CONSOLIDATED BANK OF KENYA
LIMITED AND ITS SUBSIDIARIES

ANNUAL REPORT & FINANCIAL STATEMENTS

FOR THE YEAR ENDED 31 DECEMBER 2019

Consolidated Bank
Growing with you

Contents

The Bank celebrated Customer Service Week 2019 from 7th - 11th October 2019. Below are the photos from across the Branches.

Thomas Kiyai-CEO (Center) serving the staff from the Treasury team with cake during the Customer Service week 2019

Japhet Kisilu- CCO leads the Koinange staff and customers to mark the Customer Service week 2019

Staff from Harambee branch led by their Team leader Kennadoh Odonde (Seated on the far right) pose for a photo during the Customer Service week

Embakasi Branch Customer led by the Team leader Jackson Talibong (on the right)cut a cake to mark the Customer Service Week

Thika Branch Team Leader serves her customers with cake to make the end of Customer Service Week 2019

Happy Customer Service Week 2019

Board of Directors

Current

Dr. Iyaya Wanjala -	Chairman
Thomas Kiyai -	Chief Executive Officer
Cabinet Secretary -	National Treasury
Managing Trustee -	NSSF
Hon. Yusuf Chanzu	
Dr. Kennedy Otiso	
Miriam Cherogony	
Dr. Nathan Psiwa	
Hardlyne Lusui	

DR. IYAYA WANJALA
CHAIRMAN

Dr. Iyaya Wanjala was appointed as Chairman of the Consolidated Bank Board of Directors on 6th June, 2018. He has a Doctorate in Applied Mathematics from Kenyatta University where his Thesis was 'Investigation of Some Singular Cauchy Problems'. He also has a Master of Science degree in Applied Mathematics from the University of Nairobi. Dr. Wanjala Iyaya has done several scholarly publications in Kenya. He is currently a Senior Lecturer at Multimedia University of Kenya. He has also served as a Lecturer at Kenyatta University and an Assistant Lecturer at Maseno University College. He has served in his own capacity as Chairman of Benevolent fund of Multimedia University of Kenya and as a Chairman of the Mathematics department. He has supervised several Masters and PHD students in various

MR. THOMAS KIPKEMEI KIYAI
CHIEF EXECUTIVE OFFICER

Thomas Kipkemei Kiyai joined Consolidated Bank in April 2015. He has over 20 years of banking and finance experience having joined Consolidated Bank of Kenya from Kenya Commercial Bank, where he served as Director, Financial planning and Control. He holds a Bachelors of Commerce Degree in Accounting and a Masters of Business Administration Degree in Corporate Finance from the University of Nairobi. In addition to this, he is also an alumni of the Oxford University Management & Leadership Development Programme. Thomas Kiyai is a member of the Institute of Certified Public Accountants of Kenya (ICPAK).

WAKONYO IGERIA
COMPANY SECRETARY

Wakonyo Igeria was appointed as the Head of Legal Services and Company Secretary in June 2004. She holds a Bachelor of Laws Degree and a Diploma in Law from the Kenya School of Law. She is an Advocate of the High Court of Kenya with 29 years' experience, a Commissioner for Oaths and Notary Public and a Certified Public Secretary (Kenya). Wakonyo Igeria is a member of the Law Society of Kenya and the Institute of Certified Public Secretaries of Kenya.

DR. ANTHONY OMERIKWA - MANAGING TRUSTEE, NSSF
INSTITUTIONAL DIRECTOR

Dr. Anthony Omerikwa is the CEO/Managing Trustee of the National Social Security Fund. Prior to his current position, he served as the Acting General Manager Operations in the same institution overseeing Information Technology, Human Resource, Administration and Procurement functions. He holds a Doctoral degree from the University of Georgia, a specialist advanced degree in labour, workforce development and education and a Master of Science degree in Human Resource Development both from Pittsburgh State University, a Bachelor of Arts degree in Economics from Kenyatta University and a Diploma in Data Processing and Management from Strathmore College. Dr. Omerikwa is an associate member of the Institute of Human Resource Management and Institute of Directors.

HON. UKUR YATANI KANACHO – CABINET SECRETARY, NATIONAL TREASURY
INSTITUTIONAL DIRECTOR

Hon. Ukur Yatani Kanacho has over 27 years experience in public administration, politics, diplomacy and governance in the public sector since 1992. Before his appointment as Cabinet Secretary for the National Treasury & Planning he served as the Cabinet Secretary for Labour and Social Protection, Member of Parliament for North Horr constituency, Assistant Minister for Science and Technology and as a pioneer Governor of Marsabit County.

Between June 2009 and October 2012, he served as Kenya's Ambassador to Austria. In this position, he aggressively pursued and advanced Kenya's foreign interests. He has also held senior leadership positions at various diplomatic and international agencies such as International Atomic Energy Agency (IAEA), United Nations Organization on Drugs and Crimes (UNODC), UNIDO, UNTOC, Vice President of Convention on Crime Prevention and Criminal Justice (CCPJ), and chair of African Group of Ambassadors among others.

HARDLYNE LUSUI
MEMBER OF THE BOARD

Hardlyne Lusui was appointed as a Member of Board of Directors at Consolidated Bank of Kenya Limited on 19th December 2018 vide gazette notice No. 13234. Having come from World Poles Ltd as Marketing and Credit Control Manager, she has over 15 years of experience in the banking and finance sector. Remarkably, she has worked as a Project Manager at Israel for Africa and previously for I&M Bank Limited, National Bank of Kenya, Equity Bank Kenya Limited and Cadbury Kenya Ltd. She holds a degree in Information Science from Kenya Methodist University, alongside two First Class Honors from the Institute of Banking and Business Communication in Corporate Banking, Credit Analysis and IBBC-Retail Banking Courses.

BOARD OF DIRECTORS

DR. KENNEDY NTABO OTISO
MEMBER OF THE BOARD

Dr. Kennedy Ntabo Otiso, PhD, was appointed to the Board of Consolidated Bank on the 20th of September, 2018. He holds a Doctor of Philosophy in Business Management (Marketing Option), a Master of Business Management (Marketing Option) all from Moi University. He has a bachelor's degree in Business Administration (Marketing Option-Cum Laude) graduated from the University of Eastern Africa, Baraton.He has over 10 years of experience serving in different capacities in various institutions of higher learning in Kenya. Notably he has served at Kibabii University as a lecturer as well as a founding Chairman of the Department of Business Administration and Management. In addition he served as an assistant Lecturer at the University of Eastern Africa, Baraton. He has also served as Chief Principal at Elgonview College. Dr. Otiso currently serves as a lecturer in the School of Business and Management Sciences in the University of Eldoret. He has published widely scholarly works; he has reviewed peer academic journals and actively attended several international conferences. He has supervised and examined many postgraduate students from various Universities in Kenya. He is the current Chairman, Board of Management, Ntana High School in Nyamira County. Dr. Otiso is a trained professional marketer as well as a member of the Marketing Society of Kenya and Kenya Institute of Management respectively.

MIRIAM CHEROGONY
MEMBER OF THE BOARD

Miriam Jerotich Cherogony was appointed to the Board of Consolidated Bank on 20th September 2018. She has over 20 years' experience in research, design & formulation, monitoring & evaluating, development plans and policies as well as a wide knowledge of office work and managing people. Ms. Cherogony has acquired a wide knowledge in strategy development, project and procurement management.She has also worked in various capactities Internationally in the following countries namely: Canada, Ethiopia, Eritrea, Ghana, Kenya, Lesotho, Mozambique, Nigeria, Rwanda, Sierra Leone, Somaliland, South Africa, Swaziland, Tanzania, Uganda, and Zambia. Ms. Cherogony has worked as the Africa Regional Manager - Global Development Incubator, Team Leader & Development Finance Specialist-Rural Finance Knowledge Management Partnership (KMP), Team Leader & Knowledge Management Specialist – IFAD Africa Grant, Programme Coordinator at African Rural and Agricultural Association (AFRACA), Nairobi Kenya. She has also served as a Senior Research Officer at K-Rep Development Agency Nairobi, Kenya , Senior Manager-Rural Financial Services Department and Manager-Rural Financial Services Department among other notable institutions. She has a Master of Science and a Bachelor of Science degree in Agricultural Economics both from the University of Manitoba, Canada.

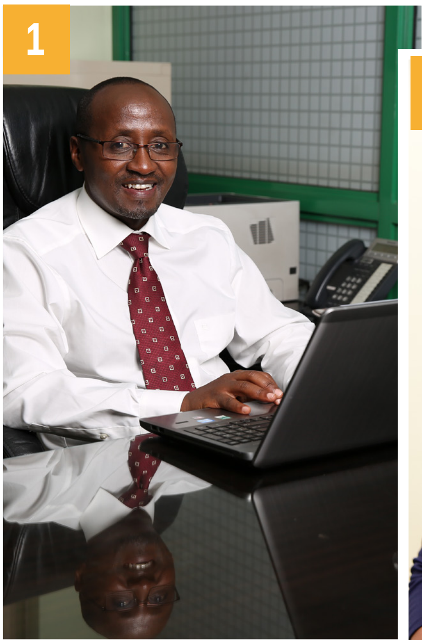
DR. NATHAN KITIO PSIWA
MEMBER OF THE BOARD

Dr. Nathan Kitio Psiwa was appointed to the Board of Consolidated Bank on 20th September 2018. He has over 15 Years' experience in Orthodontics. He has served in three boards, two as a member and one as a Chairperson. He has been a Chairperson and a Member of Council at Rongo University and a Chairperson at Kenya Industrial Research and Development Institute (KIRDI). He is currently a lecturer at University of Nairobi, Department Of Paediatric Dentistry And Orthodontics. Dr. Nathan Psiwa holds a Certificate in Audit and Risk Management from Association of Internal Auditors Kenya (AIK) and a Certificate in Governance from Kenya School of Governance (KSG). He holds a Master of Science in Dental Surgery (Ortho) from University of the Western Cape in South Africa and a Bachelor of Dental Surgery from the University of Nairobi. He is currently a member of the following bodies: the Kenya Dental Association, the Kenya Medical Association, the Orthodontic Society of Kenya and Institute of Directors (IOD-K). He is an Associate member of South African Association of Orthodontists (SASO) and Tanzania Medical Association.

HON. YUSUF KIFUMA CHANZU
MEMBER OF THE BOARD

Hon. Yusuf Kifuma Chanzu, CBS, OGW, HSC was appointed to the Board of Consolidated Bank on 20th September, 2018. He has over 30 years of public service. He has been a Member of Parliament, Vihiga Constituency from December 2007 to August 2017 where he was Involved in all legislative work of Parliament, performed the oversight role, and representation. He has served in various capacities in the government as Commissioner with Communications Commission of Kenya, Assistant Minister for Labour & Human Resource Development where he was Involved in the management and running of the Ministry, Assistant Minister for Energy where he was Involved in the management and running of the Ministry, Assistant Minister for Water Resources where he was Involved in the management and running of the Ministry. He has also been an Advisor Quipcons Associates, Consulting Quantity Surveyors & Project Managers. He was also a Chief Quantity Surveyor, Ministry of Public Works/ Local Government.He has been honored by the Head of State with The First Class Order of the Chief of Burning Spear (CBS), The Order of Grand Warrior (OGW) and The Head of State Commendation (HSC) for his work in public service. He holds a Master of Science in Construction Management (Corporate Strategy) from Heriot - Watt University, Edinburgh. He also has an undergraduate degree Course, B.A Building Economics (Honours),University of Nairobi. He is a Corporate Member of the Architectural Association of Kenya (Quantity Surveying), a Registered Quantity Surveyor with the Board of Registration of Architects and Quantity Surveyors Kenya and Fellow of the Institute of Quantity Surveyors of

SENIOR MANAGEMENT



1. Japheth Kisilu
   Chief Commercial Officer

2. Wakonyo Igeria
   Company secretary & Head of Legal Services

3. Joseph Njuguna
   Head of Finance & Administration

4. Erastus Gachoya
   Head of Corporate Banking

5. Jacinta Lwanga
   Head of Human Resource

6. Joshua Kagia
   Head of Treasury

SENIOR MANAGEMENT

7. Josephine Kioko
   Head of Retail & SME

8. Edward Nthuli
   Head of Operations

9. Julie Odadi
   Ag. Head of Credit

10. George Rutto
    Head of Internal Audit

11. Harrison Muthoka
    Ag. Head of Risk & Compliance

12. Martin Omido
    Head of ICT

Chairman’s
Statement

IYAYA WANJALA
Chairman

I am pleased to present to you the Annual Report and Financial Statements for the year ended December 31, 2019. This is against a backdrop of tough year for the bank characterised by a difficult macroeconomic environment.

Macroeconomic Overview

The real Gross Domestic Product (GDP) is estimated to have expanded by 5.4% in 2019 compared to a growth of 6.3 % in 2018. The growth was spread across all sectors of the economy but was more pronounced in service-oriented sectors. Financial services sub-sector grew by 5.7 % in 2019 relative to 4.8 % recorded in 2018. Domestic credit improved to 7.5% in 2019 compared to a growth of 6.4 % in 2018. The capping of bank interest rates previously enshrined in section 33B of the 2016 Banking Act, was repealed through enactment of the Finance Act, 2019. This is meant to enhance access to credit by the private sector as commercial banks adopt the risk based credit pricing under the Kenya Banking Sector Service Charter.

Annual average inflation rate rose to 5.20 % in 2019 compared to 4.69 % recorded in 2018 but remained within the medium-term target of 5.0 %, with a range of plus or minus 2.5 %. In a bid to boost economic growth Central Bank of Kenya continued to ease monetary policy by reducing the CBR to 8.5% in December 2018 from 9% in 2018.

Bank's Performance

The bank operated under severe capital challenges for the first 9 months of the year when core capital position declined to minus 166 million in September 2019 from Kshs 58 million in December 2018. Total assets declined by 8% to Kshs 11.9 billion in 2019 from Kshs 12.9 billion in 2018. Net advances significantly declined by 13% to Kshs 7.4 billion from Kshs 8.4 billion in 2018. Customer deposits however increased by 2% to Kshs 8.8 billion from Kshs 8.6 billion in 2018 confirming the customer confidence in the bank despite the challenges.

> *"The fresh capital injection not only enabled the bank to settle the medium term note of Kshs 1.52 billion but also improved the bank's capital position and prudential capital ratios."*

The Bank however made a major breakthrough on 22 October 2019 when the National Treasury, the majority shareholder injected fresh capital of Kshs 1.6 billion into the business. The fresh capital injection not only enabled the bank to settle the medium term note of Kshs 1.52 billion but also improved the bank's capital position and prudential capital ratios. The bank's total capital and the core capital to risk weighted assets ratios improved to 13.5% (regulatory minimum 14.5%) and 11.4% (regulatory minimum 10.5%) in December 2019 from 1% and 0.5% respectively in December 2018. The National Treasury's share holding in the bank increased to 93.4% from 85.8% following this injection of capital.

With the improved capital position the bank has now crafted a 3 year strategy to turnaround the bank performance from loss making to profitability by 2021.

Corporate Social Responsibility

The bank recognizes its corporate responsibility commitments and is determined to sustain high standards of corporate citizenship by preserving and promoting human values as well as conserving the environment for sustainability. The bank continued its partnership with Kenya Forest Service and other stakeholders and planted over 5,000 trees in various forests across the country. The bank also assisted various primary schools and institutions with water tanks and other infrastructure to support water harvesting.

Conclusion

On behalf of the board and management I wish to express the Bank's utmost gratitude to the National Treasury for supporting the bank through the fresh capital injection of Kshs 1.6 billion. I also take this opportunity to thank our customers, staff, suppliers and fellow board members for their dedicated contribution and support towards the growth of the Bank.

Dr. Iyaya Wanjala
Chairman
30 March 2020

Message from the CEO

THOMAS KIPKEMEI KIYAI
Chief Executive Officer

Macroeconomic Overview

Real GDP is estimated to have grown by 5.4% in 2019 driven by household consumption and investment on the demand side and services on the supply side (such as public administration, information technology, finance and insurance, and transport and storage). GDP was however down from 6.3% in 2018, caused mainly by unfavourable weather and reduced government investment. At 5.2%, inflation remains within the Central Bank's 5 ± 2.5% target band.

Bank's Performance

Total assets declined by 8% to Kshs 11.9 billion in 2019 from Kshs 12.9 billion in 2018. Net advances declined by 13% to Kshs 7.4 billion from Kshs 8.4 billion in 2018. The deposits however increased by 2% to Kshs 8.8 billion from Kshs 8.6 billion in 2018.

Interest income declined by 13% to Kshs 1.2 billion from Kshs 1.4 billion in 2018 due to the shrinking balance sheet occasioned by the capital challenges highlighted above. Total Interest expense however declined by 11% to Kshs 675 million in December 2019 from Kshs 758 million in December 2018 due to lower cost of deposits and also reduction on borrowing cost following repayment of the medium term note in October 2018. Non funded income declined by 9% to Kshs 691 million from Kshs 761 million in 2018. Overall the operating income declined by 12% to Kshs 1.2 billion from Kshs 1.4 billion. Loan loss provision increased by 13% to Kshs 416 million from Kshs 368 million in 2018 due to increase in non-performing loans to 30.7% in 2019 from 25.3% in 2018.

Other operating expenses were steady at Kshs 1.3 billion. The bank recorded an after loss of Kshs 531 million in 2019 compared to a loss of Kshs 540 million in 2018.

This performance comes against a backdrop of severe capital challenges which severely constrained the bank from implementing the business plan for 9 months up to September 2019. During this period the bank's core capital declined to minus Kshs 166 million in September 2019 from Kshs 58 million in December 2018. With negative core capital it was extremely difficult to meet customer needs and hence the balance sheet continued to decline as customers sought facilities from competition.

On 22 October 2020 the bank made a major breakthrough when the National Treasury injected fresh capital of Kshs 1.6 billion. This enabled the bank to settle medium term note of Kshs 1.52 billion which matured on 22 July 2019 and maturity was extended to 22 October 2019. The retirement of the medium term note which the bank was paying interest of 13.25% is expected to positively improve the net interest margin as the bank will now turn to more affordable sources of funding from customer deposits.

> *"Following recapitalization of the bank in October 2019 the focus has now shifted to implementation of the bank's three year turnaround strategy developed in November 2019"*

The bank is closely working with the National Treasury and Privatisation Commission to speed up the privatisation process to ensure the bank can readily access capital from the capital markets for sustainable growth.

Strategic Focus and Turnaround

Following recapitalization of the bank in October 2019 the focus has now shifted to implementation of the bank's three year turnaround strategy developed in November 2019.

The strategy which is anchored on the pillars of technology and innovation, people and culture, business growth and profitability is expected to grow the balance sheet and turn around the bank from the current loss making position into profitability.

The world is currently battling the covid 19 pandemic which started in Wuhan China in December 2019 and rapidly spread across the globe. As at 15th August 2020, over 22 million have been infected globally with over 700,000 people succumbing to the disease. Locally in Kenya over 30,000 people have been infected while 487 have succumbed to the pandemic.

The pandemic has led to unprecedented disruption and slowdown in social, economic activities and supply chains. This has not only negatively affected business but also led to loss of jobs and sources of livelihood. The bank has implemented the pandemic containment measures directed by the Ministry of Health and also invoked its crisis management process to ensure business continuity. The bank has also embraced the new normal under covid 19 which entail part of the team working from home, increased use of the digital platform for customer transactions and interactions and adoption of virtual platforms for meetings and office interactions.

Corporate Social Responsibility (CSR)

Our corporate social responsibility is firmly anchored on the following values of our corporate brand;

- Customer-primacy: the customer is at the center of our service delivery.
- Social responsibility: as a Bank, we are sensitive to our responsibility to the environment and the community in which we operate.

The CSR theme for 2019 was: ***'Sustainability and Growth through CSR'***. The bank's CSR activities mainly focused on tree planting as directed by the President through circular No. DENR/EMC/33(31). In partnership with Kenya Forest Service and other stakeholders the bank planted over 5,000 trees in various forests across the country. To improve water harvesting and conservation, the bank also supported various schools across the country with water tanks and water harvesting infrastructure.

Conclusion and appreciation

With the unwavering support and commitment of our Board of Directors, staff, customers, shareholders and partners, we remain confident the bank will overcome and surmount the current challenges and successfully turnaround its performance.

I wish to express my deepest gratitude to firstly, our customers, for believing in us and continuing to retain us as their preferred banking partners. To our shareholders, we thank you for your support. To our regulator, as well as the communities we exist in, thank you for creating an enabling environment for our operations. Lastly, I remain indebted to all employees and the Board of Directors for their commitment and dedication to the Bank throughout the year. We remain resolute to continue serving our customers and providing value to our stakeholders going into the future.

Thomas Kipkemei Kiyai
Chief Executive Officer
14 August 2020

DIRECTORS:
Current
Dr. Iyaya Wanjala -Chairman (Term ended 7th August 2020)
Thomas Kiyai - Chief Executive Officer
Cabinet Secretary - National Treasury
Managing Trustee - NSSF
Hon. Yusuf Chanzu
Dr. Kennedy Otiso
Miriam Cherogony
Dr. Nathan Psiwa
Hardlyne Lusui

AUDIT COMMITTEE:

RISK COMMITTEE:
Nathan Psiwa-Chairman
T. Kiyai
Hardlyne Lusui
Dr. Kennedy Otiso
Managing Trustee - NSSF
Hon. Yusuf Chanzu

STAFF COMMITTEE:

Dr. Kennedy Otiso - Chairman
Miriam Cherogony
Hardlyne Lusui
T. Kiyai
Cabinet Secretary, National Treasury

FINANCE AND CREDIT COMMITTEE:

Miriam Cherogony - Chairman
Hon. Yusuf Chanzu
Dr. Nathan Psiwa
T. Kiyai
Managing Trustee - NSSF

COMPANY SECRETARY:

Wakonyo Igeria
Certified Public Secretary (Kenya)
P. O. Box 51133 – 00200, Nairobi

REGISTERED OFFICE:
Consolidated Bank House
23 Koinange Street
P. O. Box 51133 - 00200, Nairobi

AUDITORS:

Principal auditor:
The Auditor General
Anniversary Towers
P. O. Box 30084 – 00100, Nairobi

Delegated auditor:
Ernst & Young LLP
Certified Public Accountants
Kenya-Re Towers, Upper Hill,
Off Ragati Road
P. O. Box 44286 – 00100, Nairobi

CORRESPONDENT BANKS:
ABSA Bank Limited
Vostro Department
P.O. Box 585 Johannesburg 2000

BMCE Bank Interenational
Serrano 59 - 280006
Madrid
Italy

ODDO BHF AktiengesellShaft
Bockenheiner Landstr.10-60323Frankfurt am Main
Germany

LEGAL ADVISERS:

Hamilton Harrison & Mathews
Delta Suites, Waiyaki Way
P.O. Box 30333 - 00100 Nairobi, Kenya

LEGAL ADVISERS:
Ndungu, Njoroge & Kwach Advocates
12th Floor, International House
Mama Ngina Street
P. O. Box 41546 - 00100, Nairobi, Kenya

Corporate governance defines the process and structure used to direct and manage the business affairs of Consolidated Bank of Kenya Limited ("the Bank") with the aim of enhancing corporate accounting and shareholders' long term value while taking into account the interests of other stakeholders.

The Board of Directors is responsible for the governance of the Bank and is committed to ensuring that its business operations are conducted with integrity and in compliance with the law, internationally accepted principles and best practices of corporate governance and business ethics. To this end the Bank has put in place processes, systems, practices and procedures which are frequently reviewed and updated embracing the changing corporate environment and world trends.

Business ethics

The Bank conducts its business in compliance with high ethical standards of business practice. In this respect, transactions with its clients, intermediaries, insiders, employees and other stakeholders are conducted at arm's length, with integrity and transparency. The business is conducted with high levels of transparency and accountability.

Board of Directors

The names of the Directors as at the date of this report are set out on page 7.

The Board fulfils its fiduciary responsibility to the shareholders by maintaining control over the strategic, financial, operational and compliance issues of the Bank. Whilst the Board provides direction and guidance on strategic and general policy matters and remains responsible for establishing and maintaining overall internal controls over financial, operational and compliance issues, it has delegated authority to the Chief Executive Officer to conduct the day-to-day business of the Bank.

The Board consists of eight non-executive directors (including the Chairman) and the Chief Executive Officer. The Board members possess extensive experience in a variety of disciplines in banking, business and financial management, all of which are applied in the overall management of the Bank. The Board meets at least once every two months, and has a formal schedule of matters reserved for it. The Directors are given appropriate and timely information so that they can perform their fiduciary responsibilities effectively.

a) Directors' Emoluments and Loans

The remuneration of all Directors is subject to the guidelines issued by the Office of the President on terms and conditions of service for State Corporations. The Directors are not eligible for membership of the pension scheme and do not participate in any of the Bank's bonus schemes. Information on the compensation received and the dealings of the Directors with the Bank are included in notes 17 and 44 to the financial statements.

b) Related Party Transactions

There have been no materially significant related party transactions, pecuniary transactions or relationships between the Bank and its Directors or Management except those disclosed in Note 44 to the financial statements.

The Board has set up working committees to assist in discharging its duties and responsibilities as follows:

Audit Committee

The Committee reviews the integrity of the financial statements of the bank and recommends the statements for approval to the Board. The Committee considers management's recommendations in respect of impairment on loans and advances as well as other disclosure requirements. The Committee is also mandated to raise the standards of corporate governance by reviewing the quality and effectiveness of the internal control systems, the internal and external audit functions and the quality of financial reporting. In addition to advising the Board on best practice, the committee also monitors management's compliance with relevant legislation, regulations and guidelines as well as the Bank's laid down policies and procedures. The committee has direct contact with the Internal Audit function, the Company Secretary and the external auditors. During the year, the bank did not have a functional Board Audit Committee. According to the CBK prudential guidelines at least one of the members of the Audit Committee should be a Finance professional who is a member of the Institute of Certified Public Accountants of Kenya – ICPAK or an equivalent institute recognised by the by the East African Community States. During the period under review the Board did not have a member who met this criterion and hence the Board Audit Committee was not constituted. Some of the critical functions of the Board Audit Committee were performed by the Credit Finance Committee and the main Board. The matter has been raised with the National Treasury the appointing authority.

Risk Committee

The committee is responsible for overseeing the implementation of the Bank's risk management framework to ensure that all existing and potential significant risks are identified and effectively managed. The committee considers both internal and external sources of information regarding risks to keep abreast with new developments and their potential impact to the business. The committee receives periodic reports from the risk and compliance function relating to the Bank's strategic risk, credit risk, market risk (interest rate risk, price risk, and foreign exchange risk), operational risk, regulatory risk, reputational risk, and liquidity risk.

Finance and Credit Committee

The committee is mandated to review and make recommendations on the Bank's credit, financial and accounting policies, and review and make recommendations on the Bank's Annual Budget, oversight of the overall lending policy of the Bank and deliberate and consider loan applications beyond the credit discretion limits set for management.

The committee also reviews and considers all issues that may materially impact the present and future quality of the Bank's credit risk management function as well as the quality of the loan portfolio and ensure adequate bad debt provisions are maintained in line with the Central Bank of Kenya prudential guidelines and IFRS. The committee also reviews, approves and monitors the management's compliance with applicable statutory provisions, Bank policies and guidelines relating to the monitoring of price, liquidity, exchange rate and interest rate risks.

Staff Committee

The committee is mandated to formulate staff policies and procedures and ensure an adequately staffed and professionally managed human resource. The committee assists the Board in discharging its corporate governance role by reviewing staffing needs of the Bank, appoints senior management staff, reviews training needs and undertake disciplinary measures as per the staff policies.

Board meeting attendance

During the year under review, the Board held main board and working committee meetings. The Board members attendance for 2019 is as follows:

Name	Board Meeting			Audit Committee			Risk & Compliance Committee			Credit & Finance Committee			Staff Committee		
	Meetings required to attend	Meetings attended	%	Meetings required to attend	Meetings attended	%	Meetings required to attend	Meetings attended	%	Meetings required to attend	Meetings attended	%	Meetings required to attend	Meetings attended	%
Thomas Kiyai - (Chief Executive Officer)	11	11	100%				3	3	100%	5	5	100%	4	4	100%
George Omino – Representing Cabinet Secretary National Treasury	11	10	91%				-	-	-	-	-	-	4	1	25%
Moses Cheseto- Alternate to Managing Trustee - NSSF	11	5	45%				3	3	100%	5	3	60%	-	-	-
Dr. Iyaya Wanjala - (Chairman)	11	11	100%				-	-	-	-	-	-	-	-	-
Hon. Yusuf Chanzu	11	11	100%				3	3	100%	5	5	100%-	-	-	-
Miriam Cherogony	11	8	73%				-	-	-	5	5	100%	4	2	50%
Dr. Kennedy Otiso	11	11	100%				3	3	-	-	-	-	4	4	100%
Dr. Nathan Psiwa	11	9	82%				3	2	67%	5	3	60%	-	-	-
Hardlyne Lusui	4	4	100%				2	2	100%	-	-	-	2	1	50%

The Board members attendance for 2018 is as follows:

Name	Board Meeting			Audit Committee			Risk & Compliance Committee			Credit & Finance Committee			Staff Committee		
	Meetings required to attend	Meetings attended	%	Meetings required to attend	Meetings attended	%	Meetings required to attend	Meetings attended	%	Meetings required to attend	Meetings attended	%	Meetings required to attend	Meetings attended	%
Thomas Kiyai - (Chief Executive Officer)	11	11	100%	3	3	100%	3	3	100%	4	4	100%	3	3	100%
George Omino – Representing Cabinet Secretary National Treasury	11	11	100%	3	3	100%	-	-	-	4	3	75%	3	3	100%
Moses Cheseto- Alternate to Managing Trustee - NSSF	11	10	91%	3	3	100%	3	3	100%	4	4	100%	3	3	100%
Dr. Raymond Omollo	11	10	91%	2	2	100%	3	3	100%	4	4	100%	2	2	100%
Joseph Koskey	11	10	91%	3	3	100%	3	3	100%	-	-	-	3	3	100%
Dr. Iyaya Wanjala - (Chairman)	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-
Hon. Yusuf Chanzu	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-
Miriam Cherogony	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-
Dr. Kennedy Otiso	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-
Dr. Nathan Psiwa	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-

Board performance evaluation

The Chairman conducts evaluations of the performance of the Board, individual Directors and Board Committees annually. In addition, the Board and its Committees undertake an annual evaluation of their performance and report their findings and any resulting recommendations to the Board. The Board also undertakes an evaluation of the performance of the Chairman. The Board discusses the results of its evaluations and uses the process to constructively improve the effectiveness of the Board.

Shareholders

The list of the shareholders and their individual holdings at the year ended 31 December 2019 was as follows:

	Ordinary Shares				Preference shares		
	2019		2018				
	No of shares	%	No of shares	%		2019	2018
Cabinet Secretary/The National Treasury	140,000,000	93.4%	60,000,000	85.8%	-	-	-
National Social Security Fund	2,225,000	1.5%	2,225,000	3.2%	8,050,000	22.30%	22.30%
Kenya National Assurance (2001)	1,094,487	0.7%	1,094,487	1.6%	3,958,300	11.00%	11.00%
Kenya National Assurance Company Limited	835,513	0.6%	835,513	1.2%	3,021,700	8.40%	8.40%
Kenya Pipeline Company Limited	720,000	0.5%	720,000	1%	2,631,500	7.30%	7.30%
Kenya National Examination Council	695,000	0.5%	695,000	1%	2,520,000	7.00%	7.00%
Public Trustees	660,000	0.4%	660,000	0.9%	2,420,000	6.70%	6.70%
Telkom Kenya Limited	620,000	0.4%	620,000	0.9%	2,250,000	6.20%	6.20%
National Hospital Insurance Fund	590,000	0.4%	590,000	0.8%	2,120,000	5.90%	5.90%
LAPTRUST Retirement Services Limited	483,000	0.3%	483,000	0.7%	1,756,000	4.90%	4.90%
Total of 10 above	147,923,000	98.7%	67,923,000	97.1%	28,727,500	79.70%	79.70%
Other shareholders	1,997,000	1.3%	1,997,000	2.9%	7,329,000	20.30%	20.30%
				-			
TOTAL SHAREHOLDING	**149,920,000**	**100%**	**69,920,000**	**100%**	**36,056,500**	**100%**	**100%**

Compliance

The Board provides oversight to ensure that management adheres to all applicable laws, regulations, governance codes, policies, procedures and systems to monitor and control compliance across the bank. Additionally, the Bank prepares its financial statements in accordance with International Financial Reporting Standards (IFRS), requirements of the Banking Act and the Companies Act.

Chairman
Dr. Iyaya Wanjala
30/3/2020

The directors submit their report together with the audited financial statements for the year ended 31 December 2019.

INCORPORATION

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

DIRECTORATE

The Directors who held office during the year and to the date of this report are set out on page 7.

PRINCIPAL ACTIVITIES

The principal activities of the Bank, which is governed by the Banking Act, are the provision of banking, financial and related services.

RESULTS	2019 Kshs'000	2018 Kshs'000
Loss before taxation	(518,001)	(351,567)
Taxation (charge)/ credit	(13,291)	(188,467)
Loss for the year transferred to ccumulated deficit	(531,292)	(540,034)

DIVIDEND

The Directors do not recommend the payment of a dividend for the year (2018: nil).

STATEMENT AS TO DISCLOSURE TO THE BANK'S AUDITOR

With respect to each of the persons who is a Director at the date of approval of this report confirms that:

- there is, so far as the Director is aware, no relevant audit information of which the Bank's auditor is unaware; and
- the Director has taken all the steps that he/she 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.

BUSINESS REVIEW

The Kenyan economy is estimated to have grown by 5.7% in 2019, a slight decrease from the growth of 6.0% the previous year. This performance is against backdrop of difficult operating environment characterised by reduced agricultural output and considerably weak private sector investment. The banking sector remained resilient in the face of increased regulation focusing in the areas such as; Anti Money Laundering and implementation of the new IFRS 9.

In November 2019 the Finance Act 2019 amended the banking act by repealing section 33b of the Banking Act to remove the caps on interest charged on loans. It also amended section 56 of the Banking Act to prohibit banks from increasing interest rates on credit facilities entered into while the interest rate caps were in force. Under the circumstance unless revised down wards, the interest rates on such loans will remain fixed for the entire duration of the loans. This is expected to boost lending to the private sector especially SMEs and spur economic growth.

On 22 October 2019 the bank received Kshs 1.6 billion as capital injection from the National Treasury. This was utilised towards settlement of the bank's Medium Term Note of Kshs 1.52 billion which matured on 22 July 2019 and the maturity was extended to 22 October 2019. An Extraordinary General Meeting (EGM) was held on 30 January 2020 and approved the allotment of the additional shares to the National Treasury for the new capital injection. Following the capital injection of Kshs 1.6 billion in October 2019, the bank now meets all the capital ratios except one- the total capital to risk weighted assets. The three-year strategic plan however envisages this position will be corrected by the year 2021.

The Board and management have developed a three year strategic plan for the period 2020-2022 which will see the bank turnaround from a loss making position to profitability in the next twelve months.

AUDITOR

The Auditor General is responsible for the statutory audit of the Bank's books of account in accordance with section 14 and section 39(i) of the Public Audit Act, 2004 which empowers the Auditor General to nominate other auditors to carry out the audit on his behalf and subject to the approval by the Central Bank of Kenya in accordance with the requirements of Section 24(1) of the Banking Act of Kenya.

Ernst & Young LLP, who were nominated by the Auditor General, carried out the audit of the financial statements for the year ended 31 December 2019.

BY ORDER OF THE BOARD

Secretary
Wakonyo Igeria
30/3/2020

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 company 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 company maintains proper accounting records that are sufficient to show and explain the transactions of the company and disclose, with reasonable accuracy, the financial position of the company. The Directors are also responsible for safeguarding the assets of the company, and for taking reasonable steps for the prevention and detection of fraud and error.

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

The Directors have considered the matters discussed in note 9 to the financial statements, which indicate that the bank made an after tax loss of Kshs 531 million during the year ended 31 December 2019 (2018: 540 million) with accumulated losses of Kshs 2.6 billion (2018: 2.1 billion) as at that date. Further the bank's total capital to risk weighted assets was 13.5% against a CBK regulatory minimum of 14.5%.

On 22 October 2019 the bank received a fresh capital injection of Kshs 1.6 billion from the National Treasury the majority shareholder. This enabled the bank to settle the Medium Term Note of Kshs 1.520 billion which matured on 22 July 2019 and maturity was extended to 22 October 2019. As a result of this capital injection the bank's core capital improved to Kshs 1.153 billion in December 2019 from Kshs 58 million in December 2018. The bank's capital ratios improved significantly with core capital to deposits increasing to 13.5% from 0.7% in 2018, core capital to risk weighted assets to 11.4% from 0.5% in 2018 and total capital to risk weighted assets ratio to risk weighted assets to 13.5% from 1% in 2018. The bank is therefore compliant with capital ratios except the total capital to risk weighted assets which is 13.5% against the regulatory minimum of 14.5%.

The Board and management have put in place a three year strategic plan which targets to reduce the operating losses by 64% in 2020 and turn around to profitability in 2021. The improved capital position is sufficient to enable the bank implement its business plan for 2020 as it works with the Privatisation Commission and the National Treasury to finalise the privatisation process which is expected to bring on board a strategic investor and enable the bank to sustainably access capital for future growth.

Based on the foregoing the Board has made an assessment of the bank's ability to continue as a going concern and is satisfied that it has the resources to continue in business for the foreseeable future. Furthermore, management is not aware of any material uncertainties that may cast significant doubt on the Bank's ability to continue as a going concern. Therefore, the financial statements continue to be prepared on the going concern basis.

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 30/3/2020 and signed on its behalf by:

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Dr. Iyaya Wanjala	**Hon. Yusuf Chanzu**
Chairman	**Director**

The Board establishes and approves formal and transparent remuneration polices to attract and retain both Executive and Non-Executive Directors. The remuneration of all Directors is subject to the guidelines issued by the State Corporations Advisory Committee (SCAC) on terms and conditions of service for State Corporations.

In accordance with the guidelines provided by the State Corporations Advisory Committee (SCAC), Salaries and Remuneration Commission (SRC) as well as the National Treasury and other shareholders' approval during the Annual General Meetings, the Directors are paid a sitting allowance of Kshs. 20,000 for every meeting attended. The Directors and the Chairman are also paid a monthly retainer of Kshs. 50,000 and Kshs. 150,000, respectively. The Directors are not eligible for membership of the pension scheme and do not participate in any of the Bank's bonus schemes.

Contract of Service
In accordance with the Kenyan Companies Act, 2015 and the Capital Market Regulations of Kenya on Non-Executive Directors, a third of the Board is elected at every Annual General Meeting by shareholders for a term of three years, on rotational basis.

The Chief Executive Officer has a three-year renewable contract of service with Consolidated Bank of Kenya Limited starting 9 March 2015. The contract was renewed for a further term of three years with effect from 10th April 2018.

Changes to Directors' Remuneration
During the period, there were no changes in Directors' remuneration which is set as per the guidelines provided by the State Corporation Advisory Committee and the Salaries and Remuneration Commission.

Statement on approval of Directors' Remuneration during the Annual General Meeting
During the Annual General Meeting held on 27 June 2019, the shareholders approved the payment of Directors' fees for the year ended 31 December 2018 in accordance with the guidelines provided by the State Corporations Advisory Committee and the Salaries and Remuneration Commission.

The following tables shows a single figure remuneration for the CEO and Non-Executive Directors in respect of qualifying services for the year ended 31 December 2019 together with the comparative figures for 2018.The aggregate Directors emoluments are shown in note 17.

For the year ended 31 December 2019	Category	Gross payments	Honorarium	Allowances	Total
		Kshs' 000	Kshs' 000	Kshs' 000	Kshs' 000
Dr. Iyaya Wanjala - (Appointed on 9 November 2018)	Chairman Non-Executive	-	1,800	627	2,427
Thomas Kiyai	Chief Executive Officer	21,580	-	-	21,580
George Omino – Representing Cabinet Secretary National Treasury	Non-Executive	-	550	302	852
Moses Cheseto - Alternate to Managing Trustee - NSSF	Non-Executive	-	600	258	858
Hardlyne Lusui - (Appointed on 19 December 2018)	Non-Executive	-	265	1,159	1,424
Dr. Kennedy Otiso - (Appointed on 20 September 2018)	Non-Executive	-	600	1,689	2,289
Miriam Cherogony (Appointed on 20 September 2018)	Non-Executive	-	600	508	1,108
Hon. Yusuf Chanzu (Appointed on 20 September 2018)	Non-Executive	-	600	1,728	2,328
Dr. Nathan Psiwa (Appointed on 20 September 2018)	Non-Executive	-	621	570	1,191
Total		**21,580**	**5,636**	**6,841**	**34,057**

For the year ended 31 December 2018	Category	Gross payments	Honorarium	Allowances	Total
		Kshs' 000	Kshs' 000	Kshs' 000	Kshs' 000
Dr. Iyaya Wanjala - (Appointed on 9 November 2018)	Chairman Non-Executive	-	408	81	489
Thomas Kiyai	Chief Executive Officer	21,980	-	-	21,980
George Omino – Representing Cabinet Secretary National Treasury	Non-Executive	-	600	470	1,070
Moses Cheseto- Alternate to Managing Trustee - NSSF	Non-Executive	-	600	552	1,152
Dr. Raymond Omollo-(Term ended on 2 October 2018)	Non-Executive	-	451	455	906
Joseph Koskey-(Term ended on 2 October 2018)	Non-Executive	-	451	426	877
Dr. Kennedy Otiso - (Appointed on 20 September 2018)	Non-Executive	-	80	192	272
Miriam Cherogony (Appointed on 20 September 2018)	Non-Executive	-	80	62	142
Hon. Yusuf Chanzu (Appointed on 20 September 2018)	Non-Executive	-	78	62	140
Dr. Nathan Psiwa (Appointed on 20 September 2018)	Non-Executive	-	-	-	-
Total		**21,980**	**2,748**	**2,300**	**27,028**

REPORT ON THE FINANCIAL STATEMENTS

Opinion

The accompanying financial statements of Consolidated Bank of Kenya Limited set out on pages 32 to 109, which comprise the Group and the Bank statements of financial position as at 31 December, 2019, statements of profit or loss and other comprehensive income, statements of changes in equity and the statements of cash flows for the year then ended, and a summary of significant accounting policies and other explanatory information, have been audited on my behalf by Ernst & Young LLP, auditors appointed under Section 23 of the Public Audit Act, 2015. The auditors have duly reported to me the results of their audit and on the basis of their report, I am satisfied that all the information and explanations which, to the best of my knowledge and belief, were necessary for the purpose of the audit were obtained.

In my opinion, the financial statements present fairly, in all material respects, the financial position of Consolidated Bank of Kenya Limited as at 31 December, 2019, and of its financial performance and its cash flows for the year then ended, in accordance with International Financial Reporting Standards (IFRS) and comply with the Kenya Companies Act, 2015.

Basis for Opinion

The audit was conducted in accordance with International Standards of Supreme Audit Institutions (ISSAIs). I am independent of Consolidated Bank of Kenya Limited Management in accordance with ISSAI 130 on Code of Ethics. I have fulfilled other ethical responsibilities in accordance with the ISSAIs and in accordance with other ethical requirements applicable to performing audits of financial statements in Kenya. I believe that the audit evidence I have obtained is sufficient and appropriate to provide a basis for my opinion.

Emphasis of Matter

Material Incertainty Related to Going Concern

As previously reported, I again draw attention to Note 9 to the financial statements, which indicates that the Bank incurred a net loss for the year of Kshs. 529,548,000;(2018-loss Kshs.540,446,000), resulting into a reported accumulated deficit of Kshs. 2,562,072,000 (2018-Kshs. 2,061,222,000) and, as of that date, the Bank had a total regulatory capital to risk weighted assets ratio of 13.5% (2018: 1.00%) against a regulatory minimum required ratio of 14.5%. The bank received Kshs. 1.6 billion from the National Treasury, the majority shareholder on 22 October, 2019. This amount was applied to settle the Medium Term Note of Kshs. 1.52 billion that matured on 22 July, 2019 but extended to 22 October, 2019. The receipt pushed the shareholding of National Treasury to 93.4%. These conditions alongside other matters as disclosed under the same Note are indicative of the Bank's inability to continue as a going concern.

My opinion is not modified in respect of this matter.

Key Audit Matters

Key audit matters are those matters that, in my professional judgement, are of most significance in the audit of the financial statements. There were no key audit matters to report in the year under review.

Other Information

The Directors are responsible for the other information. The other information comprises the Bank information, corporate governance and the report of the Directors as required by the Kenya Companies Act, 2015. The other information does not include the financial statements and the auditor's report thereon.

My opinion on the financial statement does not cover the other information and I do not express an audit opinion or any form of assurance conclusion thereon.

REPORT ON LAWFULNESS AND EFFECTIVENESS IN USE OF PUBLIC RESOURCES

Conclusion

As required by Article 229(6) of the Constitution, based on the audit procedures performed, I confirm that, nothing has come to my attention to cause me to believe that public resources have not been applied lawfully and in an effective way.

Basis for Conclusion

The audit was conducted in accordance with ISSAI 4000. The standard requires that I comply with ethical requirements and plan and perform the audit to obtain assurance about whether the activities, financial transactions and information reflected in the financial statements are in compliance, in all material respects, with the authorities that govern them. I believe that the audit evidence I have obtained is sufficient and appropriate to provide a basis for my conclusion.

REPORT ON EFFECTIVENESS OF INTERNAL CONTROLS, RISK MANAGEMENT AND OVERALL GOVERNANCE.

Conclusion

As required by Section 7(1)(a) of the Public Audit Act, 2015, based on the audit procedures performed, I confirm that, nothing has come to my attention to cause me to believe that the internal controls, risk management and overall governance were not effective.

Basis for Conclusion

The audit was conducted in accordance with ISSAI 2315 and ISSAI 2330. The standards require that I plan and perform the audit to obtain assurance about whether effective processes and systems of internal control, risk management and overall governance were operating effectively, in all material respects. I believe that the audit evidence I have obtained is sufficient and appropriate to provide a basis for my conclusion.

REPORT ON OTHER LEGAL AND REGULATORY REQUIREMENTS

As required by Kenya Companies Act, 2105, I report based in my audit, that:

i. I have obtained all the information and explanations which, to the best of my knowledge and belief, were necessary for the purpose of the audit;

ii. In my opinion, adequate accounting records have been kept by the Bank, so far as appears from the examination of those records; and,

iii. The Bank financial statements are in agreement with the accounting records and returns.

Responsibilities of Management and the Board of Directors

Management is responsible for the preparation and fair presentation of these financial statements in accordance with International Financial Reporting Standards and for maintaining effective internal control as management determines is necessary to enable the preparation of financial statements that are free from material misstatement, whether due to fraud or error and for its assessment of the effectiveness of internal control, risk management and overall governance.

In preparing the financial statements, management is 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 management either intends to liquidate the Bank or cease operations, or have no realistic alternative but to do so.
Management is also responsible for the submission of the financial statements to the Auditor-General in accordance with the provisions of Section 47 of the Public Audit Act, 2015.

In addition to the responsibility for the preparation and presentation of the financial statements described above, management is also responsible for ensuring that the activities, financial transactions and information reflected in the financial statements are in compliance with the authorities which govern them, and that public resources are applied in an effective way.

The Board of Directors are responsible for overseeing the financial reporting process, reviewing the effectiveness of how the Bank monitors compliance with relevant legislative and regulatory requirements, ensuring that effective processes and systems are in place to address key roles and responsibilities in relation to overall governance and risk management, and ensuring the adequacy and effectiveness of the control environment.

Auditor-General's Responsibilities for the Audit

The audit 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 my opinion in accordance with the provisions of Section 48 of the Pubic Audit Act, 2105 and submit the audit report in compliance with Article 229(7) of the Constitution. Reasonable assurance is a high level of assurance, but is not a guarantee that an audit conducted in accordance with ISSAIs will always detect a material misstatement and weakness 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. In addition to the audit of the financial statements, a compliance audit is planned and performed to express a conclusion about whether, in all material respects, the activities, financial transactions and information reflected in the financial statements are in compliance with the authorities that govern them and that public resources are applied in an effective way, in accordance with the provisions of Article 229(6) of the Constitution and submit the audit report in compliance with Article 229(7) of the Constitution.

Further, in planning and performing the audit of the financial statements and audit of compliance, I consider internal control in order to give an assurance on the effectiveness of internal controls, risk management and overall governance processes and systems in accordance with the provisions of Section 7(1)(a) of the Public Audit Act, 2015 and submit the audit report in compliance with Article 229(7) of the Constitution. My consideration of the internal control would not necessarily disclose all matters in the internal control that might be material weaknesses under the ISSAIs. A material weakness is a condition in which the design or operation of one or more of the internal control components does not reduce to a relatively low level the risk that misstatements caused by error or fraud in amounts that would be material in relation to the financial statements being audited may occur and not be detected within a timely period by employees in the normal course of performing their assigned functions.

Because of its inherent limitations, internal control may not prevent or detect misstatements and instances of non-compliance. Also, projections of any evaluation of effectiveness to future periods are subject to the risk that controls may become inadequate because of changes in conditions, or that the degree of compliance with the policies and procedures may deteriorate.
As part of an audit conducted in accordance with ISSAIs, I exercise professional judgement and maintain professional skepticism throughout the audit. I 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 my 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.

- Evaluate the appropriateness of accounting policies used and the reasonableness of accounting estimates and related disclosures made by the management.

- Conclude on the appropriateness of the 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 I conclude that a material uncertainty exists, I am required to draw attention in the auditor's report to the related disclosures in the financial statements or, if such disclosures are inadequate, to modify my opinion. My conclusions are based on the audit evidence obtained up to the date of my audit 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.

- Obtain sufficient appropriate audit evidence regarding the financial information and business activities of the Bank to express an opinion on the financial statements.

- Perform such other procedures as I consider necessary in the circumstances.

I communicate with the management regarding, among other matters, the planned scope and timing of the audit and significant audit findings, including any significant deficiencies in internal control that are identified during the audit.

I also provide management with a statement that I have complied with relevant ethical requirements regarding independence, and to communicate with them all relationships and other matters that may reasonably be thought to bear on my independence, and where applicable, related safeguards.

Nancy Gathungu
AUDITOR-GENERAL
14 August 2020

GROUP STATEMENT OF PROFIT OR LOSS AND OTHER COMPREHENSIVE INCOME
FOR THE YEAR ENDED 31 DECEMBER 2019

	Notes	2019 Kshs'000	2018 Kshs'000
INTEREST INCOME	12	1,216,404	1,401,466
INTEREST EXPENSE	13	(674,955)	(758,458)
NET INTEREST INCOME		**541,449**	**643,008**
Fee and commission income	14	356,171	298,292
Foreign exchange trading income	15	21,715	21,436
Other operating income	16	313,519	442,044
OPERATING INCOME		**1,232,854**	**1,404,780**
Operating expenses	17	(1,334,823)	(1,388,179)
Credit loss expense on loans and advances	25	(416,005)	(368,162)
Credit loss expense on balances due from banking institutions	22(a)	(27)	(6)
LOSS BEFORE TAXATION		**(518,001)**	**(351,567)**
INCOME TAX CHARGE	**19(a)**	**(13,291)**	**(188,467)**
LOSS FOR THE YEAR		**(531,292)**	**(540,034)**
OTHER COMPREHENSIVE INCOME/(LOSS)			
Items that may not be reclassified subsequently to profit or loss:			
Net gain/(loss) on equity instruments designated at fair value through other comprehensive income	27	651	(412)
Net other comprehensive loss that may not be reclassified to profit or loss in subsequent periods		651	(412)
Items that may be reclassified subsequently to profit or loss (net of tax):			
Net other comprehensive loss that may be reclassified to profit or loss in subsequent periods		-	-
Total other comprehensive income for the year, net tax		651	(412)
TOTAL COMPREHENSIVE LOSS FOR THE YEAR, NET OF TAX		**(530,641)**	**(540,446)**
LOSS PER SHARE		**Kshs**	**Kshs**
Basic and diluted	20	(3.54)	(7.72)

	Notes	2019 Kshs'000	2018 Kshs'000
INTEREST INCOME	12	1,216,404	1,401,466
INTEREST EXPENSE	13	(674,955)	(758,458)
NET INTEREST INCOME		**541,449**	**643,008**
Fee and commission income	14	344,019	298,292
Foreign exchange trading income	15	21,715	21,436
Other operating income	16	313,519	442,044
OPERATING INCOME		**1,220,702**	**1,404,780**
Operating expenses	17	(1,321,578)	(1,388,179)
Credit loss expense on loans and advances	25	(416,005)	(368,162)
Credit loss expense on balances due from banking institutions	22(a)	(27)	(6)
LOSS BEFORE TAXATION		**(516,908)**	**(351,567)**
INCOME TAX CHARGE	**19(a)**	**(13,291)**	**(188,467)**
LOSS FOR THE YEAR		**(530,199)**	**(540,034)**
OTHER COMPREHENSIVE INCOME / (LOSS)			
Items that may not be reclassified subsequently to profit or loss:			
Net gain/(loss) on equity instruments designated at fair value through other comprehensive income	27	651	(412)
Net other comprehensive loss that may not be reclassified to profit or loss in subsequent periods		651	(412)
Total other comprehensive income for the year, net tax		651	(412)
TOTAL COMPREHENSIVE LOSS FOR THE YEAR, NET OF TAX		**(529,548)**	**(540,446)**
LOSS PER SHARE		**Kshs**	**Kshs**
Basic and diluted	20	(3.57)	(7.72)

	Notes	31 December 2019 Kshs'000	31 December 2018 Kshs'000
ASSETS			
Cash and balances with Central Bank of Kenya	21	906,420	918,709
Balances due from banking institutions	22(a)	179,032	119,420
Financial assets at amortised cost	23	2,082,370	2,190,093
Loans and advances to customers	24	7,369,033	8,429,659
Other assets	26	271,469	306,950
Equity instruments at fair value through other comprehensive income	27	7,378	6,727
Taxation recoverable	19(c)	6,204	2,809
Property and equipment and Right of Use Assets	28(a)	815,734	720,115
Intangible assets	29(a)	217,542	186,211
Prepaid operating lease rentals	30	6,469	6,639
TOTAL ASSETS		**11,861,651**	**12,887,332**
LIABILITIES AND SHAREHOLDERS' FUNDS			
LIABILITIES			
Deposits and balances due to banking institutions	22(b)	23,814	235,751
Balances due to Central Bank of Kenya	22(c)	720,000	1,120,000
Customer deposits	31	8,771,860	8,588,544
Other liabilities	32	351,263	285,362
Borrowings	33	-	1,732,320
TOTAL LIABILITIES		**9,866,937**	**11,961,977**
SHAREHOLDERS' FUNDS			
Share capital	34(b)	3,719,530	2,119,530
Revaluation surplus	35	361,888	370,509
Accumulated deficit	36	(2,567,139)	(2,061,222)
Statutory reserve	37	473,925	490,679
Fair value reserve	38	6,510	5,859
TOTAL SHAREHOLDERS' FUNDS		**1,994,714**	**925,355**
TOTAL LIABILITIES AND SHAREHOLDERS' FUNDS		11,861,651	12,887,332

The financial statements on pages 32 to 109 were approved and authorised for issue by the Board of Directors On **30/3/2020** and were signed on its behalf by:

Director - Dr. Iyaya Wanjala

Director - Hon Yusuf Chanzu

Chief Executive Officer - Thomas Kiyai

Company Secretary - Wakonyo Igeria

BANK STATEMENT OF FINANCIAL POSITION
AS AT 31 DECEMBER 2019

	Notes	31 December 2019 Kshs'000	31 December 2018 Kshs'000
ASSETS			
Cash and balances with Central Bank of Kenya	21	906,420	918,709
Balances due from banking institutions	22(a)	173,909	119,420
Financial assets at amortised cost	23	2,082,370	2,190,093
Loans and advances to customers	24	7,369,033	8,429,659
Other assets	26(a)	271,469	306,950
Due from subsidiaries	26(b)	17,079	-
Equity instruments at fair value through other comprehensive income	27	7,378	6,727
Taxation recoverable	19(c)	6,204	2,809
Property and equipment and Right of Use Assets	28(b)	810,437	720,115
Intangible assets	29(b)	214,842	186,211
Prepaid operating lease rentals	30	6,469	6,639
TOTAL ASSETS		11,865,610	12,887,332
LIABILITIES AND SHAREHOLDERS' FUNDS			
LIABILITIES			
Deposits and balances due to banking institutions	22(b)	23,814	235,751
Balances due to Central Bank of Kenya	22(c)	720,000	1,120,000
Customer deposits	31	8,771,860	8,588,544
Other liabilities	32	350,155	285,362
Borrowings	**33**	**-**	**1,732,320**
TOTAL LIABILITIES		9,865,829	11,961,977
SHAREHOLDERS' FUNDS			
Share capital	34(b)	3,719,530	2,119,530
Revaluation surplus	35	361,888	370,509
Accumulated deficit	36	(2,562,072)	(2,061,222)
Statutory reserve	**37**	**473,925**	**490,679**
Fair value reserve	38	6,510	5,859
TOTAL SHAREHOLDERS' FUNDS		1,999,781	925,355
TOTAL LIABILITIES AND SHAREHOLDERS' FUNDS		**11,865,610**	**12,887,332**

The financial statements on pages 32 to 109 were approved and authorised for issue by the Board of Directors On **30/03/2020** and were signed on its behalf by:

Director - Dr. Iyaya Wanjala | **Director - Hon Yusuf Chanzu**

Chief Executive Officer - Thomas Kiyai | **Company Secretary - Wakonyo Igeria**

CONSOLIDATED BANK OF KENYA LIMITED AND ITS SUBSIDIARIES
GROUP STATEMENT OF CHANGES IN EQUITY
FOR THE YEAR ENDED 31 DECEMBER 2019

	Note	Share capital Kshs'000	Revaluation surplus Kshs'000	Accumulated deficit Kshs'000	Statutory reserve Kshs'000	Fair value reserve Kshs'000	Total Kshs'000
At 1 January 2018		1,619,530	379,130	(1,368,298)	265,662	6,271	902,295
Capital injection		500,000	-	-	-	-	500,000
Loss for the year Other comprehensive loss		-		(540,034)	-	-	(540,034)
		-	-	-	-	(412)	(412)
Transfer of excess depreciation	36	-	(12,316)	12,316	-	-	-
Deferred tax on excess depreciation	36	-	3,695	(3,695)	-	-	-
Transfer to stage 1	37	-	-	63,506	-	-	63,506
Transfer to statutory reserve	37	-	-	(225,017)	225,017	-	-
At 31 December 2018		**2,119,530**	**370,509**	**(2,061,222)**	**490,679**	**5,859**	**925,355**
At 1 January 2019		2,119,530	370,509	(2,061,222)	490,679	5,859	925,355
Capital injection		1,600,000	-	-	-	-	1,600,000
Loss for the year		-	-	(531,292)	-	-	(531,292)
Other comprehensive income		-	-	-	-	651	651
		-	-	-	-	-	
Transfer of excess depreciation	36	-	(12,316)	12,316	-	-	-
Deferred tax on excess depreciation	36	-	3,695	(3,695)	-	-	-
Transfer to statutory reserve	38	-	-	16,754	(16,754)	-	-
At 31 December 2019		**3,719,530**	**361,888**	**(2,567,139)**	**473,925**	**6,510**	**1,994,714**

CONSOLIDATED BANK OF KENYA LIMITED AND ITS SUBSIDIARIES
BANK STATEMENT OF CHANGES IN EQUITY
FOR THE YEAR ENDED 31 DECEMBER 2019

	Note	Share capital Kshs'000	Revaluation surplus Kshs'000	Accumulated deficit Kshs'000	Statutory reserve Kshs'000	Fair value reserve Kshs'000	Total Kshs'000
At 1 January 2018		1,619,530	379,130	(1,368,298)	265,662	6,271	902,295
Capital injection		500,000	-	-	-	-	500,000
Loss for the year		-		(540,034)	-	-	(540,034)
Other comprehensive loss		-	-	-	-	(412)	(412)
Transfer of excess depreciation	36	-	(12,316)	12,316	-	-	-
Deferred tax on excess depreciation	36	-	3,695	(3,695)	-	-	-
Transfer to stage 1	37	-	-	63,506	-	-	63,506
Transfer to statutory reserve	37	-	-	(225,017)	225,017	-	-
At 31 December 2018		**2,119,530**	**370,509**	**(2,061,222)**	**490,679**	**5,859**	**925,355**
At 1 January 2019		2,119,530	370,509	(2,061,222)	490,679	5,859	925,355
Elimination of subsidiary accumulated losses				3,974			3,974
Capital injection		1,600,000	-	-	-	-	1,600,000
Loss for the year		-	-	(530,199)	-	-	(530,199)
Other comprehensive income						651	651
Transfer of excess depreciation	36	-	(12,316)	12,316	-	-	-
Deferred tax on excess depreciation	36	-	3,695	(3,695)	-	-	-
Transfer to statutory reserve	37	-	-	16,754	(16,754)	-	-
At 31 December 2019		**3,719,530**	**361,888**	**(2,562,072)**	**473,925**	**6,510**	**1,999,781**

	Note	2019 Kshs'000	2018 Kshs'000
CASH FLOWS GENERATED FROM OPERATIONS			
Cashflows generated from operations	40(a)	1,085,606	238,380
Tax paid	19(c)	(16,686)	(11,955)
Net cashflows from operating activities		1,068,920	226,425
CASH FLOWS FROM INVESTING ACTIVITIES			
Purchase of property and equipment	28	(23,689)	(24,190)
Proceeds on sale of property and equipment		225	112
Purchase of intangible assets	29	(139,757)	(36,619)
Net cash used in investing activities		(163,220)	(60,697)
CASH FLOWS FROM FINANCING ACTIVITIES			
Proceeds from issuance of shares		1,600,000	500,000
Repayment of principal and interest on borrowings	34	(1,835,279)	(294,233)
Repayment of principal portion of lease liability	28(b)	(61,205)	-
Repayment of interest portion on lease liability	28(b)	(13,797)	-
Net cash (used in)/from financing activities		(310,281)	205,767
NET DECREASE IN CASH AND CASH EQUIVALENTS DURING THE YEAR		**595,418**	**371,495**
CASH AND CASH EQUIVALENTS AT 1 JANUARY		**(853,219)**	**(1,224,714)**
CASH AND CASH EQUIVALENTS AT 31 DECEMBER	**40(b)**	**(257,800)**	**(853,219)**

	Note	2019 Kshs'000	2018 Kshs'000
CASH FLOWS FROM OPERATING ACTIVITIES			
Cashflows generated form/ (used in operations)	40(a)	1,072,995	238,380
Tax paid	19(c)	(16,686)	(11,955)
Net cashflows from/ (used in) operating activities		1,056,309	226,425
CASH FLOWS FROM INVESTING ACTIVITIES			
Purchase of property and equipment	28	(17,700)	(24,190)
Proceeds on sale of property and equipment		226	112
Purchase of intangible assets	29	(138,259)	(36,619)
Net cash used in investing activities		(155,733)	(60,697)
CASH FLOWS FROM FINANCING ACTIVITIES			
Proceeds from issuance of shares		1,600,000	500,000
Repayment of principal and interest on borrowings	34	(1,835,279)	(294,233)
Repayment of principal portion of lease liability	28(b)	(61,205)	-
Repayment of interest portion on lease liability	28(b)	(13,797)	-
Net cash from/(used in) financing activities		(310,281)	205,767
NET DECREASE IN CASH AND CASH EQUIVALENTS DURING THE YEAR		**590,295**	**371,495**
CASH AND CASH EQUIVALENTS AT 1 JANUARY		**(853,219)**	**(1,224,714)**
CASH AND CASH EQUIVALENTS AT 31 DECEMBER	**40(b)**	**(262,924)**	**(853,219)**

1. REPORTING ENTITY

Consolidated Bank of Kenya Limited (The "Bank") together with its subsidiaries provides retail and corporate banking services and insurance agency services in Kenya. Consolidated Bank of Kenya Limited is the ultimate parent of the group.

The address of its registered office is as follows:
Consolidated Bank House, Koinange Street
P O Box 51133
Nairobi- 00200.

The consolidated financial statements for the year ended 31 December 2019 were authorised for issue in accordance with a resolution of the directors on 30 March 2020.

2. BASIS OF PREPARATION

The consolidated and separate financial statements have been prepared in accordance with the historical cost basis except for equity instruments measured at fair value through other comprehensive income. For Kenyan Companies Act, 2015 reporting purposes, the balance sheet is represented by the statement of financial position and the profit and loss account by the statement of profit or loss and other comprehensive income in these financial statements. The financial statements are presented in Kenya Shillings (Kshs) and all values are shown in Thousands Kenya Shillings (Kshs'000) except where otherwise indicated.

3. Statement of Compliance

The group financial statements of the Bank have been prepared in accordance with International Financial Reporting Standards (IFRS) as issued by the International Accounting Standards Board (IASB), the Kenyan Companies Act 2015 and the Banking Act. The preparation of financial statements in conformity with IFRS requires use of certain critical accounting estimates. It also requires management to exercise its judgement in the process of applying bank policies. The areas involving a higher degree of judgement or complexity or where assumptions and estimates are significant are disclosed in note 8.

4. Presentation of Financial Statements

The Bank presents its statement of financial position in order of liquidity based on the Bank's intention and perceived ability to recover/ settle the majority of assets/liabilities of the corresponding financial statement line item. An analysis of the expected cash flows of financial assets and liabilities and contractual maturities as at the date of reporting is presented in note 10.8.2. Financial assets and financial liabilities are generally reported gross in the consolidated statement of financial position except when IFRS netting criteria are met.

Positions that are managed on a settle-to-market basis are transactions that are settled in cash before the close of the business day and therefore the balances are no longer recognised on the statement of financial position as an asset or a liability. The carrying amounts represent the called but not yet settled balances. Products that the Bank manages on a Settle-to-market basis include: exchange traded futures and options and over-the-counter interest rate and foreign currency swaps cleared through the bank.

5. Changes in accounting policies and disclosures

5.1 New and amended Standards Interpretation

In these financial statements the bank has applied IFRS 16 for the first time. The nature and effect of the changes are described in note 5.1.1 below. IFRS 16 'Leases' replaces IAS 17 'Leases' along with three Interpretations (IFRIC 4 'Determining whether an Arrangement contains a Lease', SIC 15 'Operating Leases-Incentives' and SIC 27 'Evaluating the Substance of Transactions Involving the Legal Form of a Lease').

Several other amendments and interpretations apply for the first time in 2019, but do not have an impact on the Bank's consolidated financial statements. The new and amended standards and interpretations are effective for annual periods beginning on or after 1 January 2019, unless otherwise stated. The Bank has not early adopted any standards, interpretations or amendments that have been issued but are not yet effective.

5. Changes in accounting policies and disclosures (continued)

5.1.1 IFRS 16 - Leases

IFRS 16 supersedes IAS 17 Leases, IFRIC 4 Determining whether an Arrangement contains a Lease, SIC-15 Operating Leases-Incentives and SIC-27 Evaluating the Substance of Transactions Involving the Legal Form of a Lease. The standard sets out the principles for the recognition, measurement, presentation and disclosure of leases and requires lessees to recognise most leases on the statement of financial position.

The Bank adopted IFRS 16 using the modified retrospective method of adoption with the date of initial application of 1 January 2019. Under this method, the standard is applied retrospectively with the cumulative effect of initially applying the standard recognised at the date of initial application. The Bank elected to use the transition practical expedient to not reassess whether a contract is or contains a lease at 1 January 2019. Instead, the Bank applied the standard only to contracts that were previously identified as leases applying IAS 17 and IFRIC 4 at the date of initial application. The bank also elected to set right of use asset equal to the lease liability as result there is no impact of retained earnings

The Bank has lease contracts for various branches. Before the adoption of IFRS 16, the Bank classified each of its leases (as lessee) at the inception date as either a finance lease or an operating lease. Refer to Note 7.3.4 for the accounting policy prior to 1 January 2019. Upon adoption of IFRS 16, the Bank applied a single recognition and measurement approach for all leases except for short-term leases and leases of low-value assets. Refer to Note 7.3.5 for the accounting policy beginning 1 January 2019. The standard provides specific transition requirements and practical expedients, which have been applied by the Bank.

Leases previously accounted for as operating leases
The Bank recognised right-of-use assets and lease liabilities for those leases previously classified as operating leases, except for short-term leases and leases of low-value assets. The right-of-use assets for most leases were recognised based on the carrying amount as if the standard had always been applied, apart from the use of incremental borrowing rate at the date of initial application. In some leases, the right-of-use assets were recognised based on the amount equal to the lease liabilities, adjusted for any related prepaid and accrued lease payments previously recognised. Lease liabilities were recognised based on the present value of the remaining lease payments, discounted using the incremental borrowing rate at the date of initial application.

The Bank also applied the available practical expedients wherein it:
- Used a single discount rate to a portfolio of leases with reasonably similar characteristics
- Relied on its assessment of whether leases are onerous immediately before the date of initial application
- Excluded the initial direct costs from the measurement of the right-of-use asset at the date of initial application

Based on the above, as at 1 January 2019:
- Right-of-use assets of Kshs 166, million were recognised and presented in the statement of financial position within “Property, Equipment and Right-of-use assets”.
- Additional lease liabilities of Kshs 166 million (included in “Other liabilities”) were recognised.

The adoption of IFRS 16 had no impact on the Bank’s retained earnings and no material impact on its Common Equity Tier 1 (CET1) ratio.

The lease liabilities as at 1 January 2019 can be reconciled to the operating lease commitments as of 31 December 2018, as follows:

Operating lease commitments as at 31 December 2018	267,904
Weighted Average incremental Borrowing rate 1 January 2019	13%
Discounted operating lease commitments 1 January 2019	171,150
Less	
Commitments relating to short term leases	1,903
Commitments relating to leases of low value assets	1,411
Add	
Lease payments relating to renewal periods not included in the operating lease as at 31 December 2018	-
Lease liabilities as at 1 January 2019	167,836

5. Changes in accounting policies and disclosures (continued)

5.1.2 IFRIC Interpretation 23 Uncertainty over Income Tax Treatment. The Interpretation addresses the accounting for income taxes when tax treatments involve uncertainty that affects the application of IAS 12 Income Taxes. It does not apply to taxes or levies outside the scope of IAS 12, nor does it specifically include requirements relating to interest and penalties associated with uncertain tax treatments. The Interpretation specifically addresses the following:

- Whether an entity considers uncertain tax treatments separately
- The assumptions an entity makes about the examination of tax treatments by taxation authorities
- How an entity determines taxable profit (tax loss), tax bases, unused tax losses, unused tax credits and tax rates
- How an entity considers changes in facts and circumstances

The Bank applies significant judgement in identifying uncertainties over income tax treatments. Since the Bank operates in a complex environment, it assessed whether the Interpretation had an impact on its consolidated financial statements. Upon adoption of the Interpretation, the Bank considered whether it has any uncertain tax positions, particularly those relating to transfer pricing. The Bank determined, based on its tax compliance and transfer pricing study, that it is probable that its tax treatments (including those for the subsidiaries) will be accepted by the taxation authorities. The Interpretation did not have an impact on the consolidated financial statements of the Bank.

5.1.3 Amendments to IFRS 9: Prepayment Features with Negative Compensation

Under IFRS 9, a debt instrument can be measured at amortised cost or at fair value through other comprehensive income, provided that the contractual cash flows are 'solely payments of principal and interest on the principal amount outstanding' (the 'SPPI' criterion) and the instrument is held within the appropriate business model for that classification. The amendments to IFRS 9 clarify that a financial asset passes the SPPI criterion regardless of the event or circumstance that causes the early termination of the contract and irrespective of which party pays or receives reasonable compensation for the early termination of the contract. Early termination can result from a contractual term or from an event outside the control of the parties to the contract, such as a change in law or regulation leading to the early termination of the contract. Where the prepayment is made at current fair value or at an amount that includes the fair value of the cost to terminate an associated hedging instrument(s), the Bank assesses the specific contractual cash flows for the relevant debt instruments in order to determine whether they meet the SPPI criterion. These amendments had no impact on the consolidated financial statements of the Bank.

5.1.4 Amendments to IFRS 9: Prepayment Features with Negative Compensation

Interest Rate Benchmark Reform: Amendments to IFRS 9, IAS 39 and IFRS 7 Interest Rate Benchmark Reform Amendments to IFRS 9, IAS 39 and IFRS 7 includes a few reliefs, which apply to all hedging relationships that are directly affected by interest rate benchmark reform. A hedging relationship is affected if the reform gives rise to uncertainties about the timing and or amount of benchmark based cash flows of the hedged item or the hedging instrument.
As indicated in the accounting policies, the Bank elected, as a policy choice permitted under IFRS 9, to continue to apply hedge accounting in accordance with IAS 39. IAS 39 requires that for cash flow hedges, a forecast transaction must be highly probable. IAS 39 also requires that a hedging relationship only qualifies for hedge accounting if the hedging relationship is highly effective in achieving offsetting changes in fair value or cash flows attributable to the hedged risk. The assessment of hedge effectiveness is made prospectively and retrospectively.
As a result of interest rate benchmark reform, there may be uncertainties about the timing and or amount of benchmark-based cash flows of the hedged item or the hedging instrument during the period before the replacement of an existing interest rate benchmark with an alternative nearly risk-free interest rate (an RFR). This may lead to uncertainty whether a forecast transaction is highly probable and whether prospectively the hedging relationship is expected to be highly effective.

Early adoption of standards

The Bank did not early-adopt any new or amended standards in 2019

The principal accounting policies applied in the preparation of the financial statements are set out below. These policies have been applied consistently, except the adoption of the new standards (IFRS 16).

6.0 Basis of Consolidation

The consolidated financial statements comprise the financial statements of the Bank and its subsidiaries as at 31 December 2019. Consolidated bank consolidates a subsidiary when it controls it. Control is achieved when the Bank is exposed, or has rights, to variable returns from its involvement with the investee and has the ability to affect those returns through its power over the investee. When assessing whether it has power over an investee and therefore controls the variability of its returns, the Bank considers all relevant facts and circumstances, including; the purpose and design of the investee, the relevant activities and how decisions about those activities are made and whether the Bank can direct those activities, contractual arrangements such as call rights, put rights and liquidation rights, whether the Bank is exposed, or has rights, to variable returns from its involvement with the investee, and has the power to affect the variability of such returns

When necessary, adjustments are made to the financial statements of subsidiaries to bring their accounting policies in line with the Bank's accounting policies. All intra-group assets, liabilities, equity, income, expenses and cash flows relating to transactions between members of the Bank are eliminated in full on consolidation. Disclosures for investment in subsidiaries, structured entities, securitisations and asset management activities are provided in Note 41.

Investments in subsidiary companies

Investments in subsidiary companies are stated at cost less impairment loss where applicable. The dormant subsidiaries listed in note 41 have no assets and liabilities and are at nil value. Details of the subsidiaries and how they are related to the bank are separately disclosed in note 36.

7 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

7.1 Interest income and expense

Interest income is recorded using the effective interest rate (EIR) method for all financial instruments measured at amortised cost. Interest expense is also calculated using the EIR method for all financial liabilities held at amortised cost. The EIR is the rate that exactly discounts estimated future cash receipts through the expected life of the financial instrument or, when appropriate, a shorter period, to the net carrying amount of the financial asset.

The EIR (and therefore, the amortised cost of the asset) is calculated by taking into account any discount or premium on acquisition, fees and costs that are an integral part of the EIR. The Bank recognises interest income using a rate of return that represents the best estimate of a constant rate of return over the expected life of the loan. Hence, it recognises the effect of potentially different interest rates charged at various stages, and other characteristics of the product life cycle (including prepayments, penalty interest and charges).

If expectations regarding the cash flows on the financial asset are revised for reasons other than credit risk, the adjustment is booked as a positive or negative adjustment to the carrying amount of the asset in the Statement of financial position with an increase or reduction in interest income. The adjustment is subsequently amortised through Interest and similar income in the income statement.

The Bank calculates interest income by applying the EIR to the gross carrying amount of financial assets other than credit-impaired assets. When a financial asset becomes credit-impaired and is, therefore, regarded as 'Stage 3', the Bank calculates interest income by applying the effective interest rate to the net amortised cost of the financial asset. If the financial assets cures and is no longer credit-impaired, the Bank reverts to calculating interest income on a gross basis. Previously unrecognised interest revenue of a cured previously credit impaired financial asset are recognised as a reversal of an impairment loss.

The average effective interest on financial assets held at amortised cost and loans and advances to customers are disclosed under notes 23 and 24 respectively.

7.2 Fees and commissions income and other fees and commissions expense

The Bank earns fee and commission income from a diverse range of financial services it provides to its customers. Fee and commission income is recognised at an amount that reflects the consideration to which the Bank expects to be entitled in exchange for providing the services. The performance obligations, as well as the timing of their satisfaction, are identified, and determined, at the inception of the contract.

When the Bank provides a service to its customers, consideration is recovered immediately upon satisfaction of a service provided at a point in time or at the end of the contract period for a service provided over time

7 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

7.2 Fees and commissions income and other fees and commissions expense (continued)

Services provided where the Bank's performance obligations are satisfied at a point in time are recognised once control of the services is transferred to the customer. This is typically on completion of the underlying transaction or service or, for fees or components of fees that are linked to a certain performance, after fulfilling the corresponding performance criteria. These include fees and commissions arising from negotiating or participating in the negotiation of a transaction for a third party, such as the arrangement/participation or negotiation of the acquisition of shares or other securities, or the purchase or sale of businesses, brokerage and underwriting fees The Bank typically has a single performance obligation with respect to these services, which is to successfully complete the transaction specified in the contract.

7.3 Property, Equipment and Right of use Assets

Property and equipment are stated at cost or as professionally re-valued from time to time less accumulated depreciation and any accumulated impairment losses respectively. Cost comprises expenditure initially incurred to bring the asset to its location and condition ready for its intended use and directly attributable to the acquisition of the asset. The Bank's policy is to regularly revalue property and equipment at least every five years to ensure that the carrying amount is not materially different from its fair value.

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 Group and the cost can be reliably measured. The carrying amount of the replaced part is derecognised. All other repairs and maintenance are recognised in profit or loss during the financial year in which they are incurred.

Any increase arising on the revaluation is recognised in other comprehensive income and accumulated in the revaluation surplus. Decreases that offset previous increases of the same asset are recognised in other comprehensive income and charged against the revaluation surplus; all other decreases are charged to profit or loss.

Addition and disposal

The addition and disposal or decommissioning of property and equipment and intangible assets is done on the date of the acquisition and the date of the disposal respectively.

7.3.2 Depreciation

Depreciation is calculated on a straight-line basis at annual rates estimated to write off the cost of each asset or the revalued amounts, to its residual values over its estimated useful life as follows:

Fixtures, fittings, equipment & ATMs	5 years
Leasehold improvements	8 years or lease period if shorter
Computers	3 years
Motor vehicles	4 years
Buildings	40 years or land lease period if shorter

Land is not depreciated as it is deemed to have an indefinite life.

The depreciation charge to profit and loss is based on the carrying amounts of the property and equipment. The excess of this charge over that based on the historical cost of the property and equipment is released each year from the revaluation surplus to retained earnings.

7.3.3 Intangible assets - computer software costs

Costs incurred on computer software are initially accounted for at cost and subsequently at cost less any accumulated amortisation and accumulated impairment losses. Amortisation is calculated on a straight-line basis over the estimated useful lives not exceeding a period of 5 years.

7.3.4 Leases (Policy applicable before 1 January 2019)

The determination of whether an arrangement is a lease, or contains a lease, is based on the substance of the arrangement and requires an assessment of whether the fulfilment of the arrangement is dependent on the use of a specific asset or assets or whether the arrangement conveys a right to use the asset.

Bank as Lessee
Leases that do not transfer to the Bank substantially all the risks and benefits incidental to ownership of the leased items are operating leases. Operating lease payments are recognised as an expense in the income statement on a straight-line basis over the lease term. Contingent rental payable is recognised as an expense in the period in which they it is incurred.

The Bank as lessor

Leases where the Bank does not transfer substantially all of the risk and benefits of ownership of the asset are classified as operating leases. Rental income is recorded as earned based on the contractual terms of the lease in other operating income. Initial direct costs incurred in negotiating operating leases are added to the carrying amount of the leased asset and recognised over the lease term on the same basis as rental income. Contingent rents are recognised as revenue in the period in which they are earned.

7 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

7.3.5 Leases (Policy applicable after 1 January 2019)

The Bank assesses at contract inception whether a contract is, or contains, a lease. That is, if the contract conveys the right to control the use of an identified asset for a period of time in exchange for consideration.

The Bank as lessee

The Bank applies a single recognition and measurement approach for all leases, except for short-term leases and leases of low-value assets. The Bank recognises lease liabilities to make lease payments and right-of-use assets representing the right to use the underlying assets.

Right-of-use assets
The Bank recognises right-of-use assets at the commencement date of the lease (i.e., the date the underlying asset is available for use). Right-of-use assets are measured at cost, less any accumulated depreciation and impairment losses, and adjusted for any remeasurement of lease liabilities. The cost of right-of-use assets includes the amount of lease liabilities recognised, initial direct costs incurred, and lease payments made at or before the commencement date less any lease incentives received. Right-of-use assets are depreciated on a straight-line basis over the lease term.

Lease liabilities
At the commencement date of the lease, the Bank recognises lease liabilities measured at the present value of lease payments to be made over the lease term. The lease payments include fixed payments (less any lease incentives receivable), variable lease payments that depend on an index or a rate, and amounts expected to be paid under residual value guarantees. The lease payments also include the exercise price of a purchase option reasonably certain to be exercised by the Bank and payments of penalties for terminating the lease, if the lease term reflects exercising the option to terminate.

Variable lease payments that do not depend on an index or a rate are recognised as expenses in the period in which the event or condition that triggers the payment occurs.

Bank as a lessor
Leases in which the Bank does not transfer substantially all the risks and rewards incidental to ownership of an asset are classified as operating leases. Rental income arising is accounted for on a straight-line basis over the lease terms and is included in revenue in the statement of profit or loss due to its operating nature. Initial direct costs incurred in negotiating and arranging an operating lease are added to the carrying amount of the leased asset and recognised over the lease term on the same basis as rental income. Contingent rents are recognised as revenue in the period in which they are earned.

7.3.6 Estimating the incremental borrowing rate

The Bank cannot readily determine the interest rate implicit in the lease, therefore, it uses its incremental borrowing rate (‘IBR’) to measure lease liabilities. The IBR is the rate of interest that the Bank would have to pay to borrow over a similar term, and with a similar security, the funds necessary to obtain an asset of a similar value to the right-of-use asset in a similar economic environment. The IBR therefore reflects what the Bank ‘would have to pay’, which requires estimation when no observable rates are available (such as for subsidiaries that do not enter into financing transactions) or when they need to be adjusted to reflect the terms and conditions of the lease, The Bank estimates the IBR using observable inputs (such as market interest rates) when available and is required to make certain entity-specific adjustments (such as the subsidiary’s stand-alone credit rating, or to reflect the terms and conditions of the lease).
IFRS

7.3.7 Impairment of non-financial assets

At the reporting date, the Bank reviews the carrying amount of its tangible and intangible assets to determine whether there is any indication that these assets have suffered an impairment loss.

If objective evidence on impairment losses exists, the recoverable amount of the asset is estimated in order to determine the extent of the impairment loss. The carrying amount of the asset is reduced through the use of an allowance account and the amount of the loss is recognised in the profit or loss. In cases where the asset is carried at revalued amount, the impairment loss is treated as a revaluation decrease. In determining the recoverable amount, the Bank considers the higher of the fair value of the asset less costs to sell, and value in use. In estimating value in use, the Bank is cognisant of the estimated future cash flows discounted to the present value using a pre-tax discount rate that is reflective of the current market assessment of time value of money and the risks specific to the asset itself.

Intangible assets with indefinite useful life are tested for impairment annually, and when there is indication that the asset may be impaired.

Where impairment loss subsequently reverses, the carrying amount of the asset (or cash-generating unit) is increased to the revised estimate of its recoverable amount, but so that the increased carrying amount does not exceed the carrying amount that would have been determined had no impairment loss been recognised, unless such asset is carried at revalued amount, in which case the reversal of the impairment loss is treated as revaluation income.

7 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

7.4 Foreign currencies

7.4.1 Functional and presentation currency

The financial statements of the Bank are measured using the currency of the primary economic environment in which the Bank operates ('the functional currency'). The financial statements are presented in Kenya shillings, which is the Bank's functional and presentation currency. Except as indicated, financial information presented in Kenya shillings has been rounded to the nearest thousand (Kshs'000).

7.4.2 Transactions and balances

Foreign currency transactions that are transactions denominated, or that requires settlement, in a foreign currency are translated into the functional currency using the exchange rates prevailing at the dates of the transactions. At the reporting date, monetary items denominated in foreign currencies are retranslated at the rates prevailing at that date. Non-monetary items carried at fair value that are denominated in foreign currencies are retranslated at the rates prevailing at the date when fair value was determined. Non-monetary items that are measured in terms of historical cost in a foreign currency are not retranslated.

Foreign exchange gains and losses resulting from the settlement of such transactions and from the translation at year end exchange rates of monetary assets and liabilities denominated in foreign currencies are recognised through profit or loss.

7.4.3 Foreign exchange contracts

Foreign exchange contracts include open spot contracts and foreign exchange forward contracts. These instruments are valued by either observable foreign exchange rates and observable or calculated forward points. These forwards and spot contracts are in foreign exchange deals carried out in the interbank markets. These are held for risk management purposes and therefore include hedges that are economic hedges, but do not meet the hedge accounting requirements. Most of the trading portfolio is within the Bank's investment banking division (Treasury Department) and is treated as trading risk for risk management purposes.

7.5 Taxation

7.5.1 Current tax

Current income tax assets and liabilities are measured at the amounts expected to be recovered from or paid to the taxation authorities. The tax rates and tax laws used to compute the amount are those that are enacted or substantively enacted at the reporting date. Current income tax relating to items recognised outside profit or loss is recognised outside profit or loss. Current income tax items are recognised in correlation to the underlying transaction either in profit or loss, other comprehensive income or directly in equity.

7.5.2 Deferred income tax

Deferred income tax is provided using the liability method on temporary differences between the tax bases of assets and liabilities and their carrying amounts for financial reporting purposes at the reporting date. Deferred tax liabilities are recognised for all taxable temporary differences, except:

(i) where the deferred tax liability arises from the initial recognition of goodwill or of an asset or liability in a transaction that is not a business combination and, at the time of the transaction, affects neither the accounting profit nor taxable profit or loss; and
(ii) in respect of taxable temporary differences associated with investments in subsidiaries, associates and interests in joint ventures, where the timing of the reversal of the temporary differences can be controlled and it is probable that the temporary differences will not reverse in the foreseeable future.

7 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

7.5 Taxation (Continued)

7.5.2 Deferred income tax (continued)

Deferred income tax assets are recognised for all deductible temporary differences, carry forward of unused tax credits and unused tax losses, to the extent that it is probable that taxable profit will be available against which the deductible temporary differences, and the carry forward of unused tax credits and unused tax losses can be utilised except:

(i) where the deferred tax asset relating to the deductible temporary difference arises from the initial recognition of an asset or liability in a transaction that is not a business combination and, at the time of the transaction, affects neither the accounting profit nor taxable profit or loss; and
(iii) in respect of deductible temporary differences associated with investments in subsidiaries, associates and interests in joint ventures, deferred tax assets are recognised only to the extent that it is probable that the temporary differences will reverse in the foreseeable future and taxable profit will be available against which the temporary differences can be utilised.

The carrying amount of deferred tax assets is reviewed at each reporting date and reduced to the extent that it is no longer probable that sufficient taxable profit will be available to allow all or part of the deferred tax asset to be utilised. Unrecognised deferred tax assets are reassessed at each reporting date and are recognised to the extent that it has become probable that future taxable profit will allow the deferred tax asset to be recovered.

Deferred tax assets and liabilities are measured at the tax rates that are expected to apply to the year when the asset is realised or the liability is settled, based on tax rates (and tax laws) that have been enacted or substantively enacted at the end of reporting period. Deferred income tax relating to items recognised outside profit or loss is recognised outside profit or loss. Deferred tax items are recognised in correlation to the underlying transaction either in profit or loss, other comprehensive income or directly in equity.

Deferred tax assets and deferred tax liabilities are offset if a legally enforceable right exists to set off current tax assets against current tax liabilities and the deferred taxes relate to the same taxable entity and the same taxation authority. The Finance Act 2015 varied the period to carry forward the tax losses from 5 years to 10 years.

Value Added Tax
Revenues, expenses and assets are recognised net of the amount of value added tax except where the value added tax incurred on a purchase of assets or services is not recoverable from the Kenya Revenue Authority (KRA), in which case the value added tax is recognised as part of the cost of acquisition of the asset or as part of the expense item as applicable; and receivables and payables that are stated with the amount of value added tax included.

The net amount of value added tax recoverable from, or payable to tax authorities is included as part of receivables or payables in the statement of financial position.
Financial instruments

A financial asset or liability is recognised when the Bank becomes party to the contractual provisions of the instrument.

7.6 Financial instruments

7.6.1 Date of initial recognition

Financial assets and liabilities, with the exception of loans and advances to customers and balances due to customers, are initially recognised on the trade date, i.e., the date that the Bank becomes a party to the contractual provisions of the instrument. This includes regular way trades: purchases or sales of financial assets that require delivery of assets within the time frame generally established by regulation or convention in the market place. Loans and advances to customers are recognised when funds are disbursed to the customers' accounts. The Bank recognises balances due to customers when funds are transferred to the Bank.

7.6.2 Initial measurement of financial instruments
The classification of financial instruments at initial recognition depends on their contractual terms and the business model for managing the instruments, as described in Notes 7.6.4 to 7.6.9
The classification of financial instruments at initial recognition depends on their contractual terms and the business model for managing the instruments. Financial instruments are initially measured at their fair value except in the case of financial assets and financial liabilities recorded at FVPL, transaction costs are added to, or subtracted from, this amount.

7 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

7.6 Financial instruments (continued)

7.6.3 Day 1 profit or loss

When the transaction price of the instrument differs from the fair value at origination and the fair value is based on a valuation technique using only inputs observable in market transactions, the Bank recognises the difference between the transaction price and fair value in net trading income. In those cases where fair value is based on models for which some of the inputs are not observable, the difference between the transaction price and the fair value is deferred and is only recognised in profit or loss when the inputs become observable, or when the instrument is derecognised

7.6.4 Classification and measurement

The Bank classifies all of its financial assets based on the business model for managing the assets and the asset's contractual terms, measured at either:

- Amortised cost, as explained in Note 7.6.5
- FVOCI, as explained in Note 7.6.8

Financial liabilities, other than loan commitments and financial guarantees, are measured at amortised cost or at FVPL when they are held for trading.

7.6.5 Due from banks, loans and advances to customers, financial investments at amortised cost

The Bank measures Due from banks, Loans and advances to customers and other financial investments at amortised cost only if both of the following conditions are met:

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

An analysis of the gross carrying amount, maximum exposure to credit risk based on the bank's internal credit grading system and year end classification and the corresponding ECLs for the loans and advances to customers and balances due from other banking institutions is shown in note 10.6.

7.6.6 Business model assessment

The Bank determines its business model at the level that best reflects how it manages groups of financial assets to achieve its business objective:

- The risks that affect the performance of the business model (and the financial assets held within that business model) and, in particular, the way those risks are managed
- How managers of the business are compensated (for example, whether the compensation is based on the fair value of the assets managed or on the contractual cash flows collected)

The expected frequency, value and timing of sales are also important aspects of the Bank's assessment. The business model assessment is based on reasonably expected scenarios without taking 'worst case' or 'stress case' scenarios into account. If cash flows after initial recognition are realised in a way that is different from the Bank's original expectations, the Bank does not change the classification of the remaining financial assets held in that business model, but incorporates such information when assessing newly originated or newly purchased financial assets going forward.

7.6.7 SPPI Test

As a second step of its classification process the Bank assesses the contractual terms of financial assets to identify whether they meet the SPPI test. Principal' for the purpose of this test is defined as the fair value of the financial asset at initial recognition and may change over the life of the financial asset (for example, if there are repayments of principal or amortisation of the premium/discount). The most significant elements of interest within a lending arrangement are typically the consideration for the time value of money and credit risk. To make the SPPI assessment, the Bank applies judgement and considers relevant factors such as the currency in which the financial asset is denominated, and the period for which the interest rate is set.

7 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

7.6 Financial instruments (continued)

7.6.8 Equity instruments at FVOCI

The bank holds quoted equity shares and has elected to classify this as equity instruments at FVOCI. Gains and losses on these equity instruments are recognised through other comprehensive income. Dividends are recognised in profit or loss as other operating income when the right of the payment has been established. Equity instruments at FVOCI are not subject to an impairment assessment.

7.6.9 Debt issued and other borrowed funds

After initial measurement, debt issued and other borrowed funds are subsequently measured at amortised cost. Amortised cost is calculated by taking into account any discount or premium on issue funds, and costs that are an integral part of the EIR. A compound financial instrument which contains both a liability and an equity component is separated at the issue date.

The bank issued a medium term note of seven years in July 2012. The medium-term notes issued by the bank do not have a conversion, write down or call option. The details of the of the medium-term notes are disclosed in note 33

Financial assets and financial liabilities at fair value through profit or loss

Financial assets and financial liabilities in this category are those that are not held for trading and have been either designated by management upon initial recognition or are mandatorily required to be measured at fair value under IFRS 9. Management only designates an instrument at FVPL upon initial recognition when one of the following criteria are met. Such designation is determined on an instrument-by-instrument basis:

- The designation eliminates, or significantly reduces, the inconsistent treatment that would otherwise arise from measuring the assets or liabilities or recognising gains or losses on them on a different basis or
- The liabilities (and assets until 1 January 2018 under IAS 39) are part of a group of financial liabilities (or financial assets, or both under IAS 39), which are managed and their performance evaluated on a fair value basis, in accordance with a documented risk management or investment strategy or
- The liabilities (and assets until 1 January 2018 under IAS 39) containing one or more embedded derivatives, unless they do not significantly modify the cash flows that would otherwise be required by the contract, or it is clear with little or no analysis when a similar instrument is first considered that separation of the embedded derivative(s) is prohibited

7.7 Impairment of Financial assets

7.7.1 Over view of the expected credit loss ± ECL principle

The adoption of IFRS 9 has fundamentally changed the Bank's loan loss impairment method by replacing IAS 39's incurred loss approach with a forward-looking ECL approach. From 1 January 2018, the Bank has been recording the allowance for expected credit losses for all loans and other debt financial assets not held at FVPL, together with loan commitments and financial guarantee and letters of credit contracts, in this section all referred to as 'financial instruments'. Equity instruments are not subject to impairment under IFRS 9.

The ECL allowance is based on the credit losses expected to arise over the life of the asset (the lifetime expected credit loss or LTECL), unless there has been no significant increase in credit risk since origination, in which case, the allowance is based on the 12 months' expected credit loss (12mECL). The Bank's policies for determining if there has been a significant increase in credit risk are set out in note 10.6.

7 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

7.7 Impairment of Financial assets (continued)

7.7.2 ECLs

The Bank has established a policy to perform an assessment, at the end of each reporting period, of whether a financial instrument's credit risk has increased significantly since initial recognition, by considering the change in the risk of default occurring over the remaining life of the financial instrument.

Based on the above process, the Bank groups its loans into Stage 1, Stage 2, Stage 3 as described below:

Staging	Internal Rating Description	12 Months Basel III PD range	External Rating Equivalent
Stage 1	Performing	0.00% - 0.50%	Very Good
Stage 2	Significant increase in credit risk	0.50% - 11.7%	Good
Stage 3	Non-performing	11.7% - 100.00%	Bad

Stage 1: These are financial instruments that are performing in accordance with contractual terms and are expected to continue to do so since there are no signs or deterioration in credit risk or circumstances of the borrower from initial recognition. The bank recognises impairment allowance based on 12 months ECL.

Stage 2: These are financial instruments that have exhibited potential weaknesses which may if not corrected weaken the asset. The financial instruments have shown significant increase in credit risk and hence the bank recognises impairment allowance on the life time ECL

Stage 3: These financial instruments that are credit impaired. The bank considers financial instruments credit impaired when the borrower becomes 90 days past due on its contractual payments. Other qualitative considerations include existence of events and circumstances that indicates that the borrower is unlikely to pay.

Calculation of ECL

The key components and the mechanics behind the computation of the ECL are outlined below

PD: The probability of default is an estimate of the likelihood of default over a given time horizon. A default may only happen at a certain time over the assessed period, if the facility has not been previously derecognised and is still in the portfolio. The bank models its PDs at sector level using survival analysis over a defined period.

EAD: Exposure at Default is an estimate of the exposure at a future default date, taking into account expected changes in the exposure after the reporting date, including repayments of principal and interest, whether scheduled by contract or otherwise, expected drawdowns on committed facilities, and accrued interest from missed payments.

LGD: The Loss Given Default is an estimate of the loss arising in the case where a default occurs at a given time. It is based on the difference between the contractual cash flows due and those that the lender would expect to receive, including from the realisation of any collateral. It is usually expressed as a percentage of the EAD.

The PD and LGD investment in government securities and bonds are considered negligible, approximating 0%. These are risk free instruments and there is no historical loss situation.

Undrawn Loan commitments guarantees and letters of credit
When estimating LTECLs for undrawn loan commitments, the Bank estimates the expected portion of the loan commitment that will be drawn down over its expected life. Details of the gross carrying exposure and the corresponding ECL are disclosed in note 5(a).

7 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

7.7 Impairment of Financial assets (continued)

7.7.3 Forward looking information

The bank has included a forward looking macro-economic overlay in its ECL model. The bank relies on the following economic indicators to develop. The bank adopts the following data sets for analysis of macroeconomic over lay;

Historical industry and Bank's non-performing loans
Historical macroeconomic statistics. The adopted macroeconomic factors include;

- Gross Domestic Product – GDP
- Inflation – consumer price index
- Exports
- Lending rates
- Exchange rates – effective

Forecast macroeconomic data
This is then regressed against Banks Non-performing loans in order to determine a relationship with the Macro economic variables.

To eliminate biasness and ensure there is probability weighting, the bank adopts base, worst and best-case forecasts adjustment factors to obtain a probability weighted PD. The weights are determined based on coefficient of determination (R2). R2 provides the Base while an even split of 1-R2 provides the weights for best and worst-case scenarios.

Collateral valuation
To mitigate its credit risks on financial assets, the Bank seeks to use collateral, where possible. The collateral comes in various forms, such as cash, securities, letters of credit/guarantees, real estate, receivables, inventories, other non-financial assets and credit enhancements such as netting agreements. The Bank's accounting policy for collateral assigned to it through its lending arrangements under IFRS 9 is the same is it was under IAS 39. The fair value of collateral affects the calculation of ECLs. The fair value of collateral values is disclosed in note 10.6.

7.7.4 Write off

The Bank's accounting policy under IFRS 9 remains the same as it was under IAS 39. Financial assets are written off either partially or in their entirety only when the Bank has stopped pursuing the recovery i.e. after exhausting all recovery efforts. If the amount to be written off is greater than the accumulated loss allowance, the difference is charged to the profit and loss account. Any subsequent recoveries are recognised as income through the profit and loss account.

7.8 Financial liabilities and equity instruments issued by the Bank

a) Classification and measurement

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

i) Equity instruments

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

ii) Other financial liabilities

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

Other financial liabilities are subsequently measured at amortised cost using the effective interest method, with interest expense recognised on an effective yield basis. The effective interest method is a method of calculating the amortised cost of a financial liability and of allocating interest expense over the relevant period. The effective interest rate is the rate that exactly discounts estimated future cash payments through the expected life of the financial liability, or (where appropriate) a shorter period, to the net carrying amount on initial recognition.

7 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

7.8 Financial liabilities and equity instruments issued by the Bank

b) Derecognition of financial liabilities

A financial liability is derecognised when the obligation under the liability is discharged or cancelled or expires. Where an existing financial liability is replaced by another from the same lender on substantially different terms, or the terms of an existing liability are substantially modified, such an exchange or modification is treated as a derecognition of the original liability and the recognition of a new liability. The difference between the carrying value of the original financial liability and the consideration paid is recognised in profit or loss. The Bank derecognises financial liabilities when, and only when, the Bank's obligations are discharged, cancelled or they expire.

c) Offsetting

Financial assets and liabilities are offset and stated at net amount in the statement of financial position when 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.

d) Provisions

A provision is recognised if, as a result of a past event, the Bank has a present legal or constructive obligation that can be estimated reliably, and it is probable that an outflow of economic benefits will be required to settle the obligation. Provisions are determined by discounting the expected future cash flows at a pre-tax rate that reflects current market assessments of the time value of money and, where appropriate, the risks specific to the liability.

7.9 Revolving credit facilities

The Bank's product offering includes a variety of corporate and retail overdraft and revolving loan facilities, in which the Bank has the right to cancel and/or reduce the facilities with one day's notice. The Bank does not limit its exposure to credit losses to the contractual notice period, but, instead calculates ECL over a period that reflects the Bank's expectations of the customer behaviour, its likelihood of default and the Bank's future risk mitigation procedures, which could include reducing or cancelling the facilities. Based on past experience and the Bank's expectations, the period over which the Bank calculates ECLs for these products, is five years for corporate and seven years for retail products. The interest rate used to discount the ECL for credit cards and overdrafts is based on the average effective interest rate that is expected to be charged over the expected period of exposure to the facilities. This estimation considers that many facilities are repaid in full each month and are consequently not charged interest.

7.10 Statutory reserve

IFRS 9 requires the Bank to record an allowance for ECLs for all loans and other debt financial assets not held at FVTPL together with loan commitments and financial guarantee contracts. The allowance is based on the ECLs associated with the probability of default in the next twelve months unless there has been a significant increase in credit risk since origination. However, Central Bank of Kenya prudential guidelines require the Bank to set aside amounts for impairment losses on loans and advances in addition to those losses that have been recognised under IFRS 9. Any such amounts set aside represent appropriations of retained earnings and not expenses in determining profit or loss. These amounts are dealt with in the statutory reserve.

7.11 Cash and cash equivalents

Cash and cash equivalents include cash in hand, unrestricted balances held with the Central Bank of Kenya and highly liquid financial assets with original maturities of less than three months, which are subject to insignificant risk of changes in their fair value, and are used by the Bank in the management of its short-term commitments. Cash and cash equivalents are carried at amortised cost in the statement of financial position.

7 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

7.12 Contingent liabilities

Letters of credit, acceptances, guarantees and performance bonds are generally written by the Bank to support 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. These obligations are accounted for as off-balance sheet transactions and disclosed as contingent liabilities. Uncertainty about these assumptions and estimates could result in outcomes that require a material adjustment to the carrying amounts of assets or liabilities affected in future periods. In calculating ECL the three-stage impairment approach is extended to apply to cover the off balance sheet items. The bank considers the nominal contractual values of financial guarantees and letters of credit net of collateral in determining the loss given default LGDs. The nominal values for the undrawn loan commitments and overdrafts is determined using a credit conversion factor calculated using the monthly average utilization over the history of the available data. The nominal values of these instruments together with the corresponding ECL are disclosed in Note 10.6.3.4

7.13 Employee benefit costs

The Bank operates a defined contribution retirement benefit scheme for all its employees. The scheme is administered by an independent investment management company and is funded by contributions from both the Bank and employees.

The Bank also contributes to the statutory National Social Security Fund. This is a defined contribution scheme registered under the National Social Security Fund Act. The obligations under the scheme are limited to specific contributions legislated from time to time.

The Bank's contributions in respect of retirement benefit costs are charged to the profit and loss in the year to which they relate.

Employee entitlement to leave not taken is charged to profit or loss as it accrues.

8. CRITICAL JUDGEMENTS AND KEY SOURCES OF ESTIMATION UNCERTAINTY

The preparation of the Bank's consolidated financial statements requires management to make judgements, estimates and assumptions that affect the reported amount of revenues, expenses, assets and liabilities, and the accompanying disclosures, as well as the disclosure of contingent liabilities. Uncertainty about these assumptions and estimates could result in outcomes that require a material adjustment to the carrying amount of assets or liabilities affected in future periods. In the process of applying the Bank's accounting policies, management has made the following judgements and assumptions concerning the future and other key sources of estimation uncertainty at the reporting date, that have a significant risk of causing a material adjustment to the carrying amounts of assets and liabilities within the next financial year. The estimates and associated assumptions are based on historical experience and other factors that are considered to be relevant including expectations of future events that are believed to be reasonable under the circumstances. Actual results may differ from these estimates.

Items with the most significant effect on the amounts recognised in the consolidated financial statements with substantial management judgement and/or estimates are collated below with respect to judgements/estimates involved.

8.1 Impairment losses on financial instruments

The measurement of impairment losses both under IFRS 9 across all categories of financial assets in scope requires judgement, in particular, the estimation of the amount and timing of future cash flows and collateral values when determining impairment losses and the assessment of a significant increase in credit risk. These estimates are driven by a number of factors, changes in which can result in different levels of allowances.

8. CRITICAL JUDGEMENTS AND KEY SOURCES OF ESTIMATION UNCERTAINTY (continued)

8.1 Impairment losses on financial instruments (continued)

The Bank's ECL calculations are outputs of complex models with a number of underlying assumptions regarding the choice of variable inputs and their interdependencies. Elements of the ECL models that are considered accounting judgements and estimates include:

- The Bank's internal credit grading model, which assigns PDs to the individual grades
- The Bank's criteria for assessing if there has been a significant increase in credit risk and so allowances for financial assets should be measured on a LTECL basis and the qualitative assessment
- The segmentation of financial assets when their ECL is assessed on a collective basis
- Development of ECL models, including the various formulas and the choice of inputs
- Determination of associations between macroeconomic scenarios and, economic inputs, such as unemployment levels and collateral values, and the effect on PDs, EADs and LGDs
- Selection of forward-looking macroeconomic scenarios and their probability weightings, to derive the economic inputs into the ECL models It has been the Bank's policy to regularly review its models in the context of actual loss experience and adjust when necessary.

8.2 Going Concern assessment

The Bank's management has made an assessment of its ability to continue as a going concern and is satisfied that it has the resources to continue in business for the foreseeable future. Furthermore, management is not aware of any material uncertainties that may cast significant doubt on the Bank's ability to continue as a going concern. Therefore, the financial statements continue to be prepared on the going concern basis.

8.3 Property, equipment and intangible assets

Critical estimates are also involved in the determination of fair values of property and equipment including the depreciation rates and residual values for property, equipment and intangible assets.

8.4 Contingent Liabilities

The Bank operates in a regulatory and legal environment that, by nature, has a heightened element of litigation risk inherent to its operations. As a result, it is involved in various litigation proceedings in Kenya arising in the ordinary course of the Bank's business. When the Bank can reliably measure the outflow of economic benefits in relation to a specific case and considers such outflows to be probable, the Bank records a provision against the case. Where the probability of outflow is considered to be remote, or probable, but a reliable estimate cannot be made, a contingent liability is disclosed. However, when the Bank is of the opinion that disclosing these estimates on a case-by-case basis would prejudice their outcome, then the Bank does not include detailed, case-specific disclosers in its financial statements. Given the subjectivity and uncertainty of determining the probability and amount of losses, the Bank takes into account a number of factors including legal advice, the stage of the matter and historical evidence from similar incidents. Significant judgement is required to conclude on these estimates. The details of the cases and resultant contingent liability are disclosed in note 43.

8.5.0 Taxation

The Bank is subjected to numerous taxes and levies by various government and quasi- government regulatory bodies. As a rule of thumb, the Bank recognises liabilities for the anticipated tax /levies payable with utmost care and diligence. However, significant judgement is usually required in the interpretation and applicability of those taxes /levies. Should it come to the attention of management, in one way or the other, that the initially recorded liability was erroneous, such differences will impact on the income and liabilities in the period in which such differences are determined.

8.5.1 Deferred income tax

Deferred income tax is provided using the liability method on temporary differences at the end of the reporting period between the tax bases of assets and liabilities and their carrying amounts for financial reporting purposes. Deferred tax liabilities are recognised for all taxable temporary differences, except:

a) where the deferred tax liability arises from the initial recognition of goodwill or of an asset or liability in a transaction that is not a business combination and, at the time of the transaction, affects neither the accounting profit nor taxable profit or loss; and
b) in respect of taxable temporary differences associated with investments in subsidiaries, associates and interests in joint ventures, where the timing of the reversal of the temporary differences can

8. CRITICAL JUDGEMENTS AND KEY SOURCES OF ESTIMATION UNCERTAINTY (continued)

8.5.1 Deferred income tax (continued)

be controlled and it is probable that the temporary differences will not reverse in the foreseeable future.

Deferred income tax assets are recognised for all deductible temporary differences, carry forward of unused tax credits and unused tax losses, to the extent that it is probable that taxable profit will be available against which the deductible temporary differences, and the carry forward of unused tax credits and unused tax losses can be utilised except:

a) where the deferred tax asset relating to the deductible temporary difference arises from the initial recognition of an asset or liability in a transaction that is not a business combination and, at the time of the transaction, affects neither the accounting profit nor taxable profit or loss; and,
b) in respect of deductible temporary differences associated with investments in subsidiaries, associates and interests in joint ventures, deferred tax assets are recognised only to the extent that it is probable that the temporary differences will reverse in the foreseeable future and taxable profit will be available against which the temporary differences can be utilised.

The carrying amount of deferred tax assets is reviewed at each end of the reporting period and reduced to the extent that it is no longer probable that sufficient taxable profit will be available to allow all or part of the deferred tax asset to be utilised. Unrecognised deferred tax assets are reassessed at each end of the reporting period and are recognised to the extent that it has become probable that future taxable profit will allow the deferred tax asset to be recovered.

The Bank offsets deferred tax assets and deferred tax liabilities if and only if it has a legally enforceable right to set off current tax assets and current tax liabilities and the deferred tax assets and deferred tax liabilities relate to income taxes levied by the same taxation authority on the same taxable entity.

Deferred tax assets and liabilities are measured at the tax rates that are expected to apply to the year when the asset is realised or the liability is settled, based on tax rates (and tax laws) that have been enacted or substantively enacted at the end of reporting period. Deferred income tax relating to items recognised outside profit or loss is recognised outside profit or loss. Deferred tax items are recognised in correlation to the underlying transaction either in profit or loss, other comprehensive income or directly in equity.

8.6 Estimating the incremental borrowing

The Bank cannot readily determine the interest rate implicit in the lease, therefore, it uses its incremental borrowing rate ('IBR') to measure lease liabilities. The IBR is the rate of interest that the Bank would have to pay to borrow over a similar term, and with a similar security, the funds necessary to obtain an asset of a similar value to the right-of-use asset in a similar economic environment. The IBR therefore reflects what the Bank 'would have to pay', which requires estimation when no observable rates are available or when they need to be adjusted to reflect the terms and conditions of the lease.

8.7. Effective Interest Rate (EIR) method

The Bank's EIR method, recognises interest income using a rate of return that represents the best estimate of a constant rate of return over the expected behavioral life of loans and deposits and recognises the effect of potentially different interest rates charged at various stages and other characteristics of the product life cycle (including prepayments and penalty interest and charges). This estimation, by nature, requires an element of judgement regarding the expected behavior and life-cycle of the instruments, as well expected changes to the Bank's base rate and other fee income/expense that are integral parts of the instrument.

8.8 Credit cards and other revolving facilities

The Bank's product offering includes a variety of corporate and retail overdraft and credit cards facilities, in which the Bank has the right to cancel and/or reduce the facilities with sufficient notice. The Bank does not limit its exposure to credit losses to the contractual notice period, but, instead calculates ECL over an estimated time frame that reflects its expectations of customer behaviour, the likelihood of default and its future risk mitigation procedures, which could include reducing or cancelling the facilities.

The ongoing assessment of whether a significant increase in credit risk has occurred for revolving facilities is similar to other lending products. This is based on shifts in the customer's internal credit grade, but greater emphasis is also given to qualitative factors such as changes in usage.

The interest rate used to discount the ECL for credit cards is based on the average effective interest rate that is expected to be charged over the expected period of exposure to the facilities. This estimation takes into account that many facilities are repaid in full each month and are consequently not charged interest.

The calculation of ECL, including the estimation of the expected period of exposure and discount rate is made, on an individual basis.

9 GOING CONCERN

The bank incurred a loss after tax of Kshs 529 million during the year ended 31 December 2019 (2018: Kshs 540 million) and accumulated losses stood at Kshs 2.6billion (2018: Kshs 2.1billion) as of that date. Further, as at 31 December 2019, the Bank had a total regulatory capital/risk weighted assets ratio of 13.5% (2018: 1.05%) against a regulatory minimum ration of 14.5%.

The losses have largely been attributable to the bank's inability to implement its business plan due to severe capital and liquidity constraints experienced over the last four years as well as adverse macroeconomic and operating conditions such as the capping of interest rates which reduced the bank's margins by about 30%.

As disclosed in note 47, Events after the reporting period, the developments surrounding COVID-19 have a profound impact on global society, the operational and financial performance of organisations and the assessment of the ability to continue as a going concern. The situation changes on a daily basis giving rise to inherent uncertainty.

The bank however received a fresh capital injection of Kshs 1.6 billion on 22 October 2019 from the National Treasury, the majority shareholder. This amount enabled the bank to not only settle the Medium Term Note of Kshs 1.52 billion which matured on 22 July 2019 and whose maturity was extended to 22 October 2019 but also significantly boosted the capital levels and regulatory capital ratios. On 30 January 2020 the shareholders, through an Extraordinary General Meeting (EGM), approved the allocation of additional 80,000,000 ordinary shares to the National Treasury in lieu of the capital injection. The National Treasury's shareholding has consequently increased to 93.4%.

As a result of this capital injection the bank's core capital improved to Kshs 1.153 billion in December 2019 from Kshs 58 million in December 2018. The bank's prudential capital ratios also improved as follows;

Prudential Capital Ratio	2019	2018	Minimum Capital Ratio
Core Capital to Deposits	13.10%	0.70%	8.00%
Core capital to Risk weighted assets	11.40%	0.50%	10.50%
Total Capital to Risk weighted assets	13.50%	1.00%	14.50%

The bank has since met all the prudential capital ratios except the total capital to risk weighted assets, which is being addressed through a planned reorganisation of the balance sheet.

In addition, the Board of Directors and management have also put in place a three year strategic plan which targets to reduce the operating losses by 64% in 2020, and turn around to profitability in 2021.

The improved capital position from the measures above, will be enough to enable the bank to implement its business plan for 2020 as it works with the Privatisation Commission and the National Treasury to finalise the privatisation process which is expected to bring on board a strategic investor and enable the bank to sustainably access capital for future growth.

Furthermore, due to the capital injection, the bank's liquidity position has improved significantly. The additional capital injection in the year eased pressure on the bank from interbank borrowing further reducing by 60%. The bank expects to significantly pay off borrowing from the market within the year 2020, which in turn would minimize borrowing costs and increase the bank's lending ability eventually leading to overall profitability.

The removal of the interest rate capping in November 2019 is also expected to improve the situation in the banking sector by enabling banks to price risk while ensuring fairness and transparency.

Based on the foregoing Management and the Board has assessed the bank's ability to continue as a going concern and is satisfied that it has the requisite resources to continue in business for the foreseeable future. Therefore, the financial statements continue to be prepared on the going concern basis. This basis of preparation presumes that the Bank will realize its assets and discharge its liabilities in the ordinary course of business.

10. RISK MANAGEMENT OBJECTIVES AND POLICIES

10.1 RISK

The Bank defines risk as the possibility that the outcome of an action or event could bring about adverse impacts on the institution's capital or earnings. Such outcomes could either result in direct loss of earnings/capital or may result in imposition of constraints on bank's ability to meet its business objectives. Whilst risk is inherent in the Bank's activities, it is managed through an integrated risk management framework, including ongoing identification, measurement and monitoring, and subject to risk limits and other controls. This process of risk management is critical to the Bank's continuing profitability and each individual within the Bank is accountable for the risk exposures relating to his or her responsibilities. The Bank is exposed to credit risk, liquidity risk and market risk, operational risk, strategic risk, reputational and regulatory & compliance risks.

10.2 Risk management structure

The Board of Directors has overall responsibility for the establishment and oversight of the Bank's risk management framework. The board has established a risk management committee comprising of three non-Executives Directors to assist in the discharge of this responsibility. The board has also established the Bank Asset and Liability (ALCO), Credit and Operational Risk committees, which are responsible for developing and monitoring risk management policies in their specified areas. These committees comprise of executive members and report regularly to the board of Directors on their activities.

The Board provides written principles for overall risk management as well as written policies covering specific risk areas. The Bank's risk management policies are established to identify and analyse the risks faced by the Bank, to set appropriate risk limits and controls, and to monitor risks and adherence to limits. Risk management policies and systems are reviewed regularly to reflect changes in market conditions, products and best market practices. The Bank, through its training 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 Audit Committee is responsible for monitoring compliance with the Bank's risk management policies and procedures, and for reviewing the adequacy of the risk management framework in relation to the risks faced by the Bank. This committee is assisted in these functions by the Internal Audit Function. The Internal Audit Function undertakes reviews of risk management controls and procedures, the results of which are reported to the committee.

10.3 Risk Mitigation and Risk Culture

As part of its overall risk management, the Bank uses derivatives and other instruments to manage exposures resulting from changes in interest rates, foreign currencies, equity risks, credit risks, and exposures arising from forecast transactions. In accordance with the Bank's policy, its risk profile is assessed before entering into hedging transactions which are authorised by the Assets Liability Committee (ALCO) of the bank. The effectiveness of all the hedge relationships is monitored by the Treasury function on a daily basis and ALCO on a monthly basis. It is the Bank's policy that in situations of ineffectiveness, it will enter into a new hedge relationship to mitigate risk on a continuous basis. The Bank actively uses collateral to reduce its credit risks.

10.4 Risk measurement and reporting systems

The Bank's risks are measured using a method that reflects both the expected loss likely to arise in normal circumstances and unexpected losses, which are an estimate of the ultimate actual loss based on statistical models. The models make use of probabilities derived from historical experience, adjusted to reflect the economic environment. The Bank also runs worst-case scenarios that would arise in the event that extreme events which are unlikely to occur do, in fact, occur.
Monitoring and controlling risks is primarily performed based on limits established by the Bank. These limits reflect the business strategy and market environment of the Bank as well as the level of risk that the Bank is willing to accept, with additional emphasis on selected industries. In addition, the Bank's policy is to measure and monitor the overall risk-bearing capacity in relation to the aggregate risk exposure across all risk types and activities.

Information compiled from all of the businesses is processed in order to analyse, control and identify risks on a timely basis. This information is presented and explained to the Board of Directors, the Board Risk Committee, and the Executive Committee EXCOM. The report includes aggregate credit exposure, credit metric forecasts, hold limit exceptions, VaR, liquidity ratios and risk profile changes. On a monthly basis, detailed reporting of industry, customer and geographic risks takes place. Senior management assesses the appropriateness of the allowance for credit losses on a monthly basis. The Board Risk Committee receives a comprehensive risk report once a quarter which is designed to provide all the necessary information to assess and conclude on the risks of the Bank.

10. Risk Management objectives and policies continued

10.5 Excessive Risk Concentration

Concentrations arise when a number of counterparties are engaged in similar business activities, or activities in the same geographical region, or have similar economic features that would cause their ability to meet contractual obligations to be similarly affected by changes in economic, political or other conditions. Concentrations indicate the relative sensitivity of the Bank's performance to developments affecting a particular industry or geographical location.
In order to avoid excessive concentrations of risk, the Bank's policies and procedures include specific guidelines to focus on maintaining a diversified portfolio. Identified concentrations of credit risks are controlled and managed accordingly. Selective hedging is used within the Bank to manage risk concentrations at both the relationship and industry levels.

The most critical type of risks to which the Bank is exposed to are financial risks which include:

a) Credit risk
b) Liquidity risk
c) Market risks

10.6 Credit Risk

Credit risk is the risk of financial loss to the Bank if a customer or counterparty to a financial instrument fails to meet its contractual obligations. Credit risk arises principally from the Bank's loans and advances to customers and other Banks and investment securities but can also arise from credit enhancement provided such as financial guarantees, letters of credit and acceptances. The Bank is also exposed to other credit risks arising from its trading activities including derivatives.

The Bank enters into derivative transactions in forwards and spot contingents in the foreign exchange deals carried out the interbank markets. The derivatives are recorded at fair value. Derivatives held for risk management purposes include hedges that are economic hedges, but do not meet the hedge accounting requirements. Most of the trading portfolio is within the Bank's investment banking division (treasury) and is treated as trading risk for risk management purposes.

Credit risk is the single largest risk for the Bank's business and management carefully manages its exposure to credit risk. For risk management reporting purposes, the Bank considers and consolidates all elements of credit risk exposure.

For risk management purposes, credit risk arising on trading securities is managed independently, but reported as a component of market risk exposure.

10.6.1 Management of credit risk

The Board of Directors has delegated responsibility for the oversight of credit risk to its Credit and Finance Committee comprising of four non-executive directors. The implementation of the credit risk policies and monitoring of the credit portfolio to ensure that risks are managed within acceptable standards is the responsibility of the credit committee comprising of executive management.

The committee assisted by the credit department is responsible for the management of the Bank's credit risk including:

- Formulating credit policies in consultation with business units, covering collateral requirements, credit assessment, risk grading and reporting, documentary and legal procedures, and compliance with regulatory and statutory requirements.
- Establishing the authorisation structure for the approval and renewal of credit facilities. Authorisation limits are delegated to the head of credit and the credit committee while larger facilities require approval by the Board of Directors.
- Limiting concentrations of exposure to counterparties, geographies and industries for loans and advances.
- Developing and maintaining the Bank's risk grading in order to categorise exposures according to the degree of risk of financial loss faced and to focus management on the attendant risks. The risk grading system is used in determining where impairment provisions may be required against specific credit exposures. The current risk grading framework consists of eight grades reflecting varying degrees of risk of default and the availability of collateral or other credit risk mitigation. Risk grades are subject to regular reviews by credit department.
- Reviewing compliance of business units with agreed exposure limits, including those for selected industries, country risk and product types. Regular reports are provided to Bank credit committee on the credit quality of local portfolios and appropriate corrective action is taken.
- Providing advice, guidance and specialist skills to branches to promote best practice throughout the Bank in the management of credit risk.

10. Risk Management objectives and policies continued

10.6.2 Credit risk measurement

In measuring credit risk of loans and advances to customers, the Bank takes into account the following factors:

- The probability of default: this is the possibility of the customer failure to pay over the stipulated period in the contract.
- Exposure at default: current exposure on the borrower and the likely future development from which the Bank derives the exposure at default
- Estimated recovery ratio should default occur; this is the amount that can be recovered through sale of collateral

The Bank assesses the probability of default of individual borrowers using internal rating methods tailored to the various categories of the borrower. In assessing the credit quality of the customer the Bank takes into account the customers financial position, past experience and other industry specific factors. The credit risk measurements are embedded in the Bank's daily operational management and closely aligned to the Central Bank of Kenya loan classifications.

Risk limit control and mitigation policies

The Bank structures the level of credit risk it undertakes by placing limits on amounts of risk accepted in relation to one borrower or a group of borrowers. Such risks are monitored on a revolving basis and are subject to annual or more frequent review.

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 limits where appropriate.

The Bank takes security for funds advances and implements guidelines on the acceptability of specific classes of collateral. To minimise credit loss the Bank will seek additional collateral from the counterparty as soon as impairment indicators are identified for the relevant individual loans and advances. Collateral held for other financial assets other than loans and advances depends on the nature of the instrument.

The primary purpose of acceptances, letters of credit and guarantees is to ensure funds are available to a customer as required. Guarantees and standby letters of credit carry the same risk as loans. Documentary and commercial letters of credit which are written undertakings by the Bank on behalf of a customer authorising a third party to draw drafts on the Bank up to a stipulated amount under specific terms and conditions are collateralised by the underlying goods to which they relate and therefore carry less risk than a direct loan.

Commitments to extend credit represent unused portions of authorisation 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.

Credit risk arising from derivative financial instruments is, at any time, limited to those with positive fair values.

10. RISK MANAGEMENT OBJECTIVES AND POLICIES (Continued)

10.6.3 Impairment assessment

The Bank considers a financial instrument defaulted and therefore Stage 3 (credit-impaired) for ECL calculations in all cases when the borrower becomes 90 days past due on its contractual payments. The Bank considers treasury and interbank balances defaulted and takes immediate action when the required intraday payments are not settled by the close of business as outlined in the individual agreements.

As a part of a qualitative assessment of whether a customer is in default, the Bank also considers a variety of instances that may indicate unlikeliness to pay. When such events occur, the Bank carefully considers whether the event should result in treating the customer as defaulted and therefore assessed as Stage 3 for ECL calculations or whether Stage 2 is appropriate. Such events include:

- A material decrease in the borrower's turnover, the loss of a major customer or cessation of significant part of operation
- A material decrease in the underlying collateral value where the recovery of the loan is expected from the sale of the collateral
- The debtor (or any legal entity within the debtor's group) filing for bankruptcy application/protection
- The borrower is deceased

It is the Bank's policy to considerer a financial instrument as 'cured' and therefore re-classified out of Stage 3 when none of the default criteria have been present for at least six consecutive months. The decision whether to classify an asset as Stage 2 or Stage 1 once cured depends on the updated credit grade, at the time of the cure, and whether this indicates there has been a significant increase in credit risk compared to initial recognition.

10.6.3.1 Loans and advances

For loans and advances to various segments including retail and SME the borrowers are assessed based on the historical, current and forward-looking information including the following

- Historical financial information together with forecasts and budgets prepared by the client. This financial information includes realised and expected results, solvency ratios, liquidity ratios and any other relevant ratios to measure the client's financial performance. Some of these indicators are captured in covenants with the clients and are, therefore, measured with greater attention.
- Any publicly available information on the clients from external parties. This includes external rating grades issued by rating agencies, independent analyst reports, publicly traded bond or CDS prices or press releases and articles. Any macro-economic or geopolitical information, e.g., GDP growth relevant for the specific industry and geographical segments where the client operates.
- Any other objectively supportable information on the quality and abilities of the client's management relevant for the company's performance.

10. RISK MANAGEMENT OBJECTIVES AND POLICIES (Continued)

10.6 Credit risk (Continued)

Maximum exposure to credit risk before collateral held

	2019 Kshs'000	%	2018 Kshs'000	%
Credit Exposures				
On – balance sheet items				
Cash and balances with the CBK	906,420	8	918,709	7
Government securities	2,082,370	17	2,190,093	16
Balances due from banking institutions	173,909	1	119,420	1
Loans and advances to customers	7,369,033	62	8,429,659	64
	10,531,732	**88**	**11,657,881**	**88**
Off-balance sheet items				
Acceptances and letters of credit	36,467	1	62,292	1
Guarantees	721,845	6	984,621	7
Undrawn formal stand-by facilities, credit lines and other commitments to lend	618,965	5	531,333	4
	1,377,277	12	1,578,246	12
At 31 December	**11,909,009**	**100**	**13,236,127**	**100**

The above represents the worst-case scenario of credit exposure for 31 December 2019 and 2018, without taking into account any collateral held or other credit enhancements attached. For on-balance sheet assets, the exposures, set out above are based on gross carrying amount as reported on the statement of financial position.

Loans and advances to customers comprise of 62% (2018 - 64%) of the total maximum exposure. The fair value of collateral held in respect of assets subject to credit risk as at 31 Decembers 2019 was Kshs. 24,512,923,720 (2018- Kshs 21,818,102,126).

While collateral is an important mitigant to credit risk, the Bank's policy is to establish that loans are within the capacity of the customer to repay, as the primary way out. The Bank holds collateral against loans and advances to customers in the form of mortgage interests over property, other registered securities over assets, and guarantees. Estimates of fair value are based on the value of collateral assessed at the time of borrowing, and generally are not updated except when a loan is individually assessed as impaired. Collateral generally is not held over loans and advances to Banks, except when securities are held as part of reverse repurchase and securities borrowing activity.

The Bank is confident that its policies and procedures provide sufficient safeguards against exposure on credit risk as shown on the table overleaf.

10. RISK MANAGEMENT OBJECTIVES AND POLICIES (Continued)

10.6 Credit risk (Continued)

The table below shows the ECL charges on financial instruments for the year 2019 recorded in the income statement:

Credit loss expense	Stage 1		Stage 2		Stage 3	Total
	collective	individual	collective	individual		
Cash and balances with Central Bank of Kenya	-	-	-	-	-	-
Financial investments at amortised cost	-	-	-	-	-	-
Balances due from banking institutions	-	-	-	-	-	-
Loans and advances to customers	3,818	-	-	2,730	409,460	416,008
Total Impairment loss	**3,818**	**-**	**-**	**2,730**	**409,460**	**416,008**

The table below shows the ECL charges on financial instruments for the year 2018 recorded in the income statement:

Credit loss expense	Stage 1		Stage 2		Stage 3	Total
	collective	individual	collective	individual		
Cash and balances with Central Bank of Kenya	-	-	-	-	-	-
Financial investments at amortised cost	-	-	-	-	-	-
Balances due from banking institutions	-	-	-	-	-	-
Loans and advances to customers	3,379	-	-	2,415	362,367	368,161
Total Impairment loss	**3,379**	**-**	**-**	**2,415**	**362,367**	**368,161**

Apart from the loans and receivables to customers all other credit exposures are neither past due nor impaired.

Loans and Advances to customers

Loans and receivables neither past due nor impaired

The Bank classifies loans and advances under this category for those exposures that are up to date and in line with contractual agreements. These exposures will normally be maintained within approved product programs and with no signs of impairment or distress. These exposures are categorised internally as grade 1, that is, normal accounts in line with CBK prudential guidelines and a provision of 1 % is made and appropriated from revenue reserves to statutory reserves.

Loans where the contractual interest or principal payments are past due but the Bank believes that impairment is not appropriate on the basis of the level of security/collateral available and/or the stage of collection of amounts owed to the Bank are classified as past due but not impaired. These exposures are graded internally as category 2 that is watch accounts in the Bank's internal credit risk grading system, in line with CBK guidelines

Loans with renegotiated terms

Loans with renegotiated terms are loans that have been restructured due to deterioration in the borrower's financial position and where the Bank has made concessions that it would not otherwise consider. Loans whose terms have been renegotiated are no longer treated as past due but are reclassified as performing loans. In subsequent years, the renegotiated terms apply in determining whether the asset is considered past due.

10. RISK MANAGEMENT OBJECTIVES AND POLICIES (Continued)

10.6 Credit risk (Continued)

Write-off policy

When a loan is uncollectible it is written off against the related provisions for loan impairment. Such loans are written off after all the necessary recovery procedures have been completed and the amount of loan has been determined.

The Bank holds collateral against loans and advances to customers in the form of mortgage interests over property, other registered securities over assets, and guarantees. Estimates of fair value are based on the value of collateral assessed at the time of borrowing, and generally are not updated except when a loan is individually assessed as impaired. Collateral generally is not held over loans and advances to Banks, except when securities are held as part of reverse repurchase and securities borrowing activity.

The Bank adopted the rebuttable presumption approach by bucketing performing loans as follows; 0-30 Days - Stage 1, 30-90 Days past due - stage 2, > 90 days past due - stage 3 loans. All financial assets are rated as normal on origination. PDs are modelled by segment based on a survival analysis by tracking points of defaults since origination to reporting date.

The table below shows the credit quality and the maximum exposure to credit risk based on the bank's internal credit rating system and year end stage classification. The amounts presented are gross of impairment allowances. Details of the banks internal grading system are disclosed in note 2.1. An analysis of the changes in the gross carrying amount and the corresponding ECL allowance in relation to loans and advances to customers as at 31 December 2018 was as follows

	Stage 1 Kshs '000	Stage 2 Kshs '000	Stage 3 Kshs '000	Total Kshs '000
Gross carrying amount as at 1 January 2018	6,350,665	808,388	1,720,171	8,879,224
New assets originated or purchased (excluding write off)	988,745	111,146	-	1,099,891
Assets derecognised or repaid	(538,836)	(11,967)	(441,451)	(992,254)
Transfer to stage 1	376,422	(321,759)	(54,663)	-
Transfer to stage 2	(442,323)	647,012	(204,689)	-
Transfer to stage 3	(368,923)	(332,443)	701,366	-
Changes to contractual cash flows due to modifications not resulting in derecognition	-	-	-	-
Amounts written off	(86)	(28)	(28,086)	(28,200)
Foreign exchange adjustment	-	-	-	-
As at 31 December 2018	**6,365,664**	**900,349**	**1,692,648**	**8,958,661**

10. RISK MANAGEMENT OBJECTIVES AND POLICIES CONTINUED

10.6 Credit Risk (continued)

An analysis of the changes in the gross carrying amount and the corresponding ECL allowance in relation to loans and advances to customers as at 31 December 2019 is as follows

	Stage 1 Kshs '000	Stage 2 Kshs '000	Stage 3 Kshs '000	Total Kshs '000
Gross carrying amount as at 1 January 2019	6,365,664	111,146	-	699,915
New assets originated or purchased (excluding write off)	588,769	(294,585)	(282,185)	(1,570,002)
Assets derecognised or repaid	(993,232)	(113,565)	(30,801)	-
Transfer to stage 1	144,366	615,880	(93,866)	-
Transfer to stage 2	(522,014)	(485,133)	871,532	-
Transfer to stage 3	(386,399)	-	-	-
Changes to contractual due to modifications not resulting in derecognition	-	(1)	(264,937)	(264,942)
Amounts written off	(4)	-	-	-
Foreign exchange adjustment	-			
As at 31 December 2019	**5,197,150**	**734,091**	**1,892,391**	**7,823,632**

ECL for loans and advances

	Stage 1 Kshs '000	Stage 2 Kshs '000	Stage 3 Kshs '000	Off-Balance sheet Kshs'000	Total Kshs '000
ECL allowance as at 1 January 2018 as per IFRS 9	100,004	18,810	-	8,017	560,732
New assets originated or purchased	21,124	1,023	(282,185)	13,135	35,282
Assets derecognised or repaid (excluding write off)	(35,210)	-	(18,388)	-	(53,598)
Transfer to stage 1	17,605	(15,781)	(1,824)	-	-
Transfer to stage 2	(9,522)	12,311	(2,789)	-	-
Transfer to stage 3	-	-	-	-	-
impact of year end ECL of exposures transferred between stages during the year	8,083	(3,470)	(4,613)	-	-
Unwind of discount	-	-	-	-	-
Changes to contractual cash flows due to modifications not resulting to derecognition	-	-	-	-	-
Recoveries	-	-	-	-	-
Amounts written off	-	-	(13,414)	-	(13,414)
Foreign exchange adjustment	-	-	-	-	-
As at 31 December 2018	**102,084**	**12,893**	**392,873**	**21,152**	**529,002**

10. RISK MANAGEMENT OBJECTIVES AND POLICIES (continued)

10.6 Credit Risk (continued)

ECL for loans and advances

	Stage 1 Kshs '000	Stage 2 Kshs '000	Stage 3 Kshs '000	Off-Balance sheet Kshs'000	Total Kshs '000
ECL allowance as at 1 January 2019 as per IFRS 9	102,084	12,893	392,873	21,152	529,002
Reclassification	(8,563)	3,273	4,615	675	-
New assets originated or purchased	5,916	17,535	-	3,107	26,558
Assets derecognised or repaid (excluding write off)	(42,046)	(11,444)	-	(11,487)	(64,977)
Transfer to stage 1	1,509	(1,509)	-	-	-
Transfer to stage 2	(2,956)	5,912	(2,956)	-	-
Transfer to stage 3	(57,622)	(70,000)	127,622	-	-
impact of year end ECL of exposures transferred between stages during the year	65,705	74,546	12,009	-	152,260
Unwind of discount	-	-	-	-	-
Changes to contractual cash flows due to modifications not resulting to derecognition	-	-	-	-	-
Recoveries	-	-	-	-	-
Amounts written off	-	-	(188,246)	-	(188,246)
Foreign exchange adjustment	-	-	-	-	-
As at 31 December 2019	**64,027**	**31,206**	**345,917**	**13,447**	**454,597**

10, RISK MANAGEMENT OBJECTIVES AND POLICIES (Continued)

10.6 Credit risk (Continued)

10.6.3.2 Financial investments at amortized cost

The table below summarizes the credit quality, the maximum exposures to credit risk based on the bank's internal credit risk rating system and year end stage classification. The amounts presented are gross of impairment allowance. Details of the bank internal grading system and policies on whether ECL allowances are calculated on an individual or collective basis are explained in note 2.1.

An analysis of the changes in the gross carrying amount and the corresponding ECL as at 31 December 2018 was as follows

	Stage 1 Kshs '000	Stage 2 Kshs '000	Stage 3 Kshs '000	Total Kshs '000
Gross carrying amount as at 1 January 2018	2,605,899	-	-	2,605,899
New assets purchased	-	-	-	
Assets derecognised or matured	(415,806)	-	-	(415,806)
Stage 1	-	-	-	-
Stage 2	-	-	-	-
Stage 3	-	-	-	-
Changes due to modifications not derecognised	-	-	-	-
Amounts written off	-	-	-	-
Foreign exchange adjustment	-	-	-	-
At 31 December 2018	**2,190,093**	**-**	**-**	**2,190,093**

An analysis of the changes in the gross carrying amount and the corresponding ECL as at 31 December 2019 is as follows

	Stage 1 Kshs '000	Stage 2 Kshs '000	Stage 3 Kshs '000	Total Kshs '000
Gross carrying amount as at 1 January 2018	2,190,093	-	-	2,190,093
New assets purchased	-	-	-	
Assets derecognised or matured	(107,723)	-	-	(107,723)
Stage 1	-	-	-	-
Stage 2	-	-	-	-
Stage 3	-	-	-	-
Changes due to modifications not derecognised	-	-	-	-
Amounts written off	-	-	-	-
Foreign exchange adjustment	-	-	-	-
At 31 December 2019	**2,082,370**	**-**	**-**	**2,082,370**

10, RISK MANAGEMENT OBJECTIVES AND POLICIES (Continued)

10.6 Credit risk (Continued)

10.6.3.2 Financial investments at amortized cost

NB. The ECL relating to government securities rounds to zero
ECL Financial investment at amortized cost as at 31 December 2018 and as 31 December 2019 rounds off to zero hence no tabular presentation.

10.6.3.3 Dues from other banking institutions

The table below shows the credit quality and the maximum exposure to credit risk based on the bank's internal credit rating system and year end classification. The amounts are gross of impairment allowances. Details of the bank's internal credit grading system are explained in note 22.
An analysis of the changes in the gross carrying amount and the corresponding ECL allowances is as follows

	Stage 1 Kshs '000	Stage 2 Kshs '000	Stage 3 Kshs '000	Total Kshs '000
Gross Carrying amount 1 January 2018	107,453	-	-	107,453
New assets originated	17,931	-	-	17,931
Assets derecognised or repaid (Excluding write offs)	(5,904)	-	-	(5,904)
Transfer stage 1		-	-	-
Transfer stage 2	-	-	-	-
Transfer stage 3	-	-	-	-
Changes to contractual cashflows due to modification not resulting to derecognition	-	-	-	-
Amount written off	-	-	-	-
Foreign currency adjustment	-	-	-	-
As at 31 December 2018	**119,480**	**-**	**-**	**119,480**

RISK MANAGEMENT OBJECTIVES AND POLICIES (Continued)

10.6 Credit risk (Continued)

10.6.3.3 Dues from other banking institutions (continued)

	Stage 1 Kshs '000	Stage 2 Kshs '000	Stage 3 Kshs '000	Total Kshs '000
Gross Carrying amount 1 January 2019	119,480	-	-	119,480
New assets originated	64,195	-	-	64,195
Assets derecognised or repaid (Excluding write offs)	(4,556)	-	-	(4,556)
Transfer stage 1		-	-	-
Transfer stage 2	-	-	-	-
Transfer stage 3	-	-	-	-
Changes to contractual cashflows due to modification not resulting to derecognition	-	-	-	-
Amount written off	-	-	-	-
Foreign currency adjustment	-	-	-	-
As at 31 December 2019	**179,119**	**-**	**-**	**179,119**

Corresponding ECL for dues from banking institutions

	Stage 1 Kshs '000	Stage 2 Kshs '000	Stage 3 Kshs '000	Total Kshs '000
ECL allowance as at 1 January 2018	54	-	-	54
Assets derecognised or repaid (Excluding write offs)	(48)	-	-	(48)
Transfer stage 1	-	-	-	-
Transfer stage 2	-	-	-	-
Transfer stage 3	-	-	-	-
Impact on year end ECL of exposures transferred between stages during the year	-	-	-	-
Changes to contractual cash flows due to modification not resulting to derecognition	-	-	-	-
Recoveries	-	-	-	-
Amount written off	-	-	-	-
Foreign currency adjustment	-			-
As at 31 December 2018	**6**	**-**	**-**	**6**

	Stage 1 Kshs '000	Stage 2 Kshs '000	Stage 3 Kshs '000	Total Kshs '000
ECL allowance as at 1 January 2019	6	-	-	6
New assets originated	21	-	-	21
Assets derecognised or repaid (Excluding write offs)	-	-	-	-
Transfer stage 1	-	-	-	-
Transfer stage 2	-	-	-	-
Transfer stage 3	-	-	-	-
Impact on year end ECL of exposures transferred between stages during the year	-	-	-	-
Changes to contractual cash flows due to modification not resulting to derecognition	-	-	-	-
Recoveries	-	-	-	-
Amount written off	-			-
Foreign currency adjustment	-	-	-	-
As at 31 December 2019	**27**	**-**	**-**	**27**

10, RISK MANAGEMENT OBJECTIVES AND POLICIES (Continued)

10.6 Credit risk (Continued)

10.6.3.4 Letters of credit and guarantees

Letters of credit and guarantees (including standby letters of credit commit the bank to make payments in the event of a specific act generally to the import or export of goods. Guarantees and standby letters of credit carry a similar credit risk to loans. The nominal values of such commitments are listed below;

	2019 Kshs '000	2018 Kshs '000
Financial guarantees	721,845	984,621
Letters of credit	36,467	62,292
Other undrawn commitments	433,107	65,824
Total	**1,191,419**	**1,112,737**

The table below shows the credit quality and the maximum exposures to credit risk based on the bank's internal credit risk internal credit rating system and year end classification. Details of the bank internal grading system and policies on whether ECL are calculated in an individual or collective basis are explained in note 7.6.

Performing	Stage 1 Kshs '000	Stage 2 Kshs '000	Stage 3 Kshs '000	Total Kshs '000
Standard Grade	172,782	-	-	172,782
Past due but not impaired (Significant increase in credit risk)	-	592,472	-	592,472
Non-performing	-	-	-	-
Individually impaired	-	-	347,483	347,483
Total	**172,782**	**592,472**	**347,483**	**1,112,737**

An analysis of the outstanding exposures and the corresponding ECLs are as follows

	Stage 1 Kshs '000	Stage 2 Kshs '000	Stage 3 Kshs '000	Total Kshs '000
Outstanding exposure as at 1 January 2019	172,782	592,472	347,483	1,112,737
Reclassification	938,049	(592,468)	(345,581)	-
New exposures	657,375	632,397	-	1,289,772
Exposures derecognised or matured/ lapsed (excluding write off)	(616,717)	(592,471)	(1,902)	(1,211,090)
Transfers to stage 1	-	-	-	-
Transfers to stage 2	-	-	-	-
Transfers to stage 3	-	-	-	-
Changes due to modifications not resulting in derecognition	-	-	-	-
Amounts written off	-	-	-	-
Foreign exchange adjustments	-	-	-	-
As at 31 December 2019	**1,151,489**	**39,930**	**-**	**1,191,419**

10, RISK MANAGEMENT OBJECTIVES AND POLICIES (Continued)

10.6 Credit risk (Continued)

10.6.3.4 Letters of credit and guarantees (continued)

The corresponding ECL

	Stage 1 Kshs '000	Stage 2 Kshs '000	Stage 3 Kshs '000	Total Kshs '000
ECL as at 1 January 2018	-	4,070	3,947	8,017
New exposures	1	3,069	10,065	13,135
Exposures derecognised or matured (excluding write offs)	-	-	-	-
Transfers to stage 1	-	-	-	-
Transfers to stage 2	-	-	-	-
Transfers to stage 3	-	-	-	-
Amounts written off	-	-	-	-
Foreign exchange adjustments	-	-	-	-
As at 31 December 2018	**1**	**7,139**	**14,012**	**21,152**
	Stage 1 Kshs '000	Stage 2 Kshs '000	Stage 3 Kshs '000	Total Kshs '000
ECL as at 1 January 2019	1	7,139	14,012	21,152
New exposures	13,203	244	-	13,447
Exposures derecognised or matured (excluding write offs)	(1)	(7,139)	(14,012)	(21,152)
Transfers to stage 1	-	-	-	-
Transfers to stage 2	-	-	-	-
Transfers to stage 3	-	-	-	-
Amounts written off	-	-	-	-
Foreign exchange adjustments	-	-	-	-
As at 31 December 2019	**13,203**	**244**	**-**	**13,447**

An estimate of the fair value of collateral and other security enhancements held against financial assets is shown below:

	Loans and advances to customers	
	2019 Kshs'000	2018 Kshs'000
Against individually impaired financial assets	2,597,304	3,778,736
Against collectively impaired financial assets	3,430,981	2,196,826
Total	**6,028,285**	**5,975,562**

Settlement risk

The Bank's activities may give rise to risk at the time of settlement of transactions and trades. Settlement risk is the risk of loss due to the failure of a company to honour its obligations to deliver cash, securities or other assets as contractually agreed.

Settlement limits form part of the credit approval/limit monitoring process described earlier. Acceptance of settlement risk on free settlement trade requires transaction specific or counterparty specific approvals from the Bank's Credit Committee.

10. RISK MANAGEMENT OBJECTIVES AND POLICIES (Continued)

10.7 Concentration of risk

Details of significant concentrations of the Bank's assets, liabilities and off-balance sheet items by industry groups are as detailed below:

	2019 Kshs'000	%	2018 Kshs'000	%
(i) Advances to customers- gross				
Manufacturing	70,341	1	179,173	2
Wholesale and retail	4,058,174	52	4,120,984	46
Transport and communication	615,973	8	806,279	9
Agricultural	46,147	1	89,587	1
Business services	128,133	2	268,760	3
Real estate	1,700,226	22	2,239,665	25
Other	1,204,638	15	1,254,213	14
	7,823,632	**100**	**8,958,661**	**100**
(ii) Customer deposits				
Central and local Government	611,486	7	508,903	6
Non-financial public enterprises	37,158	-	17,568	-
Co-operative societies	152,971	2	578,191	7
Insurance companies	62,374	1	7,073	-
Private enterprises and individuals	7,919,816	90	7,476,523	87
Non-profit institutions	9,531	-	286	-
	8,793,336	**100**	**8,588,544**	**100**
(iii) Off balance sheet items (Letters of credit and guarantees)				
Manufacturing	10,150	1	3,378	0.33
Wholesale and retail	496,081	65	755,605	66
Transport and communication	38,018	5	4,580	0.4
Business services	211,856	28	374,024	32.7
Other	2,207	-	6,869	0.6
	758,312	**100**	**1,144,456**	**100**

10.8 Liquidity risk

Liquidity risk is the risk that the Bank will encounter difficulty in meeting obligations from its financial liabilities when they fall due as a result of customer deposits being withdrawn, cash requirements from contractual commitments or other cash outflows.

Management of liquidity risk

The Bank's liquidity risk management is carried out within the Bank and monitored by the Asset Liability committee (ALCO).

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, under both normal and stressed conditions, without incurring unacceptable losses or risking damage to the Bank's reputation.

10. RISK MANAGEMENT OBJECTIVES AND POLICIES (Continued)

10.8 Liquidity risk (continued)

10.8.1 Management of liquidity risk (continued)

Liquidity risk is addressed through the following measures:

- The treasury department monitors liquidity ratios on a daily basis against internal and regulatory requirements
- Day to day funding is managed by monitoring future cash flows to ensure that requirements can be met. These include replenishment of funds as they mature or are borrowed by customers.
- The Bank invests in short term liquid instruments which can easily be sold in the market when the need arises.
- The Bank enters into lending contracts subject to availability of funds.
- The Bank has an aggressive strategy aimed at increasing the customer deposit base.
- The Bank borrows from the market through interbank transactions with other Banks and the Central Bank of Kenya for short term liquidity requirements.
- Investments in property and equipment are properly budgeted for and done when the Bank has sufficient cash flows.

The daily liquidity position is monitored and regular liquidity stress testing is conducted under a variety of scenarios covering both normal and more severe market conditions. All liquidity policies and procedures are subject to review and approval by the board. Daily reports covering the liquidity position of the Bank are regularly submitted to Asset and Liability Committee.

10.8.2 Exposure to liquidity risk

The key measure used by the Bank for managing liquidity risk is the ratio of net liquid assets to deposits from customers. For this purpose net liquid assets are considered as including cash and cash equivalents and investment grade debt securities for which there is an active and liquid market less any deposits from Banks, debt securities issued, other borrowings and commitments maturing within the next month. The Central Bank of Kenya minimum liquidity ratio is 20%. Details of the reported Bank ratio of net liquid assets to deposits and customers at the reporting date and during the reporting period were as follows:

	2019	2018
At 31 December	27%	22%
Average for the period	24%	23%
Maximum for the period	27%	28%
Minimum for the period	18%	20%

10. RISK MANAGEMENT OBJECTIVES AND POLICIES (Continued)

10.8 Liquidity risk (continued)

10.8.2 Liquidity risk based on discounted cash flows

The table below analyses the cash flows payable by the Bank under non-derivative financial liabilities by remaining contractual maturities and non-derivative financial assets by expected maturity dates as at the date of the statement of financial position.

AT 31 DECEMBER 2019	Up to 1 month Kshs'000	1 – 3 months Kshs'000	4 - 12 months Kshs'000	1 - 5 Years Kshs'000	Total Kshs'000
FINANCIAL ASSETS					
Cash and balances with the CBK	608,742	268,758	28,919	-	906,419
Balances due from banking institutions	179,119	-	-	-	179,119
Equity instruments at fair value through other comprehensive income	-	-	-	7,378	7,378
Government securities	-	128,100	430,804	1,685,670	2,244,574
Loans and advances to customers	2,223,752	228,767	481,281	5,297,410	8,231,210
Total financial assets	**3,011,613**	**625,625**	**941,004**	**6,990,458**	**11,568,700**
FINANCIAL LIABILITIES					
Balance due to Central Bank of Kenya	720,000	-	-	-	720,000
Deposits and balances due to banking institutions	23,814	-	-	-	23,814
Customer deposits	4,504,963	4,133,293	450,487	-	9,088,743
Borrowed funds- Lease liabilities	4,944	14,833	44,498	103,561	167,836
Total financial liabilities	5,253,721	4,148,126	494,985	103,561	10,000,393
Net liquidity gap	**(2,242,108)**	**(3,522,501)**	**446,019**	**6,886,897**	**1,568,307**

The above table shows the undiscounted cash flows on the Bank's financial liabilities and unrecognised loan commitments on the basis of their earliest possible contractual maturity. The Bank's expected cash flows on these instruments vary significantly from this analysis. For example, demand deposits from customers are expected to maintain a stable or increasing balance; and unrecognised loan commitments are not all expected to be drawn down immediately. The table below shows maturity analysis for the loans and commitments (off-balance sheet commitments).

AT 31 DECEMBER 2019	Up to 1 month Kshs'000	1 – 3 months Kshs'000	4 - 12 months Kshs'000	1 - 5 Years Kshs'000	Total Kshs'000
Guarantees	90,127	215,803	399,238	16,677	721,845
Acceptances and letters of credit	36,467	-	-	-	36,467
Undrawn formal stand-by facilities, credit lines and other commitments to lend	232,166	-	-	-	232,166
Total	**358,760**	**215,803**	**399,238**	**16,677**	**990,478**

AT 31 DECEMBER 2018	Up to 1 month Kshs'000	1 – 3 months Kshs'000	4 - 12 months Kshs'000	1 - 5 Years Kshs'000	Total Kshs'000
Guarantees	128,048	280,190	516,664	59,719	984,621
Acceptances and letters of credit	15,299	36,252	10,741	-	62,292
Undrawn formal stand-by facilities, credit lines and other commitments to lend	597,157	-	-	-	597,157
Total	**740,504**	**316,442**	**527,405**	**59,719**	**1,644,070**

10 RISK MANAGEMENT OBJECTIVES AND POLICIES (CONTINUED)

10.9 Market risks

Market risk is the risk that fair value or future cash flows of a financial instrument will fluctuate because of changes in market prices. Market risk arise from open positions in interest rates, currency and equity products, all of which are exposed to general and specific market movements and changes in the level of volatility of market rates or prices such as interest rates, equity prices, foreign exchange rates and credit spreads. The objective of market risk management is to manage and control market risk exposures within acceptable parameters, while optimising the return on risk.

The Bank separates exposures to market risk into either trading or non-trading portfolios. Trading portfolios include those positions arising from market-making transactions where the Bank acts as principal with clients or with the market. Non-trading portfolios mainly arise from the interest rate management of the entity's retail and commercial Banking assets and liabilities.

10.9.1 Management of market risks

Overall responsibility of managing market risk rests with the Asset and Liability Committee (ALCO). The Treasury department is responsible for the development of detailed risk management policies (subject to review and approval by ALCO) and for the day-to-day review of their implementation. The Board of Directors sets limits on the level of mismatch of interest rate repricing that may be undertaken which is monitored daily.

10.9.2 Exposure to interest rate risk

The principal risk to which non-trading portfolios are exposed is the risk of loss from fluctuations in the future cash flows or fair values of interest bearing financial instruments because of a change in market interest rates. The ALCO is the monitoring body for compliance with these limits and is assisted by Treasury Department in its day-to-day monitoring activities. Other assets are settled no more than 12 months after the reporting date. All the balances are interest bearing.

The table below summarises the Bank's exposures to interest rate risks. Included in the table are the Bank's assets and liabilities at carrying amounts, categorised by the earlier of the contractual repricing or maturity dates. The Bank does not bear an interest rate risk on off balance sheet items.

AS AT 31 December 2019	Up to 1 month Kshs'000	1 – 3 months Kshs'000	4 - 12 months Kshs'000	1 - 5 Years Kshs'000	Non-interest bearing Kshs'000	Total Kshs'000
FINANCIAL ASSETS						
Cash and balances with the CBK	-	-	-	-	906,420	906,420
Balances due from other banking institutions	179,032	-	-	-	-	179,032
Government securities	-	128,100	397,788	1,556,482	-	2,082,370
Loans and advances to customers	7,369,033	-	-	-	-	7,369,033
Total financial assets	**7,548,065**	**128,100**	**397,788**	**1,556,482**	**906,420**	**10,536,855**
	Up to 1 month Kshs'000	1 – 3 months Kshs'000	4 - 12 months Kshs'000	1 - 5 Years Kshs'000	Non-interest bearing Kshs'000	Total Kshs'000
FINANCIAL LIABILITIES						
Balance due to Central Bank of Kenya	720,000	-	-	-	-	720,000
Deposits and balances due to banking institutions	23,814	-	-	-	-	23,814
Customer deposits	1,380,482	3,934,347	423,350	-	3,037,011	8,775,190
Borrowed funds	-	-	-	-	-	-
Total financial liabilities	**2,124,296**	**3,934,347**	**423,350**	**-**	**3,037,011**	**9,519,004**
Interest rate sensitivity gap	**5,423,769**	**(3,806,247)**	**(25,562)**	**1,556,482**	**(2,130,591)**	**1,017,851**

10. RISK MANAGEMENT OBJECTIVES AND POLICIES (CONTINUED)

10.9 Market risks (continued)

Management of market risks

Interest rate / equity price volatility

Volatility measures the expected future variability of a market price. It is generally quoted as a percentage; a higher number represents a more volatile instrument, for which larger swings in price (or interest rate) are expected. Volatility is a key input in option-based models and is used to estimate the future prices for the underlying instrument (e.g., equity or interest rate). Volatility varies per instrument and in time and therefore, it is not viable to make reliable and meaningful general statements about volatility levels.

Certain volatilities, generally those relating to longer-term maturities are unobservable and are estimated by the Bank.

Sensitivity analysis on interest rates

An increase of 1 percentage point in interest rates for the period would have increased/ (decreased) profit or loss by the amounts shown below. This analysis assumes that all other variables, in particular foreign currency rates, remain constant. This analysis is performed on the same basis for 2018.

	Profit or loss		Equity	
	2019	2018	2019	2018
	KShs'000	KShs'000	KShs'000	KShs'000
Interest income	83,991			58,794
		83,991	58,794	
Interest expense	(73,784)	(73,784)	(51,649)	(51,649)
Net change in interest	10,207	10,207	7,145	7,145

A decrease of 1 percentage point in interest rates for the period would have had an equal but opposite effect on the profit or loss and equity, on the basis that all other variables remain constant.

Recovery rates
Recovery rates reflect the estimated loss that the Bank will suffer given expected defaults. The recovery rate is given as a percentage and reflects the opposite of loss severity (i.e., 100% recovery reflects 0% loss severity).

In line with general market convention, loss severity is applied to asset-backed securities while recovery rate is more often used as pricing input for corporate or government instruments. Higher loss severity levels / lower recovery rates indicate lower expected cash flows upon the default of the instruments. Recovery rates for complex, less liquid instruments are usually unobservable and are estimated based on historical data. Currently, the Bank has no such investments.

Currency risk

The bank takes on exposure to the effects of fluctuations in the prevailing foreign currency exchange rates on its financial position and cashflows. The board sets limits on the level of exposure by currency and in total for both overnight and intra-day positions which are monitored daily.

10. RISK MANAGEMENT OBJECTIVES AND POLICIES (Continued)

10.9 Market risks (continued)

The table below summarises the Bank's exposure to foreign currency exchange rate risk at 31 December. Included in the table are the Bank's financial instruments categorised by currency.

AS AT 31 DECEMBER 2019	KSHS Kshs'000	USD Kshs'000	GBP Kshs'000	EURO Kshs'000	OTHERS Kshs'000	TOTAL Kshs'000
FINANCIAL ASSETS						
Cash and balances with Central Bank of Kenya	881,829	16,455	2,498	4,949	689	906,420
Balances due from Banking institutions	-	159,130	2,638	16,962	302	179,032
Government securities	2,082,370	-	-	-	-	2,082,370
Loans and advances to customers	7,284,899	84,134	-	-	-	7,369,033
Total financial assets	**10,249,098**	**259,719**	**5,136**	**21,911**	**991**	**10,536,855**
FINANCIAL LIABILITIES						
Balance due to Central Bank of Kenya	720,000	-	-	-	-	720,000
Deposits and balances due to banking institutions	23,814	-	-	-	-	23,814
Customer deposits	8,706,919	54,828	7,969	5,474	-	8,775,190
Borrowed funds	-	-	-	-	-	-
Total financial liabilities	9,450,733	54,828	7,969	5,474	-	9,519,004
NET ON BALANCE SHEET POSITION	**798,365**	**204,891**	**(2,833)**	**16,437**	**991**	**1,017,851**
NET OFF BALANCE SHEET POSITION	**712,391**	**39,033**	**6,031**	**-**	**857**	**758,312**
AT 31 DECEMBER 2018						
Total financial assets	11,384,675	240,071	10,057	20,688	2,389	11,657,881
Total financial liabilities	11,419,527	106,882	7,678	142,117	-	11,676,204
NET ON BALANCE SHEET POSITION	(34,852)	133,189	2,379	(121,429)	2,389	(18,323)
NET OFF BALANCE SHEET POSITION	947,536	137,679	-	13,303	46,138	1,144,656

10. RISK MANAGEMENT OBJECTIVES AND POLICIES (Continued)

10.9 Market risks (continued)

Market risks - sensitivity analysis

A principal part of the Bank's management of market risk is to monitor the sensitivity of projected net interest income under varying interest rate scenarios (simulation modelling) and the sensitivity of future earnings and capital to varying foreign exchange rates. Stress tests provide an indication of the potential size of losses that could arise in extreme conditions. Consolidated Bank aims, through its management of market risk, to mitigate the impact of prospective interest rate movements and foreign exchange fluctuations which could reduce future earnings and capital.

For simulation modelling, the Bank uses a combination of scenarios relevant to local businesses and local markets. These scenarios are used to illustrate the effect on the Bank's earnings and capital.

Interest rate risks – increase/decrease of 10% in net interest margin

The Interest rate risks sensitivity analysis is based on the following assumptions.

- Changes in the market interest rates affect the interest income or expenses of variable interest financial instruments.
- Changes in Market interest rates only affect interest income or expenses in relation to financial instruments with fixed interest rates if these are recognized at their fair value.
- The interest rate changes will have a significant effect on interest sensitive assets and liabilities and hence simulation modelling is applied to Net interest margins.
- The interest rates of all maturities move by the same amount and, therefore, do not reflect the potential impact on net interest income of some rates changing while others remain unchanged.
- The projections make other assumptions including that all positions run to maturity.

The analysis below sets out the impact on future net interest income of an incremental 10% parallel fall or rise in all yield curves as at 31 December 2018.

Assuming no management actions, a series of such appreciation would increase net interest income for 2019 by Kshs 53,460,000 (2018 - Kshs 64,301,000), while a series of such falls would decrease net interest income for 2018 by Kshs 53,460,000 (2018 - Kshs 64,301,000).

Also a series of such rises would increase the adjusted core capital to RWA and Adjusted total capital to RWA by 0.5% (2018: 0.7%) and 0.5% (2018: 0.7%) respectively, while a series of such falls would decrease the adjusted core capital to RWA and Adjusted total capital to RWA by 0.5% (2018: 0.4%) and 0.5% (2018: 0.4%) respectively.

Foreign exchange risks – appreciation/depreciation of Kshs against other currencies by 10%

The Foreign Exchange Risks sensitivity analysis is based on the following assumptions:

- Foreign exchange exposures represent net currency positions of all currencies other than Kenya shillings.
- The Currency Risk sensitivity analysis is based on the assumption that all currency positions are highly effective.
- The Base currency in which the Bank's business is transacted is Kenya shillings.

The table below sets out the impact on future earnings of an incremental 10% parallel fall or rise in all foreign currencies as at 31 December 2019.

10. RISK MANAGEMENT OBJECTIVES AND POLICIES (Continued)

10.9 Market risks (continued)

Market risks - sensitivity analysis (continued)

Assuming no management actions, a series of such rise and fall would impact the future earnings and capital as illustrated in the table below:

	Amount 31 December 2019 Kshs'000	Scenario 1 10% appreciation Kshs'000	Scenario 2 10% Depreciation Kshs'000
Loss before taxation	(518,001)	(515,830)	(520,172)
Adjusted Core Capital	1,153,160	1,155,331	1,150,989
Adjusted Total Capital	1,370,206	1,372,377	1,368,035
Risk Weighted Assets (RWA)	10,125,911	10,125,911	10,125,911
Adjusted Core Capital to RWA	11.4%	11.4%	11.4%
Adjusted total Capital to RWA	13.5%	13.5%	13.5%

Assuming no management actions, a series of such appreciation would increase earnings for 2019 by Kshs. 51,800,100 (2018 - Kshs 35,156,700), while a series of such falls would decrease earning for 2019 by Kshs. 51,800,100 (2018 – Kshs 35,156,700).

Also, a series of such rises would increase the adjusted core capital to RWA and Adjusted total capital to RWA by,0.0 % (2018 - 0.0%) and 0.0% (2018 - 0.1 %) respectively, while a series of such falls would decrease the adjusted core capital to RWA and Adjusted total capital to RWA by0.0% (2018 – 0.0%) and 0.0% (2018 -0.0%) respectively.

The impact of the increase or decrease is not expected to impact significantly.

10.10 OTHER RISKS

Non-financial risk management disclosures:

10.10.1 Strategic risk

Strategic risk is the current and prospective impact on earnings or capital arising from adverse business decisions, improper implementation of decisions, or lack of responsiveness to industry changes. This risk is a function of the compatibility of organization's strategic goals, the business strategies developed to achieve those goals, the resources deployed against these goals, and the quality of implementation.

The Bank faces several strategic risks from its environment which include:

- Macro-economic changes.
- Competition from the financial industry and organisations providing similar services.
- Technological changes.
- Key legislative and regulatory changes.
- Major political events.
- Human capital or social/demographic trends and changes.
- Inadequate capitalisation

The Board of Directors is ultimately responsible for the overall generation and implementation of the Bank's strategy for purposes of enhancing shareholders' value. It has however delegated the implementation aspects to the Chief Executive Officer and the Senior Management team. The Board of Directors, with support of the Chief Executive Officer Senior Management, develops and implements a new strategic cycle every 5 years to cater for the next growth phase of the Bank.

10 RISK MANAGEMENT OBJECTIVES AND POLICIES (Continued)

10.10 OTHER RISKS (continued)

Non-financial risk management disclosures:(continued)

10.10.1 Strategic risk (continued)

The Chief Executive Officer supported by the (Executive Committee) EXCOM is responsible for the execution of the approved strategic objectives on a day to day basis and actively monitors business performance against these objectives through periodic reviews. The business carries out business performance reviews periodically but at a minimum on a monthly basis against pre-determined milestones and key performance indicators. The reviews are reported to the Board of Directors for information and advice, or action where significant deviations occur. These reports include identifying the key risks faced by the Bank and how they are being managed.

Each business head is responsible for ensuring that strategic initiatives are aligned to the overall strategy of the Bank and supported by the relevant and appropriate operating policies and programs that direct behaviour. They are also responsible for monitoring, managing and reporting on the effectiveness and risks of their business' strategic objectives, and the progress they have made towards achieving these. They oversee the direction and trends of significant current and emerging risks related to their business units and that mitigating actions are taken where appropriate.

The Chief Executive Officer co-ordinates an annual strategic planning process intended to align individual business strategies to overall enterprise level strategies as approved by the Board of Directors. They include a comprehensive review and evaluation of the business strategies, competitive positioning, financial performance, initiatives of strategic executions, and key business risks.

The Bank's financial and non-financial performance, including its key risks, is reported to the Board of Directors on a bi monthly basis for review and action, where necessary.

10.10.2 Non-financial risk management disclosures:

10.10.3 Operational risk

Operational Risk is "the risk that the Bank will incur direct or indirect loss due to an event or action causing the failure of technology, processes, infrastructure, personnel, and other risks having an operational impact". The impact of these risks can result in significant financial loss, reputational harm or regulatory censure and penalties.

The major operational risks faced by the Bank include:

- People and related issues such as staff retention, frauds, amongst others.
- Systems and processes changes related to the drive to meet our clients' needs.

The Board of Directors takes the lead in establishing the "tone at the top" which promotes a strong risk management culture. The Bank has also put in place a corporate culture that is guided by strong risk management and that supports and provides appropriate standards and incentives for professional and responsible behaviour.

10 RISK MANAGEMENT OBJECTIVES AND POLICIES (Continued)

10.10.2 Non-financial risk management disclosures (continued)

10.10.3 Operational risk (continued)

All members of staff are responsible for the management and mitigation of Operational risks. This is reflected in the continuous control environment, risk awareness and management style. Specific roles or responsibilities are assigned for leading and managing the internal control environment through the following people:

- Board and CEO;
- Audit Committee;
- Internal Audit Department;
- Board Risk Management Committee;
- Risk Management Committee;
- Risk & Compliance Department;
- Business Operational Risk functions in corporate, Retail and SME ;
- Information Technology (IT) Steering Committee; and
- Business Heads and Operations Head.

Internal Audit is responsible for assessing compliance with operational risk policy and for reporting significant issues to the Board Audit Committee and the Board of Directors.

The Bank seeks to minimise actual or potential losses arising from Operational Risk failures. These include inadequately defined procedures or policies, systems failure, internal control flaws or breaches, insufficiently skilled staff, unmanageable events or customer actions. To achieve this, the Bank ensures:

- Robust operational risk policy and procedures that reflects industry practice are put in place and operationalized. These include toolkits to help identify, assess, control, manage and report on key Operational Risks. Toolkits in the Operational Risk Procedures manual include inter alia:

  i) Framework for the Bank, businesses, and support functions to identify their major operational risks and mitigation plans;
  ii) Key control standards;

  iii) Indicators to i dentify Operational Risk; and

  iv) Incident and issues tracking mechanisms to identify causal factors and operational losses:

- All staff in business and support functions, are aware of their responsibilities for Operational Risk Management.
- Potential Operational Risk impact of Bank activities and products are considered at their outset with a view to minimising these as far as possible.
- There are structured processes to report control failures to designated individuals and escalate material issues to Risk Management Committee, Executive Committee (EXCOM) and Board Risk Management Committee as appropriate.
- Employees are given Operational Risk training appropriate to their roles.
- Employee and Bank assets are adequately protected.
- Workable Business Continuity Plans are established (including Disaster Recovery and Crisis Management procedures) to minimise the impact of unplanned events on business operations and customer service.
- The financial impact of operational losses is mitigated through the utilisation of insurance or other risk transfer mechanisms where appropriate.

10 RISK MANAGEMENT OBJECTIVES AND POLICIES (Continued)

10.10.2 Non-financial risk management disclosures (continued0

10.10.3 Operational risk (continued)

10.10.4 Compliance (policy/legal/regulatory) risk:

Compliance risk is the current or prospective risk to earnings and capital arising from violations or non-compliance with laws, rules, regulations, agreements, prescribed practices, or ethical standards, as well as from the possibility of incorrect interpretation of effective laws or regulations.

The Bank is committed to ensuring that its business activities are conducted in accordance with applicable laws and regulations, internal rules, policies and procedures, and ethical standards ("compliance laws, rules and standards"). The Bank has established appropriate policies, procedures and controls that will ensure effective compliance with laws, regulations and codes relevant to its businesses, customers and staff.

Business unit heads have the responsibility and accountability of managing regulatory and legal risks relating to their units on a day to day basis with assistance / advice and oversight from Legal and Compliance Department. The Risk and Compliance Department identifies and monitors the key risks and is responsible for ensuring that the day to day business controls comply with applicable legislation and are in line with best practice. Internal and external legal counsel work closely with business units to identify areas of existing and potential regulatory/legal risks and actively manage them to reduce the Bank's exposures.

Senior Management and the Board Risk Management Committee receive the Risk Management Department's opinions / reports on the strength of the Banks Compliance Risk Framework to enable them to determine whether it is under control and where not, tracks significant corrective actions to finality. Additionally, significant exposures under "for or against" litigation are reviewed periodically.

10.10.5 Reputational risk

Reputational risk is the potential that negative stakeholder impressions or perceptions, whether true or not, regarding the Bank's business practices, actions or inactions, will or may cause a decline in customer base, liquidity, and overall brand value. It is a resultant effect of all other risks highlighted in this report and therefore cannot be managed in isolation. Therefore, when all the other risks are managed well, this risk is substantially minimised.

The Bank's reputation is an invaluable and fragile asset that is broad and far reaching and includes image, goodwill and brand equity. Reputational risk management supports value creation and seeks to deal effectively with potential future events that create uncertainty.

Ultimate responsibility for this risk rests with the Board of Directors and Senior Management who examine the Bank's reputational risk as part of their regular mandate. They are assisted in this aspect by the Corporate Communications Department. Their purpose is to ensure that all products, services, and activities meet the Bank's reputational risk objectives in line with the Board of Director's approved appetite. The Bank's reputational risk strategy however cascades into the other Bank's policies procedures each level of management is responsible for the appropriateness of policies, processes and controls within its purview.

Senior Management and the Board of Directors receive periodic reports on the assessment of the Bank's reputational risk exposures that arise from its business activities so as to form a view on associated risks and implement corrective actions.

10. RISK MANAGEMENT OBJECTIVES AND POLICIES (Continued)

10.11 FINANCIAL ASSETS AT FAIR VALUE THROUGH OTHER COMPREHENSIVE INCOME

The following table provides an analysis of financial instruments that are measured subsequent to initial recognition at fair value, grouped into levels 1 to 3 based on the degree to which the fair value is observable.

- Level 1: fair value through OCI 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 (i.e. as prices) or indirectly (i.e. 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).

Financial assets at FVTOCI:

		Level 1	Level 2	Level 3	Total
31 December 2019	Note	Kshs'000	Kshs'000	Kshs'000	Kshs'000
Quoted investments					
31 December 2018		6,727	-	-	6,727
Quoted investments		**7,378**	**-**	**-**	**7,378**

The above was valued at quoted bid prices in an active market (Nairobi Securities Exchange). Except as detailed above, the Directors consider that the carrying amounts of financial assets and financial liabilities recognised in the statement of financial position approximate their fair values. This note provides information about how the Bank determines fair values of various financial assets and financial liabilities. Fair value of the Bank's financial assets and financial liabilities are measured at fair value on a recurrent basis. The following table gives information about how the fair values of these financial assets and financial liabilities are determined (in, the valuation technique(s) and inputs used):

Financial assets	Fair value as at	Fair value hierarchy	Valuation technique(s) and key inputs	Significant unobservable inputs	Relationship of unobservable inputs to fair value
	31/12/19	31/12/18			
	Kshs '000	Kshs'000			
			Quoted bid prices in an active market		
Quoted investments	7,378	6,727	Level 1	N/A	N/A

There were no transfers between levels 1, 2 and 3 in the period (2018: none).

10.12 Price risk sensitivity

The Bank is exposed to price risk on quoted investment securities

The table below summarizes the impact on increase in the market price on the Group's equity investments net of tax. The analysis assumes that the market prices had increased by 5% with all other variables held constant and all the Bank's equity instruments moved according to the historical correlation with the price:

	Impact on profit or loss and equity	
	2019	2018
	KShs '000	KShs '000
Effect of increase on profit	**32**	**20.6**

11 CAPITAL MANAGEMENT (Group and Bank)

Regulatory capital

The Banks objectives when managing capital are:

- To safeguard the Banks' ability to continue as a going concern so that it can continue to provide returns for the shareholders and benefits for the other stakeholders.
- To maintain a strong capital base to support the current and future development needs of the business.
- To comply with the capital requirements set by the Central Bank of Kenya.

Capital adequacy and use of regulatory capital are monitored by management employing techniques based on the guidelines developed by the Central Bank of Kenya for supervisory purposes. The required information is filed with the Central Bank of Kenya on a monthly basis.

The Central Bank of Kenya requires each Bank to:

a) Hold the minimum level of regulatory capital of Kshs 1 billion.
b) Maintain a ratio of total regulatory capital; to risk weighted assets plus risk weighted off balance assets at above the required minimum of 10.5%;
c) Maintain a core capital of not less than 10.5% of total deposit liabilities; and
d) Maintain total capital of not less than 14.5% of risk weighted assets plus risk weighted off balance sheet items.

As further disclosed in note 9, the Bank had not complied with capital to risk weighted assets of not less than 14.5% in 2019. In 2018, the Bank failed to meet all the above Key Central bank requirements.
The Bank's regulatory capital is analysed into two tiers:

- Tier 1 capital, which includes ordinary share capital, non-cumulative irredeemable non-convertible preference shares, disclosed reserves such as share premiums, retained earnings, and 50% un-audited after tax profit less investment in subsidiaries conducting banking business, investments in equity of other institutions, intangible assets (excluding computer software) and goodwill.

- Tier 2 capital, which includes 25% revaluation surplus which have received prior CBK approval, subordinated debt, hybrid capital instruments or any other capital instruments approved by CBK.

11. CAPITAL MANAGEMENT (Continued)

The Bank's regulatory capital position at 31 December 2019 and 31 December 2018 was as follows:

	2019	2018
	Kshs'000	Kshs'000
Tier 1 capital		
Ordinary share capital	2,998,400	1,398,400
Non-cumulative irredeemable shares	721,130	721,130
Share capital	3,719,530	2,119,530
Accumulated deficit	(2,567,139)	(2,061,222)
Total	1,152,391	58,308
Tier 2 capital		
Revaluation reserves (25%)	90,472	58,308
General loan loss provision-statutory reserve (Maximum of 1.25% of RWA)	126,574	-
Total	**217,046**	**58,308**
Total regulatory capital	**1,369,437**	**116,616**
Risk-weighted assets	**10,125,914**	**11,107,327**
Capital ratios:		
Total regulatory capital expressed as a percentage of total risk-weighted assets (CBK minimum 14.5%)	13.5%	1.05%
Total tier 1 capital expressed as a percentage of risk-weighted assets (CBK minimum 10.5%)	11.4%	0.52%

12. INTEREST INCOME (Group and Bank)

	2019	2018
Interest on loans and advances	1,049,913	1,223,220
Interest on Bank placements	-	1,654
Interest on investments at amortised cost	166,491	176,592
	1,216,404	**1,401,466**

13. INTEREST EXPENSE (Group and Bank)

	2019	2018
Interest on customer deposits	395,024	430,192
Interest on inter-bank borrowings	-	2,849
Interest on Central Bank of Kenya Repos	88,173	105,866
Interest on borrowed funds	177,961	219,551
Interest on leases	13,797	-
	674,955	**758,458**

14. FEE AND COMMISSION INCOME

	2019 Bank Kshs'000	2019 Group Kshs'000	2018 Bank Kshs'000	2018 Group Kshs'000
Ledger related fees and commissions	39,387	39,387	41,234	41,234
Credit related fees and commissions	208,918	208,918	162,909	162,909
Transaction related fees	95,714	107,866	94,149	94,149
	344,019	**356,171**	**298,292**	**298,292**

15. FOREIGN EXCHANGE TRADING INCOME (Group and Bank)

Foreign exchange net income includes gains and losses from spot and forward contracts and translated foreign currency assets and liabilities.

	2019 Kshs'000	2018 Kshs'000
Gains on foreign exchange trading	23,889	25,278
Losses on foreign exchange trading	(2,174)	(3,842)
	21,715	**21,436**

16. OTHER OPERATING INCOME (Group and Bank)

Rental income	71,028	69,547
Remedial recoveries	10,823	11,122
Recoveries on loans and advances	225,469	361,213
Gain on disposal of property and equipment	187	40
Sundry income*	6,012	122
	313,519	**442,044**

* relate to income on sale of tenders.

17. OPERATING EXPENSES

	2019 Bank Kshs'000	2019 Group Kshs'000	2018 Bank Kshs'000	2018 Group Kshs'000
Staff costs (note 18),	687,687	696,976	740,346	740,346
Directors' emoluments - Fees	12,476	12,476	5,048	5,048
- Other	21,580	21,580	21,980	21,980
Depreciation - Current year (note 28)	95,091	95,870	50,348	50,348
Amortisation of intangible assets (note 29)	108,129	108,427	89,935	89,935
Amortisation of operating lease (note 30)	170	170	170	170
Contribution to Kenya Deposit Insurance Corporation				
Auditors' remuneration-Current year	13,266	13,266	13,612	13,612
Other operating expenses	10,536	10,797	5,577	5,577
	372,643	375,261	461,163	461,163
	1,321,578	**1,334,823**	**1,388,179**	**1,388,179**

18. STAFF COSTS

	2019 Bank	2019 Group	2018 Bank	2018 Group
Salaries and wages	571,180	578,947	621,496	621,496
Training, recruitment and staff welfare costs	21,188	21,469	23,752	23,752
Pension contributions	37,870	38,309	39,739	39,739
Medical expenses	46,229	46,880	43,929	43,929
Leave pay provision	(162)	(162)	356	356
Staff insurance	4,383	4,517	5,090	5,090
Gratuity provision	6,346	6,346	5,326	5,326
NSSF contributions	653	669	658	658
	687,687	**696,926**	**740,346**	**740,346**

19. INCOME TAX (Group and Bank)

a) Taxation charge/(credit)

	2019 KShs	2018 KShs
Current tax based on the taxable profit for the year at 30%	13,066	15,892
Deferred tax credit (note 28)	-	-
Prior year over provision- current taxation	225	(724)
Derecognition of prior year deferred tax	-	173,299
	13,291	**188,467**

	2019 KShs	2018 KShs
Reconciliation of expected tax based on accounting loss to tax charge		
	(518,001)	**(351,567)**
Tax calculated at a tax rate of 30%		
Tax effect of expenses not deductible for tax purposes*	(155,400)	(105,470)
Non-taxable income	7,358	22,063
Prior year (under)/over provision- current taxation	(1,800)	(11,699)
Current year's deferred tax not recognised	225	(724)
Prior year deferred tax derecognition	162,908	110,998
	13,291	**188,467**

** Tax effect of expenses not deductible for tax purposes relates to expenses incurred not for business or generation of revenue e.g. donations.*

The bank has not recognised deferred tax assets of Kshs 162 million (2018: Kshs 173 million) due to uncertainty of future earnings and profits against which the deferred tax assets can be offset.

19. INCOME TAX (CONTINUED)

c) Taxation recoverable/(payable)

	2019 Kshs'000	2018 Kshs'000
At 1 January	2,809	6,022
Charge for the year	(13,066)	(15,892)
Prior year (over)/under provision	(225)	724
Tax paid during the year	16,686	11,955
At 31 December	**6,204**	**2,809**

20. LOSS PER SHARE (Bank)

Loss per share is calculated by dividing the net loss attributable to shareholders by the number of ordinary shares in issue during the year.

	2019 Kshs'000	2018 Kshs'000
Loss for the year	(530,523)	(540,034)
Number of ordinary shares (number in thousands)	149,920	69,920
Loss per share		
Basic and diluted (Kshs)	(3.54)	(7.72)

There were no potentially dilutive shares outstanding as at 31 December 2019 and 31 December 2018, respectively. Diluted earnings per share are therefore the same as basic earnings per share.

21. CASH AND BALANCES WITH CENTRAL BANK OF KENYA (Group and Bank)

	2019 Kshs'000	2018 Kshs'000
Cash in hand	296,290	372,065
Balances with Central Bank of Kenya:		
- Cash ratio reserve	599,439	535,597
- Other balances (available for use by the Bank)	10,691	11,047
	906,420	**918,709**

Cash in hand and balances with Central Bank of Kenya are non-interest bearing. The cash ratio reserve is based on the value of customer deposits as adjusted by the Central Bank of Kenya requirements. As at 31 December 2019 the cash ratio reserve requirement was 5.25% (2018 – 5.25%) of all customer deposits held by the Bank. These funds are not available to finance the Bank's day to day operations.

22. DEPOSITS AND BALANCES DUE FROM BANKING INSTITUTIONS

	2019 Bank Kshs'000	2019 Group Kshs'000	2018 Bank Kshs'000	2018 Group Kshs'000
a) Balances due from banking institutions maturing within 90 days:				
Balances with correspondent banks	94,330	94,330	79,570	79,570
Balances with local banks	79,666	84,789	39,910	39,910
	173,996	179,119	119,480	119,480
As at 1 January 2019	60	60	-	-
Impact of adopting IFRS 9	-	-	54	54
Increase in allowance for impairment	27	27	6	6
Allowance for impairment as at 31 December	87	87	60	60
Net carrying value	**173,909**	**179,032**	**119,420**	**119,420**
b) Deposits from local banks	23,814	23,814	235,751	235,751
c) Borrowing from Central Bank of Kenya	**720,000**	**720,000**	**1,120,000**	**1,120,000**

Deposits with/from local banks as at 31 December 2019 represent overnight lending. The effective interest rate on deposits due from and due to local banking institutions at 31 December 2019 was nil (2018 – 7%) and nil (2018–nil) for balances with correspondent banks.

The borrowings from Central Bank of Kenya was a REPO:
- Tenure: The period of the borrowings was 1 month from 19 December 2019 to 16 January 2020-320,000,000, 24 December 2019 to 21 January 2020-400,000,000.
- Interest rate: the borrowing attracted an interest rate of 9%.
- Security: pledge of the Bank is only a portion of the Treasury Bonds whose fair value was Kshs 900,000,000.

23. FINANCIAL ASSETS AT AMORTISED COST (Group and Bank)

	2019 KShs	2018 KShs
GOVERNMENT SECURITIES		
Kenya Government Treasury bonds – at amortised cost	2,082,370	2,190,093
Kenya Government Treasury bonds – Held to Maturity	-	-
	2,082,370	**2,190,093**
Less than 1 year	525,888	203,044
3 years to 5 years	799,372	579,694
Over 5 years	757,110	1,407,355
	2,082,370	**2,190,093**

The weighted average effective interest rate on treasury bonds was 8.3% (2018 –8.5%). As at 31 December 2019 treasury bonds with a fair value of Kshs 900,000,000 (2018–1,400,000,000) had been pledged to secure borrowings from Central Bank of Kenya.

24. LOANS AND ADVANCES TO CUSTOMERS (Group and Bank)

	2019 Kshs'000	2018 Kshs'000
a) Commercial loans	3,868,401	4,407,379
Overdrafts	994,891	1,002,391
Mortgages	1,789,699	2,024,723
Asset finance loans	804,989	1,083,094
Staff loans	365,650	441,074
Gross loans and receivables	7,823,630	8,958,661
Less:		
Impairment losses on loans and receivables (note 10.6)	(454,597)	(529,002)
Net loans and receivables	**7,369,033**	**8,429,659**

The weighted average effective interest rate on loans and receivables as at 31 December 2019 was 13% (2018 – 13%).

Included in gross loans and receivables of Kshs 7,823,633,000 (2018 – Kshs 8,958,661,000) are non-performing loans amounting to Kshs 1,892,391,000 (2018 – Kshs 1,830,300,000). These are included in the statement of financial position net of specific provisions of Kshs 345,916,938 (2018 – Kshs 397,487,000).

	2019 Kshs'000	2018 Kshs'000
b) Analysis of gross loans and receivables by maturity		
Maturing:		
Within 1 year	1,990,825	2,861,146
Between 1 and 3 years	2,435,699	2,486,298
After 3 years	3,397,108	3,611,217
Loans and receivables to customers	**7,823,632**	**8,958,661**

The concentration of advances to customers is covered under note 10.7

25. IMPAIRMENT LOSSES ON LOANS AND RECEIVABLES (Group and Bank)

	2019 Kshs'000	2018 Kshs'000
At 1 January	529,002	458,152
IFRS 9 Adjustment	-	102,579
Increase in impairment allowances	416,005	368,162
Write offs	(264,941)	(38,678)
Reversals in impairment allowances	(225,469)	(361,213)
At 31 December	**454,597**	**529,002**
Collectively assessed impairment	86,660	131,515
Individually assessed impairment	367,937	397,487
	454,597	**529,002**

26. (a) OTHER ASSETS

Other assets and other receivables that have fixed or determinable payments and that are not quoted in an active market are measured at amortised cost less any impairment loss.

	2019 Bank Kshs'000	2019 Group Kshs'000	2018 Bank Kshs'000	2018 Group Kshs'000
Un-cleared items in the course of collection	18,051	18,051	36,409	36,409
Prepayments	48,762	48,762	42,372	42,372
Rent receivable	11,247	11,247	15,199	15,199
Deposits for services	13,219	13,219	13,570	13,570
Others*	180,190	180,190	199,400	199,400
	271,469	**271,469**	**306,950**	**306,950**

** mainly relate to Mpesa and Kenswitch balances.*

	2019 Kshs'000 Bank	2019 Kshs'000 Group	2018 Kshs'000 Bank	2018 Kshs'000 Group
Due from Subsidiary*	17,079	-	-	-
	17,079	**-**	**-**	**-**

** The subsidiary referred to as here is CBL insurance Agency Limited*

	2019 KShs	2018 KShs
At beginning of the year	6,727	7,139
Gain/(loss) in market value of investment	651	(412)
At end of the year	**7,378**	**6,727**

The investment consists of 21,699 shares of Kakuzi Limited which are in the name of Jimba Credit Corporation Limited but beneficially vested in the Bank.

In accordance with IFRS 13, the fair value ranking of the investment is at level 1.

28 (a). GROUP PROPERTY AND EQUIPMENT AND RIGHT OF USE OF ASSETS

Other assets and other receivables that have fixed or determinable payments and that are not quoted in an active market are measured at amortised cost less any impairment loss.

	Land and buildings Kshs'000	Right of use of assets Kshs'000	Leasehold improvements Kshs'000	Motor vehicles Kshs'000	Fixtures, fittings, equipment & ATMs Kshs'000	Computers Kshs'000	Work in progress	Total Kshs'000
COST / VALUATION								
At 1 January 2018	719,000	-	419,636	20,476	336,267	146,195	3,019	1,644,593
Additions	-	-	3,203	-	2,132	16,684	2,171	24,190
Transfer from WIP	-	-	-	-	1,185	1,834	(3,019)	-
Disposal	-	-	-	-	(14,015)	(16,709)	-	(30,724)
At 31 December 2018	**719,000**	**-**	**422,839**	**20,476**	**325,569**	**148,004**	**2,171**	**1,638,059**
At 1 January 2019	719,000	-	422,839	20,476	325,569	148,004	2,171	1,638,059
Effects of adoption of IFRS 16 as at 1 January 2019(Note 2.1)	-							
167,836	-	-	-	-	-	167,836		
Additions	-	-	5,233	-	17,395	1,061	-	23,689
Transfer from WIP	-	-	-	-	-	-	-	-
Disposal	-	-	-	-	(1,164)	(72)	-	(1,236)
At 31 December 2019	**719,000**	**167,836**	**428,072**	**20,476**	**341,800**	**148,993**	**2,171**	**1,828,348**
Comprising	719,000	-	-	-	-	-	-	719,000
At cost								
At valuation 2019	-	167,836	428,072	20,476	341,800	148,993	2.171	1,107,847

28 (a). GROUP PROPERTY AND EQUIPMENT AND RIGHT OF USE OF ASSETS (Continued)

	Land and buildings Kshs'000	Right of use of assets Kshs'000	Leasehold improvements Kshs'000	Motor vehicles Kshs'000	Fixtures, fittings, equipment & ATMs Kshs'000	Computers Kshs'000	Work in progress	Total Kshs'000
ACCUMULATED DEPRECIATION								
At 1 January 2018	50,175	-	396,354	14,988	297,340	139,390	-	898,247
Charge for the year	16,725	-	8,755	2,472	16,926	5,470	-	50,348
Elimination on disposal	-	-	-	-	(14,014)	(16,637)	-	(30,651)
At 31 December 2018	**66,900**	**-**	**405,109**	**17,460**	**300,252**	**128,223**	**-**	**917,944**
At 1 January 2019	66,900	-	405,109	17,460	300,252	128,223	-	917,944
Charge for the year	16,725	47,408	9,689	2,472	10,879	8,697	-	95,870
Elimination on disposal	-	-	-	-	(1,139)	(61)	-	(1,200)
At 31 December 2019	**83,625**	**47,408**	**414,798**	**19,932**	**309,992**	**136,859**	**-**	**1,012,614**
NET BOOK VALUE								
At 31 December 2019	**635,375**	**120,428**	**13,274**	**544**	**31,808**	**12,134**	**2,171**	**815,734**
At 31 December 2018	**652,100**	**-**	**17,730**	**3,016**	**25,317**	**19,781**	**2,171**	**720,115**

28 (a). BANK PROPERTY AND EQUIPMENT AND RIGHT OF USE OF ASSETS

	Land and buildings Kshs'000	Right of use of assets Kshs'000	Leasehold improvements Kshs'000	Motor vehicles Kshs'000	Fixtures, fittings, equipment & ATMs Kshs'000	Computers Kshs'000	Work in progress	Total Kshs'000
COST/VALUATION								
At 1 January 2018	719,000	-	419,636	20,476	336,267	146,195	3,019	1,644,593
Additions	-	-	3,203	-	2,132	16,595	2,171	24,102
Transfer from WIP	-	-	-	-	1,185	1,834	(3,019)	-
Disposal	-	-	-	-	(14,015)	(16,709)	-	(30,724)
At 31 December 2018	**719,000**	**-**	**422,839**	**20,476**	**325,569**	**147,915**	**2,171**	**1,637,970**
At 1 January 2019	719,000	-	422,839	20,476	,325,569	147,915	2,171	1,637,970
Effects of adoption of IFRS 16 as at 1 January 2019(Note 5.1)	-		-	-	-	-	-	167,836
Additions	-	167,836	-	-	16,639	1,061	-	17,700
Transfer from WIP	-	-	-	-	-	-	-	-
Disposal	-	-	-	-	(1,164)	(72)	-	(1,236)
At 31 December 2019	**719,000**	**167,836**	**422,839**	**20,476**	**341,044**	**148,904**	**2,171**	**1,822,270**
Comprising	719,000	-	-	-	-	-	-	719,000
At cost								
At valuation 2019	-	167,836	422,839	20,476	341,044	148,904	2,171	1,103,270

28 (b). BANK PROPERTY AND EQUIPMENT AND RIGHT OF USE OF ASSETS (Continued)

	Land and buildings Kshs'000	Right of use of assets Kshs'000	Leasehold improvements Kshs'000	Motor vehicles Kshs'000	Fixtures, fittings, equipment & ATMs Kshs'000	Computers Kshs'000	Work in progress	Total Kshs'000
ACCUMULATED DEPRECIATION								
At 1 January 2018	50,175	-	396,354	14,988	297,340	139,390	-	898,247
Charge for the year	16,725	-	8,755	2,472	16,926	5,468	-	50,348
Elimination on disposal	-	-	-	-	(14,014)	(16,637)	-	(30,651)
At 31 December 2018	**66,900**	**-**	**405,109**	**17,460**	**300,252**	**128,221**	**-**	**917,942**
At 1 January 2019	66,900	-	405,109	17,460	300,252	128,221	-	917,942
Charge for the year	16,725	47,408	9,010	2,472	10,809	8,667	-	95,091
Elimination on disposal	-	-	-	-	(1,139)	(61)	-	(1,200)
At 31 December 2019	**83,625**	**47,408**	**414,119**	**19,932**	**309,922**	**136,827**	**-**	**1,011,833**
NET BOOK VALUE								
At 31 December 2019	**635,375**	**120,428**	**8,720**	**544**	**31,122**	**12,077**	**2,171**	**810,437**
At 31 December 2018	**652,100**	**-**	**17,730**	**3,016**	**25,317**	**19,781**	**2,171**	**720,115**

Land and buildings were last revalued as at 31 December 2015, by Vidmerck Limited, independent valuers. Valuations were made on the basis of the open market value using the highest and best use valuation model resulting in a total valuation surplus of Kshs 151,293,000. The book values of the properties were adjusted to the revalued amounts and the resultant surplus was credited to the revaluation surplus.

Motor vehicles, fixtures fittings and equipment with a cost of Kshs. 810,312,814 (2018- Kshs 767,740,948) were fully depreciated as at 31 December 2019. The notional depreciation charge on these assets would have been Kshs 149,990,992 (2018- Kshs 141,229,418).

In accordance with IFRS 13, the fair value ranking of the land and buildings is at Level 2 as the fair value measurement is derived from inputs other than quoted prices included within Level 1 that are observable for the asset or liability, either directly as prices or indirectly as derived from prices.

Work in progress relates to the Euro Mastercard Visa switch migration which is at various stages of completion.

28 (b). BANK PROPERTY AND EQUIPMENT AND RIGHT OF USE OF ASSETS (Continued)

Set out below are the carrying amount of lease liability (included in the liabilities under note 5.1) and the movement during the period

As at 1 January 2019 effect of adoption of IFRS 16	167,836
Additions	-
Accretion of interest	13,797
Payments	(61,205)
As at 31 December 2019	**120,428**

If the land and buildings were stated on the historical cost basis, their carrying amounts would be as follows:

	2019	2018
	Kshs'000	Kshs'000
At 1 January	122,076	126,597
Depreciation charge	(4,521)	(4,521)
At 31 December	**117,555**	**122,076**

29(a). GROUP INTANGIBLE ASSETS

	Computer Software Kshs'000	Work in Progress Kshs'000	Total Kshs'000
COST / VALUATION			
At 1 January 2018	461,260	42,720	503,980
Additions	24,347	12,272	36,619
Transfer from WIP	42,720	(42,720)	-
At 31 December 2018	**528,327**	**12,272**	**540,599**
At 1 January 2019	528,327	12,272	540,599
Additions	111,461	28,296	139,757
Transfer from WIP	5,226	(5,226)	-
Disposals	(130)	-	(130)
At 31 December 2019	**644,884**	**35,342**	**680,226**
ACCUMULATED AMORTISATION			
At 1 January 2018	264,452	-	264,452
Charge for the year	89,935	-	89,935
At 31 December 2018	**354,387**	**-**	**354,387**
At 1 January 2019	354,387	-	354,387
Charge for the year	108,427	-	108,427
Eliminated on disposal	(130)	-	(130)
At 31 December 2019	**462,684**	**-**	**462,684**
NET BOOK VALUE			
At 31 December 2019	**182,200**	**35,342**	**217,542**
At 31 December 2018	**173,939**	**12,272**	**186,211**

Work in progress relates to the Euro Mastercard Visa switch, Network access system and Security Incident Event Management system projects which were at various stages of completion.

29(b). BANK INTANGIBLE ASSETS

	Computer Software Kshs'000	Work in Progress Kshs'000	Total Kshs'000
COST / VALUATION			
At 1 January 2018	461,260	42,720	503,980
Additions	24,347	10,772	35,119
Transfer from WIP	42,720	(42,720)	-
At 31 December 2018	**528,327**	**10,772**	**539,099**
At 1 January 2019	528,327	10,772	539,099
Additions	109,963	28,296	138,259
Transfer from WIP	3,726	(3,726)	-
Disposals	(130)	-	(130)
At 31 December 2019	**641,886**	**35,342**	**677,228**
ACCUMULATED AMORTISATION			
At 1 January 2018	264,452	-	264,452
Charge for the year	89,935	-	89,935
At 31 December 2018	**354,387**	**-**	**354,387**
At 1 January 2019	354,387	-	354,387
Charge for the year	108,129	-	108,129
Eliminated on disposal	(130)	-	(130)
At 31 December 2019	**462,386**	**-**	**462,386**
NET BOOK VALUE			
At 31 December 2019	**179,500**	**35,343**	**214,842**
At 31 December 2018	**173,939**	**12,272**	**186,211**

Work in progress relates to the Euro Mastercard Visa switch, Network access system and Security Incident Event Management system projects which were at various stages of completion.

30. BANK PREPAID OPERATING LEASE RENTALS (LEASEHOLD LAND)

The Bank's regulatory capital position at 31 December 2019 and 31 December 2018 was as follows:

	2019	2018
	Kshs'000	Kshs'000
At 1 January and 31 December	45,298	45,298
ACCUMULATED AMORTISATION		
At 1 January	38,659	38,489
Charge for the year	170	170
At 31 December	38,829	38,659
NET BOOK VALUE		
At 31 December	**6,469**	**6,639**

31. CUSTOMER DEPOSITS (Group and BANK)

Current and demand accounts	3,207,533	3,113,010
Savings accounts	1,149,370	965,599
Fixed deposit accounts	4,412,619	4,419,174
Margins	2,338	90,761
	8,771,860	**8,588,544**

Maturity analysis of customer deposits:

Repayable:		
On demand	4,359,240	4,169,370
Within one year	4,412,620	4,419,174
	8,771,860	**8,588,544**

The weighted average effective interest rate on interest bearing customer deposits at 31 December 2019 was 4.4% (2018 – 5.1%). Concentration of customers' deposits is covered under note 10.7.

32. OTHER LIABILITIES

	2019	2019	2018	2018
	Kshs'000	Kshs'000	Kshs'000	Kshs'000
	Bank	Group	Bank	Group
Accrued expenses	19,918	19,918	9,244	9,244
Gratuity (note 32(a)	9,600	9,600	4,168	4,168
Leave pay provision (note 32(b))	7,521	7,521	7,683	7,683
Tenants deposits	16,755	16,755	16,804	16,804
Cheques for collection	1,024	1,024	73	73
Deferred fees income	-	-	60,402	60,402
Sundry payables	127,501	128,609	186,988	186,988
Lease liability	167,836	16 7,836	-	-
	350,155	**351,263**	**285,362**	**285,362**

32. OTHER LIABILITIES (continued)

	2019 Kshs'000	2018 Kshs'000
a) Gratuity		
Balance as at 1 January	4,168	11,442
Paid	(914)	(12,600)
Charge for the year	6,346	5,326
Balance as at 31 December	**9,600**	**4,168**
b) Leave pay provision		
Balance as at 1 January	7,683	7,327
charge /(Credit) for the year	(162)	356
Balance as at 31 December	**7,521**	**7,683**

33. BORROWINGS (Group and Bank)

As at 1 January	1,732,320	1,807,002
Interest expense	177,961	219,551
Repayments during the year	(1,910,281)	(294,233)
At the end of the year	**-**	**1,732,320**
Analysis by currency:		
Borrowings in Euros	-	127,315
Borrowings in Kenya shillings (Kshs)	-	1,605,005
	-	**1,732,320**
Analysis by lender:		
European Investment Bank (EIB)	-	127,315
Corporate bond – medium term notes	-	1,605,005

33. BORROWINGS (continued)

Facility terms:

a) EIB Loan facility: The facility from European investment Bank was a credit line of Eur 6,500,000 received by the Bank as part of its participation in the global loan facility extended by EIB to a group of financial institutions in Kenya under the Cotonou Agreement. The facility terms are as follows:

- Tenure: The period of the financing which shall be between 4 to 10 years save in respect of sub-loans for small projects where the sub loan is less than the equivalent of EUR 50,000 and finance leases, which shall have a minimum tenor of 3 years.
- Interest rate: For a tranche denominated in EUR or USD as margin of 2.88% per annum and for tranches denominated in Kenya Shillings will attract additional currency risk premium depending on the tenor of the loan
- Security: a negative pledge on present and future business undertakings together with all the assets or revenues of the Bank.
- Retirement: The bank prepaid fully the EIB loan on 22 July 2019

b) Medium term notes: this refers to a series of senior and subordinated notes issued by the Bank and traded on the Nairobi Securities Exchange. The issued and currently traded notes have a face value Kshs 1,678,200,000.

- Tenor: the notes mature on 22 July 2019
- Interest rate: the notes attract a fixed interest rate of 13.5 % for the senior notes and 13.25% for the subordinated notes.
- Retirement: The notes matured on 22 July 2019 and the Bank sort an extension of the maturity for a further 3 months to 22 October 2019 and the same was approved by the noteholders. The note was fully settled on 22 October 2019.

34. SHARE CAPITAL (Bank)

	2019 Kshs'000	2018 Kshs'000
a) Authorised:		
80,000,000 ordinary shares of Kshs 20 each	1,600,000	1,600,000
80,000,000, 4% non-cumulative irredeemable non-convertible preference shares of Kshs 20 each	1,600,000	1,600,000
	3,200,000	**3,200,000**
b) Issued and fully paid:		
149,920,000 ordinary shares of Kshs 20 each (2018 – 69,920,000)	2,998,400	1,398,400
36,056,500, 4% non-cumulative irredeemable Non-convertible preference Shares of Kshs 20 each	721,130	721,130
	3,719,530	**2,119,530**

Non-convertible non-participating preference shares are entitled to receive a discretionary dividend before any dividend is declared to the ordinary shareholders. The preference shares have no right to share in any surplus assets or profits and no voting rights.

35. REVALUATION SURPLUS (Group and Bank)

	2019	2018
	Kshs'000	Kshs'000
At 1 January	370,509	379,130
Transfer of excess depreciation	(12,316)	(12,316)
Deferred tax on transfer of excess depreciation- Buildings	3,695	3,695
At 31 December	**361,888**	**370,509**

The revaluation surplus arises on the revaluation of freehold land and buildings. Where revalued land or buildings are sold, the portion of the revaluation surplus that relates to that asset, and is effectively realised over the period in which this is transferred, is transferred directly to revenue reserves. The revaluation surpluses are non-distributable.

	2019	2019	2018	2018
	Kshs'000	Kshs'000	Kshs'000	Kshs'000
	Group	Bank	Group	Bank
36. ACCUMULATED DEFICIT				
At 1 January	(2,061,222)	(2,061,222)	(1,265,665)	(1,265,665)
Elimination of subsidiary losses from the bank		3,974		
IFRS 9 opening balance adjustment	-	-	(102,633)	(102,633)
Loss for the year	(531,292)	(530,199)	(540,034)	(540,034)
Transfer of excess depreciation	12,316	12,316	12,316	12,316
Deferred tax on transfer of excess depreciation				
Transfer to statutory reserve	(3,695)	(3,695)	(3,695)	(3,695)
	16,754	16,754	(161,511)	(161,511)
At 31 December	**(2,567,139)**	**(2,562,072)**	**(2,061,222)**	**(2,061,222)**

37. STATUTORY RESERVE (Group and Bank)

	2019	2018
	Kshs'000	Kshs'000
At 1 January	490,679	329,168
Transfer from/(to) accumulated deficit	(16,754)	225,017
Transfer to IFRS stage 1 provision	-	(63,506)
At 31 December	**473,925**	**490,679**

38. FAIR VALUE RESERVE (Group and Bank)

At 1 January	5,859	6,271
Gain/(loss) in market value of quoted equity shares	651	(412)
At 31 December	**6,510**	**5,859**

The fair value deficit shows the effects from the fair value measurement of equity instruments at fair value through other comprehensive income. Any gains and losses are not recognised in the profit or loss until the asset has been sold or impaired. Refer to note 4 (c) for additional fair value disclosures.

39 (a) NOTES TO THE GROUP STATEMENT OF CASH FLOWS

	2019 Kshs'000	2018 Kshs'000
(a) Reconciliation of loss before taxation to cash used in operations		
Loss before taxation	(518,001)	(351,567)
Adjustments for:		
Depreciation of property and equipment (note 28)	95,870	50,348
Amortisation of intangible assets (note 29)	108,427	89,935
Amortisation of leasehold land (note 30)	170	170
Interest expense on leases	13,797	-
Prepaid lease	(3872)	
(Gain)/loss on disposal of property and equipment	(187)	(40)
Interest expense on borrowings (note 34)	-	219,551
Impairment (credit)/charge on loans and advances (note 24)	190,653	6,955
Profit before working capital changes	**(113,188)**	**15,352**
Increase in cash ratio balance	(63,842)	(38,454)
Increase in other assets	35,481	(22,512)
(increase)/decrease in gross loans and receivables	870,170	(118,174)
Decrease in customer deposits	183,316	(57,761)
Increase in other liabilities	65,901	44,123
Decrease in treasury bonds	107,724	415,806
Cash from/(used in) operations	**1,085,606**	**238,380**
(b) Analysis of the balances of cash and cash equivalents as shown in the statement of financial position and notes		
Cash on hand (Note 21)	296,290	372,065
Balances with Central Bank of Kenya –other (Note 21)	10,692	11,047
Balances with other banking institutions	179,032	119,420
Balance from Central Bank (Note 21 (c))	(720,000)	1,120,000
Deposits and balances from other banking institutions (note 21 (b))	(23,814)	(235,751)
	(257,800)	**(853,219)**

For the purpose of the cash flow statement, cash and cash equivalents comprise balances with less than three months' maturity from the date of acquisition, including cash in hand, deposits held at call with banks and other short term highly liquid investments with original maturities of three months or below, less advances from banks repayable within three months from the dates of the advances.

40 (a) NOTES TO THE BANK STATEMENT OF CASH FLOWS

	2019	2018
	Kshs'000	Kshs'000
(a) Reconciliation of loss before taxation to cash used in operations		
Loss before taxation	(516,908)	(351,567)
Adjustments for:		
Depreciation of property and equipment (note 28)	95,091	50,348
Amortisation of intangible assets (note 29)	108,129	89,935
Amortisation of leasehold land (note 30)	170	170
Interest expense on leases	13,797	-
Prepaid lease	(3,872)	-
Elimination of accumulated losses for subsidiary	3,974	
Elimination of prior year financing activity (acquisition of PPE)	1,588	
(Gain)/loss on disposal of property and equipment	(190)	(40)
Interest expense on borrowings (note 34)	-	219,551
Impairment (credit)/charge on loans and advances (note 24)	190,653	6,955
Profit before working capital changes	**(107,568)**	**15,352**
Increase in cash ratio balance	(63,842)	(38,454)
Increase in other assets	18,402	(22,512)
(increase)/decrease in gross loans and receivables	870,170	(118,174)
Decrease in customer deposits	183,316	(57,761)
Increase in other liabilities	64,793	44,123
Decrease in treasury bonds	107,724	415,806
Cash from/(used in) operations	**1,072,995**	**238,380**
b) Analysis of the balances of cash and cash equivalents as shown in the statement of financial position and notes		
Cash on hand (Note 21)	296,290	372,065
Balances with Central Bank of Kenya –other (Note 21)	10,691	11,047
Balances with other banking institutions	173,909	119,420
Balance due from Central Bank (Note 21 (c))	(720,000)	(1,120,000)
Deposits and balances from other banking institutions (note 21 (b))	(23,814)	(235,751)
	(262,924)	**(853,219)**

For the purpose of the cash flow statement, cash and cash equivalents comprise balances with less than three months' maturity from the date of acquisition, including cash in hand, deposits held at call with banks and other short term highly liquid investments with original maturities of three months or below, less advances from banks repayable within three months from the dates of the advances.

41. INVESTMENTS IN SUBSIDIARIES

The consolidated financial statements include the financial statements of Consolidated Bank Ltd and its subsidiaries. Consolidated Bank does not have any joint ventures or associates
The operations of the companies below were vested in the Bank in July 2002 and are all incorporated in Kenya.
i) Jimba Credit Corporation Limited
ii) Kenya Savings & Mortgages Limited
iii) Citizen Building Society
iv) Estate Building Society
v) Estate Finance Company of Kenya Limited
vi) Business Finance Company Limited
vii) Home Savings and Mortgages Limited
viii) Union Bank of Kenya Limited
ix) Nationwide Finance Company Limited
Further to the above, the bank incorporated, Consolidated Bank Insurance Agency Limited, which commenced operations in January 2019.

All the above subsidiaries are wholly owned by the Bank. The subsidiaries except Consolidated Bank Insurance Agency Limited are dormant and had a nil carrying value as at 31 December 2019 (2018: Nil).

42. OTHER SUPPLEMENTARY INFORMATION (Bank)

The bank's business comprises the following reportable units:

- Corporate Banking – This include banking services such as business current accounts, fixed deposits, overdrafts, loans, asset finance and other credit facilities in local and foreign currencies
- Retails & SME (Small medium size enterprises) – incorporating banking current accounts, savings accounts, individual fixed deposits, personal loans, retail and SME lending
- Treasury – operates the bank's fund management and investment activities.

Others comprise rental income and other incidental income from the rental space in the Bank's Head Office building at Consolidated Bank House.

The table below summarizes the breakdown of other supplementary information l assets, liabilities, income and expenses;

Profit or loss for the year ended 31 December 2019	Corporate banking Kshs'000	Retail banking Kshs'000	Treasury Kshs'000	Other Kshs'000	Total Kshs'000
Net interest income	184,499	456,593	(99,643)	-	541,449
Net fee and commission	194,691	391,825	21,715	12,146	620,377
Other income	-	-	-	71,028	71,028
Operating income	379,190	848,418	(77,928)	83,174	1,232,854
Operating expenses	(580,197)	(1,107,120)	(19,624)	(43,914)	(1,750,855)
Profit/(loss) before tax	**(201,007)**	**(258,702)**	**(97,552)**	**39,260**	**(518,001)**

42. OTHER SUPPLEMENTARY INFORMATION (Continued)

Profit or loss for the year ended31 December 2018

	Corporate banking Kshs'000	Retail banking Kshs'000	Treasury Kshs'000	Other Kshs'000	Total Kshs'000
Net interest income	151,094	641,932	(150,019)	-	643,007
Net fee and commission	111,537	1,223,053	642	-	1,335,232
Other income	-	-	-	69,547	69,547
Operating income	262,631	1,864,985	(149,377)	69,547	2,047,786
Operating expenses	(389,416)	(1,967,163)	(18,584)	(24,190)	(2,399,353)
Profit/(loss) before tax	**(126,785)**	**(102,178)**	**(167,961)**	**45,357**	**(351,567)**

Statement of financial position as at 31 December 2019

Assets					
Short term funds	-	475,322	2,692,500	-	3,167,822
Loans	2,569,196	4,799,837	-	-	7,369,033
Other assets	-	680,121	-	644,672	1,324,793
Total assets	**2,569,196**	**5,955,280**	**610,130**	**610,130**	**11,861,648**
Liabilities and equity:					
Customer deposits	2,129,325	6,666,349	-	-	8,795,674
Borrowed funds	-	-	720,000	-	720,000
Other liabilities	-	350,492	-	-	355,544
shareholders' funds	-	1,995,482	-	-	1,995,482
Total liabilities and equity	**2,129,325**	**9,012,323**	**720,000**	**-**	**11,861,648**

Statement of financial position as at 31 December 2018

	Corporate banking Kshs'000	Retail banking Kshs'000	Treasury Kshs'000	Other Kshs'000	Total Kshs'000
Assets					
Short term funds	-	491,465	2,736,737	-	3,228,202
Loans	1,777,226	6,652,433	-	-	8,429,659
Other assets	-	749,619	-	652,100	1,401,719
Total assets	**1,777,226**	**7,893,517**	**2,736,737**	**652,100**	**13,059,580**
Liabilities and equity:					
Customer deposits	2,164,196	6,424,348	-	-	8,588,544
Borrowed funds			3,088,050	-	3,088,050
Other liabilities	-	285,362	-	-	285,362
Shareholders' funds	-	1,097,624	-	-	1,097,624
Total liabilities and equity	**2,164,196**	**7,807,334**	**3,088,050**	**-**	**13,059,580**

43. CONTINGENCIES AND COMMITMENTS INCLUDING OFF BALANCE SHEET ITEMS (Bank)

a) Contingent liabilities

In common with other financial institutions, the Bank conducts business involving acceptances, letters of credit, guarantees, performance bonds and indemnities. The majority of these facilities are offset by corresponding obligations of third parties.

	2019	2018
	Kshs'000	Kshs'000
Acceptances and letters of credit	36,467	62,292
Guarantees	721,845	984,621
	758,312	**1,046,913**
Litigations against the bank	**2,246,847**	**2,246,847**

Nature of contingent liabilities:

An acceptance is an undertaking by a Bank to pay a bill of exchange drawn on a customer. The Bank expects most acceptances to be presented, but reimbursement by the customer is normally immediate.

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

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

Concentrations of contingent liabilities are covered under note 10.7.

Litigations against the Bank relate to civil suits lodged against the Bank by customers and employees in the normal course of business. The likely outcome of these suits cannot be determined as at the date of signing these financial statements. The Directors, however, do not anticipate that any material liability will accrue from the pending suits.

b) Commitments to extend credit

	2019	2018
	Kshs'000	Kshs'000
Other commitments to lend	**386,799**	**531,333**
Undrawn formal stand-by facilities and credit lines	**433,107**	**65,824**

Commitments to extend credit are agreements to lend to a customer in future subject to certain conditions. Such commitments are normally made for a fixed period. The Bank may withdraw from its contractual obligation to extend credit by giving reasonable notice to the customer.

c) Capital commitments

	2019	2018
	Kshs'000	Kshs'000
Authorised but not contracted for	**163,945**	**97,208**

Capital commitments relate to; investment in ICT cyber security and replacement of computers and equipment for the branches. Non-convertible non-participating preference shares are entitled to receive a discretionary dividend before any dividend is declared to the ordinary shareholders. The preference shares have no right to share in any surplus assets or profits and no voting rights.

43. CONTINGENCIES AND COMMITMENTS INCLUDING OFF BALANCE SHEET ITEMS (Continued)

d) Operating lease commitments

Rental income earned during the year was Kshs 71,027,811 (2018 – Kshs 69,546,580). At the reporting date, the Bank had contracted with tenants for the following minimum future lease receivables:

The Bank as a lessor:	2019 Kshs'000	2018 Kshs'000
Within one year	53,979	44,829
In the second to fifth year inclusive	150,497	117,408
After five years	-	-
	204,476	**162,237**

Operating leases relate to the buildings and are negotiated for an average term of 6 years, with the rentals being reviewed every two years and hence classified as operating leases. The leases are cancellable with a penalty when the tenants do not give three months' notice to vacate the premises.

All operating lease contracts contain market review clauses in the event that the lessor exercises its option to renew. The lessees do not have an option to purchase the property at the expiry of the lease period. The operating lease contracts are cancellable.

The Bank as a lessee

At the reporting date, the Bank had outstanding commitments under operating leases which fall due as follows:

	2019 Kshs'000	2018 Kshs'000
Within one year	61,804	57,332
In the second to fifth year inclusive	99,914	133,336
After five years	46,076	36,779
	207,794	**227,447**

Operating lease payments represent rentals payable by the Bank for its office premises.

e) Foreign exchange contracts

The Bank enters into derivatives for trading and risk management purposes, as explained in Note 2.1 in the Summary of significant accounting policies. The Bank may take positions with the expectation of profiting from favourable movements in prices, rates or indices. The trading portfolio is within the Bank's investment banking division (treasury) and is treated as trading risk for risk management purposes. Derivatives held for risk management purposes include hedges that are economic hedges, but do not meet the hedge accounting requirements. The table below shows the fair values of derivative financial instruments recorded as assets or liabilities together with their notional amounts.

The notional amount, recorded gross, is the quantity of the derivative contracts' underlying instrument (being foreign currency, reference rate or index). The notional amounts indicate the volume of transactions outstanding at the year end and are not indicative of either the market or credit risk.

43. CONTINGENCIES AND COMMITMENTS INCLUDING OFF BALANCE SHEET ITEMS (Continued)

e) Foreign exchange contracts

	Carrying value assets	Carrying value liabilities	Notional amount
At 31 December 2019	KShs'000	KShs'000	KShs'000
Derivatives in economic hedge relationships:			
Foreign exchange contracts	685	-	61,860
At 31 December 2018			
Foreign exchange contracts	1,083	3	97,743

Forwards and spot contingents are the foreign exchange deals carried out in the interbank markets.

44. RELATED PARTY TRANSACTIONS (Bank)

Parties are considered to be related if one party has the ability to control the other party or exercise significant influence over the other party in making financial or operational decisions.

Placings are made in the Bank by Directors, their associates and companies associated to Directors. Advances to customers at 31 December 2019 include advances and loans to companies associated with the directors. Contingent liabilities at 31 December 2019 include guarantees and letters of credit for companies associated with the Directors.

	Directors	
	2019	2018
	Kshs'000	Kshs'000
Movement in related party balances was as follows:		
Loans and advances:		
At 1 January	-	1,062
Advanced during the year	-	-
Interest earned	-	28
Repaid during the year	-	(1,090)
At 31 December	-	-

As at 31 December 2019 loans and advances to staff amounted to Kshs 365,649,703 (2018– Kshs 441,073,713).

The loans and advances to related parties are performing and are adequately secured.

	Directors and employees	
	2019	2018
	Kshs'000	Kshs'000
Customer deposits:		
At 1 January	36,863	29,182
Placed during the year	1,260,033	1,106,052
Net interest applied	711	1,079
Withdrawals	(1,267,277)	(1,099,450)
At 31 December	**30,330**	**36,863**

44. RELATED PARTY TRANSACTIONS (Continued)

Key management compensation

The remuneration of Directors and other members of key management during the year were as follows:

Short term benefits		
Salaries and other benefits	131,202	127,024
Fees for services as Directors	12,476	5,048
	143,678	**132,072**

Staff number

The total number of staff as at the end of the year was as follows:

	2019	2018
Number of staff	258	267

45. INCORPORATION

The Bank is domiciled and incorporated in Kenya under the Kenyan Companies Act.

46. CURRENCY

These financial statements are prepared in Kenya shillings thousands (Kshs'000) which is the Bank's functional and presentation currency.

47. EVENTS AFTER THE REPORTING DATE

The first case of this infection was reported in Kenya on 13th March 2020 and since then a few other cases have been identified. The pandemic if prolonged, is projected to slow down the economy, causing likelihood of increased default in repayment of loans and advances. The Government has however come up with a raft of proposals awaiting parliament's input before enactment into law. These propositions, if adopted, are expected to cushion against adverse economic effects. The developments surrounding COVID-19 changes on a daily basis giving rise to inherent uncertainty. It is expected that the Bank's loan book may be affected. The financial impact of this matter cannot be quantified at this stage.

Management assesses that it is not practicable to accurately estimate the financial impact on COVID-19 now as the effects are yet to fully materialise. As of the date of approval of this report, the Bank operations were normal and uninterrupted. The directors, in consideration of the above facts, assess the post year end epidemic outbreak as a non-adjusting event.

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