Future of Energy

Palestine Electric Company P.L.C

Annual Report 2018

Palestine Electric Company P.L.C
Gaza, Al Nusirat, Salah Al Din St., Power Plant, P.O.Box: 1336
Tel.: +970 8 2888600, Ext. No.: 331, Fax: +970 8 2888607
www.pec.ps info@pec.ps

Contents

1- Chairman's Message

Samer Khoury

Chairman of the Board of Directors

Dear Shareholders,

We are pleased to meet you again to review the Company's results for 2018. On behalf of myself and members of the Board of Directors we welcome all of our shareholders who invested in this Company. I would like to assure you all that we are proceeding forward with intensive efforts to maintain the performance and progress of the Company in light of the complex investment environment because we believe in the importance of contributing effectively to the Palestinian National economy and creating job opportunities for our people in the Gaza Strip.

In spite of the general political and economic circumstances, the Company has been able to enhance its financial and operational performance for the year 2018. It has achieved satisfactory returns that contributed to the growth of our shareholders' equity. This would not have been achieved without your trust and confidence in PEC, as one of the leading strategic and national investments.

In line with our national responsibility, we are always keen to protect the rights of our shareholders in this strategic project and provide full support to the executive management and our operational team to carry out their duties in the best possible manner.

We are in continuous contact with the Palestinian Government and Palestinian Energy and Natural Resources Authority (PENRA) in order to find the appropriate solutions to overcome all obstacles and execute the necessary plans to expand the power plant and use natural gas as a primary source of fuel. This will have a positive impact on all aspects financially and technically and greatly benefit our people in the Gaza Strip.

On behalf of myself and my colleagues in the Board of Directors, we extend our gratitude to our shareholders for their confidence and investment in the Company. I also extend my appreciation to the Executive Management and all the staff working in the Company for their dedication, commitment and hard work to maintain the Company's position and ensure it meets the future challenges.

Samer Khoury
Chairman of the Board of Directors

2- Executive Managing Director's Message

Walid Salman

Vice Chairman & Executive Managing Director

Dear Shareholders,

We are pleased to present the most important achievements of 2018. These results have been attained in line with the directives of the Board of Directors in regards to financial, technical and administrative issues while meeting our contractual obligations with all relevant parties.

The Company's performance for 2018 has confirmed and proven that we are continuing to achieve further growth and success to preserve our shareholders' rights. The Company has successfully achieved a profit of USD 8,786,981 which contributed to the growth of the shareholders' equity by 3.18%, demonstrating that we are moving in the right direction.

We have been able to collect part of the outstanding receivables due from PENRA. This enabled the Company to fulfill its financial obligations and carry out its duties effectively. We are working with all PNA related authorities to confirm their commitment to settle the monthly payments on a regular basis.

Our technical team, in cooperation with the German maintenance company (SIPA), have successfully completed the major maintenance work for two of the remaining gas turbines during 2018, despite of the current circumstances and obstacles. This has contributed to the improvement of the plant's performance achieving good efficiency and high productivity.

We emphasize the need to continue supplying the power plant with the required quantities of fuel in order to maintain our production of electricity, especially that the power plant is capable to operate in a proper manner and at full capacity. We will spare no effort in providing all our resources and expertise in order to find suitable and practical solutions to end the electricity problem in the Gaza Strip in full coordination and cooperation with the Palestinian Government and Palestinian Energy and Natural Resources Authority (PENRA).

Finally, we would like to thank the Board of Directors for their continued efforts in supporting this Company and the Executive Management in view of all the difficulties they encounter. We fully acknowledge and highly appreciate the sincere efforts of our professional staff in performing their duties and commitment to achieve the Company's mission and objectives.

Walid Salman

Vice Chairman & Executive Managing Director

3- Company Overview

Palestine Electric Company (PEC) was established in Gaza, Palestine in 1999 and is registered in accordance with the Companies' Law as a Public Shareholding Company with paid-in capital of 60 million US Dollars. PEC shares were listed in the Palestine Exchange in 2004, where 33% of its shares are owned by Public Shareholders and 67% owned by Founding Companies.

The main objectives of the Company are to establish electricity generating plants in the territories of the Palestinian National Authority (PNA) and to carry out all the operations necessary for the production and generation of electricity.

The Company established its subsidiary in Gaza under the name of "Gaza Power Generating Company (GPGC)", which has an exclusive right from PNA to generate electricity in the Gaza Strip.

4- Board of Directors

The Board of Directors consist of thirteen members representing all the shareholders. The Board of Directors main duties are to set the Companys' strategies, develop the business plans, follow up on the operational and action plans in accordance with economic and political circumstances, in addition to reviewing and approving budgets, policies and procedures.

No.	Name	Position	Representative	Address
1	Mr. Samer Khoury	Chairman	Palestine Power Company LLC	Gaza, Al Nusirat, Salah Al Din St., Power Plant, Tel. 2888600
2	Mr. Walid Salman	Vice Chairman		
3	Mr. Nabil Sarraf	Board Member		
4	Mr. Tarek Aggad	Board Member		
5	Mr. Talal Nasereddin	Board Member		
6	Mr. Hani Ali	Board Member		
7	Mr. Marwan Salloum	Board Member		
8	Mr. Basim Khouri	Board Member		
9	Mr. Sharhabeel Al Zaeem	Board Member		
10	Mr. Faisal Al Shawwa	Board Member		
11	Mr. Khaled Osaily	Board Member		
12	Mr. Majed Al-Helo	Board Member	Palestinian Pension Agency	Gaza, Al Remal, Thourah St., Tel. 2829219
13	Mr. Iyad Basal	Board Member	Public Shareholder	Gaza, Al Remal, Haifa St., Tel. 2848025

Board of Directors Meetings:

The Board of Directors hold periodic meetings to monitor and discuss the performance and achievements of the Company and take necessary actions and decisions as needed.

In 2018, the Board of Directors held the following meetings:

Meeting Date	Meeting Discussions
Feb 24, 2018	Discuss and review the latest technical, administrative and financial progress as well as the operation and maintenance process, in addition to setting the date of the General Assembly Meeting for 2017.
Mar 28, 2018	Discuss 2017 financial statements before the General Assembly Meeting, recommend the declaration and distribution of cash dividends of 10% of share par value.
Jul 16, 2018	Discuss the technical, administrative and financial performance for the second quarter of 2018, in addition to the operation and maintenance process and the strategic plan of the Company.
Dec 20, 2018	Discuss the financial performance and technical progress as well as the results of the major equipments maintenance by the German Company (SIPA).

Expected and suggested date of the upcoming General Assembly Meeting is Tuesday 9th April 2019.

Board of Directors Remuneration:

The Board of Directors have agreed, during their meeting on 28 March 2018 to pay the following remunerations to the board members for the year 2017:

Board Name	Members Number	Amount in USD
Palestine Power Company LLC	11	141,000
Public Shareholder - Palestinian Pension Agency	1	14,100
Public Shareholder - Individual	1	14,100
Total	**13**	**169,200**

5- Executive Management

Mr. Walid Salman	Vice Chairman of the Board of Directors Executive Managing Director
Dr. Rafiq Maliha	Power Plant General Manager
Mr. Mahmoud Nabahin	Financial and Compliance Manager

Our Employees:

Since its inception, the Company has created many job opportunities based on its operational needs. It has hired a team of experienced and qualified personnel to execute its work and strategic plans.

By end of 2018, the Company had 148 employees where the majority are professionals, with advanced qualifications and extensive experience including engineers, technicians, financials and commercials staff. The Company is also keen to provide the exceptional opportunity to integrate many of new graduates to join its training programs that enable them to gain good experience to enter the market.

Governance:

Since its inception, the Company has committed to a set of rules and decisions stipulated internally, either in the Memorandum of Association or in the Company's Bylaws as well as all related laws and regulations applicable in Palestine.

The Company has committed to apply the principle of transparency in presenting all required information in accordance with the disclosure requirements of the Palestine Exchange and all related regulations by the Palestine Capital Market Authority since its listing on the Palestine Exchange in 2004. To maintain the confidence of its shareholders, the Company has promoted the principles of transparency when presenting information and data to its shareholders allowing them to make the proper decisions for their investments.

The Board of Directors have adopted the principles of governance, including protecting the rights of shareholders and maintaining their interests, as well as protecting the rights of other stakeholders such as: creditors, suppliers and other related parties. Executive Management follow the best standards to maintain and develop the Company's assets and optimize the use of its resources which expected to achieve the best possible return on investment.

Legal Obligations:

PEC does not have any legal issues raised against third parties or raised by third parties.

External Auditors:

Following the voting of the last General Assembly Meeting held on 28 March 2018, Ernst & Young were appointed as the Company's external auditors for the year 2018.

Legal Advisor:

Al Zaeem & Associates - Attorneys at Law & Legal Consultants.



6- Technical Overview

Gaza Power Generating Company (GPGC) was established as the power plant's arm to fulfill the electricity needs of Gaza Strip, the power plant operates with a productive capacity reaching 140MW in a combined cycle system consisting of four gas turbines and two steam turbines to form two blocks for electricity generation. The Company ensures that the power plant is operated and maintained in an environmentally sensitive manner and in accordance with applicable OPIC requirements, World Bank guidelines and local Palestinian environmental requirements and policies.

In order to keep pace with the development and experience, our technical team has accomplished successfully significant achievements in 2018, which enhance the performance and efficiency of the power plant. Technical achievements can be summarized as follows:

- In addition to successful maintenance conducted during 2017 for the gas turbine units, our technical team have performed full major overhaul, "E" inspection, for the remaining gas turbine units (GT22, GT24) in cooperation with the German Company (SIPA). Accordingly all gas turbines are operational and fully maintained.

- Preparing plans for required maintenance for steam turbine units during 2019.
- Developing standard operating procedures and improve them effectively in accordance with the highest international quality standards.
- Developing the IT systems with full enhancement of all workflow quality control and quality assurance tools using latest technologies.
- Developing the preventive maintenance program in accordance to the latest international standards in this regard.
- Cooperating with local educational institutions to create an effective environment of creativity and innovation, through organizing practical training programs that allow students to acquire knowledge and experience of power plants.

As a result of Gaza closure and restrictions on movement, the Company still faces challenges that have significantly affected the implementation of some operations and maintenance plans and prevented the required spare parts from being delivered to repair the remaining damaged facilities. Efforts are underway to overcome obstacles and find appropriate solutions for rebuilding the main fuel tanks which were damaged during the last war on Gaza in 2014.

The power plant has the ability to work at full load capacity and efficiently if fuel is delivered in sufficient quantities.

The Company aims to maintain the continuity of electricity production with the highest possible efficiency and in accordance with a mechanism that preserves its rights and fulfils its obligations whilst allowing it to further maintain and develop its facilities.

7- Shareholders Structure

By the end of 2018, the shareholders base consisted of 10,770 shareholders, distributed as follows:

Shareholders Owning more than 5%:

Company Name	Number of Shares	Percentage
Palestine Power Company LLC	38,999,600	65%

Distribution based on Shareholders Type:

Shareholders Type	Number of Shareholders	Number of Shares	Percentage
Founding Companies	5	40,200,000	67%
Public Shareholders	10,765	19,800,000	33%
Total	**10,770**	**60,000,000**	**100%**

Distribution based on Shareholders Range:

Shareholders Type	Number of Shareholders	Number of Shares	Percentage
1 - 500	3,298	995,870	1.66%
501 - 1,000	4,981	3,602,489	6.00%
1,001 - 5,000	2,074	3,719,819	6.20%
5,001 - 10,000	201	1,438,320	2.40%
10,001 - 50,000	169	3,684,677	6.14%
50,001 - 100,000	24	1,648,091	2.75%
100,001 - 1,000,000	22	5,911,134	9.85%
1,000,001 and above	1	38,999,600	65.00%
Total	**10,770**	**60,000,000**	**100%**

8- Investor Relations

Palestine Electric Company is looking to achieve shareholders satisfaction by allocating all resources to manage the relations with its current shareholders and potential investors as well as the investment environment in Palestine.

In compliance with best practices and international standards, the Investor Relations department is managing the relations with Company shareholders, Palestine Exchange, Palestine Capital Market Authority and other related parties.

Our mechanism for dividends distribution is in line with the best practices and applicable regulations. The Company distribute dividends to all shareholders within announced distribution periods across bank branches in Palestine and abroad, while any uncollected dividends are kept in a reserve account to be paid to shareholders upon their request and as per procedures.

Information Mechanism:

The Company facilitate all efforts to communicate with its shareholders to keep them up to date of its activities and achievements. The Company provides various means of communication including telephone, website, e-mail, annual report, quarterly press releases and other media tools, where the shareholders can obtain the information about the Company or by visiting the Company's headquarters located in the Power Plant, Al Nusirat - Gaza Strip.

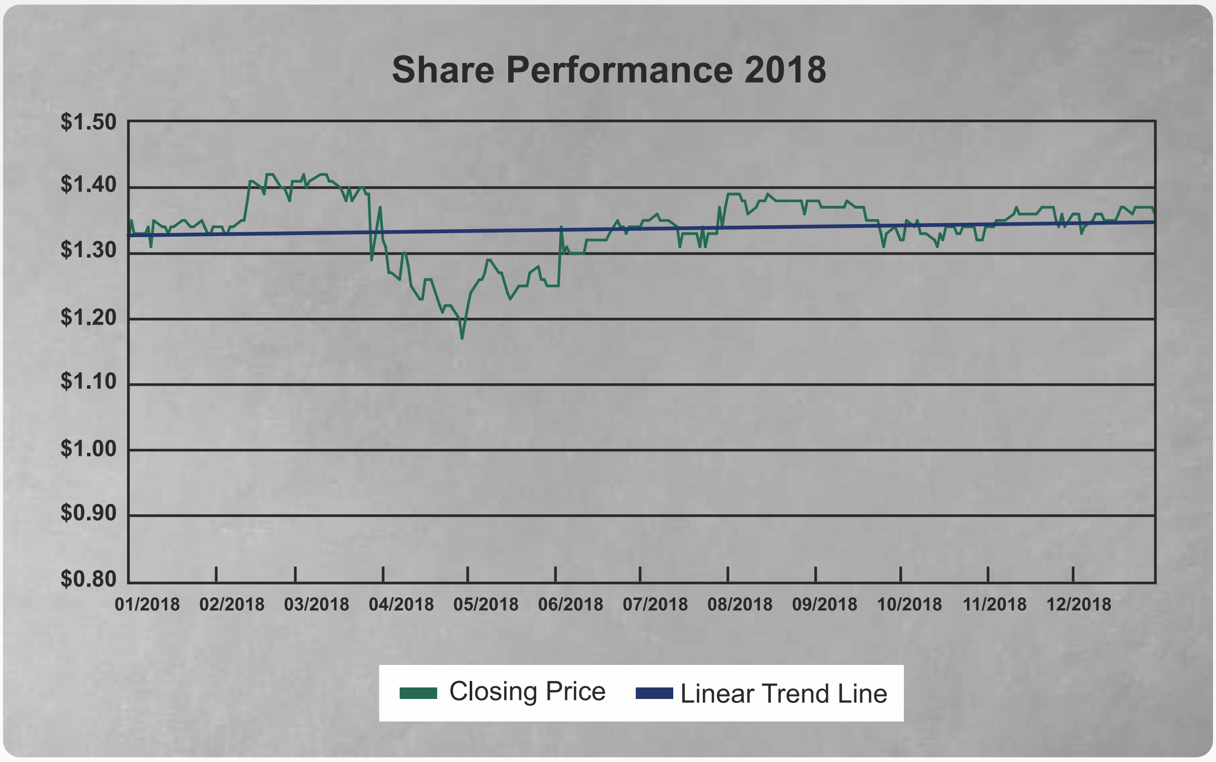
Financial Disclosures:

The Company is committed to disclose its financial statements through the quarterly review reports and its annual financial report distributed during its annual General Assembly Meetings. The financial statements are submitted to the Palestine Capital Market Authority and the Palestine Exchange pursuant to the regulations in Palestine. In addition, the annual report is published on the Company's website: www.pec.ps

9- Share Performance

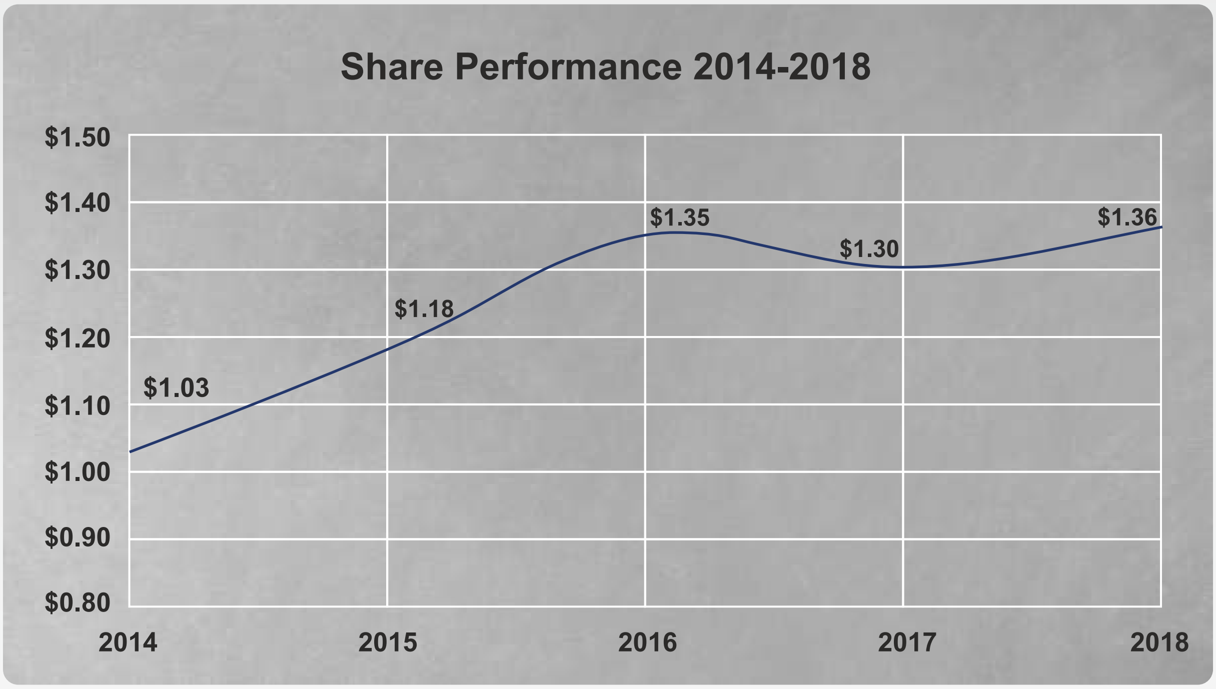
In 2018, PEC's share closed at $ 1.36 which is 4.6% higher than the closing price per share at the end of 2017. Despite political and economic instabilities, PEC's share was considered as one of the active share because of high trading volume in the Palestine Exchange, resulting from the confidence of our shareholders.

PEC's share was part of the traded shares in the first market of the Palestine Exchange. In accordance with the required conditions and standards, the Company's share was part of a selected sample group for statistical calculation of Al Quds Index in the Palestine Exchange.



PEC Share Price for Five Years:

PEC share was one of the trusted and demanded shares during the last 5 years. The share closed at $ 1.36 at the end of 2018 achieving an increase of around 32% compared to the closing price at the end of 2014.



Trading Information:

Details	2018	2017	2016	2015	2014
Trading Volume (shares)	2,878,884	5,978,428	2,451,536	1,375,518	1,003,779
Trading Value ($)	3,804,831	7,330,833	2,982,011	1,459,165	1,410,910
Number of Deals (deal)	2,038	2,750	1,786	1,154	977
Total Shares	60,000,000	60,000,000	60,000,000	60,000,000	60,000,000
Closing Price ($)	1.36	1.30	1.35	1.18	1.03
High Price ($)	1.42	1.44	1.39	1.21	1.63
Low Price ($)	1.16	1.05	1.09	0.93	1.03

Share Indicators:

Indicator	2018	2017	2016	2015	2014
Turnover Ratio (%)	4.80	9.96	4.09	2.29	1.67
Earnings Per Share ($)	0.15	0.14	(0.01)	0.23	0.03
Book Value Per Share ($)	1.51	1.46	1.42	1.53	1.30
Market to Book Value	0.90	0.89	0.95	0.77	0.79

Trading Volume:

In 2018, the number of traded shares were 2,878,884 shares with a total value of USD 3,804,831.

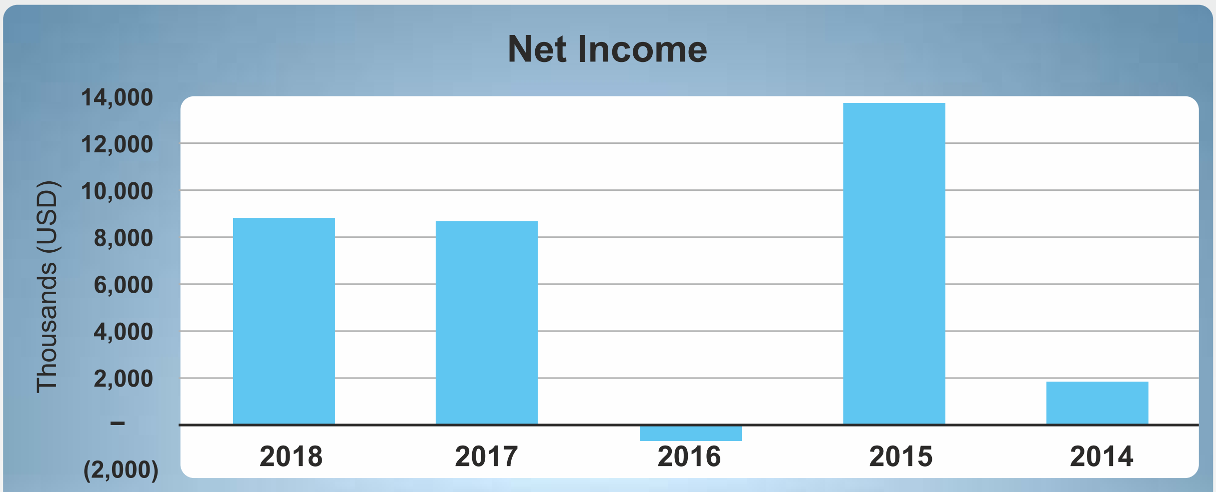
10- Social Responsibility

Based on our belief to participate in the community development and according to our understanding of Palestinian society needs, the Company is committed to social and humanitarian responsibilities towards various sectors of the society such as the marginalized, less fortunate social groups, special needs and the education sector.

The Company constantly strives to support these sectors, in addition to its active contribution to supporting seminars, conferences and meetings that help highlight vital issues, transfer and share knowledge and enable students and new graduates to gain an important experience.

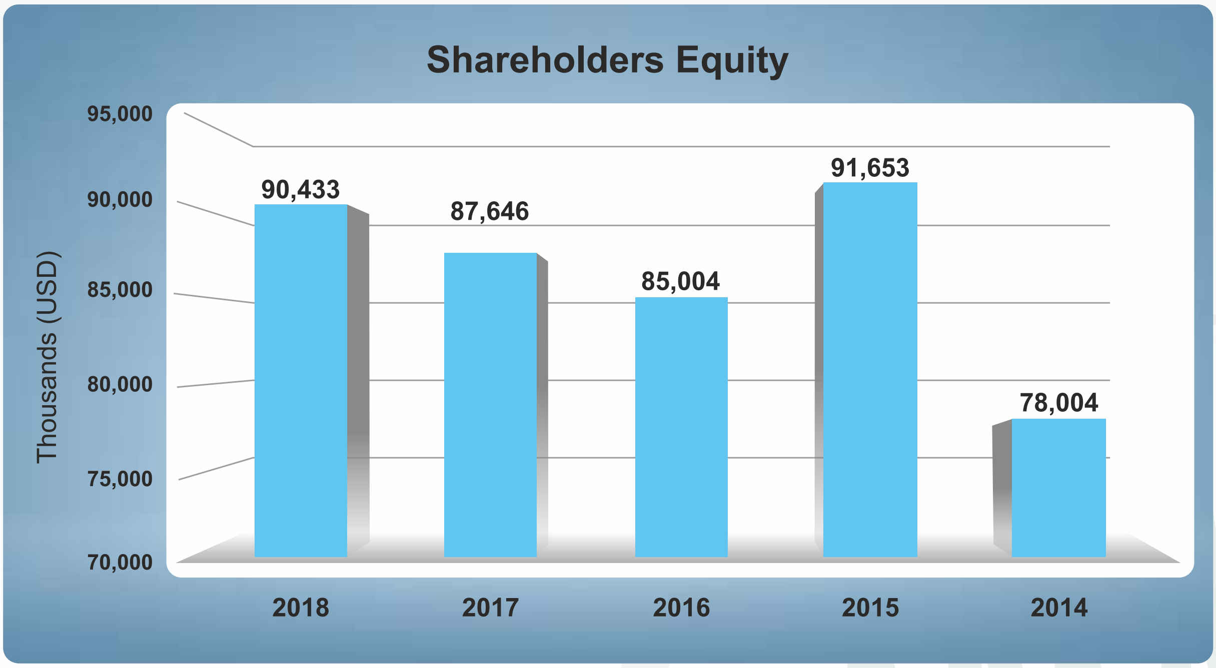
11- Financial Performance

The Company has achieved net profits of USD 8,786,981 in 2018 compared to USD 8,642,228 in 2017, reflecting a growth of 1.67%.



	2018	2017	2016	2015	2014
Net Income	8,786,981	8,642,228	(648,817)	13,648,366	1,884,873

As a result of 2018 performance, total shareholders' equity has increased by 3.18% to reach USD 90,432,978.



Financial Indicators:

Details	(Amounts in USD)				
	2018	2017	2016	2015	2014
Net Income (loss)	8,786,981	8,642,228	(648,817)	13,648,366	1,884,873
Shareholders' Equity	90,432,978	87,645,997	85,003,769	91,652,586	78,004,220
Closing Price per Share	1.36	1.30	1.35	1.18	1.03
Paid - In Capital	60,000,000	60,000,000	60,000,000	60,000,000	60,000,000
Market Value	81,600,000	78,000,000	81,000,000	70,800,000	61,800,000

Cash Dividends:

In order to maintain shareholders expectations, loyalty and confidence; the Board of Directors recommends to declare and distribute cash dividends based on annual financial performance. In 2018, the financial performance has improved regardless of the political and economic circumstances.

On March 28th 2018; the General Assembly had approved the recommendation of the Board of Directors to declare and distribute cash dividends for the year 2017 at a rate of 10% of original equity to all shareholders who hold shares at the date of the meeting.

Dividends	2018	2017	2016	2015	2014
Paid Dividends in USD	*	6,000,000	6,000,000	6,000,000	0
Percentage of Par Value	*	10%	10%	10%	0%

* To be decided by the General Assembly at the date of the meeting.

Differences between Preliminary & Audited Financial Statements:

There are no differences between the preliminary financial statements and the audited financial statements for 2018.

12- Audited Financial Statements

Palestine Electric Company, Public Shareholding Company

Consolidated Financial Statements

December 31, 2018

Ernst & Young
P.O. Box 1373
7th Floor,
PADICO House Bldg.
Al-Masyoun
Ramallah-Palestine

Tel: +972 22421011
Fax: +972 22422324
www.ey.com

INDEPENDENT AUDITOR'S REPORT
To the Shareholders of Palestine Electric Company, Public Shareholding Company

Opinion

We have audited the consolidated financial statements of Palestine Electric Company, Public Shareholding Company and its subsidiary (the Company), which comprise the consolidated statement of financial position as at December 31, 2018, and the consolidated statement of income and comprehensive income, consolidated statement of changes in equity and consolidated statement of cash flows for the year then ended, and notes to the consolidated financial statements, including a summary of significant accounting policies.

In our opinion, the accompanying consolidated financial statements present fairly, in all material respects, the consolidated financial position of the Company as at December 31, 2018, and its consolidated financial performance and its consolidated cash flows for the year then ended in accordance with International Financial Reporting Standards (IFRSs).

Basis for Opinion

We conducted our audit in accordance with International Standards on Auditing (ISAs). Our responsibilities under those standards are further described in the Auditor's Responsibilities for the Audit of the Consolidated Financial Statements section of our report. We are independent of the Company in accordance with the International Ethics Standards Board for Accountants' Code of Ethics for Professional Accountants (IESBA Code), and we have fulfilled our other ethical responsibilities in accordance with the IESBA Code. We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our opinion.

Emphasis of Matter – Credit risk

We draw attention to note (9) to the accompanying consolidated financial statements, the Company's subsidiary: Gaza Power Generating Company (GPGC) is currently exposed to credit risk as all of its revenues from the use of the power plant to generate electric capacity is generated from one customer, Palestinian Energy and Natural Resources Authority (PENRA). To the date of the financial statements, PENRA has not provided GPGC with the letter of credit of U.S. $ 20 million as required by the Power Purchase Agreement. Our opinion is not modified in respect of this matter.

Emphasis of Matter - Taxes

We draw attention to note (22) to the accompanying consolidated financial statements, according to the power purchases agreement between the Company's subsidiary: GPGC and Palestinian National Authority (PNA), PNA has agreed to exempt GPGC and its shareholders with respect to dividends and earnings from the subsidiaries, for the term of the agreement for 20 years including any extensions thereof, from all Palestinian taxes. As of the date of issuing these consolidated financial statements, neither the Company nor its subsidiary obtained a tax settlement from the tax authorities for the period from inception in 1999. Our opinion is not modified in respect of this matter.

Emphasis of Matter – Concentration of geographic risk

We draw attention to note (27) to the accompanying consolidated financial statements, non-current assets of the Company's subsidiary mainly comprise property, plant and equipment that are located in Gaza. Recoverability of these assets depends on political and economic stability in Gaza. Our opinion is not modified in respect of this matter.

Key Audit Matters

Key audit matters are those matters that, in our professional judgment, were of most significance in our audit of the consolidated financial statements as at December 31, 2018. These matters were addressed in the context of our audit of the consolidated financial statements as a whole, and in forming our opinion thereon, and we do not provide a separate opinion on these matters. For each matter below, our description of how our audit addressed the matter is provided in that context.

We have fulfilled the responsibilities described in the Auditor's Responsibilities for the Audit of the Consolidated Financial Statements section of our report, including in relation to these matters. Accordingly, our audit included the performance of procedures designed to respond to our assessment of the risks of material misstatement of the consolidated financial statements. The results of our audit procedures, including the procedures performed to address the matter below, provide the basis for our audit opinion on the accompanying consolidated financial statements.

Key audit matter	How our audit addressed the key audit matter
<u>PENRA's Account Receivable</u> As explain in note (9) to the accompanying consolidated financial statements, PENRA's account receivable as at December 31, 2018 and January 1, 2018 amounted to U.S. $ 34,606,387 and U.S. $ 29,355,806 and before Expected Credit Loss (ECL)/impairment allowance of U.S. $ 2,362,696 and U.S. $ 782,188, respectively. Because PENRA is the only customer of electricity generated from the power plant and due to the noncomplex nature of related receivables under IFRS 9, GPGC has applied the simplified approach for receivables as such receivables do not contain a significant financing component. The ECL model involves judgement and assumptions to reflect information about past events such as the age of the balance, history of disputes, historical payment patterns as well as current and expected future conditions, in addition to the amended power purchase agreement, for the purpose of estimating amounts and timing of future cash inflows discounted to their present values. Management assessed collectability of the balance based on the ECL model. This has not resulted in immaterial difference between previously reported carrying amounts under IAS 39 and the new carrying amounts under IFRS 9 as of January 1, 2018. The assessment also resulted in recording U.S. $ 1,580,508 as expected credit loss for the year 2018 in the consolidated statement of income and comprehensive income adding up the total ECL to U.S. $ 2,362,696.	Our audit procedures included the following: – Inquired management to understand sources of inputs and key assumptions used in ECL computation. – Assessed integrity and consistency of various inputs and assumptions used by GPGC to compute ECL. – Validated the exposure at default used in ECL calculation. – Performed procedures to assess the accuracy of the ECL calculation. – Obtained confirmation from PENRA supporting the existence and completeness of account receivable from PENRA. – Ensured the accuracy of disclosed facts in note (9) to the consolidated financial statements.

Other Information Included in the Company's 2018 Annual Report

Other information consists of the information included in the annual report, other than the consolidated financial statements and our auditor's report thereon. Management is responsible for the other information.

Our opinion on the consolidated financial statements does not cover the other information and we do not express any form of assurance conclusion thereon.

In connection with our audit of the consolidated financial statements, our responsibility is to read the other information and, in doing so, consider whether the other information is materially inconsistent with the consolidated financial statements or our knowledge obtained in the audit or otherwise appears to be materially misstated. If, based on the work we have performed, we conclude that there is a material misstatement of this other information; we are required to report that fact. We have nothing to report in this regard.

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

Management is responsible for the preparation and fair presentation of the consolidated financial statements in accordance with IFRSs, and for such internal control as management determines is necessary to enable the preparation of consolidated financial statements that are free from material misstatement, whether due to fraud or error.

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

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

Auditor's Responsibilities for the Audit of the Consolidated Financial Statements

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

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

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

- Obtain an understanding of internal control relevant to the audit in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Company's internal control.
- Evaluate the appropriateness of accounting policies used and the reasonableness of accounting estimates and related disclosures made by management.
- Conclude on the appropriateness of management's use of the going concern basis of accounting and, based on the audit evidence obtained, whether a material uncertainty exists related to events or conditions that may cast significant doubt on the Company's ability to continue as a going concern. If we conclude that a material uncertainty exists, we are required to draw attention in our auditor's report to the related disclosures in the consolidated financial statements or, if such disclosures are inadequate, to modify our opinion. Our conclusions are based on the audit evidence obtained up to the date of our auditor's report. However, future events or conditions may cause the Company to cease to continue as a going concern.
- Evaluate the overall presentation, structure and content of the consolidated financial statements, including the disclosures, and whether the consolidated financial statements represent the underlying transactions and events in a manner that achieves fair presentation.
- Obtain sufficient appropriate audit evidence regarding the financial information of the entities or business activities within the Company to express an opinion on the consolidated financial statements. We are responsible for the direction, supervision and performance of the group audit. We remain solely responsible for our audit opinion.

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

We also provide the Board of Directors with a statement that we have complied with relevant ethical requirements regarding independence, and to communicate with them all relationships and other matters that may reasonably be thought to bear on our independence, and where applicable, related safeguards.

From the matters communicated with the Board of Directors, we determine those matters that were of most significance in the audit of the consolidated financial statements as at December 31, 2018 and are therefore the key audit matters. We describe these matters in our auditor's report unless law or regulation precludes public disclosure about the matter or when, in extremely rare circumstances, we determine that a matter should not be communicated in our report because the adverse consequences of doing so would reasonably be expected to outweigh the public interest benefits of such communication.

Ernst & Young - Middle East
License # 206/2012

A. M. Abushaaban

Ernst + Young

A. Maher Abushaaban
License # 155/1998

March 17, 2019
Gaza - Palestine

CONSOLIDATED STATEMENT OF FINANCIAL POSITION
As at December 31, 2018

	Notes	2018 U. $. $	2017 U.S. $
ASSETS			
Non-current assets			
Property, plant and equipment	4	25,910,123	32,171,690
Intangible assets	5	1,193,962	1,415,545
Financial assets at fair value through comprehensive income	6	1,000,000	1,000,000
PENRA's account receivable - long term	9	-	4,112,634
Project in progress	7	-	249,372
		28,104,085	38,949,241
Current assets			
Materials and inventories	8	7,976,208	7,655,823
PENRA's account receivable – short term	9	32,243,691	24,460,984
Other current assets	10	18,153,111	3,230,903
Cash and cash equivalents	11	15,857,501	25,627,320
		74,230,511	60,975,030
TOTAL ASSETS		102,334,596	99,924,271
EQUITY AND LIABILITIES			
Equity			
Paid-in share capital	12	60,000,000	60,000,000
Statutory reserve	13	11,485,658	10,606,960
Retained earnings		18,947,320	17,039,037
Total equity		90,432,978	87,645,997
Non-current liabilities			
Provision for employees' indemnity	14	4,106,681	3,617,975
		4,106,681	3,617,975
Current liabilities			
Other current liabilities	15	7,794,937	8,660,299
		7,794,937	8,660,299
Total liabilities		11,901,618	12,278,274
TOTAL EQUITY AND LIABILITIES		102,334,596	99,924,271

The attached notes 1 to 28 form part of these consolidated financial statements

CONSOLIDATED STATEMENT OF INCOME AND COMPREHENSIVE INCOME
Year Ended December 31, 2018

	Notes	2018 U.S. $	2017 U.S. $
Revenues			
Capacity charges	16	32,011,680	31,681,200
Discounts on capacity charges' invoices	9	(1,800,000)	(1,800,000)
Operating expenses	17	(19,491,812)	(19,951,128)
		10,719,868	9,930,072
Expected credit loss	9	(1,580,508)	(782,188)
Finance costs		(671,257)	(721,920)
Other revenues, net	18	318,878	216,264
Profit for the year		8,786,981	8,642,228
Other comprehensive income		-	-
Total comprehensive income for the year		8,786,981	8,642,228
Basic and diluted earnings per share	19	0.15	0.14

The attached notes 1 to 28 form part of these consolidated financial statements

CONSOLIDATED STATEMENT OF CHANGES IN EQUITY
Year Ended December 31, 2018

	Paid-in Share Capital	Statutory Reserve	Retained Earnings	Total Equity
	U.S. $	U.S. $	U.S. $	U.S. $
2018				
Balance, beginning of the year	60,000,000	10,606,960	17,039,037	87,645,997
Total comprehensive income for the year	-	-	8,786,981	8,786,981
Transferred to statutory reserve	-	878,698	(878,698)	-
Dividends (note 20)	-	-	(6,000,000)	(6,000,000)
Balance, end of year	60,000,000	11,485,658	18,947,320	90,432,978
2017				
Balance, beginning of the year	60,000,000	9,742,737	15,261,032	85,003,769
Total comprehensive income for the year	-	-	8,642,228	8,642,228
Transferred to statutory reserve	-	864,223	(864,223)	-
Dividends (note 20)	-	-	(6,000,000)	(6,000,000)
Balance, end of year	60,000,000	10,606,960	17,039,037	87,645,997

CONSOLIDATED STATEMENT OF CASH FLOWS
Year Ended December 31, 2018

	Note	2018 U.S. $	2017 U.S. $
<u>Operating activities</u>			
Profit for the year		8,786,981	8,642,228
Adjustments:			
Provision for employees' indemnity		488,706	413,657
Depreciation of property, plant and equipment		6,296,135	6,305,893
Amortization		221,583	221,583
Expected credit loss		1,580,508	782,188
Impairment of project in progress		249,372	-
Finance costs		671,257	721,920
		18,294,542	17,087,469
Working capital adjustments:			
PENRA's account receivable		(5,250,581)	349,150
Other current assets		(14,922,208)	68,047
Materials and inventories		(320,385)	819,819
Other current liabilities		(534,835)	(42,113)
Employees' indemnity paid		-	(30,526)
Net cash flows (used in) from operating activities		(2,733,467)	18,251,846
<u>Investing activities</u>			
Purchase of property, plant and equipment		(34,568)	(24,217)
Available-for-sale investment		-	(250,000)
Net cash flows used in investing activities		(34,568)	(274,217)
<u>Financing activities</u>			
Loan repayments		-	(3,357,799)
Finance costs paid		(671,257)	(721,920)
Dividends paid		(6,330,527)	(5,606,062)
Net cash flows used in financing activities		(7,001,784)	(9,685,781)
(Decrease) Increase in cash and cash equivalents		(9,769,819)	8,291,848
Cash and cash equivalents, beginning of the year		25,627,320	17,335,472
Cash and cash equivalents, end of year	11	15,857,501	25,627,320

The attached notes 1 to 28 form part of these consolidated financial statements

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS
December 31, 2018

1. General

Palestine Electric Company (the Company), located in Gaza, was established on December 14, 1999, and is registered in accordance with the Companies' Law under a registration number (563200971) as Public Shareholding Company.

The main objectives of the Company are to establish electricity generating plants in the territories of the Palestinian National Authority (PNA) and to carry out all the operations necessary for the production and generation of electricity.

Gaza Power Generating Company (GPGC), being the Company's subsidiary, has an exclusive right from PNA to provide capacity and generate electricity in Gaza for the benefit of entities owned or controlled by the PNA for 20 years following commercial operation of its power plant which started on March 15, 2004 with an opportunity to extend the period of the agreement for up to two additional consecutive five-year periods.

The Company is considered a subsidiary of Palestine Power Company which owns 65 % of the Company's share capital. The financial statements of the Company are consolidated with the financial statements of Palestine Power Company.

The consolidated financial statements were authorized for issuance by the Company's Board of Directors on February 28, 2019.

2. Consolidated Financial Statements

The consolidated financial statements comprise the financial statements of the Company and its wholly owned subsidiary, GPGC, as at December 31, 2018. GPGC was established in Gaza in the year 1999 with an authorized share capital of 6,000,000 shares of U.S. $ 10 par value each.

3. Accounting Policies

3.1 Basis of preparation

The consolidated financial statements of the Company and its subsidiary have been prepared in accordance with International Financial Reporting Standards as issued by International Accounting Standard Board (IASB).

The consolidated financial statements have been presented in U.S. Dollar, which is the functional currency of the Company.

The consolidated financial statements have been prepared on a historical cost basis except for financial assets at fair value through other comprehensive income.

3.2 Basis of consolidation

The consolidated financial statements comprise the financial statements of the Company and its subsidiary as at December 31, 2018. Control is achieved when the Company is exposed, or has rights, to variable returns from its involvement with the investee and has the ability to affect those returns through its power over the investee. Specifically, the Company controls an investee if, and only if, the Company has:

- Power over the investee (i.e. existing rights that give it the current ability to direct the relevant activities of the investee)
- Exposure, or rights, to variable returns from its involvement with the investee
- The ability to use its power over the investee to affect its returns.

The Company re-assesses whether or not it controls investees if facts and circumstances indicate that there are changes to one or more of the three elements of control. Consolidation of a subsidiary begins when the Company obtains control over the subsidiary and ceases when the Company loses control of the subsidiary. Assets, liabilities, income and expenses of a subsidiary acquired or disposed of during the year are included in the consolidated financial statements from the date the Company gains control until the date the Company ceases to control the subsidiary.

All intra-company balances, transactions, unrealized gains and losses resulting from intra-company transactions and dividends are eliminated in full.

3.3 Changes in accounting policies

The accounting policies used in the preparation of the financial statements are consistent with those used in the preparation of the annual financial statements for the year ended December 31, 2017 except for the followings:

IFRS (9) Financial Instruments

IFRS (9) Financial Instruments replaces IAS (39) Financial Instruments: Recognition and Measurement for annual periods beginning on or after January 1, 2018, bringing together all three aspects of the accounting for financial instruments: classification and measurement; impairment; and hedge accounting.

IFRS (9) requires the Company to record an allowance for ECL for all debt instruments measured at amortized cost.

IFRS (9) replaces the 'incurred loss' model in IAS (39) Financial Instruments: Recognition and Measurement with a comprehensive model of recognition and recording of 'expected credit loss' (ECL), scope of hedge accounting, and classification requirement. The accounting policies related to IFRS (9) explained in "Summary of significant accounting policies (note 3.5)

Effect of applying IFRS (9) Financial Instruments

Classification and measurement

The following schedule shows measurement of financial assets in accordance with IAS (39) and the current measurement of financial assets in accordance with IFRS (9) as of January 1, 2018:

	Measurement category		Value	
Financial assets	IAS (39)	IFRS (9)	IAS (39)	IFRS (9)
			U.S. $	
			2018	2017
Investment in shares	Available-for-sale investments	Financial assets at fair value through comprehensive income	1,000,000	1,000,000

Impairment

The adoption of IFRS (9) has fundamentally changed the Company's accounting for impairment losses for financial assets by replacing IAS (39) incurred loss approach with a forward-looking expected credit loss (ECL) approach.

For all debt instruments, the Company has applied the simplified approach and has calculated ECL based on lifetime expected credit losses.

The adoption of IFRS (9) did not have an impact on the Company's consolidated financial statements.

IFRS (7) Financial Instruments – Amendments on Disclosure

IFRS (7) was amended to include more qualitative and quantitative disclosures to accommodate IFRS (9) requirements such as classifications, impairment and hedge accounting.

IFRS (15) Revenue from Contracts with Customers

IFRS (15) supersedes IAS (11) Construction Contracts, IAS (18) Revenue and related Interpretations and it applies to all revenue arising from contracts with customers, unless those contracts are in the scope of other standards. The new standard establishes a five-step model to account for revenue arising from contracts with customers. Under IFRS (15), revenue is recognised at an amount that reflects the consideration to which an entity expects to be entitled in exchange for transferring goods or services to a customer.

The standard requires entities to exercise judgement, taking into consideration all of the relevant facts and circumstances when applying each step of the model to contracts with their customers. The standard also specifies the accounting for the incremental costs of obtaining a contract and the costs directly related to fulfilling a contract. The Company applies IFRIC (4) which relates to arrangements that do not take the legal form of a lease but convey the right to use an asset in return for a payment or a series of payments. An arrangement conveys the right to use the asset if the arrangement conveys to the purchaser (lessee) the right to control the use of the underlying asset which resulted a capacity charge revenues from the use of the power plant are recognized during the period in which electricity is available according to the power purchase agreement signed with PENRA. This results in revenue recognition approximating the straight-line requirements of IAS (17) on leases. Therefore, the adoption of IFRS (15) did not have an impact on revenue recognition.

Standards issued but not effective

The standards and interpretations that are issued but not yet effective, up to the date of issuance of the Company's financial statements are disclosed below. The Company intends to adopt these standards, if applicable, when they become effective.

IFRS (16) Leases

During January 2016, the IASB issued IFRS (16) "Leases" which sets out the principles for the recognition, measurement, presentation and disclosure of leases.

IFRS (16) substantially carries forward the lessor accounting requirements in IAS (17). Accordingly, a lessor continues to classify its leases as operating leases or finance leases, and to account for those two types of leases differently.

IFRS (16) introduced a single lessee accounting model and requires a lessee to recognize assets and liabilities for all leases with a term of more than 12 months, unless the underlying asset is of low value. A lessee is required to recognize a right-of-use asset representing its right to use the underlying leased asset and a lease liability representing its obligation to make lease payments.

Transition to IFRS (16)

The Company has the option to adopt IFRS (16) retrospectively and restate each prior reporting period presented or using the modified retrospective approach by applying the impact as an adjustment on the opening retained earnings. The Company will elect to apply the standard to contracts that were previously identified as leases applying IAS (17) and IFRIC (4).

The Company will adopt IFRS (16) starting January 1, 2019, and due to the lack of sufficient information to disclose the quantitative impact of IFRS (16) as at December 31, 2018, the impact of IFRS (16) will not be disclosed in the consolidated financial statements for the year ended December 31, 2018. It is expected that application of IFRS (16) will resulted an increase in assets (right to use) and liabilities (lease commitments).

IFRIC Interpretation (23) Uncertainty over Income Tax Treatment

The Interpretation addresses the accounting for income taxes when tax treatments involve uncertainty that affects the application of IAS (12) and does not apply to taxes or levies outside the scope of IAS (12), nor does it specifically include requirements relating to interest and penalties associated with uncertain tax treatments. An entity must determine whether to consider each uncertain tax treatment separately or together with one or more other uncertain tax treatments.

The interpretation is effective for annual reporting periods beginning on or after 1January 2019, but certain transition reliefs are available.

3.4 Estimates and assumptions

The preparation of the consolidated financial statements in conformity with IFRS requires the use of accounting estimates and assumptions. It also requires management to exercise its judgment in the process of applying the Company's accounting policies. The Company's management continually evaluates its estimates, assumptions and judgments based on available information and experience. As the use of estimates is inherent in financial reporting, actual results could differ from these estimates.

Following are the significant estimates made by management:

Useful lives of tangible and intangible assets

The Company's management reassesses the useful lives of tangible and intangible assets, and makes adjustments if applicable, at each financial year end.

Impairment of financial assets (Expected Credit Loss "ECL")

Financial assets are evaluated for impairment on the basis set out in "Impairment of financial assets" paragraph.

In determining impairment of financial assets, the Company uses judgement to estimate the amount and timing of future cash flows as well as an assessment of whether the credit risk on the financial asset has increased significantly since initial recognition and incorporation of forward-looking information in the measurement of expected credit losses.

Fair value of financial instruments

Where the fair value of financial assets and financial liabilities recorded in the consolidated statement of financial position cannot be derived from active markets, they are determined using appropriate valuation techniques including the discounted cash flows model. The inputs to these models are taken from observable markets where possible, but where this is not feasible, a degree of judgment is required in establishing fair values. Judgments include considerations of inputs such as liquidity risk, credit risk and volatility. Changes in assumptions about these factors could affect the reported fair value of financial instruments.

The Company's management believes that the estimates and assumptions used are reasonable.

3.5 Summary of significant accounting policies

Revenue recognition

Revenue is recognized to the extent that it is probable that the economic benefits will flow to the Company and the revenue can be reliably measured. The following specific recognition criteria must also be met before revenue is recognized:

Capacity charges
Capacity charge revenues from the use of the power plant are recognized during the period in which electricity is available according to the power purchase agreement signed with PENRA. This results in revenue recognition approximating the straight-line requirements of IAS (17) on leases as the Company applies IFRIC (4) which relates to arrangements that do not take the legal form of a lease but convey the right to use an asset in return for a payment or a series of payments. An arrangement conveys the right to use the asset if the arrangement conveys to the purchaser (lessee) the right to control the use of the underlying asset. The right to control the use of the underlying asset is conveyed if any one of the following conditions is met:

- The purchaser has the ability or right to operate the asset or direct others to operate the asset in a manner it determines while obtaining or controlling more than an insignificant amount of the output or other utility of the asset.
- The purchaser has the ability or right to control physical access to the underlying asset while obtaining or controlling more than an insignificant amount of the output or other utility of the asset.
- Facts and circumstances indicate that it is remote that one or more parties other than the purchaser will take more than an insignificant amount of the output or other utility that will be produced or generated by the asset during the term of the arrangement, and the price that the purchaser will pay for the output is neither contractually fixed per unit of output nor equal to the current market price per unit of output as of the time of delivery of the output.

As the Palestinian Energy and Natural Resources Authority (PENRA) is the sole purchaser of the electricity generated from power plant at a price other than at market price and the price varies other than in response to market price changes, this variability is regarded by IFRIC (4) as capacity payments being made for the right to use the power plant. Hence, such arrangement is accounted for in accordance with IAS (17) on leases. The power purchase agreement does not transfer substantially all the risks and rewards incidental to the Company's ownership of the power plant to PENRA. Therefore, the Company considered the arrangement of the power plant agreement as an operating lease and electrical capacity charges from the use of power plant to generate electricity as rental payment.

Interest revenues
Interest revenue is recognized as interest accrues using the effective interest method using the rate that exactly discounts estimated future cash receipts through the expected life of the financial instrument to the net carrying amount of the financial asset.

Expense recognition

Expenses are recognized when incurred in accordance with the accrual basis of accounting.

Finance costs

Finance costs directly attributable to the acquisition, construction or production of an asset that necessarily takes a substantial period of time to get ready for its intended use are capitalized as part of the cost of the asset. All other finance costs are expensed in the period in which they occur. Finance costs consist of interest and other costs that an entity incurs in connection with the borrowing of funds.

Property, plant and equipment

Property, plant and equipment are stated at cost, net of accumulated depreciation and/or accumulated impairment losses, if any. Such cost includes the cost of replacing part of the property, plant and equipment and borrowing costs for long-term construction projects if the recognition criteria are met. All other repair and maintenance costs are recognized in the consolidated statement of income and comprehensive income as incurred. Depreciation is calculated on a straight line basis over the estimated useful lives of the assets as follows:

	Useful lives (Years)
Power plant	20
Buildings	20
Motor vehicles	5
Computers and printers	4
Office equipment	4
Furniture and fixture	5

Any item of property, plant, and equipment and any significant part initially recognized is derecognized upon disposal or when no future economic benefits are expected from its use or disposal. Any gain or loss arising on derecognition of the asset (calculated as the difference between the net disposal proceeds and the carrying amount of the asset) is included in the consolidated statement of income and comprehensive income when the asset is derecognized.

The property, plant and equipment residual values, useful lives and methods of depreciation are reviewed at each financial year-end and adjusted prospectively, if appropriate.

Project in progress

Project in progress comprises development and design costs, construction costs, direct wages, borrowing costs and a portion of the indirect costs. After completion, project in progress is transferred to property, plant and equipment.

The carrying value of the project in progress is reviewed for impairment when events or changes in circumstances indicate that the carrying value may not be recoverable. If any such indication exists and where the carrying values exceed the estimated recoverable amount, the project is written down to its recoverable amount.

Intangible assets

Intangible assets acquired through government grant and assistance are initially measured at fair value. Following initial recognition, intangible assets are carried net of any accumulated amortization and any accumulated impairment losses.

Intangible assets with finite lives are amortized over the useful economic life and assessed for impairment whenever there is an indication that the intangible asset may be impaired. The amortization period and the amortization method for an intangible asset with a finite useful life is reviewed at least each financial year-end. Changes in the expected useful life or the expected pattern of consumption of future economic benefits embodied in the asset is accounted for by changing the amortization period or method, as appropriate, and treated as changes in accounting estimates. The amortization expense on intangible assets with finite lives is recognized in the consolidated statement of income and comprehensive income in the expense category consistent with the function of the intangible asset.

Right to use PENRA's transformers

Right to use PENRA's transformers is amortized using the straight-line method over a period that equals the remaining useful life of the Power Plant at the time of acquiring the right. Amortization expense is recognized in the consolidated statement of income and comprehensive income.

Current versus non-current classification

The Company presents assets and liabilities in consolidated statement of financial position based on current/non-current classification. An asset as current when it is:

- Expected to be realized or intended to be sold or consumed in normal operating cycle
- Held primarily for the purpose of trading
- Expected to be realized within twelve months after the reporting period
- Cash or cash equivalents unless restricted from being exchanged or used to settle a liability for at least twelve months after the reporting period.

All other assets are classified as non-current.

A liability is current when:

- It is expected to be settled in normal operating cycle
- It is held primarily for the purpose of trading
- It is due to be settled within twelve months after the reporting period
- There is no unconditional right to defer the settlement of the liability for at least twelve months after the reporting period.

The Company classifies all other liabilities as non-current.

Materials and inventories

Materials and inventories are stated at the lower of cost using the weighted average method or net realizable value. Costs are those amounts incurred in bringing each item of materials and inventories to its present location and condition.

Accounts receivable

Accounts receivable are stated at original invoice amount less an allowance for expected credit loss for any impaired amounts. An estimate for impaired accounts receivable is made when collection of the full amount is no longer probable. Bad debts are written off when there is no possibility of recovery.

Accounting policies related to IFRS (9)

After adoption of IFRS (9) as at January 1, 2018:

Classification of financial assets

<u>Financial assets at fair value through other comprehensive income (FVOCI)</u>

At initial recognition, the Company makes an irrevocable election (on an instrument-by-instrument basis) to designate investments in equity instruments as at FVOCI. Designation at FVOCI is not permitted if the equity investment is held for trading.

Equity instruments at FVOCI are initially measured at fair value plus transaction costs. Subsequently, they are measured at fair value with gains and losses arising from changes in fair value recognized in other comprehensive income and accumulated in the fair value reserve. Where the asset is disposed of, the cumulative gain or loss previously accumulated in the fair value reserve is not reclassified to the consolidated income statement, but is reclassified to retained earnings. In limited circumstances, cost may be an appropriate estimate of fair value.

Dividends on these investments in equity instruments are recognized in the consolidated income statement when the Company's right to receive the dividends is established, unless the dividends clearly represent a recovery of part of the cost of the investment.

Financial assets at amortized cost

Debt instruments are measured at amortized cost if both of the following conditions are met:

- The asset is held within a business model whose objective is to hold assets in order to collect contractual cash flows; and
- The contractual terms of the instrument give rise on specified dates to cash flows that are solely payments of principal and interest on the principal amount outstanding.

Debt instruments meeting these criteria are measured initially at fair value plus transaction costs (except if they are designated as at financial assets at fair value through profit or loss (FVTPL). They are subsequently measured at amortized cost using the effective interest method less any impairment, with interest revenue recognized on an effective yield basis.

Effective interest rate is the interest rate used to discount the future cash flows over the debt instrument life (or a shorter period in certain cases), in order to match its carrying value at the date of initial recognition.

The Company may irrevocably elect at initial recognition to classify a debt instrument that meets the amortized cost criteria above as at FVTPL if that designation eliminates or significantly reduces an accounting mismatch had the financial asset been measured at amortized cost.

Impairment of financial assets

After adoption of IFRS (9) as at January 1, 2018, impairment allowances for expected credit losses (ECL) are recognized for financial instruments that are not measured at FVTPL. No impairment loss is recognized on equity investments.

An ECL provision is made at an amount equal to the lifetime ECL, except for the following, for which they are measured as a12-month ECL:

- Debt investment securities that are determined to have a low credit risk (equivalent to investment grade rating) at the reporting date; and
- Other financial instruments for which the credit risk has not increased significantly since their initial recognition.

The Company has applied the simplified approach and has calculated ECL based on lifetime expected credit losses on accounts receivable. To evaluation of expected credit loss, account receivable classified based on the characteristics of the credit risk and the maturity date.

An impairment allowances for expected credit losses (ECL) are recognised in the consolidated statement of income and comprehensive income and are reflected in an allowance account against accounts receivables.

Financial assets are written off after all restructuring and collection activities have taken place and there is no realistic prospect of recovery. Subsequent recoveries are included in other income.

Financial assets that are measured at amortised cost are tested as to whether they are credit-impaired. Objective evidence that a financial asset is credit-impaired may include a breach of contract, such as default or delinquency in interest or principal payments, the granting of a concession that, for economic or legal reasons relating to the borrower's financial difficulties.

Financial assets which have been re-scheduled or modified are no longer considered to be past due and are replaced on performing status when all principal and interest payments are up to date and future payments are reasonably assured. Financial assets subject to individual impairment assessment and whose terms have been re-scheduled, are subject to on- going review to determine whether they remain impaired.

Before early adoption of IFRS (9) as at January 1, 2018

Classification of financial assets

<u>Available-for-sale investments</u>

Available-for-sale investments include equity and debt securities. Equity investments classified as available-for-sale are those, which are not designated at fair value through profit or loss. Debt securities in this category are those which are intended to be held for an indefinite period of time and which may be sold in response to needs for liquidity or in response to changes in the market conditions.

After initial measurement, available-for-sale investments are subsequently measured at fair value with unrealized gains or losses recognized as other comprehensive income in the available-for-sale reserve until the investment is derecognized, at which time the cumulative gain or loss is recognized in the consolidated income statement, or determined to be impaired, at which time the cumulative loss is reclassified to the consolidated income statement and removed from the available-for-sale reserve, which is in turn reduced by the amount of the impairment.

The Company evaluates whether the ability and intention to sell its available-for-sale financial assets in the near term is still appropriate. When, in rare circumstances, PIF is unable to trade these financial assets due to inactive markets, PIF may elect to reclassify these financial assets into another category depending on the nature of the financial asset.

Available-for-sale investments are stated at cost when their fair value cannot be reliably determined due to the unpredictable nature of future cash flows.

<u>Loans and receivables</u>

Loans and receivables are non-derivative financial assets with fixed or determinable payments that are not quoted in an active market. After initial measurement, such financial assets are subsequently measured at amortized cost using the effective interest rate (EIR) method, less impairment. Amortized cost is calculated by taking into account any discount or premium on acquisition and fees or costs that are an integral part of the EIR.

Impairment of financial assets

An assessment is made at each reporting date whether there is any objective evidence that a financial asset or a group of financial assets is impaired. If such evidence exists, any impairment loss is recognized in the consolidated statement of income and comprehensive income.

For assets carried at amortized cost: impairment is the difference between carrying amount and the present value of future cash flows discounted at the original effective interest rate;

Equity investments classified as available-for-sale: objective evidence would include a significant or prolonged decline in the fair value of the investment below its cost. 'Significant' is evaluated against the original cost of the investment and 'prolonged' against the period in which the fair value has been below its original cost. Impairment is the difference between the acquisition cost and the current fair value, less any impairment loss on that investment previously recognized in the consolidated income statement.

Impairment losses on equity investments are not reversed through the statement of income and comprehensive income; increases in their fair value after impairment are recognized directly in other comprehensive income;

Debt instruments classified as available-for-sale: impairment is the difference between the amortized cost and the current fair value, less any impairment loss on that investment previously recognized in the consolidated income statement.

Fair value measurement

Fair value 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. The fair value measurement is based on the presumption that the transaction to sell the asset or transfer the liability takes place either:

- In the principal market for the asset or liability, or
- In the absence of a principal market, in the most advantageous market for the asset or liability

The principal or the most advantageous market must be accessible to by the Company.

A fair value measurement of a non-financial asset takes into account a market participant's ability to generate economic benefits by using the asset in its highest and best use or by selling it to another market participant that would use the asset in its highest and best use.

The Company uses valuation techniques that are appropriate in the circumstances and for which sufficient data are available to measure fair value, maximizing the use of relevant observable inputs and minimizing the use of unobservable inputs.

All assets and liabilities for which fair value is measured or disclosed in the consolidated financial statements are categorized within the fair value hierarchy, described as follows:

Level 1 — Quoted (unadjusted) market prices in active markets

Level 2 — Valuation techniques for which the lowest level input that is significant to the fair value measurement is directly or indirectly observable

Level 3 — Valuation techniques for which the lowest level input that is significant to the fair value measurement is unobservable

For the purpose of fair value disclosures, the Company has determined classes of assets and liabilities on the basis of the nature, characteristics and risks of the asset or liability and the level of the fair value hierarchy as explained above.

Cash and cash equivalents

For the purpose of the statement of cash flows, cash and cash equivalents consist of cash on hand, bank balances, and short-term deposits with an original maturity of three months or less net of restricted bank balances.

Accounts payable and accruals

Liabilities are recognized for amounts to be paid in the future for goods or services received, whether billed by the supplier or not.

Provisions

Provisions are recognized when the Company has a present obligation (legal or constructive) as a result of a past event, it is probable that an outflow of resources embodying economic benefits will be required to settle the obligation, and a reliable estimate can be made of the amount of the obligation.

Foreign currency

Transactions in foreign currencies are recorded at the rate ruling at the date of the transaction. Monetary assets and liabilities denominated in foreign currencies are translated at the rate of exchange ruling at the consolidated financial statements date. All differences are recognized to the consolidated statement of income and comprehensive income.

Earnings per share

Basic earnings per share is calculated by dividing profit for the year attributable to ordinary equity holders of the parent by the weighted average number of ordinary shares outstanding during the year.

Diluted earnings per share is calculated by dividing the profit attributable to ordinary equity holders of the parent (after adjusting for interest on the convertible preference shares) by the weighted average number of ordinary shares outstanding during the year plus the weighted average number of ordinary shares that would be issued on the conversion of all the dilutive potential ordinary shares into ordinary shares.

4. Property, Plant and Equipment

2018	Power plant U.S. $	Buildings U.S. $	Motor vehicles U.S. $	Computers and printers U.S. $	Office equipment U.S. $	Furniture and fixture U.S. $	Total U.S. $
Cost:							
Balance, beginning of the year	123,579,669	1,464,904	451,192	406,825	186,148	244,636	126,333,374
Additions	-	-	-	27,123	6,656	789	34,568
Balance, end of year	123,579,669	1,464,904	451,192	433,948	192,804	245,425	126,367,942
Accumulated depreciation:							
Balance, beginning of the year	92,018,027	924,135	451,192	374,411	169,791	224,128	94,161,684
Depreciation charges for the year	6,181,497	73,248	-	16,515	15,789	9,086	6,296,135
Balance, end of year	98,199,524	997,383	451,192	390,926	185,580	233,214	100,457,819
Net carrying amount:							
At December 31, 2018	25,380,145	467,521	-	43,022	7,224	12,211	25,910,123

2017	Power plant U.S. $	Buildings U.S. $	Motor vehicles U.S. $	Computers and printers U.S. $	Office equipment U.S. $	Furniture and fixture U.S. $	Total U.S. $
Cost:							
Balance, beginning of the year	123,579,669	1,464,904	451,192	388,490	186,148	238,754	126,309,157
Additions	-	-	-	18,335	-	5,882	24,217
Balance, end of year	123,579,669	1,464,904	451,192	406,825	186,148	244,636	126,333,374
Accumulated depreciation:							
Balance, beginning of the year	85,836,530	850,887	438,780	358,658	155,619	215,317	87,855,791
Depreciation charges for the year	6,181,497	73,248	12,412	15,753	14,172	8,811	6,305,893
Balance, end of year	92,018,027	924,135	451,192	374,411	169,791	224,128	94,161,684
Net carrying amount:							
At December 31, 2017	31,561,642	540,769	-	32,414	16,357	20,508	32,171,690

Property, plant and equipment include U.S. $ 1,226,550 and U.S. $ 1,145,811 of fully depreciated assets as at December 31, 2018 and 2017, respectively, which are still used in the Company's operations.

5. Intangible Assets

	2018	2017
	U.S. $	U.S. $
Balance, beginning of the year	1,415,545	1,637,128
Amortization	(221,583)	(221,583)
Balance, end of year	1,193,962	1,415,545

Intangible assets represent the right to use six step-up transformers installed by PENRA for the use of GPGC as part of the agreement signed on September 2, 2006 between GPGC and PENRA. According to the agreement, PENRA agreed to rectify all damages within the power plant resulted from the Israeli air strike during June 2006 to restore the power supply from the power plant. These transformers will be owned by PENRA; and GPGC will have the right to use such transformers and will be responsible for their operation and maintenance. The right to use the transformers was initially recognized at the fair value of the transformers when installed. The right to use the transformers is amortized over the remaining useful life of the power plant starting from the date of obtaining such right.

6. Financial Assets at Fair Value Through Comprehensive Income

Financial assets at fair value through comprehensive income (2017: Available-for-sale investments) represents the Company's investment in the shares capital of Palestine Power Generating Company (PPGC) in the amount of U.S. $ 1,000,000.

7. Project in Progress

Movement on the project in progress was as follows:

	2018	2017
	U.S. $	U.S. $
Balance, beginning of the year	249,372	249,372
Impairment of project in progress	(249,372)	-
Balance, end of year	-	249,372

8. Materials and Inventories

	2018	2017
	U.S. $	U.S. $
Spare parts	7,191,325	6,713,705
Consumables	321,945	280,043
Goods in transit	445,817	553,894
Others	17,121	108,181
	7,976,208	7,655,823

9. PENRA's Account Receivable

	2018	2017
	U.S. $	U.S. $
Receivable from capacity charges	34,606,387	29,355,806
Allowance for expected credit losses	(2,362,696)	(782,188)
	32,243,691	28,573,618
Current portion	(32,243,691)	(24,460,984)
Noncurrent portion	-	4,112,634

Movement on allowance for expected credit loss was as follows:

	2018	2017
	U.S. $	U.S. $
Balance, beginning of the year	782,188	-
Allowance for expected credit loss	1,580,508	782,188
Balance, end of year	2,362,696	782,188

On November 7, 2016, GPGC, together with PENRA and the Palestinian Ministry of Finance and Planning signed an amendment to the power purchase agreement. The amendment included commitment from PENRA to make monthly payments toward settling account receivable balance, in addition GPGC granted PENRA a monthly discount of U.S. $ 150,000 from the monthly capacity charge invoice starting from December 1, 2016 and presented as deductions from the monthly capacity charge invoices.

All GPGC's capacity charges revenue from the use of power plant is generated from one customer, PENRA. According to the power purchase agreement, PENRA is required to provide GPGC with a letter of credit of U.S. $ 20 million from a qualified bank as defined in the agreement. To the date of these consolidated financial statements, PENRA did not provide GPGC with the letter of credit; therefore, accounts receivable are unsecured.

10. Other Current Assets

	2018	2017
	U.S. $	U.S. $
Value Added Tax receivable	138,389	276,312
Due from shareholders	16,268,033	1,494,146
Prepaid insurance	652,723	743,431
Advances to suppliers	839,389	631,850
Others	254,577	85,164
	18,153,111	3,230,903

11. Cash and Cash Equivalents

	2018	2017
	U.S. $	U.S. $
Cash on hand	6,363	5,355
Current accounts at banks	5,851,138	5,621,965
Short-term deposit	10,000,000	20,000,000
	15,857,501	25,627,320

Short-term deposit represents U.S. Dollar deposit held with a local bank and due within 1 month after the consolidated financial statements date. The average interest rates for deposit was 4%.

12. Paid-in Share Capital

The share capital of the Company comprises 60,000,000 ordinary shares at par value of U.S. $ 1 for each share.

13. Statutory Reserve

The amount represents cumulative transfers of 10% of profits to statutory reserve in accordance with the Companies' Law. The reserve shall not be distributed to shareholders.

14. Provision for Employees' Indemnity

Movement on the provision for employees' end of service indemnity during the year was as follows:

	2018	2017
	U.S. $	U.S. $
Balance, beginning of the year	3,617,975	3,234,844
Additions	488,706	413,657
Payments	-	(30,526)
Balance, end of year	4,106,681	3,617,975

Provision for employees' indemnity is calculated in accordance with the labor law prevailing in Palestine, and the Company internal policies. The Palestinian Social Security Law was expected to go into effect during 2018. However, according to the presidential decree on January 28, 2019, the law implementation was paused and the decree called for dialogue among relevant parties for the purpose of reaching national consensus on the law and the time on which it will become effective. The current version of the law obligates the employer to settle end of service benefits for the periods preceding the application of the provisions of this law.

15. Other Current Liabilities

	2018	2017
	U.S. $	U.S. $
Dividends payable	2,623,683	2,954,210
Maintenance payable and provisions	3,433,902	3,433,902
Due to Consolidated Contractors Company	672,057	375,152
Accrued expenses	267,814	273,765
Land's lease *	-	882,000
Provision for employees' vacations	319,432	294,924
Payroll tax	185,653	71,938
Others	292,396	374,408
	7,794,937	8,660,299

* Accrued land's lease liability was settled through PENRA's account receivable.

16. Capacity Charges

The amount represents revenues from capacity charges invoices issued by GPGC for the use of power plant to generate electric capacity for the benefit of PENRA according to the power purchase agreement, which is considered an operating lease under IFRIC (4) as further explained in accounting policies note (3.5) after deducting U.S. $ 150,000, monthly starting from December 1, 2016 (note 9).

Capacity charges are materially straight-line over the life of the plant which results in revenue recognition approximating the straight-line requirements of IAS (17) on leases. According to the agreement, PENRA shall pay for all the electric capacity available from the use of GPGC's power plant, regardless of the extent to which PENRA can absorb that capacity, for a predetermined price set out in the power purchase agreement for each operating year. In addition, PENRA shall, at all times, supply and deliver all the fuel required to generate the power needed.

17. Operating Expenses

	2018	2017
	U.S. $	U.S. $
Salaries and wages	5,254,949	5,093,549
Provision for employees' indemnity	488,706	413,657
Board of Directors expenses	169,200	202,100
Employees' insurance	129,822	110,792
Travel and transportation	320,830	410,291
Power plant insurance	1,007,578	1,096,682
Power plant operation and maintenance	3,859,505	5,010,081
Depreciation of property, plant and equipment	6,296,135	6,305,893
Amortization of intangible assets	221,583	221,583
Land lease	147,000	147,000
Professional and consultancy fees	148,240	153,520
Telephone and fax	59,101	74,639
Palestine Securities Exchange listing fees	26,415	26,469
Office supplies	48,514	60,892
Advertisements	27,938	24,061
Security service costs	65,040	65,040
Donations	959,858	31,258
Miscellaneous	261,398	503,621
	19,491,812	19,951,128

18. Other Revenues, Net

	2018	2017
	U.S. $	U.S. $
Interest of deposit at bank	591,193	216,027
Impairment of project in progress (note 7)	(249,372)	-
Currency differences	(22,943)	10,395
Others	-	(10,158)
	318,878	216,264

19. Basic and Diluted Earnings Per Share

	2018	2017
	U.S. $	U.S. $
Profit for the year	8,786,981	8,642,228
	Shares	Shares
Weighted average of subscribed share capital during the year	60,000,000	60,000,000
	U.S. $	U.S. $
Basic and diluted earnings per share	0.15	0.14

20. Dividends

The Company's General Assembly approved in its meeting held on March 28, 2018, the proposed dividends distribution by the Company's Board of Directors of U.S. $ 6,000,000 for the year 2017, the equivalent of 10% of paid-in share capital.

The Company's General Assembly approved in its meeting held on April 19, 2017, the proposed dividends distribution by the Company's Board of Directors of U.S. $ 6,000,000 for the year 2016, the equivalent of 10% of paid-in share capital.

21. Related Party Transactions

Related parties represent associates, major shareholders, directors and key management personnel of the Company and GPGC, and companies of which they are principal owners. Pricing policies and terms of these transactions are approved by the Board of Directors.

Balances with related parties included in the consolidated statement of financial position are as follows:

	Nature of relation	2018 U.S. $	2017 U.S. $
Cash at Arab Bank	Major shareholder	2,760,599	3,092,030
Due from shareholders	Major shareholders	16,268,033	1,494,146
Due to Consolidated Contractors Company	Major shareholder	672,057	375,152

The consolidated statement of income and comprehensive income includes the following transactions with related parties:

	Nature of relation	2018 U.S. $	2017 U.S. $
Expenses allocated by Consolidated Contractors Company	Major shareholder	1,051,058	1,172,633
Salaries and wages	Key management	474,813	471,471
Employees' end of service indemnity	Key management	50,736	41,092
Board of Directors expenses	Board of Directors	169,200	202,100

22. Income Tax

The Palestinian National Authority has agreed to exempt GPGC (the subsidiary) and its shareholders, with respect to dividends and earnings from GPGC, for the term of the agreement of 20 years including any extensions thereof, from all Palestinian taxes.

As of the date of issuing these consolidated financial statements, the Company did not obtain a tax settlement from the taxes authorities for the period from inception in 1999.

23. Commitments and Contingencies

Contractual commitments represent the difference between the contract gross amount and the executed portion of the contract at the consolidated financial statements date and they are as follows:

	2018 U.S. $	2017 U.S. $
Land lease agreement	1,617,000	1,764,000
Maintenance service agreement	359,296	75,761
	1,976,296	1,839,761

Future capacity charges invoices from the use of the power plant according to the power purchase agreement (will be effective until the year 2024) amounted to U.S. $ 183,383,488 and U.S. $ 215,395,168 as of December 31, 2018 and 2017, respectively.

24. Fair Values of Financial Instruments

The fair value of financial instruments, are not materially different from their carrying values. The fair values for financial assets and financial liabilities are determined at amounts at which the instrument could be exchanged between willing parties other than forced or liquidation sale.

The fair value of the accounts receivables, other financial assets, and other financial liabilities are not materially different from their carrying values because these instruments have short repayment and collection periods.

The fair value of the financial assets at fair value through other comprehensive income are not materially different from its carrying amount.

25. Risk Management

The main risks arising from the Company's financial instruments are interest rate risk, credit risk, liquidity risk, and foreign currency risk. The Company's Board of Directors reviews and approves policies for managing these risks which are summarized below:

Interest rate risk

The following table demonstrates the sensitivity of the consolidated statement of income and comprehensive income to reasonably possible changes in interest rates as of December 31, 2018, with all other variables held constant.

The sensitivity of the consolidated statement of income and comprehensive income is the effect of the assumed changes in interest rates on the Company's profit for one year, based on the floating rate of financial assets and financial liabilities at December 31, 2018 and 2017. There is no direct impact on the Company's equity. The effect of decreases in interest rate is expected to be equal and opposite to the effect of increases shown below:

	Increase in interest rate	Effect on profit for the year
	Basis points	U.S. $
2018		
U.S. Dollar	10	10,000
2017		
U.S. Dollar	10	20,000

Credit risk

The Company is currently exposed to credit risk as all the revenues of its subsidiary from the use of the power plant to generate electric capacity is generated from one customer, PENRA. PENRA has not provided the Company's subsidiary with required letter of credit of U.S. $ 20 million as required by the power purchase agreement.

With respect to credit risk arising from the other financial assets, the Company's exposure to credit risk arises from the possibility of default of the counterparty, which equal the carrying values for these financial assets.

Liquidity risk

The Company and its subsidiary limit their liquidity risk by maintaining adequate cash balances to meet their current obligations and to finance its operating activities and by following up on the collection of accounts receivable from PENRA.

The table below summarizes the maturity profile of the Company's financial liabilities at December 31, 2018 and 2017 based on contractual undiscounted payments.

	Less than 3 Months	3 to 12 months	Total
	U.S. $	U.S. $	U.S. $
December 31, 2018			
Other current liabilities	293,004	7,358,719	7,651,723
	293,004	7,358,719	7,651,723
December 31, 2017			
Other current liabilities	324,263	7,083,112	7,407,375
	324,263	7,083,112	7,407,375

Foreign currency risk

The table below indicates the Company's foreign currency exposure, as a result of its monetary assets and liabilities. The analysis calculates the effect of a reasonably possible movement of the U.S. $ currency rate against foreign currencies, with all other variables held constant, on the consolidated statement of income and comprehensive income. The effect of decreases in foreign currency exchange rate is expected to be equal and opposite to the effect of increases shown below:

	Increase in EURO rate to U.S. $	Effect on profit for the year	Increase in ILS rate to U.S. $	Effect on profit for the year	Increase in SEK rate to U.S. $	Effect on profit for the year
	%	U.S. $	%	U.S. $	%	U.S. $
2018						
U.S. Dollar	10	(7,609)	10	(74,643)	10	208,572
2017						
U.S. Dollar	10	(46,366)	10	(5,941)	10	208,572

26. Capital Management

The primary objective of the Company's capital management is to ensure that it maintains healthy capital ratios in order to support its business and maximize shareholders value.

The Company manages its capital structure and makes adjustments to it in light of changes in business conditions. No changes were made in the objectives, policies or processes during the years ended December 31, 2018 and 2017. Capital comprises paid-in share capital, statutory reserve and retained earnings, and is measured at U.S. $ 90,432,978 and U.S. $ 87,645,997 as at December 31, 2018 and 2017, respectively.

27. Concentration of Risk in Geographic Area

The Company and its subsidiary are carrying out all of their operations in Gaza. The Company's non-current assets, which mainly comprise property, plant and equipment, are located in Gaza. The political and economic situation in Gaza increases the risk of carrying out business and could adversely affect their performance and impact the recoverability of their assets from operation.

28. Comparative Figures

The corresponding figures for 2017 have been reclassified in order to conform with the presentation for the current year. Such reclassifications do not affect previously reported results and equity.