

Director: ____

INDEPENDENT AUDITOR'S REPORT
TO THE MEMBERS OF
ELECTRICITY SUPPLY CORPORATION OF MALAWI LIMITED

We have audited the financial statements of Electricity Supply Corporation of Malawi Limited as set out on pages 5 to 47, which comprise the statement of financial position as at 30 June 2011, the statement of comprehensive income, statement of changes in equity and the statement of cash flows for the year then ended, and a summary of significant accounting policies and other explanatory notes.

Management's Responsibility for the Financial Statements
Management is responsible for preparation and fair presentation of these financial statements in accordance with International Financial Reporting Standards, and for such internal control as management determines is necessary to enable the preparation of financial statements that are free from material misstatement, whether due to fraud or error.

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

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation and fair presentation of the financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. An audit also includes evaluating appropriateness of accounting policies used and the reasonableness of accounting estimates made by management, as well as evaluating the overall presentation of the financial statements.

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

Opinion
In our opinion, the financial statements give a true and fair view of the financial position of Electricity Supply Corporation of Malawi Limited as of 30 June 2011, and of its financial performance and its cash flows for the year then ended in accordance with International Financial Reporting Standards and in the manner required by the Companies Act, 1984 and the Public Finance Management Act, 2003.

Emphasis of matter – Going Concern
Without qualifying our opinion, we draw attention to note 28 to the financial statements. The company has a profit for the year of K5,806m (2010: K86m) and the accumulated losses at the end of the year were K3,990m (2010: K9,827m). In addition, current liabilities exceed current assets by K5,874m (2010: K7,562m). These are indicators which cast doubt over the company's ability to continue as a going concern.

Public Accountants
Blantyre, Malawi

24 October 2011

ELECTRICITY SUPPLY CORPORATION OF MALAWI LIMITED
STATEMENT OF FINANCIAL POSITION
30 June 2011

	Notes	2011 K'000	2010 K'000
ASSETS			
NON-CURRENT ASSETS			
Property, plant and equipment	5	27,265,835	27,499,249
Capital work in progress	6	3,789,576	1,969,193
Deferred tax	7	1,310,717	-
Total non-current assets		32,366,128	29,468,442
CURRENT ASSETS			
Inventories	8	984,520	825,484
Receivables	9	2,991,630	2,189,145
Bank current accounts and cash		397,075	315,121
Bank deposit accounts		1,919,057	695,384
Taxation recoverable		30,702	16,645
Total current assets		6,322,984	4,041,779
TOTAL ASSETS		38,689,112	33,510,221
EQUITY AND LIABILITIES			
SHAREHOLDERS' EQUITY			
Share capital		110,000	110,000
Preference shares		530,000	530,000
Share premium		13,750,820	13,750,820
Pre-incorporation reserves		391,142	391,142
Revaluation reserve		2,036,077	2,067,593
Accumulated losses		(3,989,769)	(9,827,482)
Total shareholders' equity		12,828,270	7,022,073
NON-CURRENT LIABILITIES			
Deferred income	10	5,670,685	4,602,508
Severance allowance provision	11	-	2,351,345
Retirement benefit fund	12	781,595	714,775
Borrowings	13	3,574,547	3,909,510
HIPC funds	14	3,065,516	2,999,499
Bank borrowings	15	203,282	300,312
ESCOM Limited Pension Fund loan	16	170,000	-
Finance leases	17	197,929	5,839
Total non-current liabilities		13,663,554	14,883,788
CURRENT LIABILITIES			
Bank overdraft	18	56,723	935,330
Payables	19	1,908,240	2,955,765
Pension arrears	11	919,318	-
Borrowings	13	8,897,200	6,739,588
HIPC funds	14	74,085	66,017
Bank borrowings	15	175,662	231,759
ESCOM Limited Pension Fund loan	16	56,667	499,275
Finance leases	17	109,393	176,626
Total current liabilities		12,197,288	11,604,360
TOTAL EQUITY AND LIABILITIES		38,689,112	33,510,221

The financial statements were authorised for issue by the Board of Directors on 24 October 2011 and were signed on its behalf by:

……………………………..……… (Director) ……………………………………..… (Director)

ELECTRICITY SUPPLY CORPORATION OF MALAWI LIMITED
STATEMENT OF COMPREHENSIVE INCOME
For the year ended 30 June 2011

	Notes	2011 K'000	2010 K'000
INCOME FROM OPERATIONS			
Sales of energy		13,662,933	10,350,693
Capital contributions and grants released	10	166,029	140,247
Total income from operations		13,828,962	10,490,940
OPERATING EXPENDITURE			
Generation		616,566	859,522
Transmission		715,222	617,055
Distribution		2,306,693	1,046,474
Head Office		5,431,244	5,345,810
Depreciation		1,346,312	1,157,785
Interest on loans, finance leases and bank borrowings		527,827	642,411
Interest on bank overdraft		32,667	223,056
Total operating expenditure		10,976,531	9,892,113
PROFIT BEFORE OTHER INCOME		2,852,431	598,827
OTHER INCOME/(EXPENDITURE)			
Reversal of severance allowance provision	11	1,266,600	-
Exchange (losses)/gains	20	(347,836)	205,546
Decrease/(increase) in doubtful debt provisions		185,611	(1,114,494)
Loss on disposal of property, plant and equipment		(13,250)	(7,931)
Training expenses		(57,534)	(28,711)
Interest receivable		92,012	33,533
Other income		517,446	399,687
Net other income/(expenditure)		1,643,049	(512,370)
PROFIT BEFORE TAXATION	21	4,495,480	86,457
Taxation	22	1,310,717	-
PROFIT FOR THE YEAR		5,806,197	86,457
OTHER COMPREHENSIVE INCOME		-	1,139,036
TOTAL COMPREHENSIVE INCOME FOR THE YEAR		5,806,197	1,225,493

ELECTRICITY SUPPLY CORPORATION OF MALAWI LIMITED

STATEMENT OF CHANGES IN EQUITY

30 June 2011

	Share capital K'000	Share premium K'000	Preference shares K'000	Advance contribution for share capital K'000	Pre-incorporation reserves K'000	Nordic Development Fund loan K'000	Asset reserve K'000	Revaluation reserve K'000	Accumulated losses K'000	Total K'000
Year ended 30 June 2010										
At beginning of the year	100,000	610,000	-	12,763,159	391,142	917,661	39,555	957,931	(10,007,868)	5,771,580
Reversal of prior year dividend	-	-	-	-	-	-	-	-	25,000	25,000
Total comprehensive income for the year	-	-	-	-	-	-	-	1,139,036	86,457	1,225,493
Transfer to accumulated losses	-	-		-	-	-	(39,555)	-	39,555	-
Excess depreciation	-	-	-	-	-	-	-	(29,374)	29,374	-
Share capital issued during the year	10,000	13,140,820	530,000	(12,763,159)	-	(917,661)	-	-	-	-
At end of the year	110,000	13,750,820	530,000	-	391,142	-	-	2,067,593	(9,827,482)	7,022,073
Year ended 30 June 2011										
At beginning of the year	110,000	13,750,820	530,000	-	391,142	-	-	2,067,593	(9,827,482)	7,022,073
Total comprehensive income for the year	-	-	-	-	-	-	-	-	5,806,197	5,806,197
Excess depreciation	-	-	-	-	-	-	-	(31,516)	31,516	-
At end of the year	110,000	13,750,820	530,000	-	391,142	-	-	2,036,077	(3,989,769)	12,828,270

	2011 K'000	2010 K'000
Analysis of share capital		
Authorised, issued		
55,000,000 (2010:50,000,000) Ordinary shares of K2 each	110,000	110,000
Issued and fully paid		
55,000,000 (2010:50,000,000) Ordinary shares of K2 each	110,000	110,000
Irredeemable non-cumulative 2.5% preference shares of K1 each	530,000	530,000

Irredeemable preference shares

The 530 million preference shares of K1 each were issued at a premium of K387.66 million out of the Nordic Development Fund loans as per the loan agreement requirements.

Pre-incorporation reserves

Pre-incorporation reserves are not available for distribution as they represent part of the capital introduced into the company on incorporation.

Revaluation reserve

The revaluation reserve, which represents the excess of carrying value of land and buildings over cost, is not distributable until or unless the related land and buildings are realised.

ELECTRICITY SUPPLY CORPORATION OF MALAWI LIMITED

STATEMENT OF CASH FLOWS

For the year ended 30 June 2011

	2011 K'000	2010 K'000
Cash generated from operations (Note 23)	3,246,487	2,769,235
Interest paid	(674,687)	(562,775)
Net cash generated from operations	2,571,800	2,206,460
Cash flows from investing activities		
Expenditure on property, plant and equipment including capital work in progress	(1,221,051)	(1,907,186)
Proceeds from sale of property, plant and equipment	4,991	15,892
Interest received	92,012	33,533
Net cash used in investing activities	(1,124,048)	(1,857,761)
Cash flows from financing activities		
Repayment of finance leases	(155,252)	(129,886)
Proceeds from bank borrowings	-	100,000
Repayments of bank borrowings	(153,127)	(361,256)
Repayment of ESCOM Limited Pension Fund loan	(219,105)	-
Grants and capital contributions received	1,263,967	1,016,099
Net cash flow from financing activities	736,483	624,957
Increase in cash and cash equivalents	2,184,234	973,656
Cash and cash equivalents at beginning of the year	75,175	(898,481)
Cash and cash equivalents at end of the year	2,259,409	75,175
Analysis of cash and cash equivalents		
Bank current accounts and cash	397,075	315,121
Bank deposit accounts	1,919,057	695,384
Bank overdraft	(56,723)	(935,330)
	2,259,409	75,175

1. General Information

The principal activities of the company include the generation, transmission and distribution of electricity. The company's principal place of business and the address of its registered office is ESCOM House, 9 Haile Selassie Road, P.O. Box 2047, Blantyre, Malawi.

2. Adoption of new and Revised International Financial Reporting Standards

The Company has adopted all of the new and revised Standards and Interpretations issued by the International Accounting Standards Board (the IASB) and the International Financial Reporting Interpretations Committee (IFRIC) of the IASB that are relevant to its operations and effective for accounting periods beginning on 1 July 2010.

The adoption of these new and revised standards and interpretations did not have a significant impact on the financial statements of the commission.

2.2 Standards and Interpretations in issue, not yet effective

At the date of authorisation of these financial statements, the following Standards and Interpretations were in issue but not effective:

2.2.1 IFRS 7 *Financial Instruments: Disclosures* - Amendments resulting from May 2010 Annual Improvements to IFRSs (effective for annual periods beginning on or after 1 January 2011).

2.2.2 IFRS 7 *Financial Instruments: Disclosures* - Amendments enhancing disclosures about transfers of financial assets (effective for annual periods beginning on or after 1 July 2011).

2.2.3 IFRS 9 *Financial Instruments* - *Classification and Measurement* (effective for annual periods beginning on or after 1 January 2013).

2.2.4 IFRS 10 *Consolidated Financial Statements* (effective for annual periods beginning on or after 1 January 2013).

2.2.5 IFRS 11 *Joint Arrangements* (effective for annual periods beginning on or after 1 January 2013).

2.2.6 IFRS 12 *Disclosure of Interests in Other Entities* (effective for annual periods beginning on or after 1 January 2013).

2.2.7 IFRS 13 *Fair Value Measurement* (effective for annual periods beginning on or after 1 January 2013).

2.2.8 IAS 1 *Presentation of Financial Statements* - Amendments resulting from May 2010 Annual Improvements to IFRSs (effective for annual periods beginning on or after 1 January 2011).

2.2.9 IAS 12 Income Taxes – Limited scope amendment (recovery of underlying assets). Effective for annual periods beginning on or after 1 January 2012.

2.2.10 IAS 24 *Related Party Disclosures* - Revised definition of related parties (effective for annual periods beginning on or after 1 January 2011).

2.2.11 IAS 32 *Financial Instruments: Presentation* - Amendments relating to classification of rights issues (effective for annual periods beginning on or after 1 February 2010).

2.2.12 IFRIC 13 *Customer Loyalty Programmes* - Amendments resulting from May 2010 Annual Improvements to IFRSs (effective for annual periods beginning on or after 1 January 2011).

2.2.13 IFRIC 14 *IAS19* - *The Limit on a Defined Benefit Asset, Minimum Funding Requirements and their Interaction* - November 2009 Amendments with respect to voluntary prepaid contributions (effective for annual periods beginning on or after 1 January 2011).

2.2.14 IFRIC 19 *Extinguishing Financial Liabilities with Equity Instruments* (effective for annual periods beginning on or after 1 July 2010).

The directors anticipate that, other than IFRS 9 and IFRS 13, these Standards and Interpretations in future periods will have no significant impact on the financial statements of the entity. IFRS 9 will impact the measurement of financial instruments. IFRS 13 will impact all fair value measurements in the financial statements.

3. Significant accounting policies

Statement of compliance
The financial statements have been prepared in accordance with International Financial Reporting Standards.

Basis of preparation
The financial statements are prepared in terms of the historical cost convection, with the exception of land and buildings and certain financial instruments which are included at valuation. No other procedures are adopted to reflect the impact on the financial statements of specific price changes or changes in the general level of prices.

3.1 *Property, plant and equipment*

Land and buildings are shown at valuation with subsequent additions at cost, less related depreciation and impairment losses. Revaluations of land and buildings are carried out by independent valuers, with sufficient regularity such that the carrying amount does not differ materially from that which would be determined using fair values at the statement of financial position date. The basis of valuation used is Depreciated Replacement Cost. Surpluses on revaluations are transferred to the non-distributable reserve; on realisation (either through use or disposal) of the asset, the appropriate portion of the reserve is transferred to retained profit. Deficits on revaluations are charged to the profit or loss, except to the extent that they relate to revaluation surpluses previously transferred to the revaluation reserve through other comprehensive income. An amount equivalent to the additional depreciation arising from revaluations is transferred annually, net of deferred tax, from the revaluation reserve to retained profit.

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

All fixed assets other than land and buildings are shown at cost less related depreciation and accumulated impairment losses.

Depreciation on other assets is calculated using the straight-line method to write-off their cost to their residual values over their estimated useful lives, as follows:

Hydroelectric stations	- Civil Works	80 years
	- Generation Plant	30 years
Gas turbine plant		25 years
Thermal generation plant		10 - 15 years
Transmission and distribution lines		10 - 25 years
Moveable plant and equipment		5 - 10 years

Depreciation is not provided on freehold land and capital work in progress.

The assets' residual values and useful lives are reviewed and adjusted, if appropriate, at least annually.

Gains and losses on disposal are determined by comparing proceeds with carrying amounts and are included in the income statement.

3. Significant accounting policies (Continued)

3.2 *Foreign currency translation*

The results and financial position of the company are expressed in Malawi Kwacha, which is the functional currency of the company and the presentation currency for the financial statements.

Transactions in currencies other than the entity's functional currency (foreign currencies) are recorded at the rates of exchange prevailing on the dates of the transactions. At each statement of financial position date, monetary items denominated in foreign currencies are retranslated at the rates prevailing on the statement of financial position date.

Exchange differences arising on the settlement of monetary items, and on the retranslation of monetary items, are included in profit or loss for the period.

3.3 *Financial assets*

Investments are recognised and derecognised on their value date where the purchase or sale of an investment is under a contract whose terms require delivery of the investment within the timeframe established by the market concerned, and are initially measured at fair value, net of transaction costs except for those financial assets classified as at fair value through profit or loss, which are initially measured at fair value.

Financial assets are classified into the following specified categories: financial assets 'at fair value through profit or loss' (FVTPL), 'held-to-maturity investments', 'available-for-sale' (AFS) financial assets and 'loans and receivables'. The classification depends on the nature and purpose of the financial assets and is determined at the time of initial recognition.

<u>Effective interest method</u>

The effective interest method is a method of calculating the amortised cost of a financial asset and of allocating interest income over the relevant period. The effective interest rate is the rate that exactly discounts estimated future cash receipts through the expected life of the financial asset, or, where appropriate, a shorter period.

Income is recognised on an effective interest basis for debt instruments other than those financial assets designated as at FVTPL.

<u>Loans and receivables</u>

Trade receivables, loans, and other receivables that have fixed or determinable payments that are not quoted in an active market are classified as 'loans and receivables'. Loans and receivables are initially measured at fair value and subsequently at amortised cost using the effective interest method less any impairment. Interest income is recognised by applying the effective interest rate, except for short-term receivables where the recognition of interest would be immaterial.

3. Significant accounting policies (Continued)

3.3 *Financial assets* (Continued)

Impairment of financial assets
Financial assets, other than those at FVTPL, are assessed for indicators of impairment at each statement of financial position date. Financial assets are impaired where there is objective evidence that, as a result of one or more events that occurred after the initial recognition of the financial asset, the estimated future cash flows of the investment have been impacted. For financial assets carried at amortised cost, the amount of the impairment is the difference between the asset's carrying amount and the present value of estimated future cash flows, discounted at the original effective interest rate.

The carrying amount of the financial asset is reduced by the impairment loss directly for all financial assets with the exception of trade receivables where the carrying amount is reduced through the use of an allowance account. When a trade receivable is uncollectible, it is written off against the allowance account. Subsequent recoveries of amounts previously written off are credited against the allowance account. Changes in the carrying amount of the allowance account are recognised in profit or loss.

With the exception of AFS equity instruments, if, in a subsequent period, the amount of the impairment loss decreases and the decrease can be related objectively to an event occurring after the impairment was recognised, the previously recognised impairment loss is reversed through the profit or loss to the extent that the carrying amount of the investment at the date the impairment is reversed does not exceed what the amortised cost would have been had the impairment not been recognised.

In respect of AFS equity securities, any increase in fair value subsequent to an impairment loss is recognised in equity through other comprehensive income.

3.4 *Financial liabilities and equity instruments*

Classification as debt or equity
Debt and equity instruments are classified as either financial liabilities or as equity in accordance with the substance of the contractual arrangement.

Equity instruments
An equity instrument is any contract that evidences a residual interest in the assets of an entity after deducting all of its liabilities. Equity instruments are recorded at the face value of proceeds received, net of direct issue costs.

Financial liabilities
Financial liabilities are classified as either financial liabilities at FVTPL or other financial liabilities.

Financial liabilities at FVTPL
Financial liabilities are classified as at FVTPL where the financial liability is either held for trading or it is designated as at FVTPL.

3. Significant accounting policies (Continued)

3.4 *Financial liabilities and equity instruments* (Continued)

A financial liability is classified as held for trading if:

- it has been incurred principally for the purpose of repurchasing in the near future; or
- it is a part of an identified portfolio of financial instruments that the company manages together and has a recent:
  (i) Actual pattern of short-term profit-taking; or
  (ii) It is a derivative that is not designated and effective as a hedging instrument.

A financial liability other than a financial liability held for trading may be designated as at FVTPL upon initial recognition if:

- such designation eliminates or significantly reduces a measurement or recognition inconsistency that would otherwise arise; or
- the financial liability forms part of a group of financial assets or financial liabilities or both, which is managed and its performance is evaluated on a fair value basis, in accordance with the company 's documented risk management or investment strategy, and information about the grouping is provided internally on that basis; or
- it forms part of a contract containing one or more embedded derivatives, and IAS 39 permits the entire combined contract (asset or liability) to be designated as at FVTPL.

Financial liabilities at FVTPL are stated at fair value, with any resultant gain or loss recognised in profit or loss. The net gain or loss recognised in profit or loss incorporates any interest paid on the financial liability.

<u>Other financial liabilities</u>
Other financial liabilities, including borrowings, are initially measured at fair value, net of transaction costs.

Other financial liabilities are subsequently measured at amortised cost using the effective interest method, with interest expense recognised on an effective yield basis.

The effective interest method is a method of calculating the amortised cost of a financial liability and of allocating interest expense over the relevant period. The effective interest rate is the rate that exactly discounts estimated future cash payments through the expected life of the financial liability, or, where appropriate, a shorter period.

3.5 *Provisions*
Provisions are recognised when the company has a present obligation (legal or constructive) as a result of a past event, it is probable that the company will be required to settle the obligation, and a reliable estimate can be made of the amount of the obligation.

The amount recognised as a provision is the best estimate of the consideration required to settle the present obligation at the statement of financial position date, taking into account the risks and uncertainties surrounding the obligation.

3.6 *Capital work in progress*
Capital work in progress is valued at cost including capitalised borrowing costs where appropriate.

3. Significant accounting policies (Continued)

3.7 *Inventories*

Inventories are valued at lower of cost and net realisable value.

Cost is determined on the following basis:-

- Consumable stores are valued at average landed cost.
- Goods in transit are valued at invoiced cost.

3.8 *Impairment of non-financial assets*

At each statement of financial position date, the Company reviews the carrying amounts of its non-financial assets to determine whether there is any indication that those assets have suffered an impairment loss. If any such indication exists, the recoverable amount of the asset is estimated in order to determine the extent of the impairment loss (if any). Where it is not possible to estimate the recoverable amount of an individual asset, the company estimates the recoverable amount of the cash-generating unit to which the asset belongs. Where a reasonable and consistent basis of allocation can be identified, corporate assets are also allocated to individual cash-generating units, or otherwise they are allocated to the smallest group of cash-generating units for which a reasonable and consistent allocation basis can be identified.

Recoverable amount is the higher of fair value less costs to sell and value in use. In assessing value in use, the estimated future cash flows are discounted to their present value using a pre-tax discount rate that reflects current market assessments of the time value of money and the risks specific to the asset for which the estimates of future cash flows have not been adjusted.

If the recoverable amount of an asset (or cash-generating unit) is estimated to be less than its carrying amount, the carrying amount of the asset (cash-generating unit) is reduced to its recoverable amount. An impairment loss is recognised immediately in profit or loss.

3.9 *Revenue*

Revenue arises from the sale of electricity and is recognised based on meter readings made during the period. Where meters have not been read, estimated readings (based on average usage in the previous months) are used to estimate consumption.

3.10 *Deferred income*

Capital contributions from consumers and grants from Government, both of which are received in respect of property, plant and equipment costs for specific purposes, are recognised as deferred income once their receipt can be reasonably anticipated. The deferred income is taken to profit or loss in equal annual instalments over the useful lives of the related assets as determined for depreciation purposes.

3. Significant accounting policies (Continued)

3.11 *Taxation*

Income tax expense represents the sum of the tax currently payable and deferred tax.

Current tax

The tax currently payable is based on taxable profit for the year. Taxable profit differs from profit as reported in the statement of comprehensive income because it excludes items of income or expense that are taxable or deductible in other years and it further excludes items that are never taxable or deductible. The company's liability for current tax is calculated using tax rates that have been enacted or substantively enacted by the statement of financial position date.

Deferred tax

Deferred tax is recognised on differences between the carrying amounts of assets and liabilities in the financial statements and the corresponding tax bases used in the computation of taxable profit, and is accounted for using the liability method. Deferred tax liabilities are generally recognised for all taxable temporary differences, and deferred tax assets are recognised to the extent that it is probable that taxable profits will be available against which these deductible temporary differences can be utilised. Such assets and liabilities are not recognised if the temporary difference arises from goodwill or from the initial recognition (other than in a business combination) of other assets and liabilities in a transaction that affects neither the taxable profit nor the accounting profit.

Deferred tax is calculated at the tax rates that are expected to apply in the period when the liability is settled or the asset realised, based on tax rates (and tax laws) that have been enacted or substantially enacted at the statement of financial position date. The measurement of deferred tax liabilities and assets reflects the tax consequences that would follow the manner in which the company expects, at the reporting date, to recover or settle the carrying amount of its assets and liabilities.

Deferred tax assets and liabilities are offset when there is a legally enforceable right to set off current tax assets against current tax liabilities and when they relate to income taxes levied by the same taxation authority and the company intends to settle its current tax assets and liabilities on a net basis.

3.12 *Retirement benefits*

The company contributes to a defined contribution pension scheme for employees. Contributions are charged to profit or loss as incurred.

Additionally, the company provides retirement benefits to employees who have been with the company and its predecessor body for at least ten years in the form of exgratia payments (note 11).

3. Significant accounting policies (Continued)

3.13 *Borrowing costs*

Borrowing costs directly attributable to the acquisition, construction or production of qualifying assets are capitalised as part of the cost of those assets. Borrowing costs include exchange differences arising from foreign currency borrowings to the extent that they are regarded as an adjustment to interest costs. Capitalisation of such borrowing costs ceases when the assets are substantially ready for their intended use. All other borrowing costs are expensed in the period in which they are incurred. A qualifying asset is an asset that necessarily takes a substantial period of time to get ready for its intended use or sale.

4. Critical accounting judgements and key sources of estimation uncertainty

4.1 *Critical judgements in applying the company's accounting policies*

No critical judgements were made by management during the current period, which would have a material impact on the financial statements.

4.2 *Key sources of estimation uncertainty*

Key assumptions concerning the future, and other key sources of estimation uncertainty at the statement of financial position date, that have a significant risk of causing a material adjustment to the carrying amounts of assets and liabilities within the next financial year are discussed below.

4.2.1 Provision for doubtful debts

In arriving at the provisions for doubtful debts (note 8), management has taken into account the past payment history of the individual debtors, the willingness or otherwise of customers to acknowledge their indebtedness, together with other objective evidence of impairment as a result of events that have occurred after initial debt recognition which suggest that future cash flows may be impaired. Provisioning on this basis can be subjective by nature as it requires the assessment of financial, as well as non-financial information in arriving at an impairment value, which can only be borne out by future events.

4.2.2 Valuation of Land and Buildings

Land and building were revalued as at 30 June 2010 by D.R. Whayo BSC UK, Dip (Urb Man) BA, MRICS MSIM, a chartered surveyor of Knight Frank (Malawi) Limited. The basis of valuation used was depreciated replacement cost.

4.2.3 Valuation of Property, plant and equipment

The Company reviews the estimated useful lives and residual values of property, plant and equipment at the end of each annual reporting period as described in note 3.1 above.

5. Property, plant and equipment

2010	**Land and buildings K'000**	**Plant and machinery generation K'000**	**Distribution K'000**	**Other office equipment K'000**	**Motor vehicles K'000**	**Total K'000**
COST OR VALUATION						
At beginning of year	1,220,224	18,272,332	9,999,943	1,613,111	1,352,301	32,457,911
Additions	46,407	637,807	396,724	60,517	23,774	1,165,229
Transfers from capital work in progress	10,002	-	676,441	-	-	686,443
Disposals	(14,600)	-	-	(94,844)	(42,527)	(151,971)
Revaluations surplus	997,875	-	-	-	-	997,875
Derecognitions	-	(59,466)	(595,533)	(34,655)	-	(689,654)
At end of the year	2,259,908	18,850,673	10,477,575	1,544,129	1,333,548	34,465,833
DEPRECIATION						
At beginning of the year	69,595	3,175,014	2,114,125	859,415	533,734	6,751,883
Less derecognised assets	-	(56,129)	(586,067)	(31,579)	-	(673,775)
Charge for the year	71,566	477,841	373,431	98,192	136,755	1,157,785
Reversal of depreciation on revaluation	(141,161)	-	-	-	-	(141,161)
Disposals	-	-	-	(94,844)	(33,304)	(128,148)
At end of the year	-	3,596,726	1,901,489	831,184	637,185	6,966,584
NET BOOK AMOUNT At end of the year	2,259,908	15,253,947	8,576,086	712,945	696,363	27,499,249

5. Property, plant and equipment (Continued)

2011	**Land and buildings** K'000	**Plant and machinery generation** K'000	**Distribution** K'000	**Other office equipment** K'000	**Motor vehicles** K'000	**Total** K'000
COST OR VALUATION						
At beginning of year	2,259,908	18,850,673	10,477,575	1,544,129	1,333,548	34,465,833
Additions	42,494	23,369	-	100,161	278,844	444,868
Transfers from capital work in progress	-	-	842,821	-	-	842,821
Prior year adjustment	-	-	(156,546)	-	-	(156,546)
Disposals	-	-	-	(3,187)	(6,250)	(9,437)
Derecognitions	-	(72,184)	(8,506)	(436,979)	(560,462)	(1,078,131)
At end of the year	2,302,402	18,801,858	11,155,344	1,204,124	1,045,680	34,509,408
DEPRECIATION						
At beginning of the year	-	3,596,726	1,901,489	831,184	637,185	6,966,584
Less derecognised assets	-	(72,184)	(8,502)	(423,206)	(560,462)	(1,064,354)
Prior year adjustment	-	-	41,488	(9,727)	-	31,761
Charge for the year	70,899	486,021	395,409	145,040	217,182	1,314,551
Disposals	-	-	-	(1,805)	(3,164)	(4,969)
At end of the year	70,899	4,010,563	2,329,884	541,486	290,741	7,243,573
NET BOOK AMOUNT						
At end of the year	2,231,503	14,791,295	8,825,460	662,638	754,939	27,265,835

5. Property, plant and equipment (Continued)

Siltation

The company has four generation plants, one at Wovwe on South Rukuru River and three on the Shire River. The generation plants historically experience problems with siltation which reduces dam capacities and this, in turn, impacts on electricity generation capabilities. The level of siltation varies throughout the period, with the problem at its worst during the rainy season (the period from November to March). Siltation is a direct result of environmental degradation along the Shire River's catchment area.

To maintain operational capacity the company is involved in a continuous process of desiltation. This involves the dredging of the dams and during the rainy season efforts are also undertaken to remove debris from the Shire River. These efforts are set to continue for the foreseeable future. All costs associated with these efforts are expensed to profit or loss as they are incurred.

There are times when load shedding is effected due to reduced generation capacity. This is largely restricted to weekends and peak times during week days.

International Accounting Standard 36, *Impairment of Assets*, requires that where there is evidence that indicates that an asset's economic performance will be less than expected then the asset is assessed for impairment. An impairment loss should then be recognised in the financial statements where appropriate. No impairment loss has been recognised in these financial statements, as for most of the period ESCOM is able to generate the power requirements of the country. In addition, such problems are a normal operational feature of hydro generation plants in relation to the environment in which they operate, hence load shedding up to a point is within the planned service levels of such plants.

Valuation of land and buildings

Land and buildings were valued as a 30 June 2010 by D.R. Whayo BSC UK, Dip (Urb Man) BA, MRICS MSIM, a chartered surveyor of Knight Frank, (Malawi) Limited. The basis of valuation used was depreciated replacement cost.

			2011 K'000	2010 K'000
Land and buildings at cost or revaluation comprises the following:				
Leasehold	-	at cost	123,159	80,665
Freehold	-	at 2010 valuation	681,170	681,170
Leasehold	-	at 2010 valuation	1,498,073	1,498,073
Total cost or valuation at end of the year			2,302,402	2,259,908

Derecognitions

The Corporation carried out a physical verification of assets as at 30 June 2010. The exercise revealed that there were assets out there which were not being used due to the fact that they were in a state of disrepair or that they are damaged beyond repair. The Corporation identified these assets and resolved to derecognise them. The derecognised assets are being sold as scrap.

Reclassifications

Some reclassifications have been processed within certain asset categories to align the schedule with the detailed fixed asset register. These reclassifications do not have an impact on the net amount of property, plant and equipment.

Encumbrance

The assets are encumbered as disclosed in notes 15, 17 and 18.

Prior year adjustment

In the current year, the Corporation has reversed the prior year overstatement in transfers from capital work in progress. The overstatement arose when some stores issues were captured twice in 2010.

		2011 K'000	2010 K'000
6.	**Capital work in progress**		
	Balance at beginning of the year	1,969,193	1,996,290
	Write offs	(128,131)	(30,485)
	Additions:		
	Funded from internal resources	868,585	689,831
	Funded from capital grants	1,922,750	-
		4,632,397	2,655,636
	Transfer to property, plant and equipment	(842,821)	(686,443)
	Balance at end of the year	3,789,576	1,969,193
	Capital work in progress is analysed as follows:		
	Projects	3,100,988	725,966
	General development	688,588	1,243,227
	Total capital work in progress	3,789,576	1,969,193

7. Deferred tax

The major components of deferred tax provision are analysed as follows:

Revaluation surplus	610,823	-
Accelerated capital allowances	6,709,371	-
Tax losses	(7,736,330)	-
Other temporary differences	(894,581)	-
Total deferred tax assets	1,310,717	-

8. Inventories

General stores	476,739	718,121
Goods in transit	755,219	376,883
Provision for obsolete inventory	(247,438)	(269,520)
Total inventories	984,520	825,484

9. Receivables

	2011 K'000	2010 K'000
Trade receivable	2,749,564	4,089,275
Staff loans and advances	723,469	837,384
Other receivables and prepayments	512,180	333,312
Gross receivables	3,985,213	5,259,971
Doubtful debt provisions:		
- trade receivables	(913,473)	(2,368,820)
- government accounts	(35,996)	(545,564)
	3,035,744	2,345,587
Loans and advances impairment provision	(44,114)	(156,442)
Total receivables	2,991,630	2,189,145

Included in staff loans and advances are housing loans of K163m (2010: K195m) which are repayable over periods of up to twelve years. Staff housing loans are secured by charges over the related properties.

The Company's credit risk is primarily attributed to its trade receivables, which comprise of individual and corporate customers who use electricity throughout the country.

	2011 K'000	2010 K'000
Movement in allowance for doubtful debts		
At beginning of the year	2,914,384	1,799,845
Bad debts written off	(1,779,304)	-
(Decrease)/increase in the year	(185,611)	1,114,539
At end of the year	949,469	2,914,384

In determining the recoverability of a trade receivable, the company considers any change in the credit quality of the trade receivables from the date credit was initially granted up to the reporting date.

There is no significant concentration of credit risk, with exposure spread over a relatively large number of customers across the country.

The directors believe that the value of the receivables as at 30 June 2011 represent their fair value as at that date.

10. Deferred income

	Government grants K'000	Capital contributions K'000	2011 Total K'000	2010 Total K'000
At beginning of the year	1,029,520	3,572,988	4,602,508	3,726,656
Received during the year	522,922	741,045	1,263,967	1,016,099
Grants written off	(29,761)	-	(29,761)	-
Released to income statement during the year	(72,685)	(93,344)	(166,029)	(140,247)
At end of the year	1,449,996	4,220,689	5,670,685	4,602,508

11. Pension arrears (Severance allowance provision)

	2011 K'000	2010 K'000
At beginning of the year	2,351,345	2,427,917
Payments made during the year	(165,427)	(517,157)
(Reversal)/charge for the year	(1,266,600)	440,585
At end of the year	919,318	2,351,345

Within the year, the legislation giving rise to the requirement to provide for severance pay, the Employment Act was revised and Parliament passed into law the Pensions Act. The principal change in the legislation is the removal of the provision requiring employers to accrue for severance pay relating to future retirement costs. In addition, the legislation has introduced an obligation on the part of employers to ensure that employees are covered by registered pension arrangements.

The legislations have given rise to changes in accounting for post retirement benefits for all employers. The company has adopted the provisions of the new legislation as at 30 June.

The balance on the severance provision account, after making provision for the requirements of the new legislation, cystallised into pension arrears on 1 June 2011. The amount is payable to a pension fund over an eight year period.

12. Retirement benefit fund

	2011 K'000	2010 K'000
At beginning of the year	714,775	688,407
Payment made during the year	(29,421)	(62,423)
Charge for the year	96,241	88,791
At end of the year	781,595	714,775

Upon retirement, employees who have worked for the company and its predecessor body for a period longer than fifteen years are entitled to one and a half years' salary as a retirement benefit. Those employees who retire after working for the company and its predecessor body for ten years or more but not exceeding fifteen years, are entitled to a retirement benefit equal to one year's salary.

The provision, which is unfunded, is based on the assumption that salaries will increase broadly in line with inflation. An actuarial valuation of the obligation was carried out as at 30 June 2008 by QED Actuaries and Consultants (Pty) Limited of South Africa represented by Giulia Tognon, Fellow of the Actuarial Society of South Africa who provided for estimates up to 2012 on the basis that there would be no significant changes in the work force and the underlying assumptions.

The assumptions used were:

- Discount rate of 8.5% per annum
- Salary increase rate of 7% per annum
- Redundancy rate of 3% per annum at all ages
- Voluntary withdrawals rate of 12 % at age 18, reducing to nil from age 50
- Mortality at a rate of 0.4% at age 20, increasing to 0.8% from age 50

The Company is of the opinion that there has not been a significant change to the assumptions and consider these to be relevant in the current year.

13. Borrowings

		2011 K'000	2010 K'000
Balance at beginning of the year		10,649,098	10,756,577
Additions:	- interest charged	426,118	360,914
	- exchange losses expensed	451,294	(170,201)
Less:	- interest paid	(578,447)	(156,527)
	- amount transferred to HIPC funds	(69,266)	(71,327)
	-amount transferred from capital contribution	1,675,232	-
	- movement in fair value of zero coupon bond	(82,282)	(70,338)
Total borrowings at end of the year		12,471,747	10,649,098
Less amounts included in current liabilities		(8,897,200)	(6,739,588)
Non-current borrowings		3,574,547	3,909,510
Analysis of current borrowings			
Amounts due within one year		4,225,137	2,945,710
Principal and interest in arrears		4,672,063	3,793,878
		8,897,200	6,739,588

		2011 K'000	2010 K'000
13.	**Borrowings** (Continued)		
	Details of borrowings are set out below:		
	Government of Malawi	8,209,626	6,202,064
	These Malawi Kwacha loans are repayable over terms of up to 30 years and carry interest at rates varying between 3% (2010: 3%) and 12% (2010: 12%). The last payment is due in 2034.		
	Included in the Government loans is a soft loan amounting to K1,675m from Malawi Government. The loan was obtained from Chinese Government for construction works at Kapichira Power Station. The loan bears no interest but the formal agreement incorporating all the terms and condition of the loans has not been signed.		
	European Investment Bank	424,259	429,904
	The loan, which is denominated in Euros, was obtained from this lender and qualifies for HIPC relief. As the principal amounts fall due the amount due is transferred to a separate HIPC account. The amount converted to the HIPC loan fund was K69.3m (2010: 71.3m). The loan attracts interest at a rate of 3.5% (2010: 3.5%) per annum. The last installment is due in 2017. The amount is now payable to the Government of Malawi.		
	SEB SCADA	66,689	65,899
	The loan is denominated in Swedish Kroner. It is repayable in half yearly installments in April and October over a period of 25 years after a grace period of 7 years. The agreement was signed in 1997 and all interest to April 2005 was capitalised. The loan is on lent to ESCOM from the Government of Malawi.		
	The loan attracts interest at a rate of 3% (2010: 3%) per annum.		
	SIDA	2,256,455	2,209,233
	This loan is in Swedish Kroners. The agreement was signed on 17 November 2000. The loan was obtained through the Malawi Government. The loan attracts interest at a rate of 3% (2010: 3%) per annum. Repayments commenced in 2007. The loan is on lent to ESCOM from Government of Malawi.		
	Development Bank of Southern Africa	2,280,525	2,323,670
	The loan is denominated in South African Rands. The capital amount is repayable in one payment after a grace period of 15 years in 2019. The loan is secured by a Cessation and Pledge Agreement in respect of a zero coupon bond with a maturity value of the principal amount which is R85 million after 15 years. Interest is at the rate of 3 months ZAR-JIBAR-SAFEX plus operating and funding cost margin currently 0.9% (2010: 0.9%) plus a 5% (2010: 5%) risk margin. Interest is repayable half yearly in arrears. The loan is guaranteed by the Government of Malawi.		
	Fair value of zero coupon bond held with Investec Bank	(874,973)	(690,839)
	World Bank Project Preparatory Fund	109,166	109,167
	The purpose of this loan is to finance the preparation activities for the Southern African Power Pool Project. The fund amount is USD 380,000. The loan is guaranteed by the Government of Malawi. The project failed and the loan has become immediately payable and is therefore classified as current liability.		
	Total borrowings	12,471,747	10,649,098

13. **Borrowings** (Continued)

	2011 K'000	2010 K'000
The following summary indicates the repayment terms of the loans outstanding:		
Dates of repayment:		
Within 5 years	6,740,515	4,917,866
Between 5 and 10 years	1,479,371	1,479,371
After 10 years	4,251,861	4,251,861
	12,471,747	10,649,098
The loans are repayable in:		
Malawi Kwacha	10,302,052	8,479,403
Foreign currencies	2,169,695	2,169,695
	12,471,747	10,649,098

Defaults and breaches of Loan Agreements

Development Bank of Southern Africa Limited

The company has not met the requirements of Article 12.3 of the loan agreement which requires the following ratios:-

Ratios	Required	Actual 2011	Actual 2010
Debt/Equity	1:1	3	3.08
Debt to capital Employed ratio %	50	308	308
Liquidity ratio	1.2:1	0.37:1	0.37:1

Article 11 of the Agreement states that DBSA is entitled, after giving the borrower 30 days notice, to suspend draw downs from the loan or to terminate the agreement and claim from the borrower immediate payment of all outstanding amounts should the borrower commit any breach of this agreement, provided that DBSA may at its entire discretion, dispense with the giving of the 30 (thirty) days notice. ESCOM has not obtained a waiver from DBSA to prevent the loan from being recalled. The full amount of the loan has been classified as a current liability.

Government loans

In addition, the Corporation was at the statement of financial position date, in arrears on Malawi Government loans by K4,416 million. Discussions are underway between ESCOM and Malawi Government to have the loans converted into equity. The arrears have been included in the current portion of the borrowings in the statement of financial position.

14. HIPC funds

	2011 K'000	2010 K'000
Industrial Development Company of South Africa	32,051	32,051
Commonwealth Development Corporation Company plc	2,489,559	2,489,559
European Investment Bank	523,287	448,711
Eksportifinans (NORAD) –NOK	89,885	89,885
Principal amounts transferred from loans	3,134,782	3,060,206
Interest accrued on funds	4,819	5,310
Total HIPC funds at the end of the period	3,139,601	3,065,516
Less- due within one year included in current liabilities	(74,085)	(66,017)
Non-current HIPC funds	3,065,516	2,999,499
Movement in HIPC funds:		
At beginning of the year	3,065,516	2,994,190
Amount qualifying for HIPC during the period	69,266	66,016
Accrued interest on HIPC funds	4,819	5,310
At end of the year	3,139,601	3,065,516

Following Malawi's qualification for the Highly Indebted Poor Countries (HIPC) initiative from its multilateral donors in 2004, certain loans that the company had from Commonwealth Development Corporation Company plc, European Investment Bank and the Industrial Development Company of South Africa were waived. The loans are now repayable to the Government. The liability is set out at the Kwacha value at the date the loans qualified for the HIPC initiative and the repayment terms remain unchanged. In a letter dated 15 February 2005 from the Secretary to the Treasury to ESCOM, the Malawi Government advised ESCOM to credit this amount to a HIPC account held at Reserve Bank of Malawi as the loan repayments fell due. Interest has been accrued at the rates of the original loans from third parties and no objection has been received from Government to this treatment.

The interest rates are 12% for IDC of South Africa, 9.25% for CDCC and 1% for the EIB Loan. The loans are payable in half yearly instalments as follows:

- IDC: 2 March and 2 September;
- CDCC: 20 June and 20 December; and
- EIB: 15 April and 15 October.

15. Bank borrowings

	2011 K'000	2010 K'000
National Bank of Malawi	378,944	532,070
Total bank borrowings	378,944	532,070
Analysed as:		
Amount due within one year	175,662	231,759
Amount due after one year	203,282	300,312
Total	378,944	532,071
Movement in the year		
At beginning of the year	532,071	790,852
New loans	-	100,000
Repayments	(153,127)	(361,256)
Interest charge	57,641	136,912
Interest paid	(57,641)	(134,437)
At end of the year	378,944	532,071

The borrowings carry interest of 17.75% (18.75%: 2010 p.a) for National Bank of Malawi (2.75% above base rate). The National Bank of Malawi borrowings, which are secured over certain land and buildings of ESCOM Ltd, are repayable over a period of 84 months and the last installment is due 30 November 2012.

16. ESCOM Limited Pension Fund loan

	2011 K'000	2010 K'000
At the beginning of the year	499,275	444,878
Interest charge for the year	-	54,397
Repayments during the year	(219,105)	-
Interest reversal	(53,503)	-
At end of the year	226,667	499,275
Analysed as:		
Amount due within one year	56,667	499,275
Amount due after one year	170,000	-
	226,667	499,275

In September 2007, ESCOM entered into an agreement with the registered Trustees of Electricity Supply Corporation of Malawi Limited Pension Fund to advance K400 million which ESCOM used to advance to its employees who are members of the Pension Fund. The loan attracts interest of 17.5% (2010:17.5) per annum and is repayable quarterly over a period of five years.

During the year, the Board of ESCOM Pension Fund Trustees authorised to suspend interest on the loan. It was further resolved that interest that was accrued as at 31 December 2009 on the loan will still be payable to ESCOM Pension Fund. As a result, in the current year, ESCOM reversed part of the interest that will not be payable and stopped accruing for interest on the loan.

17. Finance leases

	2011 K'000	2010 K'000
Leasing and Finance Company of Malawi Limited	26,810	121,459
National Bank of Malawi	7,821	61,006
Standard Bank of Malawi Limited	272,691	-
Total finance leases	307,322	182,465
Analysed as:		
Amount due within one year	109,393	176,626
Amount due after one year	197,929	5,839
Total	307,322	182,465
Movement in the year		
At beginning of year	182,465	301,458
Additions	278,844	10,893
Repayments	(155,252)	(129,886)
Interest charge	42,782	48,755
Interest paid	(41,517)	(48,755)
At end of year	307,322	182,465

The leases carry interest of 18.75% (2010: 18.75 % p.a.) for National Bank of Malawi and 19% p.a. for Leasing and Finance Company of Malawi Limited. The leases are secured over the vehicles they finance.

18. Financing facilities

The company has the following banking facilities:

	2011 K'000	2010 K'000
Secured overdraft facility with National Bank of Malawi	450,000	450,000
Secured documentary credit facility reviewed annually	50,000	50,000
Secured revolving Bank Insurance Premium	150,000	100,000
Secured long term loan	370,146	527,375
Secured medium term loan	107,461	377,335
Revolving finance lease	150,000	150,000

These facilities are secured on the following securities held by the bank.

a. Board resolution authorising aggregate borrowing of K1,654m;
b. Ministry of Finance consent for K521m;
c. Lien over call accounts held with National Bank of Malawi;
d. Bill of sale over vehicles financed under finance lease facility;
e. Letter of undertaking by the Corporation to the bank assigning all proceeds of the Corporation's from major customers: Illovo Sugar (Malawi) Limited, Limbe Leaf Tobacco Company Limited, Unilever South East Africa (Pvt) Limited, The Bottling and Brewing Group Limited, Packaging Industries (Malawi) Limited, Blantyre Water Board; and
f. All assets debenture for K300m; and
g. Lien over all credit balances in the Corporation's name in ESCOM's books;
h. Letter of undertaking to create a charge of K200m and debenture for K300m if called upon to do so; and
i. A charge of K200m over the Corporation's Head office building valued by Knight Frank at K254m on 8th April 2008.

19. Payables

	2011 K'000	2010 K'000
Trade and other payables	1,544,637	2,062,239
Project payables and retention	167,590	730,250
Consumer deposits	196,013	163,276
Total payables	1,908,240	2,955,765

Included in payables are liabilities of K506m (2010: K241m) denominated in foreign currencies. The average trade payables period is 60 days. No interest is charged on overdue balances.

20. Exchange losses

		Funding of capital assets K'000	Other liabilities K'000	2011 K'000	2010 K'000
Realised	- Bank deposit	-	(11,013)	(11,013)	(3,686)
	- short-term (payables)	(55)	-	(55)	24,203
		(55)	(11,013)	(11,068)	20,517
Unrealised	- borrowings	507,212	-	507,212	(269,239)
	- short-term (payables)	(46,455)	-	(46,455)	43,176
	-Assets (Zero Coupon Bond)	(101,853)	-	(101,853)	-
Total unrealised		358,904	-	358,904	(226,063)
Total exchange losses		358,849	(11,013)	347,836	(205,546)

21. Loss before taxation

Profit/loss before taxation is arrived at after taking into account:

	2011 K'000	2010 K'000
Auditors' remuneration - current period	19,106	17,000
- prior period	-	1,651
Directors' fees	2,178	1,263
Directors expenses	21,062	21,567
Staff costs	4,417,307	3,030,066
Severance allowance (reversal)/charge	(1,266,600)	440,585
Retirement benefit charge	95,422	88,790
Pension costs	101,807	85,716

22. Taxation

22.1 Income tax

	2011	2010
Deferred taxation	(1,310,717)	-

22. Taxation (Continued)

22.2 The standard rate of tax is reconciled as follows:

	2011	2010
	K'000	K'000
Standard rate	30%	-
Deferred tax asset not recognised in previous years	(59%)	-
Effective rate of tax	(29%)	-

The deferred asset has been recognised in the financial statements in the current year as the directors believe that the company will, in future, make taxable profits which will offset the tax losses.

23. Reconciliation of profit/(loss) before interest and taxation to cash generated from operations

	2011 K'000	2010 K'000
Profit before interest and taxation	4,963,962	918,391
Depreciation of property, plant and equipment	1,346,312	1,157,785
WIP write off and derecognition of assets	141,909	46,364
Profit on disposal of property, plant and equipment	(13,250)	(7,931)
Capital contributions and grants released to profit/(loss)	(166,029)	(140,247)
Exchange losses expensed	347,836)	(205,546)
	6,620,740	1,768,816
Movements in working capital:		
Movement in inventories	(159,036)	448,113
Movement in receivables	(802,485)	390,473
Movement in payables	(1,047,525)	212,037
Movement in retirement benefit provision	66,820	26,368
Movement in severance provision	(1,432,027)	(76,572)
Cash generated from operations	3,246,487	2,769,235
Loss before interest and taxation is determined as follows:		
(Profit)/loss before taxation	4,495,480	86,457
Interest on borrowings, financed leases and bank borrowings	527,827	642,411
Interest on bank overdraft	32,667	223,056
Interest receivable	(92,012)	(33,533)
Profit before interest and taxation	4,963,962	918,391

24. Capital commitments

	2011 K'000	2010 K'000
Authorised by the company and contracted	639,747	759,817
Authorised by the company but not contracted	3,368,032	14,915,850
Total commitments	4,007,779	15,675,667

Capital commitments will be financed by external borrowings together with internally generated funds.

		2011 K'000	2010 K'000
25.	**Contingent liabilities**		
25.1	Legal claims	420,711	476,407

These are claims, inclusive of legal fees, by various customers against ESCOM in respect of goods damaged, etc., due to surges in power supply. The figures are estimated based on information provided by the company's lawyers.

25.2 Guarantees

The Company makes an undertaking by introducing its employees to various financial institutions to obtain personal loans. The Company undertakes to continue remitting the employees' salaries to such institutions and should there be a default on such loans, the Company's responsibility is to remit the employees' salaries to the financial institutions. The Company's obligation is limited to the employees' salaries. If such amounts are not adequate to cover the outstanding employees' loans, the financial institutions have no recourse against the Corporation.

26. Related party transactions

Related party transactions are at arms length and the amounts due from and due to related parties are as follows:

	2011 K'000	2010 K'000
Receivables		
Statutory corporations	133,845	107,358
Government departments	56,685	630,979
Specific provision for bad debts	(44,603)	(545,564)
	145,927	192,773
Loans		
Government of Malawi including SIDA and EIB Loan (Note 13)	10,890,340	8,395,629
HIPC Funds		
Government of Malawi (Note 14)	3,139,601	3,065,516
Compensation of key management staff		
Salaries, bonuses and benefits	67,010	61,774

The following transactions were carried out with related parties:

	2011 K'000	2010 K'000
Interest on Government of Malawi loans	101,531	73,632
Sales to Statutory Corporations	1,186,376	965,421
Sales to Government Departments	481,731	341,781
	1,668,107	1,307,202

27. Financial assets and liabilities

Accounting categories and fair values

	Notes	Held to maturity K'000	Loans and receivables K'000	Other amortised cost K'000	Total carrying amount K'000	Fair value K'000
30 June 2011						
Assets						
Receivables	9	-	2,991,630	-	2,991,630	2,991,630
Bank current account and cash		-	397,075	-	397,075	397,075
Bank deposit account		1,919,057	-	-	1,919,057	1,919,057
Short term investments		30,702	-	-	30,702	30,702
Total financial assets		1,949,759	3,388,705	-	5,338,464	5,338,464
Liabilities						
Borrowings	13	-	-	12,471,747	12,471,747	12,471,747
HIPC Funds	14	-	-	3,139,601	3,139,601	3,139,601
Bank borrowings	15	-	-	378,944	378,944	378,944
ESCOM Limited Pension Fund loan	16	-	-	226,667	226,667	226,667
Finance leases	17	-	-	307,322	307,322	307,322
Bank overdraft		-	-	56,723	56,723	56,723
Payables	19 & 11	-	-	2,827,558	2,827,558	2,827,558
Total financial liabilities		-	-	19,408,562	19,408,562	19,408,562

27. Financial assets and liabilities (Continued)

Accounting categories and fair values	Notes	Held to maturity K'000	Loans and receivables K'000	Other amortised cost K'000	Total carrying amount K'000	Fair value K'000
30 June 2010						
Assets						
Receivables	9	-	2,189,145	-	2,189,145	2,189,145
Bank current account and cash		-	315,121	-	315,121	315,121
Bank deposit account		695,384	-	-	695,384	695,384
Short term investments		-	16,345	-	16,345	16,345
Total financial assets		695,384	2,520,611	-	3,215,995	3,215,995
Liabilities						
Borrowings		-	-	10,649,098	10,649,098	10,649,098
HIPC Funds	14	-	-	3,065,516	3,065,516	3,065,516
Bank borrowings		-	-	532,071	532,071	532,071
ESCOM Limited Pension Fund loan		-	-	499,275	499,275	499,275
Finance leases		-	-	182,465	182,465	182,465
Bank overdraft	18	-	-	935,330	935,330	935,330
Payables	19	-	-	2,955,765	2,955,765	2,955,765
Total financial liabilities		-	-	18,819,520	18,819,520	18,819,520

27. Financial risk management (Continued)

(a) Introduction and overview

The Company has exposure to the following risks arising from its transactions in financial instruments:

- Credit risk;
- Liquidity risk;
- Market risk;
- Currency risks; and
- Operational risk.

This note presents information about the Company's exposure to each of the above risks, the Company's objectives, policies and processes for identification, measurement, monitoring and controlling risk, and the Company's management of capital.

Risk management framework

The Company's approach to risk management is based on a well-established governance process and relies both on individual responsibility and collective oversight, supported by comprehensive reporting. This approach balances stringent corporate oversight with independent risk management structures within the business units.

The Board of Directors has overall responsibility for the establishment and oversight of the Company's risk management framework. The Board develops the risk appetite and risk tolerance limits appropriate to the Company's strategy and requires that management maintains an appropriate system of internal controls to ensure that these risks are managed within the agreed parameters. The Board delegates risk related responsibilities to Board committees, which are as follows: The Audit committee, Staff and Finance Committee and the Technical Committee. All Board committees have non-executive members and report regularly to the Board of Directors on their activities.

The Company's risk management policies are established to identify and analyse the risks faced by the Company, to set appropriate risk limits and controls, and to monitor risks and adherence to limits. Risk management policies and systems are reviewed regularly to reflect changes in market conditions on the services offered. The Company strives to maintain a disciplined and constructive control environment, in which all employees understand their roles and obligations.

The Audit Committee is responsible for monitoring compliance with the company's risk management policies and procedures, and for reviewing the adequacy of the risk management framework in relation to the risks faced by the company. The Audit Committee is assisted in these functions by senior members of management who undertakes both regular and ad-hoc reviews of risk management controls and procedures, the results of which are reported to the Board and its committees where necessary.

27. Financial risk management (Continued)

(b) Credit risk

Credit risk is the likelihood of financial loss to the Company if a customer or counterparty to financial instrument fails to meet its contractual obligations, and arises principally from the company's trade receivables. For risk management reporting purposes, the company considers and consolidates all elements of credit risk exposure such as individual obligor default risk. The Company carries a risk of loss due to default of payment by customers. Settling of bills with cheques increases the risk due to the likelihood of the cheques being dishonored by various financial institutions.

Management of credit risk

The Company's terms are normally 30 days and if the customers do not settle the bills before 30 days, electricity to the customer is disconnected and is only reconnected upon payment of the bill. Periodically together with the management accounts, the debtors' age analysis is reviewed and action points agreed to reduce the trade receivables. The Board of Directors has delegated this responsibility to its senior management through the Audit Committee to ensure that the risk is minimised. Some of the measures being taken to reduce the risk are:

- Installing of pre-paid meters which eliminates the debt as customers pay upfront for the service;
- Disconnecting customers' accounts with an unsettled bill of more than 30 days;
- Minimising on non-technical losses to avoid pilferage or illegal connections by physically inspecting customer's premises;
- Enforcing credit control procedures when allowing customers to make cheque payments; and
- Engaging lawyers or debt collection agencies to collect money from defaulting customers.

Exposure of credit risk

Maximum exposure to credit risk

The table below shows the maximum exposure to credit risk by class of financial instrument. Financial instruments include financial instruments defined and recognised under IAS 39 *Financial Instruments: Recognition and Measurement* as well as other financial instruments not recognised. The maximum exposure is shown gross as the nature of the debtors is such that the company holds no collateral over the receivables.

27. Financial risk management (Continued)

Gross maximum exposure

	2011 K'000	2010 K'000
Financial assets		
Receivables	2,991,630	5,259,971
Bank current account	397,075	315,121
Bank deposits accounts	1,919,057	695,384
Taxation recoverable	30,702	16,645
Total	5,338,464	6,287,121

The Company's credit risk is primarily attributed to provision of electricity on credit extended to its customers. The amounts presented in the statement of financial position are net of provisions for doubtful debts as shown note 8. The specific provision represents allowances for estimated irrecoverable amounts when there is objective evidence that the asset is impaired.

The credit risks on balances with banks are limited because the counterparties are financial institutions with satisfactory credit ratings.

	2011 K'000	2010 K'000
Trade receivables		
Gross amount	2,749,564	4,089,275
Allowance for impairment losses	(949,469)	(2,914,384)
Carrying amount	1,800,095	1,174,891
Past due but not impaired	293,896	940,950
Past due comprises:		
60 days	89,578	139,466
60 - 90 days	25,313	94,947
90 - 120days	179,005	706,537
	293,896	940,950

Past due but not impaired receivables

These are debtors over 30 days that have not been provided for because in the opinion of management and based on past experience, some customers delay paying for their bills because either the bills are received late or the disconnection campaign has not been carried out efficiently. Receivables are considered doubtful if the account is dormant and there is evidence that there have been no billings over the past three years.

27. Financial risk management (Continued)

c) Liquidity risk

Liquidity risk is the risk that the Company will encounter difficulty in meeting obligations from its financial liabilities.

The Company's approach to managing liquidity is to ensure, as far as possible, that it will always have sufficient liquidity to meet its liabilities when due, under both normal and stressed conditions, without incurring unacceptable losses or risking damage to the Company's reputation.

Cash flow uncertainty is the Company's major liquidity risk and it is caused mainly by two elements:

- Failing to meet revenue collection targets; and
- Sudden unexpected cash outflows i.e. paying suppliers before due dates or paying penalties or legal charges.

Liquidity risk tends to compound other risks and affects the business operations as liabilities cannot be met when they fall due. For example if customers default, the Company will have to raise cash from other sources to meet its obligations.

Management of Liquidity Risk

Liquidity risk is managed in addition to market, credit and other risks. Because of its tendency to compound other risks, it is impossible to isolate liquidity risk. However, the company takes the following measures to manage the risks.

- Weekly cashflow reviews by senior management to look at company liquidity and to project future net cash flows;
- Monitoring of bank balances and movements by the Treasury office to ensure a healthy cash position;
- Invoices being paid only on due dates;
- Monitoring of slow moving stocks and re order levels in order to hold stocks at appropriate levels; and
- Ensuring that debtor days do not exceed 30 days. Where 30 days are exceeded, ensuring that the customer premises are disconnected of electricity.

Other methods that are used include:

- Looking at future net cash flows on a day-by-day basis. Any day that has a sizeable negative net cash flow is of concern. Such an analysis is supplemented with stress testing by looking at net cash flows on a day-to-day basis assuming that an important counter party defaults.
- Certain techniques of asset-liability management are applied to assess liquidity risk. This is done by matching payables and receivables according to due date patterns.

27. Financial risk management (Continued)

(c) Liquidity risk (Continued)

The table below analyses assets and liabilities into relevant maturity profiles based on the remaining period at 30 June 2011 to the contractual maturity date.

	Notes	Less than 1 month K'000	1 - 3 months K'000	3 - 12 months K'000	Over 1 year K000	Total K'000	Carrying amount K'000
30 June 2011							
Assets							
Receivables	9	1,230,594	861,066	899,970	-	2,991,630	2,189,145
Bank current account and cash		397,075	-	-	-	397,075	397,075
Bank deposits accounts		1,064,105	854,952	-	-	1,919,057	695,384
Taxation recoverable		-	-	30,702	-	30,702	30,702
Total financial assets		2,691,774	1,716,018	930,672	-	5,338,464	3,312,306
Liabilities							
Borrowings	13	4,049,036	-	2,021,610	6,401,101	12,471,747	10,796,986
HIPC Funds	14	-	-	68,321	3,139,601	3,207,922	3,139,601
Bank borrowing	15	17,387,	52,868	89,868	222,648	382,771	226,666
ESCOM Limited Pension Fund loan	16	16,667	10,000	40,000	165,000	231,667	226,666
Finance leases	17	23,253	71,989	209,817	10,846	315,905	307,322
Bank overdraft	18	56,723	-	-	-	56,723	56,723
Payables	19	645,664	95,046	1,559,622	526,981	2,827,313	2,160,620
Total financial liabilities		4,808,730	229,903	3,989,238	10,466,177	19,494,048	16,914,584
Contractual liquidity mismatch		**(2,116,956)**	**1,486,115**	**(3,058,566)**	**(10,466,177)**	**(14,155,584)**	**(13,602,278)**
Cumulative mismatch		**(2,116,956)**	**(630,841)**	**(3,689,407)**	**(14,155,584)**	**-**	**-**

27. Financial risk management (Continued)

	Notes	Less than 1 month K'000	1 - 3 months K'000	3 - 12 months K'000	Over 1 year K'000	Total K'000	Carrying amount K'000
30 June 2010							
Assets							
Receivables	9	1,036,073	130,608	77,864	944,600	2,189,145	2,189,145
Bank current account and cash		315,121	-	-	-	315,121	315,121
Bank deposits accounts		318,836	418,270	-	-	737,106	695,384
Taxation recoverable		-	-	16,645	-	16,645	16,645
Total financial assets		1,670,030	548,878	94,509	944,600	3,258,017	3,216,295
Liabilities							
Borrowings	13	4,063,182	-	1,979,126	6,303,456	12,345,764	10,649,098
HIPC Funds	14	-	-	71,327	3,065,516	3,136,843	3,065,516
Bank borrowing	15	28,377	86,284	146,670	363,376	624,707	532,071
ESCOM Limited Pension Fund loan	16	252,911	237,938	-	-	490,849	499,275
Finance leases	17	14,958	46,309	134,971	6,977	203,215	182,465
Bank overdraft	18	935,330	-	-	-	935,330	935,330
Payables	19	1,340,739	94,986	1,356,765	163,275	2,955,765	2,955,765
Total financial liabilities		6,635,497	465,517	3,688,859	9,902,600	20,692,473	18,819,520
Contractual liquidity mismatch		**(4,965,467)**	**83,361**	**(3,594,350)**	**(8,958,000)**	**(17,434,456)**	**(15,603,225)**
Cumulative mismatch		**(4,965,467)**	**(4,882,106)**	**(8,476,456)**	**(17,434,456)**	**-**	**-**

The contractual liquidity mismatch shows the mismatch before any adjustments are made for product and customer behavioral assumptions. The company's managers address this mismatch by setting guidelines and limits for anticipated liquidity gaps and monitors these gaps daily.

27. Financial risk management (Continued)

(d) Market risk

Market risk is the risk that changes in market prices, such as interest rate, equity prices, foreign exchange rates and credit spreads will affect the Company's income or the value of its holdings of financial instruments. The objective of market risk management is to manage and control risk exposures within acceptable parameters, while optimising the return on risk.

Changes in market conditions expose the Company to risks that can be favourable or unfavourable to its cash flows.

This could be unexpected changes in the rate of inflation, the state of the economy or in interest rates. For example electricity sales demand could be higher than expected due to an increase in economic activities i.e. establishment of new manufacturing companies. Changes in legislation/regulation, exchange rates or interest rates might move favourably or unfavourably to the Company's interests.

Management of market risks

- Marketing, Environmental and Corporate Planning departments monitor the external environment (market) to detect market changes to ensure that the Company is in line with those changes;
- Prompt connection of new customers avoids alternative power usage by customers;
- Converting or replacing overdraft and floating rate finance with fixed rate finance where interest rates are expected to rise and vice versa when they are expected to fall; and
- Matching foreign currency payments with foreign currency receipts which are normally paid in dollars using Mozambique and Zambia receipts.

Exposure of interest rate risk: non-trading portfolio
The principal risk to which non-trading portfolio are exposed is the risk of loss from fluctuations in the future cash flows or fair values of financial instruments because of a change in market interest rates. The Company's interest rate risk is managed principally through borrowings from different banks at the best interest rates it can obtain and monitoring these loans to ensure that they are repaid on a timely basis.

<u>Interest rate sensitivity analysis</u>
The sensitivity analyses below have been determined based on the exposure to interest rates for the finance leases and other bank borrowings as at 30 June 2011. For floating rate liabilities, the analysis is prepared assuming the amount of the liability outstanding at 30 June 2011 was outstanding for the whole year. A 2.5% increase or decrease is used when reporting interest rate risk internally to key management personnel and represents management's assessment of the reasonably possible change in interest rates.

If interest rates had been 2.5% (for all bank borrowings) and 0.5 % (for the 3 months Jibar) higher/lower and all other variables were held constant, the Corporations':

- Profit for the year ended 30 June 2011 would decrease/increase by K20.416 million (2010: K52.864 million). This is mainly attributable to the Corporations' exposure to interest rates on its bank borrowings as all other loans have a fixed interest rate.

The Corporations' sensitivity to interest rates has decreased during the current period mainly due to reduced overdraft and borrowings.

A summary of the Company's maturity profile gap position on non-trading portfolio is as follows:

27. Financial risk management (Continued)

	Notes	Less than 1 month K'000	1 - 3 months K'000	3 - 12 months K'000	over 1 year K'000	Total K'000	Carrying amount K'000
30 June 2011							
Assets							
Bank current account and cash		397,075	-	-	-	397,075	397,075
Bank deposits accounts		1,064,105	854,952	-	-	1,919,057	1,919,057
Taxation recoverable		-	-	30,702	-	30,702	30,702
Total financial assets		1,461,180	854,952	30,702	-	2,346,834	2,346,834
Liabilities							
Borrowings	13	4,131,925	-	2,021,610	6,318,212	12,471,747	10,796,956
HIPC Funds	14	-	-	68,321	3,139,601	3,207,922	3,139,601
Bank borrowing	15	17,387	52,868	89,868	222,648	382,771	378,944
ESCOM Limited Pension Fund loan	16	16,667	10,000	40,000	165,000	231,667	226,667
Finance leases	17	23,253	71989	209,817	10,846	315,905	307,322
Bank overdraft	18	56,723	-	-	-	56,723	56,723
Total financial liabilities		4,245,955	134,857	2,429,616	9,865,307	16,666,735	14,906,213
Contractual liquidity mismatch		**(2,784,775)**	**720,095**	**(2,389,914)**	**(9,865,307)**	**(14,319,901)**	**(12,559,379)**
Cumulative mismatch		**(2,784,775)**	**(2,064,680)**	**(4,454,594)**	**(14,319,901)**	**-**	**-**

27. Financial risk management (Continued)

	Notes	Less than 1 month K'000	1 - 3 months K'000	3 - 12 months K'000	over 1 year K'000	Total K'000	Carrying amount K'000
30 June 2010							
Assets							
Bank current account and cash		315,121	-	-	-	315,121	315,121
Bank deposits accounts		300,789	394,595	-	-	695,384	695,384
Taxation recoverable		-	-	16,645	-	16,645	16,645
Total financial assets		615,910	394,595	16,645	-	1,027,150	1,027,150
Liabilities							
Borrowings	13	4,063,182	-	1,979,126	6,303,456	12,345,764	10,649,099
HIPC Funds	14	-	-	71,327	3,065,516	3,136,843	3,065,516
Bank borrowing	15	28,377	86,784	140,670	363,376	619,207	532,071
ESCOM Limited Pension Fund loan	16	256,911	287,938	-	-	544,849	499,275
Finance leases	17	14,958	46,309	134,971	6,977	203,215	182,465
Bank overdraft	18	935,330	-	-	-	935,330	935,330
Total financial liabilities		5,298,758	421,031	2,326,094	9,739,325	17,785,208	15,863,756
Contractual liquidity mismatch		**(4,682,848)**	**(26,436)**	**(2,309,449)**	**(9,739,325)**	**(16,758,058)**	**(14,836,606)**
Cumulative mismatch		**(4,682,848)**	**(4,709,284)**	**(7,018,733)**	**(16,758,058)**	**-**	**-**

27. Financial risk management (Continued)

(e) Currency risk

The company had the following significant foreign currency positions:

	Notes	USD K'000	ZAR K'000	Swedish Kroner K'000	EURO K'000	Total K'000
30 June 2011						
Assets						
Bank deposits accounts		24,943	-	-	-	24,943
Total financial assets		24,943	-	-	-	24,943
Liabilities						
Borrowings	13	109,167	1,568,385	65,617	426,526	2,169,695
Payables	19	260,906	59,622	-	186,376	506,904
Total financial liabilities		370,073	1,628,007	65,617	612,902	2,676,599
Net open position		**(345,130)**	**(1,628,007)**	**(65,617)**	**(612,902)**	**(2,651,656)**

27. Financial risk management (Continued)

(e) Currency risk (Continued)

	Notes	USD K'000	ZAR K'000	Swedish Kroner K'000	EURO K'000	Total K'000
30 June 2010						
Assets						
Bank deposits accounts		24,943	-	-	-	24,943
Total financial assets		24,943	-	-	-	24,943
Liabilities						
Borrowings	13	109,167	1,632,831	65,617	426,526	2,234,141
Payables	19	717,860	59,622	-	186,376	963,858
Total financial liabilities		827,027	1,692,453	65,617	612,902	3,197,999
Net open position		**(802,084)**	**(1,692,453)**	**(65,617)**	**(612,902)**	**(3,173,056)**

Foreign currency sensitivity analysis
The corporation is exposed mainly to South African Rand, US Dollar, the Euro and the Swedish Kroner as follows: If the external value of the Kwacha was to move by 5% the Company would incur exchange losses as follows:

	Rand impact		US Dollar impact		Euro impact		Swedish Kroner	
	2011 K'000	2010 K'000	2011 K'000	2010 K'000	2011 K'000	2010 K'000	2011 K'000	2010 K'000
Profit or loss	81,400	84,622	17,257	40,104	30,645	30,645	3,281	3,281

(i) This is mainly attributable to the exposure outstanding on payables denominated in Rands and the DBSA loan outstanding as at 30 June 2011 coupled with a change in fair value of the zero coupons bond that is also denominated in Rands.

(ii) This is mainly attributable to the exposure to outstanding dollar project payables as at 30 June 2011.

27. Financial risk management (Continued)

(f) Operational risk

Operational risk arises from execution of the Corporation's business functions. As such, it is a very broad concept including fraud risks, technology risk, legal risk, physical or environmental risks, machine breakdown etc.

More specific it is the risk of loss resulting from inadequate or failed internal processes, people and systems or from external events.

Management of Operational Risk

Operational risk management is coordinated centrally but most commonly implemented in different operational units, the IT department takes care of information risks, the HR department takes care of personnel risks, etc.

Capital risk management

The company manages its capital to ensure that it will be able to continue as a going concern while maximising the returns to stakeholders through the optimisation of the debt and equity balance. The entity's overall strategy remains unchanged from 2009.

The capital structure of the entity consists of debt, which includes the borrowings disclosed in the statement of financial position, cash and cash equivalents and equity attributable to equity holders comprising issued capital, revaluation reserves and retained earnings as disclosed on page 8.

The company is highly geared with the bulk of loans payable to Malawi Government which is also the shareholder of the company.

Gearing ratio
Management reviews the capital structure on a regular basis. The gearing ratio at the year end was as follows:

	2011 K'000	2010 K'000
Debt (i)	19,408,562	18,810,378
Cash and cash equivalents	(2,316,132)	(1,010,505)
Net debt	17,092,430	17,799,873
Equity (ii)	12,828,270	7,022,073
Net debt to equity ratio	1.33:1	2.53:1

(i) Debt includes borrowings and overdrafts
(ii) Equity includes capital and reserves

28. Going concern

The Company's performance has improved greatly from that of previous year, registering a profit of K5.8 billion (2010: K86 million). The bank overdraft has also improved to an overdraft of K56 million (2010: K935 million) with net cash of K2.3 billion (2010: K75 million). Management and the Board believe that the company will continue as a going concern despite the fact that ESCOM's current liabilities still exceed current assets. The situation is as a result of default on repayments of Government loans some of which (especially HIPC Loans) will be converted into equity. In addition to this, the Company has resumed servicing all its external direct loans and this will also improve the solvency position. Management believes that with the current improvement in its financial position, it will be able to maintain its aged system and pay for its long outstanding debts. Furthermore, the Company is about to embark on projects that will substantially improve its operations and make a turn –around to be financially sustainable. Some of these projects are acquisition of a new Billing System, installation of prepaid meters that will improve the revenue management and inflow, rehabilitation of machines at Nkula, upgrading of transmission lines from 132kV to 220kV, rehabilitating the distribution network and increasing the Generation Capacity by implementing Kapichira Phase 2 that will add 64 megawatt, all of which will result in improved power supply reliability, reduced system losses and increased revenue.

29. Exchange rates and inflation

The average of the period end buying and selling rates of the currencies most affecting the performance of the company is stated below, together with the increase in the National Consumer Price Index for the preceding year, which represents an official measure of inflation.

	2011	**2010**
Kwacha/US Dollar	150.80	150.80
Kwacha/Rand	22.50	20.28
Kwacha/Euro	216.90	185.99
Inflation rate (%)	7.0	7.5

As at 10 October 2011, the exchange rates noted above had moved as follows:

Kwacha/US Dollar	166.18
Kwacha/Rand	20.94
Kwacha/Euro	222.43
Inflation rate as at August 2011 (%)	7.6