M Oriental Bank Limited

ANNUAL REPORT
& FINANCIAL STATEMENTS

For the year ended 31st December 2020

M Oriental Bank Limited

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For the year ended 31st December 2020

BANK INFORMATION

Board of Directors	Shanti V. Shah - Chairman Rupen M. Haria Jayesh G. Shah * Simon D. Gregory * Alakh Kohli - Managing Director Mary R. M. Chabeda (Appointed on 8th June 2020) Nalinkumar M. Shah (Resigned on 30th July 2020) * British
Company Secretary	Joseph Kamau P.O. Box 46786 - 00100 Nairobi, Kenya.
Registered Office	L.R. No.209/1326, Finance House, 2nd Floor Koinange Street, Nairobi (CBD) P.O. Box 44080 - 00100 Nairobi, Kenya.
Independent Auditor	RSM Eastern Africa LLP Certified Public Accountants 1st Floor, Pacis Centre, Slip Road, off Waiyaki Way, Westlands P.O. Box 349 - 00606 Nairobi, Kenya.
Principal Correspondents	Standard Chartered Bank, New York, United States of America Standard Chartered Bank, London, United Kingdom Standard Chartered Bank, Frankfurt, Germany Axis Bank, Mumbai India

ANNUAL REPORT
& FINANCIAL STATEMENTS

For the year ended 31st December 2020

Chairman’s Report

Dear Shareholders

I am delighted and honored to present to you the Annual Report and Financial Statements of M Oriental Bank for year 2020, on behalf of the Board of Directors, Management and Staff. Despite the strained macroeconomic environment brought on by the COVID 19 pandemic that has ravaged the globe since the start of 2020, I am pleased to report that the Bank steered through the tough operating environment to register growth on its balance sheet and resilience in its performance despite the headwinds faced.

Macro-Economic Overview

Kenya’s real GDP is estimated to have contracted by 0.3% in 2020 compared to a growth of 5.4% in 2019 largely against the backdrop of COVID-19 disruptions that hit Kenya’s economy hard through supply and demand shocks on both the external and domestic fronts in 2020. Agricultural output grew robustly, but manufacturing and many services subsectors (e.g., tourism, education) were severely disrupted. However, according to Kenya National Bureau of Statistics (KNBS) December 2020 publications, the economy started to recover in the third quarter of 2020 as the contraction narrowed to 1.1% compared to 5.5 % in the second quarter of 2020. The recovery was mostly a result of the impressive performance of agriculture sector which grew by 6.3%. The local currency was stable against regional currencies but lost ground against major international currencies. Kenya Shilling depreciated by 7.73% against the US Dollar from end of December 2019 to end of December 2020. The usable foreign exchange reserve held by CBK as at end December 2020 was adequate at USD. 7,750 Million representing an import cover of 4.76 months against a required minimum threshold of 4.0 months. The inflation rates were stable throughout the year oscillating within the Government’s target range of 5.00% +/- 2.50%. The average annual inflation rate in 2020 was 5.21% compared to 5.20% in previous year.

Banking Sector Overview

Like all other sectors of the economy, the banking sector has been negatively impacted by the COVID 19 pandemic. The sector witnessed a substantial rise in non-performing advances resulting to increased loan loss provisions and lower profits in 2020. Gross non-performing advances in the banking sector rose to about 15.00% as at end of 2020 from about 12.00% as at end of previous year. Profit before tax dropped by 31% from Kshs.159 Billion in 2019 to Kshs. 110 Billion in 2020.

Nevertheless, the industry remained stable and resilient with sufficient capital adequacy and liquidity.

MOBL's Performance Overview

MOBL’s balance sheet size grew by a commendable 5% to Kshs. 12.98 Billion as at end of December 2020 from Kshs. 12.39 Billion as at end of previous year. The growth was funded by a 6 % growth in customer deposits from Kshs. 9.19 Billion as at end December 2019 to Kshs.9.75 Billion as at end December 2020 proving the confidence and loyalty that the depositors have with the bank, and as a result of the revised strategic plan of the Bank embarked upon two years ago resulting in our growth – it is imperative to note that our client deposits have grown by over 40% in just two years

Chairman's Report (continued)

Gross customer advances grew by 4% to Kshs. 7.55 Billion as at end of 2020 from Kshs. 7.22 Billion as at end of previous year. The bank maintained conscious stance to support the existing clients and have a prudent and merit-based approach to new advances considering the evolution of the COVID 19 pandemic.

Tough business environment that persisted for the better part of 2020 led to an increase in non-performing advances resulting to erosion of interest margin and increase in impairment losses, loans and advances. Consequently, profit before tax dipped by 34% from Kshs.64.4 Million in 2019 to Kshs. 42.5 Million in 2020. Notwithstanding this, I am pleased to advise that profit after tax grew by Kshs. 50 Million from a loss after tax of Kshs. 21. 9 Million in 2019 to profit after tax of Kshs. 27.7 Million in 2020.

The Bank's overall financial position remained sound and stable with sufficient capital adequacy and liquidity levels. It maintained healthy buffers on its capital ratios over the minimum regulatory requirement. Core Capital to Customer Deposit ratio as at end of 2020 stood at 26% against a statutory minimum requirement of 8%, core capital to total risk weighted assets stood at 29% against a regulatory minimum of 10.50% while total capital to total risk weighted assets stood at 30% against a regulatory minimum of 14.50%. This indicates that the Bank has a wherewithal to support an almost threefold balance sheet size growth from the current levels while complying with minimum regulatory requirements. Similarly, the Bank's liquidity ratio stood at 55% as at close of 2020 against regulatory minimum requirement of 20%. The average liquidity ratio in 2020 was maintained at the same level.

During year 2020, the bank successfully migrated to a new robust core banking software that is expected to enable roll out of competitive products and enhance service delivery, which will result in further growth and efficiency gains for the Bank, and most importantly, an enhanced experience for our clients.

Directors do not recommend declaration of dividend for the year 2020 considering that the bank is yet to clear accumulated losses. Our efforts to pursue significant loan recoveries that were hitherto at advance stages of materialisation to lump up the bank's bottom line and ultimately clear the past losses, were frustrated by slow judicial process and strained property market. All linked to challenges brought about by the unforeseen pandemic.

Covid 19 Response

The bank took and continues to take various safety measures in line with the guidelines issued by the government to ensure business continuity and provide the maximum support for our staff and clients alike.

We have also stood by and supported our borrowers to navigate through the pandemic period, through provision of reliefs including waiver of loan penalties, loan restructuring and fresh facilities to ensure businesses continuity. The bank restructured advances worth Kshs.1.34 Billion in 2020 and we are happy to note that most of these facilities are performing within the restructured terms.

Regulations

We are compliant with CBK prudential guidelines, the Banking Act and other business regulations.

Board of Director Changes

During the year Ms. Mary Reba Chabeda, a lawyer by profession, was appointed as an independent non-executive director becoming the first female director to sit in our Board.

Mr. Nalinkumar M. Shah resigned from the B.O.D after having served as a non-executive director for close to two decades. I sincerely thank Mr. N.M. Shah for the invaluable service which has immensely contributed to the success of the Bank.

Chairman's Report (continued)

Outlook

Evolution of the COVID 19 pandemic will continue to play a significant role in the global and Kenyan economy. Vaccinations provide a ray of hope to get to normalcy. However, unavailability of adequate vaccines in developing countries like Kenya coupled with new mutations of the virus will at best delay the return to normalcy. MOBL is putting appropriate mitigation measures to ensure business continuity during these challenging times. I believe the Bank is well placed to face the future with confidence and our strategic directives will continue to bear fruit.

Appreciation

I would like to express my gratitude to all our stakeholders. I particularly thank our loyal customers for their unwavering support without which the Bank would not have made the stride that it has made.

I also thank my colleagues in the Board for their invaluable support and contribution.

Further, I wish to thank the entire staff and management team, under the very able leadership of the Managing Director & Chief Executive Officer for their drive, initiatives, and commitment.

The Board joins me in extending our heartfelt thanks to:

a) Central Bank of Kenya and their officials for their total support and guidance,
b) Our external Auditors, RSM Eastern Africa, for their guidance and understanding,
c) Shareholders of the Bank for their confidence in the BOD and management.

Shanti V. Shah
Chairman

Board of Directors

Reba Chabeda Ouko
Director

Shanti Shah
Chairman

Rupen Haria
Director

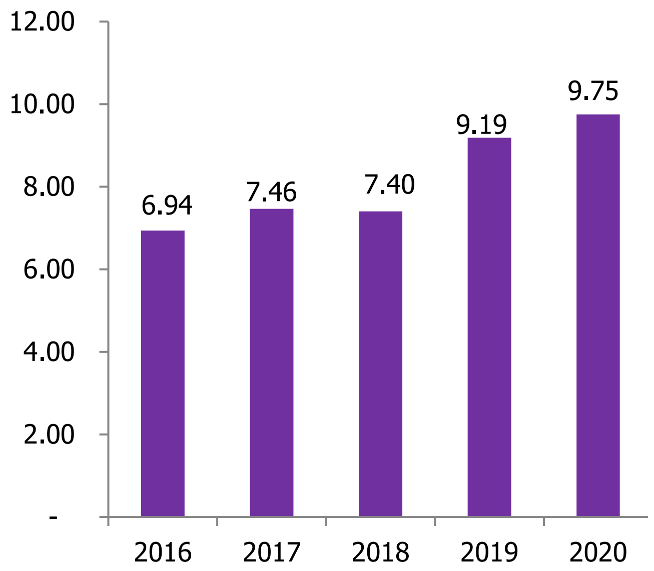
Simon Gregory
Director

Alakh Kohli
Managing Director & CEO

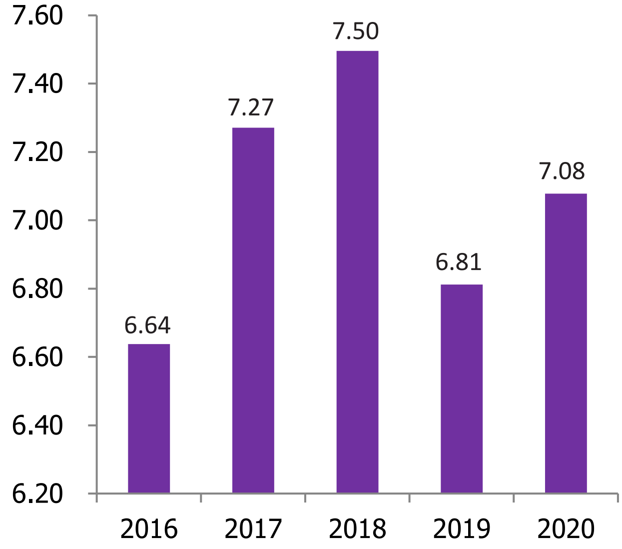
Jayesh Shah
Director

Financial Highlights

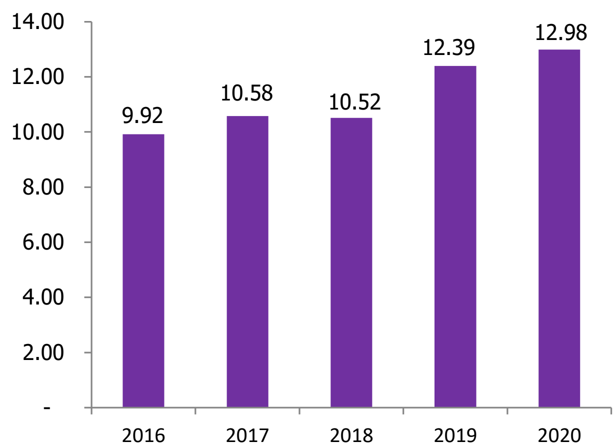
Customer Deposits in Kshs. Billions



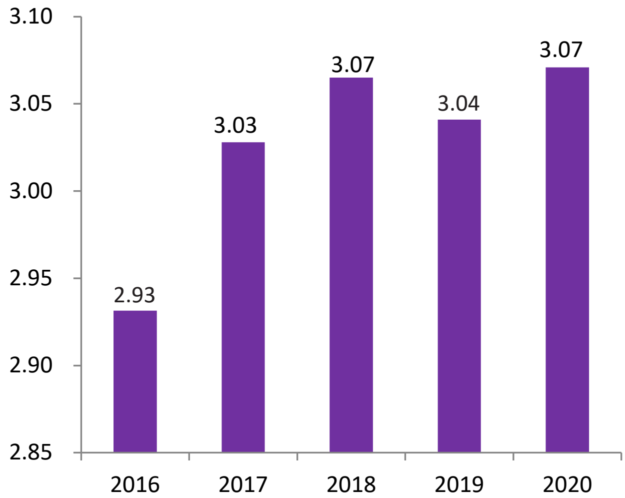
Net Loans & advances in Kshs. Billions



Total assets in Kshs. Billions



Shareholders' Fund in Kshs. Billions



Statement of Corporate Governance

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 auditor of the Bank.

Board of Directors

The Board meets regularly and had four sittings during the year 2020 as shown on page 4. 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 Chief Executive Officer (CEO) but retains the overall responsibility for financial and operating decisions as indicated on the statement of directors' responsibilities. 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) Mary R. M. Chabeda- 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) Mary R. M. Chabeda - Chairperson
(ii) Jayesh G. Shah - Member
(iii) Simon D. Gregory - Member

Statement of Corporate Governance (Continued)

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

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 2020. 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.

Statement of Corporate Governance (Continued)

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	Chief Manager Credit Chief Operations Officer Financial Controller Manager – Treasury	Chief Manager Credit Financial Controller	Chief Operations Officer Financial Controller
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.

Statement of Corporate Governance (Continued)

Board Meeting Attendance

Date of Meeting	S.V. Shah	N.M. Shah*	R.M. Haria	S.D. Gregory	J.G. Shah	A. Kohli	M.R. M. Chabeda*
27/03/2020	✓	✓	✓	✓	✓	✓	✗
30/07/2020	✓	✓	✓	✓	✓	✓	✓
24/10/2020	✓	✗	✓	✓	✓	✓	✓
23/12/2020	✓	✗	✓	✓	✓	✓	✓
Total meetings attended	4	2	4	4	4	4	3
Percentage attendance	100%	50%	100%	100%	100%	100%	75%

N.M. Shah*- resigned on 30th July 2020
M.R.M Chabeda- Appointed on 8th June 2020

....

Shanti V. Shah
Chairman

....

Alakh Kohli
Managing Director & CEO

Report of the Directors

The directors submit their report together with the audited financial statements for the year ended 31 December 2020, 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'').

Directorate

The directors who held office during the year and to the date of this report are set out on page 1.

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 (2019: Nil).

Business review

Macro economic environment in 2020 was significantly negatively impacted by COVID 19 pandemic that raveged the country and the globe. The country's GDP for 2020 is expected to have contracted by 0.3% against a growth of 5.40% in previous year. The local currency lost ground against major international currencies in 2020. On average basis Kenya Shilling (KSh) depreciated by 4.4% aganst United States Dollar (USD) in 2020. However, the inflation rate remained stable and within the Govenment target. The Bank made a conscious stance to support our existing clients to emerge from difficulties emanating from the COVID 19 pandemic and have a cautious, judicious and merit based approach to new advances resulting to marginal growth in customer advances coupled with an increase in non performing advances levels attributable to business environment challenges. This led to a 34% decline in profit before tax from KSh 64 million in 2019 to KSh 42 million in 2020. However, profit after tax went up by KSh 50 million from a loss of KSh 22 million in 2019 to a profit of KSh 28 million in 2020 primarily contributed by a one-off tax adjustment in the former.

The Bank's accumulated losses increased from KSh 92 million to KSh 155 million as at 31st December 2020 contributed by increased statutory/Central Bank of Kenya (CBK) provisions. Transactional business and bad debts collections are being given immense attention to compensate for the erosion on interest margin. Gradual easing of COVID 19 containment measures coupled with vaccinations and expected to restore and spur economic growth in 2021 and beyond. This will enable the bank to grow the business and ultimately the profitability.

With 7 branches across most of the major towns in Kenya, 98 experienced and highly skilled staff members, M Oriental Bank is a highly respected financial institution which serves discerning customers across the country.

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 director 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.

Report of the Directors (continued)

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 4,000,000 has been charged to profit or loss in the year.

By order of the board

....

Chairman

Nairobi 2021

Statement of Directors' Responsibilities

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 17th March 2021 and signed on its behalf by:

.... Chairman

.... Managing Director & CEO

Report Of The Independent Auditor To The Members Of M Oriental Bank Ltd

Opinion

We have audited the accompanying financial statements of M-Oriental Bank Limited (the ''Bank''), set out on pages 16 to 55, which comprise the statements of financial position as at 31st December 2020, the profit and loss account, statements 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 2020 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, other than that prescribed by the Kenyan Companies Act, 2015, as set out below.

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 Ltd

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 matters prescribed by the Kenyan Companies Act, 2015

In our opinion the information given in the report of the directors on page 11 is consistent with the financial statements.

RSM Eastern Africa LLP

Certified Public Accountants
Nairobi

17 March 2021
040/2021

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

Financial Statements

PROFIT AND LOSS ACCOUNT FOR THE YEAR ENDED 31ST DECEMBER 2020

	Note	2020 KSh'000	2019 KSh'000
Interest income	5	1,305,856	1,117,726
Interest expense	6	(613,193)	(610,152)
Net interest income		**692,663**	**507,574**
Fee and commission income	7	117,911	123,767
Fee and commission expense	7	(4,599)	(6,772)
Net fee and commission income		**113,312**	**116,995**
Net trading income	8	30,627	9,634
Changes in fair value of financial assets at fair value	9	(2,931)	(4,774)
Other income	10	1,129	3,476
Total income		**834,800**	**632,905**
Employee benefits expense		(220,413)	(221,544)
Other expenses		(227,025)	(217,510)
Net impairment losses on loans and advances	11	**(344,781)**	**(129,398)**
Profit before tax expense	12	42,581	64,453
Tax expense	13	**(14,861)**	**(86,401)**
Profit/(loss) for the year attributable to the owners of the Bank		**27,720**	**(21,948)**
Earnings per share attributable to the owners of the Bank			
Basic and diluted (KSh per share)	14	0.22	(0.18)

STATEMENT OF FINANCIAL POSITION AT 31ST DECEMBER 2020

	Note	2020 KSh'000	2019 KSh'000
ASSETS			
Cash and balances with Central Bank of Kenya	15	775,869	1,059,687
Loans and advances to banking institutions	16	1,408,625	1,873,377
Loans and advances to customers	17	7,078,318	6,811,799
Government securities at amortised cost	18	3,224,805	2,145,839
Other financial assets at fair value through profit or loss	19	20,548	24,625
Other receivables	20	103,178	79,257
Intangible assets	21	45,600	5,348
Property and equipment	22	43,294	64,535
Right – of – use assets	23	72,420	114,985
Deferred income tax	24	211,897	214,324
Total assets		**12,984,554**	**12,393,776**
LIABILITIES			
Deposits from customers	25	9,748,877	9,187,522
Lease liabilities	26	77,946	111,999
Current tax payable		12,434	-
Other payables	27	74,406	51,084
Total liabilities		**9,913,663**	**9,350,605**
SHAREHOLDERS' EQUITY			
Share capital	28	2,491,031	2,490,811
Shareholders' contributions pending allotment	28	8,969	9,189
Share premium	28	412,819	412,819
Regulatory reserve	29	313,450	222,004
Accumulated losses		(155,378)	(91,652)
Total shareholders equity		**3,070,891**	**3,043,171**
Total liabilities and shareholders equity		**12,984,554**	**12,393,776**

The financial statements on pages 16 to 55 were approved for issue by the board of directors on 17th March 2021 and were signed on its behalf by:

Chairman

Managing Director & CEO

STATEMENT OF CHANGES IN EQUITY FOR THE YEAR ENDED 31ST DECEMBER 2020

	Note	Share capital	Shareholders' contributions pending allotment	Share premium	Regulatory reserve	Accumulated losses	Total
		KSh'000	KSh'000	KSh'000	KSh'000	KSh'000	KSh'000
At 1st January 2019		2,490,811	9,189	412,819	189,373	(37,073)	3,065,119
Changes in equity in 2019							
Loss for the year		-	-	-	-	(21,948)	(21,948)
Transfer to regulatory reserve	29	-	-	-	32,631	(32,631)	-
At 31st December 2019		2,490,811	9,189	412,819	222,004	(91,652)	3,043,171
At 1st January 2020		2,490,811	9,189	412,819	222,004	(91,652)	3,043,171
Changes in equity in 2020							
Profit for the year		-	-	-	-	27,720	27,720
Transfer to regulatory reserve	29	-	-	-	91,446	(91,446)	-
Transactions with owners:							
Transfer to share capital	28	220	(220)	-	-	-	-
At 31st December 2020		2,491,031	8,969	412,819	313,450	(155,378)	3,070,891

STATEMENT OF CASH FLOWS FOR THE YEAR ENDED 31ST DECEMBER 2020

	Note	2020 KSh'000	2019 KSh'000
Cash flows from operating activities			
Interest receipts		1,302,017	1,104,402
Interest payments		(700,191)	(607,071)
Net fees and commission receipts		113,312	116,995
Net trading income		30,627	9,634
Other sundry income		1,052	1,831
Payments to employees and suppliers		(380,370)	(387,137)
Cash flows generated from operating activities before changes in operating assets and liabilities		**366,447**	**238,654**
Decrease/(increase)in operating assets and liabilities:			
- Cash reserve ratio		73,638	(110,263)
- Financial assets at amortised cost		(1,241,169)	-1,588,259
- Financial assets at fair value		-	200,137
- Loans and advances		(445,257)	554,700
- Other receivables		(21,801)	20,650
- Customer deposits		654,735	1,789,949
- Other payables		17,566	9,447
Net cash (used in)/generated from operating activities		**(595,841)**	**1,115,015**
Cash flows from investing activities			
Purchase of property and equipment	22	(6,512)	(7,394)
Purchase of intangible assets		(28,824)	(1,581)
Proceeds from disposal of property and equipment		-	66
Proceeds from sale of financial assets at fair value		1,094	407
Dividend received		129	1,577
Net cash used in investing activities		**(34,113)**	**(6,925)**
Cash flows from investing activities			
Lease liabilities payments - Principal	26	(38,596)	(32,238)
Lease liabilities payments - Interest	26	(6,382)	(10,182)
Net cash used in financing activities		**(44,978)**	**(42,420)**
Net (decrease)/increase in cash and cash equivalents		(674,932)	1,065,670
Cash and cash equivalents at start of year		**2,449,491**	**1,383,821**
Cash and cash equivalents at end of year	30	**1,774,559**	**2,449,491**

Notes

1. General information

M-Oriental Bank Limited (''the Bank'') is domiciled in Kenya where it is incorporated under the Kenyan Companies Act, 2015 as a private company limited by shares. The address of its registered office and principal place of business is L.R. No. 209/1326, Finance House, Nairobi (CBD), P.O. Box 44080 - 00100, Nairobi, Kenya.

2. 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) issued by the International Accounting Standards Board. 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 profit or loss), statement of financial position (balance sheet), statement of changes in equity, statement of cash flows, and notes. Income and expenses are recognised in the profit and loss account.

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."

Notes (continued)

2. Summary of significant accounting policies (continued)

b) New and revised standards

i) Adoption of new and revised standards

Three amendments to standards became effective for the first time in the financial year beginning 1st January 2020 and have been adopted by the Bank. None of the Amendments has had an effect on the Bank's financial statements.

ii) New and revised standards that have been issued but are not yet effective

The Bank has not applied any of the new or revised Standards and Interpretations that have been published but are not yet effective for the year beginning 1st January 2020, and the Directors do not plan to apply any of them until they become effective. Note 33 lists all such new or revised standards and interpretations, with their effective dates, none of which is expected to have a significant impact on the Bank's financial statements in the period of initial application.

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.

Notes (continued)

2. Summary of significant accounting policies (continued)

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.

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.

Notes (continued)

2. Summary of significant accounting policies (continued)

i) Income taxes (continued)

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.

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.

Notes (continued)

2. Summary of significant accounting policies (continued)

l) Financial instruments (continued)

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.

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.

Financial instruments held during the year were classified as follows:

- Loans and advances, and investments in government securities were classified at amortised cost;

- Other investments in shares were classified as at fair value through profit or loss;

- Customer deposits other liabilities were classified as 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.

Notes (continued)

2. Summary of significant accounting policies (continued)

l) Financial instruments (continued)

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.

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.

Notes (continued)

2. Summary of significant accounting policies (continued)

l) Financial instruments (continued)

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.

n) Leases

Leases under which the Bank is the lessee

On the commencement date of each lease (excluding leases with a term, on commencement, of 12 months or less and leases for which the underlying asset is of low value) the Bank recognises a right-of-use asset and a lease liability.

The lease liability is measured at the present value of the lease payments that are not paid on that date. The lease payments include fixed payments, variable payments that depend on an index or a rate, amounts expected to be payable under residual value guarantees, and the exercise price of a purchase option if the Bank is reasonably certain to exercise that option. The lease payments are discounted at the interest rate implicit in the lease. If that rate cannot be readily determined, the Bank's incremental borrowing rate is used.

For leases that contain non-lease components, the Bank allocates the consideration payable to the lease and non-lease components based on their relative stand-alone components.

The right-of-use asset is initially measured at cost comprising the initial measurement of the lease liability, any lease payments made on or before the commencement date, any initial direct costs incurred, and an estimate of the costs of restoring the underlying asset to the condition required under the terms of the lease.

Subsequently the lease liability is measured at amortised cost, subject to remeasurement to reflect any reassessment, lease modifications, or revised fixed lease payments.
For leases with a term, on commencement, of 12 months or less and leases for which the underlying asset is of low value, the total lease payments are recognised in profit or loss on a straight-line basis over the lease period.

Notes (continued)

2. Summary of significant accounting policies (continued)

n) Leases (continued)

Leases under which the Bank is the lessor

Leases that transfer substantially all the risks and rewards of ownership of the underlying asset to the lessee are classified as finance leases. All other leases are classified as operating leases. Payments received under operating leases are recognised as income in the profit and loss account on a straight-line basis over the lease term. The Bank has not entered into any finance leases.

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.

Notes (continued)

2. 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.

Notes (continued)

3. Significant judgements and key sources of estimation uncertainty

In the process of applying the accounting policies adopted by the Bank, the directors make certain judgements and estimates that may affect the amounts recognised in the financial statements. Such judgements and estimates are based on historical experience and other factors, including expectations of future events that are believed to be reasonable under the current circumstances. However, actual results may differ from those estimates. The judgements and estimates are reviewed at each financial reporting date to ensure that they are still reasonable under the prevailing circumstances based on the information available, and any revisions to such judgements and estimates are recognised in the year in which the revision is made.

a) Significant judgements made in applying the Banks 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:

i) classification of loans and advances, including whether or not the loan or advance is impaired.

ii) classification of financial assets: whether the business model in which financial assets are held has as its objective the holding of such assets to collect contractual cash flows or to both collect contractual cash flows and sell the assets; and whether the contractual terms of financial assets give rise on specified dates to cash flows that are solely payments of principal and interest;

iii) whether credit risk on financial assets has increased significantly since initial recognition; and

iv) how to determine the incremental borrowing rate used in the discounting of lease liabilities.

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.

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.

Notes (continued)

4. Nature and extent of risks arising from financial instruments

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 and expected credit losses

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.

Loans and advances to customers

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.

Notes (continued)

4. Nature and extent of risks arising from financial instruments (continued)

a) Financial risk management (continued)

i) Credit risk and expected credit losses (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.

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.

Notes (continued)

4. Nature and extent of risks arising from financial instruments (continued)

a) Financial risk management (continued)

i) Credit risk and expected credit losses (continued)

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 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.

Notes (continued)

4. Nature and extent of risks arising from financial instruments (continued)

a) Financial risk management (continued)

i) Credit risk and expected credit losses (continued)

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.
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 2020				
Cash and balances with Central Bank of Kenya	775,869	-	-	775,869
Loans and advances to banking institutions	1,408,625	-	-	1,408,625
Loans and advances to customers	5,758,363	70,914	1,719,122	7,548,399
Government securities at amortised cost	3,224,805	-	-	3,224,805
Other receivables	103,178	-	-	103,178
Gross carrying amount	11,270,840	70,914	1,719,122	13,060,876
Loss allowance	(31,575)	(42,894)	(395,612)	(470,081)
Exposure to credit risk	11,239,265	28,020	1,323,510	12,590,795
At 31st December 2019				
Cash and balances with Central Bank of Kenya	1,059,687	-	-	1,059,687
Loans and advances to banking institutions	1,873,377	-	-	1,873,377
Loans and advances to customers	5,813,544	277,175	1,127,266	7,217,985
Government securities at amortised cost	2,145,839	-	-	2,145,839
Other receivables	79,257	-	-	79,257
Gross carrying amount	10,971,704	277,175	1,127,266	12,376,145
Loss allowance	(40,990)	(65,143)	(300,053)	(406,186)
Exposure to credit risk	10,930,714	212,032	827,213	11,969,959

Notes (continued)

4. Nature and extent of risks arising from financial instruments (continued)

a) Financial risk management (continued)

i) Credit risk and expected credit losses (continued)

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 16,458,000,000 (2019: KSh 16,919,000,000), which includes KSh 2,955,461,000 (2019: KSh 1,641,463,000) in respect of impaired loans and advances.

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

	12-month expected credit losses	Lifetime expected credit losses		
		Stage 2	Stage 3	Total
		KSh'000	KSh'000	KSh'000
Year ended 31st December 2020				
At start of year	40,990	65,143	300,053	406,186
Changes arising from whether the loss allowance is measured at an amount equal to 12-month or lifetime expected credit losses	(9,415)	(22,249)	216,903	185,239
Changes because of financial assets that were written off during the year	-	-	(121,344)	(121,344)
At end of year	31,575	42,894	395,612	470,081
Year ended 31st December 2019				
At start of year	36,886	55,968	250,677	343,531
Changes arising from whether the loss allowance is measured at an amount equal to 12-month or lifetime expected credit losses	4,104	9,175	49,632	62,911
Changes because of financial assets that were written off during the year	-	-	(256)	(256)
At end of year	40,990	65,143	300,053	406,186

	12-month expected credit losses	Lifetime expected credit losses		
		Stage 2	Stage 3	Total
The loss allowances at the end of each year relate to the following financial assets:	KSh'000	KSh'000	KSh'000	KSh'000
At 31st December 2020				
Loans and advances to customers	31,575	42,894	395,612	470,081
At 31st December 2019				
Loans and advances to customers	40,990	65,143	300,053	406,186

Notes (continued)

4. Nature and extent of risks arising from financial instruments (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 (4.25%) and liquidity ratio (20%) requirements, with the average liquidity maintained at 55% (2019: 55%) during the year. The Bank has not defaulted on its Cash Reserve Ratio requirements.

The liquidity ratio at the balance sheet date was:

	2020 KSh'000	2019 KSh'000
Liquid assets	5,409,299	5,078,903
Deposits	9,748,877	9,187,522
Other payables	74,406	51,084
Current tax payable	12,434	-
Lease liabilities	21,075	14,140
Liquidity (%)	55	55

The scenario testing at 31st December 2020 indicated a liquidity ratio of 44 % (2019: 43%) 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.

Notes (continued)

4. Nature and extent of risks arising from financial instruments (continued)

a) Financial risk management (continued)

ii) Liquidity risk (continued)

	Up to 1 month KSh'000	1 - 3 months KSh'000	3 - 12 months KSh'000	1 - 5 years KSh'000	Total KSh'000
At 31st December 2020					
Financial liabilities					
Deposits from customers	4,860,332	3,748,806	1,139,700	-	9,748,838
Other payables	74,406	-	-	-	74,406
Lease liabilities	9,079	850	11,146	56,871	77,946
Total financial liabilities	4,943,817	3,749,656	1,150,846	56,871	9,901,190

	Up to 1 month	1 - 3 months	3 - 12 months	1 - 5 years	Total
At 31st December 2019					
Financial liabilities					
Deposits from customers	4,636,801	4,031,303	519,419	-	9,187,523
Other payables	51,084	-	-	-	51,084
Lease liabilities	3,535	10,605	28,280	69,579	111,999
Total financial liabilities	4,691,420	4,041,908	547,699	69,579	9,350,606

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.

Notes (continued)

4. Nature and extent of risks arising from financial instruments (continued)

a) Financial risk management (continued)

iii) Market risk (continued)

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 45,881,000 (2019:KSh 44,264,0000) 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.

The significant currency positions are detailed below:

Notes (continued)

a) Financial risk management (continued)

At 31st December 2020	US KSh'000	GB £ KSh'000	GB £ KSh'000	Indian Rupee KSh'000	Others KSh'000	Total KSh'000
Assets						
Cash in hand	27,766	905	6,197	-	1	34,869
Cash and balances with Central Bank of Kenya	27,744	71,545	1,149	-	-	100,438
Deposits and balances due from banking institutions	492,749	558,961	7,286	76	-	1,059,072
Loans and advances to customers	499,556	16,045	13,025	-	-	528,626
Other foreign Assets	17		555			572
Total assets	1,047,832	647,456	28,212	76	1	1,723,577
Liabilities						
Deposits from customers	1,061,493	647,493	17,120	-	-	1,726,106
Other foreign liabilities	214	-	-	-	-	214
Total liabilities	1,061,707	647,493	17,120	-	-	1,726,320
Net balance sheet position	(13,875)	(37)	11,092	76	1	(2,743)
At 31st December 2019						
Total assets	1,116,462	1,038,120	20,742	295	1	2,175,620
Total liabilities	1,112,584	1,037,320	18,070	-	-	2,167,974
Net balance sheet position	3,878	800	2,672	295	1	7,646
Credit commitments	6,086	(2,580)	(3,493)	-	-	13

Had the Kenya Shilling weakened by 10% against each currency, with all other variables held constant, post-tax profit would have decreased by KSh 8,776,000 (2019:KSh 535,000). If the Kenya Shilling strengthened against each currency, the effect would have been the opposite.

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.

Notes (continued)

4. Nature and extent of risks arising from financial instruments (continued)

b) Capital management (continued)

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.

	Balance sheet nominal amount		Risk weighted amount	
	2020	2019	2020	2020
	KSh'000	KSh'000	KSh'000	KSh'000
Cash in hand and balances with Central Bank of Kenya	775,869	1,059,687	-	-
Placements and deposits with banking institutions	1,408,625	1,873,377	281,725	374,675
Loans and advances to customers	7,078,318	6,811,799	5,778,275	5,342,483
Government securities at amortised cost	3,224,805	2,145,839	-	-
Other financial assets at fair value through profit or loss	20,548	24,625	20,548	24,625
Other receivables	103,178	79,257	103,178	79,257
Property, plant and equipment	43,294	64,535	43,294	64,535
Intangible assets	45,600	5,348	45,600	5,348
Right - of - use assets	72,420	114,985	72,420	114,985
Deferred tax asset	211,897	214,324	211,897	214,324
	12,984,554	12,393,776	6,556,937	6,220,232
Off-balance sheet positions			320,510	205,439
Total credit risk weighted assets			6,877,447	6,425,671
Less: market risk qualifying assets			20,548	24,625
Adjusted credit risk weighted assets			6,856,899	6,401,046
Market risk equivalent assets			686,455	282,391
Operation risk equivalent assets			1,168,631	1,175,191
Total risk weighted assets			8,711,985	7,858,628

Notes (continued)

4. Nature and extent of risks arising from financial instruments (continued)

b) Capital management (continued)

	2020 KSh '000	2019 KSh '000
Tier 1 capital	2,545,544	2,606,843
Tier 2 capital	108,900	98,233
Total capital	2,654,444	2,705,076
Total deposit liabilities	9,748,877	9,187,522

	Actual ratios		Minimum requirement	
	2020 %	2019 %	2020 %	2019 %
Core capital to total risk weighted assets	29	33	10.5	10.5
Total capital to total risk weighted assets	30	34	14.5	14.5
Core capital to deposit liabilities	26	28	8.0	8.0

The Kenyan Banking Act also sets out the minimum core capital requirement of KSh 1 Billion (2019: KSh 1 Billion) which the bank fully complied with.

5. Interest income

	2020 KSh '000	2019 KSh '000
Loans and advances to customers	853,118	868,758
Interest income on impaired loans and advances	166,042	69,030
Placements with and loans and advances to banking institutions	27,656	31,733
Financial assets at amortised cost	259,040	148,205
	1,305,856	1,117,726

Notes (continued)

6. Interest expense

	2020 KSh '000	2019 KSh '000
Customer deposits	606,729	599,967
Deposits from other banking institutions	82	3
Lease liabilities	6,382	10,182
	613,193	610,152

7. Net fee and commission income

	2020 KSh '000	2019 KSh '000
Fee and commission income:		
Loans and advances	98,958	103,125
Other fees and commissions	18,953	20,642
	117,911	123,767
Fee and commission expense:		
Other	(4,599)	(6,772)
	113,312	116,995

8. Net trading income

	2020 KSh '000	2019 KSh '000
Net foreign exchange trading income	34,443	13,689
Net foreign exchange loss	(3,816)	(4,055)
	30,627	9,634

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

	2020 KSh '000	2019 KSh '000
Equity investments	(2,931)	(4,774)

10. Other income

	2020 KSh '000	2019 KSh '000
Dividend income from financial assets at fair value through profit or loss	129	1,577
(Loss)/profit on sale of financial assets at fair value through profit or loss	(52)	2
Profit on disposal of property and equipment	-	66
Other sundry income	1,052	1,831
	1,129	3,476

Notes (continued)

11. Net impairment losses on loans and advances

	2020 KSh '000	2019 KSh '000
Net increase in specific provision charged to profit and loss account (Note 17(b))	351,281	131,941
Recoveries from loans and advances written off	(6,500)	(2,543)
Charge to the profit and loss account	344,781	129,398

12. Profit before tax expense

(a) Items charged

The following items have been charged in arriving at profit before tax expense:

	2020 KSh '000	2019 KSh '000
Employee benefits expense (Note 12(b))	192,675	192,701
Depreciation of property and equipment	27,753	35,312
Depreciation of right – of – use assets	47,108	29,252
Operating lease rentals expense	(402)	5,129
Amortisation of intangible assets	5,846	4,274

(b) Employee benefits expense

	2020 KSh '000	2019 KSh '000
Wages and salaries	185,657	185,936
Retirement benefit costs:		
– Defined benefit scheme	6,786	6,481
– National Social Security Fund	232	284
	192,675	192,701

The average number of persons employed during the year, by category, were:

	Number	Number
Non-management	49	48
Management and administration	49	55
Total	98	103

Notes (continued)

13. Tax expense

	2020 KSh '000	2019 KSh '000
Current income tax	12,434	-
Deferred tax credit (Note 24)	2,833	-
Deferred tax expense/ (income) relating to change in tax rate (Note 24)	(406)	86,401
Income tax expense	14,861	86,401
The tax on the Company's profit/(loss) before income tax differs from the theoretical amount that would arise using the statutory income tax rate of 25% (2019: 30%) as follows:		
Profit before income tax	42,581	64,453
Tax calculated at a rate of 25% (2019: 30%)	10,645	19,336
Tax effect of:		
Income not subject to tax	(3,145)	(6,218)
Expenses not deductible for tax purposes	6,955	2,153
Effect of difference in current taxes and deferred tax rate	406	-
Deferred tax on losses not recognised	-	71,130
Income tax expense	14,861	86,401

The statutory tax rate was reduced from 30% to 25% for the year of income 2020 by the Tax Laws (Amendment) Act, 2020. The Tax Laws (Amendment) (No.2) Act, 2020 increased the rate back to 30% with effect from 1st January 2021.

14. 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.

Net profit attributable to shareholders	27,720	(21,948)
Weighted average number of ordinary shares in issue during the year ('000)	124,552	124,541
Basic earnings per share	0.22	(0.18)

There were no potentially dilutive shares outstanding at 31st December 2020 and 31st December 2019. Diluted earnings per share is therefore the same as basic earnings per share.

15. Cash and balances with Central Bank of Kenya

	2020 KSh '000	2019 KSh '000
Cash in hand (Note 30)	168,855	222,569
Balances with Central Bank of Kenya:		
Restricted balances (Cash Reserve Ratio)	409,935	483,573
Unrestricted balances (Note 30)	197,079	353,545
	775,869	1,059,687

Notes (continued)

15. Cash and balances with Central Bank of Kenya (continued)

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 2020 the Cash Reserve Ratio requirement was 4.25% (2019: 5.25%) of all customer deposits. These funds are not available to finance the Bank's day to day operations.

16. Deposits and balances due from banking institutions (Note 30)	2020 KSh '000	2019 KSh '000
Balances with banking institutions in Kenya	470,269	669,504
Balances with banking institutions abroad	938,356	1,203,873
	1,408,625	1,873,377

17. Loans and advances to customers

a) Loans and advances to customers		
Overdrafts	3,624,176	3,480,179
Commercial loans	3,924,223	3,737,806
Gross loans and advances to customers	7,548,399	7,217,985
Less: Provision for impaired loans and advances (Note 17(b))	(470,081)	(406,186)
Net loans and advances	7,078,318	6,811,799
b) Impairment losses on loans and advances		
At 1st January	406,186	343,531
Net increase in provision for impairment charged to profit and loss account (Note 11)	351,281	131,941
Interest income on impaired loans and advances	(166,042)	(69,030)
Provisions utilised during the year for write off	(121,344)	(256)
At 31st December	470,081	406,186

c) Concentration of risk

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

	2020 KSh 000	2020 %	2019 KSh 000	2019 %
Manufacturing	1,782,515	24	1,443,285	20
Wholesale, retail trade and hotels	4,110,659	54	3,697,380	51
Transport and communications	197,285	3	190,853	3
Agriculture	216,089	3	214,090	3
Business services	158,458	2	85,513	1
Building, construction and real estate	880,430	11	1,275,601	18
Social, community and personal service	202,963	3	311,263	4
	7,548,399	**100**	**7,217,985**	**100**

Notes (continued)

18. Government securities at amortised cost

	2020 KSh '000	2019 KSh '000
Government Securities – Treasury bills	474,648	1,103,863
Government Securities – Treasury bonds	2,750,157	1,041,976
	3,224,805	2,145,839
Financial assets at amortised cost (continued)		
Maturing:		
– Within 1 year	660,088	1,548,160
– Over 1 year	2,564,717	597,679
	3,224,805	2,145,839

Included in the above are financial assets with a carrying amount of KSh 100,000,000 (2019: KSh 100,000,000) that is held by the Central Bank of Kenya under lien as security for Letters of Credit.

The fair value of the Treasury Bonds carried at amortised cost at the balance sheet date, based on quoted prices (unadjusted) in active markets for identical assets was KSh 2,665,000,000 (2019: KSh 1,160,000,000).

19. Financial assets at fair value through profit or loss

	2020 KSh '000	2019 KSh '000
Equities	20,548	24,625

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

20. Other receivables

	2020 KSh '000	2019 KSh '000
Clearing account	46,103	37,852
Prepayments	38,906	36,786
Other receivables	18,169	4,619
	103,178	79,257

21. Intangible assets (software costs)

	2020 KSh '000	2019 KSh '000
Cost		
At 1st January	25,605	24,024
Additions	46,098	1,581
At 31st December	71,703	25,605
Amortisation		
At 1st January	20,257	15,983
Charge for the year	5,846	4,274
At 31st December	26,103	20,257
Net book amount	45,600	5,348

The annual amortisation rate used is 33.3%.

Notes (continued)

22. Property and equipment

	Computers, copiers & fax KSh'000	Motor vehicles KSh'000	Furniture, fittings & equipment KSh'000	Total KSh'000
At 1st January 2019				
Cost or valuation	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
Year ended 31st December 2019				
Opening carrying amount	2,883	3,332	86,238	92,453
Additions	205	–	7,189	7,394
Depreciation charge	(1,211)	(883)	(33,218)	(35,312)
Closing carrying amount	1,877	2,449	60,209	64,535
At 31st December 2020				
Cost	20,790	7,678	285,972	314,440
Accumulated depreciation	(18,913)	(5,229)	(225,763)	(249,905)
Net carrying amount	1,877	2,449	60,209	64,535
Year ended 31st December 2020				
Cost				
Opening carrying amount	1,877	2,449	60,209	64,535
Additions	3,322	–	3,190	6,512
Depreciation charge	(1,043)	(883)	(25,827)	(27,753)
At 31st December 2020	4,156	1,566	37,572	43,294
At 31st December 2020				
Cost	24,112	7,678	289,162	320,952
Accumulated depreciation	(19,956)	(6,112)	(251,590)	(277,658)
Net carrying amount	4,156	1,566	37,572	43,294

The annual depreciation rates used are as follows:

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

Notes (continued)

23. Right - of - use assets

	Land and buildings KSh '000 2020	Land and buildings KSh '000 2019
Cost		
At 1st January	144,237	125,377
Additions	11,579	18,860
Prior year adjustments	(7,036)	-
At 31st December	148,780	144,237
Depreciation		
At 1st January	29,252	-
Depreciation charge	38,759	29,252
Prior year adjustments	8,349	-
At 31st December	76,360	29,252
Carrying amount at 31st December	72,420	114,985

The Bank leases various offices. The leases of offices and warehouses are typically for periods of between 3 and 7 years, with no options to renew. None of the leases contains any restrictions or covenants other than the protective rights of the lessor or carries a residual value guarantee.

In the statement of cash flows, the amount for payments for right-of-use assets represents:

	2020 KSh'000	2019 KSh'000
Lease liabilities payments - Principal	38,596	32,238
Lease liabilities payments - Interest	6,382	10,182
Cash flow	44,978	42,420

For information on the related lease liabilities, see Note 26.

24. Deferred income tax

Deferred income tax is calculated using the enacted tax rate of 30%, which is the enacted rate applying from 1st January 2021 (2019: 30%). However, the statutory tax rate for the year ended 31st December 2020 was 25% (2019: 30% (see Note 13).

Deferred tax assets/(liabilities), and the deferred tax charge/(credit) in the profit and loss account are attributable to the following items:

Notes (continued)

24. Deferred income tax (continued)

Year ended 31st December 2020

	At 1st January 2020 KSh'000	Effect of Change in tax rate	(Charge) to profit & loss KSh'000	At 31st December 2020 KSh'000
Deferred income tax asset				
Property and equipment	26,210	(528)	3,696	29,378
Intangible assets	620	460	(3,219)	(2,139)
Right - of - use assets	(34,496)	(12,237)	25,007	(21,726)
Lease liabities	33,600	11,812	(22,028)	23,384
Staff leave accrual	1,346	75	(524)	897
Provisions for impaired loans and advances	187,044	824	(5,765)	182,103
Tax losses carried forward	71,130	-	(71,130)	-
Net deferred tax asset before allowance	285,454	406	(73,963)	211,897
Deferred tax on losses not recognised	(71,130)	-	71,130	-
Net deferred tax asset	214,324	406	(2,833)	211,897

Year ended 31st December 2019

	At 1st January 2019 KSh'000	(Charge) to profit & loss KSh'000	At 31st December 2019 KSh'000
Deferred income tax asset			
Property and equipment	22,487	3,723	26,210
Intangible assets	351	269	620
Right - of - use assets	-	(34,496)	(34,496)
Lease liabities	-	33,600	33,600
Staff leave accrual	1,400	(54)	1,346
Provisions for impaired loans and advances	168,170	18,874	187,044
Tax losses carried forward	108,317	(37,187)	71,130
	300,725	(15,271)	285,454
Deferred tax on losses not recognised	-	(71,130)	(71,130)
Net deferred tax asset	300,725	(86,401)	214,324

The deferred tax assets and liabilities relate to income tax in the same jurisdiction, and the law allows net settlement. Therefore, they have been offset in the balance sheet.

Notes (continued)

25. Deposits from customers

	2020 KSh'000	2019 KSh'000
Call deposits	3,467	775
Current and demand accounts	868,935	667,082
Savings accounts	520,354	487,544
Term deposits	8,356,121	8,032,121
	9,748,877	9,187,522

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

	2020 KSh'000	2020 %	2019 KSh'000	2019 %
Individuals	6,523,927	67	6,455,473	71
Non-profit institutions	204,185	2	219,535	2
Private companies	2,564,765	26	2,158,383	23
Insurance companies	456,000	5	354,131	4
	9,748,877	100	9,187,522	100

Included in customer deposits were deposits amounting to KSh,978,616,000 (2019: KSh 2,225,147,000) that were held as collateral for loans and advances.

26. Lease liabilities

	2020 KSh'000	2019 KSh'000
Lease liabilities	77,946	111,999
The total cash outflow for leases in the year was:		
Payments of principal portion of the lease liability	38,596	32,238
Interest paid on lease liabilities	6,382	10,182
	44,978	42,420

For more information on the nature of the leases entered into and the related right-of-use assets, see Note 23.

Notes (continued)

27. Other payables

	2020 KSh'000	2019 KSh'000
Outstanding bankers cheques	14,909	9,769
Staff leave accrual	2,990	4,487
Sundry creditors	56,507	36,828
	74,406	51,084

28. 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 2019 and 31st December 2019	124,540,569	2,490,811	412,819	9,189
Shares allotment	10,965	220	-	(220)
At 31st December 2020	124,551,534	2,491,031	412,819	8,969

The total number of authorised ordinary shares is 175,000,000 (2019: 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.

29. Regulatory reserve

	2020 KSh '000	2019 KSh '000
At 1st January	222,004	189,373
Transfer from retained earnings	91,446	32,631
At 31st December	313,450	222,004

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.

Notes (continued)

30. Cash and cash equivalents

	2020 KSh'000	2019 KSh'000
For the purposes of the cash flow statement, cash and cash equivalents comprise the following:		
Cash in hand (Note 15)	168,855	222,569
Unrestricted cash balances with Central Bank of Kenya (Note 15)	197,079	353,545
Placements with and loans and advances to banking institutions (Note 16)	1,408,625	1,873,377
	1,774,559	2,449,491

31. 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:

	2020 KSh'000	2019 KSh'000
Letters of credit and acceptances	110,161	93,064
Guarantees	402,978	272,589
	513,139	365,653

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.

b) Pending litigation and claims

	2020 KSh'000	2019 KSh'000
Pending litigation and claims	191,091	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.

Notes (continued)

31. Off balance sheet contingencies and commitments (continued)

c) Commitments

Undrawn formal stand-by facilities, credit lines and other commitments to lend at 31st December 2020 totalled Ksh. 567,532,000 (2019: KSh 744,988,000).

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.

32. 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 31) include guarantees and letters of credit of KSh 4,565,000 (2019: KSh 10,444,000) which have been issued to related companies.

The following transactions were carried out with related parties:

a) Outstanding loans and advances	Directors		Related companies	
	2020	2019	2020	2019
	KSh'000	KSh'000	KSh'000	KSh'000
At 1st January	266,476	-	1,027,065	1,092,252
Advances during the year	58,140	398,715	2,740,903	1,925,868
Interest charged during the year	24,082	27,757	158,106	154,478
Repayments during the year	(290,368)	(159,996)	(2,731,693)	(2,145,533)
At 31st December	58,330	266,476	1,194,381	1,027,065
Contingent liabilities	-	-	4,565	10,444

As at 31 December 2020, loans and advances to staff amounted to KSh.31,115,000 (2019: KSh 36,099,000).

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.

Notes (continued)

32. Related party transactions (continued)

	Directors 2020 KSh'000	Directors 2019 KSh'000	Related companies 2020 KSh'000	Related companies 2019 KSh'000
b) Deposits				
At 1st January	420,378	457,368	245,508	14,836
Deposits received during the year	4,838,378	4,605,173	2,500,296	2,666,420
Interest paid during the year	20,312	23,706	6,311	4,001
Withdrawals during the year	(4,841,695)	(4,665,869)	(2,734,888)	(2,439,749)
At 31st December	437,373	420,378	17,227	245,508
c) Directors' remuneration (key management compensation)				
Directors' remuneration				
- Fees			5,686	5,146

33. 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 2020.

Amendments to IFRS 16 titled Covid-19 Related Rent Concessions (issued in May 2020)

The amendments, applicable to annual periods beginning on or after 1 June 2020, permit lessees, as a practical expedient, not to assess whether particular rent concessions occurring as a direct consequence of the covid-19 pandemic are lease modifications and instead to account for those rent concessions as if they are not lease modifications.

Amendments to IAS 37 titled Onerous Contracts - Cost of Fulfilling a Contract (issued in May 2020)

The amendments clarify that for the purpose of assessing whether a contract is onerous, the cost of fulfilling the contract includes both the incremental costs of fulfilling that contract and an allocation of other costs that relate directly to fulfilling contracts. They are effective for contracts for which an entity has not yet fulfilled all its obligations on or after 1 January 2022.

Amendments to IAS 16 titled Property, Plant and Equipment: Proceeds before Intended Use (issued in May 2020)

The amendments, applicable to annual periods beginning on or after 1 January 2022, prohibit a company from deducting from the cost of property, plant and equipment amounts received from selling items produced while the company is preparing an asset for its intended use. Instead, a company will recognise such sales proceeds and related cost in profit or loss.

Notes (continued)

33. New and revised financial reporting standards (continued)

Amendment to IFRS 1 titled Subsidiary as a First-time Adopter (issued in May 2020 as part of the Annual Improvements to IFRS Standards 2018-2020)

The amendment, applicable to annual periods beginning on or after 1 January 2022, provides a subsidiary that becomes a first-time adopter later than its parent with an exemption relating to the measurement of its assets and liabilities. The exemption does not apply to components of equity.

Amendment to IFRS 9 titled Fees in the 10 per cent Test for Derecognition of Financial Liabilities (issued in May 2020 as part of the Annual Improvements to IFRS Standards 2018-2020)

The amendment, applicable to annual periods beginning on or after 1 January 2022, to IFRS 9 clarifies the fees that a company includes when assessing whether the terms of a new or modified financial liability are substantially different from the terms of the original financial liability.

Amendment to IAS 41 titled Taxation in Fair Value Measurements (issued in May 2020 as part of the Annual Improvements to IFRS Standards 2018-2020)

The amendment, applicable to annual periods beginning on or after 1 January 2022, to IAS 41 removed the requirement to exclude taxation cash flows when measuring fair value. This amendment aligned the requirements in IAS 41 on fair value measurement with those in other IFRS Standards.

IFRS 17 Insurance Contracts (issued in May 2017)

The new standard, effective for annual periods beginning on or after 1st January 2023, 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 IAS 1 titled Classification of Liabilities as Current or Non-current (issued in January 2020)

The amendments, applicable to annual periods beginning on or after 1 January 2023, clarify a criterion in IAS 1 for classifying a liability as non-current: the requirement for an entity to have the right to defer settlement of the liability for at least 12 months after the reporting period.

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.
The following new and revised standards have become effective for the first time in the financial year beginning 1st January 2020:

Notes (continued)

33. New and revised financial reporting standards (continued)

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.

Amendments to IFRS 9, IAS 39 and IFRS 7 titled Interest Rate Benchmark Reform (issued in September 2019)

The amendments, applicable to annual periods beginning on or after 1 January 2020, modify specific hedge accounting requirements so that entities apply those hedge accounting requirements assuming that the interest rate benchmark on which the hedged cash flows and cash flows of the hedging instrument are based is not altered as a result of interest rate benchmark reform.

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