M Oriental Bank Limited

# 2018

# ANNUAL REPORT AND FINANCIAL STATEMENTS

# Contents



# Bank Information

FOR THE YEAR ENDED 31ST DECEMBER 2018

| | |
|---|---|
| **Board of directors** | Shanti V. Shah - Chairman<br>Nalinkumar M. Shah<br>Jitendrakumar C. Patel (Resigned on 7.06.2018)<br>Rupen M. Haria<br>Jayesh G. Shah<br>Simon D. Gregory |
| **Company secretary** | Joseph Kamau<br>P.O. Box 14357 - 00800<br>Nairobi,<br>Kenya. |
| **Registered office** | L.R. No.1870/1569, Apollo Centre, 2nd Floor<br>Ring Road, Westlands<br>P.O. Box 14357 - 00800<br>Nairobi,<br>Kenya. |
| **Independent auditor** | RSM Eastern Africa LLP<br>Certified Public Accountants<br>1st Floor, Pacis Centre, Slip Road,<br>Off Waiyaki Way, Westlands<br>P.O. Box 349 - 00606<br>Nairobi,<br>Kenya. |
| **Principal correspondents** | Standard Chartered Bank, New York, United States of America<br>Standard Chartered Bank, London, United Kingdom<br>Standard Chartered Bank, Frankfurt, Germany<br>Axis Bank, Mumbai, India |

# Notice of Annual General Meeting

**NOTICE IS HEREBY GIVEN that the 2019 Annual General Meeting of the Company will be held at The Ole-Ken Hotel, West Road, Nakuru, on 12th June 2019 at 2.30p.m. to conduct the following Ordinary Business:-**

**ORDINARY BUSINESS:**

1. To table proxies, note the presence of a quorum and record apologies.

2. To receive and adopt the Annual Report and Financial Statements for the year ended 31st December 2018 together with the Directors and Auditors Reports therein.

3. To note that Directors do not recommend payment of dividend.

4. To elect Directors:In accordance with clauses 89, and 91 of Table A Mr. S.V. Shah, and Mr. J.G. Shah retire by rotation and being eligible, offer themselves for re-election.

5. To approve the remuneration of the Directors.

6. To reappoint the Auditors.

7. Any other business which due notice has been received.

By Order of the Board
J Kamau
Company Secretary
Dated: 3rd May 2019

**Note:**

1. A shareholder entitled to attend and vote at the meeting may appoint one or more proxies (who need not be members) to attend and vote in his stead. Proxy forms must be received at the Head Office of the Company, *Finance House, Koinange Street, Nairobi, PO Box 44080- 00100 Nairobi* not later than 48 hours before the time for holding the meeting.

2. Any shareholder wishing to propose a director for election at the Annual General Meeting should send the proposal to the Board signed by the proposer and the person seconding the proposal, so as for it to be received at the Registered Office at the address shown in Note (1) above, at least 10 days before the date of the meeting.

3. In accordance with Articles 128 and 132 of the Company's Articles of Association, shareholders are requested to obtain the full Annual Report and Financial Statements for the year ended 31 December 2018 at the Bank's website: *www.moriental.co.ke*
Any shareholder interested in printed copy of the reports may obtain it at any of the Bank's branches.

# Chairman’s Report



**I am pleased to present the Annual Report for the year ending 31st December 2018. The Bank made great strides forward despite a challenging industry and economic environment that prevailed during the year.**

We are proud to have leveraged on our relationships to withstand the challenges attributed to the Kenyan economy and deliver a consistently strong result and healthy balance sheet position. The global economy started 2018 with strong, synchronized growth but as the year progressed, momentum faded and growth trends diverged due to increased trade tensions. The US economy accelerated, thanks to fiscal stimulus enacted early in the year, while the economies of the Eurozone, the UK, Japan and China began to weaken. As growth and interest rates grew more in the US than other economies, the dollar appreciated against most currencies.

Kenya’s Real GDP is estimated to have grown by 6.3% in 2018, from 4.9% in 2017, supported by favorable weather, eased political uncertainties, improved business confidence, and strong private consumption. On the supply side, services accounted for 52.5% of the growth, agriculture for 23.7%, and industry for 23.8%. On the demand side, private consumption was the key driver of growth. The International Monetary Fund, in debt sustainability analysis elevated the country’s risk of debt stress to moderate.

With the Presidential Assent to the revised Finance Bill 2018, Excise Duty applicable on fees charged on money transfer services as well as on other fees charged by Banks was increased from 10% to 20%. In addition, there was an industry revision of interest rates for Ksh savings accounts in response to market developments.
To stimulate growth, the Central Bank of Kenya reduced the interest rate to 9% in July 2018 from 9.5% in May. However, despite the reduction there is still need to remove the interest rate capping as it limits credit access to the majority of people and businesses as evidenced in the private sector credit growth decline by almost half to 2.4 % in 2018, as compared to 4.4% in 2017.

**Shanti V. Shah**
**Chairman**

# Chairman’s Report (continued)

Your Bank demonstrated its resilience in the face of a difficult business environment during the year. We were able to increase our loans and advances by 3.07 % to KSh.7.496 B from KSh.7.273B in 2017 while the deposits from customers were retained at KSh.7.40B. This follows a careful policy by management to optimize the balance sheet and yields while taking a cautious, risk based approach to lending.

As part of our client engagement strategy, we held various events across the branches for our clientele so as to interact with them and appreciate them for the continued business relationship.

We are also proud to say that we have implemented the IFRS 9 provisioning model and remain fully compliant with the Central Bank of Kenya Prudential Guidelines and industry practices at all times.

Community engagement is one of the vital pillars that we believe demonstrates value to those we interact with. We endeavor to strike the right balance on both our financial performance as well as our responsibility within the communities we engage in.

Through partnerships with various charity organizations and religious bodies we have brought about a positive change to our society. During the year, we facilitated the refurbishment of schools in Eldoret, continued with our support of the Catholic Diocese of Kitale and aided in environmental conservation as well as education of needy children in various places we operate in.

## APPRECIATION

I am grateful for the immense support by our various stakeholders. My sincere gratitude to our customers whose patronage has seen us grow over the years. To my fellow Directors, Management and staff, I am thankful for your commitment and dedication. My appreciation to Mr. J.C. Patel who resigned from the Board of Directors in June 2018.

I also acknowledge the Central Bank of Kenya for its invaluable guidance and our auditors RSM Eastern Africa for services rendered. I am optimistic about an even strong growth rate for 2019 to take your Bank to new heights.

**Shanti V Shah**
**Chairman**

# Board of Directors



Shanti V. Shah

Nalinkumar M. Shah

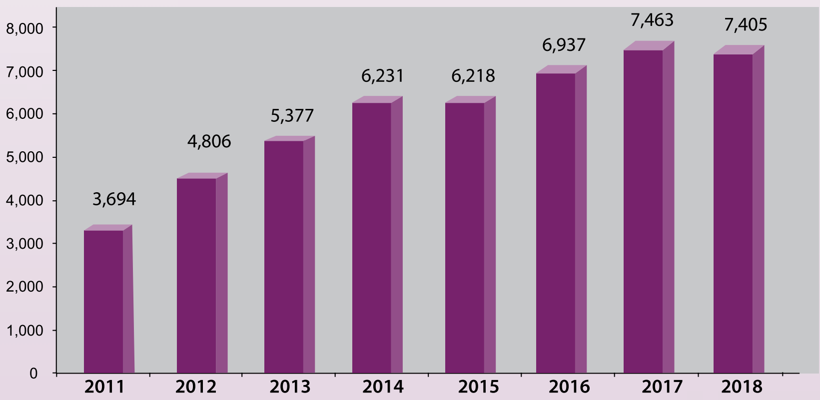
Rupen M. Haria

Simon D. Gregory

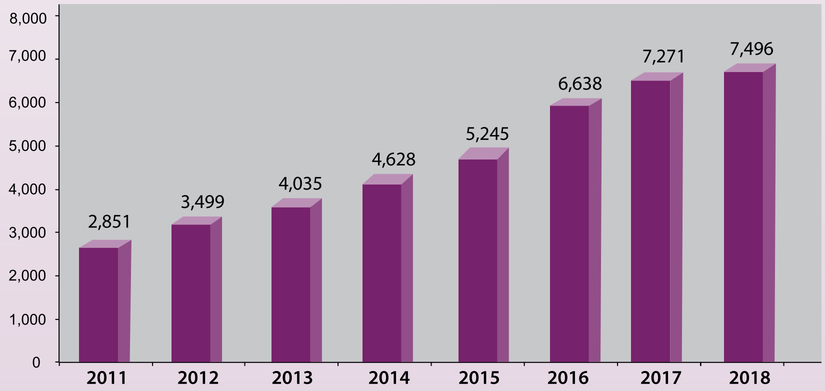
Jayesh G. Shah

# Financial Highlights

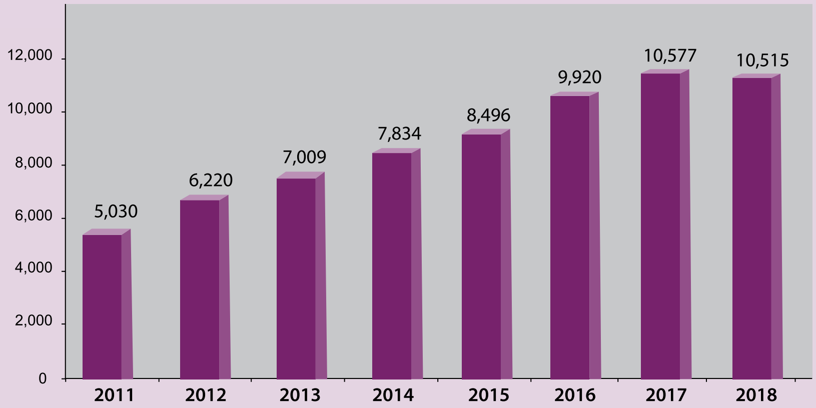
## CUSTOMER DEPOSITS IN KSh MILLIONS



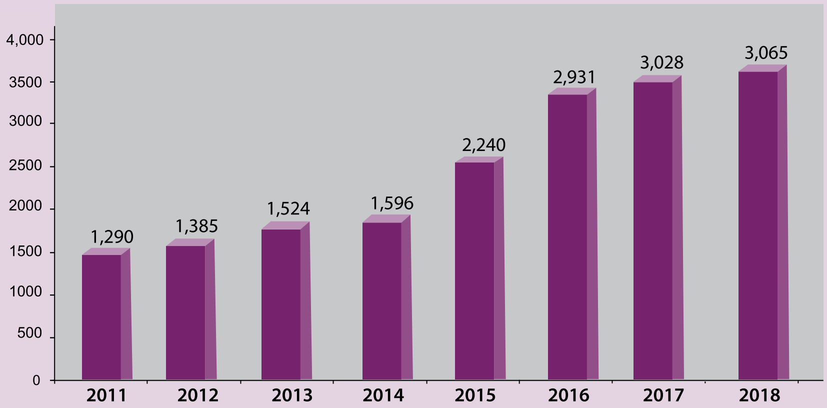

## NET LOANS & ADVANCES IN KSh MILLIONS




## TOTAL ASSETS IN KSh MILLIONS




## SHAREHOLDERS' FUND IN KSh MILLIONS



# Corporate Governance Statement

FOR THE YEAR ENDED 31ST DECEMBER 2018

Corporate governance involves a set of relationships between a broad group of stakeholders, including shareholders, Board of Directors, management, employees, customers, suppliers, regulators and the general public that guides the way companies are directed and controlled. The Board of Directors recognises importance of good corporate governance and is fully committed to achieving and sustaining the highest standards of corporate governance.

## Shareholders

The shareholders' roles are firstly to appoint the Directors and hold the Board accountable and responsible for efficient and effective governance of the Bank. Secondly they also appoint the Independent Auditors of the Bank.

## Board of Directors

The Board meets regularly and had four sittings during the year 2018 as shown on page 12. Matters requiring urgent attention were resolved through circular resolutions. Apart from the regular Board meetings, communication between the Executive Management and the Board is on a continuous basis mainly by way of Board memoranda and electronic mail which are circulated to all Directors.

The Board has delegated the authority of day to day management to the CEO but retains the overall responsibility for financial and operating decisions as indicated as shown on page 12. The Board has access to the Company Secretary. To ensure effectiveness, the Board has set up various committees which operate within and in accordance with clearly set terms of reference. The committees report to the Board at periodic intervals and by circulation.

## These committees are:-

### 1. Board Audit Committee

The role of the Board Audit Committee is to assist the board of directors in fulfilling its oversight responsibilities for the financial reporting process. It is also responsible for continually evaluating the effectiveness of internal control systems and regularly receives reports from internal and external auditors and management's corrective actions in response to the findings. The committee meets on a quarterly basis and its members are:

(i) Simon D. Gregory- Ag. Chairman
(ii) Nalinkumar M. Shah - Member
(iii) Rupen M. Haria - Member

### 2. Board Risk and Compliance Committee

The Board Risk and Compliance Committee monitors all risk exposures against defined thresholds and appetite. The committee also monitors legal and regulatory changes in the external environment and oversees compliance with relevant laws, regulations and directives. The committee meets on a quarterly basis and its members are:

(i) Jayesh G. Shah - Chairman
(ii) Nalinkumar M. Shah - Member
(iii) Rupen M. Haria - Member

### 3. Board Credit Committee

The function of this committee is to appraise and approve credit applications within the limits set by the Board and review of the quality of loans portfolio ensuring adequate loan loss provisions are held in line with the prudential guidelines. The committee also oversees and reviews the overall lending policies of the Bank. The committee meets as and when need arises. Members of this committee are:

(i) Jayesh G. Shah - Chairman
(ii) Shanti V. Shah - Member
(iii) Rupen M. Haria - Member
(iv) Nalinkumar M. Shah - Member

### 4. Board Appointment & Compensation Committee

The function of this committee is to oversee appointments and the compensation system's design and operation on behalf of the Board of Directors. The committee meets as and when the need arises. Members of this committee are:

(i) Rupen M. Haria - Chairman
(i) Shanti V. Shah - Member
(iii) Jayesh G. Shah - Member

### Board Evaluation

The Board has had regular communication on its composition and effectiveness. Through the communications, directors are called upon on the functions requiring their expertise. This is taken into account in peer review performance.

A Board assessment and peer review on performance was undertaken for the year ended 31st December 2018. This performance evaluation is an annual exercise aimed at ensuring that the Board remains efficient and effective while discharging its responsibilities.

A detailed report has been separately submitted to Central Bank of Kenya as per Prudential Guidelines.

### Management committees

For effective delegation the CEO has also set up various committees made up of senior officers of the Bank entrusted with different responsibilities which operate within prescribed Terms of Reference as approved by the Board. These Committees include Asset and Liabilities Committee (ALCO), Executive Credit Committee, Management Committee and Human Resource Committee.

# Corporate Governance Statement (continued)

FOR THE YEAR ENDED 31ST DECEMBER 2018

Tabulated below are the committees, their membership, frequency of meetings and functions.

| | **Asset and Liabilities Committee** | **Management Credit Committee** | **Executive Committee** |
|---|---|---|---|
| Chairman | C.E.O | C.E.O | C.E.O |
| Members | Head - Treasury | Chief Credit Risk Officer | Chief Credit Risk Officer |
| | Chief Credit Risk Officer | Financial Controller | Chief Operations Officer |
| | Chief Operations Officer | | Financial Controller |
| | Financial Controller | | |
| | Manager - Treasury | | |
| Frequency of meetings | Monthly | Monthly | Monthly |
| Main functions | Management of statement of financial position and liquidity | Appraisal and approval of credit applications | Strategy decision making |

The Bank is a public limited company and fully complies with the Banking Act and the Central Bank of Kenya Prudential Guidelines. The Bank distributes its annual report and financial statements and also publishes quarterly reports and notices in the national dailies to ensure that the shareholders are fully informed of the Bank's performance. No individual shareholder has direct or indirect control powers to control the institution and all shareholders have access to the Bank and it's Company Secretary who responds to their correspondences. In accordance with the Companies Act, 2015 the shareholders have access to the shares register.

# Corporate Governance Statement (continued)

FOR THE YEAR ENDED 31ST DECEMBER 2018

### Board Meeting Attendance

| Date of Meeting | S.V. Shah | N.M. Shah | R.M. Haria | J.C. Patel* | S.D. Gregory | J.G. Shah |
|---|---|---|---|---|---|---|
| 20/03/2018 | √ | √ | √ | √ | √ | √ |
| 07/06/2018 | √ | √ | √ | √ | √ | √ |
| 06/09/2018 | √ | √ | √ | x | √ | √ |
| 05/12/2018 | √ | √ | √ | x | √ | √ |
| Total meetings attended | 4 | 4 | 4 | 2 | 4 | 4 |
| Percentage attendance | 100% | 100% | 100% | 50% | 100% | 100% |

J.C. Patel*- Resigned on 7th June 2018

Shanti V. Shah
Chairman

Alakh Kohli
Chief Executive Officer

# Report of the Directors

FOR THE YEAR ENDED 31ST DECEMBER 2018



The directors submit their report together with the audited financial statements for the year ended 31 December 2018, in accordance with Section 22 of the Banking Act and Section 653 of the Kenyan Companies Act, 2015, which disclose the state of affairs of M-Oriental Bank Limited (''the Bank'').

## Incorporation

The Bank is domiciled in Kenya where it is incorporated as a company limited by shares under the Kenyan Companies Act, 2015. The address of the registered office is set out on page 1.

## Directorate

The directors who held office during the year and to the date of this report are set out on page 3.

## Principal activities

The Bank is licensed under the Banking Act and provides banking, financial and related services.

## Dividend

The directors do not recommend the declaration of a dividend for the year (2017: Nil).

## Business review

Business environment as exhibited by macro-economic indicators viz GDP, local currency stability, and inflation rates improved in 2018 compared to previous year partly attributable to better weather conditions and a relatively stable political environment. However, a relaxation of the interest cap law did not happen as envisaged. Interest rate floor/limit on customer deposits was removed but the interest rates cap on local currency lending remained and therefore challenges on pricing credit facilities based on credit risk persisted in 2018. Further, the Central Bank Rate (CBR) which forms the basis of interest rates on advances reduced by 100 basis points in 2018. Consequently, the interest margin for the Bank was eroded thereby contributing to a decline in profit after tax by 15 % from KSh 96,510,000 in 2017 to KSh 82,446,000 in 2018.

The Bank's accumulated losses reduced to KSh 37,073,000 as at 31st December 2018. Transactional business and bad debts collections are being given immense attention to compensate for the erosion on interest margin. The Bank held a deferred tax asset of KSh 300,725,000 as at 31st December 2018, which relies on generating taxable profits to exhaust past tax losses. It is expected that the Bank will be able to generate enough profits to offset the accumulated tax losses by end of 2019, especially through loan recoveries. The new International Financial Reporting Standard on financial instruments, IFRS 9, that came into effect on 1st January 2018 that basically requires impairment assessment on performing assets will continue to have a detrimental impact on the Bank's profitability.

With 7 branches across most of the major towns in Kenya, 100 experienced and highly skilled staff members, M Oriental Bank is a highly respected financial institution which serves discerning customers across the country.

# Report of the Directors (continued)

FOR THE YEAR ENDED 31ST DECEMBER 2018

### Statement as to disclosure to the Bank's auditor

With respect to each director at the time this report was approved:
(a) there is, so far as the director is aware, no relevant audit information of which the Bank's auditor is unaware; and

(b) the director has taken all the steps that the person ought to have taken as a director so as to be aware of any relevant audit information and to establish that the Bank's auditor is aware of that information.

### Terms of appointment of the auditor

The directors approve the annual audit engagement contract which sets out the terms of the auditor's appointment and the related fees. The agreed auditor's remuneration of KSh 4,500,000 has been charged to profit or loss in the year.

### By order of the board

……………………………………..
**Chairman**
Nairobi 27th February 2019

# Statement of Directors' Responsibilities

FOR THE YEAR ENDED 31ST DECEMBER 2018

The Kenyan Companies Act, 2015 requires the directors to prepare financial statements for each financial year that give a true and fair view of the financial position of the Bank as at the end of the financial year and of its profit or loss for that year. It also requires the directors to ensure that the Bank keeps proper accounting records that: (a) show and explain the transactions of the Bank; (b) disclose, with reasonable accuracy, the financial position of the Bank; and (c) enable the directors to ensure that every financial statement required to be prepared complies with the requirements of the Companies Act, 2015.

The directors accept responsibility for the preparation and presentation of these financial statements in accordance with International Financial Reporting Standards and in the manner required by the Kenyan Companies Act, 2015. They also accept responsibility for:

i. designing, implementing and maintaining such internal control as they determine necessary to enable the presentation of financial statements that are free from material misstatement, whether due to fraud or error;
ii. selecting suitable accounting policies and applying them consistently; and
iii. making accounting estimates and judgements that are reasonable in the circumstances.

Having made an assessment of the Bank's ability to continue as a going concern, the directors are not aware of any material uncertainties related to events or conditions that may cast doubt upon the Bank's ability to continue as a going concern.

The directors acknowledge that the independent audit of the financial statements does not relieve them of their responsibilities.

Approved by the board of directors on 27th February 2019 and signed on its behalf by:

| | |
|---|---|
| ………………………………………… | ………………………………………… |
| **Chairman** | **Chief Executive Officer** |

# Report of the Independent Auditor To the Members of M Oriental Bank Limited

## Opinion

We have audited the accompanying financial statements of M-Oriental Bank Limited, set out on pages 18 to 64, which comprise the statements of financial position as at 31st December 2018, the profit and loss account, statement of changes in equity and cash flows for the year then ended, and notes, including a summary of significant accounting policies.

In our opinion the accompanying financial statements give a true and fair view of the financial position of the Bank as at 31st December 2018 and of its financial performance and cash flows for the year then ended in accordance with International Financial Reporting Standards and the Kenyan Companies Act, 2015.

## 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 Financial Statements section of our report. We are independent of the Bank in accordance with the International Ethics Standards Board for Accountants’ Code of Ethics for Professional Accountants (IESBA Code) together with the ethical requirements that are relevant to our audit of the financial statements in Kenya, and we have fulfilled our ethical responsibilities in accordance with these requirements and the IESBA Code. We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our opinion.

## Other information

The directors are responsible for the other information. Other information comprises the information included in the Annual Report, but does not include the financial statements and our auditor’s report thereon.

Our opinion on the 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 financial statements, our responsibility is to read the other information and, in doing so, consider whether the other information is materially inconsistent with the 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.

## Directors’ responsibility for the financial statements

The directors are responsible for the preparation and fair presentation of the financial statements that give a true and fair view in accordance with International Financial Reporting Standards and the requirements of the Kenyan Companies Act, 2015, and for such internal control as the directors determine is necessary to enable the preparation of financial statements that are free from material misstatement, whether due to fraud or error.

In preparing the financial statements, the directors are responsible for assessing the Bank’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 the directors either intend to liquidate the Bank or to cease operations, or have no realistic alternative but to do so.

# Report of the Independent Auditor To the Members of M Oriental Bank Limited (continued)

## Auditor's responsibilities for the audit of the financial statements

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

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

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

- obtain an understanding of internal control relevant to the audit in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Bank's internal control.

- evaluate the appropriateness of accounting policies used and the reasonableness of accounting estimates and related disclosures made by management.
- conclude on the appropriateness of management's use of the going concern basis of accounting and, based on the audit evidence obtained, whether a material uncertainty exists related to events or conditions that may cast significant doubt on the Bank's ability to continue as a going concern. If we conclude that a material uncertainty exists, we are required to draw attention in our auditor's report to the related disclosures in the financial statements or, if such disclosures are inadequate, to modify our opinion. Our conclusions are based on the audit evidence obtained up to the date of the auditor's report. However, future events or conditions may cause the Bank to cease to continue as a going concern.
- evaluate the overall presentation, structure and content of the financial statements, including the disclosures, and whether the financial statements represent the underlying transactions and events in a manner that achieves fair presentation.

We communicate with those charged with governance 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.

## Report on other legal requirements

In our opinion the information given in the report of the directors on page 13 is consistent with the financial statements.

RSM Eastern Africa LLP

**RSM Eastern Africa LLP**
**Certified Public Accountants**
**Nairobi**
**27th February 2019**
**053/2019**

The signing partner responsible for the independent audit was CPA Elvis Ogeto, Practising Certificate No. 2303.

# Profit and Loss Account

FOR THE YEAR ENDED 31ST DECEMBER 2018

| | Note | 2018 KSh'000 | 2017 KSh'000 |
|---|---|---|---|
| Interest income | 4 | 1,174,132 | 1,227,535 |
| Interest expense | 5 | (574,154) | (576,702) |
| **Net interest income** | | **599,978** | **650,833** |
| Fee and commission income | 6 | 97,794 | 117,713 |
| Fee and commission expense | 6 | (3,336) | (3,319) |
| **Net fee and commission income** | | **94,458** | **114,394** |
| Net trading income | 7 | 11,493 | 13,452 |
| Changes in fair value of financial assets at fair value through profit and loss | 8 | (12,357) | 10,541 |
| Other income | 9 | 4,044 | 4,265 |
| **Total income** | | **697,616** | **793,485** |
| Employee benefits expense | | (226,879) | (242,041) |
| Other expenses | | (220,361) | (273,799) |
| Net impairment losses on loans and advances | 10 | (145,063) | (161,630) |
| **Profit before tax expense** | 11 | **105,313** | **116,015** |
| Tax expense | 12 | (22,867) | (19,505) |
| **Profit for the year attributable to the owners of the Bank** | | **82,446** | **96,510** |
| **Earnings per share attributable to the owners of the Bank** | | | |
| Basic and diluted (KSh per share) | 13 | 0.66 | 0.84 |

# Statement of Financial Position

AS AT 31ST DECEMBER 2018

| | Note | 2018 KSh'000 | 2017 KSh'000 |
|---|---|---|---|
| **ASSETS** | | | |
| Cash and balances with Central Bank of Kenya | 14 | 1,161,044 | 974,582 |
| Loans and advances to banking institutions | 15 | 596,087 | 561,922 |
| Loans and advances to customers | 16 | 7,495,897 | 7,272,765 |
| Government securities at amortised cost | 17 | 538,131 | 1,207,628 |
| Government securities at fair value through profit or loss | 18 | 200,137 | - |
| Other financial assets at amortised cost | 17 | 6,125 | 16,070 |
| Other financial assets at fair value through profit or loss | 18 | 29,804 | 45,698 |
| Other receivables | 19 | 86,571 | 69,550 |
| Intangible assets | 20 | 8,041 | 4,854 |
| Property and equipment | 21 | 92,453 | 119,289 |
| Deferred income tax | 22 | 300,725 | 304,167 |
| **Total assets** | | **10,515,015** | **10,576,525** |
| **LIABILITIES** | | | |
| Deposits from customers | 23 | 7,404,674 | 7,463,416 |
| Other payables | 24 | 45,222 | 85,111 |
| **Total liabilities** | | **7,449,896** | **7,548,527** |
| **SHAREHOLDERS' EQUITY** | | | |
| Share capital | 25 | 2,490,811 | 2,490,811 |
| Shareholders' contributions pending allotment | 25 | 9,189 | 9,189 |
| Share premium | 25 | 412,819 | 412,819 |
| Regulatory reserve | 26 | 189,373 | 247,707 |
| Accumulated losses | | (37,073) | (132,528) |
| **Total shareholders' equity** | | **3,065,119** | **3,027,998** |
| **Total liabilities and shareholders' equity** | | **10,515,015** | **10,576,525** |

The financial statements on pages 18 to 64 were approved for issue by the board of directors on 27th February 2019 and were signed on its behalf by:

……………………………… 
**Chairman**

……………………………… 
**Chief Executive Officer**

……………………………… 
**Director**

……………………………… 
**Director**

# Statement of Changes in Equity

FOR THE YEAR ENDED 31ST DECEMBER 2018

| | Note | Share capital KSh'000 | Shareholders' contributions pending allotment KSh'000 | Share premium KSh'000 | Regulatory reserve KSh'000 | Accumulated losses KSh'000 | Total KSh'000 |
|---|---|---|---|---|---|---|---|
| **At 1st January 2017** | | **2,490,811** | **9,189** | **412,819** | **233,378** | **(214,709)** | **2,931,488** |
| **Changes in equity in 2017** | | | | | | | |
| Profit for the year | | - | - | - | - | 96,510 | 96,510 |
| Transfer from regulatory reserve | 26 | - | - | - | 14,329 | (14,329) | - |
| **At 31st December 2017** | | **2,490,811** | **9,189** | **412,819** | **247,707** | **(132,528)** | **3,027,998** |
| **At 1st January 2018** | | | | | | | |
| As previously reported | | 2,490,811 | 9,189 | 412,819 | 247,707 | (132,528) | 3,027,998 |
| Adjustment on initial application of IFRS 9: | | | | | | | |
| Excess allowance for credit losses | 30 | - | - | - | - | (64,750) | (64,750) |
| Deferred tax on the above | | | | | | 19,425 | 19,425 |
| Transfer to regulatory reserve prior year additional provisions | 26 | - | - | - | (64,750) | 64,750 | - |
| As restated | | 2,490,811 | 9,189 | 412,819 | 182,957 | (113,103) | 2,982,673 |
| **Changes in equity in 2018** | | | | | | | |
| Profit for the year | | - | - | - | - | 82,446 | 82,446 |
| Transfer to regulatory reserve | | - | - | - | 6,416 | (6,416) | - |
| **At 31st December 2018** | | **2,490,811** | **9,189** | **412,819** | **189,373** | **(37,073)** | **3,065,119** |

# Statement of Cash Flows

FOR THE YEAR ENDED 31ST DECEMBER 2018

| | Note | 2018 KSh'000 | 2017 KSh'000 |
|---|---|---|---|
| **Cash flows from operating activities** | | | |
| Interest receipts | | 1,096,702 | 1,225,053 |
| Interest payments | | (564,044) | (564,355) |
| Net fees and commission receipts | | 94,458 | 114,394 |
| Net trading income | | 11,493 | 13,451 |
| Other sundry income | | 1,878 | 1,070 |
| Payments to employees and suppliers | | (452,358) | (427,079) |
| **Cash flows generated from operating activities before changes in operating assets and liabilities** | | **188,129** | **362,534** |
| Decrease/(increase) in operating assets and liabilities: | | | |
| - Cash reserve ratio | | 2,428 | (29,225) |
| - Financial assets at amortised cost | | 673,922 | 283,506 |
| - Financial assets at fair value | | (199,164) | - |
| - Loans and advances | | (350,911) | (796,341) |
| - Other receivables | | (13,765) | 3,488 |
| - Customer deposits | | (68,852) | 514,352 |
| - Other payables | | 4,092 | (3,975) |
| **Net cash generated from operating activities** | | **235,878** | **334,339** |
| **Cash flows from investing activities** | | | |
| Purchase of property, plant and equipment | 21 | (11,238) | (72,391) |
| Purchase of intangible assets | 20 | (7,309) | (3,117) |
| Proceeds from disposal of property plant and equipment | | 2,042 | 250 |
| Proceeds from sale of financial assets at fair value | | 3,042 | 6,018 |
| Dividend received | | 640 | 1,698 |
| **Net cash used in investing activities** | | **(12,823)** | **(67,542)** |
| **Net increase in cash and cash equivalents** | | **223,055** | **266,797** |
| **Cash and cash equivalents at 1st January** | | **1,160,766** | **893,969** |
| **Cash and cash equivalents at 31st December** | 27 | **1,383,821** | **1,160,766** |

## 1. Summary of significant accounting policies

The significant accounting policies adopted in the preparation of these financial statements are set out below:

### a) Basis of preparation

The financial statements are prepared on a going concern basis and in compliance with International Financial Reporting Standards (IFRS). They are presented in Kenya Shillings, which is also the functional currency (see (c) below), rounded to the nearest thousand (KSh'000).

The financial statements comprise a profit and loss account (statement of comprehensive income), balance sheet, statement of changes in equity, statement of cash flows and notes.

#### Measurement basis

The measurement basis used is the historical cost basis except where otherwise stated in the accounting policies sumarised below.

Under the historical cost basis, assets are recorded at the amount of cash or cash equivalents paid or the fair value of the consideration given to acquire them at the time of their acquisition. Liabilities are recorded at the amount of proceeds received in exchange for the obligation or, in some cases, at the amounts of cash or cash equivalents expected to be paid to satisfy the liability in the normal course of business.

For those assets and liabilities measured at fair value, 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. When measuring the fair value of an asset or a liability, the Bank uses market observable data as far as possible. If the fair value of an asset or a liability is not directly observable, it is estimated by the Bank using valuation techniques that maximise the use of relevant observable inputs and minimise the use of unobservable inputs (e.g. by use of the market comparable approach that reflects recent transaction prices for similar items or discounted cash flow analysis). Inputs used are consistent with the characteristics of the asset/liability that market participants would take into account.

Fair values are categorised into three levels in a fair value hierarchy based on the degree to which the inputs to the measurement are observable and the significance of the inputs to the fair value measurement in its entirety:

- Level 1 fair value measurements are those derived from quoted prices (unadjusted) in active markets for identical assets or liabilities.
- Level 2 fair value measurements are those derived from inputs other than quoted prices included within Level 1 that are observable for the asset or liability, either directly (that is, as prices) or indirectly (that is, derived from prices).
- Level 3 fair value measurements are those derived from valuation techniques that include inputs for the asset or liability that are not based on observable market data (unobservable inputs).
- Transfers between levels of the fair value hierarchy are recognised by the Bank at the end of the reporting period during which the change occurred.

# Financial Notes (continued)

FOR THE YEAR ENDED 31ST DECEMBER 2018

## 1. Summary of significant accounting policies (continued)

### b) New and revised standards

#### i) Adoption of new and revised standards

Two new standards and a number of amendments to standards became effective for the first time in the financial year beginning 1st January 2018 and have been adopted by the Bank. None of the amendments has had an effect on the Bank’s financial statements, but the two new standards have had an impact, as follows:

**IFRS 9 Financial Instruments**

From 1st January 2018, to comply with IFRS 9, which replaced IAS 39, provision has been made for either 12-month or lifetime expected credit losses (ECLs) for all the loans receivables. As a result, additional provisions of KSh 64,750,000 have been recognised at 1st January 2018 with a corresponding decrease, net of deferred tax, in retained earnings at that date. In accordance with the transition requirements of IFRS 9, the results of prior periods have not been restated since, in the opinion of the directors, it would not be possible to do so without the use of hindsight. Further details of the restatement are set out in Note 30.

The consequential amendments to the disclosures required by IFRS 7 have also only been applied to the current period. The comparative period notes disclosures repeat those disclosures made in the prior year.

**IFRS 15 Revenue from Contracts with Customers**

Under IFRS 15, revenue from sale of services is recognised over time provided the consumption of the service by the customer is simultaneous with the performance of the service by the Bank. The application of the standard, retrospectively, in the current year has not had a material impact on the financial position or financial performance of the Bank, and a prior period adjustment has, therefore, not been required.

#### ii) New and revised standards and interpretations which have been issued but are not yet effective

The Bank has not applied any new or revised standards and interpretations that have been published but are not yet effective for the year beginning 1st January 2018, and the Directors do not plan to apply any of them until they become effective. Note 32 lists all such new or revised standards and interpretations, with their effective dates, and provides reasonably estimable information relevant to assessing the possible impact that application of them will have on the Bank’s financial statements in the period of initial application.

## 1. Summary of significant accounting policies (continued)

### c) Translation of foreign currencies

On initial recognition, all transactions are recorded in the functional currency (the currency of the primary economic environment in which the Bank operates), which is Kenya Shillings.

Transactions in foreign currencies during the year are converted into the functional currency using the exchange rate prevailing at the transaction date. Monetary assets and liabilities at the balance sheet date denominated in foreign currencies are translated into the functional currency using the exchange rate prevailing as at that date. The resulting foreign exchange gains and losses from the settlement of such transactions and from year-end translation are recognised on a net basis in the profit and loss account in the year in which they arise, except for differences arising on translation of non-monetary available-for-sale financial assets, which are recognised in other comprehensive income.

### d) Revenue recognition

Revenue is derived substantially from banking business and related activities and comprises interest income, fee and commission income and trading income, and is recognised only when it can be reliably measured and it is probable that the economic benefits associated with the transaction will flow to the Bank.

The specific revenue recognition policies for interest income, fee and commission income and trading income are set out in (e), (f) and (g) below.

### e) Net interest income and expense

Interest income and expense on financial assets or liabilities are recognised in the profit and loss account using the effective interest method.

The effective interest rate is the rate that exactly discounts estimated future cash payments or receipts through the expected life of the financial instrument or, when appropriate, a shorter period to the net carrying amount of the financial asset or financial liability. The effective interest rate is established on the initial recognition of the financial asset or liability and is not revised subsequently. When estimating the future cash flows all contractual cash flows from the financial asset or liability are taken into consideration with the exception of the estimates of future credit losses. This includes all fees paid or received between parties to the contract, transaction costs and discounts or premiums received or paid.

Once a credit-impaired financial asset has been written down to reflect the lifetime expected credit loss, interest income is calculated by applying the effective interest rate to the amortised cost of the financial asset in subsequent reporting periods.

### f) Fee and commission income

Fee and commission income and expenses that are integral to the effective interest rate on financial assets or liabilities are included in the measurement of the effective interest rate. Other fee and commission income, including servicing fees, investment management fees and syndication fees are recognised over time as the related services are performed. Loan commitment fees for loans that are likely to be drawn down are deferred (together with related direct costs) and recognised as an adjustment to the effective interest rate on the loan.

**1. Summary of significant accounting policies(continued)**

**g) Net trading income**

Net trading income comprises gains less losses related to trading assets and liabilities, and includes all realised and unrealised fair value changes and foreign exchange differences.

Foreign exchange income is recognised at the time of effecting the transactions and includes income from spot and forward deals and translation gains/losses.

**h) Offsetting**

Items of assets and liabilities are not offset unless there is a legally enforceable right to set off and there is an intention to settle on a net basis, or realise the asset and settle the liability simultaneously. Items of income and expenses are presented on a net basis only for gains and losses arising from a group of similar transactions such as foreign exchange trading activities.

**i) Income taxes**

Income tax expense is the aggregate amount charged/(credited) in respect of current tax and deferred tax in determining the profit or loss for the year. Tax is recognised in the profit and loss account except when it relates to items recognised in other comprehensive income, in which case it is also recognised in other comprehensive income, or to items recognised directly in equity, in which case it is also recognised directly in equity.

Current tax

Current income tax is the amount of income tax payable on the taxable profit for the year, and any adjustment to tax payable in respect of prior years, determined in accordance with the Kenyan Income Tax Act.

Deferred income tax

Deferred tax is determined for all temporary differences arising between the tax bases of assets and liabilities and their carrying amounts for financial reporting purposes, using tax rates and laws enacted or substantively enacted at the balance sheet date and expected to apply when the asset is recovered or the liability is settled.

The measurement of deferred tax assets and liabilities reflects the tax consequences that would follow from the manner in which the company expects, at the end of the reporting period, to recover or settle the carrying amount of its assets or liabilities.

Deferred tax liabilities are recognised for all taxable temporary differences except those arising on the initial recognition of an asset or liability, other than through a business combination, that at the time of the transaction affects neither the accounting nor taxable profit or loss.

Deferred tax assets are recognised only to the extent that it is probable that future taxable profits will be available against which temporary differences can be utilised. Recognised and unrecognised deferred tax assets are reassessed at the end of each reporting period and, if appropriate, the recognised amount is adjusted to reflect the extent that it has become probable that future taxable profits will allow the deferred tax asset to be recovered.

## 1. Summary of significant accounting policies(continued)

### j) Share capital and share premium

Ordinary shares are recognised at par value and classified as 'share capital' in equity. Any amounts received over and above the par value of the shares issued are classified as 'share premium' in equity.

### k) Earnings per share

Basic earnings per share is calculated by dividing profit or loss attributable to ordinary equity holders of the Bank (the numerator) by the weighted average number of ordinary shares outstanding (the denominator) during the period.

Diluted earnings per share is determined by adjusting the profit or loss attributable to ordinary equity holders of the Bank and the weighted average number of ordinary shares outstanding for the after-tax effect of all dilutive potential ordinary shares.

### l) Financial instruments

Initial recognition

Financial instruments are recognised when, and only when, the Bank becomes party to the contractual provisions of the instrument. All financial assets are recognised initially using the trade date accounting which is the date the Bank commits itself to the purchase or sale.

Classification

The Bank classifies its financial instruments into the following categories:

i) Financial assets that are held within a business model whose objective is to hold assets in order to collect contractual cash flows, and for which the contractual terms of the financial asset give rise on specified dates to cash flows that are solely payments of principal and interest on the principal amount outstanding, are classified and measured at amortised cost;

ii) Financial assets that are held within a business model whose objective is achieved by both collecting contractual cash flows and selling financial assets, and for which the contractual terms of the financial asset give rise on specified dates to cash flows that are solely payments of principal and interest on the principal amount outstanding, are classified and measured at fair value through other comprehensive income.

iii) All other financial assets are classified and measured at fair value through profit or loss

iv) Notwithstanding the above, the Bank may:
a) on initial recognition of an equity investment that is not held for trading, irrevocably elect to classify and measure it at fair value through other comprehensive income
b) on initial recognition of a debt instrument, irrevocably designate it as classified and measured at fair value through profit or loss if doing so eliminates or significantly reduces a measurement or recognition inconsistency.

## 1. Summary of significant accounting policies(continued)

### I) Financial instruments (continued)

Classification (continued)

v) Financial liabilities that are held for trading (including derivatives), financial guarantee contracts, or commitments to provide a loan at a below-market interest rate are classified and measured at fair value through profit or loss. The Bank may also, on initial recognition, irrevocably designate a financial liability as at fair value through profit or loss if doing so eliminates or significantly reduces a measurement or recognition inconsistency.

vi) All other financial liabilities are classified and measured at amortised cost.

Initial measurement

On initial recognition:

i) Financial assets or financial liabilities classified as at fair value through profit or loss are measured at fair value.

ii) All other categories of financial assets and financial liabilities are measured at the fair value plus or minus transaction costs that are incremental and directly attributable to the acquisition or issue of the instrument.

Subsequent measurement

Financial assets and financial liabilities after initial recognition are measured either at amortised cost, at fair value through other comprehensive income, or at fair value through profit or loss according to their classification.

Interest income, dividend income, and exchange gains and losses on monetary items are recognised in profit or loss.

Fair value is determined as set out in Note 1(a), Amortised cost is the amount at which the financial asset or liability is measured on initial recognition minus principal repayments, plus or minus the cumulative amortisation using the effective interest method of any difference between the initial amount and the maturity amount and, for financial assets, adjusted for any loss allowance.

Impairment

The Bank recognises a loss allowance for expected credit losses on debt instruments that are measured at amortised cost or at fair value through other comprehensive income. The loss allowance is measured at an amount equal to the lifetime expected credit losses for loans and advances and for financial instruments for which: (a) the credit risk has increased significantly since initial recognition; or (b) there is observable evidence of impairment (a credit-impaired financial asset). If, at the reporting date, the credit risk on a financial asset other than a loan and advance has not increased significantly since initial recognition, the loss allowance is measured for that financial instrument at an amount equal to 12-month expected credit losses. All changes in the loss allowance are recognised in profit or loss as impairment gains or losses.

Lifetime expected credit losses represent the expected credit losses that result from all possible default events over the expected life of a financial instrument. 12-month expected credit losses represent the portion of lifetime expected credit losses that result from default events on a financial asset that are possible within 12 months after the reporting date.

## 1. Summary of significant accounting policies(continued)

### l) Financial instruments (continued)

Impairment (continued)

Expected credit losses are measured in a way that reflects an unbiased and probability-weighted amount determined by evaluating a range of possible outcomes, the time value of money, and reasonable and supportable information that is available without undue cost or effort at the reporting date about past events, current conditions and forecasts of future economic conditions.

Derecognition/write off

Financial assets are derecognised when the rights to receive cash flows from the financial asset have expired, when the Bank has transferred substantially all risks and rewards of ownership, or when the Bank has no reasonable expectations of recovering the asset.

Financial liabilities are derecognised only when the obligation specified in the contract is discharged or cancelled or expires.

Offsetting

Financial assets and liabilities are offset and the net amount reported in the balance sheet only when there is a legally enforceable right to set off the recognised amounts and there is an intention to settle on a net basis, or realise the asset and settle the liability simultaneously.

Sale and repurchase agreements

Securities sold under sale and repurchase agreements (Repos) are retained in the financial statements with the counter party liability included in amounts due to banking institutions.

Treasury Bills purchased from the Central Bank of Kenya under agreements to resell (Reverse Repos) are not negotiable or discountable during their tenure and are presented as ‘balances with Central Bank of Kenya’ until they are repurchased.

The difference between the sale and repurchase price is treated as interest and accrued over the life of the agreement using the effective interest method.

### m) Regulatory reserve

Banking institutions are required to comply with Central Bank of Kenya Prudential Guideline CBK/PG/04 - Risk Classification of Assets and Provisioning which sets out amongst other issues, provisioning guidelines for loans and advances to customers based on performance. Where the impairment provision calculated using CBK/PG/04 exceeds the impairment provision calculated in accordance with the Bank’s accounting policy, the excess is shown as an appropriation of retained earnings, within equity.

## 1. Summary of significant accounting policies (continued)

### n) Leases

Leases of assets where a significant proportion of the risks and rewards of ownership are retained by the lessor are classified as operating leases. Payments made under operating leases are charged to the profit and loss account on a straight line basis over the lease period. Prepaid operating lease rentals are recognised as assets and are subsequently amortised over the lease period.

The Bank has not entered into any finance leases, either as lessor or lessee.

### o) Post-employment benefit obligations

The Bank operates a defined contribution retirement benefits plan for its employees, the assets of which are held in a separate trustee administered scheme managed by an insurance company. A defined contribution plan is a plan under which the Bank pays fixed contributions into a separate fund, and has no legal or constructive obligation to pay further contributions if the fund does not hold sufficient assets to pay all employees the benefits relating to employee service in the current or prior periods. The Bank's contributions are charged to the profit and loss account in the year to which they relate.

The Bank and the employees also contribute to the National Social Security Fund (NSSF), a national defined contribution scheme. Contributions are determined by local statute and the Bank's contributions are charged to the profit and loss account in the year to which they relate.

### p) Short term employee benefits

The estimated monetary liability for employees' accrued annual leave entitlement at the balance sheet date is recognised as an employment cost accrual.

### q) Property and equipment

All categories of property, plant and equipment are initially recognised at cost and subsequently carried at cost less accumulated depreciation and accumulated impairment losses. Cost includes expenditure directly attributable to the acquisition of the assets. Computer software, including the operating system, that is an integral part of the related hardware is capitalised as part of the computer equipment.

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

Depreciation is calculated using the straight line method to write down the cost of each asset to its residual value over its estimated useful life.

The assets' residual values and useful lives are reviewed, and adjusted if appropriate, at each balance sheet date.

Gains and losses on disposal of property and equipment are determined by reference to their carrying amount and are taken into account in determining operating profit.

## 1. Summary of significant accounting policies (continued)

### r) Intangible assets

Software licence costs and computer software that is not an integral part of the related hardware are initially recognised at cost, and subsequently carried at cost less accumulated amortisation and accumulated impairment losses. Costs that are directly attributable to the production of identifiable computer software products controlled by the Bank are recognised as intangible assets. Amortisation is calculated using the straight line method to write down the cost of each licence or item of software to its residual value over its estimated useful life.

### s) Impairment of non-financial assets

Non-financial assets that are carried at amortised cost are reviewed at the end of each reporting period for any indication that an asset may be impaired. If any such indication exists, an impairment loss is recognised for the amount by which the asset's carrying amount exceeds its recoverable amount. The recoverable amount is the higher of an asset's fair value less costs to sell and value in use.

### t) Cash and cash equivalents

Cash and cash equivalents for the purposes of the cash flow statement comprise cash in hand, unrestricted balances with the Central Bank of Kenya, government securities and loans and advances to Banks with maturities of three months or less from the date of acquisition that are readily convertible to known amounts of cash and which are subject to an insignificant risk of changes in value, less deposits from banking institutions. Cash and cash equivalents exclude the cash reserve requirement held with the Central Bank of Kenya. Cash flows from Repo agreements are included as part of cash flows from operating activities.

### u) Contingent liabilities

Letters of credit, acceptances, guarantees and performance bonds are accounted for as off balance sheet transactions and disclosed as contingent liabilities. Estimates of the outcome and of the financial effect of contingent liabilities is made by the management based on the information available up to the date the financial statements are approved for issue by the directors. Any expected loss is charged to the profit and loss account in the year in which it is determined.

# Financial Notes (continued)

FOR THE YEAR ENDED 31ST DECEMBER 2018

## 2. Significant judgements and key sources of estimation uncertainty

In the process of applying the accounting policies adopted by the Bank, the directors make certain estimates and judgements that may affect the carrying values of assets and liabilities in the next financial period. Such estimates and judgements are based on historical experience and other factors, including expectations of future events that are believed to be reasonable under the current circumstances. The directors evaluate such estimates and judgements at each financial reporting date to ensure that they are still reasonable under the prevailing circumstances based on the information available.

### a) Significant judgements made in applying the Bank's accounting policies

The judgements made by the directors in the process of applying the Bank's accounting policies that have the most significant effect on the amounts recognised in the financial statements include classification of loans and advances, including whether or not the loan or advance is impaired. .

### b) Key sources of estimation uncertainty

Key assumptions about the future made by the directors that have a significant risk of causing a material adjustment to the carrying amount of assets and liabilities within the next financial year include:

i) Estimates made in determining the expected credit losses on financial assets. Such estimates include the determination of probabilities of default including the use of forward looking information, and of losses given default.

ii) The deferred tax asset on tax losses carried forward has been recognised based the successful achievement of the Bank's business plan resulting in future taxable profits that will be available for utilisation against the tax losses as at the end of the year.

iii) The Bank is exposed to various contingent liabilities in the normal course of business. Management evaluates the status of these exposures on a regular basis to assess the probability of the Bank incurring related liabilities. However, provisions are made in the financial statements only where, based on the management's evaluation, a reliable estimate of the obligation can be made.

## 3. Risk management objectives and policies

### a) Financial risk management

The Bank's activities expose it to a variety of financial risks including credit, liquidity and market risks. The Bank's overall risk management policies are set out by the board and implemented by the management and involve analysis, evaluation, acceptance and management of some degree of risk or a combination of risks. Taking risk is core to the banking business, and compliance and regulatory risks, operational risks and reputational risks are a normal consequence of such a business undertaking. The bank's aim is therefore to achieve an appropriate balance between risk and return and minimise potential adverse effects of such risks on the bank's financial performance.

The Bank's risk management policies are designed to identify and analyse these risks, to set appropriate risk limits and controls and to monitor the risks and adherence to limits by means of reliable and up-to-date information systems. The bank regularly reviews its risk management policies and systems to reflect changes in markets, products and services offered, and emerging best practice. The Bank, through its training programme and management standards and procedures, aims to develop a disciplined and constructive control environment, in which all employees understand their roles and obligations.

The board has established a Board Risk and Compliance Committee and an Asset and Liability Committee (ALCO), which are responsible for developing and managing the Bank's risk management policies in their specified areas. All board committees have both executive and non-executive members and report regularly to the Board of Directors on their activities.

The Board Audit Committee, through the Internal Audit Department, is responsible for monitoring compliance with the Bank's risk management policies and procedures and for reviewing the appropriateness of the risk management framework in line with the risks faced by the bank.

#### i) Credit risk

Credit risk is the risk that one party to a financial instrument will cause a financial loss for the other party by failing to discharge an obligation and arises principally from the Bank's loans and advances to customers, to banking institutions, and investment securities. Management and control of credit risk is centralised at the credit and treasury departments of the Bank.

<u>Loans and advances to customers</u>

Exposure to credit risk is managed through regular analysis of the ability of borrowers and potential borrowers to meet interest and capital repayment obligations and by changing lending limits where appropriate. Exposure to credit risk is also managed in part by obtaining collateral against loans and advances in the form of mortgage interests over property, other registered securities over assets and guarantees. The following factors are considered when assessing credit risk of loans and advances to customers:

- the probability of default by borrowers on their contractual obligations;

- current exposures to the borrowers and likely future developments, from which the Bank derives its exposure to risk; and

- the likely recovery ratio on the defaulted obligations.

**3. Risk management objectives and policies (continued)**

**a) Financial risk management (continued)**

**i) Credit risk (continued)**

Loans and advances to customers (continued)

The Bank structures the level of credit risk it undertakes by placing limits on the amount of risk accepted in relation to one borrower, or groups of borrowers, and to geographical and industry segments. In addition, the Kenyan Banking Act also sets the maximum exposure to a single party or group. It also sets the maximum exposure to insiders and places a ceiling on the total lending to insiders. Such risks are monitored on a revolving basis and subject to an annual or more frequent review, when considered necessary. Limits on the level of credit risk by product and industry sector are approved as and when required by the credit committee. The exposure to any one borrower is further restricted by sub-limits covering on and off balance sheet exposures in relation to trading items.

The Bank monitors default of individual borrowers by using internal rating methods, which are based on Central Bank of Kenya Prudential Guideline CBK/PG/04. As per the Prudential Guideline, loans and advances are graded into the following categories:

- Normal
- Watch
- Substandard
- Doubtful
- Loss

Management assesses the credit quality of each borrower, taking into account their financial position, past experience and other factors. Individual limits are set based on internal or external information and in accordance with guidelines set by the management. The utilisation of credit limits is regularly monitored and corrective action taken, where necessary.

The Bank also uses credit-related commitments as a control and mitigation measure for credit risk on loans and advances. The primary purpose of these instruments is to ensure that funds are available to a customer as and when required. Guarantees and letters of credit carry the same credit risk as loans and advances.

Commitments to extend credit represent unused portions of authorisations to extend credit in the form of loans, guarantees or letters of credit. With respect to credit risk on commitments to extend credit, the Bank is potentially exposed to loss in an amount equal to the total unused commitments. However, the likely amount of loss is less than the total unused commitments, as most commitments to extend credit are contingent upon customers maintaining specific credit standards. The Bank monitors the term to maturity of credit commitments because longer-term commitments generally have a greater degree of credit risk than shorter-term commitments.

## 3. Risk management objectives and policies (continued)

### a) Financial risk management (continued)

#### i) Credit risk (continued)

Loans and advances to customers (continued)

In certain cases, the Bank, in an effort to recover a past due or impaired loan and advance, renegotiates the repayment terms with the individual customers. Restructuring activities include extended payment arrangements, approved external management plans, modification and deferral of payments. Following restructuring, a previously overdue customer account is reset to a normal status and managed together with other similar accounts. Restructuring policies and practices are based on indicators or criteria which, in the judgment of the credit committee, indicate that payment will most likely continue. These policies are kept under continuous review.

Letters of credit are collateralised by the underlying shipments of goods to which they relate and therefore carry less risk than a direct advance or loan.

Other financial assets

Credit risk on loans and advances to banking institutions is managed by dealing with institutions, taking into account internal ratings and placing limits on deposits that can be held with each institution.

Due to the inherent nature of Government securities, these are considered to have minimal credit risk.

Expected credit losses

The Bank applies a 'three-stage" model for impairment based on changes in credit quality since initial recognition, as summarised below:

Stage 1: financial assets that is not credit impaired at initial recognition and for which credit risk has not increased significantly since initial recognition;
Stage 2: financial assets for which credit risk has increased significantly since initial recognition, but is not yet deemed to be credit-impaired; and
Stage 3: financial assets that are credit-impaired.

In accordance with the Bank's accounting policy, for assets in Stages 2 and 3 allowance is made for expected credit losses that result from all possible default events over the expected life of a financial instrument. For assets in Stage 1 allowance is made for that portion of lifetime expected credit losses that result from default events that are possible within 12 months after the reporting date.

In assessing whether the credit risk on a financial asset has increased significantly, the Bank compares the risk of default occurring on the financial asset as at the reporting date with the risk of default occurring on that financial asset as at the date of initial recognition. In doing so, the Bank considers reasonable and supportable information that is indicative of significant increases in credit risk since initial recognition and that is available without undue cost or effort. A downgrading of the Bank's internal credit rating (see above) would be considered as indicating a significant increase in credit risk. There is also a rebuttable

**3. Risk management objectives and policies (continued)**

**a) Financial risk management (continued)**

**i) Credit risk (continued)**

Expected credit losses (continued)

assumption that the credit risk on a financial asset has increased significantly since initial recognition when contractual payments are more than 30 days past due.

For these purposes default is defined as having occurred if the borrower is in breach of contractual obligations, or if information is available internally or externally that suggests that the borrower is unlikely to be able to meet its obligations.

If the Bank does not have reasonable and supportable information to identify significant increases in credit risk and/or to measure lifetime credit losses when there has been a significant increase in credit risk on an individual instrument basis, lifetime expected credit losses are recognised on a collective basis. For such purposes, the Bank groups financial assets on the basis of shared credit risk characteristics, such as:

- type of instrument
- industry in which the borrower operates
- nature of collateral.

A financial asset is credit-impaired when one or more events that have a detrimental impact on the estimated future cash flows of the financial asset have occurred. Evidence that a financial asset is credit-impaired include observable data about the following events:

- significant financial difficulty of the borrower
- a breach of contract, such as a default or past due event
- it is probable that the borrower will enter bankruptcy
- the disappearance of an active market for the financial asset because of financial difficulties.

However, there is a rebuttable assumption that a financial asset that is 90 days past due is credit-impaired.

### 3. Risk management objectives and policies (continued)

#### a) Financial risk management (continued)

##### i) Credit risk (continued)

The gross carrying amount of financial assets with exposure to credit risk at the balance sheet date was as follows:

| Basis for measurement of loss allowance | 12-month expected credit losses | Lifetime expected credit losses | | |
|---|---|---|---|---|
| | | Stage 2 | Stage 3 | Total |
| | KSh'000 | KSh'000 | KSh'000 | KSh'000 |
| **At 31st December 2018** | | | | |
| Cash and balances with Central Bank of Kenya | 1,161,044 | - | - | 1,161,044 |
| Loans and advances to banking institutions | 596,087 | - | - | 596,087 |
| Loans and advances to customers | 6,627,019 | 507,304 | 705,105 | 7,839,428 |
| Government securities at amortised cost | 538,131 | - | - | 538,131 |
| Other financial assets at fair value through profit or loss | 29,804 | - | - | 29,804 |
| Other financial assets at amortised cost | 6,125 | - | - | 6,125 |
| Government securities at fair value through profit or loss | 200,137 | - | - | 200,137 |
| Other receivables | 86,571 | - | - | 86,571 |
| Gross carrying amount | 9,244,918 | 507,304 | 705,105 | 10,457,327 |
| Loss allowance | (36,886) | (55,968) | (250,677) | (343,531) |
| Exposure to credit risk | 9,208,032 | 451,336 | 454,428 | 10,113,796 |

The Bank holds collateral against loans and advances to customers in the form of residential and commercial property, plant and machinery, and pledged deposits. The fair value of collateral held is estimated credit of KSh 16,839,000,000 (2017: KSh 15,068,000,000), which includes KSh1,000,000,000 (2017: KSh 1,004,000,000) in respect of impaired loans and advances.

### 3. Risk management objectives and policies (continued)

#### a) Financial risk management (continued)

##### i) Credit risk (continued)

The changes in the loss allowance during the year were as follows:

| Basis for measurement of loss allowance | 12-month expected credit losses | Lifetime expected credit losses | | |
|---|---|---|---|---|
| | | Stage 2 | Stage 3 | Total |
| | KSh'000 | KSh'000 | KSh'000 | KSh'000 |
| **Year ended 31st December 2018** | | | | |
| At start of year | 28,015 | 36,735 | 218,504 | 283,254 |
| Changes arising from whether the loss allowance is measured at an amount equal to 12-month or lifetime expected credit losses | 8,871 | 19,233 | 38,480 | 66,584 |
| Changes because of financial assets that were written off during the year | - | - | (6,307) | (6,307) |
| At end of year | 36,886 | 55,968 | 250,677 | 343,531 |

| Basis for measurement of loss allowance | 12-month expected credit losses | Lifetime expected credit losses | | |
|---|---|---|---|---|
| | | Stage 2 | Stage 3 | Total |
| | KSh'000 | KSh'000 | KSh'000 | KSh'000 |
| The loss allowances at the end of each year relate to the following financial assets: | | | | |
| **At 31st December 2018** | | | | |
| Loans and advances to customers | 36,886 | 55,968 | 250,677 | 343,531 |
| Total | 36,886 | 55,968 | 250,677 | 343,531 |

# Financial Notes (continued)

FOR THE YEAR ENDED 31ST DECEMBER 2018

## 3. Risk management objectives and policies (continued)

### a) Financial risk management (continued)

#### i) Credit risk (continued)

Disclosures for the year ended 31st December 2017

Comparative amounts and disclosures have not been restated following the adoption of IFRS 9 and the amendments to IFRS 7 from 1st January 2018. Disclosures relating to credit risk in the year ended 31st December 2017 were as follows :

The Bank's exposure to credit risk on loans and advances to customers is analysed as follows:

| | 2017<br>KSh'000 |
|---|---|
| **Past due and individually impaired (sub-standard and doubtful)** | |
| Gross loans and advances | 740,642 |
| Less: impairment provision | (218,504) |
| | 522,138 |
| **Past due but not impaired (watch)** | |
| Between 31 - 90 days | 418,339 |
| | 418,339 |
| **Fully performing (normal)** | |
| Gross loans and advances | 6,332,288 |
| **Net loans and advances** | **7,272,765** |

The Bank's maximum exposure to credit risk on other financial assets is analysed as follows:

| | 2017<br>KSh'000 |
|---|---|
| **Neither past due nor impaired** | |
| Balances with Central Bank of Kenya | 822,778 |
| Loans and advances to banking institutions | 561,922 |
| Government securities at amortised cost | 1,207,628 |
| Other financial assets at amortised cost | 16,070 |
| Financial assets at fair value | 45,698 |
| Other receivables | 49,356 |
| On balance sheet exposure | 2,703,452 |
| Letters of credit | 96,885 |
| Guarantees | 356,710 |
| Total exposure | 3,157,047 |

No impairment provisions are held against other financial assets.

**3. Risk management objectives and policies (continued)**

**a) Financial risk management (continued)**

**ii) Liquidity risk**

Liquidity risk is the risk that the Bank will encounter difficulty in meeting obligations associated with financial liabilities. The Bank'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 without incurring unacceptable losses or risking damage to the Bank's reputation. This responsibility rests with the Assets and Liabilities Committee (ALCO).

The matching and controlled mismatching of the maturities and interest rates of assets and liabilities is fundamental to the management of liquidity risk. It is unusual for banks to ever be completely matched since business transacted is often on uncertain terms and of different types. An unmatched position potentially enhances profitability, but can also increase the risk of losses. The maturity of assets and liabilities and the ability to replace, at an acceptable cost, interest bearing liabilities as they mature are important factors in assessing the liquidity of the bank and its exposure to changes in interest and exchange rates.

The Bank does not maintain cash resources to meet all liabilities as they fall due as experience shows that a minimum level of reinvestment of maturing funds can be predicted with a high level of certainty. The bank maintains a portfolio of short-term liquid assets, made up of loans and advances to banking institutions and balances with Central Bank of Kenya to manage the day-to-day liquidity requirements. Management reviews the liquidity ratio of liquid assets to customer deposits on a daily basis and performs scenario testing to ensure that sufficient liquidity is maintained to meet maturing deposits. The bank fully complies with the Central Bank of Kenya's minimum Cash Reserve Ratio (5.25%) and liquidity ratio (20%) requirements, with the average liquidity maintained at 32% (2017: 34%) during the year. The bank has not defaulted on its Cash Reserve Ratio requirements.

The liquidity ratio at the balance sheet date was:

| | **2018 KSh'000** | **2017 KSh'000** |
|---|---:|---:|
| Liquid assets | 2,695,536 | 2,744,132 |
| Deposits | 7,404,674 | 7,463,416 |
| Liquidity (%) | 36.4 | 36.8 |

# Financial Notes (continued)

FOR THE YEAR ENDED 31ST DECEMBER 2018

### 3. Risk management objectives and policies (continued)

#### a) Financial risk management (continued)

##### ii) Liquidity risk (continued)

The scenario testing at 31st December 2018 indicated a liquidity ratio of 22 % (2017: 26%) in the worst case scenario.

The table below analyses financial liabilities into the relevant maturity groupings based on the remaining period at the balance sheet date to the contractual maturity date.

| At 31st December 2018 | Up to 1 month KSh'000 | 1 - 3 months KSh'000 | 3 - 12 months KSh'000 | 1 - 5 years KSh'000 | Total KSh'000 |
|---|---|---|---|---|---|
| **Financial liabilities** | | | | | |
| Deposits from customers | 3,944,563 | 2,734,636 | 725,200 | 275 | 7,404,674 |
| Other payables | 45,222 | - | - | - | 45,222 |
| **Total financial liabilities** | **3,989,785** | **2,734,636** | **725,200** | **275** | **7,449,896** |

| At 31st December 2017 | Up to 1 month KSh'000 | 1 - 3 months KSh'000 | 3 - 12 months KSh'000 | 1 - 5 years KSh'000 | Total KSh'000 |
|---|---|---|---|---|---|
| **Financial liabilities** | | | | | |
| Deposits from customers | 4,024,025 | 2,897,721 | 541,670 | - | 7,463,416 |
| Other payables | 85,111 | - | - | - | 85,111 |
| **Total financial liabilities** | **4,109,136** | **2,897,721** | **541,670** | **-** | **7,548,527** |

## 3. Risk management objectives and policies (continued)

### a) Financial risk management (continued)

#### iii) Market Risk

Market risk is the risk that the fair value or future cash flows of financial instruments will fluctuate because of changes in market price and arises from open positions in interest rates and foreign currencies, both of which are exposed to general and specific market movements and changes in the level of volatility.

The objectives of market risk management is to manage and control market risk exposures within acceptable limits, while optimising the return on risk. Overall the management of market risk rests with the Assets and Liability Committee (ALCO).

The Treasury Department is responsible for the development of detailed risk management policies, subject to review and approval by the board, and for the day to day implementation of these policies.

Market risks arise mainly from trading and non-trading activities. Trading portfolios include those positions arising from market-making transactions where the Bank acts as a principal with clients or with the market. Non-trading portfolios primarily arise from the interest rate management of the entity's retail and commercial banking assets and liabilities. Non-trading portfolio risks also include foreign exchange risk and risks arising from the Bank's government and other investment securities carried at amortised cost.

Interest rate risk

The Bank is exposed to various risks associated with the effects of fluctuations in the prevailing levels of market interest rates on its financial position and cash flows. The management closely monitors the interest rate trends to minimise the potential adverse impact of interest rate changes.

The Bank is exposed to cash flow interest rate risk on its variable rate financial instruments carried at amortised cost (loans and advances, call deposits and savings accounts, and government securities carried at amortised cost). If market interest rates were to increase/decrease by one percentage point, with all other factors remaining constant, post-tax profit would be higher/lower by KSh 49,535,000 (2017: KSh 47,602,000) in respect of cash flow interest rate risk.

Currency risk

The Bank operates wholly within Kenya and its assets and liabilities are reported in the local currency. It conducts trade with correspondent banks and takes deposits and lends in other currencies. The Bank's currency position and exposure are managed within the exposure guideline of 10% of the core capital as stipulated by the Central Bank of Kenya. This position is reviewed on a daily basis by the management.

# Financial Notes (continued)

FOR THE YEAR ENDED 31ST DECEMBER 2018

## 3. Risk management objectives and policies (continued)

### a) Financial risk management (continued)

#### iii) Market Risk (Continued)

Currency risk (continued)

The significant currency positions are detailed below:

| At 31st December 2018 | US KSh'000 | GB £ KSh'000 | Euros KSh'000 | Indian Rupee KSh'000 | Others KSh'000 | Total KSh'000 |
|---|---|---|---|---|---|---|
| **Assets** | | | | | | |
| Cash in hand | 13,588 | 446 | 9,472 | - | 1 | 23,507 |
| Cash and balances with Central Bank of Kenya | 35,274 | 44,109 | 273 | - | - | 79,656 |
| Deposits and balances due from banking institutions | 309,510 | 183,587 | 1,570 | 1,166 | - | 495,833 |
| Loans and advances to customers | 568,521 | 12,854 | 10,400 | - | - | 591,775 |
| Other foreign assets | 402 | 342 | - | - | - | 744 |
| **Total assets** | **927,295** | **241,338** | **21,715** | **1,166** | **1** | **1,191,515** |
| **Liabilities** | | | | | | |
| Deposits from customers | 892,598 | 240,499 | 14,964 | - | - | 1,148,061 |
| Other foreign liabilities | 669 | - | - | - | - | 669 |
| **Total liabilities** | **893,267** | **240,499** | **14,964** | **-** | **-** | **1,148,730** |
| **Net balance sheet position** | **34,028** | **839** | **6,751** | **1,166** | **1** | **42,785** |
| **Credit commitments** | **6,086** | **(2,580)** | **(3,493)** | **-** | **-** | **13** |
| **At 31st December 2017** | | | | | | |
| Total assets | 643,091 | 9,598 | 17,592 | (117) | 1 | 670,165 |
| Total liabilities | 456,859 | 10,515 | 16,142 | - | - | 483,516 |
| **Net balance sheet position** | **186,232** | **(917)** | **1,450** | **(117)** | **1** | **186,649** |
| **Credit commitments** | **-** | **-** | **-** | **-** | **-** | **-** |

Had the Kenya Shilling weakened by 10% against each currency, with all other variables held constant, post-tax profit would have decreased by KSh 2,995 (2017: KSh 13,065 ). If the Kenya Shilling strengthened against each currency, the effect would have been the opposite.

**3. Risk management objectives and policies (continued)**

**b) Capital management**

The Bank's objectives when managing capital, which is a broader concept than the 'equity' on the face of balance sheet, are:

i) To comply with the capital requirements set by the Central Bank of Kenya;

ii) To safeguard the Bank's ability to continue as a going concern while at the same time maximise the returns to the shareholders and benefit the other stakeholders; and

iii) To maintain a strong capital base to support the development of its business.

The Bank monitors the adequacy of its capital using the minimum capital requirements and ratios established by Central Bank of Kenya. These ratios measure capital adequacy by comparing the Bank's core capital with total risk-weighted assets plus risk weighted off-balance sheet items, total deposit liabilities and total risk weighted off balance sheet items.

Assets are weighted according to broad categories of notional credit risk, being assigned a risk weighting according to the amount of capital deemed to be necessary to support them. Four categories of risk weights (0%, 20%, 50% and 100%) are applied. For example cash in hand (domestic and foreign), balances held with Central Bank of Kenya including securities issued by the Government of Kenya have a zero risk weighting, which means that no capital is required to support the holding of these assets. Property, plant and equipment carries a 100% risk weighting. Based on these guidelines, such assets must be supported by capital equal to 100% of their carrying amount. Other asset categories have intermediate weightings.

Off-balance sheet credit related commitments such as guarantees and acceptances, performance bonds, documentary credit etc, are taken into account by applying different categories of credit risk conversion factors, designed to convert these items into balance sheet equivalents. The resulting credit equivalent amounts are then weighted for credit risk using the same percentages as for balance sheet assets. Core capital (Tier 1) consists of paid-up share capital, retained profits less investments in equity instruments of other financial institutions. Supplementary capital (Tier 2) includes general provisions appropriated from revenue reserves, up to a maximum of 1.25% of total risk weighted assets.

# Financial Notes (continued)

FOR THE YEAR ENDED 31ST DECEMBER 2018

## 3. Risk management objectives and policies (continued)

### b) Capital management (continued)

| | Balance sheet nominal amount | | Risk weighted amount | |
|---|---|---|---|---|
| | 2018 KSh'000 | 2017 KSh'000 | 2018 KSh'000 | 2017 KSh'000 |
| Cash in hand and balances with Central Bank of Kenya | 1,161,044 | 974,582 | - | - |
| Placements and deposits with banking institutions | 596,087 | 561,922 | 119,217 | 112,384 |
| Loans and advances to customers | 7,495,897 | 7,272,765 | 6,331,157 | 6,242,027 |
| Government securities at amortised cost | 538,131 | 1,207,628 | - | - |
| Government securities at fair value through profit or loss | 200,137 | - | - | - |
| Other financial assets at amortised cost | 6,125 | 16,070 | 6,125 | 16,070 |
| Other financial assets at fair value through profit or loss | 29,804 | 45,698 | 29,804 | 45,698 |
| Other receivables | 86,571 | 69,550 | 86,571 | 69,550 |
| Property and equipment | 92,453 | 119,289 | 92,453 | 119,289 |
| Intangible assets | 8,041 | 4,854 | 8,041 | 4,854 |
| Deferred tax asset | 300,725 | 304,167 | 300,725 | 304,167 |
| | 10,515,015 | 10,576,525 | 6,974,093 | 6,914,039 |
| Off-balance sheet positions | | | 230,608 | 353,620 |
| Total credit risk weighted assets | | | 7,204,701 | 7,267,659 |
| Less: market risk qualifying assets | | | 29,804 | 45,698 |
| Adjusted credit risk weighted assets | | | 7,174,897 | 7,221,961 |
| Market risk equivalent assets | | | 291,685 | 386,530 |
| Operation risk equivalent assets | | | 1,208,331 | 1,103,774 |
| Total risk weighted assets | | | 8,674,913 | 8,712,265 |

# Financial Notes (continued)

FOR THE YEAR ENDED 31ST DECEMBER 2018

## 3. Risk management objectives and policies (continued)

### b) Capital management (continued)

| | 2018<br>KSh'000 | 2017<br>KSh'000 |
|---|---|---|
| Tier 1 capital | 2,575,021 | 2,780,291 |
| Tier 2 capital | 108,436 | 108,903 |
| Total capital | 2,683,457 | 2,889,194 |
| Total deposit liabilities | 7,404,674 | 7,463,416 |

| | Actual Ratios | | Minimum Requirement | |
|---|---|---|---|---|
| | 2018<br>% | 2017<br>% | 2018<br>% | 2017<br>% |
| Core capital to total risk weighted assets | 30 | 32 | 10.5 | 10.5 |
| Total capital to total risk weighted assets | 31 | 33 | 14.5 | 14.5 |
| Core capital to deposit liabilities | 35 | 37 | 8.0 | 8.0 |

The Kenyan Banking Act also sets out the minimum core capital requirement of KSh 1 Billion (2017: KSh 1 Billion) which the bank fully complied with.

# Financial Notes (continued)

FOR THE YEAR ENDED 31ST DECEMBER 2018

## 4. Interest Income

| | 2018 KSh'000 | 2017 KSh'000 |
|---|---|---|
| Loans and advances to customers | 964,182 | 958,375 |
| Interest income on impaired loans and advances | 82,034 | 97,623 |
| Placements with and loans and advances to banking institutions | 22,940 | 49,418 |
| Financial assets at amortised cost | 104,976 | 122,119 |
| | 1,174,132 | 1,227,535 |

## 5. Interest expense

| | 2018 KSh'000 | 2017 KSh'000 |
|---|---|---|
| Customer deposits | 567,855 | 575,334 |
| Deposits from other banking institutions | 6,299 | 1,368 |
| | 574,154 | 576,702 |

## 6. Net fee and commission income

| | 2018 KSh'000 | 2017 KSh'000 |
|---|---|---|
| Fee and commission income: | | |
| Loans and advances | 77,504 | 96,806 |
| Other fees and commissions | 20,290 | 20,907 |
| | 97,794 | 117,713 |
| Fee and commission expense | | |
| Other | (3,336) | (3,319) |
| | 94,458 | 114,394 |

# Financial Notes (continued)

FOR THE YEAR ENDED 31ST DECEMBER 2018

## 7. Net trading income

| | 2018 KSh'000 | 2017 KSh'000 |
|---|---|---|
| Net foreign exchange trading income | 17,145 | 14,230 |
| Net foreign exchange loss | (5,652) | (778) |
| | 11,493 | 13,452 |

## 8. Changes in fair value of financial assets at fair value through profit or loss

| | 2018 KSh'000 | 2017 KSh'000 |
|---|---|---|
| Government securities - Treasury bonds | 56 | - |
| Equity investments | (12,413) | 10,541 |
| | (12,357) | 10,541 |

## 9. Other income

| | 2018 KSh'000 | 2017 KSh'000 |
|---|---|---|
| Dividend income from financial assets at fair value through profit or loss | 640 | 1,698 |
| (Loss)/profit on sale of financial assets at fair value through profit or loss | (439) | 1,410 |
| Profit on disposal of property and equipment | 1,965 | 87 |
| Other sundry income | 1,878 | 1,070 |
| | 4,044 | 4,265 |

## 10. Net impairment losses on loans and advances

| | 2018 KSh'000 | 2017 KSh'000 |
|---|---|---|
| Net increase in specific provision charged to profit and loss account (Note 16(b)) | 148,618 | 177,294 3 |
| Recoveries from loans and advances written off | (3,555) | (15,664) |
| Charge to the profit and loss account | 145,063 | 161,630 |

# Financial Notes (continued)

FOR THE YEAR ENDED 31ST DECEMBER 2018

## 11. Profit before tax expense

| | 2018 KSh'000 | 2017 KSh'000 |
|---|---|---|
| **(a) Items charged** | | |
| The following items have been charged in arriving at profit before tax expense: | | |
| Employee benefits expense (Note 11(b)) | 198,971 | 213,451 |
| Depreciation of property and equipment | 37,997 | 34,161 |
| Operating lease rentals expense | 40,706 | 40,698 |
| Amortisation of intangible assets | 4,122 | 1,852 |
| **(b) Employee benefits expense** | | |
| Wages and salaries | 194,728 | 206,678 |
| Retirement benefit costs: | | |
| - Defined benefit scheme | 3,959 | 6,517 |
| - National Social Security Fund | 284 | 256 |
| | 198,971 | 213,451 |
| The average number of persons employed during the year, by category, were: | | |
| | Number | Number |
| Non-management | 48 | 60 |
| Management and administration | 55 | 45 |
| Total | 103 | 105 |

# Financial Notes (continued)

FOR THE YEAR ENDED 31ST DECEMBER 2018

## 12. Income tax expense

| | 2018 KSh'000 | 2017 KSh'000 |
|---|---|---|
| Current income tax | - | - |
| Deferred income tax (Note 22) | 22,867 | 19,505 |
| Income tax expense | 22,867 | 19,505 |
| The tax on the Bank's profit before income tax differs from the theoretical amount that would arise using the statutory income tax rate as follows: | | |
| **Profit before income tax** | 105,313 | 116,015 |
| Tax calculated at a rate of 30% (2017: 30%) | 31,594 | 34,805 |
| Tax effect of: | | |
| Income not subject to tax | (11,890) | (15,422) |
| Expenses not deductible for tax purposes | 4,038 | 313 |
| Prior year under provision | (875) | (191) |
| Income tax expense | 22,867 | 19,505 |

## 13. Earnings per share

Basic earnings per share is calculated by dividing the net profit attributable to shareholders by the weighted average number of shares in issue during the year.

| | 2018 | 2017 |
|---|---|---|
| Net profit attributable to shareholders | 82,446 | 96,510 |
| Weighted average number of ordinary shares in issue during the year ('000) | 124,541 | 115,323 |
| Basic earnings per share | 0.66 | 0.84 |

There were no potentially dilutive shares outstanding at 31st December 2018 and 31st December 2017. Diluted earnings per share is therefore the same as basic earnings per share.

## 14. Cash and balances with Central Bank of Kenya

| | 2018 KSh'000 | 2017 KSh'000 |
|---|---|---|
| Cash in hand | 191,660 | 151,804 |
| Balances with Central Bank of Kenya: | | |
| Restricted balances (Cash Reserve Ratio) | 373,310 | 375,738 |
| Unrestricted balances | 596,074 | 447,040 |
| | 1,161,044 | 974,582 |

The Cash Reserve Ratio is non-interest bearing and is based on the value of customer deposits adjusted in accordance with Central Bank of Kenya requirements. As at 31st December 2018 the Cash Reserve Ratio requirement was 5.25% (2017: 5.25%) of all customer deposits. These funds are not available to finance the Bank's day to day operations.

## 15. Deposits and balances due from banking institutions

| | 2018 KSh'000 | 2017 KSh'000 |
|---|---|---|
| Balances with banking institutions in Kenya | 380,404 | 327,158 |
| Balances with banking institutions abroad | 215,683 | 234,764 |
| | 596,087 | 561,922 |

## 16. Loans and advances to customers

| | | 2018 KSh'000 | 2017 KSh'000 |
|---|---|---|---|
| a) | **Loans and advances to customers** | | |
| | Overdrafts | 3,877,475 | 3,683,989 |
| | Commercial loans | 3,961,953 | 3,807,280 |
| | **Gross loans and advances to customers** | 7,839,428 | 7,491,269 |
| | Less: Provision for impaired loans and advances (Note 16(b)) | (343,531) | (218,504) |
| | **Net loans and advances** | 7,495,897 | 7,272,765 |
| b) | **Impairment losses on loans and advances** | | |
| | At 1st January | 218,504 | 204,657 |
| | Net increase in provision for impairment charged to profit and loss account (Note 10) | 148,618 | 177,294 |
| | Interest income on impaired loans and advances | (82,034) | (97,623) |
| | Prior year provision for stage 1 &2 book charged to retained earnings | 64,750 | - |
| | Provisions utilised during the year for write off | (6,307) | (65,824) |
| | At 31st December | 343,531 | 218,504 |

## 16. Loans and advances to customers (continued)

### c) Concentration of risk

Economic sector risk concentrations within the loans and advances portfolio are as follows:

| | 2018 KSh'000 | 2017 % | 2018 KSh'000 | 2017 % |
|---|---|---|---|---|
| Manufacturing | 1,809,927 | 24 | 1,285,149 | 17 |
| Wholesale, retail trade and hotels | 3,940,254 | 50 | 3,848,688 | 51 |
| Transport and communications | 172,007 | 2 | 233,139 | 3 |
| Agriculture | 245,403 | 3 | 270,133 | 4 |
| Business services | 251,112 | 3 | 425,886 | 6 |
| Building, construction and real estate | 1,092,880 | 14 | 1,246,757 | 17 |
| Social, community and personal service | 327,845 | 4 | 181,517 | 2 |
| | 7,839,428 | 100 | 7,491,269 | 100 |

## 17. Financial assets at amortised cost

| | 2018 KSh'000 | 2017 KSh'000 |
|---|---|---|
| Government securities - Treasury bills | 187,845 | 484,949 |
| Government securities - Treasury bonds | 350,286 | 722,679 |
| | 538,131 | 1,207,628 |
| Corporate bonds | 6,125 | 16,070 |
| | | |
| Maturing: | | |
| - Within 1 year | 368,319 | 1,118,922 |
| - Over 1 year | 175,937 | 385,800 |
| | 544,256 | 1,504,722 |

Included in the above are financial assets with a carrying amount of KSh 176,000,000 (2017: KSh 295,000,000) that is held by the Central Bank of Kenya under lien as security for Letters of Credit.

The fair value of the Treasury Bonds and Corporate Bonds carried at amortised cost at the balance sheet date, based on quoted prices (unadjusted) in active markets for identical assets was KSh 336,000,000 (2017: KSh 682,000,000) and KSh 6,000,000 (2017: KSh 15,000,000) respectively.

### 18. Financial assets at fair value through profit or loss

| | 2018<br>KSh'000 | 2017<br>KSh'000 |
|---|---|---|
| Government securities - Treasury bonds | 200,137 | - |
| | 29,804 | 45,698 |

The fair values of the treasury bonds and equity investments are based on quoted prices (unadjusted) in active markets for identical assets (Level 1).

### 19. Other receivables

| | 2018<br>KSh'000 | 2017<br>KSh'000 |
|---|---|---|
| Clearing account | 54,654 | 36,532 |
| Prepayments | 23,450 | 20,194 |
| Other receivables | 8,467 | 12,824 |
| | 86,571 | 69,550 |

### 20. Intangible assets (software costs)

| | 2018<br>KSh'000 | 2017<br>KSh'000 |
|---|---|---|
| **Cost** | | |
| At 1st January | 16,715 | 13,598 |
| Additions | 7,309 | 3,117 |
| At 31st December | 24,024 | 16,715 |
| **Amortisation** | | |
| At 1st January | 11,861 | 10,009 |
| Charge for the year | 4,122 | 1,852 |
| At 31st December | 15,983 | 11,861 |
| **Net book amount** | **8,041** | **4,854** |

The annual amortisation rate used is 33.3%.

# Financial Notes (continued)

FOR THE YEAR ENDED 31ST DECEMBER 2018

## 21. Property and equipment

| | Computers, copiers & fax KSh'000 | Motor vehicles KSh'000 | Furniture, fittings & equipment KSh'000 | Total KSh'000 |
|---|---|---|---|---|
| **At 1st January 2017** | | | | |
| Cost or valuation | 18,406 | 8,988 | 202,616 | 230,010 |
| Accumulated depreciation | (14,236) | (7,496) | (126,698) | (148,430) |
| Net carrying amount | 4,170 | 1,492 | 75,918 | 81,580 |
| **Year ended 31st December 2017** | | | | |
| Opening carrying amount | 4,170 | 1,492 | 75,918 | 81,580 |
| Additions | 1,484 | - | 70,907 | 72,391 |
| Disposals | - | - | (163) | (163) |
| Write offs | (105) | - | (253) | (358) |
| Depreciation charge | (1,869) | (989) | (31,303) | (34,161) |
| Closing carrying amount | 3,680 | 503 | 115,106 | 119,289 |
| **At 31st December 2017** | | | | |
| Cost | 19,890 | 8,988 | 271,960 | 300,838 |
| Accumulated depreciation | (16,105) | (8,485) | (156,959) | (181,549) |
| **Net carrying amount** | **3,785** | **503** | **115,001** | **119,289** |
| **Year ended 31st December 2018** | | | | |
| **Cost** | | | | |
| Opening carrying amount | 3,785 | 503 | 115,001 | 119,289 |
| Additions | 695 | 3,530 | 7,013 | 11,238 |
| Disposals | - | (46) | (31) | (77) |
| Depreciation charge | (1,597) | (655) | (35,745) | (37,997) |
| **At 31st December 2018** | **2,883** | **3,332** | **86,238** | **92,453** |
| **At 31st December 2018** | | | | |
| Cost | 20,585 | 7,678 | 278,783 | 307,046 |
| Accumulated depreciation | (17,702) | (4,346) | (192,545) | (214,593) |
| Net carrying amount | 2,883 | 3,332 | 86,238 | 92,453 |

The annual depreciation rates used are as follows:

| | Rate - % |
|---|---|
| Furniture, fittings and equipment | 10 - 25 |
| Computers, copiers & faxes | 25 |
| Motor vehicles | 25 |

## 22. Deferred income tax

Deferred income tax is calculated using the enacted tax rate of 30% (2017: 30%). Deferred tax assets and liabilities, and the deferred tax (charge) in the profit and loss account is attributable to the following items:

| Year ended 31st December 2018 | At 1st January 2018 KSh'000 | Prior period adjustment Note 30 KSh'000 | (Charge) to profit & loss KSh'000 | At 31st December 2018 KSh'000 |
|---|---|---|---|---|
| **Deferred income tax asset** | | | | |
| Property and equipment | 19,063 | - | 3,424 | 22,487 |
| Intangible assets | 33 | - | 318 | 351 |
| Staff leave accrual | 1,451 | - | (51) | 1,400 |
| Provisions for impaired loans and advances | 127,895 | 19,425 | 20,850 | 168,170 |
| Tax losses carried forward | 155,725 | - | (47,408) | 108,317 |
| | 304,167 | 19,425 | (22,867) | 300,725 |

| Year ended 31st December 2017 | At 1st January 2017 KSh'000 | Prior period adjustment Note 30 KSh'000 | (Charge) to profit & loss KSh'000 | At 31st December 2017 KSh'000 |
|---|---|---|---|---|
| **Deferred income tax asset** | | | | |
| Property and equipment | 17,014 | - | 2,049 | 19,063 |
| Intangible assets | 142 | - | (109) | 33 |
| Staff leave accrual | 1,364 | - | 87 | 1,451 |
| Provisions for impaired loans and advances | 103,994 | - | 23,901 | 127,895 |
| Tax losses carried forward | 201,158 | - | (45,433) | 155,725 |
| | 323,672 | - | (19,505) | 304,167 |

The Bank has an express approval from the National Treasury to carry the tax losses forward for a further five (5) years, effective 30th June 2014. The directors have made an application for the further extension to the Cabinet Secretary, National Treasury through the Kenya Revenue Authority which was granted on 31st August 2018.

| Arising in: | Tax losses Ksh | Expiring: |
|---|---|---|
| 2010 | 361,057,628 | 31st December 2019 |

The deferred tax asset on tax losses carried forward has been recognised based on the projected future taxable profits that will be available against which the losses can be utilised.

# Financial Notes (continued)



## 23. Deposits from customers

| | 2018<br>KSh'000 | 2017<br>KSh'000 |
|---|---|---|
| Call deposits | 876 | 11,741 |
| Current and demand accounts | 618,326 | 621,129 |
| Savings accounts | 418,572 | 460,723 |
| Term deposits | 6,366,900 | 6,369,823 |
| | 7,404,674 | 7,463,416 |

The economic sector concentrations within the customer deposits portfolio were as follows:

| | 2018<br>KSh'000 | 2018<br>% | 2017<br>KSh'000 | 2017<br>% |
|---|---|---|---|---|
| Individuals | 4,812,805 | 64% | 4,744,675 | 64% |
| Non-profit institutions | 212,413 | 3% | 171,338 | 2% |
| Private companies | 2,190,417 | 30% | 2,304,901 | 31% |
| Insurance companies | 189,039 | 3% | 242,502 | 3% |
| | 7,404,674 | 100% | 7,463,416 | 100% |

Included in customer deposits were deposits amounting to KSh 851,612,000 (2017: KSh 889,843,000) that were held as collateral for loans and advances.

## 24. Other payables

| | 2018<br>KSh'000 | 2017<br>KSh'000 |
|---|---|---|
| Outstanding bankers cheques | 11,805 | 8,671 |
| Staff leave accrual | 4,668 | 4,835 |
| Sundry creditors | 28,749 | 71,605 |
| | 45,222 | 85,111 |

## 25. Share capital

| | No. of ordinary shares | Issued and paid up capital KSh '000 | Share premium KSh '000 | Shareholders' contributions pending allotment KSh'000 |
|---|---|---|---|---|
| At 1st January 2018 and 31st December 2018 | 124,540,569 | 2,490,811 | 412,819 | 9,189 |

The total number of authorised ordinary shares is 175,000,000 (2017: 175,000,000) with a par value of KSh 20 each.

The share premium account arose on issue of shares at a premium and is not distributable.

**Shareholders' contributions pending allotment**

The shareholders' contributions pending allotment relates to amounts received from shareholders in the past which the Bank does not have sufficient details to make an allotment.

## 26. Regulatory reserve

| | 2018 KSh'000 | 2017 KSh'000 |
|---|---|---|
| At 1st January | 247,707 | 233,378 |
| Adjustment on initial application of IFRS 9 (Note 30) | (64,750) | - |
| Transfer from retained earnings | 6,416 | 14,329 |
| At 31st December | 189,373 | 247,707 |

The regulatory reserve represents an appropriation from retained earnings to comply with the Central Bank of Kenya's Prudential Regulations. The balance represents the excess of impairment provisions determined in accordance with Prudential Regulations over the impairment provisions recognised in accordance with the Bank's accounting policy. The reserve is not distributable.

.

# Financial Notes (continued)



## 27. Cash and cash equivalents

| | 2018 KSh'000 | 2017 KSh'000 |
|---|---|---|
| For the purposes of the cash flow statement, cash and cash equivalents comprise the following: | | |
| Cash in hand (Note 14) | 191,660 | 151,804 |
| Unrestricted cash balances with Central Bank of Kenya (Note 14) | 596,074 | 447,040 |
| Placements with and loans and advances to banking institutions (Note 15) | 596,087 | 561,922 |
| | 1,383,821 | 1,160,766 |

## 28. Off balance sheet contingencies and commitments

**a) Contingent liabilities**

In common with the banking business, the Bank conducts business involving acceptances, guarantees, performance bonds and letters of guarantees. The majority of these facilities are offset by corresponding obligations from third parties. At the year end, the contingencies were as follows:

| | 2018 KSh'000 | 2017 KSh'000 |
|---|---|---|
| Letters of credit and acceptances | 98,745 | 96,885 |
| Guarantees | 365,803 | 356,710 |
| | 464,548 | 453,595 |

**Nature of contingent liabilities**

i) **An acceptance** is an undertaking by a bank to pay a bill of exchange, drawn on a customer, on a specified due date. The bank expects most acceptances to be presented and reimbursement by the customer is normally immediate.

ii) **Letters of credit** commit the bank to make payments to third parties, on production of documents, which are subsequently reimbursed by customers.

iii) **Guarantees** are generally written by a bank to support the performance by a customer to third parties. The bank will only be required to meet these obligations in the event of the customer's default.

Based on the estimate of the financial effect of the contingencies and the corresponding obligations from third parties, no material loss is anticipated.

## 28. Off balance sheet contingencies and commitments (continued)

### b) Pending litigation and claims

| | 2018 KSh'000 | 2017 KSh'000 |
|---|---|---|
| Pending litigation and claims | 474,266 | 474,266 |

The bank had a number of pending claims and litigation cases at end of the year. The directors, having taken necessary professional consultations, are of the opinion that the above claims are unlikely to lead to any material financial loss to the bank.

### c) Commitments

Undrawn formal stand-by facilities, credit lines and other commitments to lend at 31st December 2018 totalled KSh 890,060,000 (2017: KSh 664,135,000).

Commitments to lend are agreements to lend to customers in future subject to certain conditions. Such commitments are normally made for a fixed period. The bank may withdraw from its contractual obligation for the undrawn portion of agreed facilities by giving reasonable notice to the customer.

### d) Operating lease commitments

The future minimum lease payments under non-cancellable operating leases are as follows:

| | 2018 KSh'000 | 2017 KSh'000 |
|---|---|---|
| Not later than 1 year | 35,052 | 41,083 |
| Later than 1 year and not later than 5 years | 51,966 | 86,636 |
| | 87,018 | 127,719 |

## 29. Related party transactions

Included in loans and advances and customer deposits are amounts advanced to/received from certain directors and companies in which directors are involved either as shareholders or directors (related companies). In addition, contingent liabilities (Note 28) include guarantees and letters of credit of KSh 6,875,000 (2017: KSh 12,275,000) which have been issued to related companies.

The following transactions were carried out with related parties:

| | Directors | | Related companies | |
|---|---|---|---|---|
| | 2018 KSh'000 | 2017 KSh'000 | 2018 KSh'000 | 2017 KSh'000 |
| **a) Outstanding loans and advances** | | | | |
| At 1st January | - | - | 752,906 | 625,303 |
| Advances during the year | - | - | 2,647,058 | 2,055,580 |
| Interest charged during the year | - | - | 114,829 | 97,882 |
| Repayments during the year | - | - | (2,422,541) | (2,025,859) |
| At 31st December | - | - | 1,092,252 | 752,906 |
| **Contingent liabilities** | **-** | **45,829** | **6,875** | **12,275** |

As at 31 December 2018, loans and advances to staff amounted to KSh 40,127,000 (2017: KSh 36,746,000).

The loans and advances to related parties are performing and are fully secured. No provisions have been recognised in respect of the loans and advances to directors, related parties or staff.

| | Directors | | Related companies | |
|---|---|---|---|---|
| | 2018 KSh'000 | 2017 KSh'000 | 2018 KSh'000 | 2017 KSh'000 |
| **b) Deposits** | | | | |
| At 1st January | 124,805 | 59,038 | 13,093 | 65,975 |
| Deposits received during the year | 3,901,619 | 703,430 | 2,119,593 | 1,459,484 |
| Interest paid during the year | 16,833 | 6,164 | 1,805 | 1,753 |
| Withdrawals during the year | (3,585,889) | (643,827) | (2,119,655) | (1,514,119) |
| At 31st December | 457,368 | 124,805 | 14,836 | 13,093 |

**c) Directors' remuneration (key management compensation)**

| | | |
|---|---|---|
| Directors' remuneration | | |
| - Fees | 5,775 | 6,556 |

## 30. Prior period adjustment

### a) Classification and measurement of financial instruments

The date of initial application of IFRS 9 was 1 January 2018. The Bank was already applying IFRS 9 before this date. The measurement attributes of all other financial assets and liabilities remained the same.

Expected credit losses

As explained in Note 1(b)(i), IFRS 9 requires impairment provisions to be made based on expected credit losses instead of incurred credit losses. The effect of this has been applied retrospectively at 1st January 2018 without restating comparative amounts.

12-month expected credit losses have been recognised for cash and balances with the Central Bank of Kenya, deposits with and balances due from banking institutions, government securities, and other financial assets at amortised cost, since all of these were assessed as being of low credit risk at 1 January 2018. Loans and advances to customers have been categorised as stage 1, stage 2 or stage 3 at 1st January with expected credit losses determined accordingly.

The following table sets out the changes in the carrying amount of financial assets due to changes in impairment provisions as a consequence of the application of IFRS 9 on 1st January 2018:

| | Carrying amount under IFRS 9 KSh'000 | Carrying amount under IAS 39 KSh'000 | Prior period adjustment KSh'000 |
|---|---|---|---|
| At 1st January 2018 | | | |
| Cash and balances with Central Bank of Kenya | 974,582 | 974,582 | - |
| Deposits with and balances due from banking institutions | 561,922 | 561,922 | - |
| Loans and advances to customers | 7,208,015 | 7,272,765 | ( 64,750) |
| Government securities at amortised cost | 1,207,628 | 1,207,628 | - |
| Other financial assets at amortised cost | 16,070 | 16,070 | - |
| Financial assets at fair value through profit and loss | 45,698 | 45,698 | - |
| Other receivables | 69,550 | 69,550 | - |
| | 10,083,465 | 10,148,215 | (64,750) |

A corresponding adjustment, reducing the regulatory reserve by the same amount, has been made.

Also, a corresponding adjustment of 30% of the above amount has been made to deferred tax, increasing the deferred tax asset by KSh 19,425,000.

# Financial Notes (continued)



## 31. Comparative amounts

As stated in Note 1(b)(i), IFRS 9 has been applied retrospecively from 1st January 2018, but comparative amounts for 2017 have not been restated. The accounting policies applied in 2017 differ from those applied in 2018 principally with respect to the impairment of financial assets. The accounting policies under this heading applied in 2017 were:

Impairment

At the balance sheet date, all financial assets carried at amortised cost are individually assessed for impairment. Impairment loss is the amount by which the carrying amount of an asset exceeds its recoverable amount.

Financial assets are considered impaired when there is a default or delinquency by a borrower, restructuring of a loan or advance on terms that the Bank would not otherwise consider, indications that the borrower might not be able to continue as a going concern or is about to compound with his creditors or facing bankruptcy prospects, the disappearance of an active market for a security, or changes in the payment status of borrowers or issuers either individually or in a group.

Impairment losses on assets carried at amortised cost are measured as the difference between the carrying amount of the financial asset and the present value of the estimated cash flows discounted at the asset's original effective interest rate. In the case of loans and advances to customers, the estimated cash flows from the realisation of security held are also taken into account. Losses are recognised in the profit and loss account and reflected as a provision against the financial asset. When a subsequent event causes the amount of impairment loss to decrease or increase, the decrease or increase is recognised in the profit and loss account. Where the financial asset is deemed uncollectible, it is written off against the related provision for impairment. Subsequent recoveries of amounts previously written off are credited to the profit and loss account in the year of recovery.

Changes in impairment provisions attributable to time value are reflected as a component of interest income.

## 32. New and revised financial reporting standards

The Bank has not applied the following new and revised standards and interpretations that have been published but are not yet effective for the year beginning 1st January 2018.

Amendments to IFRS 10 and IAS 28 titled Sale or Contribution of Assets between an Investor and its Associate or Joint Venture (issued in September 2014)

The amendments, applicable from a date yet to be determined, address a current conflict between the two standards and clarify that a gain or loss should be recognised fully when the transaction involves a business, and partially if it involves assets that do not constitute a business.

IFRS 16 Leases (issued in January 2016)
The new standard, effective for annual periods beginning on or after 1st January 2019, introduces a new lessee accounting model, and will require a lessee to recognise assets and liabilities for all leases with a term of more than 12 months, unless the underlying asset is of low value. A lessee will be required to recognise 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.

## 32. New and revised financial reporting standards (continued)

Application of IFRS 16 in 2019 will require right-of-use assets and lease liabilities to be recognised in respect of most operating leases where the Bank is the lessee. Based on the Directors' preliminary assessment, right of use assets of KSh 87,018,000 and lease liabilities of KSh 87,018,000 will have to be recognised at 1st January 2019 with a corresponding decrease of the net amount in retained earnings at that date.

### IFRIC 23 Uncertainty over Income Tax Treatments (issued in June 2017)

The Interpretation, applicable to annual periods beginning on or after 1st January 2019, clarifies how to apply the recognition and measurement requirements of IAS 12 when there is uncertainty over income tax treatments.

### IFRS 17 Insurance Contracts (issued in May 2017)

The new standard, effective for annual periods beginning on or after 1st January 2021, establishes principles for the recognition, measurement, presentation and disclosure of insurance contracts issued. It also requires similar principles to be applied to reinsurance contracts held and investment contracts with discretionary participation features issued. The objective is to ensure that entities provide relevant information in a way that faithfully represents those contracts. The Bank does not issue insurance contracts.

### Amendments to IFRS 9 titled Prepayment Features with Negative Compensation (issued in October 2017)

The amendments, applicable to annual periods beginning on or after 1 January 2019, allow entities to measure prepayable financial assets with negative compensation at amortised cost or fair value through other comprehensive income if a specified condition is met.

### Amendments to IAS 28 titled Long-term Interests in Associates and Joint Ventures (issued in October 2017)

The amendments, applicable to annual periods beginning on or after 1st January 2019, clarify that an entity applies IFRS 9, rather than IAS 28, in accounting for long-term interests in associates and joint ventures.

### Amendments to IFRS 3 - Annual Improvements to IFRSs 2015–2017 Cycle, issued in December 2017

The amendments, applicable to annual periods beginning on or after 1st January 2019, provide additional guidance on applying the acquisition method to particular types of business combination.

### Amendments to IFRS 11 - Annual Improvements to IFRSs 2015–2017 Cycle, issued in December 2017

The amendments, applicable to annual periods beginning on or after 1st January 2019, clarify that when an entity obtains joint control of a business that is a joint operation, it does not remeasure its previously held interests.

## 32. New and revised financial reporting standards (continued)

### Amendments to IAS 12 - Annual Improvements to IFRSs 2015–2017 Cycle, issued in December 2017

The amendments, applicable to annual periods beginning on or after 1st January 2019, clarify that all income tax consequences of dividends should be recognised when a liability to pay a dividend is recognised, and that these income tax consequences should be recognised in profit or loss, other comprehensive income or equity according to where the entity originally recognised the transactions to which they are linked.

### Amendments to IAS 23 - Annual Improvements to IFRSs 2015–2017 Cycle, issued in December 2017

The amendments, applicable to annual periods beginning on or after 1st January 2019, clarify that the costs of borrowings made specifically for the purpose of obtaining a qualifying asset that is substantially completed can be included in the determination of the weighted average of borrowing costs for other qualifying assets.

### Amendments to IAS 19 titled Plan Amendment, Curtailment or Settlement (issued in February 2018)

The amendments, applicable to plan amendments, curtailments or settlements occurring on or after the beginning of the first annual reporting period that begins on or after 1st January 2019, requires an entity to use updated actuarial assumptions to determine current service cost and net interest for the remainder of the annual reporting period after the plan amendment, curtailment or settlement when the entity remeasures its net defined benefit liability (asset) in the manner specified in the amended standard.

### Amendments to IFRS 3 titled Definition of a Business (issued in October 2018)

The amendments, applicable to business combinations for which the acquisition date is on or after the beginning of the first annual reporting period beginning on or after 1st January 2020 and to asset acquisitions that occur on or after the beginning of that period, clarify the definition of a business, with the objective of assisting entities to determine whether a transaction should be accounted for as a business combination or as an asset acquisition.

### Amendments to IAS 1 and IAS 8 titled Definition of Material (issued in October 2018)

The amendments, applicable to annual periods beginning on or after 1 January 2020, clarify the definition of material and how it should be applied by including in the definition guidance that previously featured elsewhere in IFRS.

# CORPORATE SOCIAL RESPONSIBILITY

FOR THE YEAR ENDED 31ST DECEMBER 2018

***We understand our responsibility and the need to positively impact our society and our people. By integrating social, environmental and ethical concerns as well as those on human rights and stakeholders into our daily business and engagements.***

Throughout the year, we actively participate and engage in the creation of sustainable and shared values for our stakeholders, shareholders and the society in which we operate in.

In 2018, our Corporate Social Responsibility program has helped bring a positive impact in the lives of those we have interacted with. This has been done through strategic partnerships with concerned stakeholders and Trust Foundations.

Below highlights some of the initiatives we have been engaged in:

1 Sukuma Twende Golf Tournament at the Sigona Golf Club in March, 2018. Through our strategic partnership with The Sukuma Twende Trust, we sponsored a golf tournament to help raise funds towards a charity project. The sponsorship goes towards education of under privileged children as well as taking care of their welfare. The Trust also aids in environmental conservation.

2 Kitale Catholic Diocese Family Day Celebrations. The Church plays an integral role in our society and also runs numerous welfare projects. The Family Day celebrations is an annual celebration bringing together various parishes in aid of the Diocese projects. The Bank was able to actively contribute towards this cause not only financially, but also actively through a special desk which was set up on the day to collect contributions on behalf of the Church.

3 Aiding in Refurbishment of Arya Primary school in Eldoret through a sponsorship of the painting.


1

2

3

# Notes

# Appendix 1

The Secretary,
**M-Oriental Bank Limited**

# Proxy Form

I/We ______________________________________________

being a member/members of M-Oriental Bank Limited hereby appoint ______________________________

______________________________________________

of ______________________________________________

and failing him ______________________________________________

and failing him, the Chairman of the Meeting as my/our proxy to vote for me/us and on my/our behalf at the Annual General Meeting of the Company to be held on Wednesday, 12th June 2019 at 2.30pm and at any adjournment thereof.
As witness my/our hand(s) this ____________________ day of ______________ 2019

Signatures: ______________________________

______________________________

***IMPORTANT NOTES:***

1. *If you are unable to attend this meeting personally this form of proxy should be completed and returned to the Secretary at the Registered Office, Finance House, Koinange Street, Nairobi, PO Box 44080-00100 Nairobi. To be valid the proxy form must be received at the Head Office not later than 2.00 p.m. on Monday, 10th June 2019. Alternatively duly signed proxy form may be scanned and emailed to mobl.proxy@moriental.co.ke in pdf format not later than 2.00pm on 10th June 2019. In this case the original has to be presented at the registration desk.*

2. *If the shareholder is a corporation, this form must be under its common seal or under the hand of an officer or attorney duly authorised in writing.*

3. *A person appointed to act as a proxy need not be a member of the Company.*

4. *In case of joint holders, the signature of any one holder will be sufficient but the names of all joint holders should be stated.*


## Our Branches

**Head Office &**
**Koinange Street Branch**
Finance House, Koinange Street
P.O.Box 44080 - 00100, Nairobi, Kenya
Tel: (020) 2228461/2
Cell: 0733 333291, 0722 209585
Fax: (020) 2219469
info@moriental.co.ke

**Westlands Branch**
Apollo Centre, 2nd Floor
Ring Road, Westlands
P.O.Box 14357 - 00800, Nairobi, Kenya
Tel: (020) 3743278/87, 3743289/98
Cell: 0733 610410, 0714 611466
info@moriental.co.ke

**Sameer Business Park Branch**
Mombasa Road
P.O.Box 62080 - 00200, Nairobi, Kenya
Tel: (020) 6551668, 6551669
info@moriental.co.ke

**Eldoret Branch**
Muya House, Kenyatta Street
P.O.Box 3631 - 30100,
Tel: (053) 2062871
Cell: 0731 015125, 0729 327276
Fax: (053) 2031147
info@moriental.co.ke

**Kitale Branch**
Robert Ouko Road
P.O.Box 1521 - 30200
Tel: (054) 319884/6
Cell: 0731 015095, 0729 327278
Fax: (054) 31985
info@moriental.co.ke

**Mombasa Branch**
Hassanali Building, Nkrumah Road
P.O.Box 2846 - 80100
Tel: (041) 2220723/4
Cell: 0720 350574
Fax: (041) 2220735
info@moriental.co.ke

**Nakuru Branch**
AFC Building, Kijabe Row
P.O.Box 1955 - 20100,
Tel: (051) 2211638/9
Cell: 0731 008280, 0729 327030
Fax: (051) 2216426
info@moriental.co.ke

Regulated by the Central Bank of Kenya